Encyclopedia of

Business Ethics and Society

Vol. 5

Editor

Robert W. Kolb

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Editor

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All the entries in this *Encyclopedia* have been arranged into this Reader's Guide. Here each entry finds its place in one or more thematic groupings of entries that pertain to a central conceptual domain covered by the *Encyclopedia.* For example, the *Encyclopedia* contains a number of entries on topics such as "Applied Ethics" and "Corporations in the Social Sphere." Classifying the entries into such groupings allows an interested reader to quickly peruse many entries pertaining to one of the key conceptual areas addressed by this *Encyclopedia.*

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He has published more than 50 academic research articles and more than 20 books. In 1990, he founded Kolb Publishing Company to publish finance and economics university texts, built the company's list over the ensuing years, and sold the firm to Blackwell Publishers of Oxford, England, in 1995.

He also recently published the sixth edition of *Understanding Futures Markets* and the fifth edition of *Futures, Options, and Swaps* (both with James A. Overdahl). He recently edited three monographs: *The Ethics of Executive Compensation, The Ethics of Genetic Commerce,* and *Corporate Retirement Security: Social and Ethical Issues*.

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Introduction

Commerce is by its very nature a normative enterprise. It is concerned with creating value for owners and other constituencies, ranging from the firm's immediate stakeholders, such as employees, customers, and suppliers, to the entire society within which the business operates. As a field of study, *business ethics* aims to specify the principles under which businesses must operate to behave ethically. Thus, business ethics focuses on issues such as those that have recently attracted so much public scrutiny: executive compensation, honesty in accounting, transparency, treatment of stakeholders, and respect for the environment. These are, in fact, perennial questions that accompany the long history of human economic activity and that will also be present through an indeterminate future.

Business and society is a distinct field of study closely related to business ethics. Business and society explores the entire range of interactions between business entities and the societies in which they operate. Almost all the questions addressed by business and society have a normative dimension. But in contrast to business ethics, the discipline of business and society relies much more strongly on the tools of the social sciences. Thus, business and society scholars frequently examine the effects of business on society using empirical tools such as surveys, empirical data, and statistics.

There is no firm demarcation between the two disciplines of business ethics and business and society. While both disciplines may have their separate academic societies, the questions explored are clearly related, and many scholars belong to both kinds of societies and move between the two areas of inquiry with perfect ease.

While business ethics and business and society are united by a common concern with normative issues surrounding commerce, they are most strongly distinguished by their typical methodologies. The paradigmatic methods of business ethics are drawn from the Western philosophical tradition, while business and society scholars turn most naturally to the methods of the social sciences. Each of these fields of study relies to a considerable degree on the methods of the other, however. The questions of value that business ethics finds most compelling naturally draw the greatest attention from scholars in business and society. For its part, business ethics as an applied discipline relies on the findings of business and society to help identify those issues most in need of study.

Rationale for the *Encyclopedia*

The *Encyclopedia of Business Ethics and Society* recognizes the inherent unity between business ethics and society that stems from their shared primary concern with value questions in commerce. Topics of study do not come neatly divided into those that require conceptual analysis or philosophical consideration and others that will succumb to empirical study or generate empirical generalizations. To isolate the two disciplines impoverishes both, as is well recognized by scholars who find their most natural home in one discipline or the other. Therefore, the focus of the *Encyclopedia* embraces all normative aspects of business.

As an example of this breadth of vision, consider the relationship between the employer and her employees, whose essential relationship is specified by an employment contract, which can be a legal document or merely specified by custom. A host of issues surround this one business relationship. The contract specifies rights and obligations of both parties, so it is inherently normative. Some forms of employment contract prevail over others in different situations. Thus, there is an empirical issue concerning what types of contracts occur in various industries and why specific forms of employee contracts seem to arise in particular industries and for employees with specific skills. Of course, in a complex industrial economy, government plays a major role in the employer-employee relationship, with laws and institutions that set bounds on the kinds of contracts that can exist and the way in which given contracts are expressed in daily life. Here, one need only think of minimum wage laws and safety regulation. No full understanding of the relationship between employer and employee can be attained without a consideration of all these different factors.

To that end, the *Encyclopedia* addresses the normative dimensions of commerce with a broad mandate that embraces the following themes and dimensions of business:

Accounting

Applied ethics

Corporate management and the environment

Corporate powers, organization, and governance

Corporations in the social sphere

Customers and consumers

Economics and business

Employee issues

Environmental thought, theory, regulation, and legislation

Ethical thought and theory

Finance

Gender, age, ethnicity, diversity, and sexual orientation

Information systems

International social and ethical issues

Justice

Legislation and regulation

Management

Marketing

Organizations

Political theory, thought, and policy

Problematic practices

Rights

These topics are the headings for the Reader's Guide, and all the entries in the *Encyclopedia* fall under one or more of these broad themes. As the list indicates, the scope of the *Encyclopedia* encompasses the theoretical and ranges to the very practical social and ethical issues that beset the various functional areas of business.

Content and Organization

The *Encyclopedia* is composed of almost 900 entries arranged in alphabetical order. The entries range in length from about 500 words to almost 11,000 words. As has already been touched on above, the *Encyclopedia* embraces commerce in all its ethical and social dimensions. This ambition requires comprehensive and fairly lengthy essays on such crucial topics as justice, freedom, stakeholder theory, and regulation. At the other end of the spectrum, very brief essays introduce important personages in the field, while other similarly brief entries explain the nature and function of various organizations.

Because so many of the topics discussed in the *Encyclopedia* relate to other matters, every entry has cross-references to other entries in the *Encyclopedia.* In addition, a list of references and suggested readings accompanies each entry. The Reader's Guide allows a user of the *Encyclopedia* to find the many entries related to each of the broad themes covered by the work.

How the *Encyclopedia* Was Created

The *Encyclopedia* was created in several steps.

1. I began by examining all the leading university texts in business ethics and business and society to create an initial list of potential headwords. In addition, I explored the leading journals in both fields for the immediately previous 5 years to capture new terms and ideas that were entering the profession but were not yet enshrined in textbooks.
2. Armed with this initial list of prospective headwords, I approached the most eminent scholars in business ethics and business and society to solicit their participation in the project as editors. Eventually, I recruited five of the very best scholars in the two fields to serve as a team of associate editors.
3. The associate editors and I worked together to refine and expand the headword list. The associate editors also played a pivotal role in developing a broader editorial board of about 25 exceptional scholars from both fields.

4. I also recruited a highly respected university librarian, who specializes in business and leads the business library at the University of Colorado, to serve as a special library consultant. The idea here was to capture the talent and knowledge of someone who works every day with college students who are actually exploring other resources similar to the *Encyclopedia.*

5. With the editorial team in place, we again revised the headword list and the editors collectively began to develop a list of potential contributors for each topic. Anxious to capture the insight of the very best scholars in the field, members of the editorial team undertook the writing of some of the most lengthy and most important entries in the *Encyclopedia.* After several iterations of refining the list of headwords, we began the process of recruiting authors for each entry.

6. Before assigning entries, I created several diverse sample entries to serve as guides for authors as to the level of intellectual rigor and complexity of language that we desired. Also, potential authors received very detailed submission guidelines before they were assigned, and they were asked to review both the sample entries and the submission guidelines before agreeing to write for the *Encyclopedia.*

7. Every entry was reviewed by at least two members of the editorial team. The editors requested revisions, sometimes numerous revisions, of virtually every entry in the *Encyclopedia*, including those written by the editorial team. We believe that this lengthy process of criticism and refinement led to the creation of much better entries than would have been possible otherwise.

Acknowledgments

The *Encyclopedia* began when Rolf Janke, publisher of the reference division at Sage, approached me with the idea of developing a two-volume work in the general area of business ethics. I was immediately intrigued by the idea, because I thought that creating an *Encyclopedia* could be an important contribution to the field and help define a still nascent discipline.

It quickly became apparent that any adequate treatment of the normative issues facing business required a perspective beyond business ethics per se, because so many issues impinge on each other. We, therefore, decided to broaden the scope of the project to include not only business ethics but also business and society. The scope and success of the project owe much to Rolf, not only for the original idea but also for his flexibility in expanding the project by more than 100%.

The editorial team, which includes the associate editors, the editorial board, and the special library consultant, all deserve the greatest appreciation. Not only did they write many of the key entries; they also patiently read many drafts of many entries and guided all of them to a higher state of excellence.

The *Encyclopedia* consists of the writing of scholars drawn from the fields of both business ethics and business and society, so the greatest thanks go to the contributors. Over the course of the project, it became ever more apparent how deeply these men and women care about their respective fields and how fully they are committed to their growth and development. I think that they shared with me a belief in the project's importance, and they almost invariably made the extra effort to improve the entries and to make each one as good as it could possibly be.

Throughout the writing phase, I worked very closely with Yvette Pollastrini, the developmental editor for the *Encyclopedia* at Sage. Yvette read every entry for substance and style and never hesitated to ask for clarification of passages that were too technical or too complex for university students. Amy Parziale, a graduate student at the University of Colorado and now at the University of Arizona, was instrumental in serving as the managing editor. Amy handled many of the thousands of e-mail communications with authors, and she employed her very considerable organizational talents to discipline a somewhat scattered lead editor.

To all these people, I owe a great deal of appreciation. However, one other person lived the entire multiyear experience of creating the *Encyclopedia* and deserves special gratitude. My wife, Lori Kolb, listened to my complaints (or at least pretended to), was always understanding when the work of the *Encyclopedia* interfered with family plans, and provided the best support one could ever ask from a spouse.

—Robert W. Kolb
General Editor

A

AACSB International

See Association to Advance Collegiate Schools of Business (AACSB International)

AARP

AARP, known as the American Association of Retired Persons until 1999, is one of the largest nonprofit, nonpartisan associations in the United States. The new name was part of a branding effort to attract the baby boomers, soon to attain the membership age of 50. AARP's mission is on their Web page: AARP is dedicated to enhancing the quality of life for aging Americans and to lead positive social change and deliver value to members through information, advocacy, and service. Their vision is of a society in which everyone ages with dignity and purpose and in which AARP helps people fulfill their goals and dreams. AARP has over 35 million members.

Founded by retired high school principal Dr. Ethel Percy Andrus in 1958, AARP grew out of the National Retired Teachers Association (NRTA), which she had founded to enable retired teachers to access private health insurance. NRTA is now a division within AARP. Her vision included encouraging older persons to serve rather than being served. She turned the organization into a national force through publicity—inspirational speeches, testimony in Congress before an antitrust commission, participation in the first White House Conference on Aging, an article for *Reader's Digest*, and an AARP exhibit at the 1964 New York World's Fair. Insurance executive Leonard Davis partnered with her to sell health insurance to the members.

AARP's national headquarters is in Washington, D.C. The executive director, under the supervision of an elected 21-member board, coordinates field operations and state offices. Each state's office helps identify legislative matters concerning the members and advocates for change at that level. There are also over 2,500 community chapters. Thousands of volunteers work at all levels on advocacy issues such as health care, social security, elder abuse, and other legislations affecting the elderly.

There are two affiliated groups—AARP Foundation and AARP Services, Inc. The Foundation is nonprofit and runs programs such as free tax preparation and counseling, work training for low-income older persons, support for major litigation, and training volunteers for dealing with elder law and advocacy. It also sponsors programs on crime prevention and defensive driving. AARP Services, Inc. is a wholly owned for-profit subsidiary that manages for-sale products such as Medicare supplemental health insurance, discounts on prescription drugs and consumer goods, entertainment and travel packages, long-term care insurance, and automobile, home, and life insurance.

AARP is financed through membership dues ($12.59 per year), advertisements in their publications, and fees from the service providers. Publications include the bimonthly *AARP Magazine* (formerly

Modern Maturity), monthly *AARP Bulletin*, quarterly *Segunda Juventud,* the AARP Web site, numerous research reports and consumer education booklets from AARP's Public Policy Institute, and an online database, *Ageline.*

AARP is not without controversy. They have been accused of conflict of interest between lobbying for health care and selling insurance, of misusing their political influence, of being pro-Democrat and pro-Republican, and, throughout the years, of being unwilling to change social security in any way. The Internal Revenue Service and the Postal Service considered it a profit-making business, and Senator Alan Simpson held a congressional hearing in 1995 about this issue. Members resigned in the thousands when AARP endorsed President George W. Bush's prescription drug program. In 2005, they were staunchly defending social security from another attempt to change it and have been fiercely criticized by those who advocate private accounts. They also published a research report on stem cell research. Throughout the years, AARP has taken stands and lobbied on issues based on their understanding of views shown through membership polls and their own research.

—*Carol H. Krismann*

See also Age Discrimination; Conflict of Interest; Medicare; Nonprofit Organizations

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Absolutism, Ethical

Ethical absolutism is the belief that all individuals are held to a particular moral standard. This view establishes that certain actions are always correct while others are always wrong. No matter where in the world absolutists may be, they are responsible to treat others according to the same moral standard established by their beliefs. Those who adhere to ethical absolutism insist that a distinction can be made between what is thought to be right and what is truly correct, and they believe that all people are held to these standards whether or not they are aware of their existence. The prescriptive nature of ethical absolutism allows for the acceptance of fundamental ethical principles without any qualifications with regard to place or time. This view provides a contrast to ethical relativism, which asserts that something is morally relative to a particular situation or standpoint.

Deontological viewpoints complement ethical absolutism well in that they provide guidelines for what exactly the moral standards are that should be upheld. For example, the Kantian would assert that lying is wrong in any situation because it violates the categorical imperative (i.e., lying cannot be willed a universal law). Although utilitarianism, unlike deontology, clearly has no absolutist starting point, utilitarian theorizing can result in absolutist prescriptions, such as Peter Singer's defense of animal rights.

Ethical absolutism is sometimes historically linked to traditions based on Divine Command such as Judeo-Christian practice and the Ten Commandments or the five pillars of Islam as well as other religious doctrines that provide distinct prescriptions for action. However, individuals may view their particular religious viewpoint as the basis for an absolutist belief system. Due to the variety of possible foundations for an absolutist standpoint, the outlook frequently faces fire from its critics. When absolutist beliefs, such as radical fundamentalist movements, are taken out of their religious context, they often do not stand up to rational criticism.

An absolute moral standard has never been proven, but recent attempts have been made to empirically demonstrate the existence of these unconditional rules. These principles, sometimes referred to as hypernorms, stem from integrative social contracts theory (ISCT). ISCT provides an account of the moral appropriateness of business practices through the formulation of fair agreements based on both micro and macro principles. As hypernorms represent the convergence of political, religious, and philosophical viewpoints, further empirical exploration of hypernorms may demonstrate the existence of global absolutist ethical beliefs.

—*Tara L. Ceranic*

See also Deontological Ethical Systems; Golden Rule, The; Integrative Social Contract Theory; Kant, Immanuel; Utilitarianism

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Academy of Management

The Academy of Management, founded in 1936, is the largest professional organization for management scholars and teachers in the world. With nearly 15,000 members in 2005, the Academy has members from 90 different countries, is headquartered in the United States, and is governed by its members. Membership consists of scholars at colleges, universities, and research institutions, who create and disseminate knowledge about organizations and management, and some practicing managers with scholarly interests from business, government, and nonprofit organizations.

The Academy has a mission to enhance the practice of management through scholarship and also to advance the professional development of its members. It accomplishes these ends through a variety of scholarly means. It holds an annual conference that draws together the world's leading management scholars to share their research and also includes professional development activities. The Academy publishes four peer-reviewed scholarly journals: *Academy of Management Journal*, *Academy of Management Review*, *Academy of Management Executive*, and *Academy of Management Learning and Education.* The Academy publishes a newsletter, brings out a Best Paper Proceedings CD based on the annual meeting, and provides its members online access to articles published in its journals. It services members through online list servers, job placement at the annual meeting, and awards for research, scholarship, teaching, and service.

Structured into 21 divisions and interest groups, the Academy focuses on a broad range of scholarly issues facing managers today as highlighted by division names. Divisions in 2005 reflect the breadth of interests among members: Business Policy and Strategy, Careers, Conflict Management, Critical Management Studies (interest group), Entrepreneurship, Gender and Diversity in Organizations, Health Care Management, Human Resources, International Management, Management Consulting, Management Education and Development, Management History, Management Spirituality and Religion (interest group), Managerial and Organizational Cognition, Operations Management, Organizations and Management Theory, Organizational Behavior, Organizational Communication and Information Systems, Organizational Development and Change, Organizations and the Natural Environment (interest group), Public and Nonprofit, Research Methods, Social Issues in Management, and Technology and Innovation Management.

Topical coverage in the Academy's journals and conferences reflects a similar broad range of interests. Much of the scholarly work on business and management ethics and the role of business in society can be found under the umbrella of the Social Issues in Management division; critical scholarship is found within the Critical Management Studies interest group. Numerous other divisions also reflect scholarship with an ethical, ecological, diversity, public interest, meaning-making, social issues, or leadership orientation as well.

The Social Issues in Management division domain includes the following: social environment, including corporate social responsibility, corporate philanthropy, stakeholder management, corporate social performance; the ethical environment, including codes of ethics, corporate crime, individual and organizational ethical behavior, ethical implications of technology, personal values, and corporate culture; the public policy environment, including political action committees, legal and regulatory areas; the ecological environment, including environmental management and ecological issues; stakeholder environment, including impact of technology, workplace diversity, corporate governance, public affairs management; and the international environment, including topics mentioned above, plus how the nation-state system affects international organizations.

—*Sandra Waddock*

See also Business for Social Responsibility (BSR); Moral Education; Networking; Social Ethics

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ACCOUNTABILITY

Accountability can be defined as "being answerable"—that is, being able to give an account. In the corporate environment, it has been closely associated with financial auditing and reporting, as well as accountancy in general. Within the neoclassical conception of the corporation, it is described in terms of duties owed toward its shareholders. Recently, however, corporate social responsibility (CSR), or corporate citizenship (CC) as it is otherwise referred to, movements have led to an increased awareness of the duties associated with the various other relationships in which corporations typically participate. From this perspective, the corporation is compelled to acknowledge its accountability to a wider network of stakeholders.

AccountAbility, the organization responsible for the AA 1000 standard for "social and ethical accounting, auditing, and reporting," defines accountability as follows: "To account for something is to explain or to justify the acts, omissions, risks, and dependencies for which one is responsible to people with legitimate interest." From this description, it is clear that the notion of accountability is closely related to the concept of responsibility. It belongs to the area of causal responsibility that assigns blame or punishment, and it should ideally also include credit or reward in recognition of corporate success. The primary focus has, however, been on how corporate blame or punishment is appropriated. It is, therefore, understandable that accountability has become associated with corporate control, that is, the establishment of a meaningful way of accounting for corporations' efforts to protect the interests of their shareholders. The notion of corporate sustainability and the introduction of triple-bottom-line reporting have underscored the fact that corporate success can be conceived in nonfinancial as well as in financial terms. Both CSR and CC argue that corporations should be responsive to all stakeholders and not only to shareholders. Instead of defining accountability primarily from the perspective of the fiduciary duties that managers owe to the owners of the corporation, a proper understanding of accountability must now also reflect the mutual dependence between corporations and their stakeholders. From this perspective, accountability refers to the way in which a corporation is able to account for its economic, social, and environmental activities. Social corporate control not only involves the mechanism by which society could respond to corporate failures but also the way in which relationships between corporations and broad groups of stakeholders are proactively sustained.

It is possible to distinguish between "hard" or "involuntary" accountability and "soft" or "voluntary" accountability. Hard or involuntary accountability refers to the kind of accountability that is imposed as a legal, organizational, or societal requirement. This constitutes a more reactive reading of accountability, which focuses on the way in which corporations and their agents are dealt with when something goes wrong. Soft or voluntary accountability is something that the corporation engages in on its own terms and of its own volition. This represents a more positive, proactive approach to accountability in which the corporation actively manages its reputation by fulfilling its responsibilities toward its various stakeholders. It also addresses the way in which the corporation's various agents account for everyday business decisions and actions. Changes in the contemporary business environment, however, make a clear-cut distinction between voluntary and involuntary accountability problematic. In fact, the increasing complexity of business relationships may require a new understanding of accountability, one that is able to deal with multiple stakeholder constituencies, intangible assets, and complex decision-making processes.

Involuntary Accountability

When things go wrong, society wants to hold someone, or some institution, accountable. When corporate scandals such as Enron and WorldCom happen, there is inevitably a demand that those responsible be punished and that stricter penalties and tighter procedures be implemented. Legislation such as Sarbanes-Oxley, therefore, assigns direct accountability for the accuracy of financial statements to specific corporate officers. Corporate control is typically exercised through the enforcement of compliance with processes and procedures, and failures are punished via legal mechanisms.

The assumption that underpins this strategy is that accountability entails controlling conduct and, more particularly, preventing misconduct. There are clear limitations to this strategy. If something is not technically illegal, or if no particular moral agent can be held directly liable for a corporate failure, this form of control ceases to be effective.

Legal Strategies for Effecting Accountability: Assumptions and Limitations

The legalistic strategy for dealing with ethical failures is based on certain assumptions. In the first place, it assumes that there is a direct cause-and-effect relationship between the decisions of individuals and organizations and the negative results of those decisions. It also suggests that decisions and acts are the deliberate responses of rational individuals. One assumes that, to exercise this rational capacity, corporate agents have a clear understanding of the principles or values held within a specific society and the expectations around decisions and actions that these values or principles create. This notion of accountability relies heavily on the belief that decision makers are capable of developing a clear, "objective" view of what is "right" and "wrong" in any given situation. It is also associated with a tendency to unproblematically assume that following certain basic rules will guarantee positive results. It is based on a belief in strict cause-and-effect relationships between individual decision and actions and the consequences of those decisions and actions.

Conventional notions of accountability have, therefore, come to rely on the ability of the individual business practitioner or executive team to consider in an unbiased fashion only the objective rules and facts that pertain to a given situation and to act strictly in accordance with the official mandate that their professional roles afford them. This notion of accountability encourages rule-driven behavior, mirrors the belief in direct cause-and-effect relationships, and suggests that judgments should be based on a factual analysis of right and wrong.

One objection to such an understanding of accountability in business is that it offers too simple and inflexible a way of looking at things. For instance, from this perspective, the individual corporate executive or management team is supposed to be able to base decisions on a full and objective understanding of only the "hard" facts. A command of the "facts" is, however, often gained solely through a survey of the debit and credit entries that are encoded in the double-entry accounting system. The problem with this approach is that the positive and negative values of particular kinds of behaviors and decisions cannot readily be calculated and assessed in terms of this limited evaluative paradigm. The double-entry accounting system is unable to adequately account for so-called intangibles. Markets today are driven as much by perception as by analysis, and the value of brand and reputation in such an environment is as important as it is difficult to quantify precisely and reliably. The trust and respect that an organization or individual comes to command within the business environment is often simply the cumulative effect of countless acts of personal investment in the intangible quality of relationships. Since the effects of these actions are often not immediately apparent, it is difficult, if not impossible, to assess their effect or value in simple, concrete terms and to account for them in the more conventional sense. To discount them, though, would be to ignore one of the major factors that drive business activity today. Within the analyst community, the importance of measuring these variables has been evidenced in the development of metrics that attempt to measure nonfinancial performance. The success of these metrics to account for these often intangible factors will have to be tested over time. What seems clear, though, is that one's ability to get to an accurate reflection of the true state of a business organization's affairs will require an awareness of how the distinction between objective facts and subjective opinions has become blurred in contemporary business life.

Particular occurrences within the business environment are not always decidable in terms of a simple cause-and-effect chain of events. They often emerge as anomalous side effects of the multidirectional interaction of a large number of diverse actors or institutions. As a result, an understanding of accountability structures that depend on strict cause-and-effect relationships between the actions or decision of a rational individual and the negative outcomes of these decisions has become increasingly problematic. In business environments that are characterized by a complex network of multidirectional, interactive relationships between diverse practitioners and institutions, it is the dynamics of the system as a whole that determine the significance of particular actions and decisions rather than individual decision makers. This complicates the ability of the legal system to assign accountability to specific agents.

The study of moral agency is very pertinent to understanding the limitations of legal mechanisms for ensuring accountability. Some contemporary moral theorists propose a radical departure from the notion of an isolated, rational moral agent who acts on a priori universal imperatives and who can therefore be held individually accountable for his or her rational, deliberate decision and acts. It is argued that contemporary business practitioners are not homogeneous and that they do not necessarily function in an independent, rational way. Business practice in an increasingly interrelated, virtual world challenges this understanding of agency. Instead of being calculating, isolated decision makers, business practitioners are compelled to act in relation to, and in interaction with, one another. From this perspective, therefore, moral agency is not located in an isolated individual agent—in fact, it is a thoroughly relational affair.

This view of moral decision making may lead to a comprehensive reconsideration of more conventional notions of moral accountability. From a modernist perspective, normative judgment involved the identification of universal moral principles and the operationalization of appropriate rational protocols for their application to specific problems. A number of 20th-century theorists have, however, challenged this account of normative judgment and objected to it being characterized as a form of a priori principled reasoning. They have drawn attention to the way in which historical contexts, social practices, metaphoric language, as well as his or her embodiment shape the moral agent's moral judgments. In their view, moral judgments reflect tacit knowledge and social grammars that the moral agent is seldom conscious of. Judgments that are made on this basis, it is argued, are neither necessarily purposeful nor willful. In fact, moral knowledge is acquired by an ongoing process of trial and error. The specific actions or decisions of individuals and organizations represent a whole constellation of unarticulated beliefs and half-remembered perceptions. Together, these beliefs and perceptions constitute the corporate culture of a particular organization, which informs the moral sensibilities of individual employees. For instance, an immediate supervisor's example tends to play a more important role in giving an employee direction on appropriate behavior than written codes and policies.

If there is any validity to these proposals, legal mechanisms may prove not only inadequate but also inappropriate as a means of ensuring corporate accountability. If moral decision making is indeed as complex an affair as some theorists suggest, it may prove helpful to explore a more proactive notion of accountability within the context of a dynamic, self-sustaining corporate culture.

Voluntary Accountability

Corporations have come to appreciate the potential benefits of increased stakeholder trust and an enhanced corporate reputation and, therefore, seek to display their commitment to accountability. The assumption underpinning this strategy is that the market will reward a corporation for its commitment to accountability. The market mechanism for ensuring proactive accountability, however, depends on consumer activism and stakeholder interaction. These mechanisms are only effective if individuals and groups have access to reliable information, and if there is a way to measure, compare, and verify corporate reporting. This has led to the development of a whole array of instruments and reporting frameworks that seek to assist stakeholders in assessing the quality and veracity of corporate triple-bottom-line reports. Examples of these are AA1000, SA8000, relevant ISO standards, and the Global Reporting Initiative's guidelines.

The notion of voluntary accountability is reliant on the willingness and ability of a corporation to make accurate corporate information available. As such it requires an uncompromising commitment to transparency on the part of the corporation. The reliance on transparency in the system becomes particularly problematic in cases where ethical failures are already present. Cases such as Enron and WorldCom highlighted the fact that corporations sometimes misrepresent the true state of affairs to keep stakeholders under the impression that all is well. What all this seems to suggest then is that without a general corporate commitment to ethical practices, and more specifically to transparency and honesty, voluntary accountability becomes untenable.

Corporate misrepresentations are not only the result of a lack of transparency. In the case of Enron, it was exacerbated by the fact that certain professions, which were supposed to act as checks and balances within the system, failed to do so. Professions have since become more strictly regulated than ever before, precipitating the implementation of involuntary accountability in professional environments that could previously pride itself on its ability to self-regulate.

It seems as though the notion of voluntary accountability becomes increasingly untenable in a context where the public cannot trust corporations and the professions that support them. It also seems unlikely that involuntary accountability, enforced through enhanced legislations and heavier penalties, could rebuild the trust relationship between corporations and their stakeholders once it is compromised. It may, therefore, prove necessary to pursue a third kind of accountability, one that seeks to use more dynamic, relational mechanisms to account for corporate actions. Accountability, from this perspective, becomes an emergent property of a complex network of institutions, organizational practices, and multiple stakeholder interactions.

Accountability as Responsiveness Within Complex Corporate Environments

There is evidence to suggest that the notion of the complex adaptive system may be the most appropriate way of interpreting and understanding the dynamics of today's business environment. Multinational organizations are increasingly becoming more powerful than national governments, and increasing decentralization grants corporate entities more freedom to explore new partnerships and associations. As companies seek and terminate strategic partnerships, and as they introduce new strategies and products, the economic landscape is constantly transformed, making business a far more volatile and uncertain affair. These dynamics have the effect of moving the business environment toward a greater degree of interrelation and complexity. In the process, multiple interdependent cooperation networks are created, and an organization's success depends on its ability to navigate this intricate network of relationships. Some theorists describe the increasing dematerialization and decentralizing within contemporary business as a shift from a representationalist to a relational understanding of the economy. Wealth creation is no longer understood as the orderly accumulation of capital through the scientific application of objective economic principles, but as something that takes place primarily within the context of ongoing relationship building and reputation management.

This may require a broadening of our understanding of accountability. We usually think of moral agents as being accountable *for* something. However, we may expand our understanding by also considering what it would mean for a moral agent to be accountable *toward others* or *in terms of* some form of normative orientation. The notion of being accountable *for* something is usually associated in the business environment with responsibility for a set of defined concrete assets. There is merit in this, but it may be insufficient within the context of an open network of interactive relationships where perceptions and other intangible dynamics play such a crucial role. It may, therefore, be more meaningful for individual business practitioners and organizations to consider their responsibilities in terms of the obligation to be accountable *toward* those who participate with them in this extended network of functional relationships. To do so would be to acknowledge that much of the value of an organization is generated in and through multiple relationships and that the quality of these relationships represents the organization's most valuable assets. The emphasis in such an approach is on the way in which an organization and its employees engage with and respond to its partners and competitors within an extended network of reciprocal business relationships. In addition, the nature and limits of an individual or organization's moral responsibility toward those with whom they interact could be clarified if it was understood *in terms of* a particular relational form of moral orientation. This is an approach that remains cognizant of the fact that an individual's professional inclinations and an organization's moral priorities develop relationally in the course of the interpersonal interaction between agents within a system of relations as well as under the influence of contact with alternative perspectives that may enter the system from without. The tacit sense of reciprocal responsibility, loyalty, and common cause that develops among colleagues and collaborators in this way may resist formal articulation in the form of rules and procedures, but they nevertheless form the normative backdrop against which the actions and decisions of individuals and organizations become intelligible. As such, it is also an understanding of the nature of accountability that acknowledges the need for discretion and discernment. It also relies on the nurturing of normative orientations in and through the corporations' multiple relationships and activities. Accountability is simultaneously the effect of the decisions and actions of individual agents and the systemic forces operating within the system as a whole.

From this perspective, accountability is not something that can be institutionalized in any final, intransigent form. Instead, accountability requires that individuals and corporations remain constantly aware of the changing dynamics of the interactive network of stakeholder relationships in which they participate. Accountability within a highly dynamic contemporary business environment is likely to be enhanced by both voluntary and involuntary mechanisms, but perhaps, it requires most of all that individuals and corporations remain responsive to the duties that emerge from participation in a broad matrix of dynamic stakeholder relationships. It remains the task of business ethicists and practitioners to be attuned to these dynamics and to constantly work toward the development of new ways of fostering this ongoing responsiveness within organizations.

—Mollie Painter-Morland

See also Corporate Citizenship; Corporate Social Responsibility (CSR) and Corporate Social Performance (CSP); Enron Corporation; Moral Agency; Sustainability; Triple Bottom Line

Further Readings

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Accounting, Ethics of

Accounting ethics determines the ethical obligations and responsibilities of an accountant. A professional accountant has an obligation to record, provide, and attest to information regarding the economic affairs of an organization. The fundamental ethical responsibility of an accountant is to fulfill this obligation, which is crucial to the functioning of commerce in any market. All other ethical responsibilities of the accounting professional are derivative on the performance of this task.

Originally, financial records were kept by and for the person who used the information. As economic and market systems grew more complex, the nature of the information required for the successful functioning of the economic systems became more complex as well and the demand for this information by various stakeholders increased. These two factors combined with the ever increasing volume of data led business owners and decision makers to request the services of a professional accountant.

To fully understand this definition, it is necessary to examine each of the three constituent parts; the first requirement is to record information. The accountant is required to accurately record the debit and credit entries produced by a specific person or organization. The second requirement is to provide this record to the legitimate users of the information. Legitimate users span the spectrum of stakeholders and there are four different reasons why users would seek this information: The first is that managers of the organization need the information provided by professional accountants to effectively plan and control the organization's operations. For example, if a certain division is consistently losing money despite repeated investments of time and treasure, it would be very helpful for a manager to have this information. The second is that investors use the information to determine which organizations would be a good investment for them based on their own risk tolerance and other factors.

Third, rating agencies, lenders, and other groups use this information to assess the value of the organization and make decisions about its viability and future. Finally, the government uses this information to determine how much tax should be levied on an organization.

The third obligation requires the accountant to attest to the truthfulness of the information they provide to the users. Accountants, then, are asked to affirm that the information that they have recorded and provided to legitimate users is true to the best of their knowledge. This formal act of attestation is manifested through the signature of the accountant.

However, the notion of a "true" and "accurate" picture presents a problem. Similar to the adage regarding the malleability of statistics, there are any number of ways to interpret the economic data of an organization. Therefore, it is possible to present several different pictures of a company that either highlight or shadow the strengths and weaknesses of the organization depending on the circumstances. For example, a picture developed by a corporate accountant for the purposes of securing a loan can make an organization appear healthy and strong. On the other hand, if the picture is being developed for submission to the Internal Revenue Service (IRS), the outlook is likely to be far less rosy. Quite often the picture developed by the professional accountant serves the interest of the party who hired the accountant more than the interests of other parties who need information concerning the organization.

The Ethical Considerations

The question often asked is, "Why is an accountant obliged to disclose the true picture of the organization?" In response, it is possible to argue that accountants provide information, and if this information persuades people to act in one way or other, and their action either benefits or harms the persons giving or getting the information, such information giving takes on ethical importance. Depending on the use, giving out information can be very much like selling. For example, the CEO may be selling the board or the stockholders on the soundness of a company's financial situation. His or her bonus might be tied to how rosy a picture he or she is painting. The worth of his or her stock options may rest on the financial picture he or she is able to present. At the same time, the CEO is selling the IRS a different picture of the company, and still a different one to potential investors and/or lenders. Since accounting involves presenting the product to be sold, it enters into and influences market transactions.

In the ideal market transaction (assuming the ethical probity of the market system), two people decide to exchange goods because they believe that the exchange will make both better off. Ideally, there is perfect information about the worth of what is being given and gotten in return. If one of the parties involved in a market exchange is misled into believing a product is not as it is being represented, then the effect of both sides being better off is undermined. The deceived party most likely would not have *freely* entered into the exchange had that party known the full truth about the product. If the true picture of the company had been available, the bank would not have made the loan, the public offering of stock would not have been so successful, and the bonus for the CEO would not have been so large. The bottom line is that the conditions for an ideal market transaction include *informed consent.* Informed consent cannot be presumed if one lacks adequate knowledge of the product one is acquiring. The purpose of misrepresentation is to get someone to act in a way detrimental to them and beneficial to the one doing the misrepresentation, which they would not do if they knew the truth. In these cases and others like them, the manipulation and withholding of information is not "creative accounting," it is simply an unethical action.

What Sort of Disclosure and Auditing Requirements Do Accountants Face?

In the United States, the Securities and Exchange Commission (SEC) oversees financial statements of corporations. Despite the proliferation of "watchdog" groups, the accounting profession is largely self-regulating. It was the self-regulatory nature of the industry that caused a great deal of controversy during the accounting scandals of the late 1990s. Financial statements continued to be prepared by the company's own accountants and "independent" accountants. Certified public accountants (CPAs) in the United States and chartered accountants in United Kingdom audit the financial statements. CPAs and chartered accountants are responsible for certifying that the companies' financial statements are *complete* in all material aspects and the figures have been arrived at through the *use of acceptable measurement principles.* These watchdog functions were set up to protect the integrity of the financial systems.

Watchdog Organizations

There are several watchdog organizations that are charged with overseeing the accounting industry. To ensure that the financial statement provided by the accountant gives a reliable and useful picture of the financial affairs of an organization, guidelines have been developed by the profession itself. The accounting practice in the United States rests on a conceptual framework, which can be described as a coherent structure of objectives and ideals that are expected to promote consistent standards for the entire profession. The first watchdog group is the Financial Accounting Standards Board (FASB), which is one of the organizations designated to establish standards for the financial accounting and reporting that govern the preparation of financial reports. FASB develops both broad accounting concepts and specific standards for financial reporting. In addition, FASB offers guidance regarding the implementation of these concepts and standards, and their mission states that the FASB is also engaged in educating both the profession and the public. Although the FASB is composed of members of constituent organizations with an interest in financial reporting, the board itself is independent from the other organizations.

A second watchdog group is the Governmental Accounting Standards Board (GASB), the counterpart of FASB for state and local government. The GASB describes its purpose as to both establish and improve the standards of state and local accounting and reporting to provide useful information and educate the public. A third group, the Financial Accounting Foundation (FAF), provides oversight and funding for the FASB and the GASB. A fourth group is the Public Company Accounting Oversight Board (PCAOB), which is a private, nonprofit corporation, created by the Sarbanes-Oxley Act in 2002. PCAOB is charged with the oversight of the auditors of public companies to protect the interests of the public in general and investors in particular. Finally, the American Institute of Certified Public Accountants (AICPA) is a national, professional association responsible for providing its members, who are all CPAs, with the resources and information to perform their jobs well and contribute to the public interest. In addition, it was the AICPA that designated the Federal Accounting Standards Advisory Board (FASAB) to establish accounting principles for federal entities. FASAB created a framework referred to as the Generally Accepted Accounting Principles (GAAP). GAAP encompasses the set of principles and guidelines for the recording and summarizing of transactions in the preparation of financial statements. Every country has its own version of the GAAP.

The AICPA Code of Ethics

The purpose of ethics in accounting is to preserve public trust in the profession and to maintain its integrity. Statements of the profession's ethics are found in the rules and regulations of the AICPA, state accounting societies, the SEC, the General Accounting Office, and the PCAOB. Since rules and regulations are in constant change, however, accountants are guided first and foremost by professional codes that reflect the enduring ethical principles of the profession.

The AICPA, for example, has promulgated a code of professional conduct for public accountants, which the organization maintains and enforces. The Institute of Management Accountants (IMA) and the Institute of Internal Auditors (IIA) have also established codes of ethics. These codes provide guidelines for responsible behavior by accounting professionals. The codes are largely consistent, in that they all emphasize integrity, objectivity, confidentiality, and competency. The following principles capture the primary ethical concerns for the accounting profession.

Integrity

Integrity is an element of character that entails performing work honestly, diligently, and responsibly. Integrity refers to the professionalism displayed by accountants, particularly as this professionalism (or lack thereof) affects public confidence and the trust of stakeholders. The notion of professionalism has proved particularly important in the wake of recent scandals, where a lack of professionalism has resulted in deterioration of this trust.

Integrity, considered fundamental to the accounting profession, requires accountants to be honest and forthcoming with information. Accountants are expected to respect client confidentiality with regard to their personal communications. This means that, as long as fraud is not suspected, accountants are expected to remain silent regarding client communications. Only if legally required to do so are accountants permitted to disclose confidential information without the authority of the client. Accountants are responsible for the financial statements they certify; if they have suspicions or knowledge that information on the financial statements is not accurate, they are required to do what is necessary (including revising the information or conducting further investigation) to ensure that the financial statements they certify are accurate.

Objectivity

Objectivity refers to the necessary independence and freedom from conflicts of interest. When providing auditing and other attestation services, accountants are expected to be independent in fact and appearance. Accountants are required to advise all parties of any actual, apparent, or potential conflicts of interest.

Objectivity is a distinguishing characteristic of the accounting profession. Whereas other professionals—such as lawyers and doctors—are named advocates of their clients/patients, accountants are explicitly not advocates—at least not in the traditional sense. On the contrary, accountants are expected to be honest and impartial. In this way, their assessments of their clients' financials can be considered valid and trustworthy.

The principle of objectivity, therefore, has two key components: impartiality and disclosure. Accountants are expected to behave impartially, and they are required to disclose any information that could be viewed as distorting their assessments.

Competency

Competency is fundamental, and professional accountants are required to maintain an appropriate level of professional expertise. They are expected to do this through the ongoing development of knowledge and skills, such as through continuing education programs. In addition, they are required to have knowledge of relevant laws and regulations, and they are required to behave consistently with those standards.

This is also referred to as "due care." This requires accountants to treat their responsibilities competently, to the best of their ability, in the best interest of those being served.

Client Interest/Public Interest

A further obligation, which accountants have and which accrues to all professionals, is to look out for the best interest of the client. The accountant is hired to perform a service for the client. Given that, it goes without saying that when an accountant accepts a position with a client, there is at the very least an implied understanding that the accountant will look out for the interests of the client.

But the accountant's code of ethics is unique in the emphasis that it places on an often overlooked obligation specific to the accountant, the obligation to the public. Since accountants have a responsibility to all those who use their professional services, they are different from most professionals. Most professionals have an overriding responsibility to their client, but accountants, whose role in the financial markets is so crucial, have numerous constituencies depending on the information that only they can provide. Professions such as law and medicine are clearly client oriented. Doctors and lawyers would state that their first, and possibly only, obligation is to their patient or client, subject only to the constraints of some higher moral principle, for example, a lawyer cannot suborn perjury. A distinguishing mark of "public" accountants is that their primary obligation is to the public, and in a broader sense to the truth—the accuracy or veracity of the financial statements they deal with. Because the scope of their responsibility extends to all those who use the information, accountants have prima facie responsibilities beyond those to their clients, or to those who pay their fee.

It follows that if accountants are responsible to various groups—clients, colleagues, and the public—they will inevitably face conflicting pressures from each of the groups. How is one to handle these pressures? The AICPA code of ethics suggests that the best interest of the client is served when accountants fulfill their responsibility to the public. This passage reveals an interestingly optimistic motivation for being ethical. It claims that there cannot be a substantial conflict between the public, clients', and employers' interests. In doing what is right for the public, the client's and employer's interests are best served. Hence, it follows that if an employer pressures a management accountant to "cook the books," the accountant should not acquiesce, not only because it would not be in the public's best interest but also because it would not be in the employer's interest. In short, the code assumes that ethical business is always good business. Therefore, accountants are encouraged to interpret interests in such a way that even though something appears to be in a client's or employer's interest, if it is not in the public's interest, then that appearance is false and misleading.

Accounting Roles

While the major function of the accountant is to present a picture of the financial affairs of an organization, accountants play many other roles. We will examine the roles of auditing, managerial or financial accounting, and tax accounting—and the consequent ethical responsibilities that they bring. We will look briefly at the role of consulting and the difficulties it brings with respect to conflict of interest and independence, particularly for accountants or firms who are fulfilling both auditing and consulting roles for a client.

Auditing

Perhaps the most important role of the accountant is the role of the independent auditor. The function of the auditor (internal or external) is to determine whether the organization's estimates are based on formulas that seem reasonable in light of whatever evidence is available and to make sure that the same formulas are applied consistently from year to year. Thus, the accountant has to ensure both reasonable and consistent application. Given the way financial markets and the economic system have developed, society has carved out a role for the independent auditor, and this role is absolutely essential for the effective functioning of the economic system. If accounting is the language of business, it is the auditor's job to make sure that the language is used properly so that relevant material is communicated accurately.

The classic statement of the function and responsibility of the external auditor is given by Justice Warren Burger in the 1984 landmark Arthur Young case. In his opinion, Justice Burger insisted that the auditor had several responsibilities; the first is to issue an opinion as to whether the financial statement fairly presents the financial position of the corporation. The second responsibility is for accountants to protect themselves from undue influence (or even the appearance of undue influence), since any blemish on the reputation of a professional auditor undermines the accuracy and credibility of the financial picture that he or she presents. Finally, professional auditors and those who manage them must do everything in their power to bolster the public trust in their industry. Given the conflict of interests between the public and clients, it is clear that auditors face conflicting loyalties.

Another responsibility of the auditing profession is to report on any significant uncertainties that are detected in financial statements. To perform this task, the *Statement on Auditing Standards* recommends an attitude of professional skepticism in which the auditor assumes neither honesty nor dishonesty on the part of management and considers evidential matter objectively to see whether they are free of material misrepresentation. This requirement of skepticism makes it clear why there needs to be independence on the part of the auditor.

The reasons for avoiding even the appearance of having a conflict of interest, as Justice Burger suggests, are obvious. The first is that for people to make informed decisions they need faith in the information that they use to make those judgments. And information provided by people who have, or even appear to have, conflicting interests does not inspire such faith. Reasonable people, taking a commonsense approach to human behavior, tend to think that certain relationships affect one's behavior. The second reason is that although there may indeed be no conflict at all, the appearance of conflict is sufficient to weaken public trust and inspire public cynicism concerning the auditing industry. Finally, even if the auditor continues to act appropriately in a situation of conflict, such a situation presents a temptation that, while it is currently being resisted, will sooner or later likely prevail.

Managerial Accounting

A second role for accountants is that of a managerial accountant. Businesses need controllers and internal auditors since they need in-house accountants, whose role is to give the most accurate picture of the economic state of the organization so that it can flourish. But to the extent that the board, managers, and shareholders can be at cross-purposes, the accountant is conflicted. These conflicts create the grounds for many ethical problems.

The accountants within the firm, whether they work for the firm as financial officers, valuations experts, or bookkeepers, have responsibility for the picture of the firm's financial situation that is portrayed. There is an obligation to represent the firm as accurately and truthfully as possible, even if this representation may be detrimental to the company. One could say that while the management accountant has a responsibility to the firm that is his or her employer, the management accountant has an overriding obligation to disseminating the truth.

According to their ethics code, management accountants have obligations to at least four stakeholders—the general public, the members of their profession, the organization they serve, and themselves. The primary obligation of the management accountant is to present as accurate a picture as possible of the financial situation of the company, including assets and liabilities and as good advice as possible to all those entitled to it based on that picture. Consequently, the basic function of accountants does not change whether an individual is an auditor or a managerial accountant. This is the case since the use of independent judgment, with complete freedom, is required of both public and managerial accountants.

Because of the management accountant's special obligation of fair reporting, the accounting function should be kept separate from the rest of the management process. This is not only ethically sound, it is managerially wise. To make decisions about a company it is important, even for those within the company, to have as accurate a picture as possible of the company's financial condition. The managerial accountant has a clear responsibility to the company and its stakeholders to tell the truth about the financial state of the company, and this obligation overrides their responsibility to do what the president asks, if what the president asks is to mask the true picture of the company.

Tax Accounting

A third role for accountants is the determination of tax liabilities for clients, either individual or corporate. The tax accountant has further responsibilities to the public, on account of the relation of his or her role to the government's right and responsibility to impose tax. The first responsibility is that the tax accountant has an obligation not to lie or be party to a lie on a tax return. The second responsibility is that as an attester the tax accountant declares, under penalty of perjury, that the return and accompanying materials are accurate and complete. This attestation indicates a responsibility to both the client and the public to be forthright and, at the very least, not to be complicit in a client's attempt to deceive, even if that means breaking off the relationship with the client. These responsibilities flow from the nature of the tax system. The tax system, which depends on self-assessment to function effectively, needs everyone to give honest assessments and pay their fair share of taxes.

Thus, tax accountants have a duty not only to their clients but also to the system. The client's duty is to pay the taxes they legally owe, no more no less. The taxpayer has the final responsibility for the representation of the facts and for the positions taken on the return, but the accountant has the responsibility to point out to the client what is legally owed and not owed and the responsibility not to go along with a client who wants to take advantage of the tax system.

Some object that the above representation is naïve and even unjust, since certain taxes are unfair. However, fairness is a notoriously ambiguous concept, and in applying it to the evaluation of tax burdens, the most prudent course is that of adhering to what the society, following its due process of passing determining legislation, decides is fair. The founding fathers of the United States did not rail against taxes so much as taxation without representation. There should be general agreement to go with what the current tax demands are and, if one thinks such demands are unfair, work through the proper procedures to change them. Furthermore, not only is working within the system called for, more recent emphasis claims that the tax accountant should be ruled by the spirit of the law and not just the letter of the law.

Defenders of tax-evasion schemes will argue that these evasion activities are necessary given the competition of the marketplace. They will refer to Oliver Wendell Holmes's view that we should not pay one iota more than the law allows. Still, every law, being composed by fallible human beings, will have a loophole that can be exploited. It can be argued that it is contrary to the principle of fairness and the promotion of public welfare in attempting to circumvent the obvious purpose of a specific law to facilitate clients paying less than their determined share of taxes. Furthermore, there is general agreement that ethically a tax accountant should not recommend a position that "exploits" the IRS audit selection process or that serves as a mere "arguing" position. Taxation, as much as one does not like it, is the human invention that centralizes the sharing of the expense of performing government functions in a fair and equitable manner. To view accounting as a profession best employed in dodging those expenses is an unethical distortion of the role of the accountant.

Implicit in all the above arguments is a recognition of the responsibility of the accountant and firms to uphold the soundness of our tax system—to draw the delicate balance between intended tax advantages and loopholes that undermine the system.

Financial Planning

More and more accountants are engaging in a fourth kind of activity, which springs from their knowledge of tax law and financial investment markets—financial planning. One could argue that this is not a role of an accountant as such, but rather a role an accountant is well qualified to take on given some of his or her areas of expertise.

Consulting

Finally, there is the area of consulting. Since accountants are so familiar with the financials of companies, they become quite valuable for companies as consultants in helping with money management, income distribution, and accounting and auditing functions. Here, too, we could argue that this is not a role of an accountant, as such, but a potential role an accountant can play based on his or her particular experience.

The performance of all these different functions, and in particular the adoption of roles such as consultant and financial planning roles, has caused the accounting profession to move from the more traditional profession of the auditor to the more entrepreneurial professions of consultant and planner. Many claim that these moves have created a crisis for accountants. The face of accounting is changing, if not in accounting itself that maintains the same functions—auditing, attesting, preparing taxes, and running the financials of a company—then at least in the make-up and orientation of the larger, and sometimes the smaller, accounting companies.

The Role of Education

Education and professional development play a particularly significant role in the accounting profession. Particularly since Sarbanes-Oxley, ongoing education is essential for accountants to remain competent and knowledgeable regarding the many rules and regulations governing the accounting profession.

There are numerous resources available today for accountants. In addition to the continuing education courses offered by numerous providers in every state, there are also books, pamphlets, and Web resources readily available.

Conclusion: Ethical Implications of Accounting

In spite of the numerous rules and regulations and professional codes, not all ethical problems are resolved successfully by accountants, as demonstrated by the troubles at WorldCom. The accounting industry suffered an additional blow when, in June 2004, the Securities and Exchange Commission (SEC) announced that Symbol Technologies, Inc., a recognized leader in providing mobility products and solutions, agreed to pay a $37 million penalty for fraudulent accounting practices and other misconduct. Then, in September 2004, the SEC announced the settlement of fraud charges against Computer Associates International, Inc., one of the world's largest IT management software providers, and three of the company's former top executives. It was found that the company prematurely recognized billions of dollars of revenue. Although accounting fraud continues, the consequences are becoming increasingly severe as the public (and other stakeholders) has indicated that unethical accounting behavior will not be tolerated.

—Ronald F. Duska, Brenda Shay Duska, and Julie Anne Ragatz

See also Accountability; Adelphia Communications; American Institute of Certified Public Accountants (AICPA); Arthur Andersen; Enron Corporation; Financial Accounting Standards Board (FASB); Sarbanes-Oxley Act of 2002; Securities and Exchange Commission (SEC); Tyco International; WorldCom

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Acid Rain

Acid rain is a term that is used to describe the several ways in which acids fall out of the atmosphere and reach the earth. *Acid deposition* is a more precise term that can be used to describe this phenomenon, which has both wet and dry aspects. Wet deposition refers to acidic rain, fog, and snow, which fall to the ground and affect a variety of plants and animals. What effect the acid deposition has depends on many factors, including the acidity of the water, the chemistry and buffering capacity of the soils affected, and the types of fish and trees and other living things relying on the water. Dry deposition refers to acidic gases and particles that are blown about by the wind onto buildings, cars, homes, and trees. These gases and particles can also be washed from trees and other surfaces by rainstorms, adding to the acidity of runoff water.

Acid rain is traceable to the burning of fossil fuels in power plants, factories, and smelting operations and, to a somewhat lesser extent, the burning of gasoline in automobiles. It is believed to be largely a man-made problem, as the burning of fossil fuels releases sulfur dioxide, nitrogen oxides, and traces of toxic metals such as mercury and cadmium into the atmosphere to mix with water vapor. Acid rain then results from chemical reactions that follow to produce dilute solutions of nitric and sulfuric acids. Sunlight increases the rate of most of these reactions. These solutions then come down to the ground level in the form of either rain, hail, snow, or fog or as dry particles. They may travel hundreds of miles before falling to the ground and do not respect political or national boundaries.

These acid depositions are formally defined as having a pH level under 5.6, compared with a neutral solution that has a pH level of 7. Most of the acid rain falling in the United States has a pH of about 4.3. The pH levels of acid rain and the chemicals that cause it are monitored by two networks supported by the Environmental Protection Agency (EPA). The National Atmospheric Deposition Program measures wet deposition and discloses through its Web site maps of rainfall pH and other important precipitation chemistry measurements. The Clean Air Status and Trends Network measures dry deposition and discloses information about the data it collects, the measuring sites, and the kinds of equipment used.

Acid rain is believed to cause many serious environmental problems. When it enters a body of water, acid rain carries a deadly burden of toxic metals that can stunt or kill aquatic life. Many lakes that had previously supported fish life became fishless due to their high acid content. As the buffering effect of the acid-neutralizing minerals in the water diminishes, lakes appear to die suddenly and turn clear and bluish. Surface waters that have a low acid-buffering capacity are unable to neutralize the acid effectively and are quickly affected.

Snowmelt in Northern areas can quickly kill a lake as all the acids accumulated in the snow are released at once. Because of the freezing point depression phenomenon combined with the recrystallization of snow after it falls, the most acidic snow crystals will melt first, thereby releasing 50% to 80% of the acids in the first 30% of snowmelt.

When acid rain is absorbed into the soil, it can rob plants of nutrients because it breaks down minerals containing calcium, potassium, and aluminum. This aluminum may eventually reach lakes through water tables and streams and further contribute to the suffocation of fish. Acid rain is suspected of spiriting away mineral nutrients from the soil on which forests thrive. Areas with acid-neutralizing compounds in the soil can experience years of acid rain without serious problems. But the thin soils of the mountainous and glaciated Northeast have very little buffering capacity, which makes them vulnerable to damage from acid rain. It contributes to the damage of trees at high elevations and can have a corrosive assault on buildings and statutes and sculptures that are part of our nation's cultural heritage. Acid rain can also affect water systems, which costs millions of dollars annually. It can degrade visibility and may also pose a substantial threat to human health principally by contaminating public drinking water.

Over 80% of the sulfur dioxide emissions in the United States originated in the 31 states east of or bordering the Mississippi River, and more than half the acid rain that fell on the eastern United States originated from the heavy concentration of coal-and-oil burning power and industrial plants in seven central and upper Midwestern states. Prevailing winds transported these emissions hundreds of miles to the Northeast across state and national boundaries. The acidity of the precipitation falling over much of this region had a pH of 4.0 to 4.2, which was 30 to 40 times greater than the acidity of the normal precipitation that fell on this region.

Before the 1970 Clean Air Act, sulfur dioxide and nitrogen oxide emissions in the United States were increasing dramatically. Between 1940 and 1970, annual sulfur dioxide emissions had tripled. By 1986, however, after pollution control equipment had been installed on many facilities, annual sulfur dioxide emissions had declined by 21% and nitrogen oxide emissions had increased by only 7%, even though the economy and the combustion of fossil fuels had grown substantially over the same time period. More reductions, however, needed to be accomplished to solve the problem.

The new Clean Air Act passed in 1990 contained provisions for large reductions in emissions of sulfur dioxide and nitrogen oxides to reduce acid rain to manageable levels. By the year 2000, sulfur dioxide emissions were to be reduced nationwide by 10 million tons below the 1980 levels, a 40% decrease. Emissions of nitrogen oxide were also to be reduced by 2 million tons below levels that would occur in the year 2000 without new controls. This represents about a 10% reduction from the 1980 levels. These reductions were to be achieved by instituting a variety of reforms aimed at limiting emissions after 1995 from electric power plants and other sources.

Reductions in sulfur dioxide were to be obtained through a program of emission allowances where each utility can "trade and bank" its allowable emissions, something of a market-based approach to pollution control. It was hoped that this program would achieve regional and national emission targets in the most cost-effective manner. Power plants covered by the program are issued allowances that are each worth 1 ton of sulfur dioxide released from smokestacks during a specified year. To obtain reductions in sulfur dioxide pollution, these allowances are set below the current level of sulfur dioxide releases.

Plants can release only as much sulfur dioxide as they have allowances to cover. If a plant expects to release more sulfur dioxide than it has allowances, it has to buy allowances from plants that have reduced their releases below their number of allowances and therefore have them to sell or trade. These allowances can be bought and sold nationwide, with stiff penalties for plants that release more pollutants than their allowances cover.

The program to reduce nitrogen oxide emissions has many of the same features as the sulfur dioxide trading program. It also has a results oriented approach, flexibility in the method to achieve emission reductions, and maintenance of program integrity through measurement of emissions. However, it does not cap emissions nor does it use an allowance-trading system. Emission limitations for boilers that emit nitrogen oxides provide flexibility by focusing on the emission rate to be achieved and give options for utilities to meet the emission limitations in the most cost-effective manner and allow for the development of technologies to reduce the cost of compliance.

The acid rain program supposedly allows sources to select their own compliance strategy rather than having this dictated by the federal government with a command-and-control approach. They can use coal containing less sulfur, wash the coal, or use devices called scrubbers to chemically remove pollutants from the gases leaving smokestacks. They can also use a cleaner burning fuel such as natural gas or reassign some of their energy production from dirtier units to cleaner ones. Sources may also reduce their electricity generation by adopting conservation or efficiency measures or switch to alternative energy sources such as wind power or solar energy.

In its 2003 progress report, the EPA reported that in that year there were 10.6 million tons of sulfur dioxide emissions, which represented a 38% reduction from the 1980 levels. The program was thus on target to reach its goal of 8.95 million tons by 2010. Nitrogen oxide emissions stood at 4.2 million tons, which were close to 4 million tons less that forecasted for 2000. The electric power industry achieved nearly 100% compliance with the requirements of the program as only one unit had emissions exceeding the sulfur dioxide allowances that it held and no units were out of compliance with the nitrogen oxide program.

This report also indicated that over the last decade (1) ambient sulfur dioxide and sulfate levels are down more than 40% and 30%, respectively, in the eastern part of the country; (2) wet sulfate deposition has decreased 39% in the northeastern United States and 17% in the southeastern United States; (3) some modest reductions in inorganic nitrogen deposition and wet nitrate concentrations have occurred in the

Northeast and Mid-Atlantic regions, but other areas have not shown much improvement; and (4) signs of recovery in acidified lakes and streams are evident in the Adirondacks, the northern Appalachian Plateau, and the upper Midwest. These signs include lower concentrations of sulfates and nitrates and improvement in acid-neutralizing capacity.

Acid rain is also a problem in Europe as well as in Russia and China. Due to industrialization across Europe during the 1970s and 1980s, acid deposition became a particularly prevalent problem across the region. Pollution across national boundaries is a problem there due to the relatively small size of countries. To deal with this problem, the United Nations Economic Commission for Europe implemented the Convention on Long Range Transboundary Pollution in 1979, and since its implementation, sulfur emissions have fallen significantly. But with the increase in vehicle traffic across Europe, nitrogen oxides emissions have been reduced only slowly.

The United Kingdom has been called the dirty old man of Europe because it emits more pollution than is deposited there. Sulfur and nitrogen emissions are carried to other countries further east because of prevailing wind conditions. Most of the sulfur dioxide comes from power stations, while the largest source of nitrogen oxides is road transport and power stations. The 1998 Gothenburg Protocol requires the United Kingdom to reduce sulfur emissions by 85% and nitrogen emissions by 49% by the year 2010 from the 1980 levels. To meet these goals, emissions of sulfur dioxide in the United Kingdom are being reduced through the use of cleaner technology in power stations and the use of cleaner fuels and car engines in the transport sector.

—Rogene A. Buchholz

See also Emissions Trading; Environmental Protection Agency (EPA); Pollution; Regulation and Regulatory Agencies

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ACORN

See Association of Community Organizations for Reform Now (ACORN)

Adelphia Communications

Founded by brothers John and Gus Rigas in 1952, Adelphia Communications Corporation eventually became the dominant cable provider in southern Florida, western New York, and Los Angeles. In addition to cable entertainment, the publicly traded firm offered high-speed Internet access, long-distance telephone service, digital cable, home security, and paging. The company was admired for its aggressive growth and was recognized for industry leadership. By the early 2000s, Adelphia was one of the largest cable television companies in the United States, and John's sons, Michael, Tim, and James, were executives and members of the board of directors at Adelphia.

Adelphia filed for reorganization under Chapter 11 of the U.S. Bankruptcy Code in June 2002, shortly after the Rigas family executives resigned their positions. The events leading to the bankruptcy highlight the misconduct that can occur when a firm's corporate governance system is weak. In addition to the use of corporate jets for personal business, off–balance sheet loans were made to Rigas family members. For example, Adelphia helped fund the family purchase of a golf course and the Buffalo Sabres hockey team. John Rigas's daughter and her husband, who served on Adelphia's board of directors, lived rent-free in a Manhattan apartment owned by Adelphia. A Rigas-owned farm made most of its revenue by performing snow removal, landscaping, and related services for

Adelphia. A Rigas relative was paid nearly $13 million for furniture and design services in 2001.

Adelphia was a public firm with thousands of stockholders. However, the Rigas family controlled the firm with over 50% of the share votes, despite holding only 11% of the shares. This dual-stock structure, along with the executive power held by Rigas family members, set this corporate governance scandal apart from those at Enron and WorldCom. The U.S. Securities and Exchange Commission (SEC) detailed evidence of $2.3 billion in off–balance sheet debt, inflated earnings, falsified operations statistics, and blatant self-dealing by the family.

Adelphia pursued a lawsuit against Rigas family members and 20 companies controlled by the family. The lawsuit focused on violations of the Racketeer Influenced and Corrupt Organizations Act, including a breach of fiduciary duty, abuse of control, waste of corporate assets, and substantial self-dealing. Adelphia's external auditor, Deloitte & Touche, paid $50 million to settle SEC charges stemming from its audit of Adelphia's fiscal year 2000 financial statements. Adelphia paid $715 million to settle charges with the SEC and United States Department of Justice, while the Rigas family forfeited more than $1.5 billion in assets. The scandal caused losses to investors of more than $60 billion.

In mid-2005, 80-year-old John Rigas was sentenced to 15 years in prison after a U.S. District Judge rejected his plea for leniency. Timothy Rigas was sentenced to 20 years in prison, while other cases are yet to be determined. Observers noted that the sentences sent a clear signal about the extent to which white-collar crime would be punished. Under its bankruptcy reorganization plan, most of Adelphia's assets were to be sold to Time Warner and Comcast.

—Debbie M. Thorne

See also Corporate Governance; Scandals, Corporate

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Administrative Procedures Act (APA)

The Administrative Procedures Act (APA) governs the way federal agencies make and enforce regulations. First made law in 1946, it was the product of concern about the rapid increase in federal agencies and their power at the beginning of the 20th century. Federal agencies were not new—the first was authorized in 1789 to estimate appropriate import duties. Over the next 120 years, about one third of federal peacetime agencies came into being. In just 30 years, from 1900 to 1930, another third was established. President Roosevelt then used federal agencies extensively to implement New Deal programs. The amount of government authority wielded by these new agencies focused attention on competing policy issues.

Agencies are extensions of the executive branch of government that have the ability to make rules and interpret and enforce them, which combines executive, legislative, and judicial functions in a nonelected body. This structure seems to some to upset the balance of powers among the three branches of government. Others argue that the protection from tyranny comes, not from separating these powers, but from a system of supervision: The legislature supervises and the judiciary reviews administrative actions. Either way, agencies serve an important pragmatic need to move more quickly and in more detail than Congress can to deal with specific issues. Often, they are called on to apply specific scientific, technical, or administrative expertise to implement the broad policy decisions made by the legislative branch.

In 1938, President Roosevelt commissioned a full study of existing administrative procedures and recommendations for change. Before the committee report could be issued, Roosevelt vetoed a bill that would have placed administrative agencies directly under the courts, allowing judicial review of all agency decisions (the 1940 Walter-Logan bill). He indicated in his veto message that a report would soon address comprehensive regulation of federal administrative processes.

The 1941 report by the committee of lawyers, jurists, scholars, and administrators laid the groundwork for the APA. The purposes of the act are (1) to require agencies to keep the public informed of their organization, procedures, and rules; (2) to provide for public participation in the rule-making process; (3) to prescribe uniform standards for the conduct of formal rule making and adjudicatory proceedings; and (4) to restate the law of judicial review.

An agency is defined as any authority of the United States, excluding Congress, the courts, and the governments of the territories, possessions, or District of Columbia. The APA sets out specific procedures to be followed when agencies make rules or enforce them (adjudication). Each process can be formal or informal. Informal rule making requires agencies to at least publish the proposed rule and allow interested parties to respond (notice and comment). Formal rule making is less common. It is quasi-legislative, requiring detailed hearings (rule making on the record). Similarly, formal adjudication is like a trial, presided over by an administrative law judge. Most agency decisions are subject to judicial review.

In 1990, two laws allowed agencies to use more collaborative methods of making and enforcing rules as supplements to the APA. Negotiated rule making (reg-neg) lets an agency meet with affected interest groups to reach a consensus on a proposed rule. Agencies were also authorized to employ alternative dispute resolution methods such as mediation and arbitration to resolve differences.

—Cynthia Scheopner

See also Alternative Dispute Resolution (ADR); Regulation and Regulatory Agencies

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5 U.S. Code Annotated. §§ 551–559, 701–706.

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Adverse Selection

Adverse selection is a term used in economics and insurance in reference to a market process in which buyers or sellers of a product or service are able to use their private knowledge of the risk factors involved in the transaction to maximize their outcomes, usually at the expense of the other parties to the transaction. The concept of adverse selection was first used predominantly in the insurance industry to describe the greater likelihood that the people who elect to purchase insurance policies are more likely to file claims that will, over the life of the policy, exceed the total dollar value of the premiums that they pay.

The individuals who elect to purchase insurance know that they have higher risk factors than the population norm that enhance the chance that they will file future claims. If insurers use the risk factors of the general population to set premiums, they will lose money when the number of individuals who file claims exceeds the population norm. If insurers raise the cost of premiums to cover the increased claims, they also increase the likelihood that individuals who know that they are less likely to file future claims will opt out of the plan, increasing the number of individuals remaining in the plan that will file claims.

Insurers may also use adverse selection to their financial advantage. If insurers have the ability to deny coverage to individuals who are deemed "high risk," they will try to avoid insuring all individuals except for those believed to be least likely to file future claims. This practice, known as "cherry picking" or "cream skimming," may result in insurers providing coverage to a group of individuals who are less likely to file claims than the population norm, thereby increasing the insurers' profits. In these instances, the costs incurred by the higher-risk individuals are generally borne by society. To combat this practice, the government may forbid insurers to act on information about their population even if they are able to discover it. For example, some U.S. states require health insurance providers to insure all who apply at the same cost, regardless of their individual risk factors.

Adverse selection is most likely to occur in situations in which there is an asymmetry of information. In economics, information asymmetry occurs when one party to a transaction has more or better information than the other party. While information asummetry tends to favor the buyer in the insurance industry, the concept of adverse selection has been expanded by economists into numerous markets other than insurance where similar asymmetries of information may exist that tend to favor the seller. Examples of situations where the seller usually has better information than the buyer include used-car sales, stock, and real estate.

—Carmen M. Alston

See also Asymmetric Information; Economic Efficiency

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Advertising, Subliminal

The word *subliminal* comes from two Latin words, "sub," meaning "below," and "limen," meaning "threshold." If something is subliminal, then, it is something that is "below the threshold"—here, below the threshold of conscious experience. Subliminal advertising, then, is advertising that operates below the limits of the consciousness of its audience. Subliminal advertising operates by including text or images into the overt, perceived advertising product that will not themselves be consciously perceived but will appeal to basic and universal human needs, such as for food, sex, security, or status. Such advertising messages are sometimes referred to as "hidden" or "embedded" messages.

The potential use of subliminal techniques has been recognized since 1898, with the publication of a book by E.W. Scripture called *The New Psychology*. The public awareness of subliminal advertising, however, was stimulated by two events that occurred in 1957. The first of these was a widely publicized experiment that James Vicary, the person who coined the term subliminal advertising, claimed to have performed at a Fort Lee, New Jersey, movie theater during the summer of 1957. Vicary claimed to have placed a tachistoscope in the projection booth of the theater and then to have used it to flash messages onto the screen every 5 seconds during the showing of the movie *Picnic*. (A tachistoscope is a shutter fixed to a projector that can flash slides onto a screen at speeds down to 1/125th of a second.) The messages that Vicary claimed to flash onto the screen were "Drink Coca-Cola" and "Hungry? Eat Popcorn." Vicary claimed that these messages resulted in an 18.1% increase in Coca-Cola sales and a 57.8% increase in popcorn sales. The second event that popularized the idea of subliminal advertising was the 1957 publication of Vance Packard's book *The Hidden Persuaders*, which outlined how advertising draws on knowledge of human psychology to motivate persons to purchase goods—including the possible use of subliminal techniques. Packard, however, was skeptical of the efficacy of subliminal advertising and did not use the term subliminal in *The Hidden Persuaders*. Indeed, even Vicary expressed the view that subliminal messages could only remind people to do what they would have done anyway and could not be used to motivate people to perform actions that they would not have otherwise done.

Yet despite Packard's skepticism and Vicary's modesty, between 75% and 80% of the American public believes in the existence and efficacy of subliminal advertising, according to Martha Rogers and Kirk Smith, in a survey whose results were published in the March 1993 edition of the *Journal of Advertising Research*. Moreover, according to the same source, consumers spend $50 million a year on subliminal self-help products. Such confidence in the power of subliminal advertising is partly owed to the success of a series of three books written by Wilson Bryan Key—*Subliminal Seduction*, *Media Sexploitation*, and *The Clam Plate Orgy*—in which he discusses various alleged uses of subliminal advertising. For example, Key claimed that the word sex was embedded on the face of Ritz crackers through the placement of holes on them and that the same word was embedded on the ice cubes of a drink shown in a well-known advertisement for Gilbey's gin. A similar case of the alleged use of subliminal advertising occurred in 1990, when Pepsi Cola withdrew one of its "Cool Can" designs after complaints that the random lines on the cans would spell the word sex when two cans were stacked on top of each other. Regulators have also taken the power of subliminal advertising seriously. In 1974, for example, the Federal Communications Commission issued a report saying that the use of subliminal advertising was contrary to public interest. More recently, in 2000, two Democratic Senators, Ron Wyden and John Breaux, requested that the Federal Communications Commission review the Republican National Committee's advertisement that was run against

Senator Gore's prescription drug plan. If the film was slowed down, they claimed, the word "Rats" appeared in large white letters superimposed over the words "The Gore Prescription Plan."

However, this widespread belief in the power of subliminal motivational techniques is at odds with the received view of them within the academy and within the advertising community. Although Vicary's New Jersey experiment has become so famous that it has even entered popular culture (even gaining an explicit mention in the movie *Double Exposure*), its alleged demonstration of the power of subliminal advertising is now widely discredited. Vicary himself admitted in a 1962 interview with *Advertising Age* that his "experiment" proved nothing. Earlier still, Vicary failed to produce any evidence for his claims when asked to do so in 1958 by the Advertising Research Foundation, and he failed to replicate his claimed results when he conducted the same experiment under the invigilation of a firm of independent investigators at the request of Henry Link, the president of Psychological Corporation. A similar lack of success was had by the Canadian Broadcasting Corporation when in 1958 it flashed the message "Phone Now" during the broadcast of a popular Sunday night television show called "Close-Up." The widely held view among academics and advertising professionals that subliminal advertising is ineffective has recently gained empirical support from studies conducted by S. C. Draine at the University of Washington in Seattle. In his 1997 doctoral dissertation "Analytic limitations of unconscious language processing," Draine shows that combinations of two or more words to form grammatical wholes cannot be comprehended by unconscious cognition. This means that the subliminal commands "Eat Popcorn" and "Drink Coca-Cola" could not be efficacious in stimulating behavior, even if the persons who saw them were inclined to eat popcorn and drink Coca-Cola prior to seeing such images.

Although it is widely accepted that subliminal advertising is ineffective, this does not mean that it never occurs. For example, advertisers who believe that it is efficacious might attempt to use it. Furthermore, disgruntled employees might embed words or images into advertising copy as an attempt at revenge against their employers.

—*James Stacey Taylor*

See also Advertising Ethics

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Advertising Ethics

In a modern capitalist society, ads are ubiquitous; criticisms of advertising are nearly as common. Some ethical criticisms concern advertising as a social practice, while others attack specific ads or advertising practices. Central to ethical criticisms are concerns that ads subvert rational decision making and threaten human autonomy by creating needs, by creating false needs, by developing one-sided narrowly focused needs that can only be satisfied by buying material products and services, and/or by appealing to genuine and deeply rooted human needs in a manipulative way. A second sort of criticism is that ads harm human welfare by keeping everyone dissatisfied. At a minimum, ads try to make us dissatisfied with not currently having the product, but many ads also aim at keeping us permanently dissatisfied with our social positions, our looks, our bodies, and ourselves. Advertising has been blamed for people today being neurotic, insecure, and stressed.

Business ethicists have traditionally either considered advertising in general or divided ads into information ads, which are ethical as long as they are honest, and persuasive ads, which are always problematic. However, recent literature on advertising ethics considers the division of ads into informative and persuasive to be entirely inadequate because it fails to consider separately the various persuasive techniques that ads use.

Economic Criticisms and the Function of Advertising

One economic criticism of advertising in general is that advertising is a wasteful and inefficient business tool; our standard of living would be higher without it. This criticism fails to understand that economies of scale for mass-produced goods can often more than offset advertising costs, making advertised products cheaper in the end. It is also suggested that advertising causes people to spend money they do not have and that advertising combined with credit cards creates a debt-ridden society, which causes stress and unhappiness. Furthermore, it is claimed that advertising encourages a society based on immediate gratification, which discourages savings and the accumulation of capital needed for a thriving capitalist economy. Granted that American society may currently be deeply in debt, this cannot be blamed on advertising because there are numerous societies that are inundated with ads but have positive savings rates and fiscal surpluses. Canada is one, and there are others in Europe and Asia.

There are also economic defenses of advertising. It has been argued that the creation of consumer demand is an integral part of the capitalist system; capitalism needs advertising since capitalism has an inherent tendency toward overproduction. And capitalism is an economic system that has made us the richest, longest lived, healthiest society in human history; even the poor in consumer societies are better off than most people in the Third World. Surely such well-being makes advertising ethically justified.

Information Ads

Many ads are simple information ads. Consider, for example, the flyers left on your doorstep that say that certain products are on sale at a certain price at a store in your neighborhood. Such ads are generally considered ethical provided they are honest. Problems arise if they make claims that are false, misleading, or exaggerated. Making false claims is a form of lying and, hence, clearly unethical. A claim is misleading if it is literally true, but is understood by most consumers in a way that includes a false claim. The ad is misleading whether or not the advertiser intends the misunderstanding. Generally, the honesty of ads should be judged not on their literal truth, but on how consumers understand the ad; this is because companies have, or can easily get, this understanding of the ad from focus groups and other marketing research techniques. Exaggeration, or puffery, in ads is thought acceptable by many people on the grounds that consumers can be expected to discount claims in ads. This is true except for vulnerable groups such as young children.

Normally, withholding information in advertising does not raise ethical issues. Car ads, for example, do not often print crash and repair reports; such information is readily and inexpensively available, and obtaining it is rightly viewed as the customer's responsibility. However, ethical constraints on exaggeration, withholding information, and misleading advertising become much more severe in cases where the customer cannot obtain accurate information, or cannot obtain it at reasonable cost, and the information is important to the customer's physical or financial well-being. Drug advertising by pharmaceutical companies is often criticized for failure to meet these more stringent standards, even though regulations in many countries try to control this for prescription drugs by requiring details on possible side effects, contraindications, and so on. This is a clear case of the information not being available since drug trial results are often confidential to the corporation, and the implications for the user's well-being are clear. This situation is not helped by press coverage of new drugs; such coverage tends to emphasize benefits over risks.

Impact of Persuasive Ads on Individuals

Discussion of the ethical issues surrounding persuasive advertising must consider separately various persuasive techniques such as benefit advertising, emotional manipulation, symbol creation, and so on.

Benefit ads emphasis a product's benefits to the user rather than product features. Typically, benefit ads show an enthusiastic, often exuberant, person enjoying the results of using the product; for example, a housewife is shown as jubilant that her laundry detergent got her sheets whiter than her neighbors'. In benefit ads, users tend to appear like real people and are not overly idealized; their emotions, however, are greatly exaggerated. Most benefit ads are ethically harmless if we allow for consumer discounting of exaggeration. Some critics, however, question the hidden premise that the consumer ought to want the benefit. Why should a person care if their wash is whiter, their car is faster, their hair is bouncier? Though a consumer's ability to deal with this form of persuasion may be made more difficult by the fact that a benefit ad assumes but does not state its premises, most of these ads are not a serious threat to human autonomy. However, there are some cases for concern. Consider, for example, ads placed by pharmaceutical companies for mood-changing drugs; life's little hassles become stress, sadness becomes depression, tranquility becomes listlessness, and contentment becomes apathy. Normalcy is not stated but assumed to be a medical condition requiring prescription pills. We are encouraged to be constantly dissatisfied with our most personal emotions. There are ethical problems with the intentions of the advertisers in this case, regardless of the actual effect on people's autonomy.

Ads try to manipulate many human emotions; fear ads are only one example, but they make clear the ethical issues. Fear ads tend to become more common during economic recessions, and they reached a crescendo during the 1930s. A Johnson & Johnson ad for bandages from 1936, for example, shows a boy with his right arm amputated because a cut without Johnson & Johnson bandages became infected. More recently, American Express used a print ad in eerie gold and black colors showing a distraught mother frantically phoning while her feverish daughter lies in the background. The solution offered is that American Express keeps lists of English-speaking physicians in most large cities. Critics maintain that appeals to emotions undermine rational decision-making processes and threaten our autonomy. Defenders point out that the fears portrayed (of infection before penicillin, communication problems with foreign doctors) are real even if dramatized, and the product offers a legitimate solution for the problem.

Advertising can persuade by turning a product into a symbol of something entirely different from itself. Chanel is a symbol of Parisian sophistication, Calvin Klein a symbol of sex, DeBeers diamonds symbolize love, and Mercedes Benz is a status symbol. We often do not buy products for what they are, but what they mean to us, and, just as importantly, what they mean to others. Critics claim this undermines human rationality by preventing us from assessing products based on their intrinsic worth; symbolic meaning of the product invariably biases our judgments. But, in fact, it is not irrational for people to buy a symbol if they want to express something meaningful. There is nothing irrational, for example, with buying and waving your country's flag. If you want to project high economic status, a Mercedes does indeed do so. Symbolic ads are not false or misleading for the simple reason that they do in fact work; products and logos do come to have symbolic meaning for us. To give a diamond is to give an object useless in itself, but the symbolic meaning, largely created by decades of DeBeers advertising, can give the gift life-changing significance. Symbolic meaning can add to the price you pay for a product (consider designer labels, for example), but there is nothing irrational in paying a price for a symbol that you want. Indeed, advertising provides a useful social service by creating symbols that allow consumers to communicate various meanings to those around them.

A self-identity image ad turns the product into a symbol of a particular self-image; the product then allows the buyer to express to themselves or others what sort of person they are. For example, Marlboro cigarette ads for decades featured the Marlboro man, a symbol of rugged independence and masculine individuality. Marlboros were very popular with teenage males, not because they thought the product would turn them into cowboys, but because they wanted to conceive of themselves as ruggedly masculine and because they wanted their peers to see them like that.

The more unnecessary a product type is, the more likely it will be promoted with self-identity image ads; they are a common type of ad for perfumes and colognes, cigarettes, beer, and expensive designer labels. One of the ethical objections to self-identity ads is that they manipulate our fundamental conceptions of ourselves to sell us dangerous (as in the case of Marlboro cigarettes mentioned above) or useless products. In response, it can be argued that these ads do not manipulate us without our active participation; we have to play the image game for these ads to have any affect, and experimenting with one's self-image is voluntary. Perhaps concern should only be for vulnerable groups or individuals, such as insecure teenagers under peer pressure; but then, images available through logos may help teenagers feel more secure if they can afford the product with the label. There have been stories of people who have committed violent crimes to obtain footwear with the right logo, but advertising cannot be held responsible for poverty or the resulting violence. Ads that specifically target the poor may be unethical because they target a vulnerable group; ads for "power" beer that target inner-city neighborhoods have been criticized for this.

Self-identity image ads cannot be criticized for being false or misleading because they do not work by giving information or making promises. They mostly appeal to our fantasies, and fantasies as fantasies are not false. A woman, for example, does not buy a perfume because she thinks it will transform her into the slim, beautiful, chic young woman in the ad. Consumers are not that gullible. She buys the perfume because associating herself with that image in her own mind makes her feel good about herself. The resulting self-confidence may, in fact, make her more attractive.

If we actively buy into the identity images of ads, there may be an element of self-fulfillment. None of this threatens human autonomy since active participation is required and is voluntary.

Even if self-identity image advertising is considered generally an ethical technique, there may still be ethical objections to specific images. For example, the images of women in ads have raised many ethical complaints. The most serious complaints concern the unremitting presentation as beautiful of an ideal body that is excessively thin or even anorexic looking, is extremely tall and long legged, and has a poreless, wrinkleless, perfectly smooth china-like complexion. That this body image dominates ads for women's beauty and fashion products is true, though recently there has been an increase in ads using more realistic body types. The tall thin image extends to fashion models, who now average more than 6 feet in height and are generally underweight. This body type is impossible for most women to achieve even with dieting and plastic surgery. In fact, the images in ads often have their hair and complexions airbrushed and their legs stretched using computer techniques; the result is a distorted body image that no woman, not even the models in the photos, have or can ever obtain.

The purpose of this idealization and distortion is to make women dissatisfied with their own bodies; this leads them to purchase the "beauty" product in the hope of looking and feeling better. But since the ideal is so extreme and unachievable, dissatisfaction quickly returns, and the woman is ready to buy more beauty products. Constant dissatisfaction with one's own body is the objective.

Ethical objections to these beauty ads include claims that they undermine women's self-confidence; that they cause anorexia and other serious eating disorders; that they distract women from family, careers, and other serious aspects of life; that the "beauty myth" drains women of energy and locks them into a stereotype that belittles the serious contributions they make; and that all this is a male power move that oppresses women. There is much debate about how many of these criticisms are true, but the fact that many women react so strongly against body image ads seems by itself to indicate that there is at least some problem. Some advertisers have listened to women and other critics, and other more realistic body types have become more common in advertising over the past few years. The accusation that such body image ads are unfair to women is mitigated by the fact that in the past 15 years or so more and more body image ads have been targeted at men. How men will be affected by this in the long run will not be clear for a generation. This trend may mitigate the gender fairness issue, but the other ethical issues are made twice as extensive. Of course, the idealized body image is different for men, but it is nearly as hard to attain; we may soon be seeing excessive steroid use for fashion reasons as the male equivalent of anorexia.

Self-identity image ads also raise the problem of false consciousness. Image ads try to create a consumer who desires products as symbols of his or her self-image. The individual is seen by defenders of advertising as a free and autonomous self who chooses to play the image game and chooses which self-image to project. But the autonomous self may be an illusion: The reality is (according to some) that people are not defined by consumption; they are defined by their role in the system of production. That the individual can choose a self-image is an illusion that would be shattered by the consciousness of the person's true alienated relationship to themselves and others. A young male may choose Marlboros, for example, as a symbol of ruggedness and independence, but reality is earning the money for the Marlboros by working in a fast-food franchise where he humbly takes orders from both his boss and the customers, adapts his every movement to a predefined time-and-motion system, and is forced to fake a smile on cue. The real self is his role as worker; the consumer self is an illusion created by the capitalist system through advertising precisely to prevent consciousness of reality. Defenders of advertising can reply that people's consumer self-image is just as real to them as the self-image they derive from their job. Though the consumer image game is pleasant, why should we assume it blinds people to their role in production? They may be well aware of it.

Impact of Ads on Society

Besides concerns about how ads affect individuals, critics have raised ethical issues about how advertising affects society. For example, J. K. Galbraith argued that advertising creates the desires that the production of consumer goods then satisfies. This dependence effect, in which consumer desires for goods depend on the process of creating the goods, undermines the usual ethical justification of capitalism based on consumer freedom of choice and the value of supplying people with the goods that they want. Others accuse advertising of creating a materialistic society full of people who think that happiness lies in owning things and who are obsessed with buying consumer goods. These critics think we are creating a society in which private goods are plentiful but in which public goods, which are seldom advertised, are ignored—a society rich in private cars but whose highways and streets are disintegrating. Ads drive selfish consumption at the expense of friendship, community, art, and truth. Furthermore, advertising allows the system to "buy off" politically unsatisfied people with promises and consumer goods, leading to political apathy and the undermining of democracy.

However, there are many who think these sorts of criticisms exaggerate the impact of ads on society. Schudson, for example, claims that advertising does not have much impact on society because it does not increase product-type usage; it only leads to brand switching and functions primarily as reminders to people who are already heavy users of a product-type. Major social changes are not caused by advertising; ads follow social trends, they do not create them.

This debate centers on two perhaps unresolvable issues. First, there is the empirical question of how much impact advertising has on society; this is difficult to answer because the effect of ads cannot be separated from other social forces, and because it is hard to determine whether ads cause or follow social trends. Second, there is the ethical question of whether the purported effects, such as materialism, are morally objectionable. Perhaps it is more helpful to look at specific issues rather than the social impact of advertising in general.

Lifestyle Ads: Sex and Violence in Ads

Some people object to ads that encourage sex, gambling, smoking, the consumption of alcohol, and other "vices." Even people who are not much concerned about such vices are still concerned that ads encourage *underaged* sex, gambling, smoking, the consumption of alcohol, and other vices. They believe that ads present bad role models. Advertising, some critics say, contributes to the moral breakdown of society because it presents ubiquitous images of unconstrained hedonism.

Ethical concerns about ads for gambling, tobacco, and alcohol are often legitimate. Products that are harmful and sometimes addictive raise ethical issues in themselves; encouraging the use of such products is even more questionable. Many countries and states limit, control, or even ban ads for some or all these products.

Violence in advertising would be ethically objectionable if there was much of it, but it is rare. The main exceptions are ads for films and video games, but objections in these cases should be aimed at the violence in the products, not just in the ads. The exposure of unsuspecting people and children to such ads is an issue that should be, and in many jurisdictions is, controlled by regulations on the placement of the ads.

Sex in advertising is a much bigger issue because there is so much of it. The ethical issues can be best seen if we separate consideration of sex in ads for products that are connected to sex from consideration of sex in ads where it is gratuitous and has no or only a tenuous connection with the product.

Ads for condoms and sex clubs, of course, emphasize sex. Except for puritans, the only ethical issue about these ads is making sure young children are not exposed. Other products, such as fashions, jeans, underwear, perfume, and chocolate, are related to sex, and advertising is often used to associate a product or logo with sex. Calvin Klein, for example, has built his business on making his clothes and perfumes sexy. Raising ethical objections to this is difficult unless one objects ethically to current sexual mores in most developed countries. Advertising did not cause our liberal attitudes toward sex; the sexual revolution was caused by the pill, penicillin, and other social forces. Any decrease of sex in advertising would probably not change society's sexual attitudes, so there is no ethical problem with Calvin Klein jeans, underwear, and perfume being thought sexy.

Sex is also used gratuitously in ads for products that have nothing directly to do with sex. We are all familiar with scantily clad women in ads for beer, cigarettes, cars, trucks, and vacation beaches. Note that for the most part these ads are aimed at straight males and use the stereotypical sexy woman—sexy, that is, in the minds and fantasies of straight males. Consider, for example, a two-page ad from a men's magazine that shows on the first page a woman with huge breasts, clad only in a bikini and posed in a sexually suggestive fashion. The copy asks if her measurements get the reader's heart racing. Turn the page and there is a pickup truck and the reader is asked to look at the truck's measurements. Horsepower, torque, and so on are listed. How do such ads work? Their ubiquity in men's magazines certainly suggests that they do sell cars, trucks, and beer. Such ads seem to say, "If you are a straight male attracted to big breasted women, you can prove it to yourself and others by buying our 'masculine' product." This interpretation presupposes that many straight males are very insecure about their sexual orientation and need to have their masculinity constantly confirmed by buying products with a masculine image. Is this manipulation of insecurities unethical? Perhaps not; straight males are generally capable of freely choosing to buy or not buy these products.

A more serious ethical objection to such ads is the attitude toward women that they imply and encourage. Women in these ads are being used as sex objects. One does not have to be a radical feminist to be concerned about the effects that exposure to thousands of such ads might have on straight men. It does not encourage them to see women as intelligent, productive, and competent individuals. Perhaps the vast majority of straight males are not greatly affected individually, but it does set a social tone about what are acceptable attitudes toward women. And the few men who take the objectification of women as sex objects seriously sometimes commit extremely unethical actions.

Advertising and Culture: Clutter, Appropriation, and Imperialism

Some critics of advertising are deeply concerned about the impact of advertising on our culture. Many of these criticisms are not so much about ethics as they are about aesthetics and taste, but some raise genuine ethical concerns.

Ads clutter our culture. Outdoor ads are unsightly, commercials interrupt television programs and sports, jingles jam the airwaves, and magazines seem to be nothing but ads. And ads are creeping everywhere. Clutter and ad creep raise two issues: general concerns about the ubiquity of ads and concerns about ads creeping into specific places such as public schools.

The ubiquity of ads certainly raises aesthetic issues, but in itself is not an ethical problem. Most ads are placed in media that people can choose to use or not. Magazines, newspapers, television, and radio can be avoided if a person wishes, and there are ad free news sources and alternatives to most media. Outdoor ads cannot be avoided, but their unsightliness is and should be a matter for local bylaws. Ad creep will not increase the impact of advertising on the consumer or society. The psychological wall we all have that blocks out ads is only made stronger by more ads. In terms of advertising impact, more is less. It is the lack of impact of advertising that is forcing advertisers to place more and more ads.

There are, however, specific places that many feel should be ad free. These include religious institutions, government buildings, and schools. The first is a private matter for the institution. Policy on placing ads on government property should be decided democratically. Ads in schools, on the other hand, raise ethical issues. School attendance is compulsory and so the audience for the ads is trapped; school pupils are children or adolescents so they may be vulnerable; the ads are shown in an educational environment so children may find it hard to discount their message; and finally, the peer pressure and groupthink inevitable in classrooms may dramatically increase the impact of ads. However, as long as schools are underfunded, schools will be tempted to accept advertising. Any solution to the ethical concerns about ads in schools will have to be enacted democratically.

Ads appropriate images from cultures and history, using them for the private gain of the advertiser. For example, perfume ads have used images of the beautiful "Indian princes"; motorcycles and cigarettes have used the "Indian brave" with feathers or a headdress as a symbol of masculinity. Is it ethical to use cultural symbols and images such as this? If an ad does use such a symbol, do they have any obligation to historical accuracy, or are faux simulacra acceptable? The peoples who created these symbols and images in the first place are generally not able to trademark or copyright them. Asking permission is often not an option; it is frequently not possible to identify whom to ask. One possibility that would minimize the ethical concerns would be to refrain from using cultural symbols if people from the relevant culture object. Images that do not receive complaints could be used; the Scots, for example, seem to like the kilted curmudgeon who sells malt whiskey. This approach requires a certain amount of cultural sensitivity on the part of corporations and a willingness to pull ads if they offend, even if those offended are not consumers of the product advertised.

Some critics complain that advertising is a form of American cultural imperialism. It is true that American advertising images such as Ronald McDonald and Coca-Cola are a large part of globalization, but European and Japanese corporations advertise worldwide too, and Chinese, Indian, and other cultures will be playing much larger roles in the future. Also, the dominance of American images is partly caused by the desire of many people for these images; Coca-Cola is advertised in many countries because the people there are eager to buy the product. In fact, it is this local popularity of American symbols and products that make some people in other cultures feel threatened. Some Italians and French may think that liking McDonald's food shows bad taste compared with liking their traditional foods, but the fact that McDonald's offends some people does not make it unethical to promote a popular symbol or product. Interfering with people's free choice by, for example, occupying or destroying restaurants raises more ethical issues than does advertising foreign products.

Advertising to Vulnerable Groups

Children and some people in the Third World are especially vulnerable to manipulation by advertising. Furthermore, we are all vulnerable to subliminal techniques if subliminal advertising works.

Children are vulnerable to advertising because they do not understand the purpose of ads; cannot tell ads from the rest of their environment; cannot separate fantasy from reality; find it difficult to control their emotions; do not understand finances, takeoffs, and deferred gratification; and do not have the psychological wall that blocks most ads in adults. Some people defend ads aimed at children by pointing out that young children cannot themselves buy most of the products advertised; they have to ask their parents who can and should make rational decisions on the child's behalf. But this defense leaves out advertising's intentional and conscious use of the "nag factor." Ads are designed (with verification using focus groups) to get children to whine and nag their parents for the advertised products. This technique tends to undermine the rationality of parental decisions, and it causes unhappiness in both parents and children, which is unethical on utilitarian grounds.

Some jurisdictions, such as Quebec and some European countries, ban altogether television or other advertising aimed at children. Many others ban only images that might be traumatic to children, such as sex and violence, or try to control the use of fantasy by insisting ads be realistic. Some people advocate also banning ads for products that might harm a child, calling, for example, for bans on junk food ads during children's programs. Ethically, corporations ought at least to stay within the law, but should also consider the impact of their ads on children's happiness and welfare.

Advertising to people in those Third World countries in which advertising is not a traditional part of their culture and who are not used to advertising yet can raise special ethical issues. These issues can be aggravated if the population targeted by the ads is illiterate, uneducated, and lacking in freedom and empowerment. A good example is the advertising campaigns Nestlé used in Africa that featured images of Caucasian "doctors" and "nurses" advocating the use of Nestlé baby formula in place of breast-feeding. The ads exploited the target market's illiteracy and lack of familiarity with advertising and its purpose, but the ethical issues in this case went beyond this; the ads were deceptive in that Western medical opinion did not support the use of formula feeding in the Third World. But the most serious ethical problems arose because of the consequences of the use of baby formula; it exposed the infants to malnutrition, disease, and contaminated water. International agencies claimed many babies died as a result. This case makes clear that using advertising to exploit people's vulnerabilities puts an ethical obligation on the advertiser to ensure that no harm results.

Subliminal ads are ads that the target market cannot see, hear, or otherwise be aware of. For example, if a movie theater flashes "Drink Band X Soda" on the screen so fast no one can perceive it, this is an attempt to manipulate people below their level of consciousness; as such, it tries to subvert rational decision making and so is unethical. Key's book titled *Subliminal Seduction: Ad Media's Manipulation of a Not So Innocent America,* popular in the 1970s, claimed that this technique was common and that large numbers of people were being brainwashed by it. Since then, experiments have failed to show that subliminal advertising works, and it is unlikely that it was ever widely used. Notwithstanding that, many legal jurisdictions have banned it.

Subliminal ads should not be confused with suggestive ads. As an example of a suggestive ad, consider a magazine ad that shows a couple passionately embracing in the background; in the foreground is a long cylindrical bottle of men's cologne obviously suggestive of a phallus. This is not subliminal; the viewer can clearly see what is going on. (In case the viewer needs confirmation, the letters "man's co. . . ." disappear strategically around the side of the bottle.)

Suggestive advertising is not inherently unethical since there is no evidence that it manipulates below our level of awareness or that it subverts rationality.

Advertising and the Natural Environment

Advertising affects the natural environment in three ways: ads use resources; some ads encourage destructive activities; and ads always encourage consumption, never nonconsumption.

Although radio ads and television commercials use a minimum of natural resources, print ads such as newspaper ads and inserts, flyers, and direct marketing mailings use vast amounts of paper. However, pulpwood for paper is a renewable resource if forests are harvested sustainably, and paper can be recycled, so reduced usage may not be ethically required. What is required is a sustainable paper industry, but is this the ethical responsibility of the advertisers? If advertisers insist on print media using sustainable paper supplies, the pulp industry would be hugely affected in a positive way. But the grounds for saying this is that the advertiser's ethical responsibility are not clear unless, of course, the advertiser claims to be an environmentally friendly company.

Some ads encourage activities destructive to the environment, such as the multitude of SUV ads that idealize off-road driving. Ethically, it is questionable whether advertisers should use such images. Sometimes, a negative environmental impact is inherent in the product advertised; for example, flying to the Caribbean on a vacation package uses petroleum, a nonrenewable and polluting natural resource. In such cases, environmental concerns should concentrate on the product, not just the advertising. What actions should be taken about such products is greatly debated, but the ads do not interfere with environmentalists who choose, for example, to vacation nearer home. Nor do they interfere with such environmentalists advocating this course of action to others.

Finally, critics of ads point out that consumer advertising always promotes consumption; reduced consumption is never advertised except occasionally by some advocacy groups that never have the money to compete with large corporations. Even government advocacy ads tend to emphasize recycling rather than reduced consumption; reduced consumption threatens jobs, taxes, and the economy. Environmentalists argue that, ethically, the developed countries ought to reduce their level of consumer consumption. Perhaps this is true, but the ethical responsibility cannot lie with the individual advertisers because they would be at a potentially fatal competitive disadvantage if they stopped advertising. This is a social and cultural problem that should only be changed by citizens through democratic processes and changes of their own behavior.

Corporate Control of the Media

Advertising critics claim that advertising gives corporate advertisers too much control of the programming and editorial content of the media; advertising biases mass media news coverage, and as a result, the media in North America only present what is in the interests of corporations for people to believe. For example, cigarette advertisers for decades threatened to and did pull their ads from any magazine or newspaper that carried articles on the health risks of cigarettes. Most magazine advertisers ask for advanced information on articles in the issues their ads will appear in; their ads are pulled if any article might create negative associations with their products.

Defenders of advertising do not deny that corporations sometimes withdraw ads or threaten to; they argue that corporations have a right to select where they advertise, and a fiduciary duty to shareholders and other stakeholders not to jeopardize the image of the corporation or its products. It can also be pointed out that newspapers and magazines that do not rely on corporate advertising are available to those who choose them; their subscription price is, of course, much higher (compare, e.g., the subscription prices of *Time* or *Newsweek* with the *Guardian Weekly*), but if people choose to be free of corporate influence they cannot expect to benefit from the subsidy that advertising gives much of the media.

In Defense of Advertising

The volume of criticism of advertising can make us lose sight of possible ethical defenses. Besides the economic role of advertising mentioned above, it can also be pointed out that advertising gives us information, introduces us to new products, presents us with images we can enjoy, creates symbols that allow us to express ourselves, subsidizes our media, and promotes human freedom by presenting to us vast numbers of products from which we can freely choose what we want to buy. Those who want to ban or strictly regulate all advertising should remember that advertising is a form of expression and that freedom of expression is a basic human right recognized in the UN Declaration of Human Rights and most national constitutions. However, that should not prevent the regulation of ad techniques or placements that cause specific harms. Those who worry about advertising should consider Schudson's point that ads are targeted primarily at people who are already heavy uses of a product-type and that the purpose of most advertising is not increase product-type usage, only brand switching. Ethical objections to ads have to make a case about specific ads on grounds of harm, viewer vulnerability, subversion of rationality, or plain dishonesty.

—John Douglas Bishop

See also Advertising, Subliminal; Bait-and-Switch Practices; Bluffing and Deception in Negotiations; Cause-Related Marketing; Children, Marketing to; Consumer Activism; Consumer Federation of America; Consumer Fraud; Consumer Goods; Consumerism; Consumer Preferences; Consumer Rights; Consumer's Bill of Rights; Consumer Sovereignty; Cross-Cultural Consumer Marketing; Cultural Imperialism; Deceptive Advertising; Deceptive Practices; Food and Drug Safety Legislation; Goodwill; Green Marketing; Information Costs; Lemon Laws; Marketing, Ethics of; Multinational Marketing; Persuasive Advertising, Ethics of; Public Relations; Public Relations Ethics; Signaling

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Advisory Panels and Committees

Advisory panels and committees make recommendations, give advice, identify important issues, and produce reports to guide decision making. An organization uses advisory panels and committees to increase the scope of its moral imagination to deal with uncertain situations with which its own members lack familiarity. Current examples of such uncertain situations that advisory panels and committees have been called to address include the consequences of rapidly innovating in biotechnology and nanotechnology; medical care providing experimental therapies; and the use of surveillance technology in free societies. In such unfamiliar situations, even well-intentioned people within the organization may be uncertain about the most appropriate principled behavior that considers and justly balances multidimensional consequences.

In addition to the need for guidance in uncertain situations, it may be difficult to make decisions that are credible to all stakeholders when the decision makers' self-interest also is at stake. It is helpful to balance the subjectivity of decision makers with input from wise, compassionate, skilled, and objective experts. Advisory panels and committees are formal institutional mechanisms whose function is to provide this seasoned and objective input. Recently, for example, advisory panels have been used to recommend the pay and benefits of top-level business managers and to avoid negative perceptions of self-interested managers awarding themselves extraordinarily extravagant pay and benefits.

As institutional mechanisms to signal an organization's objectivity, advisory panels and committees also have been called on to interpret policies for an organization, hold hearings on organizational members accused of policy violations, review draft decisions and approve final decisions, and provide oversight for policy implementation. By performing this function with independence, objectivity, and fairness, panels serve to increase procedural justice within an organization.

The effectiveness of advisory panels as mechanisms to introduce objectivity into decision making depends on the lack of any conflict of interest in the panel members. Such conflict of interest, unfortunately, has been a frequent criticism of advisory panels. In the example of panels used to recommend the pay and benefits of top-level business managers, interlocking membership between the advisory panels and managers is a common way of introducing conflict of interest. Interlocking membership means a person sits on a panel that makes a recommendation, such as setting pay, and the manager whose pay is being recommended sits on a similar panel for their recommender—a clear conflict of interest that interferes with objectivity in setting a fair pay level. In addition to not forming interlocking memberships, another common way for advisory panels and committees to avoid the appearance of conflicts of interest is for its members to serve without pay. The absence of pay for panel members suggests the absence of incentives for them to bias their decisions in favor of a paying organization.

Advisory panels and committees typically do not have all the information that is available to the organizational insiders. The effectiveness of panels, therefore, requires effort to overcome this information asymmetry. This effort is a function of the time and resources decision makers allocate to nurturing relationships between the organization and the panel. Some managers may minimize or neglect this effort because they think it is a burden on their costs and a constraint on their activity. By going without effective guidance, however, these managers are taking on the compound risk that they may act with suboptimal principles, that their expedient behavior may be publicly discovered, and that they will not be able to credibly demonstrate their intention to behave ethically.

Organizations that frequently and transparently communicate with advisory panels and committees before significant actions are proactively ensuring their behavior is scrutinized for integrity. Because of the significant time and resources required for this, advisory panels and committees often are found in those organizations that can demonstrate the positive cost-benefit consequences of the relationship. In the United States, such tangible and significant consequences may result from legal processes of public policy or tort law. For this reason, advisory panels and committees often are found in branches of government, hospitals, and businesses with significant assets.

Organizations can establish a reputation for compassionate concern for the public welfare by including outsiders (nonemployees, nonowners) from the community in the membership of their advisory panels and committees. Broad membership is particularly important when there are diverse views in the community concerning the appropriate principles that should be applied to a specific situation. Panels are a means for organizations to connect to a network of relationships in the communities its actions affect.

The smooth functioning of an advisory panel composed of people with a broad range of backgrounds and diversity of philosophical perspectives may be a challenge. Important ethical principles for the management of the process include fairness, efficiency, and utilitarianism balanced by respect for the rights of minorities. Absent these principles, advisory panels and committees may serve little more than an ineffective public relations function.

The important role of advisory panels and committees to guide their constituencies in uncertain and critical situations calls for these panels to be transparent in their ethical principles and distribute them widely. This communication process is supported by multiple and rich media such as an intranet that enables dialogue to promote high ethical standards throughout an organization whose members may be dispersed by a global economy across many geographic areas and cultures. Furthermore, by linking advisory panels to external communities via the Internet, business can sustain the relevance of its ethical principles and initiatives to the broader communities to which it is responsible.

—Greg Young

See also Asymmetric Information; Conflict of Interest; Cost-Benefit Analysis; Genetics and Ethics; Impartiality; Moral Imagination; Motives and Self-Interest; Networking; Procedural Justice: Philosophical Perspectives; Procedural Justice: Social Science Perspectives; Public Relations; Self-Interest; Signaling; Situation Ethics; Stakeholder Responsibility; Torts; Transparency; Utilitarianism; Virtue and Leadership

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Affirmative Action

The origins of affirmative action lie in a 1965 executive order issued by U.S. President Lyndon Johnson that required federal contractors to develop policies to combat discrimination. Since this order, several U.S. policies and laws have encouraged or required corporations and other institutions to advertise jobs fairly and to promote the hiring and promotion of members of groups formerly discriminated, most notably women and minority ethnic groups. Implementation of both the letter and the spirit of these federal requirements has often involved employment goals and targeted employment outcomes intended to eliminate the vestiges of discrimination. These goals and policies are the core of affirmative action.

Target goals, timetables, and quotas were originally initiated to ensure more equitable opportunities by counterbalancing apparently intractable prejudice and systemic favoritism. Over the years, many policies initiated with these lofty ambitions were criticized on grounds that they establish quotas that unjustifiably elevate the opportunities of members of targeted groups, discriminate against equally qualified or even more qualified members of majorities, and perpetuate racial and sexual paternalism. The problem of affirmative action is whether such policies can be justified and, if so, under which conditions. At its roots, this problem is moral rather than legal. However, the most influential arguments have been legal ones advanced in the opinions of judges.

What Does "Affirmative Action" Mean?

The term *affirmative action* refers to positive steps to rank, admit, hire, or promote persons who are members of groups previously or presently discriminated against. It has been used to refer to everything from open advertisement of positions to quotas in employment and promotion.

The original meaning of affirmative action was minimalist. It referred to plans to safeguard equal opportunity, advertise positions openly, ensure fair recruitment, and create scholarship programs for specific groups. Few now oppose these means to the end of equal treatment, and if this were all that were meant by affirmative action, few would oppose it.

However, affirmative action has acquired broader meanings—some advanced by proponents, others by opponents. Most important, it became closely associated—especially through its opponents—with quotas and preferential policies that target specific groups, primarily women and minorities, for preferential treatment. Stern critics of affirmative action hold that affirmative action today means little more than naked preference by race. Proponents of affirmative action wholly reject this suggestion. They see affirmative action as confined to policies that favor qualified women and minority candidates over similarly qualified men or nonminority candidates, where there is an immediate objective of remedying persistent discrimination, achieving diversity, and achieving a race- and color-blind society.

Criticism of affirmative action policies has often centered on the alleged use of quotas. *Quota* here refers to fixed numbers of a group that must be admitted, hired, or promoted—even to the point of including less qualified persons if they are the only available members of a targeted group. However, the term *quota* originally was not used with this meaning. Quotas were understood as target numbers or percentages that an employer, admissions office, recruitment committee, and the like sincerely attempts to meet. In this second sense, quotas are numerically expressible goals pursued in good faith and with due diligence, but they do not require advancing unqualified or even less qualified persons.

The language of quotas seems now to be going out of fashion, most likely to be replaced with the language of "diversity." Many goals of affirmative action are today discussed as issues of "diversity in the workplace."

Divergent Accounts of Discrimination and Its Remedies

Although racism and sexism—the primary sources of discrimination in the history of affirmative action—are commonly envisioned as *intentional* forms of favoritism and exclusion, intent to discriminate is not a necessary condition of discrimination in the relevant sense. Employees are frequently hired through a network that, without design, excludes women or minority groups. For example, hiring may occur through personal connections or by word of mouth, and layoffs may be controlled by a seniority system. It has proved particularly difficult in the more camouflaged areas to shatter patterns of discrimination and reconfigure the environment through affirmative action remedies.

Empirical evidence of social discrimination is readily available, though not always easy to interpret. Data indicate that in sizable parts of American society (and many other societies) white males (or other male groups) continue to receive the highest entry-level salaries when compared with all other social groups and that women with similar credentials and experience to those of men are commonly hired at lower positions or earn lower starting salaries than men. Whether these statistics demonstrate invidious discrimination is controversial, but additional data drawn from empirical studies reinforce the judgment that racial and sexual discrimination are the best explanation of the data. For example, studies of real estate rentals, housing sales, home mortgage lending, and employment interviews show significant disparities in rejection rates, usually comparing white applicants and minority applicants. Disparities seem to exist even after statistics are adjusted for economic differences. Race appears to be as important as socioeconomic status in failing to secure both houses and loans.

Persons who believe that such apparent discrimination is detectable and correctable by recourse to legal remedies are unlikely to defend strong affirmative action measures. In contrast, anyone who believes that discrimination is securely and almost invisibly entrenched in many sectors of society will likely endorse, or at least tolerate, affirmative action policies. These policies have had their strongest appeal, and firmest justification, when discrimination that barred groups from desirable institutions persisted even though strictly forbidden by law. All parties today agree that *individuals* who have been injured by past discrimination should be made whole for the injury by some form of compensation and that when we reach the point that a color-blind, sex-blind society can be achieved by legal guarantees of equal opportunities to all, affirmative action policies should be dispatched.

Those who support affirmative action and those who oppose it both seek the best means to the end of a color-blind, sex-blind society. In this respect their ends do not differ. Nor do they entirely disagree over the means to these ends. If a color-blind, sex-blind society can be achieved and maintained by legal guarantees of equal opportunities to all, both sides agree that social policies should be restricted to this means. But here agreement ends. Those who support affirmative action do not believe that such guarantees can, at present, be fairly and efficiently achieved other than by affirmative action policies. They see the goals of affirmative action as broader than mere legal guarantees of equal opportunity—for example, diversity itself can be a warranted goal. Those who oppose affirmative action believe that this recourse is unnecessary and that affirmative action policies unjustifiably discriminate in reverse. Many also try to show that today's affirmative action policies are, on balance, more harmful than beneficial.

The Justification of Affirmative Action

Presumably, affirmative action policies (in whatever form) are justified if and only if they are necessary to overcome the discriminatory effects that could not otherwise be eliminated with reasonable efficiency. Those who believe in aggressive policies of affirmative action point to the intractable, often deeply hurtful, and consequential character of racism and sexism. The history of affirmative action, from their perspective, is an impressive history of fulfilling once-failed promises, displacing disillusion, and protecting the most vulnerable members of society against demeaning abuse. They believe that affirmative action policies will likely be needed in pockets of the most vicious and visceral racism for roughly another generation, after which it can be reasonably expected that appropriate goals of fair opportunity and equal consideration have been reached. The goal to be reached at that point is not proportional representation, which has occasionally been used as a basis for fixing target numbers in affirmative action policies, but merely the end of discrimination. That is, the ultimate goal is fair opportunity and equal consideration. Once this goal has been achieved, affirmative action will no longer be needed or justified and should be abandoned.

Many supporters of affirmative action do not hold that it is needed now for *all* institutions. They believe that racial, sexual, and religious discrimination has been so substantially reduced or eliminated in some sectors of society that affirmative action no longer has a purpose in these sectors. The problem is that in other social sectors it is still common to encounter discrimination in favor of a favored group or discrimination against disliked, distrusted, unattractive, or neglected groups.

The Role of the Courts

The U.S. Supreme Court has upheld some affirmative action programs and found others insupportable. It is difficult to pin down exactly what, in the history of the Court's opinions, has been sustained and what has been discouraged. Both sides of the moral controversy over affirmative action have commonly appealed to the authority of the Court for support.

In two cases decided in the late 1980s, the Supreme Court supported the permissibility of specific numerical goals in affirmative action plans that are intended to combat a manifest imbalance in traditionally segregated job categories (even if the particular workers drawn from minorities were not victims of past discrimination). In *Local 28 v. Equal Employment Opportunity Commission*, otherwise known as *Sheet Metal Workers*, a minority hiring goal of 29.23% had been established. The Court held that specific numbers of this sort are justified when dealing with persistent or egregious discrimination. The Court found that the history of Local 28 was one of complete "foot-dragging resistance" to the idea of hiring without discrimination in their apprenticeship training programs from minority groups. The Court argued that "affirmative race-conscious relief" may be the only reasonable means to the end of assuring equality of employment opportunities and to eliminate deeply ingrained discriminatory practices and devices that have fostered racially stratified job environments to the disadvantage of minority citizens.

In a 1989 opinion, in contrast, the Supreme Court held in *City of Richmond v. J. A. Croson* that Richmond, Virginia, officials could not require contractors to set aside 30% of their budget for subcontractors who owned "minority business enterprises." This particular plan was not written specifically to remedy the effects of either prior or present discrimination. The Court found that *this way* of fixing a percentage based on race, in the absence of evidence of identified discrimination, denied citizens an equal opportunity to compete for subcontracts. Parts of the reasoning in *Croson* were affirmed in the 1995 case of *Adarand Constructors Inc. v. Pena.* Some writers have interpreted *Croson*, *Adarand*, and a 1997 decision of a three-judge panel of the 9th U.S. Circuit Court of Appeals—to the effect that a California voter-approved ban on affirmative action (Proposition 209) is constitutional—as the dismantling of affirmative action plans that use numerical goals.

This prediction could turn out to be correct, but the U.S. Supreme Court has not specifically so determined and has, with reasonable consistency, adhered to a balancing strategy. As important as its landmark cases are, no comprehensive criteria have yet been established by the Court for legally valid affirmative action plans.

Impact on Business

Affirmative action programs and various attempts to achieve diversity in the workplace have affected U.S. businesses in profound ways. Some of these plans were imposed by government on business, but most plans that survive today have been voluntarily undertaken by corporations.

Nonvoluntary Plans

In the early history of affirmative action, plans were nonvoluntary. In the typical circumstance, the government announced that it found a pattern of discrimination and that diversity was noticeably lacking in a company and that affirmative action must be enforced. An early and classic case in law and business ethics is an AT&T affirmative action agreement in the 1970s. The salient facts of this case are as follows: The U.S. Equal Employment Opportunity Commission (EEOC) had investigated AT&T in the 1960s on grounds of employee-alleged discriminatory practices in hiring and promotion. In 1970, the EEOC stated that the firm engaged in "pervasive, system-wide, and blatantly unlawful discrimination in employment against women, African-Americans, Spanish-surnamed Americans, and other minorities" (U.S. Equal Employment Opportunity Commission, "Petition to Intervene," Federal Communications Commission Hearings on A.T.&T. Revised Tariff Schedule, December 10, 1970, p. 1.). The EEOC argued that employment practices at AT&T violated several civil rights laws and excluded women from all job classifications except low-paying clerical and operator positions.

AT&T denied all charges and produced a massive body of statistics about women and minorities in the workforce. However, these data ultimately worked to undermine the corporation's own case. The data showed that half of the company's 700,000 employees were female and that the women were uniformly either secretaries or operators. It became apparent that the company categorized virtually all its jobs in terms of men's work and women's work. The federal government was determined to obliterate this aspect of corporate culture in the belief that no other strategy would break the grip of entrenched sexism. Eventually AT&T entered a consent decree, which was accepted by a Philadelphia court in 1973. This agreement resulted in payments of $15 million in back wages to 13,000 women and 2,000 minority-group men and $23 million in raises to 36,000 employees who had been harmed by previous policies.

Out of this settlement came a companywide "model affirmative action plan" that radically changed the character of AT&T hiring and its promotion practices. The company agreed to create an "employee profile" in its job classifications to be achieved in an accelerated manner. It established racial and gender goals and intermediate targets in 15 job categories to be met in quarterly increments. The goals were determined by statistics regarding representative numbers of workers in the relevant labor market. The decree required that under conditions of a target failure, a less qualified (but qualified) person could take precedence over a more qualified person with greater seniority. This condition applied only to promotions, not to layoffs and rehiring, where seniority continued to prevail.

Today it is no longer seriously doubted that AT&T's hiring and promotion practices did, at the time, involve unjustified discrimination and serious wrongdoing. Even basic moral principles were violated—for example, that one ought to treat persons with equal consideration and respect, that racial and sexual discrimination are impermissible, and the like. Less clear—and still unresolved today—is whether or to what degree the responsible corporate executives should be morally blamed. Several factors place limits on judgments about the blameworthiness of agents—or at least the fairness of doing so. These factors include culturally induced moral ignorance, a changing landscape in civil rights law, and indeterminacy in an organization's division of labor and designation of responsibility. All were present to some degree in the AT&T case.

Judgments of exculpation depend, at least to some extent, on whether proper moral standards were openly acknowledged in the culture in which the events transpired—for example, in the professional ethics of the period. If society generally had possessed clear standards regarding the justice of hiring and promotion in the 1950s and 1960s, it would be easier to find AT&T officials culpable. The absence of such standards is a factor in assessing culpability and exculpation, but need not be included in judgments of the wronging that occurred. Individuals and groups may be owed compensation even when parties to the wrongdoing cannot reasonably be held culpable for their actions.

However, the fact of culturally induced moral ignorance does not by itself entail exculpation or a lack of accountability for states of ignorance. A major issue in the past, and still today, is the degree to which persons are accountable for holding and even perpetuating or disseminating discriminatory beliefs when an opportunity to remedy or modify the beliefs exists. If such opportunities are unavailable, a person may have a valid excuse; but the greater the opportunity to eliminate ignorance the less is exculpation appropriate. Culturally induced moral ignorance was a mitigating factor in the 1960s and early 1970s, but history also suggests that it was mixed with a resolute failure to face moral problems that were widely appreciated to be serious, and they were problems that had been directly faced by other institutions.

Voluntary Affirmative Action Plans

Most corporate affirmative action policies are now voluntary plans, and these plans have arguably been more successful in transforming multiple corporate workplaces than have government-mandated policies. Many American corporations have welcomed these plans, on grounds that discrimination causes the institution to lose opportunities to make contact with the full range of qualified persons who might be contacted. These institutions have found that carefully controlled selection for diversity in the workforce is correlated with high-quality employees, reductions in the costs of discrimination claims, a lowering of absenteeism, less turnover, and increased customer satisfaction. Many corporations also report that they have invested heavily in eliminating managerial biases and stereotypes while training managers to hire and promote appropriately. They are concerned that without the pressure of an affirmative action plan managers will fail to recognize their own biases and stereotypes.

One moral worry about today's voluntary plans concerns a failure of truthfulness in publicly disclosing and advertising the practical commitments of the policies. Advertisements for jobs and the public statements of corporations about their affirmative action plans rarely contain detailed information about a corporation's objectives and policies, yet more information would be of material relevance to applicants and employees. The following are examples of facts or objectives that might be disclosed: a unit may have reserved its position for a woman or a minority candidate; the chances may be overwhelming that only a minority group member will be hired; the interview team may have decided in advance that only women will be interviewed; or the advertised position may be the result of a corporate policy that offers an explicit incentive (perhaps a new position) if a minority representative is appointed. Incompleteness in disclosure and advertising sometimes stems from fear of legal liability, but more often from fear of embarrassment and harm either to reputation or to future recruiting efforts.

Many corporations seem to be in the odd situation of fearing to make public what they believe to be morally commendable in their recruiting efforts. There is something deeply unsatisfactory about a reluctance to disclose one's real moral commitments and goals. This situation is striking, because the justification for the policy is presumably that it is a morally praiseworthy endeavor. Here we have a circumstance in which the actions taken may not be wrong, but the agents may be culpable for a failure to clearly articulate the basis of their actions and to allow those bases to be openly debated so that their true merits can be assessed by all affected parties.

—Tom L. Beauchamp

See also Civil Rights; Diversity in the Workplace; Employment Discrimination; Equal Employment Opportunity; Equal Opportunity; Gender Inequality and Discrimination; Minorities; National Origin Discrimination; Preferential Treatment; Racial Discrimination; Religious Discrimination; Reverse Discrimination

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AFL-CIO

The AFL-CIO, a federation of over 50 labor unions and more than 13 million members as of 2005, was formed in 1955 with the merger of the American Federation of Labor (AFL) and the Congress of Industrial Organizations (CIO) to become the largest labor organization in the United States representing 85% of the country's unionized workers. This merger renewed an old but tenuous alliance between trade unions and industrial unions that had fractured in a bitter confrontation at the height of the Great Depression in 1935 at the AFL annual convention in Atlantic City. At issue was the failure of the AFL to support the organizing efforts of industrial workers who had become the engine of a national economy increasingly built on mass production.

Originating with the craft and trade unions of skilled workers, such as shoemakers, typesetters, and metal workers, the AFL was slow to recognize the value of cheap, unskilled workers—minorities, immigrants, and women—who threatened the livelihoods of its membership base of mostly white, English-speaking men who built small businesses as they moved up the ranks from apprenticeship to master tradesmen. The AFL unions were more concerned with the competitive position of small businesses than with creating a platform of rights for industrial workers. Tensions increased as some organized labor leaders urged solidarity and support for industrial unions as well as elimination of racist and ethnic barriers within the trade unions. At the time of the Atlantic

City convention in 1935, when one fifth of American men were out of work, there was little sympathy among skilled trade unions for the plight of unemployed or underpaid factory workers.

The AFL leadership was itself split, with the majority steadfastly loyal to the trade union interests. Frustrated when AFL leaders rejected his efforts to expand the AFL agenda to include industrial workers through a new AFL Committee on Industrial Organizations, John L. Lewis led eight industrial unions in forming the independent Congress of Industrial Organizations in 1938, which quickly succeeded in organizing workers in several large mass production industries, including automobile, mining, steel, and rubber, to build a membership of 6 million by 1945. Building on initial victories won by strike strategies in the auto industry, CIO leaders went on to organize strikes in other industries to secure salary and benefit concessions in addition to labor-organizing rights. Both the AFL and the CIO worked successfully to gain political support for American workers and organize American labor, enabled in part by the Depression that highlighted the vulnerability of American workers and a booming World War II and postwar economy that provided ample work opportunities for both skilled tradesmen and industrial workers who began to see their common interests in relation to an emerging class of white-collar professional and technical workers with specialized knowledge in an economy oriented more toward service and technology than toward material production. Both organizations came to share the basic union agenda of promoting worker benefits through collective bargaining, political action, legislative initiatives, and strikes. When the presidents of both unions died in 1952, with many of the initial disagreements diminished, both organizations sought the 1955 merger under the leadership of George Meaney (AFL) and Walter Reuther (CIO).

The AFL-CIO and the U.S. Labor Movement

American economic interests were initially framed from the perspective of property owners who viewed labor as an input cost of business to be contained as much as possible to generate profit. Slavery was just one institutional expression of this viewpoint. It wasn't until 1914 that the Clayton Antitrust Act affirmed that labor was not a commodity. The craft and trade unions traced their roots to the medieval European guilds formed to protect the business interests of tradesmen and artisans by controlling occupational entry through a system of supervised apprenticeship and journeyman phases leading to master, grandmaster status with corresponding autonomy and income potential. Struggling with cyclic depressions and competition from the Southern slave-based economy, Northern apprentices and journeymen who found it difficult by the 19th century to establish their own independent shops sought instead to improve their lot as employees of master tradesmen. American workers' early efforts in the 19th century to assert their economic interests were met with strong, sometimes violent, resistance. The Philadelphia journeyman Cordwainers's campaign for wage increases in 1806 was met with a criminal conviction on conspiracy charges brought by their trade master employers. Eighteen more conspiracy cases were brought to trial until the Massachusetts Supreme Court ruled in 1842 (*Commonweath v. Hunt*) that labor unions were not de facto criminal conspiracies. The AFL was founded by Samuel Gompers in 1886 at the height of campaigns to protect workers in the American economy's shift to industrial production.

The impetus for the AFL was sparked by widespread dissatisfaction among trade union constituents impatient with the ineffectiveness of leadership in existing unions, such as the Knights of Labor, in securing legal and economic guarantees (10-hour workday, elimination of child labor, workplace safety) for workers. To distinguish itself from its predecessors, the new AFL promoted the autonomy of its affiliated unions, barred employers from membership, and focused on achieving benefits for its working members. Gompers himself, however, accommodated the AFL base of skilled workers unions, who insisted on restrictive membership policies excluding minorities, unskilled, illiterate, and immigrant workers. By the late 19th century, industrial unions such as the United Mine Workers, International Ladies' Garment Workers' Union, and the United Brewery Workers had joined the AFL, broadening its membership base and generating competing agendas among its affiliated unions. Despite this influx of industrial members, the AFL continued its primary focus on the concerns of skilled workers, hoping to ensure its own organizational stability and avoid potentially hazardous and futile political confrontations.

Contemporary critics of the AFL-CIO see it as a declining organization, citing the loss of union membership, diminished influence in both Democrat and Republican parties, the failure of unions to stand unequivocally for the equality of women and minority workers, and recurrent scandals among its leadership and member unions. Once a vocal and visible champion of American workers, organized labor no longer attracts members in a postindustrial economy rapidly shifting from manufacturing to service, technology, and knowledge. From a high of 32.5% in 1953, union membership among American workers has dropped steeply to the current 13%, or 15.7 million workers. While losing membership among its industrial base of mining and manufacturing industries, the young, and in most occupational groups, however, the AFL-CIO has successfully organized teachers, government employees, and protective service workers (firefighters, law enforcement, security, and corrections). Despite these gains, however, the AFL-CIO has failed to attract workers among the emerging technology, professional, and services sectors.

While the demise of unions and collective bargaining as a force in American political and economic life is not much disputed, the causes of union decline and possibilities for renewal are a subject of debate among labor historians. Labor demands are sometimes characterized as narrowly self-serving and intransigent in the face of pervasive conditions of industry or market failure. Workers are no less alienated by excess, greed, and corruption from their union bosses than from their employers. The negative effects of union-negotiated wage inflation and occupational entry barriers are more apparent to an increasingly mobile and adaptive workforce less amenable to industry-based organizing practices designed for stable, long-term employees of large corporations. These same workers, however, face new challenges of underemployment, work and wage restructuring, and global competition for which organized labor has yet to demonstrate its effectiveness in mediating the demands of a multiple stakeholder environment.

—Lindsay J. Thompson

See also Labor Unions

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African Business Ethics

African business ethics needs to be viewed in the context that each person belongs to a group defined by social, religious, political, or geographical parameters. It, therefore, carries a high degree of complexity and constant changing environments and as such requires a degree of flexibility to operate in. Nonetheless, the distinctive features of African business ethics can be made clear.

Marshall, in a seminal passage constructing the topicality of business ethics in the book *Business and Society,* sketches three different kinds of ethics based on three separate approaches to what is right and what is wrong: social ethics, transcendental ethics, and tactical ethics. It is suggested that social ethics (ethics determined from within any particular society) and tactical ethics (ethics based on the calculated observance of ethical standards in their conduct) are particularly relevant to African business ethics, each encapsulating a wide scope of ethical action and practice.

In the context of business ethics in relation to Africa, three key components need to be kept in mind: (1) cultural subtleties (ethics and tradition), (2) the natural environment (ethics and subsistence, including arable land scarcity), and (3) historical factors that have shaped and misshaped the human experience (ethics and social organization). Each category is cast with a caution, "In Africa, worldviews and ethics have reference points in traditional nations, the modern state leading to conflict as well as liberation."

Africa is a continent imbued with complexities and mixed signals; ethnic diversity, a range of religious and spiritual traditions, and the consequences of colonialism have had an impact on the dynamic cultural mosaic (the impact of Anglophile and Francophile cultural artifacts should not be ignored in the analysis). Its diverse geographical canvas covers the north and south temperate zones, the thick tropical cores lying in the North and in the South. In every area, Africa's geographical features have shaped cultural practices throughout its long history.

An understanding of the relationship between the environment, culture, and ethics is crucial in making sense of African business ethics. Africa's multifaceted cultures, landscapes, and peoples require diligence in studying the ethical content; simplistic binaries are not useful, although struggles between the strongest and smartest help in an understanding of ethics within Africa. In simplistic categories, the northern part is influenced by Arabic traders who veer toward Europe in the ebb and flow of business relations. The eastern side is heavily shaped by the Indian traders. The south is modeled by Europeans. The west is organized by a combination of African, Lebanese, European, and Indian business cultures.

The business climate in countries such as Angola, Ghana, Nigeria, South Africa, and Libya is relatively positive, whereas the range of social and economic problems in Liberia, Sierra Leone, Ethiopia, and Mozambique produce an atmosphere where business ethics are secondary to the instinct of base survival. To reiterate, laws, codes, regulations, and minor "norms of behavior" need to be considered in a local setting, each being cross-referenced to norms constructed by the family, the community, and "the state." This to a larger extent would determine the success or failure on the part of a business on its ability to adjust to Africa's dynamic market.

Africa is rich in resources, encapsulating substantive deposits of diamonds, gold, and oil. The wealth accrued from these commodities has not benefited the vast majority of citizens, the spoils often leading to widespread corruption, avarice, coups, and civil wars. Citizens are increasingly vocal in criticizing dysfunctional systems and structures that impede development and, in most cases, are ready to take the law into their own hands. Civil society is active in responding to the negativity that prevails in some areas, but recognizes its limits in terms of power. Nonetheless, traditional governmental structures organized by an intransient core are being challenged. Similarly, tribal codes and practices are being questioned by traditionally passive recipients, access to knowledge being democratized albeit unevenly.

Corruption among civil servants is extensive, highlighting the problems of accountability and responsibility in civil organizations. As a result of poor pay and unsustainable employment, bribery is embedded in the conduct of business. Bribes are common, and law enforcement is often corrupt. Taxes are not collected systematically or regulated in a positive sense. The culture of defrauding is not necessarily linked to the motive of generating large financial gain. It is operated to procure a modest improvement to the individual, family, and community, which can only be obtained through recourse to the network of favors, facilitated in part by brides, particularly in the area of health, education, and employment.

At the government level, there are problems with capital flight, embezzlement, and aid dispersion. Government and big business have been complicit in some areas, leading to international condemnation. For example, the case of Ken Saro-Wiwa in Nigeria, which resulted in the death of the activist following public criticism against the Nigerian government and Shell, is important in understanding the often tenuous relationship between foreign investment and environmental destruction. Numerous cross-sector industry cases, for example, fair trade and diamond mining, highlight the full challenges in relation to the ethical minefield in Africa.

International responsibilities that have an impact on ethics are also related to the military-industry complex, which in some cases extenuates the longevity of local conflicts and impedes social alternatives. The ethics of using Africa as a resource—plants, animals, and minerals—has long been an area of animosity, which is debated at length in the literature on global political economy. Johan Galtung, for example, in his well-known article, makes clear the relationship between imperialism and exploitation and between core and periphery. African business ethics are shaped by the numerous cultures that coexist in the continent: Clues or guidance to a shared ethical reference point is more likely to be found in the indigenous arts than Western textbooks; external international relations, however, should not be ignored in seeking to understand the complexities that operate in this unique and culturally rich continent.

—Paul D. Sheeran

See also Agriculture, Ethics of; AIDS, Social and Ethical Implications for Business; Corporate Social Responsibility (CSR) and Corporate Social Performance (CSP); Developing Countries, Business Ethics in; Political Legitimacy

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Age Discrimination

Acts of age discrimination are motivated by prejudice toward an individual's or group's age.

In the workplace, age discrimination occurs when an employer treats an employee or prospective employee differently than others because of the person's age.

In the United States, there have been several fundamental pieces of legislation enacted to protect individuals against age discrimination. The Age Discrimination in Employment Act of 1967 (ADEA) is the most significant. It protects individuals who are 40 years of age and older from employment discrimination based on age. The ADEA was created to extend the law stated in the Civil Rights Act of 1964, which prohibits discrimination based on race, sex, creed, color, religion, or ethnic origin, to include age.

The ADEA's protections apply to both employees and job applicants. Under the ADEA, it is unlawful to discriminate against a person because of the individual's age with respect to any term, condition, or privilege of employment, including hiring, firing, promotion, layoff, compensation, benefits, job assignments, and training. The ADEA further states that it is unlawful to retaliate against an individual complainant or participant in any age discrimination charge, investigation, proceeding, litigation, or testimony.

Regulations set forth by ADEA apply to employers with 20 or more employees, including federal, state, and local government organizations. Employment agencies, apprenticeship programs, and labor organizations are also subject to ADEA. Age preferences, limitations, or specifications are prohibited, but they may apply under rare exceptions. An employment agency, for example, may not make age specifications when posting job notices or making preemployment inquiries.

ADEA waivers are allowed, but only if they meet minimum standards. For example, an airline pilot is required to have a maximum level of correction relative to eye sight. A firefighter may be required to lift and carry 150 pounds. Age and other physical requirements are considered when filling these jobs. A waiver could be requested in these instances. The employer would be required to use specific language that would apply to all employment notices and advertisements for these positions. Discrimination also occurs with younger employees, but protections and liabilities are not legislated, and thus, cases and claims are rarely documented.

The ADEA is enforced by the Equal Employment Opportunity Commission (EEOC), a federal government agency. The EEOC is charged with eliminating illegal discrimination from the workplace. Individuals who think they are victims of age discrimination can report the activity to the EEOC. The EEOC provides information about how to file charges at the state and federal levels.

Age discrimination laws are also defined and imposed at the state level. These laws are based on the mandates stipulated in existing federal laws, although some state laws enforce broader protections. For example, there are states that enforce protections that apply to employers with fewer than 20 employees.

Age Discrimination and Employees

Age discrimination most commonly occurs as older workers seek new jobs, make efforts to sustain current employment, or compete for a promotion. Older workers are frequently highly compensated. These individuals tend to be employed for a lengthier period of time, achieving senior-level positions and progressively higher compensation.

Some individuals maintain that employers target these workers for replacement because they are more costly to keep than younger workers. Younger workers tend to be compensated at a lower rate, benefits are less costly, and there is a longer time horizon before retirement. These individuals are less expensive to hire and employ. A company may also consider younger workers as opposed to older workers because these individuals are perceived to be more creative, innovative, energetic, and adaptable. Benefits and pension plans are affected also. These programs are expensive to maintain for older workers. Employers may use these data to impose layoffs that are targeted at a disproportionate number of older workers. For example, due to newly revised pension arrangements, an older worker may be forced to make employment decisions, such as early retirement or a job change, which would not normally be the case or differ from younger counterparts. In this case, there are protections under the law.

The Older Workers Benefit Protection Act (OWBPA) was passed in 1990. It guarantees protection against discrimination in benefits packages. For example, OWPBA sets strict guidelines prohibiting companies from converting their pension plans in a way that would provide fewer pension dollars to older workers.

Age discrimination may eventually result in a job or career change, a significant transition for an older worker. Replacing a lost job with a comparable position is very difficult due to the high level of compensation and rank this worker has attained in the profession. There are fewer jobs available at this level, so there is more stringent competition for key positions.

Age discrimination comes in more subtle forms as well, and it is more common than estimated. These occurrences take many forms and are more noticeable in everyday activities. A younger worker may be awarded important job assignments or training opportunities over older workers, for example. A company may reorganize resulting in an older worker being reassigned to a new area, deemed a "lateral move," yet this person has fewer responsibilities and is no longer functioning in a primary role with the original work unit. Older workers may be encouraged to consider retirement by a supervisor in the instance where other employees are not. This is a dangerous form of subtle age discrimination because it is difficult to prove.

Claims between older employees and employers usually arise when compensation and promotion decisions are made unfairly, favoring equally qualified younger workers. Disputes also surface when an older worker has been fired or laid off over a younger worker of equal or lesser qualifications or when a qualified older worker has been declined employment in the hiring process, whether it is for a new position or a promotion. An older worker may have an outstanding performance record or may have been a key contributor to a company's success over a lengthy period of time, yet a younger professional with less experience, time, and expertise is chosen for important positions and promotion.

Age Discrimination and Employers

Employers may intentionally or unintentionally infringe on age discrimination laws. An intentional violation occurs when an employer makes overt statements about a job candidate that exclude this individual from the rest of the hiring pool because of age. For example, a company may review potential candidates and eliminate the older applicant because it is assumed that this individual will not be able to keep pace with the workload. Other common assumptions include the following: the older worker will not be as adaptable to the corporate culture, this individual will not be a long-term worker, or the older worker will suffer from poor health.

Another intentional, and sometimes unintentional, tactic is to create unclear employment documentation that may be legitimate for the purposes of the company, yet it provides an opportunity to exclude applicants and employees from job opportunities. In addition, a firm may develop company policies that unintentionally exclude individuals because of age.

In most cases, a company will make decisions that result in age discrimination to save costs. In so doing, a company takes certain risks that may result in adverse financial consequences. Age discrimination conflicts frequently result in a lawsuit or other form of conflict mediation. Plaintiffs may sue for past wages, future lost wages, emotional distress, and punitive damages, resulting in potentially costly verdicts.

Victims of age discrimination may sue for disparate treatment or disparate impact. Disparate treatment occurs when the employee is treated unfairly because of age, race, sex, creed, color, religion, or ethnic origin. Disparate impact takes place when the employer creates policy that negatively affects employees based on age, race, sex, creed, color, religion, or ethnic origin. Disputes are expensive, not only financially but they may also adversely affect a company's reputation. Small to medium-sized businesses are particularly vulnerable to these effects because they typically do not have the financial wherewithal to spend on lengthy and expensive lawsuits. Plaintiffs also bear the expense of these lawsuits. They are time intensive and expensive for all parties.

There are circumstances where age-related reorganizations are acceptable. Companies will sometimes provide financial incentives and severance packages to older workers that are favorable to the employee. This strategy enables the firm to create positions for younger workers and to reduce the number of highly paid individuals. Firms may also set mandatory retirement age under certain exceptions. For example, federal law recognizes ADEA exemptions in the case of air traffic controllers, federal police officers, airline pilots, and firefighters. In 1996, Congress passed legislation that allowed state and local governments to set retirement ages for these and similar employees as young as 55. In addition to mandatory retirement ages, many public safety jobs also have mandatory hiring ages, thus closing the door to potentially otherwise qualified people. There are some individuals who argue against mandatory retirement age exceptions because it would be fairer to all employees to rely on periodic fitness testing, since some older workers may be just as able (or perhaps more so) to carry out their duties as younger ones.

Age Discrimination and Society

Societal values and expectations both favor and discriminate against age. Many contend that older workers are more productive, stable, loyal, and wise. Older workers provide institutional knowledge that may not be recorded elsewhere. Studies show that these individuals are just as productive as younger counterparts, experience less absenteeism, and are less costly to recruit.

The counterargument is that older workers are inflexible, slow to change, and less apt to adopt new technologies.

These differing viewpoints and the conflict between them require employers to acknowledge age discrimination as a real and present issue. Baby boomers are moving through middle age and toward retirement in the United States. These individuals are healthier and are working beyond traditional retirement age. If an employer has not already embraced the value of having a mixed, age-diverse workforce, the demographics will present many issues in the future.

Employers most frequently have a financial incentive to discriminate against older workers. Firms are under tremendous pressure to meet and exceed the expectations of shareholders and other corporate constituents. Companies are in the businesses of maximizing profits and reducing costs. To accomplish these goals, employers experience difficulty balancing the obligations to worker welfare and the important role of contributing to the society at large. Employers have a responsibility to eliminate discrimination and consider employee welfare, regardless of a worker's age.

Conclusion

Age discrimination is a real and present issue in the workplace, and it will become more so for the United States as the large population of baby boomers grows older. Businesses without a firm philosophy and belief in diversity in the workplace will have to examine age-related bias and determine whether these biases are warranted. Are older workers less productive than younger workers, or is it simply a difference in work style and maturity? Relative to costs, what does an employer lose in institutional knowledge, skills, and talents if it eliminates categories of jobs that are commonly held by mature workers—what is the real financial cost?

If the business is stable or growing, a worker's job should be secure when the worker possesses a history of strong performance and ability. Businesses that must reduce workforce for economic reasons should do so with a balanced approach, being mindful of the overall implications to the business, economic development, and society.

What is the cost of age discrimination to the older worker? Whether age discrimination is overt or subtle, it frequently takes a financial and psychological toll. An unanticipated job search for an older worker usually takes longer than it would for a younger worker. Finding equivalent work at the same salary can be difficult, even in favorable market conditions.

A business makes decisions on its overall values and the values of its stakeholders. Workers of diverse ages can promote a balanced workplace while serving society and the public good. It behooves a business to closely examine whether age-related bias exists and, if so, why, and whether it is founded in a realistic framework. This examination should reveal the true costs of making decisions that discriminate against older workers, proving the impracticality of maintaining age-related bias.

—Pamela C. Jones

See also AARP; Egalitarianism; Equal Employment Opportunity; Equal Opportunity; Meaningful Work; Preferential Treatment; Right to Work; Rights, Theories of

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Agency, Theory of

The theory of agency seeks to explain why and how service and control can succeed or fail in a wide variety of social settings. One actor, the agent, is modeled as acting for another, the principal. These actors face characteristic problems that can appear remarkably similar across social or organizational contexts. The agent's problems focus on serving the principal (and, sometimes, on avoiding or manipulating such service). The principal's problems generally entail dilemmas of how to assure that the agent will do what the principal wants him or her to do (although the use of agents can also be a way to defer, shift, or avoid real action). Thus, the analysis of agency relationships features both an agent side and a principal side. Because human systems often feature multiple agents, and multiple principals, the problems of agency can quickly become quite complex, both to the participants and to social scientists seeking to understand such behavior.

Agents, principals, and their problems are pervasive in human relationships. Because of the utility of seeing common patterns across such relationships, the theory of agency, in various forms, has spread across the social sciences. Thus, agency theory can help social scientists explain such otherwise diverse phenomena as employee-employer, physician-patient, legislator-constituent, director-shareholder, parent-child, social worker–special needs client, and a host of other relationships and more complex settings that feature agents and principals in interaction. Agency relationships can be viewed as the building blocks in complex organizational settings as well as in societal networks.

Some Characteristic Behaviors and Problems of Agency

Agents can help solve the principal's problems in action in several ways. Agents are employed when the principal has a fundamental or qualitative inability to perform the needed action by himself or herself. For example, the principal lacks the expertise to cure himself or herself of illness or the balance or agility to clean leaves out of the gutter of his or her house. A second circumstance can arise when the principal is capable of doing the agency task but finds it rational to have another perform it instead. Thus, editors use foreign correspondents to get the news and senior managers delegate work to junior managers. In general, it may be more efficient for the principal to have someone else do the work, or there may be technical or structural reasons that prevent the principal from performing it. A third reason is rooted in the ability of agents to assist in resolving collective action dilemmas, providing a coordinating or coercive service that permits group action to occur. For example, the United Way acts as an agent for corporations in resolving problems of ensuring and distributing charitable contributions from many corporations to many charities. Finally, agents can serve symbolic purposes, as when presidents establish national study commissions with the purpose not of solving a pressing national issue but of defusing criticism from third parties for lack of action.

A central logic in the analysis of agency relationships focuses on the factors that interfere with perfect service and/or perfect control. *Perfect agency,* featuring the exact realization of the principal's goals in the relationship, rarely obtains. A host of factors can intervene to prevent perfect agency. They include, for example, biases or errors in perception, differences or conflicts in goals or values, differences in risk preference among the actors, differences in information conditions, incompetence or skill deficits, communication problems, lack of effort, emergent factors generated by the existence of systems of agent action, challenges from other institutions, and so on. In general, principals and agents expend resources on the costs of specifying what the agent is supposed to do and in monitoring and policing what actually occurs, or is perceived to have occurred. These costs have been termed *specification costs* and *policing costs.*

Among the major insights of agency theory is the observation that the consequences of agency failure due to the operation of such factors are often rationally and even routinely tolerated. That is, it may not pay the principal to insist that the agent perform perfectly because the costs of insistence, both in specification and policing, exceed the benefits to the principal of doing so. This tolerance applies also to the agent side (and to third parties who might participate in the relationship): It may not pay agents or third parties to invest in behaviors that result in perfect service because their gains in doing so do not exceed their costs. Thus, both control failures and service failures can have rational bases.

These patterns of failure can be institutionalized into social systems, with routinization both of their management and their tolerance. Two such problem patterns that deal with subsets of the general set of agency problems are the problems labeled by Kenneth Arrow as "hidden information" (*adverse selection*) and "hidden action" (*moral hazard*) problems. In adverse selection, the principal can observe the agent's behavior but cannot judge the quality of that behavior. In moral hazard, the principal cannot observe the agent's behavior, though could judge the quality of the agent's behavior were observation possible.

Barry Mitnick argues that, in the contexts of organizational action that produce common dilemmas in business ethics, the problem of adverse selection is better understood as two problems: the problem of *adverse claims*, which occurs as agents are hired by the principal, and the problem of *adverse performance*, which occurs after the agency is created, as the principal attempts to assess the quality of the agent's performance within the relationship of agency. In the first case, the principal must assess the credibility of the agent's claims regarding his or her ability to perform as agent, if hired by the principal. In the second case, the principal must devise means of evaluating the agent's performance, distinguishing the agent's contributions from those of other agents in the organization while having the benefits of observing ongoing, perhaps repeated acts of agency as well as the availability inside the organization of other, potentially more expert and reliable evaluators of that performance. Thus, the first case is essentially a credibility problem, while the second case turns on measurement and evaluation issues. Ethical issues can arise in either circumstance, as agents misrepresent their capabilities or conceal or collude to gain advantages in the relationship. Given the interdependent character of organizational agency, adverse performance issues also encounter problems in the judgment of fairness or justice among agents. The full range of agency problems, their consequences, and the means by which they are managed are far from understood.

Origins of the Theory of Agency

The term *agency theory* is often used to refer to a particular body of work that has developed in economics, accounting, and financial economics. This work is actually a subset of the wider range of work using the concepts of agency. Its assumptions about human motivation, especially its assumption of self-interest in the actors, and its focus on decisions as the key modeling contexts constitute significant simplifications that enable theoretical development to be formalized. But this approach, sometimes labeled the *economic theory of agency*, is also limited by these assumptions and has been the target of criticism from scholars working in other traditions.

As it has spread through the social sciences, research in agency theory has incorporated normative, institutional, cognitive, social, and systemic factors, going beyond the assumptions of the economics-based model. Thus, the best-known application of the approach, to the theory of the firm, is only one application of it.

Agency theory grew out of several rich theoretical streams in the social sciences. In economics it goes back at least to Ronald Coase's work on the firm in the late 1930s, in management to Chester Barnard's classic work on the functions of the executive about the same time, and in accounting and control to William Cooper's work in 1940 and 1951. In sociology, there is even earlier work of relevance in some of the classic works of George Herbert Mead and Georg Simmel.

In economics, the stream carried a series of studies on the divergence of owner and manager interests and behavior and on the objective function of the managed firm (notably from such scholars as Adolf Berle and Gardiner Means through Andreas Papandreou, Edith Penrose, Robin Marris, and William Baumol to Oliver Williamson's 1964 theory of managerial discretion; see also work on agency and the firm by Harvey Leibenstein). Jacob Marschak and Roy Radner's 1972 work on the theory of teams and Michael Spence and

Richard Zeckhauser's 1971 work on risk and insurance highlighted the effects of differing information states and risk preferences. Oliver Williamson's 1975 transaction costs approach examined how institutional choices could be understood as economizing on costs in *exchange.* In contrast, agency theory uses the costs of specification, monitoring, and policing to understand the choice of institutions in its modeling of *control.* In 1972, Armen Alchian and Harold Demsetz explained the emergence of organization from the functional need to monitor individual contributions in situations of joint production; it is often seen as one of the foundational works in an agency theory of the firm. In several works, Arrow observed the importance of considering noneconomic factors in relations in which one party acts for another, as well as critical information asymmetries; his 1963 article on medical care is widely cited (another accessible discussion by Arrow appears in a 1985 book edited by John Pratt and Richard Zeckhauser on principals and agents).

A number of other early works used agency concepts, but they did not propose agency as a coherent and general theoretical approach. In economics, examples included Anthony Downs's economic model of democracy in 1957 and papers by Victor Goldberg and by Barry Weingast in the early 1970s. In political philosophy, we saw agency concepts employed in books by Joseph Tussman in 1960 and Hanna Pitkin in 1967. In sociology, we saw them, for example, in an article by Guy Swanson in 1971.

Work on incentive systems and on the use of inducements in employment relations in political science and economics provided approaches useful in the conceptualization of the governance of agency relations. In particular, Herbert Simon's work on administrative behavior and on the employment relation (see also the later work on the employment relationship in economics by Oliver Williamson, Michael Wachter, and Jeffrey Harris), James March and Herbert Simon's inducements-contributions model, and Peter Clark and James Q. Wilson's incentive systems theory suggested how the discretionary zone that Barnard left to managers could be shaped and shrunk by attention to the reward system. Attention to the shaping of choice via incentives suggested a focus on control that flows directly into modern institutional agency theory. Those who view agency as a creature of economics often miss these critical theoretical ties. In addition, work in sociology on exchange theory by such scholars as George Homans, Peter Blau, Richard Emerson, Bo Anderson, Karen Cook, and Peter Marsden should be seen as theoretical development cognate to that in agency and in the transaction costs literature in economics.

Despite the history of work in related areas, and a long stream of research that developed many key concepts, the first scholars to propose, explicitly, that a theory of agency be created, and to actually begin its creation, were Stephen Ross (in a 1973 proceedings article) and Barry Mitnick (in a 1973 proceedings and a 1975 journal article), independently and roughly concurrently. Both labeled the proposed theoretical approach the "theory of agency." Ross is responsible for the origin of the economic theory of agency and Mitnick for the institutional theory of agency, though the basic concepts underlying these approaches are similar. Ross introduced the study of agency in terms of problems of compensation contracting; agency was seen, in essence, as an incentives problem. Mitnick introduced the now common insight that institutions form around agency, and evolve to deal with agency, in response to the essential imperfection of agency relationships. Behavior never occurs as it is preferred by the principal because it does not pay to make it perfect. But society creates institutions that attend to these imperfections, managing or buffering them, adapting to them, or becoming chronically distorted by them. Thus, to fully understand agency, we need both streams—to see the incentives as well as the institutional structures.

The work that has probably had the biggest impact on agency studies is Michael Jensen and William Meckling's 1976 article, which provided an explicit agency theory of the firm as a "nexus of contracts." Subsequent work by Eugene Fama and Jensen identified the decision process in firms as central, and argued that study of the assignment of rights to "decision management" and "decision control" could explain many features of firm behavior. The contexts of research in the Jensen-Meckling stream usually concern the economic theory of the firm, not necessarily a general theory of agency relations in social behavior. Because this work tends to focus on incentives and decision contexts, it should be seen as an outgrowth more of the economic theory of agency than its institutional agency counterpart.

One of the first papers published in the institutional agency stream was by Edward Banfield in 1975. Relying on concepts from and influenced by Mitnick's work, Banfield developed a comparative analysis of the production of corruption in public versus private organizations. In the mid-1970s, Mitnick's work introduced institutional agency theory to economics, political science, and sociology via presentations and publications. But it was a long time before agency theory took root outside economics. Agency did not enter political science in a major way until Terry Moe's article in 1984; did not enter sociology similarly until Susan Shapiro's article in 1987; and did not become prominent in management work until after Kathleen Eisenhardt's article in 1989. Today, use of agency theory is common throughout the social sciences as well as across studies in business school disciplines.

Agency Theory in Social Science and Management Studies

At present there is no unified, coherent "theory of agency." Depending on the research tradition in which the particular work in agency has been developed, different explicit logics, based on different social science literatures, such as economics or sociology, and sometimes displaying divergent approaches even within disciplines, are used to construct explanations. This diversity in logics produces the appearance of streams of work, each stream tending to operate within its own assumptional world. Even within the economics area agency work divides into formal mathematical modeling and modeling based on a more descriptive theory of the firm. The accounting literature also features behavioral/descriptive theoretic works in such areas as auditing relationships, ethical issues (see Eric Noreen's 1988 article), and contract design (including such public sector application areas as contracting out and municipal bond decisions). The formal work in economics, finance, and accounting features proofs of theorems based on assumptions about such characteristics of the agency situation as the preferences (including risk) of the agent and principal, the contract between them and its incentive structure, the sequencing of action in the relation, and conditions of information held by the parties about each other and the state of the environment (see also work sometimes labeled as "information economics"). A number of reviews of this now extensive work can be found in the finance, economics, and accounting literatures (e.g., by Oliver Hart, David Sappington, Stanley Baiman, Glenn MacDonald, Joseph Stiglitz; see also work by such scholars as Bengt Holmstrom, Jean Tirole, James Mirrlees, Steven Shavell, and a number of others).

In contrast, some of the work in management, sociology, and political science has explored agency using variables and perspectives that are of more traditional interest within those fields. For example, there is work in agency now examining the role of trust and of sociological norms (e.g., Mitnick's 1973 and 1975 work on norms in agency; Susan Shapiro's 1987 article on trust and agency; there is work by Mitnick and by the sociologist Arthur Stinchcombe on what they call the "fiduciary norm," and later work on the fiduciary relationship by Robert Cooter and Bradley Freedman in the law and economics literature; on agency theory and sociology, see the 2005 review by Shapiro, as well as works by Edgar Kiser, Carol Heimer, Arthur Stinchcombe, and others). The study of control has been linked to older traditions in management, sociology, and political science as well as to newer networks approaches by such scholars as Robert Eccles, Joseph Galaskiewicz, Kathleen Eisenhardt (see her 1989 article), and Harrison White. Agency analysis has been applied to political corruption and to bureaucratic behavior by such scholars as Gary Miller, Terry Moe (see his 1984 article), and Susan Rose-Ackerman, in addition to the work by Banfield and by Mitnick. Agency has been used to study corporate political activity (e.g., Mitnick's 1993 book). There are quite a number of applications of agency to government regulation and some in public administration, for example, by Mitnick (in his 1980 book); Barry Weingast; Daniel Spulber; Pablo Spiller; Jeffrey Cohen; B. Dan Wood; and Richard Waterman and Kenneth Meier. A whole subfield of research on delegation to bureaucratic agents now exists, beginning with Mitnick's 1980 book and including works by Morris Fiorina; Mathew McCubbins, Roger Noll, and Barry Weingast; Rod Kiewiet and Mathew McCubbins; David Epstein and Sharyn O'Halloran; Daniel Spulber and David Besanko; Jonathan Macey; and a number of others.

In management, scholars have used (or modified) agency approaches to explore such topics as behavior in boards of directors (e.g., works by Barry Baysinger; Gerald Davis; Amy Hillman and Tom Dalziel; John Hendry; Kevin Hendry and Geoffrey Kiel; James Westphal; and Edward Zajac), organizational control (e.g., works by Lex Donaldson and James Davis; Kathleen Eisenhardt; Huseyin Leblebici; Benjamin Oviatt; and James Walsh), stakeholder theory (Charles Hill and Thomas Jones), information policy in the firm (Michael Jacobides and David Croson), disclosure (Eric Abrahamson and Choelsoon Park), competence (John Hendry), managerial risk taking (Robert Wiseman and Luis Gomez-Mejia), behavior of professionals (Anurag

Sharma), bargaining (e.g., works by Mitnick; David Lax and James Sebenius; and Lawrence Mnookin and Robert Susskind), and compensation practices (e.g., works by Luis Gomez-Mejia; Henry Tosi; Edward Zajac and James Westphal; and Edward Conlon and Judi McLean Parks). An area of work termed "organizational economics," which includes both agency and transaction cost approaches under its umbrella, has been developing (see, e.g., work by Jay Barney). Agency has also seen some attention in the marketing literature. The appearance of each body of work more nearly resembles the kinds of theory construction and hypothesis testing practiced in these disciplines.

In an important stream of work in management, Lex Donaldson, F. David Schoorman, and James Davis (see, e.g., their 1997 article) offer a "theory of stewardship" as a counter to the economic agency theory of the firm that originated in Michael Jensen and William Meckling's 1976 article. The economic theory of agency seems biased toward the analysis of corrections; it is a theory of decisions about control (or of who gets control, e.g., decision rights). But agency has two sides: control and service. There is no reason why a viable theory of the firm cannot be constructed taking the service side as primary (e.g., other things equal, managers seek performance; correction is then taken as a secondary, marginal activity). Of course, the most descriptive theory of the firm may take a contingent approach that simply uses the conceptual tools of both service and control to understand the production of behavior in and around the firm.

Scholars using agency theory tend to rely on the sources for that theory with which they are most familiar. Because most scholars have assumed that agency originated in economics and are often unaware of institutional alternatives, they usually rely on the major works in the economic theory of agency, such as Jensen and Meckling's 1976 article, and adapt its features to the study at hand. The reliance on models in the economics stream tends to lead to more limited kinds of analysis as assumptions from the economics paradigm are imported into settings for which social science has additional tools available. Susan Shapiro's 2005 review notes that the agency approach need not rely solely on that paradigm, citing the more general work of Mitnick.

Agency theory is sometimes confused with scholarship on the law of agency; there are important differences. In the law of agency, it is presumed that the agent is acting under the orders of the principal; the law itself functions, of course, as a normative guide to behavior and to the resolution of disputes regarding appropriate action in agency roles (see the *Restatement of the Law Third, Agency,* published with this title by the American Law Institute in 2006). Agency theory is just that, a group of descriptive theoretical approaches that seek to provide understanding of a broad class of social behaviors; agents need not be presumed to be under explicit direction and hence to possess particular obligations, legal or otherwise. The law of agency does, however, provide rich materials for exploration via agency theory, and contributes central insights that can expand the quality and domain of agency theory (the first such use of the law of agency was in Mitnick's 1973 paper, but there is much work now by such scholars as Robert Clark; Robert Cooter; Frank Easterbrook and Daniel Fischel; and in a number of the law reviews). The same may be said of the related bodies of law and legal analysis in contracts and trusts; of particular interest is work on "relational contracting" by Ian Macneil.

Implications for Business Ethics

Applications of concepts relevant to agency are found in numerous places in the business ethics literature, but, with the exception of the 1992 volume edited by Norman Bowie and Edward Freeman and some scattered work elsewhere (see work in accounting by Eric Noreen in 1988 and by Wanda Wallace), most applications in business ethics use materials based on the law of agency (e.g., the concept of fiduciary duty) and on moral philosophy (e.g., the obligations of the moral agent; it is sometimes discussed as corporate moral agency). But Thomas Jones (also, with Dennis Quinn, on "agent morality") has explored the potential of applying guiding moral principles to agency and to stakeholder theories in general, which usually involve concepts that look like agency's relationship of "acting for."

Agency relations take on a special character when the principal is highly dependent on, or vulnerable to, the actions of an agent who has agreed to act on behalf of the principal. Under such circumstances, the fiduciary norm, a social norm commonly supported by informal societal sanctions, is prescribed. When the contract between agent and principal is formal, the similar but legally prescribed (and defended) fiduciary principle governs. Agents acting under fiduciary prescriptions must meet special expectations for agent performance: They must act diligently, with appropriate skills and with appropriate levels of effort, for the principal. No other interests must be permitted to interfere with that action; only the principal is to be served. The greater the principal's dependence on the agent, the more highly prescribed is the fiduciary norm and the fiduciary principle.

Fiduciary prescriptions (and general expectations) are common in societal roles that feature high dependency. They are ways of ensuring both to dependent agents and to observers that efficient, capable service is being provided, without exploitation of the principal. In general, the use of fiduciary controls is a great economizing tool—it lessens the principal's need for costly monitoring and policing of the agent. It can help ensure ethical performance of agency. In addition, publicity regarding the presence of fiduciary prescriptions signals assurance to observers, that is, it can have an important symbolic role. For example, the members of corporate boards are supposed to serve as fiduciaries for shareholder interests, so that the presence of a board filled with apparently competent, high-status directors—what Mitnick terms a *pantheonic directorate*—signals investors that their wealth is in good hands. Yet a huge literature on the myths of director performance suggests that it is common to find that such boards too often fail to provide the kind of oversight of top management that is required.

In the professions, the fiduciary prescription is commonly formalized. For example, medicine features a severe adverse selection problem, in that patients as principals lack the expertise to evaluate the quality of service provided by their agents, physicians. Thus, in medicine the fiduciary expectation is conveyed via the Hippocratic Oath required of new physicians: Do no harm. Note that the prescription goes beyond what would be required of a fiduciary: The physician is expected not only to act as the patient (principal) desires but to not harm the patient as well. Physicians do not necessarily follow the direction of their patients. We might presume, of course, that what patients want when they go to see a doctor is to be made well. But they may also request the use of particular therapies, for example, that a physician would recognize as inappropriate or even dangerous to the patient. In such cases, physicians are required to *not* follow the instructions of their principals, so as to avoid harming them. Thus, the service relationship in medicine is not purely fiduciary in character. The physician must add to the expectation that the patient's preferences will be served an additional prescription that says that that service must not harm the patient. Otherwise, in the extreme case, we might see physicians willfully performing euthanasia for patients who, whether sick or not, simply request it.

We see fiduciary expectations formalized across the professions; examples include law, dentistry, certified public accountancy, and so on. In many, if not most, cases, such professional relationships are also, like medicine, not simple fiduciary relationships. In some cases, considerable attention is given both to the defense of fiduciary behavior as well as to situations in which breach of fiduciary duty is acceptable in certain narrow circumstances to serve potentially conflicting but overriding interests. The recognition of conflict and/or limits in agency is most obvious in the law, in such situations as attorney-client relations and the attorney's accompanying role as an officer of the court and the extent to which the responsibilities of trustees as agents can be limited. The social scientific study of such relationships using agency theory is only beginning.

Although sometimes described as a professional role, the role of the business manager is not that of a professional. Yet, like any professional, a manager can experience the normative pressure to act as a fiduciary in service to a supervisor who may be dependent because he or she cannot observe the manager and/or cannot determine whether the manager's exercise of expertise is optimal. Indeed, from the perspective of the study of ethical failures in business, one of the central dilemmas comes exactly when managers do act as fiduciaries, but without the constraints or the superior interests imposed on true professionals. Instructed by the provisions of fiduciary behavior, agents set aside their self-interests—indeed, they set aside all interests that question the nature, appropriateness, or extremity of their acts of agency. And, if the principals either are not present, not able, or not inclined to set limits to the discretionary excesses of such dedicated agents, the outcomes from such agency can be frightening. Fiduciaries can produce not only the caring behaviors of health professionals but also the efficient implementation of the Holocaust's "final solution."

Thus, it is not enough to argue that management must become a profession and institutionalize the expectations of the fiduciary. What is also needed is a clear statement of the full, appropriate extent of the obligations placed on agents in business. Fiduciary service is only part of those obligations. Indeed, nothing highlights the critical role of concepts such as corporate social responsibility and corporate citizenship more than the realization that societally undesirable outcomes can follow from the behavior of dedicated agents in business wearing fiduciary blinders. Thus, study of the normative structure of business relationships must yet work out the nature, forms, and management of prescriptions that would ensure that professional agents in business are not only efficient but also serve socially acceptable ends.

Agency relations in business, as well as in organization and social life in general, are pervasive. Therefore, it will not be surprising if modern agency theory evolves into a useful and powerful descriptive theory of service and control that can greatly improve our understanding of the behaviors as well as the normative dilemmas of agents in business.

—Barry M. Mitnick

Note: Portions of this entry are adapted from Mitnick, B. M. (1997). Agency theory. In P. Werhane & R. E. Freeman (Eds.), *The Blackwell encyclopedic dictionary of business ethics* (pp. 12–15). Oxford, UK: Blackwell.

See also Adverse Selection; Arrow, Kenneth; Asymmetric Information; Coase, Ronald H.; Conflict of Interest; Corporate Moral Agency; Fiduciary Duty; Fiduciary Norm; Incentive Compatibility; Moral Agency; Moral Hazard; Transaction Costs

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Agrarianism

Agrarianism is a philosophy of society and politics that stresses the primacy of family farming, widespread property ownership, and political decentralization. These tenets are typically justified in terms of how they serve to cultivate moral character and to develop the full and responsible person. Many proponents of agrarianism bear a reverent affection toward nature (understood as natural phenomena or as God's creation), respect tradition and experience, distrust ideological systems of thought, and regard skeptically what they perceive as the pretensions of science and technology. By attaching individuals to nature, the agrarian suggests that our labor can enhance life; by bonding individuals to the rooted and stable associations of family and locale, we may experience, in a nonacquisitive way, the goods of a grounded community, including leisure, friendship, love, art, and religion.

Agrarianism has strong roots in classical Greece and Rome. As early as the eighth century BCE, in his *Works and Days*, Hesiod forged a link between moral improvement and farming. In the third and second centuries BCE, the Roman, Cato the Censor, in his only surviving work, *On Agriculture*, defended the honor of farming, offering moral prescription and wisdom alongside advice on the tilling and managing of land. Virgil's highly praised *Georgics*, written in the last century BCE, and influenced by Hesiod, expresses a love for the countryside and includes instruction in agriculture. Horace, a friend of Virgil, and himself the recipient of a farm granted by a benefactor, also praised the country life. In his *Odes*, he revisited the hills and woods of his childhood and set forth the rural life as the means to independence and self-reliance.

In the modern era, there have been several notable defenses of agrarian themes. In his *Notes on the State of Virginia*, Thomas Jefferson maintained that farming, rather than urban manufacture, would more likely ensure the independence and strength of character necessary for the free citizens of a decentralized republic. In 1782, about the time that Jefferson was composing his *Notes*, J. Hector St. John de Crèvocoeur, a Frenchman who had spent a decade in America, published his *Letters From an American Farmer.* The land-owning farmer not only acquires independence and freedom but personifies the new American. In the early 19th century, in his book, *Arator*, John Taylor of Caroline defended the Jeffersonian view. Taylor decried the use of law to favor factional and commercial interests, upheld wide property ownership, defended decentralized political power, and advocated rural rather than urban living. For Taylor, as for Jefferson, it is the free farmer whose independence is crucial for citizenship.

In the early 20th century, agrarian ideas also found expression in the Country Life movement led by Liberty Hyde Bailey and through the books of Ralph Borsodi, who published in the 1920s and 1930s. Defending the family farm and decentralization, Bailey and Borsodi each expressed a confidence in technology and expertise, and each maintained a critical attitude toward traditional religion. On the other hand, in the distributist thought of G. K. Chesterton and Hilaire Belloc, one finds the wedding of agrarian ideas to Catholicism. Belloc, for example, argued for a wide distribution of property and upheld the importance of the traditional household and local community.

The most notable of the 20th-century agrarians were those of the American south. The Southern agrarians, some of whom were poets, developed an explicit and resonant defense of their views in *I'll Take My Stand.* John Crowe Ransom, Robert Penn Warren, Allen Tate, Andrew Lytle, and Donald Davidson, along with seven other southerners, most affiliated with Vanderbilt University, defended a mode of life they believed consonant with European rather than industrial society. Against the economic doctrines of socialism and corporate capitalism (not to mention the assumptions of humanism and technocratic science), these thinkers proffered a wide-ranging portrayal of the settled and traditional mode of farm life that they believed typical of the southern region of the United States. Theirs is a portrait not of the sometimes perversely romanticized "Old South" of plantations and slavery, but of the yeoman farmer whose way of life and culture they regarded as threatened by both industrialization and the proponents of progress. Although their version of agrarianism derived from their experience as southerners, they maintained that they were expressing universal ideals. In their estimation, a society dominated by science, technology, and industry, and a nation inclined to favor the urban over the rural population, would suffer an impoverishment of manners, art, education, community, and spirit. The family farm and the rhythms of rural life were essential to a good society. Such a life would encourage consonance with nature, discourage the ambitious pursuit of material goods, permit the leisurely enjoyment of family and community, and allow the appreciation and experience of the spiritual and the aesthetic. The property-owning individual, granted an independence of mind and spirit, would nonetheless be attached to a stable community rooted in the traditions and experiences of a locale whose culture was part of the larger whole. Thus, the Southern agrarian was attempting to defend a manner of living, a way of life. To do so, of course, ultimately required consideration of the individual, society, economy, culture, religion, and politics, each of which finds mention in *I'll Take My Stand.*

The ideas of the Southern agrarians were often greeted with hostility. Although their considerations have had little practical import, some of their ideas have reverberated in the writings of Richard Weaver, and more recently in the works of Wendell Berry, since 1960 the most significant person associated with agrarian ideas, including the defense of the farm against agribusiness.

In defending a mode of life that emphasizes family, culture, leisure, and manners, as well as the historical and contingent particularities of persons and places, agrarianism poses interesting issues for business and society. Agrarian ideas challenge the notion of progressive industrialization and offer a rebuke to those who seek to reform and remake the provincial and particular. The agrarian suggests that the regional and the traditional contain goods that cannot be replicated by persons focused on acquisition or institutions guided by some ideal of abstract humanity. In this sense, the agrarian counters the advocates of growth and globalization, as well as those who defend egalitarian doctrines of democratic capitalism. Second, agrarians call into question the dominance of corporations. In their view, the corporation separates ownership from control, thereby diminishing the way in which private property has traditionally encouraged and demanded owner responsibility. Some agrarians also criticize the corporation as an artificial creature of the state, and one that has, in their view, secured ever more legal privileges or subsidies. Third, the agrarian perspective revisits questions concerning the commodification of society and the extension of the profit motive into all fields of endeavor. For example, the agrarian shares with certain environmentalists a critique of farming for profit, a wariness regarding the use of technology to control nature, and a strong concern about the factory farming of animals. Finally, agrarians raise important questions about the extent to which governments too often privilege one group (or mode of activity) over others, perhaps favoring an elite that seeks to impose its notion of progress on those deemed backward. Although their works are not always systematic, the agrarians' vision of independence, decentralization, and tradition raises significant questions about the nature of the good life and poses interesting challenges to modern conceptions of progress, commerce, and politics.

—*F. Eugene Heath*

See also Agribusiness; Agriculture, Ethics of; Biocentrism; Corporate Rights and Personhood; Deep Ecology; Environmental Ethics; Factory Farming; Land Ethic; Property and Property Rights

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Agribusiness

"Agribusiness" identifies several 20th-century changes in the way food is grown and food animals are raised, especially in the United States, Canada, Australia, and, to some extent, Northern Europe, consisting in an expansion (by several orders of magnitude) in the size of the average working farm, a new emphasis on profitable operation (or "the bottom line"), the systematic application of laboratory and experimental findings to the growing of crops, consolidation of ownership and control in companies not always directly involved in the actual cultivation of the soil, and a vastly increased reliance on technology and external inputs to agricultural operations.

If by "business" we mean a privately initiated enterprise instituted for the purpose of yielding a living for its principals, then farming has always been a business. The Neolithic farmer with his digging stick knew that his work had to yield enough for his family to eat, or they would die. Profit and loss was never stated more simply. Yet distinct changes in the enterprise in the last century permit us to distinguish "agribusiness" from the kinds of farming that preceded it. The term *agribusiness* was brought into popular use by populist author Jim Hightower in his 1973 work, *Hard Tomatoes, Hard Times*, and some critics have used it as a catch-all term to sum up what they see as agricultures' negative social impacts.

The Growth and Success of Agribusiness

For purposes of this entry, we may divide agriculture into two periods—traditional agriculture (comprising the vast extent of human prehistory and history) and the agribusiness era (beginning essentially in the Enlightenment, but taking its present form in the Americas in the 20th century).

As agriculture developed into historical time, it was certainly successful as a productive enterprise; its success by 6000 BCE allowed the creation of castes of priests, soldiers, and governors who did not work the land but lived off its surplus. It fed elaborate cities, empires, and crusades. During most of this time, agriculture was governed almost entirely by tradition (each generation doing just what was done in the last), prescription (priests or overlords dictating the allocation of land, the seasons of planting, and the crops to be delivered), and luck—what was available was planted, what grew was harvested. Progress was made, between the origins of agriculture and the end of the medieval period, in choosing the best of the seed to save for each year's planting and in increasingly sophisticated irrigation systems. Where new crops, domesticated animals, or productive trees became available, they were nurtured and cultivated. But agriculture was essentially a fatalistic enterprise, dependent on the luck of weather and on the patience to wait for the crop, and over much of its activity it was open to investment with superstition and consequent fear of change.

Until the Age of Enlightenment agriculture was rarely studied scientifically, with specific intent to increase yield or expand the number of foods available on the market. Unremarked in that period, when the effects of human activities on the planet were considered insignificant, even the earliest agriculture took a devastating toll on the natural environment.

The farmers who came to the New World from the British Isles (and later from the remainder of Northern Europe) were not the tradition-bound peasants of the Middle Ages; they were entrepreneurs who rapidly adapted what they knew to the conditions of the land in which they found themselves to survive and prosper. The Pilgrims' legendary introduction, on the advice of the indigenous agricultural consultant Squanto, of dead fish as fertilizer for the corn hills (included in every elementary school's Thanksgiving pageant) may be the earliest example of technology transfer in the Americas. It paved the way for many others.

The United States institutionalized its commitment to scientific farming and the improvement of agricultural output by the establishment of agricultural experiment stations in 1887, followed by the state and national agricultural extension services in 1914. The laws created a tightly linked alliance of the federal government (in the United States Department of Agriculture, USDA), land grant universities heavily invested in agricultural research, and the businesses that supply the products that emerge from that research, from tractors and cultivators through pesticides, fertilizers, and herbicides to genetically engineered seed—including seed genetically engineered to flourish despite liberal application of the firm's own herbicides (for instance, Monsanto's genetically engineered "Roundup Ready" soybeans that are resistant to Monsanto's effective herbicide, Roundup). The more extensive the technological input to the process of growing the crops, the larger the farm had to be to take advantage of it. On an American farm run on the agribusiness model, monster machines cultivate, sow, harvest, and bale 40 rows at a time of food or fiber. Aerially delivered herbicides eliminate weeds between the rows while the genetically engineered soybeans, corn, or canola grows untouched. The entire product is purchased, processed, and distributed by the same firms that provided the machines, fertilizer, pesticides, and herbicides. And the product (in the form of food, fiber, meat, or milk) is distributed to the consumer through enormous food distribution chains. In agribusiness, farming is now one small component of an enormous and highly technological industrial process, with higher rates of return on investment in the input industries (mechanical, chemical, and genetic) and the food manufacturing, transportation, and distribution industries. Over the past decade, large corporations have purchased or have effective managerial control over all phases of these input, production, and supply chains.

Does the system work? It certainly provides enough good food, and with a fraction of the human effort historically required. An enterprise that used to absorb the energies of 85% of the population now requires only 2% or less; it is mechanized from start to finish. Economically, the system is very problematic: This whole process is part of a "free market" system in name only. It cannot support itself on the prices the market can bear, so government subsidies of billions per year are required to keep it going. But the result for the consumer is truly marvelous; Americans spend a smaller portion of their income on food and fiber than any other nation, leaving a historically atypical amount in the family budget for discretionary purchases. The same pattern can be found in Canada and Australia; the Green Revolution of the 1950s and 1960s meant to establish it world wide and end world hunger for good.

Doubts About Agribusiness

From the point of view of the private sector and the consumer, the growth and success of agribusiness would seem to be an unqualified good. Yet it has drawn the attention of many critics; in this section, we will characterize the criticisms and use them as a framework to place agribusiness in social context.

First, *criticisms from the perspective of the public good*, especially from the perspective of the social good for the countryside. From a populist point of view, agribusiness has been devastating to rural life, a veritable neutron bomb, replacing farming jobs with machinery. As a result, many rural communities in the United States have suffered population declines that threaten their viability. The life of a town turns on a certain population size in its base industry, which supports the rest. When 6 to 12 people (varying by season) lived on a 300- to 400-acre family farm, the 30 or 40 farms in a township easily supported a general store, a hardware store, and a lively food and clothing exchange, not to mention a bank, a school, two (or three) churches, a social or service club or two, and at least two bars, one of which would be in a small hotel. The milk and produce created by a typical town justified a railroad station for daily pickups of milk and grain, often supplemented by a canal or river port, and generated a satisfying economic existence and cultural life for its residents. But when all those farms are rolled up into two, one in corn and one in soybeans, tended by huge machines, there is not enough employment to attract anyone at all to live there—the school closes, the stores fail, and each closure means fewer people to support what remains. Brave people will announce, often on the front page of sympathetic urban newspapers, their determination to stay in the town and revitalize the downtown, but the success of such efforts is very much in doubt. The end result is that the country towns, and all the richness of country life, are gone, leaving only a remote-controlled mechanism for producing food and fiber. Jim Hightower's work exemplifies this perspective.

Second, *criticisms from a liberal or left-oriented economic perspective*. It is very worrisome, especially to critics from the left half of the political spectrum, that agribusiness concentrates power and control over food production firmly in the hands of the large suppliers of agricultural inputs, such as Archer Daniels Midland (ADM). Such concentration is bad, not only because it permits the kind of price-fixing of which ADM was convicted, a crime in any free market system, but more generally because it entrenches the possessors of great wealth in positions of economic power, which has eventually to be bad for worker and consumer alike.

Third, *criticisms from the environmental perspective*. Rachel Carson shocked the consciousness of the United States in 1962 with the release of *Silent Spring*. She described how invisible agricultural pesticides were having the unintended consequence of poisoning the environment and threatening wildlife, and she argued that this was wrong. Her work triggered the most important reform of U.S. pesticide policy and the creation of the U.S. Environmental Protection Agency. Subsequent critics have described agriculture as being the human activity with the longest running and most extensive negative environmental impacts.

Fourth, *criticisms from the perspective of earth science*. Rachel Carson, a first-rate biologist, laid part of the blame for widespread pesticide contamination on the undue influence that input manufacturers have on the kind of science conducted at public agricultural research institutions (the land grant universities). She and subsequent critics condemn the very close working relationships of agricultural science with the same companies that profit most from industrial agriculture, and question the quality of the results on that basis. For instance, efforts to "streamline" the agricultural enterprise, but working with only the two or three most productive genetic stocks of certain products, has led to a steep decline in the number of varieties of produce (apples and potatoes, for instance) available for the ordinary consumer. Paralleling the critics of our dependence on fossil fuel, this voice asks for further research into alternatives (such as organic farming) that may not be as "efficient" as our current practices, but which in the long run may be healthier for our bodies and the long-term prospects for the industry.

Fifth, *criticisms from the perspective of nutrition*. Many nutritionists have concluded that millions of Americans suffer from poor health due to their diet and that agribusiness bears a major responsibility for this because its advertising plays such a large role in shaping consumer choices. Public health information about diets has been strongly influenced by research funded by agribusinesses, and many nutritionists claim that obesity, heart diseases, and cancers can be traced back to contemporary U.S. diets, and indirectly to agribusiness advertising. The powerful bonds between agribusiness and the fast-food industry are worth a moment's notice. The potato most grown for the market is the New Leaf, a genetically engineered variety whose major virtue is that it produces slices of perfect length for McDonald's French fries. It requires a great deal of pesticide; it would require less pesticide if several varieties of potatoes could be grown in the same field, or if they were grown in smaller sections, but the pressure from the enormous market created by the fast-food chain McDonald's dictates the size of the field and the number of varieties that will be grown. The hamburger market similarly dictates the feedlot practices of the beef growers, while KFC accounts for the mass pens of chickens. America is rapidly becoming a fast-food nation, and this economics does not support careful shopping for produce and meats differentiated by taste, texture, or nutritional qualities.

Sixth, *criticisms from the perspective of animal welfare*. When the precepts of agribusiness are applied to the flocks and herds as well as the plants, the results can be devastatingly unhealthy, discomforting, and sometimes terrifying to the animals. The conditions under which animals are raised for maximum productivity are generally described as factory farming, and they always include the conditions of crowding, unnatural quarters, antibiotics, steroids, and food additives (such as the corn-based supplement lysine) to get the animal or bird from birth to market in the shortest and most profitable terms.

Seventh, *criticisms from the perspective of national economic policy*. Political scientists and economists have called attention to the market distortions caused by the continued federal subsidies for the most important crops, such as corn, soybean, rice, or cotton. These subsidies were launched during the New Deal era of President Franklin Roosevelt to preserve rural life, but the program has continued, even as agriculture has undergone dramatic changes, because it is so popular among elected officials from farm states. These subsidy policies have also had the effect of keeping consumer food prices artificially low. The vast majority of federal dollars go nowhere near the small remainder of family farms, for which they were originally intended; they now flow to a small minority of very large farms. Taxpayer watchdog groups, environmental organizations, and economists have begun to join forces to attack farm subsidy policies as having outlived their purpose, causing economic distortion, and contributing to environmental degradation by providing incentives for continued high agrochemical use.

Eighth, *criticisms from the perspective of food safety*. We may be willing to sacrifice the variety, taste, and nutrition of our food for the convenience of a fast-food dinner, but safety is not so easy to ignore. Recent changes in agricultural practices, especially in meat and poultry production, have compromised the safety of some foods produced and marketed by agribusinesses. Food-borne illnesses, caused by, for example, salmonella and *E. coli*, have sickened hundreds and in a few cases resulted in deaths, especially of children and those with compromised immune systems. There is no doubt that the prevalence of these food-borne diseases is directly related to the crowded conditions of their rearing and that the occasional severity of the diseases caused by these microbes, their nonresponsiveness to antibiotics, is directly related to the use of antibiotics in their feed. This is a serious concern and one that some states are trying to address with legislation limiting the use of antibiotics.

Singly, most of these criticisms can be answered. Collectively, though, their effect has been to raise serious doubts about our current agricultural practices. Over the course of several decades, these critiques of agribusiness have had the effect of raising some questions in the mind of the public about the health and safety of their food, as well as the social and environmental ethics of the industrial agricultural system in general and the behavior of agribusinesses in particular.

A Future of Sustainable Agriculture?

The industrial model of agriculture may have outlived its usefulness. The enormous damage being done to the soil and to the aquifers, by the wasteful practices initiated to keep farming cheap, cannot be sustained.

Alternatives are available and can be instituted quickly. Agribusiness may soon, like the buggy-whip shops and phrenology institutes of yesterday, be of merely historical importance. Food will never be so cheap again, but we will have to find a way of tilling the soil that will preserve it for our grandchildren. Companies working in the agribusiness sector are now addressing some of these ethical critiques in their practices and marketing efforts.

Since the 1980s, critics of agribusiness have worked together to advance the notion of "sustainability" as an alternative approach to agriculture and food. This term has emerged from international conferences held by the United Nations. Sustainability is founded on the principle that human societies must meet the needs of the present generation without compromising the ability of future generations to meet their own needs. Sustainable agriculture integrates three main goals—environmental health, economic profitability, and social and economic equity. People in many different capacities, from farmers to consumers, have shared this vision and contributed to it.

Firms involved in agriculture are recognizing that a small but influential sector of the consuming public is willing to pay a premium price for quality foodstuffs and that definitions of quality often extend to sustainability issues in production (adequate wages, and environmentally responsible farming practices). The price premium captured by organic agriculture is the most widely recognized example of this emerging phenomenon. Note on the use of the word *agribusiness*: The term connotes big business, more than any particular kind of agricultural practices. Right now organic farming is a tiny slice of the agricultural market and not eligible for concentration into large vertically integrated corporations. It will be interesting to see if the term follows organic farming into mega-economic concentrations.

—Keith Douglass Warner and Lisa H. Newton

See also Agriculture, Ethics of; Archer Daniels Midland; Factory Farming; Genetic Engineering

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Agriculture, Ethics of

Agricultural ethics as a field is a virtual orphan, the child of three neglectful parents, applied or professional ethics (which would govern the professional ethics of the farmer or agricultural extension worker), business ethics (which would govern the business conduct of farmers and of all who participate in the enterprise of bringing food from seed to supermarket shelf or fast-food outlet), and environmental ethics (which would govern the interactions between farmer and ecosystem). The orphan is truly acknowledged by none of them and at the best of times has not swung securely among them. Let us consider it from all three of its inheritances.

As a branch of professional ethics, agricultural ethics explores the several dimensions of a field of practice, namely, farming or agriculture. In that sense, it is like any other field of occupational ethics—medical ethics, legal ethics, or engineering ethics—which together, with some additions, constitute the field of applied ethics. All fields of occupational ethics address multiple layers of problems: At the personal level, the rules for acceptable conduct on the part of the practitioner (Should a physician refer a patient to an X-ray facility that he or she owns?); at the field level, the policies for optimal practice for the profession as a whole (Should hospital policies prohibiting "futile" treatment overrule families' demands to "do everything" for a dying patient?); at the societal level, the policies for limiting and guiding the practice of the profession for the greater good of the nation and for human society as a whole (What are we going to do about 45 million people with no health insurance?). We may note at this point that the multiple layers addressed by applied ethics are not necessarily congruent.

Agriculture as a profession has the same layers of problems. Should the farmer represent his crop as "organically grown" if he has used hormonal root stimulants to grow them, if the laws defining "organic" simply don't mention such substances? Should the farmer plant, and the law support him in planting, "fencerow to fencerow" even though everyone knows that better environmental practice leaves wildlife corridors between the fields? And at the national level, should we be subsidizing agriculture in a way that encourages, even demands, overproduction and consequent dumping of agricultural products on the world market?

At the business level of agricultural ethics, new sets of problems arise. As soon as we look up from the plow, we notice that the farmer's work, the daily toil in the earth, coaxing it to yield food for the body and fiber for our clothes, has no more independence at all; it is part of a huge enterprise, integrated horizontally and vertically, that supplies the machinery for the huge farms, the seed, the fertilizer, the herbicides that keep down the weeds, the pesticides—or, alternatively, the genetically modified seed that resists the herbicide and has its pesticide bred into it—then buys the crops, processes them, and delivers them to the door of the consumer. This business has not always behaved itself very well, but its underlying ethic, as a business, is more troubling than its occasional brushes with the law. Critics of agriculture argue against "productivism," or the dominant philosophy in agriculture that holds production as the sole criterion for evaluating its success; it is as if IBM were to measure its success by how many computers it could make, working day and night around the world, regardless of whether or not the world needed those computers. The result of this philosophy is the despised "subsidies": When the farmer has produced far more than the market can purchase, the taxpayers are required to buy the surplus to keep the farmer from going out of business. Surely a better business philosophy is possible?

Environmental ethics has even more problems with agriculture. We have to remember that the relationship of the farmer to wild nature has been adversarial since the New Stone Age, and it is not surprising that environmentalist pleas to practice environment-friendly agriculture fall on deaf ears unless accompanied by strong financial incentives, usually financed by the same taxpayer who buys the surplus. Industrial agriculture has arguably had the broadest environmental impacts of any human activity, chiefly because it is the most extensive land-based activity of human society. Yet to a surprising extent environmental ethicists have actually ignored agriculture, largely because they have focused on "pure," "natural" ecosystems. Agriculture takes place in working, multifunctional landscapes, and thus, ethical positions always involve balancing multiple social goods. The lack of attention by environmental ethicists is all the more ironic, given the considerable interest in agriculture by one of its pioneers, Aldo Leopold (author of *A Sand County Almanac*, one of the bibles of ecocentrism), and the impact that Rachel Carson's *Silent Spring* had on U.S. society.

The central tension agricultural ethics attempts to negotiate is that between food production and resource preservation. Industrial agriculture is highly effective at producing foodstuffs, but it threatens the environmental resource base on which production depends and, thus, threatens the ability of future generations to produce food. Paul Thompson, the leading figure in agricultural ethics, articulates competing duties for those involved in agriculture: fulfilling the duty to produce safe and abundant food, while conducting operations in such a way as to preserve the soil and water resources on which future generations have a legitimate moral claim. Thompson proposes integrated pest management, or IPM, as an example of balancing production and protection. IPM is an approach to pest management based on ecological principles, preferring to control insect (and other) pests using strategies that do not result in environmental harm.

Agricultural ethicists argue for an ethic that can hold together such tensions. Drawing from environmental ethics, Thompson recommends "holism" as an ethical approach, proposing that the multiple social functions of agriculture should be evaluated in light of their impact on the sum of social benefits and costs of agriculture, including environmental degradation. This approach to agriculture could help its practitioners negotiate the competing moral claims on it.

The dramatic expansion of confined animal feeding operations has added concerns about animal welfare to agricultural ethics.

—Lisa H. Newton and Keith Douglass Warner

See also Agribusiness; Archer Daniels Midland; Factory Farming

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AIDS, Social and Ethical Implications for Business

AIDS is an acronym for acquired immunodeficiency syndrome. AIDS is associated with the presence of HIV, the human immunodeficiency virus, though all persons with HIV cannot appropriately be said to have AIDS. The United States Centers for Disease Control's (CDC's) technical descriptor of AIDS has to do with either the presence of an opportunistic infection associated with HIV or a diminution of the body's CD4 (T-lymphocyte or T-cell) count to below 200 per cubic millimeter of blood. Evidence suggests that HIV is spread through transmission of bodily fluids typically associated with intimate sexual contact and/or intravenous drug use, though cases of in utero mother-to-child transmission are both on the rise and well documented. HIV is fragile once outside the body and is therefore not transmittable through casual contact. AIDS is treatable but not curable. With proper treatment, it is not unusual for individuals to live 10 years or even longer from time of initial diagnosis with HIV, with death no longer an eventuality.

The statistics related to HIV/AIDS are staggering. Originally identified as a disease of male homosexuals in the United States, as of 2006, 65% of the total cases of HIV are in Sub-Saharan Africa. Nearly 13,000 people are newly infected every day, and less than 10% of the 40 million people living with the virus know they are infected—dramatically increasing the likelihood of their transmitting the disease to others. China, India, Russia, Ethiopia, and Nigeria are identified as second-wave countries for HIV infection. With these five regions accounting for 43% of the world's population, the potential for infection to spread is virtually without limit. It is sobering that in regions such as the English-speaking Caribbean HIV/AIDS is the leading cause of death among 15- to 44-year-olds. In general, epidemics might eventually become concentrated among economically disadvantaged populations due primarily to the fact that those who are wealthier and better educated are in a position to take preventative or curative action. As noted in the literature, throughout the world one of the greatest barriers to preventing the spread of HIV and even caring for people with AIDS is the persistent level of stigma and denial associated with the disease.

HIV/AIDS and Business

The Joint United Nations Programme on HIV/AIDS (UNAIDS) describes a situation unfamiliar to business leaders accustomed to the pandemic in the United States. While the United Sates suffers from an HIV infection rate of about one in every 265 people, there are countries where the rate can be as high as one in four urban-based adults, and these countries are now experience staffing shortages and productivity interruptions.

The impact of HIV/AIDS on business takes a number of forms. Bloom and his colleagues suggest these can be categorized as the effect on the workforce, the threat to the customer base, the impact on brand and corporate reputation, and concern for the global good. Others have added to the list the general economic toll HIV/AIDS takes on a country's gross domestic product (GDP).

Effect on the Workforce

Globally, the labor force has decreased by more than 28 million people as a direct result of the onslaught of the pandemic. If there were no further intervention, it is predicted this number could grow to 74 million during the next decade. UNAIDS estimates that 37 million working people are living with HIV/AIDS. The International Labour Office estimates that an average of 15 years of working life will be lost for each employee affected by AIDS.

HIV/AIDS is not an equal opportunity disease where workers are concerned. The most active industry groups are food/beverages, mining and minerals, and energy. A key occupational risk is work involving mobility. Workers engaging in regular travel and living away from spouses and partners in high prevalence countries are at particular risk for contracting HIV/AIDS. Costs of dealing with HIV/AIDS can be substantial. One global mining company has calculated that total expenses for dealing with the disease could amount to 8% to 17% of their total payroll by 2009; a manufacturer in South Africa puts the figure at 4% of its total current wage bill. More sobering is a report from *The Economist* documenting that some multinationals in South Africa hire three workers for each skilled position to ensure that replacements are available when trained workers die.

The onslaught of escalating expenses has precipitated a shift in policy, which runs counter to workplace privacy rights. In the summer of 2004, the World Health Organization and UNAIDS, in partnership with the Global Business Coalition on HIV/AIDS (GBC), endorsed a change from voluntary counseling and testing to an approach that routinely offers and recommends testing. While there is always the ability to "opt out," the clear intent is that mandatory testing for HIV become the company norm. The positive economic and utilitarian justifications for this change pepper the literature.

The GBC has become a visible presence regarding issues of HIV/AIDS and business activity. Established in 1997 to fully engage the private sector and recognize business as an important partner in ending the HIV/AIDS pandemic, the GBC is organized as a nongovernmental organization (NGO) to get businesses to do their part against the spread of HIV/AIDS. By 2001, the organization had only 17 members; today, the partnership boasts 215 members. In 2006, GBC issued their first annual "the State of Business and HIV/AIDS" report, and labeled it an effort to document a baseline for identifying trends and new frontiers to help companies improve their response to the HIV/AIDS pandemic. Booz Allen Hamilton, one of the GBC's most active members, played the lead in the report.

This report is the first attempt to provide a foundation on which business could consider the pace, range, and content of its response to the pandemic. The study was designed using GBC's Best Practice AIDS Standard, a 10-component self-assessment tool enabling companies to confidentially monitor their business AIDS response and examine their progress.

The report provides some evidence that business has been successful in partnering with NGOs, as well as with education and prevention programs. Other activities were proving more difficult. Companies found it challenging to engage business associates and supply chains in the fight against HIV/AIDS. That area was the one with the lowest score in the survey, with only 9% of companies able to successfully engage their supply chain contractually in supporting their HIV programs. Companies reported taking about 3 years to get fully into action around their own response to the pandemic. After that, a company was generally active in 20 of the 50 specific activities that the GBC surveyed.

One critical component of HIV/AIDS programming is prevention and treatment. A total of 82% of companies reported providing workplace information on HIV/AIDS, or to approximately 11 million workers. One of the more interesting findings has been that companies with operations only in America and Europe are less likely to focus on workplace programs, ostensibly because employees' medical insurance coverage tends to cover HIV/AIDS. In addition, the report notes that only 41% of those companies were conducting surveys and assessments to make sure that the programs in place were hitting the targets they were aiming at. In the area of treatment, 84% of the companies in the survey ensured that their staff had access to treatment; only 34% of these companies, however, fully subsidized that treatment. Of critical import, some 94% of HIV-infected employees were able to continue normal working life after receiving treatment.

The baseline report underlined that the fight against HIV/AIDS was now a real strategic concern for business and had moved on from simply being a matter of corporate responsibility. Treatment coverage has increased as costs of antiretroviral treatment (ART) have fallen over the past 6 years from around US$10,000 to US$140–300 per person per year. Cost reductions are to the point that in the short term the cost of ART is more than covered by the savings achieved through a reduction in absenteeism. Globally, 36% of companies surveyed by the GBC (which by their own admission are not necessarily representative of the population at large) are fully subsidizing treatment for direct employees, with 45% additionally providing access to treatment for all dependents.

Threat to Consumer Base

It is well known that HIV/AIDS affects people within their most productive years. As a result, both saving rates and disposable income among infected populations drop precipitously. In the long run, this has the effect of reducing the market size for business. One study published by UNAIDS shows that monthly consumption per capita of families living with AIDS was roughly half that of the general population.

The impact on the market has historically been concentrated by region and industry. A leading manufacturer in South Africa—the hardest hit of any country by the HIV/AIDS pandemic—has forecast the prevalence of HIV among its customers. Their conclusion? An expected increase from 15% in 2000 to 27% in 2015, with a corresponding reduction in their customer base of 18%.

Infection rates have accelerated to the point that the GDP for entire countries is predicted to drop as a result of the pandemic. As one example, over the next 10 years a 2005 report predicts China's GDP growth rate will drop by a full 1% as a result of HIV/AIDS.

The news is not all bad, however. In a recent survey, 71% of consumers indicated they would pay more for a product if they knew the extra proceeds would benefit HIV/AIDS. And companies such as Levi Strauss, United Distillers, and Northwest Airlines actually report improved community relations and even increased sales after being associated with work on AIDS.

Business Interventions

Bloom and his associates have noted that business interventions have been employee driven, market driven, brand driven, or a combination of the three. Whatever their impetus, virtually all the literature on business and HIV/AIDS recommends collaborative interventions crossing all sectors of the economy as most effective. The GBC is adamant that the next frontier for business response to HIV/AIDS includes creative partnerships and collaboration, including leveraging supply chains, linking business growth with HIV prevention, and realizing investment in new technologies.

The GBC approach is to rate companies using a common index capturing 10 global business HIV/AIDS categories. The baseline report outlines success on 2 of the 10 categories: prevention initiatives and community and government partnerships. The other categories fall below what the GBC establishes as an acceptable threshold of engagement. These eight categories include the following:

- Nondiscrimination in the workplace
- Care, support, and treatment
- Product and service donation
- Testing and counseling
- Corporate philanthropy
- CEO advocacy and leadership
- Monitoring, evaluation, and reporting
- Business associates and supply chain

In many instances, the business response to HIV/AIDS has been delegated to already overworked parts of the organization or passed down several levels, resulting in efforts that appear fragmented, low level, or even invisible.

HIV/AIDS, Business, and Ethics

Deep ethical concerns underlie the pragmatic impacts of HIV/AIDS. Links between HIV infection and social "baggage" such as homosexuality, sexual promiscuity, and drug abuse render HIV/AIDS a volatile issue for those formulating corporate policy.

From the view of Kantian ethics, or deontology, there is a potential clash of rights between the HIV positive worker and the HIV negative coworkers. The concern on the part of some during the early years of the HIV/AIDS pandemic that the ease of transmitability of HIV had been grossly understated has since been countered by evidence documenting the fragility of the virus. Calls for disclosure of HIV/AIDS status persist, however—although for different reasons than those advanced during the early years of the disease. Those infected with HIV are justifiably concerned with the variety of discriminatory practices, including erosion of the right to privacy, revocation of health benefits or escalation of the cost of such benefits, shunning by coworkers, and even termination of employment, which often accompany making a positive diagnosis with HIV a matter of public record. As recently as five years ago, a survey in Thailand showed that 12% of businesses fired staff known to have HIV/AIDS.

It is not immediately apparent how much regard ought to be given to an employee's right to privacy when the company has a countervailing duty to protect its shareholders' interests—in part by securing its workforce from disruption. Furthermore, the right of the HIV/AIDS sufferer to his or her work must be considered against the backdrop of the right of the employer to exercise the doctrine of employment at will, if such applies. This particular conflict is compounded—or perhaps alleviated—by the Americans with Disabilities Act, which in part treats workers with AIDS as a disabled class subject to the protections contained in this legislation.

Utilitarianism requires consideration be given to the consequences of including or excluding HIV/AIDS sufferers from the workplace, with an eye toward bringing about the "greatest good for the greatest number." The presupposition of utilitarian logic is that relevant benefits and costs can be both identified and quantified. On this logic, the "end" of corporate profitability may well justify the "means" of violating the rights of HIV/AIDS workers. Utilitarians must, however, come to terms with research into the longevity of HIV positive individuals indicating that a supportive community leads to life extension.

Perhaps the most relevant ethical perspective to adopt relative to HIV/AIDS is the ethic of care. This perspective demands attention be given to consideration of the personal—and relational—implications of AIDS policy formulation and implementation. The topic of AIDS in the workplace needs to be connected to how we as human beings live, and more particularly how we live in a caring relationship with one another. Jonsen offers perhaps the best insight to any discussion of policy alternatives relating to HIV/ AIDS in the workplace as he argues that in all epidemics fear stimulates isolation while responsibility requires inclusion—adding this might well be called the moral law of epidemics.

—Craig P. Dunn

See also African Business Ethics; Americans with Disabilities Act of 1990 (ADA); Business Ethics and Health Care; Employment Discrimination; Gender Inequality and Discrimination; Informed Consent; Life Settlements; Privacy; Shame

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Airline Deregulation

The Airline Deregulation Act (ADA) of 1978 initiated an era of fundamental change in the U.S. airline industry. The ADA attempted to address the economic inefficiencies of regulated air carriers by opening the airline marketplace to competition among both established and predicted new entrants. Prior to the passage of the ADA, the U.S. government used regulation as a tool both for protecting the airlines' economic interests and for overseeing the traveling public's safe, reliable access to service. The U.S. airline industry's response to the opportunities presented by government deregulation under the ADA has spawned a wide array of initiatives that have changed the basic nature of this industry's customer-supplier relationship. The consequences of these actions have affected both the structures and the operating philosophies of airlines globally.

The early days of the U.S. airline industry—generally considered as the time period between the end of World War I and the onset of the global depression of the 1930s—contained a mixture of government support schemes and competitive marketplace efforts. Most air carriers survived only through air mail contracts granted by the government on behalf of the U.S. Post Office. In the 1930s, though, the modern U.S. airline industry began to grow and take shape: Fledgling aircraft manufacturers and air transport companies began to develop the technologies and infrastructure needed to transform air travel from a novelty to an economic necessity.

However, during this decade the world was in the midst of a major economic depression, which many people blamed on the previous decade's lack of governmental control over national and international economic activities. Accordingly, the U.S. government under Franklin D. Roosevelt's New Deal policies established governmental agencies whose enforcement agendas combined protection of the public's welfare with the promotion of economic growth. In this context, the government established regulatory structures that encouraged the airlines' economic development while protecting them from unrestrained competition in national and international markets.

In 1938, the Civil Aeronautics Act created the Civil Aeronautics Board (CAB) as the regulatory body mandated to oversee the sometimes conflicting interests of growth within the nascent U.S. airline industry and safe, reliable service for the traveling public. To accomplish these goals, airline regulation in the United States followed the pattern of regulation employed for the most heavily used form of interstate transportation in the early 20th century—the railroads. This pattern dictated that regulation should encompass both route restrictions and price controls as effective means for ensuring industry profitability and guaranteed levels of service. However, the pricing and route protections afforded by government regulation, in turn, shielded this industry from external competition, creating barriers to entry that encouraged market-sharing collusion among the established participants in the industry. The result was the development of regulated oligopolies that, over time, limited supply and thus increased prices for the traveling public.

The rapid growth of aeronautical technology in the first decade after the onset of regulation—a product of the gradual economic recovery from the depression coupled with the global military rearmament occasioned by World War II—soon highlighted the practical consequences of the CAB's dual "growth and service" mandate. After the conclusion of wartime hostilities in 1945, the commercial airline industry had access to technologically advanced aircraft and highly trained air personnel—resources that, in an unregulated market, could have fostered increased service and customer-friendly competition at reduced prices. What arose instead, though, were problematic economic distortions driven by the CAB's regulatory mandates for the commercial airline system. On the one hand, as early as the 1950s critics of government regulation noted that when surplus aircraft and trained air crews became available for newly formed charter air companies, the CAB generally restricted these companies' scope of operations to protect the economic interests of the established carriers. This protective regulatory behavior suggests the working of the so-called capture thesis of regulation, whereby regulatory agencies and their legislative oversight committees are captured or co-opted by agents of the regulated industry to ensure the continuation of their regulated oligopoly. Yet during this same time period government regulation also provided substantial consumer benefits such as subsidized air service to smaller communities—service that otherwise would have been economically unfeasible for individual air carriers.

As the airline industry expanded and aircraft technology continued to improve in the two decades after World War II, political pressure mounted for reforming the process of governmental oversight of the industry. By the late 1960s, the growing economic inefficiencies and overall high price levels of the regulated airline industry began to generate increasing political criticism from both anti–big business liberal forces and conservative free market advocates. Belief in the benefits of free, unregulated markets was gaining strength as the United States entered the 1970s, a decade marked by economic recession, inflationary pressures, and decreasing public trust of government's beneficial role for society. Furthermore, proponents of airline deregulation began to laud the financial and service performance of intrastate regional airlines, which were not subject to the federal interstate regulations established under the CAB to control entry to or exit from the industry, as an example of the potential benefits of broader industry deregulation. The economic success and consumer benefits of these localized air operations supported the assertions of deregulation advocates that a free market would provide the necessary incentives for lower prices and increased choices for consumers.

When the CAB, in response to the political pressures supporting deregulation, in turn started to relax its regulatory restrictions in the late 1970s, air fares on average declined industrywide. Industry growth, as calculated by revenue-generating passenger miles, accelerated at a faster pace than it had over the previous decade. These immediate economic gains under the CAB's tentative moves toward government deregulation created further political support for complete economic deregulation of the industry. Although the economic recovery that followed the national recession of the early 1970s, and an easing of the Organization of Oil Exporting Countries oil embargo of 1973–1974, also contributed to these early successes, the apparent confirmatory trend of economic and consumer benefits resulting from reduced regulatory strictures led to the passage of the ADA of 1978.

Once airline deregulation became law, the number of airlines competing for customers increased dramatically. This competitive growth allowed two significant factors to drive competitive activity within the airline industry: the newly gained ability of airlines to set fares without prior governmental approval and the greatly expanded ability of airlines to add and remove routes at will. Both new entrants and established air carriers used pricing as a competitive tactic: They began ticket discounting, established various restricted and unrestricted ticket fare classifications, and created peak and off-peak travel times as common pricing stratagems. Airline route systems also changed under deregulation from the previously used market-to-market (point-to-point) route pattern to hub-and-spoke route models: Airlines scheduled short-haul (relatively short distance) flights as “feeders” to a central airport location, where passengers would then switch to connecting flights to their final destinations.

These structural changes in the airline industry’s pricing and operations increasingly shifted the industry’s performance focus from the qualitative elements of service (such as customer amenities, frequency of flights, and customer satisfaction) employed under regulation to the more quantifiable elements of operating costs and operating efficiency. This shift in emphases often brought the established airlines into conflict with their workforces, which were predominantly unionized. With deregulation affecting the predictability of revenue growth from ticket sales, airlines found that they could improve their financial performance by working to minimize their fixed costs, which consisted primarily of physical assets (airplanes), ground lease agreements (for airport landing gates and services), fuel, services, and labor. Both established air carriers and new entrants under deregulation carried similar cost burdens for ground lease agreements and fuel; however, they increasingly faced substantially different financial structures for their physical assets, services, and labor costs.

The first significant cost difference among airline competitors created by deregulation was a change in the costs for physical assets. Prior to deregulation, most air carriers had owned their aircraft fleets: Because CAB policies ensured a guaranteed economic profit for all competitors based on the operating costs of the industry, the costs of new aircraft were simply added to this calculated cost basis. In this approach, the CAB mirrored the price-setting approach taken in other regulated industries, such as natural gas and electric utilities. However, when the recessionary pressures of the 1970s forced several established airlines into bankruptcy, this provided a temporary low-cost opportunity for new entrants to obtain used airplanes at reduced prices. In addition, the new entrants were able to choose those types of aircraft best suited to the changing route structure of the deregulated environment, thereby achieving load factor efficiencies, while established carriers often owned a wide variety of aircraft types purchased over many years to meet the varied route structures of the regulated environment. Finally, the growth of new approaches to financial management in a wide range of industries led many new entrants to lease aircraft rather than purchase them, thereby reducing their initial cost outlays as they moved to challenge the established industry players.

Service then became an important cost factor under deregulation. Under a regulated structure, where all fares were set by the CAB, competing airlines could only differentiate themselves from their competition through the use of service incentives such as improved meals, free beverages, and customer amenities such as airport lounges and convenient scheduling. Deregulation brought the rise of “no frills” carriers, which initially lowered ticket prices by reducing or eliminating previously supplied levels of customer service. While the established “full service” carriers often matched these reduced ticket prices, they also chose for many years to maintain their previously set level of customer service. This created a cost differential between established players and new entrants, which proved difficult to lessen without accompanying decreases in services and amenities.

The largest cost element affected by deregulation, though, was labor costs. Established air carriers had contractual relationships with unionized labor forces in most critical operations—pilots, flight attendants, mechanics, baggage handlers, and maintenance. New airlines entering the now deregulated marketplace could not only enter the market with lower labor cost structures because of their (generally nonunion) employees’ lower levels of experience, but they could also take advantage of a labor surplus created by the same recessionary conditions that had affected the availability of lower-priced aircraft. This labor cost differential was the competitive variable most open to modification by the established carriers, as bankruptcy or the threat of bankruptcy allowed them to renegotiate or, in some cases, terminate entirely their previously negotiated labor agreements.

Since the passage of the ADA of 1978, then, the U.S. airline industry has worked through a series of "boom or bust" cycles. While under regulation the industry's profitability would rise and fall with economic conditions, the protective fare-setting role of the Civil Aeronautics Board ensured that, as a whole, the industry remained financially healthy. Under deregulation, though, global economic and competitive pressures affected air carriers much more directly and much more intensively. This has produced mixed results for both consumers and industry participants. Consumers benefited from overall lower fares, although not necessarily to equal degrees in all markets (middle- to large-size markets tended to reap the greatest rewards); they also found improved overall quality of air service, although again this change tended to benefit middle- to large-size markets more and smaller consumer markets less; and they sometimes found expanded consumer choice in the number of carriers and travel options available. Accompanying these benefits, though, was a decrease in service predictability and stability for consumers, as both fare schedules and even the continuation of service could change on a daily basis. As a result, in many major air travel markets near oligopoly conditions have again arisen—now under deregulation—driven by the economic strength of the larger carriers and the operational barriers to entry created by major airlines' hub-and-spoke airline route systems.

For industry participants, the contrasts have been much more drastic. While low-cost carriers have entered the marketplace and succeeded in the deregulated environment, over two decades of deregulated air travel have produced many more unsuccessful new entrants than viable ones. Likewise, the legacy carriers have undergone considerable change since deregulation, with consolidation during the first decade of deregulation leading to a reduction of the number of long-standing carriers in the United States to less than 10. This level of economic consolidation intensified the industry's boom or bust response to economic conditions. During the extended period of economic growth of the 1990s, these "legacy" carriers and many viable new entrants transported record-setting passenger loads and thus reaped record-setting profits. However, when the U.S. economy moved into recession in early 2001, followed by the impacts of the September 11, 2001, hijackings on U.S.-based airlines and the subsequent economic burdens of increasing fuel prices, the majority of these air carriers soon registered unprecedented financial losses, which led several into bankruptcy reorganization and threatened the continued viability of others.

A less-recognized, although significant and growing, impact of airline deregulation in the United States, though, was its influence on the global airline industry. The U.S. airline industry, even under regulation, maintained tens of air carriers, from small short-haul airlines through regional, national, and international carriers. When the United States chose to deregulate its domestic airline market, it also began to pursue agreements with other governments to permit greater airline competition internationally. Attempts to imitate the pattern of deregulation followed since the late 1970s in the United States have encountered a critical difference in many other countries that was not faced in the United States during the move toward deregulation—direct state ownership of part or all of many countries' major national air carriers. This structural difference has proved to make deregulation an extremely contentious political and economic issue in many international venues, as non-U.S. governments and consumers have viewed air service not simply as "another business" requiring free market remedies but as an essential national service.

With sluggish economic growth outside of North America throughout the 1990s, the financial costs of supporting state-owned air carriers placed considerable strains on many countries' national budgets. When these countries then initiated tentative actions toward deregulation of their air travel markets, the results were decidedly mixed. Arrayed against the successes achieved by emerging low-cost carriers in Europe and Asia were several high-profile, expensive failures of established national airlines. This provided a confirmation that many of the volatile economic consequences of deregulation witnessed in the United States were not bounded by geography. Airline deregulation emerged and grew as part of a larger post–World War II movement toward economic globalization and the "liberalization" of economic markets. In many senses, the deregulation of the airline industry across national boundaries provides a striking expression of the larger globalization of industry competition in the 21st century. Whether the consumer benefits and drawbacks of deregulation witnessed in the United States will also extend globally—where the dynamics of national and regional markets differ markedly from the conditions driving deregulation in the United States—is a question that the coming years will answer. Regardless, airline deregulation has played a significant role in the restructuring of pricing and service for this critical global industry.

—*William E. Martello*

See also Air Transportation Stabilization Board (ATSB); Barriers to Entry and Exit; Competition; Deregulation; Downsizing; Free Market; Interstate Commerce Commission (ICC); Labor Unions; Mergers, Acquisitions, and Takeovers; Monopolies, Duopolies, and Oligopolies; National Transportation Safety Board (NTSB); Regulation and Regulatory Agencies

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Air Transportation Stabilization Board (ATSB)

The Air Transportation Stabilization Board (ATSB) was created by the Air Transportation Safety and System Stabilization Act, which was signed by President George W. Bush on September 22, 2001, for the purpose of issuing federal loan guarantees to airlines experiencing financial difficulties following the terrorist attacks of September 11, 2001. As of May 2005, seven airlines have been granted such guarantees and nine airlines have been denied.

Applicants must meet three criteria under the act: (1) the airline is unable to obtain a loan without the guarantee, (2) the amount of the loan is prudent, and (3) the guarantee is necessary for a viable air transportation system in the United States. ATSB often demands stock warrants or related securities, giving the government an ownership stake in those airlines whose loans are guaranteed.

The creation of ATSB has been surrounded by controversy from the beginning. Although the terrorist attacks of 2001 clearly caused a drastic drop in airline patronage, it is debatable whether the proper role of government is to aid failing businesses. Some airlines that received guarantees were losing money prior to the 2001 attacks, in which case the government is inadvertently rewarding mismanaged airlines while better managed airlines do not enjoy the same benefits. Also, one could argue that it was unfair to single out one industry for federal assistance due to the terrorist attacks. What about New York hotels and theaters? What about restaurants and other service providers who rent space in airports? If federal assistance is available to airlines, one could argue that it should be equally available to all businesses directly affected by the terrorist attacks.

Another objection to ATSB, rooted in broader ideological concerns, comes from those who believe government should never interfere with free market processes. Airlines have the responsibility to plan for terrorism and other traumatic shocks to the industry, and it could be argued that airlines that were inept in their planning deserve to fail so that more competently managed airlines can take their place.

In contrast, there are strong arguments in favor of ATSB rooted in the premise that it is proper for government to ameliorate the harm caused by terrorism. Generous government aid was made available to individuals harmed in the 2001 attacks, so perhaps aid should likewise be offered to affected companies. The airlines were treated differently than, for instance, airport restaurants, because a slew of restaurant closures would not threaten the U.S. economy as much as the collapse of the airline industry.

Also, it should be emphasized that ATSB does not give loans; it merely guarantees the loans made by others. The government is responsible for the debt only if an airline defaults on its loan, which should not occur if ATSB's criteria are properly applied. ATSB's cautious approach is illustrated by the fact that it has rejected over half the airlines that have applied for loan, including the large and financially troubled United Air Lines.

—*Marc S. Mentzer*

See also Airline Deregulation; Deregulation; Subsidies

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Alien Tort Claims Act

The Alien Tort Claims Act (ATCA) is a part of the Judiciary Act of 1789 organizing the U.S. federal court system. The brief one-sentence passage states simply that the federal district courts have jurisdiction over any civil action brought by an alien for a tort in violation of international law or a U.S. treaty. The obscure provision was likely intended to deal with piracy on the high seas and issues arising in connection with foreign ambassadors. There was until 1980 little application of the ATCA.

A tort is any wrongful act not involving a breach of contract for which a civil suit can be brought. The U.S. Bill of Rights, Amendment VII of the Constitution, guarantees jury trial for nontrivial damages. The ATCA permits aliens to bring tort actions in U.S. federal courts against individuals and corporations regardless of nationality or location. To fall under the ATCA, an act must be universally prohibited, there must be sufficient criteria to determine whether an action constitutes the prohibited act, and the prohibition is always binding. A related cause for tort litigation is the Torture Victim Protection Act (TVPA) of 1991.

The rising number of ATCA actions since 1980 continues the expansion of modern tort litigation. Businesses complain that the burden of litigation is too high, that much of the punitive damages simply go to lawyers, and that personal injury lawyers are out of control. There is a social cost of litigation, in the sense that compensatory and punitive damages may ultimately pass to consumers. On appeal, however, judges often reduce jury damage awards—even in notoriously plaintiff-friendly jurisdictions. A difficulty with calculable punitive damages is that it may lead on to the callousness to human life and limb that allegedly occurred in the Ford Pinto case. A successful tort litigation lawyer presumably builds up a war chest with which to tackle tougher defendants.

Expansion of ATCA Litigation

Since 1980, ATCA litigation has expanded from an initial application to oppression by foreign governments of their own citizens to private individuals to U.S. and non-U.S. companies. Complaints have spread from alleged human rights abuses to alleged environmental damages. Complaints against businesses have been mostly by poor rural citizens of developing countries.

To date, no ATCA plaintiff has prevailed at trial against a U.S. corporation. However, Unocal settled out of court in an ATCA case arising in Myanmar (Burma). The business concern is that, if any suit prevails, then all multinational corporations (MNCs) will be sued in due course. The U.S. Chamber of Commerce, the National Association of Manufacturers, the National Foreign Trade Council, and the George W. Bush administration have all opposed business application of the ATCA. The counterargument is that MNCs avoiding human rights abuses exposure should have nothing to fear in U.S. federal courts.

In 1980, the Second Circuit Court of Appeals held in *Filártiga v. Peña-Irala* that torture committed by a Paraguayan police officer in Paraguay was a violation of the law of nations. The defendant was resident in the U.S. at the time of the litigation. The Second Circuit permitted a suit by Bosnian Serbs against the president of the so-called Bosnian-Serb republic within Bosnia-Herzegovina in the 1995 case *Kadic v. Karadzic*. In 1995, in *Wiwa v. Royal Dutch Petroleum Co.*, the Second Circuit permitted Nigerian emigrants to sue two foreign holding companies for alleged participation in human rights violations against them by government forces in connection with their opposition to oil exploration activities in Nigeria. The case involved as well claims of coercive land appropriation without adequate compensation and environmental claims of air and water pollution. In 1996, in *Mushikiwabo v. Barayagwiza*, a U.S. district court awarded $105 million to five Rwandan citizens for torture and execution of relatives by government forces and Hutu political militias during the 1994 genocide campaign against the Tutsi. Since the early 1990s, at least an estimated two dozen companies have been sued over alleged complicity in abuses committed in other countries—for example, torture in Guatemala (Del Monte), murder in Colombia (Coca-Cola), and environmental damage in Ecuador (Chevron Texaco).

The U.S. Supreme Court held in June 2004 in *Sosa v. Alvarez-Machain* that U.S. courts have jurisdiction under ATCA to hear claims concerning violations of international treaties or customary international law. Alvarez, a Mexican citizen, was allegedly abducted to California by a fellow citizen hired by the Drug Enforcement Agency (DEA) to face trial for torture murder of a DEA agent. The Supreme Court unanimously dismissed Alvarez's claims as not meeting ATCA standards, but determined that the ATCA was suitable for claims concerning human rights violations.

The Unocal Case

In December 2004, following the *Sosa* decision, Union Oil of California (Unocal) settled an ATCA lawsuit out of court. Unocal was then acquired for about $18 billion by Chevron Texaco (itself subsequently under ATCA litigation concerning alleged environmental pollution in Ecuador, as described in the next section).

Unocal was sued in 1996 by human rights activists in both federal and California state courts on behalf of anonymous ("John Doe") Burmese farmers. The suits alleged complicity in and liability for human rights abuses in connection with the Yadana Gas Pipeline Project in Burma. There was an activist effort to revoke Unocal's California corporate charter. The George W. Bush administration filed a brief in the Unocal case arguing that human rights violations and environmental claims should be regarded as impermissible under the ATCA, which should be restricted to offenses against diplomatic immunity.

The Yadana Gas Pipeline Project in the southern Tenasserim region of the country was organized to move energy resources from the Andaman Sea across Burma to Thailand. Yadana is the largest foreign direct investment project in Burma. The project has been widely criticized both for potentially propping up the regime with revenues and for the regime's alleged abuses of local populations during construction of the pipeline. The project is a 1993 joint venture among Total (France) at about 31% share, Unocal (Union Oil of California) at 28%, PTTEP (Thailand) at 25%, and the Burma Oil and Gas Enterprise (a state-owned entity) at 15%. Total contracted for government security before Unocal joined. There have been accusations of human rights atrocities by the Burmese military providing security for the project in terms of forced labor, forcible relocation, rape, and murder. Total took the position that it was the victim of a disinformation campaign. Unocal argued that all work is paid labor and that local contractors must follow fair hiring practices.

After extended legal maneuverings, the Ninth Circuit Court of Appeals ordered the case to trial. The appeals opinion contains an informative discussion of whether the legal basis for the suit should be international law or federal common law—involving the allegation of forced labor as akin to slavery prohibited in the United States. The courts concluded that no action was feasible against Total or the Burmese and Thailand governments (due to sovereignty immunity). Unocal was the remaining defendant. In the United States, tort litigation involves joint and several liability doctrine, meaning Unocal could be found liable for damages.

International business may occur in countries where there are pervasive human rights abuses and social and economic repression. Burma is in the grip of a repressive military regime. In 1988, socialism-oriented dictator General U Ne Win gave up power after 36 years. A military junta seized power and did not honor the 1990 national election results in which the National League for Democracy (NLD), led by Daw Aung San Suu Kyi—daughter of the nationalist hero General Aung San assassinated in 1947 (he worked with the Japanese occupation during World War II against the British)—reportedly won 60% of the popular vote and over 80% of government seats. Daw Suu Kyi was placed under house arrest in July 1989 (remaining in that condition off and on to the present day) and received the 1991 Nobel Peace Prize. Levi Strauss discontinued outsourcing contracts in 1992; PepsiCo subsequently exited under pressure from a U.S. boycott campaign. There has been a prolonged international debate over whether sanctions or constructive engagement is the better approach for dealing with the Burmese situation. Daw Suu Kyi and most activist lobbies call for sanctions to bring down the regime.

Extension of ATCA to Environmental Claims

U.S. courts more typically dismiss environmental rather than human rights claims on procedural or jurisdictional grounds. In *Aguinda v. Texaco*, 30,000 Ecuadorian Indians sued Texaco (subsequently merged with Chevron) for alleged improper oil exploration and waste disposal practices in the Amazonian rain forest region. The district court dismissed on procedural grounds that Ecuador itself was an adequate alternative forum. The Second Circuit reversed on the basis that Texaco must submit to jurisdiction of Ecuador courts. The district court again sent the case to Ecuador, where litigation is underway. A remaining issue is whether the U.S. courts should and will enforce if necessary the findings of the judicial system of Ecuador. A suit concerning the Bhopal, India, chemical plant disaster by Union Carbide Corp. was dismissed by the Second Circuit on grounds that claims had been fully litigated and settled in India already.

An International Bill of Rights

The conception of human rights can be broadly expanded. The Chad-Cameroon Petroleum Development and Pipeline Project constructed by Exxon Mobil and joint venture partners with investment by the World Bank trying to develop a model project approach to controlling corruption and stakeholder impacts has received human rights criticism from Amnesty International in its September 2005 report "Contracting Out of Human Rights: The Chad-Cameroon pipeline project." A vital matter concerns whether the notion of a tort-violating law of nations or U.S. treaties can expand beyond genocide, slavery, and torture to forced relocation, fraud, and breach of duty to treat with dignity.

The global importance of the ATCA or the TVPA is the potential role of private litigation in expanding human rights protection. Generally, international law reflects what countries are willing to support and mostly out of national self-interest. International law develops progressively by customary practice, international treaty, and multilateral convention. The "International Bill of Rights" presently comprises three statements adopted by the UN General Assembly: the 1948 Universal Declaration of Human Rights, the 1966 International Covenant on Civil and Political Rights, and the 1966 International Covenant on Economic, Social and Cultural Rights.

—*Duane Windsor*

See also Bottom of the Pyramid; Cost-Benefit Analysis; Developing World; Justice, Compensatory; Legal Rights; Multinational Corporations (MNCs); Punitive Damages; Tort Reform; Torts

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Alternative Dispute Resolution (ADR)

Alternative dispute resolution (ADR) is a blanket term that refers to a number of different procedures for settling disputes that do not rely on litigated judgments. The hallmark of ADR is that all parties voluntarily accept a third party who assists with the process and/or the substance of the dispute.

The court system is designed to resolve serious disputes. Trained lawyers use an adversarial approach to make their case before a judge and jury. The hearings are formal in that there are strict rules about acceptable evidence and procedure. There is usually a public record of a case, and rulings may serve to set policy or precedent. Litigation is often expensive, time consuming, and leads to judgments where a win for one side represents a loss for the other. Court cases are particularly effective when there is a need for a clear ruling on a particular matter or when they involve distributing resources between rival claimants. However, the vast majority of disputes in America are resolved outside the courts. Sometimes this is because settlement talks produce agreement prior to the case being heard. Many cases are resolved by various means of ADR. The incentives for moving to ADR may include the potential for a resolution that is less expensive, less time consuming, more predictable, or one that may be customized to the particular details of the conflict. ADR is appropriate in cases where there is a continuing relationship between the parties, and the issues are not limited to allocation. Thus, a violation of worker safety standards or establishing a payout of assets after a bankruptcy may benefit from formal adjudication, whereas ADR is useful in cases such as contract negotiations or settling a dispute between neighbors.

ADR encompasses a number of processes that range from the parties framing their own settlements to private systems that echo what goes on in court. The kinds of ADR are quite flexible and may be adapted as the parties see fit. They include arbitration, mediation, hybrid mediation/arbitration, early neutral evaluation, minitrials, and summary jury trials. Parties may choose to engage in ADR instead of going to court or may undertake it concurrently with regular court procedures, so that they have the default of litigating if ADR is unsuccessful.

The two most common forms of ADR are arbitration and mediation. Arbitration involves a neutral party who hears evidence and decides on an outcome that is then imposed on the parties. Essentially, it is a form of private judgment that echoes the court system except that it has more relaxed rules on procedure and evidence and takes place in an informal setting. In contrast, a mediator is more of a negotiation expert who assists the parties to come to a settlement of their own. Legal precedent and findings of right and wrong take a minor role in mediation because the mediator's job is to help the parties find an outcome that satisfies their interests to the greatest extent possible. Some institutions have integrated internal ADR functions into the office of the ombudsperson.

Arbitration

Arbitration is a form of delegated decision making. The authority to make a decision or render an award is handed over to a third party, who adjudicates the case and then the parties abide by the ruling. Both sides in a dispute mutually and voluntarily choose the arbitrator. Arbitrators can be anyone that the parties agree to: A construction company may feel that a retired engineer would be more acquainted with the specialized issues and more capable of rendering an authoritative decision in a dispute than someone trained as a lawyer. The American Arbitration Association is a commercial organization that trains and refers professional arbitrators.

Arbitration is often included in purchasing or service contracts as the initial procedure to be used in the case of a dispute. For example, it is not unusual for customers to agree at the time of a new car purchase that they will go to arbitration if there is a subsequent dispute with the dealer or manufacturer and then be bound by the arbitrator's decision. Parties may agree to arbitration as a step before litigation or even after court proceedings have begun.

Arbitration may be attractive because it is more flexible and efficient than the formal legal system. The parties are not bound by strict rules on procedure, and may frame the approach they believe most appropriate for their case. Thus, issues of discovery, rules of evidence, and reliance on case law are all negotiable before the arbitration begins. The process allows greater involvement and opportunities to be heard than formal litigation. Arbitration is often more inexpensive and faster than traditional resolution through the courts.

Decisions made by arbitrators differ from court-mandated judgments in several ways. First, they do not carry the force of precedent. Therefore, individuals with similar cases cannot rely on previously arbitrated decisions as a basis for a later ruling, nor can they automatically expect a similar outcome. Second, the arbitration procedure does not usually allow for an appeal. Hence, although it is efficient it carries the risk of infringing on the legal rights of one party without providing a forum for recourse.

There are many varieties of arbitration. One of the best-known is "baseball" arbitration because it has been used to settle salary disputes of major-league players. In this procedure, disputants attempt to reach a settlement, but if they fail to do so by a set date they are obliged to submit their last offer to an arbitrator who is required to choose one of them. As well as "last best offer" arbitration, there is wide latitude in process design. For example, in "control contract" arbitration, parties agree to a range of settlement ahead of time and adjust the arbitrator's award so that it stays within those limits.

Private judging is another kind of arbitration. Parties contract with a knowledgeable legal expert, usually a retired judge, to hear their case, apply the rule of law, and render a binding decision. The process is typically more expeditious, inexpensive, and confidential than the traditional court setting. A more sophisticated form of private judging is the minitrial, which is a voluntary settlement conference. Attorneys typically represent parties and reveal their entire case to a judge during the process, who then renders an opinion or, if the parties agree, a judgment. It tends to be less adversarial than regular court proceedings, because both sides are aware that the goal is settlement rather than victory. It is rare for a minitrial to involve witnesses, and thus, the focus of the proceeding is on questions of law and fact instead of personal credibility.

Nonbinding arbitration invites experts to give an unbiased advisory opinion about a case, or the use of judges or other professionals to predict how the case might be resolved in court. This gives the disputants an idea of how worthwhile it is to pursue legal remedies and what a realistic settlement range might be. It is also useful when expert opinion may sway the parties' perceptions, for instance, in settlement negotiations that have reached impasse or where impartial third parties can assess the value of economically elastic assets such as art or real estate.

Mediation

Mediation is a procedure that enhances the parties' ability to negotiate. Mediation is the intervention into the dispute of an acceptable, neutral, and impartial third party without decision-making authority who is present to assist the parties in developing their own mutually acceptable agreement. A mediator's main job is to manage the process without imposing decisions on the parties. For example, in a dispute over terms over working conditions the mediator will invite the parties to treat the issue as a mutual problem that the parties have to solve together rather than telling them what the outcome will be.

In most states, mediation is considered confidential, and this allows the parties to disclose matters that may lead to settlement. Mediators examine the causes of a dispute and attempt to define issues in a way that makes them clearer and more easily resolvable. They may suggest a process that enables each party to maximally satisfy their interests. Because mediators have no independent authority other than that granted to them by the disputants, their main role is to manage the procedure rather than the substance of the negotiation. They may set ground rules and reframe statements into more value-free language. Mediators often test agreements by asking the parties to consider hypothetical situations and options. Sometimes they test whether the parties have realistic perceptions about their potential for winning a lawsuit or the time and cost involved in a particular course of action.

Mediators often classify negotiation approaches as either positional or interest based. A position represents an explicit demand for a particular settlement—perhaps an amount of money or other restitution. Interest-based bargaining begins with the discovery of the parties' underlying interests as opposed to the positions that they espouse.

For example, if an employee wants to leave a company but contests its no-compete clause, both sides may face the time and expense of litigation. In confidential discussions, the employee discloses that he is going through a nasty divorce and his wife works in the same department. His interests are to avoid being around his spouse in the workplace, yet he feels constrained in his employment opportunities because of his specialized training. The employer wants to keep their competitive advantage in the market by keeping trade secrets. A skillful mediator would allow both sides to put their positions on the table and then see if there is room for mutual accommodation or compromise that would still satisfy both parties' needs; it may be that the employee could move to another department within the company, or the company could modify their clause to cover only certain aspects of the job. The outcomes need not be optimal for all concerned—indeed, both could be equally unhappy with them, but they are probably more attractive than the alternative of prolonged and expensive litigation. Mediation is usually initiated when the parties are willing to negotiate but feel that they need assistance in dealing with emotional or psychological barriers to substantive agreement.

Mediators differ widely as to how directive they are with the disputants. Some actively suggest solutions and craft agreements, whereas others are more concerned with encouraging the parties to come up with their own settlement. Mediated agreements may be quite informal and rely on the voluntary compliance of the parties, while others are memorialized as formal contracts drafted by lawyers. Mediators come from a variety of backgrounds, including law, social work, and psychology.

Because mediation involves some degree of accommodation or compromise, it will be unsuitable for some types of dispute. Thus, some cases are useful in establishing public policy and are best dealt with in the courts. Other poor candidates are those that involve safety or tortious liability. There are concerns that although mediation has high settlement rates, the process itself is shielded by confidentiality agreements and does not afford much opportunity for legal review or appeal.

Hybrid Processes

Mediation/arbitration (or med/arb) is a hybrid process that starts by having the parties try to come to an agreement themselves. If they fail, then they ask the mediator to decide on a settlement. The process may be more efficient if mediation fails because the neutral is already aware of the facts and issues involved. However, there are concerns that the dynamics of the mediation will change; participants will be unwilling to fully disclose information that may later prejudice their arbitration case, and they may treat the mediator as an adjudicator.

Another variation is known as early neutral evaluation, where court officials screen disputes that are slated for litigation, and those with the potential for settlement are steered to evaluators who facilitate settlement discussions.

Special masters are appointed by federal judges to assist in settlement of large lawsuits under Federal Rules of Civil Procedure 53. They are typically specialized experts who manage complex issues and encourage settlement. Their decisions have the backing of the court. They will often act as arbitrators who present the parties with a settlement zone and expect the parties to come to resolution within it.

Another court-ordered form of ADR is the summary jury trial. This usually occurs when all parties are fully prepared for trial. In corporate cases, executives with settlement authority are required to attend the trial. The judge may order each side to produce exhibit lists and summaries of likely witness testimony. A jury is selected and hears the evidence from both sides. At each stage of the hearing, the executives are encouraged to engage in settlement negotiations. After the jury reaches a verdict, representatives of each side are allowed to question members on their perceptions of the case. The process has the benefit of allowing the parties to have a court hearing while at the same time promoting autonomous and efficient settlement.

Individuals are faced with significant outlays in time, money, and emotional strain when taking cases to court. In many cases, the intervention of a third party can help disputants realize their procedural, psychological, and substantive interests more effectively than a judicial decision could.

—Kevin Gibson

See also Litigation, Civil; Negotiation and Bargaining; Ombudsperson; Satisficing

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Altruism

Altruism is the conscious devotion to helping others regardless of whether the motivation is self-interested or other centered. It is a premeditated pursuit of charity to unify and increase the overall welfare of society. Although there is some dispute among moral philosophers as to the merits of the doctrine, altruism is generally viewed as the opposite of "egoism." *Altruism* was first employed as a term or concept by the French positivist philosopher Auguste Comte in 1831. Derived from the French root, *autrui*, meaning "other people," Comte favored an ethical perspective that individuals need to attend to the interests of others as a way of achieving universal happiness. The specific definition and focus of altruism varies significantly across different disciplines. Despite its ethical roots, more modern views offered by political scientists, psychologists, sociologists, and biologists have led to different approaches to the concept. Altruism's place in business has also been questioned.

Altruism and Moral Philosophy

From a philosophic point of view, altruistic behavior is deliberate with the underlying intent to help others. Ancient accounts on ethics explored the virtue of being helpful to others. To understand human nature, Plato and Aristotle devised a naturalistic ethics that focused on how moral virtues were linked with a person's happiness. A moral way of life involves behaviors that generate intrinsic happiness within individuals. It is part of human nature that individuals would seek such pleasure. Principles of justice were considered an altruistic quality by Plato but were closely tied to the psychological motivation to produce intrinsic happiness. The Socratic position differed slightly in that virtuous behavior was viewed to be derived from moral wisdom and that justice toward others is a good in itself for the greater benefit it generates. Altruism developed as a refutation of ethical egoism—that it is unethical and irrational for individuals to engage in behavior that compromises their own self-interest.

From this groundwork laid down by moral philosophers in response to the idea of ethical egoism, Auguste Comte originated the actual term *altruism* in the mid-19th century. However, the creator of the term believed that emotion did indeed play a role in the motivation to care for others over self. Comte posited that human beings were motivated by both self-interested feelings and socially benevolent emotions. His ethical theory stated that morality is the subjugation of self-interested tendencies in favor of other-regarding drives to promote societal welfare. True happiness could be found in a life that serves others' needs and interests. This understanding of altruism has religious overtones as well. Christian dogma professes that decent followers should love their neighbors as they would love themselves. By serving the needs of the greater humanity, an individual is serving God.

In contrast to Comte's view of altruism, English social evolutionist Herbert Spencer took a more psychological approach to understanding the motivation to be altruistically inclined toward others. Having coined the phrase "survival of the fittest," Spencer—a contemporary of Charles Darwin—believed that feelings of pleasure or happiness became biologically inherited in the later stages of evolution, when social relationships were important for survival. Intrinsic egoistic feelings of happiness transformed into pleasurable feelings associated with helping others. Spencer claimed that humans were capable of making psychological associations between certain actions and the pleasure generated by those actions. Behaviors that sustained and promoted the greater good of society—a utilitarian notion—induced emotional and psychological pleasure for those individuals engaging in those prosocial acts. The ethical standard of altruism resulted when these associations of personal happiness and greater societal utility were passed down to later generations. Societies prosper when the greater utility of the community is served by individual acts.

Psychological Altruism

Also skeptical that such a selfless motivation exists, psychologists waged their own critique of altruism. One idea that is counter to the existence of altruism is psychological egoism. Psychological egoism describes behavior that is seemingly altruistic but that has underlying selfish motivations. This view contends that individuals are instrumental in nature and will perform acts of kindness that help others but only in the hope that the favor will be returned some day. The promise of reciprocated rewards provides the motivation for the act. However, it is difficult to prove whether or not purely altruistic behavior actually exists. The biologists attempt to provide the mechanism and rationale for altruism.

In contrast, the cognitive basis of psychological altruism rests in people's desires. Being concerned for another's welfare does not mandate self-sacrificing behavior, however. Wishing that someone else other than you succeeds need not mean incurring a cost. Often, assisting another person does not involve an expense or risk to the benefactor.

The psychological perspective on altruism strongly emphasizes the role of cognition in determining moral behavior. Cognitive psychologists such as Lawrence Kohlberg do not ignore the fact that emotions have a role in determining how individuals are motivated to act morally, but they do play up the role of reason for making moral decisions. In his hierarchical stage model of moral development, Kohlberg asserted that people progressed from self-centered motives for behaving morally to a concern for others as they developed morally through their experiences, education, and growth. The fact that a concern for the welfare of others only becomes a motivation for moral behavior at later stages in his model suggests that altruistic motivations are considered a higher morality.

In game theoretic terms, the prisoner's dilemma demonstrates how altruistic behavior is rationally the best choice in a single-iteration game. Given a situation where you and an accomplice are questioned for a crime, does it pay the two parties to act selfishly and confess the crime, or is it more advantageous for them to act altruistically and remain silent in the interrogation? Cumulatively, in terms of the costs incurred for confessing the crime, the parties are worse off if they both act selfishly than if they had acted altruistically. The jail time is longer if both acted in his or her own self-interest.

Biological Perspective

In biology, altruism occurs when a living being performs an act that benefits another being at the expense of the creature performing the act. It is when someone behaves for the sake of someone else at a personal expense with no immediate observable benefit. With biological altruism, no conscious motive needs to underlie the behavior. This is quite different from philosophical notions of altruism, which are centered on the idea that individuals consciously behave to help others for the sake of the good of the act. The implicit motive is based on the moral sensibilities of the person performing the act. In classical economics, altruism was counterintuitive to the rationally self-interested human. In evolution, altruism made more sense because of the purpose it served.

William Hamilton addressed the issue by examining individuals' survival abilities in their environment. He posited that altruism is not dispensed randomly but with reference to kin. Individuals will discriminate against those organisms that do not appear to be close kin to the individual offering the altruistic act. In the face of the concept survival of the fittest, Hamilton argued that genes can only be spread if the gene benefits from a behavior. It has little to do with whether the host of the gene benefits from a behavior. Altruistic tendencies proliferate in groups of individuals if the behavior is toward family members who may possess that altruist's genes. Thus, Hamilton developed his concept of inclusive fitness, where the principles of survival and adaptability not only pertained to the individual person but also to anyone in the group who may have similar genes. Behavior that seemingly costs the altruist in some regard at the organism level may in fact benefit the altruist's building blocks at the gene level of analysis.

For business ethics this is important because the biological explanation of altruism assumes that the trait became part of an organism's genetic makeup or phenotype. Altruism as a moral principle served an adaptive function that aided human beings to survive. Group cooperative behavior was facilitated by moral principles and enabled humans to maneuver through social exchanges.

Altruism and Business

As a concept, altruism has faced sharp criticism from philosophers such as Friedrich Nietzsche and Ayn Rand, who claim that purely selfless behavior does not exist and that the concept itself is morally subversive. These critiques of altruism are based on the morality of egoistic behavior. Nietzsche argued that it is unnatural for an individual not to be concerned for personal self-interest. Rand asserted that altruistic behavior is unethical and detrimental to business organizations because it represents a conscious disregard for the natural values that are necessary for survival. Her objectivist ethical standard focused on rational values with no regard for feelings or emotion. These rational selfish values did not include human sacrifices.

Altruism's place in business ethics is subject to debate and is dependent in large part on which model of human nature is used. Free market beliefs espoused by neoclassical economists viewed humans as rationally self-interested. In this view, people are motivated to advance their own interests in spite of potential costs to others. In a laissez-faire economy, the market will operate to society's benefit if everyone strives to satisfy their own needs. Adam Smith argued that by pursuing one's own self-interest, the interests of society are served. He states that individuals cannot depend on the benevolence of others in society to survive. Rather, it is people's self-orientation that supports industry and business.

Managerial capitalism, based on assumptions from neoclassical economics, contends that the firm is run in the interests of the shareholders, or owners of the business. In this model, the interests of parties outside of the stockholders are not directly considered. Milton Friedman believed that managers of businesses had no obligation to attend to the needs of other individuals, unless otherwise dictated by a majority of the shareholders. To him, no social responsibility existed outside of making a profit for the owners of the firm. The managers were agents of the owners and were solely responsible for making money for the company. Altruistic behavior would go against this agenda. Thus, does altruism have a role in organizations at all if business is driven by self-interested motives?

In an alternative theory of the firm, a broader group of interests are considered. Stakeholder theory allows room for the needs of others to be taken into account by business. In fact, stakeholder theory states that business interests are better served when managers pay attention to the demands of any individual or group who has a stake in the operations of the company. So a manager's role is to attend to the claims of multiple parties. The goal is to have a balanced relationship with the stakeholders of the firm. Certainly, in the course of satisfying multiple stakeholder claims, the interests of the shareholders should be served. Many studies have shown a correlation between corporate social performance and corporate financial performance. In effect, the argument is that firms can do well by doing "good" for others. Corporate social responsibility is based on the core idea that managers are stewards of society. Taking care of stakeholders will generally result in shareholders doing well financially. It could also be argued that generating shareholder wealth and increasing their value in the firm will benefit several stakeholder groups as well. As a doctrine, corporate social responsibility encourages that businesses work to promote the betterment of society. If shareholders do not get anything in return, however, the business may ultimately cease to exist. This is not exactly a selfless act to benefit others if the underlying motivation is to generate profit.

Taking into account all the varying perspectives on why people act in a prosocial manner, it is difficult to conclude what specifically motivates this behavior. Regardless of whether altruism truly exists, individuals do help others. Even if the underlying motive is personal gain, acts that benefit others do occur. Perhaps the most accurate description of altruism incorporates a pluralistic view of motivation, in which both self-regarding and other-regarding drives are acknowledged.

—David M. Wasieleski

See also Agency, Theory of; Cognitive Moral Development; Darwinism and Ethics; Egoism; Evolutionary Psychology; Kohlberg, Lawrence; Positivism; Rand, Ayn; Reciprocal Altruism; Utilitarianism

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American Bar Association

The American Bar Association (ABA) is believed to be the largest voluntary professional association in the world. In 2005, there were more than 400,000 members. Five main aspects of the ABA will be considered: (1) origins, (2) purpose and goals, (3) structure and divisions, (4) lobbying, and (5) programs.

Origins of the ABA

Saratoga Springs, New York, was the birthplace of the ABA. It was founded on August 21, 1878, by a group of approximately 100 attorneys representing 21 states. The profession was very different at that time from the contemporary legal world. The law industry that exists today was only beginning to emerge at that time. Attorneys were typically solo practitioners who had been trained as an apprentice.

Purpose and Goals

The purpose of the ABA can be discerned from its mission statement and the published ABA goals. "The mission of the American Bar Association is to be the national representative of the legal profession, serving the public and the profession by promoting justice, professional excellence, and respect for the law," the ABA proclaims.

The published goals of the ABA are as follows: (1) to provide improvements in the American system of justice; (2) to promote meaningful access to legal representation and the America system of justice for all persons regardless of their economic or social condition; (3) to provide ongoing leadership in improving the law to serve the changing needs of society; (4) to increase public understanding of and respect for the law, the legal process, and the role of the legal profession; (5) to achieve the highest standards of professionalism, competence, and ethical conduct; (6) to serve as the national representative of the legal profession; (7) to provide programs, benefits, and services that promote professional growth and enhance the quality of life of the members; (8) to advance the rule of law in the world; (9) to promote full and equal representation in the legal profession by minorities; (10) to preserve and enhance the ideals of the legal profession as a common calling and in dedication to public service; and (11) to preserve the independence of the legal profession and the judiciary as fundamental to a free society.

ABA Structure

The ABA is an inherently complex and extensive organization, because of the size of its membership and the diversity of the issues with which it deals. The main assembly of the ABA, the House of Delegates, was established in 1936. ABA publications call this body the policy-making organ of the association and, therefore, responsible for the direction and administration of the ABA.

In addition, the ABA is managed by a board of governors. This 38-member group supervises the general operation of the association and develops specific tactical plans. This committee meets quarterly.

Much of the operational activity of the ABA is accomplished through the approximately 2,200 organizational entities encompassed within the association. In fact, there are six levels or types of entity within the ABA; the main three are sections, divisions, and forums. There are 22 sections, 6 divisions, and 6 forums. The purpose of the ABA sections, divisions, and forums is to provide a consistent structural organizational presence with respect to the specific subject in question, such as business law, antitrust law, and taxation. Much of the work of the ABA is accomplished through these organizational entities. In addition, the ABA structure includes committees, commissions, and task forces. In 2005, there were an estimated 3,500 committees, six forums, and half a dozen task forces.

Not only is there a relatively large number of subgroups within the ABA, but the membership of these specialized subsections tends to be substantial. The ABA estimated that section membership size ranges from a low of at least 2,300 to larger entities with more than 70,000 members.

ABA Lobbying

Lobbying might be the main activity of the ABA. The Government Affairs Office lobbies governmental entities on behalf of association interests. For instance, the 106th Congress, which met in 1999 to 2000, was lobbied on more than 100 different public policy issues, gave testimony at nearly 30 congressional hearings, and sent about 160 letters to various members of Congress, certain congressional committees, and particular executive branch offices.

Political lobbying is not uncommon. The ABA has in the past denounced President Bush's warrantless domestic surveillance program. The death penalty has also attracted the attention of the ABA, which has called for a moratorium of the practice.

ABA Programs

ABA members actively participate in a number of very important social outreach programs. The ABA declared that it provides law school accreditation, continuing legal education, information about the law, programs to assist lawyers and judges in their work, and initiatives to improve the legal system for the public.

The ABA has implemented literally hundreds of legally oriented client service programs, addressing a diverse range of public interests, another source noted in 2006. It specified that these programs concerned child abuse, protection of the elderly, affordable legal services, law clinic practice management, domestic violence, and juvenile justice programs, to name a few. Another important instance of ABA benevolence involves the charitable work of the association. The ABA, in fact, supports three different major charities: the American Bar Endowment, the Fund for Justice and Education, and the American Bar Federation.

—Andrea Clark, Glen Loveland,
and Dirk C. Gibson

See also Alternative Dispute Resolution (ADR); Association of Trial Lawyers of America (ATLA); Business Law; Natural Law Ethical Theory; Tort Reform; Trade Associations; Warranties

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American Civil Liberties Union (ACLU)

The American Civil Liberties Union (ACLU) dedicates itself to protecting the rights guaranteed by the Bill of Rights of the United States Constitution. The framers of the Bill of Rights designated those areas of civil life where government could not intrude, ensuring that those rights belonged to individuals and the associations to which they belonged. The Bill of Rights limited the government's authority to regulate freedom in areas such as speech, religion, assembly, press, the right to petition one's government, and to be safe from unwarranted search and seizure. From its founding in 1920, the ACLU has grown from a single office to an organization with chapters in almost every state.

Chapters possess some degree of autonomy and may pursue strategies prior to the national board voting on an ACLU position. As a national organization, the ACLU protects civil liberties through litigation, lobbying, and public education. Since its founding, the ACLU has expanded to include staff attorneys and a membership of over 500,000 persons. Some chapters have developed specific projects focusing on issues such as juvenile rights, prisoner's rights, national security, gay and lesbian issues, immigrant rights, and voting rights, although all are dedicated to the mission of vindicating civil liberties.

Two historical facts help explain the development of the ACLU. Many of the Constitution's framers did not believe a Bill of Rights was necessary. Fearful that enumerating rights would suggest federal powers that were not explicitly named, the framers initially believed that the federal government would only possess powers specifically enumerated in the Constitution, thus securing those liberties not regulated by the Constitution. The absence of a Bill of Rights, however, threatened state ratification resulting in the adoption of the first 10 amendments that specifically prevented Congress or the government from infringing on individual rights. Unlike the government's duty to prosecute crime, however, government was not specifically charged with enforcing the Bill of Rights. Protecting these rights often necessitated litigating against government action that appeared to violate constitutional protection or lobbying against legislation that would authorize government restriction of individual liberties. Even the judiciary, established to complete the checks and balances between the branches of government, required a party to file a case to determine whether a constitutional violation occurred. An affected individual or association or some nongovernment entity acting on behalf of that individual would have to call the government's alleged violation of those civil rights into question.

Second, the 20th century witnessed expansive growth of the federal government, especially in its reach over the lives of its citizens. The Supreme Court's interpretation of the Constitution's Fourteenth Amendment incorporating the protections of the Bill of Rights against state governments led to a concomitant need for protection against encroachment of rights by any government, whether federal, state, or local. Simultaneously, the United States became a world power with its involvement in the two World Wars and leadership throughout the Cold War. That new role increasingly raised concerns over new national security laws. Furthermore, the expansion of the welfare state as orchestrated by the federal government multiplied government regulations affecting all citizens and residents.

Under a constitution that necessitates citizen diligence to ensure that government does not overstep its bounds, the task of defining and protecting liberty never ends. The expanding scope of government and the constant threats, domestic and international, will always lead to imperfect responses to perceived threats. In times of war and economic crisis, elected leaders often interpret their duty to provide for the common defense and promote the general welfare in ways that limit individual rights. Majority concerns about national security and the loss of a perceived unique American culture lead to legislation that places vulnerable minorities or the foreign-born at risk. In response, the ACLU grew into a national organization with both staff and volunteer attorneys to address these new challenges. Even the United States Supreme Court has recognized the ACLU's role, finding that it has "engaged in the defense of unpopular causes and unpopular defendants and has represented individuals in litigation that has defined the scope of constitutional protection in areas such as political dissent, juvenile rights, prisoners' rights, military law, amnesty, and privacy" (*In re Primus*, 1978).

Although the ACLU reacts to new laws and threats to liberty, it also lobbies and educates prior to legislation. Because it represents the most vulnerable at times of war or natural emergency, it often engages in great internal debates and endures hostile public opinion. A few examples culled from its eight decades reveal these tensions and consequences. Initially, the ACLU developed in the post–World War I years when the National Civil Liberties Union worked on behalf of the rights of conscientious objectors who had been imprisoned and fined during the war. Recognizing that the expanding reach of government would affect civil liberties beyond conscientious objection to war, Roger Baldwin proposed to establish a new organization whose mission would be dedicated to protecting all civil liberties. In January 1920, the ACLU began its work with Baldwin, Crystal Eastman, and Albert DeSilver among its founding members. Unlike other civil rights organizations, which were dedicated to a particular group or cause, the ACLU's founding principles called for the defense of civil liberties regardless of the person or organization professing the views.

Subsequent to World War I, the ACLU concentrated on labor's right to organize. In the absence of federal labor legislation, states frequently enacted laws restricting union organizing. In the 1920s, Attorney General Palmer arrested hundreds of immigrant union organizers and activists under the allegation that they were anarchists and terrorists. The Palmer raids led to the deportation of hundreds of immigrants and their families and affirmed the ACLU founders' beliefs that the Bill of Rights applied to more than just conscientious objection to war. In the 1920s and 1930s, the ACLU defended union activists and opposed the anti–civil libertarian restrictions that had stemmed from World War I. Significantly, dedication to protecting free speech also raised the issue of whether to protect the liberty interest itself, or the speaker. In 1937, when the National Labor Relations Board sought to restrict the Ford Motor Company's distribution of literature opposing the organization of its workers, the ACLU faced intense debate within its ranks because of its historical support of labor. Although the free speech principle led the ACLU to support Ford's position, the incident highlighted the complexity often faced by the ACLU in defending free speech.

As federal labor legislation increasingly protected employees, the ACLU responded to new challenges as religious groups such as Jehovah Witnesses were restricted from proselytizing and were punished for refusal to recite the Pledge of Allegiance in public classrooms. Often working in conjunction with the Jehovah Witnesses' attorneys, the ACLU defended the freedom to leaflet, sell literature, and exercise their religion. Young Jehovah's Witnesses following their biblical understanding to follow no other gods were expelled from schools for refusing to pledge allegiance to the flag. In an early case, the Supreme Court upheld school suspensions, but subsequently, in the midst of World War II, the Court rendered one of the most famous maxims in American constitutional history: "If there is any fixed star in our constitutional constellation, it is that no official, high or petty, can prescribe what shall be orthodox in politics, nationalism or other matter of opinion or force citizens to confess by word or act their faith therein" (*West Virginia v. Barnette,* 1943). Thus, the ACLU through many individual cases helped develop case law protecting religion and speech.

World War II brought President Franklin D. Roosevelt's executive order to designate military zones excluding Japanese Americans from residing within, thus leading to the internment of over 100,000 persons. The ACLU, despite great internal discord on whether to contest the president's wartime actions, challenged the president's executive order. The Supreme Court eventually upheld the president's right to detain the Japanese Americans, but the ACLU litigated after the war to restore rights lost by the detainees.

World War II again raised questions of conscientious objection to war and whether a segregated military violated the rights of African American soldiers. These issues constantly confronted the ACLU to determine how to support national efforts at defeating dictatorships without conceding the right of the United States to engage in unconstitutional activities. Whether supporting conscientious objectors, challenging internment procedures, or defending free speech in the Cold War, such controversies subjected the ACLU to intense internal debate and external criticism.

Defending unpopular minorities reached its high point when the ACLU decided to defend the right of an American Nazi to march in Skokie, Illinois, in 1977.

Initially rebuffed from marching in Marquette Park in Chicago, he sought permission to march in nearby suburbs. When Skokie requested a $350,000 bond, the ACLU was asked to contest the restrictions on free speech. Jewish residents composed almost half of Skokie's population and a significant number were survivors of the Nazi Holocaust. The tension between free speech and harm to a community's citizens could not be more marked. Skokie then enacted three ordinances that banned, in part, symbols offensive to the community and material that incited hatred based on race, national origin, or religion. The Illinois chapter, with the national ACLU's endorsement, challenged the ordinances. The federal district court, granting an injunction, reaffirmed that the First Amendment precludes government from restricting expression because of its message, its ideas, its subject matter, or its content. Although prevailing at court, the ACLU's Skokie case raised national questions of how far freedom of speech should be protected when its consequences harmed those receiving the speech. The ACLU became the center of controversy itself, and thousands resigned their membership.

Other areas reveal the difficulties of defending the concept of liberty as one person's liberty may infringe another's freedom. The First Amendment protects the exercise of religion and prohibits government establishment of religion. Throughout the 1940s, the ACLU filed numerous briefs supporting the free exercise of Jehovah's Witnesses to stand on streets and proclaim their religion. They helped defend public school children who believed their religion would be violated if they pledged allegiance to anything or anyone other than their God. Subsequently, the ACLU's position on the establishment clause led to litigation contesting perceived religious partnerships with government, championing the metaphor that the Constitution guarantees separation of church and state. But that separation may infringe one's free exercise when courts remove familiar symbols such as Ten Commandments from parks and courthouses, eliminate prayer from public schools, or delete "under God" from the Pledge of Allegiance. Many other legal organizations have since argued that the ACLU limits liberty because free exercise permits more public recognition of religion, and establishment jurisprudence does not call for a strict separation of church and state.

The growth to meet expanding issues has not occurred without controversy. By seeking to protect any violation of rights, the ACLU confronts the question of how to protect all civil liberties without turning allies into opponents. The Skokie case and the religious freedom cases reveal this intrinsic stress point within a large national organization. Protecting individual liberties during the Cold War called on the ACLU to decide how to protect the liberties of those accused of subverting our government while supporting a rule of law that permitted such challenges. State chapters and interest-related programs often view issues from their context and disagree with the national leadership. Local-national perspectives may place different priorities on developing issues involving racial discrimination, women's rights, sexual orientation, traditional concepts of marriage, or the rights of the foreign-born leading to conflicts within the ACLU. New challenges arise. Technologies unimagined by the drafters of the Constitution provide greater information to government, but raise complex issues involving privacy and freedom of speech. Shortly after September 11, 2001, Congress enacted the USA PATRIOT Act containing provisions granting access to private information, restricting immigrants, limiting legal recourse against government action, and increasing surveillance and monitoring of citizens. The ACLU has contested broad interpretation of the act and lobbied to eliminate provisions during renewal legislation. Although internal and external critics challenge the ACLU as subverting traditional values or strengths in a time of war or great social change, the ACLU has encouraged more speech and more ideas to help determine how best to define liberty in the 21st century.

To some extent, the ACLU remains reactive to laws that affect liberties. Its defense of the vulnerable has raised significant deliberations of how to protect liberty against government encroachment. Through its lobbying and educational efforts, it not only encourages greater citizen involvement but also attempts to persuade government officials to enact legislation that secures the national defense without trampling on individual liberties. The ACLU's history of defending those who are threatened, seeking more transparency in government action, and educating the public calls government to accountability and serves to ensure the continued vitality of the Bill of Rights' protections.

—Craig B. Mousin

See also Labor Unions; Liberalism; Rights, Theories of; USA PATRIOT Act

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American Federation of State, County and Municipal Employees

The American Federation of State, County and Municipal Employees (AFSCME) is the largest public services union in the United States. The union seeks to promote economic and social justice in the workplace. AFSCME is an affiliate of the American Federation of Labor and the Congress of Industrial Organizations (AFL-CIO).

The constitution of the AFSCME lists seven objectives for the organization. The first four objectives center on membership: (1) to promote the organization of workers in general and public employees in particular, (2) to promote the welfare of the membership and to provide a voice in the determination of the terms and conditions of employment, (3) to promote civil service legislation and career service in government, and (4) to provide research and educational services. The remaining three objectives focus on AFSCME cooperation with other constituencies: (5) to foster cooperation among affiliates; (6) to cooperate with labor organizations and others to justly distribute the material riches of American society; and (7) to work with people in other lands to improve the conditions of work in all countries, toward the diminution of international tensions.

The AFSCME has more than 1.4 million members. They work in child care centers, corrections facilities, government facilities, hospitals, offices, schools, and universities. Approximately 45% of its members work in county and municipal governments and for school districts. State government workers account for approximately 37% of the union's membership. College and university and nonprofit members compose 10% of the union's membership.

The officers of the AFSCME include the international president, the international secretary-treasurer, and the international vice presidents. There is an international vice president for each of the union's 24 legislative districts. In addition, some districts have two or three international vice presidents based on their concentration of members. All sovereign powers of the union rest with its biennial convention; however, a special convention for specific purposes can be called at any time by the international executive board or by the request of any 10 legislative districts. The headquarters of the union is, by its charter, in the Washington, D.C., metropolitan area.

In 1965, the AFSCME held a special convention to create a "Bill of Rights" for its membership as part of a campaign by International President Jerry Wurf to emphasize union reform and union democracy. The Bill of Rights for the union membership emphasized eight areas: (1) equal opportunity in union membership, (2) active and free discussion of union affairs, (3) the right to conduct internal union affairs free from employer domination, (4) free and democratic elections at all levels of the union, (5) equal rights by members to run for and hold office, (6) a full and clear accounting of all union funds, (7) full participation in all union decision making, and (8) a fair trial with strict due process for any member or officer charged with wrongdoing.

The AFL chartered AFSCME in September of 1936. At that time the primary focus of the union was to lobby to pass or strengthen civil service laws. After the AFL-CIO merger in 1955, the union began stressing public workers' rights and collective bargaining as a means to improve the working conditions of its members.

Around 1970, the union began to focus on political action in its efforts to increase its membership and as a means to increase its power. Currently, the AFSCME views itself as an important participant in dialogues concerning a variety of critical political and national issues. The AFSCME has sponsored political advertising and grassroots political campaigns supporting Medicare and other government entitlement programs.

Through its pension program, the union has established a program to conduct shareholder proxy campaigns targeted toward restraining excessively generous executive compensation packages.

The current emphasis on political power has sparked an ongoing debate on the nature and appropriateness of political activity by public employee unions. This debate is framed around potential conflicts of interest. The argument goes as follows: Public sector employees in a "monopoly position" pay union dues that then support and elect self-interested political officials who in exchange for continued campaign contributions are co-opted to the self-interested demands of the unions in subsequent contract negotiations. These inherent conflicts of interest lead to self-reinforcing cycles of inefficient and dysfunctional government actions and public policy that, in turn, lead to higher taxes at every level of government. Such potential conflicts of interest are not unique to unions; they also could apply to corporations, PACs, and other interest groups.

—Frank L. Winfrey

See also AFL-CIO; Job Security; Justice, Distributive; Labor Unions

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American Federation of Teachers

The American Federation of Teachers (AFT) is a labor union that represents teachers and other educational workers. It is a national organization of over 1 million members, over 40 state groups, and over 3,000 local groups. Founded in Chicago in 1916, it is affiliated with the American Federation of Labor-Congress of Industrial Organizations (AFL-CIO). The mission of the AFT, adopted in July 2000, is to improve the lives of their members by representing their aspirations and strengthening their institutions. The AFT Web page states several beliefs that the organization advocates: high academic and conduct standards for students, greater professionalism for teachers and school staff, cooperative problem solving and workplace innovations, and high-quality health care provided by qualified professionals.

The AFT has five divisions: teachers; paraprofessional and school-related personnel; local, state, and federal employees; higher education faculty and staff; and nurses and health care professionals. The groups of members elect delegates to biennial conventions where officers are elected and union policy is set. The president and secretary-treasurer are also vice presidents of the AFL-CIO.

The AFT has a long and proud history of proactive political activities on behalf of their members. Early teachers' contracts included dress and social strictures with some districts banning union membership. The 1932 Norris-LaGuardia Act outlawed such contracts. During the McCarthy years, the union defended their members' academic and personal freedoms. One of the first groups to extend full membership to minorities, they were also heavily involved with the Civil Rights Movement, with their emphasis on desegregation of schools and voter registration drives in the South. During the 1960s, teacher militancy began with a 1-day walkout in New York City. More than 300 teacher strikes followed across the country, leading to comprehensive contracts with higher pay and better benefits. By 1970, membership numbered over 200,000. Since then, the union has been involved in the fight against tuition tax credits, educational reform, and educational standards. By 2005, there were 1.3 million members and 43 state affiliations.

The AFT has been criticized for putting their support of liberal political and economic activities before the education of children. The union officers and elected representatives choose which activities to support without a vote from the membership. The AFT social agenda is international as well as liberal and, as a result, sometimes these activities are not what individual union members would choose. Other criticisms are that the dues are very high and that union officials are too generously compensated.

—Carol H. Krismann

See also AFL-CIO; Civil Rights; Labor Unions

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American Institute of Certified Public Accountants (AICPA)

The American Institute of Certified Public Accountants (AICPA or the Institute) is the premier national, professional organization for certified public accountants (CPAs) in the United States and its territories. Although the majority of its active members are employed by either public accounting firms (39%) or in industry (42%), its members also occupy positions in law, consulting, government, and education.

A significant portion of the Institute's efforts relate to ensuring the ongoing professionalism of the Institute's members, primarily in the areas of accounting, auditing, and taxation. This is an extremely important part of the Institute's efforts, as it directly supports the critical role that CPAs have in relation to one of their primary functions—performing audits of the financial statements of public, private, nonprofit, and governmental organizations. This assurance function is an important component of the U.S. economic system, as it provides investors and creditors with independent verification that a company's financial statements have been prepared on a consistent basis in accordance with generally accepted accounting principles.

In addition, the AICPA seeks the highest possible level of uniform certification and licensing standards and promotes and protects the CPA designation. To accomplish this, the AICPA has assumed responsibility for maintaining the Uniform CPA Examination and works through the individual state boards of accountancy to administer the exam throughout the states. The AICPA also requires that its CPA members receive continuing professional education (CPE) to stay abreast of current developments in accounting-related areas and in general business topics as well.

The AICPA's mission is to provide its members with the resources, information, and leadership that will enable them to provide high-quality services in a manner that will benefit the public as well as employers and clients of CPAs. This is accomplished in a variety of ways, including member newsletters, publications (e.g., *The Journal of Accountancy*), educational programs, and special interest divisions of the Institute such as Taxation and Personal Financial Planning. In fulfilling its mission, the AICPA also works closely with state CPA organizations, giving priority to areas where public reliance on CPA skills is most significant. With approximately 335,000 active members, the AICPA serves the accounting profession by representing and promoting the interests of CPAs before governments, regulatory bodies, and other organizations.

The AICPA's history dates back to 1887, when the American Association of Public Accountants (AAPA) was formed in New York City by a group of British chartered accountants and American practitioners. One of the results of the Industrial Revolution in the United States was that a high degree of public reliance was beginning to be placed on the financial information provided by accountants. Thus, the founders of the AAPA sought ways in which the public interest might be protected. The AAPA proposed a college of accounts, where a 1,000-hour course of training, overseen by the AAPA, would have to be completed by anyone wishing to enter the accounting profession.

In 1895, the AAPA changed its direction and, instead, focused on securing legislation in the state of New York for the licensing of CPAs, a model more consistent with those used to demonstrate professional competency in other professions. Within a very short period of time, legislation had been passed in eight other states, and by 1925, almost every state had adopted some form of legislation relating to the accounting profession.

In 1917, the AAPA changed its name to the American Institute of Accountants and remained so until 1957, when it adopted its current name. Ultimately, in 1936, the AICPA merged with the American Society of Certified Public Accountants, which had been formed in 1921 to act as a federation of state societies. The merged organizations remain today as the AICPA. When the two organizations merged, it was decided that full membership in the AICPA should be restricted to CPAs.

The AICPA offers three different levels of membership, each having its own specific requirements. A full member must possess a valid and unrevoked CPA certificate, have passed the Uniform CPA examination, be employed by a firm enrolled in Institute-approved practice-monitoring programs, and agree to abide by the AICPA bylaws and its code of professional conduct (Code). Full membership also requires that individuals remain in public practice and complete a total of 120 hours of CPE during each 3-year reporting period, with a minimum of 20 hours completed each year. Associate membership is limited to those who have passed the CPA examination, but have not yet met their state's other licensing requirements (i.e., experience). Associate members, too, must agree to abide by the AICPA bylaws and its Code. Non-CPAs may belong to the AICPA as section associates provided they are employed by a CPA firm that participates in an Institute-approved practice-monitoring program. Section associates also must agree to abide by the AICPA bylaws and its Code.

The above membership requirements emphasize the prominent role of the AICPA's Code. The Code provides guidance and rules to AICPA members to assist them in performing their professional responsibilities and serving the public interest with honesty, integrity, and high moral standards.

The Code is divided into two major sections, the Principles and the Rules. The Code sets forth six principles—professional responsibilities, public interest, integrity, objectivity and independence, due care, and nature and scope of services. The rules govern the performance of professional services by AICPA members. Technical standards outline more detailed applications and interpretations of the rules. The AICPA bylaws require that members adhere to both the rules and standards.

Since state boards of accountancy, not the AICPA, issue licenses to CPAs, only those agencies have the authority to take actions affecting the status of the licenses issued by that state. Thus, compliance with the Code is left primarily to members' voluntary actions, secondarily to reinforcement by peers and public opinion, and ultimately on disciplinary proceedings brought by the Institute against those alleged to have violated the code. Enforcement is overseen by the AICPA's Professional Ethics division. Since the AICPA cannot affect the licenses of CPAs for violations of its Code, the bylaws of state and territorial CPA societies provide for the societies to participate in a Joint Ethics Enforcement Program so that actions taken by one or more of these societies or the AICPA are in the names of both the society and the AICPA.

When alleged violations of the Code come to the attention of the AICPA's Ethics division, the division investigates the matter under due process procedures. Depending on the facts found in the investigation, the Ethics division has the option to take a confidential disciplinary action, settle the matter with suspension or revocation of membership rights, or refer the matter to a panel of the Trial Board division for a hearing. The bylaws mandate publication of the member's name in *The CPA Letter* published and distributed to the membership of the AICPA if the member is found guilty or is suspended or expelled.

As the premier professional organization representing CPAs, the AICPA has sought to serve the interests of both its membership and the public for over 120 years. It is through its Code that the public interest is protected.

—Sharon Green and Robert J. Kollar

See also Accounting, Ethics of; Certified Public Accountants (CPAs); Codes of Conduct, Ethical and Professional; Professional Ethics; Public Interest

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American Management Association (AMA)

The American Management Association (AMA) is a global not-for-profit, membership-based association. It was on March 14, 1923, that the National Personnel Association changed its name to AMA on the ground that the members of the former association believed that the personnel manager should have complete and final authority in all matters concerning employees. AMA has an interesting descent in a line from various progenitors. In 1922, the National Personnel Association was formed by the merger of the National Association of Corporation Training and the Industrial Relations Association of America. The National Association of Corporation Training was founded in 1913 as the National Association of Corporation Schools, while the Industrial Relations Association of America was founded in 1918 as the National Association of Employment Managers. Soon after the AMA was founded, AMA merged with the National Association of Sales Managers in 1924 and acquired the International Management Association in 1957 to form the AMA International.

AMA had issued various kinds of monthly or periodical membership magazines including *Management Review.* This professional publication dealt with topical issues. Concerning business ethics and society, it featured articles on the changing social environment in the1970s and stakeholder negotiations. AMA formed its Supervisory Management Association and issued the booklet-sized membership magazine *Supervisory Management* in 1955. AMA founded its own publishing division AMACOM in the 1960s. AMACOM publishes numerous titles concerning management, business, and personal development and some guides to promote business ethics and ethical leadership.

AMA played a major role in investigating the lack of job opportunities for minorities and establishing equality at work places. Before the War, AMA researched the job opportunities for African American factory workers in 1942 and reported on a study on lack of opportunities for women in 1943. These studies and reports made an impression on corporate managers and the business community. During and after the War, AMA and its publishing departments worked on social security, minimum wages, collective bargaining, and fair trade problems. In the post-War economic reforms, AMA made its attitude clear by employing a catchphrase "Greater Productivity through Labor-Management Cooperation." As the post-War economic boom ended, the business community assigned AMA to play a role in the field of management education and ethics training programs.

Every year, AMA issues the Corporate Values Survey.

The mission statement of AMA is as follows: AMA provides managers and their organizations worldwide with the knowledge, skills, and tools they need to improve business performance, adapt to a changing workplace, and prosper in a complex and competitive business world. AMA encourages managers to continuously enhance their professional and personal development and increase their value to their organizations. In 2005, more than 3,000 organizations and 25,000 individuals in 89 countries are members of the AMA, and most of the Fortune 500 companies adopt AMA seminars and its training programs.

—Norihiro Mizumura

See also Equal Employment Opportunity; Ethics Training Programs

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American Medical Association (AMA)

The American Medical Association (AMA) is the largest and most influential organization representing medicine in the United States. The AMA was founded in 1847 with the aim of improving medical education and establishing a code of medical ethics (and thereby improving the status of the profession). Today, the AMA maintains those aims within its more general advocacy for the welfare of physicians and the health of the public.

The AMA is both a membership organization and an umbrella organization; that is, physicians can join as individuals (roughly a third of physicians do so), but the House of Delegates consists of representatives of specialty organizations (e.g., the American Academy of Pediatrics) and state medical societies (e.g., the Michigan State Medical Society). Each of these organizations has its own method of choosing delegates. The officers of the AMA itself (its president, board members, etc.) are elected by the House of Delegates. The duality of this structure creates certain internal conflicts: Funding comes from the dues of the individual physician members, but policy is made by the House of Delegates.

Five AMA councils advise the House of Delegates as well as produce authoritative statements on their own. They are the Council on Ethical and Judicial Affairs (CEJA), the Council on Long Range Planning and Development, the Council on Medical Education, the Council on Medical Service, and the Council on Science and Public Health.

The AMA publishes the highly respected *Journal of the American Medical Association* (founded 1883) and contributes to the publication of nine important *Archives* (not literally archives but peer-reviewed professional journals for particular specialties). They are the *Archives of Internal Medicine*, the *Archives of Neurology*, the *Archives of Ophthalmology*, the *Archives of General Psychiatry*, the *Archives of Pediatrics & Adolescent Medicine*, the *Archives of Dermatology*, the *Archives of Otolaryngology—Head & Neck Surgery*, and the *Archives of Facial Plastic Surgery.*

Members are offered various kinds of assistance in medical practice: They can, for instance, purchase a demographic analysis of areas where there are high numbers of potential patients. The AMA's "Physician Select" is an online database including virtually every licensed physician in the United States and its possessions; listings of AMA members offer considerably more information than listings of nonmembers. Osteopaths, the only other group of physicians recognized in the United States, are accepted as members of the AMA and are listed in the Physician Select database.

The code of ethics adopted in 1847 closely resembled Thomas Percival's 1803 *Code of Medical Ethics*, a document marking the move from vague oaths of honor to codified behavioral requirements. The AMA was the first national assembly of professionals to propose a code of conduct for all its members and the first to present it as an explicit social contract between the profession, its patients, and the general public. The original code has been revised several times; in the 1950s, there was an attempt to separate etiquette from ethics and in the 1970s, to separate law from ethics. Today's code includes, besides nine statements of basic principle, the opinions of the Council on Ethical and Judicial Affairs (CEJA). These address nearly 200 topics, ranging from the use of placebos through assisting a suicide, testifying in court, and patenting medical inventions. CEJA Reports, giving the rationale for these opinions, are available separately.

The AMA has been highly influential in the politics of health care. Its two aims—to promote the interests of physicians and the health of the general public—are often mutually reinforcing. Early efforts to improve and standardize physician education not only strengthened the social and economic status of doctors but also protected the public from quackery and fraud. Today, the AMA lobbies for reform of medical legal liability, and argues that protecting doctors would lessen incentives for them to leave practice or areas of practice. Similarly, the AMA lobbies for increasing the reimbursement for Medicare patients, arguing that this would encourage more physicians to accept such patients.

The two aims—physician well-being and patient welfare—can also conflict. When the Roosevelt administration proposed universal health care in the 1930s, the AMA opposed it; 30 years later, when Congress was considering Medicare, the AMA lobbied against it. Nevertheless, by 2001, the organization's rarely revised central "principles" were changed to include the idea that physicians should support access to medical care for all people.

In recent decades, the organization has been involved in several controversies. In the late 1990s, it entered into a contract with Sunbeam, allowing the manufacturer to use the AMA's logo in return for payment (as opposed to simply giving a seal of approval to all products that meet certain standards, as the American Dental Association does). The subsequent uproar led the AMA to break its contract with Sunbeam and draw up guidelines for interactions with industry. In the early years of the 21st century, a more complex controversy had arisen over the organization's acceptance of pharmaceutical industry funds in its campaign discouraging doctors from accepting gifts from that same industry.

Recent decades have also seen a number of progressive initiatives and programs. The AMA expressed early opposition to discrimination against HIV/AIDS patients. In 1986, it stopped investing in tobacco funds and encouraged medical schools and universities to do the same; in 1995, *JAMA* published a significant selection of previously secret documents from the tobacco industry (culled from the millions of pages made available through legal proceedings). Currently, the AMA is promoting healthy lifestyles and working to eliminate health disparities (particularly between races). In 1997, the AMA established its Institute of Ethics, a forum for grappling with emerging ethical issues such as those that arise from genetic science, the rise of managed care, and the growing influence of the pharmaceutical industry on drug trials. In response to the latter concern (which has included at times industry control over which results are published), the AMA has called for a comprehensive, publicly available database of clinical trials.

—*Judith Andre*

See also Professional Ethics

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Americans with Disabilities Act of 1990 (ADA)

The Americans with Disabilities Act (ADA) gives individuals with disabilities the same types of civil rights protections that are provided to individuals on the basis of race, sex, national origin, and religion. The ADA is modeled after the Rehabilitation Act of 1973, which applies to federal contractors and grantees. In contrast, the ADA applies to private employers (of 15 or more employees), state and local governments, employment agencies, and labor unions. Discrimination in all employment practices is prohibited (e.g., job application procedures, hiring, firing, promotion, compensation, training, etc.). The ADA also prohibits discrimination in public accommodation and requires transportation and communication systems to facilitate access for people with disabilities.

Since the act's passage in 1990, the courts have been working to define the meaning of its terms. The definition of the term *disability* was particularly problematic. In June 1998, the Supreme Court decided that the definition of "disability" included both major and minor impairments. Under this ruling, the definition of disability covers a wide range of conditions, such as HIV, cancer, dyslexia, and bad backs. However, this broad definition was later restricted in 2003, when the Equal Employment Opportunity Commission (EEOC) ruled that a condition only qualifies as a disability if it substantially limits a major life activity. As defined by the EEOC, these major life activities include seeing, hearing, speaking, walking, breathing, performing manual tasks, learning, caring for oneself, and working.

Not all people with disabilities are covered by the ADA. Individuals qualify for ADA protection only if they can perform the *essential functions* of the job. As with the term *disability*, the definition of essential function can be a challenge to pin down. One well-publicized case where this definition was particularly problematic involved professional golfer Casey Martin. Martin suffers from Klippel-Trenaunay-Weber syndrome, a degenerative circulatory disorder that obstructs the flow of blood from his right leg to his heart. Due to the severe pain caused by this progressive disease, Martin was physically incapable of walking an 18-hole golf course. Walking would not only cause him pain but also create a risk of significant injury. Martin applied to the PGA for permission to ride a cart in PGA tournaments while other players were walking the course. The PGA refused and Martin sought protection under the ADA. The core issue in question was whether walking the golf course was an essential function of playing professional golf. Eventually, the Supreme Court ruled in Martin's favor, deciding that he could use a cart because using the cart would not alter the game in any fundamental way. In other words, walking the court was deemed to not be an essential function of golf. When an individual qualifies for ADA protection (i.e., the disability impairs a major life activity but the individual is still able to perform the essential functions of the job), firms are expected to provide *reasonable accommodations* to the individual as long as the act of providing these accommodations does not present an *undue hardship* for the firm.

—*Ann Buchholtz*

See also Disability Discrimination; Employment Discrimination; Equal Employment Opportunity; Equal Opportunity; Rehabilitation Act of 1973

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AMORALITY

The term *amoral* is usually used to refer to decisions or persons that are said to be void of ethical values or removed from the moral realm. A decision is amoral if it is made without taking ethical factors into consideration. Persons are said to be amoral when they do not incorporate moral principles, concepts, or codes of conduct in their decisions, actions, or behaviors.

Usually, decisions that are said to be amoral are those decisions that are based on criteria that are believed not to include values such as justice, fairness, and equality. For example, a decision to close down a plant is said to be an amoral decision if it was made solely based on economic parameters. The well-being of the labor, employees, and communities attached to this plant are not included as decision criteria. Managers are regarded as amoral when they are guided by their concern for the economic performance of their companies while paying no attention to any social or human considerations. The phrase "business is business" embodies the essence of amorality. It implies that morality is not applicable in the domain of business.

Some scholars consider the notion of amorality to be a pure version of Adam Smith's perception of capitalistic behavior. The main idea is that common good is achieved by the pursuit of self-interest. Business decisions, practices, and activities are only concerned with the pursuit of profits, and no moral purpose is incorporated. This approach to business decisions, practices, and activities is sometimes referred to as the *theory of amorality*.

Two Types of Amorality

The amoral person may intentionally or unintentionally not subject decisions, actions, or behaviors to moral evaluation. Such a distinction led some scholars to identify two types of amoral persons—intentionally amoral and unintentionally amoral. The intentional amoral person consciously and deliberately chooses not to acknowledge ethical considerations in his or her deliberations. The unintentional moral person, on the other hand, does not subject his or her decisions, actions, or behaviors to moral evaluation due to carelessness or lack of sensitivity or knowledge.

A manager who holds that the realm of ethics and that of business are separate is an intentionally amoral person. He or she deliberately excludes ethical notions from the spheres of business. For example, an intentionally amoral manager may reject a proposal to expand an investigation of the effects of a new drug on patients that extends beyond the requirements of the Food and Drug Administration on the grounds that a concern for the implications on the well-being of patients beyond what is required by law is not within the scope of business. The sole criterion for evaluating proposals is their impact on the corporation's financial bottom line. On the other hand, an unintentionally amoral manager may include height as a selection criterion when hiring construction workers, for example, without considering the negative impact that this criterion would have on women and certain minorities. Women and some minorities may be systematically excluded from the hiring process due to their disadvantage on height when compared with average white males. In this example, the manager did not take the care to consider the moral implications of his or her decision criteria. He or she was thus unintentionally amoral.

Morality

To better appreciate a discussion of amorality, it is useful to understand the different contexts, approaches, and philosophies of morality.

Three Definitions of Morality

The term *morality* frequently is used in three different ways. First, morality may be used to refer to a set of beliefs that is held by an individual. Second, the term may be used to refer to a set of beliefs or a system of principles and judgments shared by a society, culture, or community. Third, the term may be used to refer to philosophical codes of behavior.

Three Philosophies of Morality

Three major philosophies of morality include moral absolutism, moral relativism, and moral skepticism. First, moral absolutism refers to the belief that right and wrong are determined by absolute standards. Individuals who believe in moral absolutism would hold that their set of beliefs is universal and appropriate for application globally. Managers who believe in moral absolutism would adhere to a certain code of conduct and be guided by it in whichever society or community they conduct business.

Second, moral relativism refers to the belief that right and wrong is different from one society to another. Individuals who believe in moral relativism would hold that right or wrong behaviors depend on the society or community in which the behavior occurs. Managers who believe in moral relativism are more likely to acknowledge the international context in which they conduct business.

Third, moral skepticism, which is closely related to moral nihilism, contends that moral statements are neither true nor false. Moral skepticism supports such a claim through doubting the possibility of moral knowledge, its justifications or logical arguments, and moral truth or facts. Moral skepticism may be regarded as the polar opposite to moral absolutism. While moral skeptics zealously support their position, opponents of moral skepticism assert that it is dangerous and absurd. It is useful to understand moral skepticism and compare it with amorality, because there are slight differences.

Amorality and Moral Skepticism

Amorality is different from moral skepticism. As previously stated, an amoral person is a person who does not subject his or her decisions, actions, or behaviors to moral evaluation. Moral skepticism, on the other hand, is the belief or ideology that asserts that moral statements are neither true nor false. Amorality does not correspond to moral skepticism. In the case of an amoral agent, not subjecting decisions, actions, or behaviors to moral evaluation does not necessarily mean that the agent doubts the truthfulness of moral statements. The agent, intentionally or unintentionally, just does not subject his or her decisions, actions, or behaviors to moral evaluation. In contrast, a moral skeptic, or nihilist, would refuse to even acknowledge moral evaluation of decisions, actions, or behaviors. He or she would challenge the truthfulness and philosophical basis of the moral statement itself.

An intentional amoral manager may develop a work schedule that does not provide accommodations for some minorities to observe certain religious holidays. The manager would defend his or her position arguing that the moral obligation to provide such accommodations should not have an effect on business decisions since such issues do not apply to business decision making. An unintentional amoral manager may also fail to provide such accommodations, but for a different reason. He or she may not have been careful enough to incorporate certain accommodation criteria in his or her decision-making process; he or she may have been just careless or inattentive to ethical facets. A moral nihilist, in contrast with the intentional and unintentional manager, would question the truthfulness of the obligation itself. The moral nihilist would argue that the statement "minorities '*should*' be accommodated to observe religious holidays" could neither be regarded as true or false.

Amorality, Consequentialism, and Deontology

Consequentialism is a moral concept that evaluates the rightness or wrongness of decisions, actions, and behaviors in light of their consequences. A decision, action, or behavior is deemed right, or ethical, if it results in favorable consequences. If the consequences are unfavorable, the decision, action, or behavior is deemed wrong, or unethical. Utilitarianism is one of the most widely known types of consequentialism. For example, according to one version of utilitarianism, broadening the scope of investigating the side effects of a new drug on patients beyond what is required by law would be justified and morally right if it would make the aggregate benefit to all concerned parties higher than it is in the absence of such an investigation. Note that the justification for building the day care facility is the conclusion that the aggregate welfare of all concerned parties is enhanced. The criterion for justification is the outcome, or consequence.

In contrast with consequential ethics, which considers the results of an action or decision in determining its appropriateness, deontological ethics is an approach that considers the nature of the action or decision itself in determining its ethics. Kantian ethics is a main strand of deontological ethics. According to

Kant, ethical evaluation is based on duty. It is one's duty that mandates certain actions and decisions, regardless of the outcomes. For example, a justification for broadening the research scope of investigating the side effects of a new drug on patients beyond what is required by law, discussed in the pervious example, would be justified based on the obligation that the company has toward its customers, not the conclusion that such an investigation would make all concerned parties better off. The consequences of this project have no bearing on the rightness and wrongness of the decision.

Some scholars argue that decisions that are usually referred to as amoral are in fact a restricted or limited form of consequentialism. Managers who only consider economic parameters are usually deemed amoral. However, since the decisions of the amoral agent rely on certain criteria and are aimed at achieving a certain outcome, then such an agent may be regarded as a consequentialist. Managers who base their decisions on economic parameters only aim at achieving a desired financial objective for their organizations and maximizing the wealth of their investors. For these managers the outcome matters. Consequences matter. The manager, in this case, did not lack a code of conduct. The manager was always aware of the appropriate behavior. For such a manager, the financial performance of the organization and the wealth maximization for investors were the guiding ethical notions. According to this view, a manager is considered to be amoral if he or she does not incorporate deontological notions of ethics in his or her moral evaluation and only adopts a limited version of consequentialism where the only evaluation criterion is shareholder wealth maximization.

Distinctions Between Amorality and Immorality

Amorality should not be confused with immorality. In contrast to an amoral person who does not incorporate moral considerations in his or her decisions, actions, or behaviors, an immoral person has a clearer sense of moral dimensions of his or her decisions, actions, or behaviors. This person is aware of the applicable codes of conduct. However, such codes of conduct are not followed. Consequently, the behavior of the amoral person is not influenced by any codes of conduct. The immoral person, on the other hand, acts in a manner that conflict with sound ethics. The immoral person elects to do wrong and is aware of it and acknowledges his or her wrongdoing, even if only admitted to himself or herself.

In contrast to the two types of amorality—intentional and unintentional—according to Ronald D. Milo, Aristotle depicted two types of immoral behavior—wickedness and moral weakness. A wicked person deliberately acts in an immoral way. A wicked person prefers to act in the way he or she does by committing a wrongdoing. In contrast, a morally weak person is overpowered by external forces and circumstances that he or she cannot resist. The morally weak person prefers not to act in an immoral manner, but he or she ends up committing a wrongdoing. Moral weakness results from a weak will, not from ill intentions or motives.

Amorality in Business Ethics Literature

In business ethics literature, the term *amoral manager* refers to a manager who does not subject his or her decisions, actions, or behaviors to moral evaluation. The term *amoral decision* refers to decisions that do not incorporate ethical factors or standards into the decision-making criteria. The following are two examples of how the notion of amorality has been used in business literature.

Models of Management Morality

Archie B. Carroll proposed three models of management morality—moral, immoral, and amoral. First, moral managers are those managers who incorporate ethical values into their decisions, actions, and behaviors. They follow ethical principles or an ethical code of conduct. They believe that ethics applies to business and business practices. The operational strategy of moral managers is to maximize shareholders' wealth through appropriate means and within the bounds of ethics. For example, a moral manager would consider the social and moral implications of the contents of a computer or video game when marketing such a product. He or she will market it to the appropriate customer segment with the appropriate rating.

Second, immoral managers knowingly violate ethical codes of conduct, usually in pursuit of their self-interest at the expense of others. The operational strategy of immoral managers is maximizing shareholders' wealth through any possible means. For example, the concern of an immoral manager would be to maximize profits from marketing a computer or video game even if the content would have a negative social or moral impact on the target market, which, in this case, are usually children.

Third, in contrast to moral and immoral managers, amoral managers are those managers who do not subject their decisions, actions, or behaviors to moral judgment. Their decisions, actions, and behaviors are void of moral content. Amoral managers may be intentionally or unintentionally amoral. For example, an amoral manager would not incorporate the social or moral impact of the content of a computer or video game on the customers. To the intentionally amoral manager, such considerations are irrelevant to business decision making. To the unintentionally amoral manager, such considerations are excluded due to carelessness, inattentiveness, or lack of ethical perception.

Carroll also proposed two hypotheses regarding the three models of moral management. The first, the population hypothesis, suggests that the majority of managers are amoral. The second, the individual hypothesis, suggests that the majority of the decisions made by an individual manager are amoral. Carroll's hypotheses suggest that the amoral model of management is the dominant model of management morality. The amoral model of management seems to best describe the moral status of professional managers.

Value Neglect and Value Attunement

Consistent with Carroll's models of moral management, yet investigating decision making in corporate social policy, Diane L. Swanson proposed two ideal types of the decision-making process—value neglect and value attuned. First, in the value neglect ideal type of decision making, the decision maker is one who perceives that values are irrelevant to the decision-making process. Normative myopia characterizes the policy formulation process. The resulting corporate social responsiveness is of the "value neglect" ideal type.

Second, in the value attuned type of decision making, the influence of personally held ethical values on the decision-making process is acknowledged. Normative receptivity characterizes the policy formulation process. The resulting corporate social responsiveness is of the "value attunement" ideal type.

The value neglect type of decision making proposed by Swanson is similar to the notion of amoral decision making. The value attunement ideal type of decision making is similar to the notion of moral decision making.

—Kareem M. Shabana

See also Ethical Nihilism; Ethics, Theories of; Kantian Ethics; Moral Principle; Moral Reasoning

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Anarchism

Anarchism is the doctrine or theory that the state is immoral and unjustified and that society may flourish without any coercive governmental institutions. Anarchism (from the Greek *an archos*, without a ruler) is not a synonym for chaos or violence but a critique of the state and a theory of how voluntary interaction and organization allows individuals to flourish freely. As a philosophy, anarchism has arisen in the modern period, though one may discern anarchistic suggestions in the ancient Greek Stoic Zeno of Citium (fourth to third century BCE) and in the ancient Chinese philosopher Lao Tse (sixth century BCE). There is no single anarchist doctrine, and many anarchists have been antitheoretical, but all anarchists agree on the illegitimacy of the state and emphasize the importance of liberty and autonomy or the significance of equality and solidarity.

Kinds of Anarchism

Anarchists make two types of claims: that the state is illegitimate and that a society without the state is preferable to the alternative. The anarchist typically contends that the state is intrinsically coercive and, therefore, unjust. (Some anarchists, such as Mikhail Bakunin, have accepted the state as necessary in some historical circumstances.) The injustice of the state is explained in terms of how the state transgresses liberty or autonomy, violates rights, or exploits one group or class against another. Others (such as the contemporary economist David Friedman) have argued that the state is immoral on broadly consequentialist grounds: All things considered, anarchy is preferable to government. The anarchist critique of the state is sometimes coupled with attacks on justifications of the state, including the theory of the social contract or the contention that public goods cannot exist without the state. Against the social contract, anarchists remark that almost all states have arisen through acts of violence or conquest. Against the public goods argument, it is pointed out that there may be fewer such goods than commonly claimed and that the public goods that the state arrogates to itself could be generated (if not improved!) through voluntary activities.

One might distinguish two broad classes of anarchists—those on the left and those on the right. Left anarchists have argued for communally based forms of society (socialist or communist anarchists) or for federations of worker-owned firms (anarcho-syndicalists); more recent types of left anarchists include ecological anarchists. Left anarchists emphasize equality and solidarity and seek to overcome not only the coercion of the state but also other forms of domination that may occur between rich and poor, employer and employee, and so on. By eliminating or diminishing the property relations and other unequal social structures created and enforced by the state, individuals will realize their humanity and antisocial behavior will diminish. On the right are individualist anarchists, including market anarchists or anarcho-capitalists, who contend that private property allows for freedom, individual flourishing, and pluralism. The anarcho-capitalist maintains that the protective functions now assumed by the state can be provided by private firms competing to sell both security and adjudication services.

From the perspective of either the left or the right, the anarchist argument runs counter to Thomas Hobbes's well-known argument that a state of nature (anarchy) would be so horrible that all would agree to institute an absolute sovereign. Hobbes's account suggests that without the state certain public goods (indivisible goods from which nonpayers cannot be excluded) would not come into existence. Under conditions of anarchy, even if individuals desire these goods (e.g., security), no one has an incentive to provide them. However, if anarchists are correct, voluntary cooperation is possible. For example, left anarchists suggest that human nature is not, in fact, as corrupt as it has become under the conditions of state capitalism. And individualist anarchists maintain, following the conclusions of game theory, that iterated interactions among individuals provide incentives for cooperation. In this way, so-called public goods could be provided by voluntary contract; for example, private security firms could compete peacefully to provide protective services and adjudication.

Brief History of Anarchism

Some of the earliest instances of anarchist thought are to be found in the work of Étienne de la Boétie in *The Politics of Obedience: The Discourse of Voluntary Servitude*, 1577. However, William Godwin is often taken as the first systematic architect of modern anarchism in *An Enquiry Concerning the Political Justice*, 1793. For him, the object of humankind, happiness, is achieved best without the state generating injustice, violence, and inequality. The thought of Pierre-Joseph Proudhon, the first to use the term *anarchism*, proved more influential than that of Godwin. In his 1840 work *What Is Property?* Proudhon distinguishes illegitimate forms of property (receiving state sanction) from possessions (land or goods) that should be equally available to all. Rejecting revolution and communism, he argues for "mutualism," under which credit banks would lend money without interest.

Mikhail Bakunin was the first to articulate a theory to appeal to large masses of workers, influencing thereby the emergence of anarcho-syndicalism, such as that developed in Spain well into the 20th century. Bakunin's works, including *Statism and Anarchism*, 1873, offer an atheistic anarchism according to which the overthrow of the state will allow for federations of workers' associations. The goal is the moral and material development of each individual's humanity through collective labor.

Unlike Bakunin, who maintained that reward should accord with labor, anarcho-communists, such as Peter Kropkotin, author of *Fields, Factories and Workshops*, 1899, sought the Marxist goal of rewarding each according to need. For Kropotkin, each individual should live an integrated life that includes the work of the field and that of industry. Leo Tolstoy, like Kropotkin, also maintained that the distribution of goods should correspond to need, but Tolstoy based his anarchist philosophy of nonviolence and nonresistance on Christian ideals in *The Kingdom of God Is Within You*, 1894.

In more recent times, left anarchists have included the linguist Noam Chomsky and Murray Bookchin, author of *The Philosophy of Social Ecology*, 1994, and a former communist who turned to anarchism and then adopted a communalist outlook. Against both capitalism and private property, he has sought to decentralize society, so that the locus of governance is at the level of the municipality. There, individuals would meet face to face and in democratic assembly, neither dominating others or nature itself.

Among 19th-century anarchists, there were also thinkers of a decidedly individualist outlook. For example, Max Stirner argued, in *The Ego and His Own*, 1845, for individual egoism and against the state. More prescient is the Belgian economist Gustave de Molinari, who, in *The Production of Security*, 1849, anticipates the arguments of recent anarcho-capitalists that the state should have no monopoly on the provision of security. The classical liberal Herbert Spencer developed a natural rights defense of equal freedom and drew an important distinction between a militant (compulsory and warlike) and an industrial (voluntary and peaceful) society. He influenced several thinkers, including Auberon Herbert, who argued in *The Right and Wrong of Compulsion by the State*, 1885, that state functions must be supported voluntarily.

One of the first of the American anarchists was Josiah Warren. Impressed by Proudhon's mutualism, Warren also defended the idea of self-ownership. In turn, he influenced Benjamin Tucker, who published, from 1881 to 1908, a journal, *Liberty*, devoted to anarchism. Espousing an individualist form of anarchism, bearing the influence of Spencer, Tucker distinguished between violence in self-defense and that initiated against another person. Associated with Tucker's journal was Lysander Spooner, a strong abolitionist and advocate of natural rights, including those of property. In a series of robust essays, *No Treason*, published after the Civil War, he argued that he could not be bound to a constitution that he had not signed.

Among the individualist anarchists of the past 30 years, the most provocative and prolific has been Murray N. Rothbard. An economist of the Austrian School and an anarcho-capitalist, Rothbard contends that individuals have natural rights to life, liberty, and justly acquired property. Such rights entail that one ought to be free of the threat or initiation of force, whether wielded by bandits or agents of the state. Not only is taxation an illegitimate use of force but so is the government's monopoly on security. In anarchy, private protective agencies could provide systems of law and adjudication; other needed services (e.g., roads) could be provided through private firms competing in a market governed by private legal norms.

Problems and Prospects

There exist a variety of objections to anarchism. In a real sense, however, any political theory that attempts to justify allegiance to the state serves as an argument against anarchism. Thus, the classic social contract theory of Hobbes, or that of John Locke, seeks to show why individuals would seek to live in societies governed by a state. More recently, Robert Nozick has sought to explain how, in an anarchy governed by Lockean natural rights and featuring competing protection agencies, a state could emerge without violating anyone's rights.

Criticisms such as these may suggest that the topic of anarchism is far removed from the ethical considerations of markets and commerce. However, there are several anarchist considerations to which business ethicists might attend. Although anarchy typically refers to a whole society functioning without a state apparatus, it may also describe processes at smaller levels. And at this dimension, or at the societal level, business ethicists might consider whether there are self-regulating processes available for ameliorating or solving problems. Second, some business ethicists assume the coherence and strength of a notion of a social contract, but anarchists consistently argue that there is no contract without the consent of each individual. Third, the possibility of the provision of private law and private security raises interesting, albeit hypothetical, questions about the ethics of restitution, as well as the business ethics of private punishment and the nature of impartial arbitration and mediation. Finally, many anarchists speak eloquently of the way in which the apparatus of the state may be taken over by a particular faction or class. When this occurs, the state is no longer a neutral instrument but a blunt one wielded less for the public good than for the interests of a group. State policies and regulations that aim, ostensibly, at some public good may, in fact, serve private interests, including the interests of those whose livelihood depends directly on the state rather than on interactions in society or market.

—F. Eugene Heath

See also Austrian School of Economics; Hobbes, Thomas; Libertarianism; Locke, John; Marxism; Nozick, Robert; Public Goods; Self-Ownership; Self-Regulation; Spontaneous Order; Statism

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Animal Rights

Businesses use animals in numerous ways. The fish and meat on the table for dinner come from farms, fish markets, and butchers. Many items of clothing are from the leather industry, the animal dye industry, and the fur trade. Circuses, zoos, and trained-animal fights (such as cockfights) are parts of the entertainment industry. Many cosmetics have been safety tested on animals, and the pharmaceutical and chemical industries each year expend millions of research dollars on millions of animals used in toxicological studies.

Many businesses have internal review committees established, at least in part, to protect the interests of research animals. Their charge is to see that prevailing policies intended to protect animals are properly implemented and that pain and suffering are minimized. Many corporations in the pharmaceutical, chemical, and cosmetics industries have such committees, often with veterinarians and other experts on animals involved in deliberations. However, committees in these industries may intentionally allow a high level of harmful activity, such as the acute toxicity test (increasing doses until animal welfare is seriously compromised). Other industries—such as circuses, slaughter houses, and farms—generally do not use ethics committees for purposes of reviewing their practices (though these industries are regulated by governments in some uses of animals). Concerns in these industries center more on having healthy animals, a pragmatic rather than moral concern.

Differences in the review of uses of animals derives in part from tradition and in part from diverse conceptions of when animals have interests that must, from a moral point of view, be protected.

Do Animals Have Rights?

Animal rights is a generic term that refers to a wide range of accounts of how animals should be protected against human misuse. The language of *rights* derives historically from the need for strong and meaningful protections of citizens in political states against oppression, unequal treatment, intolerance, and the like. Given this history, many framers of declarations about protections for animals chose rights language as the basic terminology. Others interested in animal welfare intentionally do not use the language of rights.

Although the term *animal rights movement* is broadly used, social movements to protect animal interests divide roughly into two (or, when the two are combined, three) different types or approaches: (1) those who believe that animals have rights (animal rightists) and (2) those who believe that animals do not have rights but that humans have obligations to protect the welfare interests of animals (animal welfarists).

A third position situated between these two approaches holds that rights and obligations are correlative, and therefore, whenever an animal has a right some human has an obligation and whenever a human has an obligation to an animal, the animal has a right. Thus, if a farmer has obligations to feed his cattle and abstain from using painful electrical prods, then the cattle have rights to be fed and not to have the pain inflicted.

Animal rightists generally endorse strong positions on rights, for example, declaring that certain animals have a right to life, a right to an uncontaminated habitat, a right not to be constrained in tight cages or pens, and comparable rights. "Rights" are here understood as justified claims that individual animals or groups of animals have and that are binding on human agents and societies. If an individual or group possesses a right, others are validly constrained from interfering with the exercise of that right. A right, then, is a justified claim or entitlement. The position that *animals* have such rights has been regarded by many critics as an inappropriate and innovative doctrine, and some even view it as a radical, revolutionary doctrine. Nonetheless, the view that animals have rights has come to be one of the most important ideas in the literature on animals and human responsibilities for them.

Animal welfarists, in contrast to animal rightists, tend to have more utilitarian and pragmatic perspectives. They acknowledge that humans have a duty not to cause animals avoidable harm, but animal welfarists are generally prepared to use animals for human benefit. Many utilitarians, for example, regard the idea of rights as undercutting the risk-benefit calculus at the heart of utilitarian reasoning. Many animal welfarists accept the view that some level of suffering may be necessary to produce food for humans, to produce products such as leather goods, to use animals to test for the safety of cosmetic products, and even to use animals in chemical and pharmaceutical testing.

Many writers on human uses of animals reject both the animal rightist and the animal welfarist positions. They take human obligations to animals to be either self-imposed obligations or obligations owed only to the owners of animals. The so-called rights of animals are not truly rights; they are ways of restating various provisions that have been or could be made by humans for the protection of animals. Since claiming a right occurs only within a community of moral agents authorized to make such claims, rights and real obligations appear only in human communities. A more appropriate vocabulary than rights, from this perspective, is *charity*, *stewardship*, and *moral ideal.* In this conception, even the idea of obligations of beneficence toward animals should be stated in terms of kindness, compassion, and generosity.

Moral Status

The major issue in moral philosophy about animals and their rights is that of *moral status* (or moral standing). To have moral status is to deserve the protections afforded by the basic norms of morality. The starting question about moral status is "Which individuals and groups are entitled to the protections afforded by morality?" Throughout much of human history, certain groups of human beings (e.g., racial groupings, tribes, or enemies in war) and effectively all nonhuman animals have been treated as less than persons, as not being able to act morally, or as not members of the moral community. The assumption has been that these groups either have no moral status whatever or at least have a considerably reduced moral status.

If animals have no place in the moral community—no moral status—then it appears that humans owe nothing to animals and can do with animals as they wish. On one such account, we owe obligations to the humans who own animals but not to the animals owned. Thus, if a man poisons all the cattle on a dairy farm, he violates a moral obligation to not destroy the owner's cattle, but the man does not violate any obligation to the cattle. The property owner is injured by the action; the cattle that are killed are not wronged.

Many people find this conclusion deeply counterintuitive, and some judge it false and offensive. Others think these questions are difficult to judge because they are at the outer boundaries of proper moral concern. For example, they are like questions about moral obligations to future generations of humans and obligations to the environment. Such questions are at the frontiers of ethics.

To sort through these issues requires examining several underlying issues about the nature of animals and about their moral status. The mainstream approach to the question of what *kind of entity* merits moral protection has been to ask which *properties* of the entity qualify it for moral protection. Some say that there is one and only one property that confers moral status. For example, some say that this property is human dignity—a very unclear notion that moral theory has done little to clarify. Others say that another property or perhaps several properties are required for acquiring moral status—for example, sentience, rationality, or moral agency. Each such property has been developed as a general theory of moral status. The leading theories have turned on (1) distinctively human properties or (2) properties of sentience and other psychological properties such as emotions. Each type theory of moral status now has a considerable body of supporting literature.

The first type of theory, based on distinctively human properties, has long been attractive, because these theories supposedly distinguish humans in the relevant ways from animals and justify the ways in which we traditionally allow human interests to rank higher, have more value, and count for more whenever they are in conflict with the interests of animals. Much of the recent discussion about moral status has centered on the criteria for being a *person*, under the assumption that all and only persons have the relevant distinctive properties for which we are looking.

Most theories of this sort do not restrict themselves to mere human biological criteria and species criteria. The theories tend to telescope to certain *cognitive* properties ("cognition" here refers to processes of awareness and knowledge, such as perception, memory, thinking, and linguistic ability). The thesis is that individuals have moral status because they are able to reflect on their lives through their cognitive capacities and are self-determined by their beliefs in ways that nonhuman animals seem not to be. Properties found in various theories of this first type include (1) self-consciousness (consciousness of oneself as existing over time, with a past and future), (2) freedom to act and capacity to engage in purposive sequences of actions, (3) having reasons for action and the ability to appreciate reasons for acting, (4) capacity to communicate with other persons using a language, and (5) rationality and higher-order volition. Any entity having such higher-level properties has moral status, which confers moral rights.

However, cognitive properties may in the end not confer moral status only on humans. Many writers believe that capacities such as intention, understanding, desire, preferences, suffering, free action, having systems of communication, and having beliefs are not distinctively human, because many animals exhibit significant levels of these capacities. In addition, critics of theories based on the idea of distinctively human properties argue that some creatures deserve moral status even if they do not possess a single *cognitive* capacity. They argue that a *noncognitive* property may be sufficient to confer some measure of moral standing. This opens the way to a second type of theory.

In the second approach, properties that are not cognitive are highlighted. The most frequently invoked properties are those of sensation—especially pain and suffering—but also mentioned are properties of emotion—especially those associated with fear and suffering. As Jeremy Bentham pointed out long ago, the capacity to feel pain might by itself be sufficient for conferring a significant moral status. The emotional lives of animals have long been avoided in scientific literature, where attributions of emotion, intention, and the like have been criticized as an unscientific abandonment of critical standards and precise measurements, as well as an importing of anthropomorpism. Yet many good reasons exist for attributing a range of emotions to animals, and the basis of belief in their emotional life is as good as we have for the attribution of pain and suffering.

Animal Minds

At the root of many of the issues addressed thus far is a rich body of theoretical issues not only about moral status but also about animal minds. Most observers of animal behavior today agree that many animals have capacities to understand and have developed complicated, sometimes elaborate forms of social interaction and communication (whether these qualify as "linguistic" is controversial). Intelligence and adaptation in animal behavior, as explored by ethologists and psychologists, is often inexplicable without acknowledging that animals exhibit understanding, intention, thought, imaginativeness, and various forms of communication. Certain facts of *mental* life in animals do not seem any more in doubt than facts about *physical* processes in these creatures.

Little agreement exists, however, about the levels and types of mental activity in these animals or about the ethical significance of their mental activity. Humans understand very little about the inner lives of animals, or even about how to connect many forms of observable behavior with other forms of behavior. Even the best scientists and the closest observers have difficulty understanding *intention* and *emotion* in animals. Forms of communication in animal communities have proved extremely difficult to grasp. Neither evolutionary descent nor the physical and functional organization of an animal system (the conditions responsible for its having a mental life) gives us the depth of insight we would like to have in understanding the animal's mental states. Even when we have as full an explanation as can be obtained, we still have to decide about an animal, as with a brain-damaged human, whether the individual truly has certain attributed mental states or is just acting *as if* he or she had such states. The more we are in doubt about an animal's mental life, the more we may be in doubt about moral status and issues of rights.

The Problem of Species Preference

Speciesism is a widely discussed term in discussions of animal rights. A speciesist is one who believes that the interests of members of the species *Homo sapiens* are to be favored over the interests of other species. Species membership, therefore, determines whether a creature has moral status.

The term *speciesism* is often used pejoratively by analogy to racism and sexism; in this usage, speciesism is understood as an *improper* failure to respect the lives and rights of animals. Just as gender, race, IQ, accent, national origin, and social status are not relevant properties in moral assessments of humans, neither is species relevant to assessing an animal's moral entitlements. "To each according to species" seems as morally irrelevant and unfair as "to each according to one's skin color." However, speciesism need not be understood in such a pejorative manner. Some speciesists willingly and even enthusiastically accept the label if it is used only to mean placing a moral priority on members of the human species.

In the practical world of how animals should be treated in business and commerce, speciesism may be the major topic that needs to be addressed. The strong human bonds of species preference often override all other considerations. But even if such partiality comes naturally, is this as it should be?

—Tom L. Beauchamp

See also Animal Rights Movement; Darwinism and Ethics; Deep Ecology; Environmental Ethics; Environmentalism; Environmental Protection Legislation and Regulation; Factory Farming; Moral Standing; People for the Ethical Treatment of Animals (PETA); Rights, Theories of; Speciesism; Utilitarianism

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Animal Rights Movement

The animal rights movement is a political movement that ascribes to nonhuman animals some of the same protections that many people recognize as belonging to all humans. It has taken two main tracks. First, there have been diverse activists whose conduct runs the spectrum from those who have made personal choices about animals and have become vegetarian, for example, to those who are much more radical and engage in various public acts of social disruption, upheaval, and, in some cases, even extreme violence. These individuals find grave fault with the way humans treat animals in contexts such as factory farming and agribusiness, the entertainment industry, and in medical experimentation and seek to change practices in these areas. However, this movement also can be depicted as a scholarly and more academic endeavor that has been led by a number of prominent applied ethicists among other concerned individuals. Together the intellectual and activist movements form the backbone of the animal rights movement. And, it should be said, there has not always been a positive reaction to this movement as many see the idea of ascribing rights to animals as wrongheaded and, for some, just plain silly.

The goals of the animal rights movement vary from activist to activist, and not all ethicists who advance the intellectual claims of animal rights agree on a common set of purposes, but there are some positions that present recurring themes. First, the theme of reducing, if not eliminating entirely, the suffering of animals is a position that many advocate. Whether this pain comes at the hand of intentional cruelty or arises from the treatment many animals receive in the commercial sectors of factory farming and agribusiness, suffering is often pointed to as abridging the rights of animals. Second, the issue of the morality of using animals in medical and other forms of experimentation is one that is in the forefront of the movement. Is animal experimentation a form of inhumane exploitation of them, especially if it leads to a reduction in disease for humans and animals?

Third, the issue of using animals for entertainment in venues such as small and confining zoos, circuses, rodeos, and traveling carnivals also present concerns for many advocates. They are especially troubled by the usually poor and degrading treatment that animals receive in such entertainment facilities and there are often news items of petting zoos that report cruelty to animals. Likewise, staged animal fighting and bullfights are highlighted as unacceptable forms of entertainment. Finally, many animal rights advocates seek an end to the hunting and trapping of wild animals where, they say, human pleasure is had through animal pain and suffering. The hotly debated U.K. controversy over the "blood sport" of fox hunting with hounds, which was banned in 2004, is a good case in point.

Animal Rights Activists

On the activist front, any number and variety of groups and organizations can be identified. There is a spectrum of these concerned citizens, and they can be categorized according to the kinds of activities in which they engage. For example, there is the well-known American Society for the Prevention of Cruelty to Animals, founded in 1866. This organization is best known for its support of animal shelters and programs that encourage the humane treatment of animals. The Humane Society of the United States also promotes animal rescue and shelters.

Then there are groups that engage in more direct political action. One such organization is People for the Ethical Treatment of Animals, or "PETA" as it is widely known. With a membership of over 800,000, PETA has staged publicity stunts and supported celebrities urging the public to recognize that animals have certain rights that have been denied to them. One tactic that PETA has used was throwing buckets of red paint on furs in expensive furriers, making the point that minks, sables, and foxes had given their blood so that humans might wear their skins as coats. Other advocates in the movement—variously called "animal liberationists," "animal welfare militants," and "animal terrorists"—have made something of a name for themselves as they engage in the destruction of property to make their case. For example, the Animal Liberation Front (ALF), started in Great Britain in the mid-1970s, has accepted responsibility for much damage to public and private property. In congressional testimony in 2002, the Federal Bureau of Investigation proclaimed ALF, along with the environmental militant group Earth Liberation Front (ELF), a domestic terrorist group.

ALF has taken aim at fur companies, animal farms, restaurants, and animal research laboratories as targets for their illegal direct actions that include raids in which animals are released from their confines and set free. However, the most destructive direct action that ALF has engaged in is arson. Estimates are that this group alone is responsible for losses to commercial and medical research facilities in excess of \$45 million. Adding in the destruction done by environmental militants, the total cost of damages has been placed at more than \$110 million for the decade ending in 2005.

The driving force and major motivation that seems to stand behind these sorts of radical tactics is that the activists are protesting some fairly cruel and unusual treatment of animals in various contexts, but especially their treatment in animal experimentation. Here, the claim is that not only will animals suffer great pain from the actual experiments that they are being used in but that the conditions under which they are kept during the experimentation are inhumane. The unnecessary punishment inflicted on research animals including beatings, inducing fear, cramped living conditions, poor nutrition, and so on has been documented. It is just this sort of inhumane treatment that has prompted radical animal rights activists to engage in the kind of direct actions that get them newspaper headlines. The radicals are also motivated by the mistreatment of animals in agriculture, where they say factory farming creates great pain for all kinds of farm animal. Many other uses and abuses of animals also come under their fire such as sport hunting, especially trapping and "canned hunts" where large and small game is kept within the confines of an "animal preserve" and hunters have an easy time in finding and shooting them.

In Europe, radical antivivisection groups have also formed adding fuel to the animal rights campaign and making it a worldwide phenomenon. In 1999, Stop Huntingdon Animal Cruelty (SHAC) was set up in the United Kingdom with the express goal of closing down Huntingdon Life Sciences (HLS), Europe's largest animal testing laboratory. HLS uses all kinds of animals in its tests of drugs, pesticides, household cleaners, and other substances. SHAC was established after a covert video, taken by PETA revealing much animal cruelty at an HLS facility, was shown on British television. SHAC has used various tactics of direct action against HLS, including the harassment of managers and employees, their families, and any companies that do business with HLS. Even though SHAC openly disavows physical harm to people, in 2001, three men wielding pickax handles and spraying CS gas attacked the HLS managing director.

The SHAC campaign against HLS has gone international as the firm itself grew with clients from around the world. It now has a research facility in the United States and boasts resources from three continents. Protests by SHAC have taken place in numerous countries where HLS clients have their home base. In 2005, SHAC saw success in the United States when the New York Stock Exchange (NYSE) postponed a listing of HLS on the market. The decision to delay a listing for the company came in the wake of a massive e-mail campaign directed at the NYSE. If they are not listed, then the ability of HLS to raise capital will be severely hampered. At the time, HLS was only being traded on a NASDAQ over-the-counter bulletin board as "Life Sciences Research."

In reaction to the radical tactics of some activists and to the general idea that animals actually should be considered as having rights, there has been a backlash of those who hold that the animal rights movement is a misguided one. For example, in the area of animals and medical experimentation, the Foundation for Biomedical Research has been advocating what it calls the humane and responsible use of animals in medical and scientific research. This group tries to expose the radical practices of ELF and SHAC and paint them as primarily criminal acts. It offers the public arguments to demonstrate what it sees as the major benefits to both humans and animals when medical experimentation includes the use of animals but without any mistreatment in the conduct of the research.

Intellectuals and Animal Rights

While it may be thought that the animal rights movement is purely a contemporary one, there are actually a number of well-known thinkers throughout history who have promoted rights for animals or at least for changes in the way that humans treat them. Among the major forerunners of the contemporary movement, Jeremy Bentham (1748–1842) should be mentioned. Bentham, who is recognized as one of the founders of utilitarianism in ethics, also offered an argument for animal rights based on the notion of sentience. This view holds that since animals are aware of their own suffering, they deserve the right to be free from it. For Bentham, it is not a matter that animals can't talk or can't reason; for him the point was that they can and do suffer.

In the 19th century, the German philosopher Arthur Schopenhauer (1788–1860), an antivivisectionist who criticized Christianity for leaving animals out of moral consideration, based his philosophy of animal rights on "universal compassion." He held that even though animals are less rational, they have the same "essence" as humans and as such they deserve our respect. Schopenhauer was likewise critical of the position of the philosopher Immanuel Kant on animals and morality, as Kant had argued that we have no moral duties to animals because they lack reason and only beings that can reason deserve respect. The philosopher René Descartes had gone even further in his understanding of animals when he said that they were akin to machines and so could not be the sort of entities about which we could even say that they possessed rights.

The question of the moral standing of animals has been a central concern for those who have pondered about animal rights. For many, though, the moral significance of animals is essentially a nonissue since they see animals as having only instrumental value for humans. In this strong anthropocentric view, where only humans are considered as morally significant, animals have only one purpose—to serve the ends of humans. In some accounts, the Bible is pointed to as giving man dominion over the world including its flora and fauna, and humans have the responsibility to shepherd the animals of the world to fulfill human need. Yet others see animals as personal property, and their instrumentality as pets or as farm animals providing food for humans becomes paramount. In either case, the view that animals have only an instrumental value will serve as an obstacle to any granting of bona fide rights to them. What is required is widespread recognition that animals have an intrinsic or inherent value, if they are to become rights bearers. Hence, much of the intellectual effort of the animal rights movement has been spent on the construction of arguments that attempt to establish the intrinsic value of animals.

This issue has been taken up notably in the writings of well-known applied ethicists Tom Regan and Peter Singer. Such ethicists argue that animals have bona fide rights that are sacrosanct because animals have equal or near equal moral standing to humans. To hold otherwise, they further claim, is to engage in the discriminatory practice of "speciesism." Like racism and sexism, speciesism is unacceptable because it is based on an unfounded bias. This is the prejudice of "anthropocentrism." If it is wrong to discriminate on the basis of the traits of race and gender because these traits differ from those of the discriminator, so too it would be wrong to use species as such a discriminating trait according to this view.

Peter Singer's arguments are based on utilitarianism. This position claims that animals, like humans, have certain preferences and interests that should be taken as morally considerable when we make decisions about how they should be treated. Animals have an interest in avoiding pain and in continuing their existence, argues Singer, and these interests deserve to be given equal considerations to those of humans. So, for Singer, when humans eat animals, experiment on them, and perform acts of animal cruelty in agribusiness, they do not give equal consideration to the interests that animals are said to have, thereby making these behaviors morally objectionable and questionable.

Tom Regan's position differs from Singer in that he holds a "direct duty" view of animal rights. His argument is that any being that can be seen as a "subject of a life," like human beings, should never be treated as a means toward an end. Since animals too are "subjects of a life," since they have complex subjective experiences, they have intrinsic value like humans and not mere instrumental value. If it is the case that animals have intrinsic value, then they have a right to be considered as members of a moral community (as moral patients, not as moral agents that require a higher level of rationality) in which duties and respect are owed to them. For Regan, acts such as breeding animals for food, using them for entertainment, and hunting and trapping them would violate the direct duties that members of the moral community have to one another, and these acts should be held as condemnable, immoral acts.

One proviso should be mentioned here, namely, that both Singer and Regan do draw a line that circumscribes the moral standing of animals. In other words, neither intellectual hands out rights to animals in carte blanche manner. According to Singer, animals that are sentient—feel and be self-conscious—or that have a central nervous system should be seen as having rights, while for Regan the line is drawn down to adult mammals. Only these animals are truly subjects of a life, and therefore others not in possession of the defining moral traits do not have the same moral standing and need not be considered as equally partaking of intrinsic value.

The Dilemma of Animal Rights

There are any number of values that drive people to advocate for animal rights: compassion, aesthetic appreciation, the belief that all life is sacred and interconnected, the knowledge that many animal species are endangered and may become extinct, and so on. This latter item has led to controversial laws in many countries that protect vanishing species and promote biodiversity by regulating human activities that might affect the preservation of the species so endangered. In one sense, animals are given certain rights by laws such as the U.S. Endangered Species Act, which has caused much controversy in its enforcement as the interests of commerce have come into conflict with the interests of the animals that the law is designed to promote. The case of the logging industry and the preservation of the spotted owl in the Pacific Northwest is a classic example of these human-animal controversies.

However, legal protections for animals have led to difficult dilemmas and not just controversy. The most recent is that of the overpopulation of elephants in certain sections of Africa that require authorities to make hard choices deciding the fate of a number of the world's largest living land mammals. As many wildlife parks dwindled in size, their carrying capacity for large numbers of elephants has likewise diminished even while elephant populations increased. For example, in Kenya, where poaching was rampant, the 1973 elephant population was around 167,000 but fell dramatically to 16,000 in 1989. Today, the numbers have bounced back to 28,000 due at least in part to legal protections. In Kenya and elsewhere in Africa, elephants are said to be destroying park habitats and making it difficult for other species to find food. They have also been roaming out of the parks and creating human-animal conflicts where destruction of property and even the killing of people have resulted. Thus, authorities are led to difficult animal management choices. Should they force sterilization on the elephant population? Should they move elephants elsewhere and if so where? Or should they cull the population and selectively kill some elephants, so that human-animal conflicts can be avoided?

—Peter Madsen

See also Agriculture, Ethics of; Animal Rights; Anthropocentrism; Bentham, Jeremy; Biodiversity; Duty; Factory Farming; Instrumental Value; Intrinsic Value; Moral Standing; People for the Ethical Treatment of Animals (PETA); Speciesism; Utilitarianism; Values, Personal; Wilderness; World Wildlife Fund

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Anthropocentrism

The word *anthropocentrism* comes from the Greek άυθρωπος, *anthropos*, meaning "human," and κέυτρου, *kentron*, meaning "of the center." In practice, anthropocentrism is generally understood as the view that human beings are the central fact on earth.

One ancient and influential text expressing anthropocentrism is in the description of the creation of the human being, in Chapter 1 of Genesis at the beginning of the Bible. This text, in accordance with the most common interpretation, reveals that men and women have an inherent dignity, since they are in the image of God, and superiority over all other creatures on Earth. This superiority is also expressed in several other places in the Bible. However, in the Bible, the human domination on Earth is not absolute but relative to God, the absolute owner of the whole of creation. This is made clear, for instance, in Psalm 104 in which it is declared that God is just in his concern for wild species and their habitats as he is for human beings. These and others biblical texts lead most experts to interpret that humans are called to dominate the Earth as stewards—in a responsible way, not as despotic dominators.

Both Judaism and Christianity have maintained and reinforced these biblical beliefs for centuries. Islam also considers people as a priority over the rest of creation, although it still preaches respect for nature. Other religions, such as Buddhism and Hinduism, have pantheistic conceptions of the world; there is no a clear difference between God and the cosmos. This gives a divine sense to nature. Some conclude that this vision offers a more sympathetic conception of the human relation to the rest of nature and a kind of spirituality that fosters unity between humans and nonhuman nature. Monotheistic religions encourage a respectful relation between humans and material nature but not a complete unity. But they are also far from a radical dualism between human and nature, since humans are part of nature, but not only so. They have a privileged condition and distinctive moral claims. Nature is fully recognized as a value, but the supreme value is not nature but the human person.

Anthropocentrism: A Historical Perspective in Western Civilization

In the sixth century, St. Benedict stressed a sense of stewardship of humans toward creation, and St. Francis, in the 12th century, preached a loving relationship of humans toward creation. In the Middle Ages, Christian theologians presented a close connection between the loving and redemptive purposes of God for the world and the original ordering of creation.

However, this anthropocentric view started to change in the 14th century, with William of Ockham. He maintained that creation is not God's loving purpose, as previously had been believed. Instead, he supposed that it obeys the arbitrary will of God. In the Renaissance the human-nature dualism started to gain acceptance as mainstream thought, and nature was understood basically as a mechanism to be studied and dominated. Francis Bacon emphasized that nature should be used for the sake of humankind; science and technique would be the means. Bacon did not advocate value-free technology, but the human-nature relationship was no longer seen in terms of stewardship. In the 17th century, Descartes considered that animals and plants were nothing more than *res extensa* (a thing with extension, pure matter). They are like machines, while humans are *res cogitans* (something which knows, that is a mind), with a *res extensa*, or body. Consequently, both the animal and human body should be explained by "mechanics."

The mechanistic view of nature was extensively considered by Galileo and Newton, and later by many others. Frequently, this mechanistic view has not only been applied to knowing how nature works but also to explaining its origins and meaning. In this way, any transcendent or ethical vision of nature disappears and, progressively, anthropocentrism becomes synonymous with the domination of nature by humans.

While some advocated an anthropocentrism without any limits, a nonanthropocentric view also appeared. Some popular scientific theories displaced man from the center of the universe to the periphery of it. In this line, Copernicus showed that the Earth moves around the sun, and Darwin suggested humans are the latest part of the evolutionary chain. In addition, some modern ideologies have also eroded anthropocentrism in certain aspects. Agnosticism and atheism ignore the transcendent roots of human dignity, while materialism destroys the notion of a human soul or spiritual principle nonreducible to mere matter.

In recent decades, a controversy over the influence of religions on the environment has arisen. Its origin is an article by Lynn White, published in 1967, in which he blamed Christianity as the ultimate cause of the Western environmental crisis. The main arguments are the biblical concept of subduing the Earth and the idea of a creator God who is "outside" creation. This position has been criticized on several points, including the fact that the real cause of the current ecological problems are related to the economic and cultural forms of late modernity rather than to religious influence on the cultural context.

All this has led to an alternative to anthropocentrism called biocentrism or ecocentrism. In the latter model, human beings are held to be a mere animal species coexisting with others and without any outstanding dignity over other animals. Consequently, some defend "animal rights," giving them similar nobility to human rights, while others apply utilitarianism by balancing pleasure and pain for every sentient being affected by an action. As a reaction, a renewed view of anthropocentrism with more solid foundations, and establishing its limits, has appeared.

Two Kinds of Anthropocentrism

This historical overview helps us to distinguish two different kinds of anthropocentrism. One is conceived as dominion, in the sense of absolute domination, while the other is an anthropocentrism understood as stewardship.

Dominion

In this vision, a radical dualism exists between human and nonhumans, and the former have an absolute domination over the latter. Human individuals are seen as autonomous beings endowed with knowledge and power to dominate Earth for their use, and with full right to do so practically without limits. Animals and natural goods are no more than possessions to serve the interests of their owners, without further consideration. Nature is taken to be a mere instrument that is continuously manipulated through technology. In addition, for many years it was believed that the technological impacts on nature could be easily absorbed. Modern capitalism has found support in these ideas. The cultural context defending the absolute domination over nature, accumulation of wealth, and an immoderate consumerism have produced notorious abuses in the exploitation of natural resources, abundant pollution in all its forms, and an increasing amount of waste products. This way of understanding anthropocentrism seems erroneous because of both the weak philosophical bases of its vision and of the negative effects of technology on nature, which in fact is not able to absorb these impacts.

Stewardship

This way of understanding anthropocentrism is rooted in the Judeo-Christian tradition and in philosophical anthropologies (Aquinas, Kant, Personalism, and others), which overcome the mechanistic vision of the natural world and stress human rationality, conscience, and freedom. Both approaches support the idea that humans are the central fact of Earth and only they have dignity and authentic rights. But, at the same time, humans are seen as stewards of nature. Development is not reduced to an indiscriminate possession of things and an unlimited consumerism. Development is, above all, human and sustainable development, which requires using material goods with moderation and a sense of responsibility, as a means for human flourishing and concern for future generations.

Anthropocentrism-stewardship does not disdain animals and it respects an ecological order. On the contrary, one must take into account the nature of each being and of its mutual connection in an ordered system, which is precisely the cosmos. This means, among other considerations, that animals have to be considered as having their own identity, and without reducing them to a mere instrumental value. Consequently, humans have to avoid cruelty to animals and even to be sympathetic to them.

Anthropocentrism and Business

A certain vision of anthropocentrism is related with business. Since the Industrial Revolution, capitalism and modern business have contributed to a considerable economic growth, provided jobs, made products more accessible, and been an effective means to fight against poverty. But, at the same time, capitalism has often been associated with greed for wealth accumulation, insatiable use of natural resources, technology with damaging effects on the environment, accumulation of population in large cities, and chaotic urbanization in many places. In the 19th century and a great part of 20th century, an unchecked organizational exploitation of natural resources was seen as desirable and even legitimate for the sake of economic development.

While the results of business activity have been beneficial for humans, the consideration of humans in productive processes has frequently been far from being human centered. People have been used as a mere means or resource for gains or for consumption, and not in accordance with the requirements of human dignity. In this approach, based on the anthropocentric-domination model, people receive some benefits, but the human person and his or her development is not the main motivation for economic progress.

In opposition to this approach, some have proposed substituting the conventional “anthropocentric management” paradigm, which is based on the idea of an unlimited domination, for an “ecocentric management” paradigm. However, this new paradigm has met criticism. It is argued that this proposal is rooted in a romantic conception of nature and is misanthropic because of the desire to remove the privileged position of humans within nature. In addition, it is accused of using controversial tone and of being selective in the treatment of environmental information. It could be argued that the ethical arguments that support the latter paradigm lack strength and several central tenets of the ecocentric discourse are questionable.

Since the middle of the 20th century, in many countries a new awareness regarding humans, their innate rights, and their habitat has arisen. In recent decades, a greater concern for the environment, both human and natural, has emerged, and the concept of “sustainable development,” which pays attention to future generations, has become increasingly popular. Simultaneously, a “stewardship management” based on “anthropocentrism-stewardship” is emerging. This includes respect for human dignity and rights and concern for the inherent value of the cosmos. An increasing respect for the environment for the sake of humans and their future generations is also a crucial aspect of this approach.

—Domènec Melé

See also Animal Rights; Biocentrism; Buddhist Ethics; Capitalism; Christian Ethics; Environmental Ethics; Jewish Ethics; Kantian Ethics

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Antitrust Laws

Antitrust laws in the United States were passed to limit the economic power of large corporations that can control markets by reducing competition through concentration or through the adoption of anticompetitive methods of competition. Large corporations are not simply passive responders to the impersonal forces of supply and demand over which they have no control. They have economic power, which can be used to gain some control over market forces. Markets may fail if the dominant firms in an industry are allowed to engage in predatory practices that drive competitors out of business or if firms are allowed to interfere with competition by gaining a monopoly position.

Background

It only took a single generation from the end of the Civil War for the United States to emerge as a world industrial power. During this period of rapid economic growth, the modern business enterprise was born in response to changes and opportunities in the economy. The corporate form of organization was used more and more frequently to make these enterprises even larger, as it allowed more capital to be accumulated and spread the risk across large numbers of stockholders. The growth of these large enterprises, however, posed a threat to the competitive structure of the economy. They often engaged in predatory pricing practices such as cutting prices below cost to drive smaller firms out of business to gain a monopoly position.

As competition became more and more severe in the late 19th century and individual firms found it difficult to gain a monopoly position, collusion between firms was not uncommon. The largest organizations created various arrangements with their competitors such as gentlemen's agreements and pools and new organizational innovations such as trusts and holding companies to reduce competition and gain control of an industry. These practices affected competition in the economy as a whole, and the economic power of large firms gave them the ability to dictate the terms of trade to smaller groups such as farmers, wholesalers, and retailers. There were no rules to regulate the behavior of these enterprises, and competition was disappearing in an unregulated market economy that became more and more concentrated.

Society began to fear the power of these enterprises, and the government responded to this concern by passing laws aimed at curbing their economic power and restoring competition in the economy. These laws were meant to embody the ideal of competition and provided a way for society to reaffirm its belief in the notion of a purely competitive economy where economic power is limited. The history of antitrust laws in the United States shows that the complex social and economic impacts of big business lead to institutional responses that interpret and enforce economic philosophy and political ideology.

The Laws

The Sherman Act of 1890 was the first piece of antitrust legislation and was supported by a coalition of small businesses and farm groups who were concerned about the economic power of the large trusts that, at the end of the century, had come to dominate many industries. The most important parts of the Sherman Act are the first and second sections. The first section attacks the act of combining or conspiring to restrain trade and focuses on methods of competition or firm behavior. This section seems to make illegal every formal arrangement among firms aimed at curbing independent action in the market. It places restrictions on market conduct, in particular those means of coordination between sellers who use formal agreements to reduce the independence of their actions. The second section enjoins market structures where seller concentration is so high it could be called a monopoly.

The language of the Sherman Act was quite broad, leaving a good deal of uncertainty as to what specific practices were in restraint of trade and thus illegal. The Clayton Act of 1914 was passed to correct this deficiency by being more specific with regard to anti-competitive practices. It bars price discrimination, where one buyer is charged more than another for the same item, when it tends to lessen competition in any line of commerce or tends to create a monopoly. The Robinson-Patman Act of 1936 was passed to amend the section that deals with price discrimination to strengthen it and plug loopholes.

Another section bars tying arrangements, where sellers give buyers access to one line of goods only if the buyers take other goods as well, and exclusive dealing arrangements, where sellers give buyers access to their line of goods only if the buyers agree to take no goods from any of the seller's rivals. Another section was designed to slow down mergers of companies by forbidding mergers that substantially lessen competition or tend to create a monopoly. This section prevented the acquisition of the stock of one company by another in the same line of business when the effect was to lessen competition or tend to create a monopoly, but it said nothing about the purchase or sale of assets to combine firms. Merger-minded companies exploited this loophole, which was finally plugged by the Celler-Kefauver Amendments of 1950, which forbid purchase of sale of assets when the effect of such acquisition may be substantially to lessen competition or tend to create a monopoly.

The Federal Trade Commission Act was also passed in 1914 to create the Federal Trade Commission (FTC) and empower it to protect consumers against all "unfair methods of competition in or affecting commerce." Exactly what methods of commerce were unfair was left up to the commission itself to decide. The FTC initially was allowed to attack practices that it defined as unlawful even though such practices did not violate establish antitrust law. These actions were eventually curbed, but in 1938 the Wheeler-Lea Act was passed to amend the relevant section to include unfair or deceptive acts or practices in commerce. This gave the FTC the authority to pursue deceptive advertising and other marketing practices that did not necessarily affect competition.

These three laws and their amendments constitute the pillars of antitrust legislation, but they have to be updated from time to time to take account of current developments. A major revision of these laws was accomplished in 1976 with passage of the Hart-Scott-Rodino Antitrust Improvements Act. Title I of this act gave the Justice Department broadened authority of interview witnesses and gather other evidence in antitrust investigations. Title II provided for premerger notification, requiring large companies planning mergers to give federal antitrust authorities advance notice of their plans. Corporations cannot complete the merger for 30 days after the notification report is filed, giving antitrust agencies time to study the proposal and take action to block the merger if the agencies find that the proposed merger raises anticompetitive concerns. Title III of this act allows state attorneys general to sue antitrust violators in federal court for treble damages of behalf of overcharged consumers even though the state itself was not injured.

Purpose

The role of government is to maintain a workable competition given the impossibility of developing a system of perfect competition that exists only in economics textbooks. Workable competition refers to a system where there is reasonably free entry into most markets, no more than moderate concentration, and an ample number of buyers and sellers in most markets. This objective is more realistically attainable than a perfectly competitive system given the nature of modern technology and organizations. The government is also interested in promoting fair competition referring to the exercise of market power in a manner that will enhance the competitive process. Competitors who have market power are thus prevented from engaging in anticompetitive practices that would destroy the competitive process.

Antitrust laws focus on both conduct and structure, as defined by Sections 1 and 2 of the Sherman Act, where conduct is the focus of the first section and structure of the second. The conduct of firms in a competitive market tends to sink to the lowest common denominator. If a firm adopts some kind of predatory practice that helps it gain a larger market share, rivals will have to adopt the same practice to stay in business. Thus, antitrust laws are in part a set of rules that set a standard of fair competition to which everyone has to adhere.

With regard to structure, the antitrust laws prevent the attainment of a monopoly position where the firm has an unfair advantage and could dictate the terms of trade in the market as a whole. Anticompetitive conduct falls into two general classes: (1) collusive actions whereby competitive rivals act in a joint fashion to achieve monopolistic goals and (2) exclusionary policies adopted individually that bolster a firm's economic power in relation to potential rivals. Collusion may be implicit when competitive rivals act uniformly through following the leadership of the dominant firm in an industry with regard to prices or through price signaling in press releases or explicit where rivals enter into express agreements to fix prices or allocate sales territories. Exclusionary practices include predatory pricing to drive rivals out of business, price discrimination, tying arrangements, and exclusive dealing arrangements.

Market structure refers to the economically significant features of a market that affect the behavior of firms in the industry operating in that market. These features include seller concentration, product differentiation, barriers to entry, elasticity of demand, and diversification. The most important of these features is concentration, which refers to the extent to which the market is under the control of a few dominant firms in an industry. Historically, the four-firm concentration ratio has been used to measure the percentage of sales attributable to the top four firms in the industry. It was generally believed that if the top four firms had 50% of the sales, this signaled the beginning of an oligopolistic industry where market power of the dominant firms is a factor in the way the industry as a whole conducts itself. More sophisticated measures of industry concentration have been used in recent years to determine concentration.

Enforcement

Enforcement of this antitrust legislation at the federal level is shared by the Antitrust Division of the Department of Justice and the Bureau of Competition within the FTC. There is substantial overlap between these two agencies, particularly with regard to the Clayton Act and its amendments, where the Antitrust Division and the FTC have concurrent jurisdiction. Technically speaking, the Sherman Act is the sole province of the Antitrust Division and the FTC has sole responsibility for enforcing the Federal Trade Commission Act. But overlap occurs, as the FTC can reach violations of the Sherman Act under the broad mandate to deal with "unfair methods of competition." Because of these overlapping areas, the FTC and the Antitrust Division of the Justice Department exchange notifications and clearances to assure they do not duplicate efforts and file the same cases. They also coordinate their activities where necessary.

The intentionally vague language of antitrust laws allows each administration to interpret and enforce the laws in accordance with its economic philosophy. Courts also have power to interpret the meaning of antitrust legislation through their rulings on cases that come before them. The history of antitrust enforcement shows changes in notions of competition and fears about the power of big business. Enforcement efforts reflect the tensions of maintaining allegiance to the ideals of competitive markets while allowing society to reap the benefits of large-scale production, distribution, and organization. The antitrust laws thus institutionalize our fear of large concentrations of power, yet their application is flexible to allow the benefits of concentrated industries to be exploited when society deems appropriate. These realities make a straightforward application of abstract notions about competitive markets extremely difficult.

This flexibility was already evident immediately after the antitrust laws were passed as the courts remained probusiness for several years. In 1895, for example, the Supreme Court ruled that American Sugar Refining, even though a trust, was not a monopoly in restraint of trade and therefore not in violation of the Sherman Act. A year earlier, the Court had issued an injunction against the union in the Pullman strike on the basis that it was a conspiracy in restraint of interstate commerce. The framers of the law had no intention that it should apply to unions, and unions were later exempted from antitrust laws. The Justice Department lost seven of the first eight cases it brought under the Sherman Act. Finally, in 1911, two trusts, Standard Oil and American Tobacco, were found guilty of violating the Sherman Act and ordered to be dissolved into several separate firms.

In finding these firms guilty, however, the Court invoked the so-called rule of reason. These firms were found guilty because they had restrained trade unreasonably. This decision emphasized the vicious practices these companies had used against their competitors. Section 1 of the Sherman Act was thus interpreted to prohibit only unreasonable restraints of trade. Under this rule of reason test, antitrust litigation relied on extensive economic analysis and evidence to determine whether the business practice in question was actually anticompetitive. Subsequent cases against Eastman Kodak Company, United Shoe Machinery, International Harvester, and U.S. Steel were found in favor of the firms because they had not visibly coerced or attacked rivals.

Eventually, however, the courts came to adopt a per se approach to violations of Section 1 of the Sherman Act. They began to hold that certain kinds of conduct are so unreasonable that they cannot be excused by evidence that they do not adversely affect competition. In the Trenton Potteries case (*United States v. Trenton Potteries Co.*), the Court held that price-fixing per se was illegal, whether reasonable or unreasonable. "The power to fix prices," the Court said, "whether reasonably exercised or not, involves power to control the market and to fix arbitrary and unreasonable prices. The reasonable price fixed today may through economic and business changes become the unreasonable price of tomorrow."

This represented a major change in the Court's thinking, and the practices that became per se violations of Section 1 of the Sherman Act include (1) price-fixing, (2) restriction of output, (3) division of markets, (4) group boycotts, (5) tying arrangements, and (6) resale maintenance schemes. With respect to these practices, proof can be limited to the fact and amount of damage. The establishment of a per se approach to these practices relieves the parties to the suit and the Court from having to inquire into the factors relevant to a rule-of-reason analysis. Under the per se approach, it is irrelevant to inquire into the reasonableness of the restraint or attempt to provide an economic justification for an illegal practice.

With regard to structure or Section 2 of the Sherman Act, the issue is more complicated. While the rule of reason was in effect, it was clear that the law did not make mere size or the existence of unexerted power an offense. Size could only be an offense if accompanied by certain predatory types of market conduct. This changed with the Alcoa case of 1945 (*United States v. Aluminum Co. of America*), where it was held that a high level of seller concentration in and of itself could constitute a violation. The Court could find no predatory conduct on the part of Alcoa. Its 90% market share was obtained by an honest industrial effort. But Alcoa's monopoly was not thrust on it, the Court said, and by a series of normal and prudent business practices the firm had succeeded in discouraging or forestalling all would-be competitors. The Sherman Act forbade all such monopolies no matter how acquired.

In the 1970s, the Justice Department attempted to extend the reach of antitrust laws to oligopoly itself. This structure was called a "shared monopoly" in that the largest companies in some industries achieve consensus decisions on output and pricing that resemble those of a more traditional single-company monopoly. The Justice Department proposed filing a suit on this basis to test the thinking of the courts regarding this issue. The FTC actually did file a suit against the four largest manufacturers of ready-to-eat breakfast cereal, charging violation of Section 5 of the Federal Trade Commission Act (*FTC v. Kellogg et al.*). The suit charged that the largest companies in the cereal industry compete by introducing more and more brands. The result is brand proliferation, which gives little hope that new companies will get much of a foothold because they have to compete for ever smaller slices of the market. This was held to be an unfair method of competition because it raises barriers to entry for new companies and is a shared monopoly.

These efforts came to naught with the end of the "activist" period in antitrust litigation in the 1980s as the country turned more conservative. Economists began to attack antitrust laws blaming the decline of U.S. competitiveness at home and abroad at least partly on outdated antitrust enforcement practices. They argued that it is wrong to look at the structure of an industry and conclude that a small number of companies automatically means less competition. Economies of scale exist in concentrated industries, they argued, which mean unit production costs and therefore prices are often lower than if the industry were more competitive. This philosophy was reflected in the Reagan administration's approach to structure, arguing that big businesses are very valuable things because they tend to be the most efficient. Antitrust enforcement should strive for only one goal, that of maximum production at the lowest price.

Recent years have seen some changes in the application of antitrust laws, but no radical changes of philosophy regarding both conduct and structure. Most of what has occurred could be called simply a change of emphasis. Merger activity waxes and wanes in response to economic opportunities, and the antitrust laws are activated whenever it is deemed appropriate and necessary. One of the most interesting cases in recent years has been the suit against Microsoft Corporation, which came to hold about 90% of the operating system market. This gave it power to tie application programs such as its Web browser to its

Windows operating system. The government was concerned that Microsoft was using its Windows monopoly to dominate other markets and that the company had to be reined in lest it gain a choke hold on Internet development. The underlying problem was Microsoft's ongoing practice of rolling new features into its operating system, a process that made each new version of Windows better and more powerful. Because computer users are essentially locked into Windows, it was easy for the company to get them to use its other software even if competitors make better products. This practice is called bundling and is said to dampen competition, reduce choices for consumers, and retard innovation in the industry.

The government pressed hard for a breakup of the company into two separate and competing companies, one for its Windows operating system and one for its other computer programs and Internet businesses. They sought a structural remedy and believed that such a solution would be the only way to force Microsoft to change its conduct. But in the final settlement the government agreed to a solution geared to change Microsoft's conduct with respect to certain parts of its business activities. The most important part of the problem, namely Microsoft's ability to include more and more application programs in its operating system, was not addressed. The case was not the bell-weather case many had hoped for, and did not do much in providing directions regarding the way in which antitrust law will be applied to so-called new economy companies that provided computer software or hardware or were based on the Internet.

With the development of a global economy, companies such as Microsoft faced antitrust litigation in other countries. The European Union (EU) found that Microsoft violated its antitrust laws by bundling other software with its Windows operating system. Government requirements regarding antitrust laws are thus a major hurdle in geographic areas where these laws are well developed, while compliance is less burdensome in other areas of the world that do not have stringent antitrust requirements. Many argue that companies need to be large and have more freedom to compete effectively on a global scale and that U.S.- and EU-style antitrust laws are an obstacle to achieving this effectiveness.

—Rogene A. Buchholz

See also Competition; Economic Efficiency; Federal Trade Commission (FTC); Herfindahl Index; Price Discrimination; Price-Fixing; Trusts; Unfair Competition

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Arbitrage

In its strictest definition, arbitrage is defined as the activity of buying and selling a portfolio or collection of assets that provides a guaranteed, or riskless, cash flow when the present total cost of the portfolio is zero or less. Note that a positive cost for an asset suggests a cash outflow so that a negative cost would be considered a cash inflow.

In a simplified world where there are two dates for cash flows to change hands, today and some future date that we shall call tomorrow, there are two types of arbitrage that may occur:

1. Where a nonpositive investment occurs today (someone pays you today or gives you the rights to own the portfolio), which then produces a guaranteed positive cash flow tomorrow
2. Where a negative investment occurs today (someone pays you today to own the portfolio), which then produces a nonnegative (the portfolio provides a cash flow of either zero or a positive amount) cash flow tomorrow

In a competitive market, arbitrage opportunities generally do not exist. If they do exist then they will be traded on by arbitrageurs until the arbitrage opportunity that is caused by a mispricing event in the market between cash flow substitutes disappears.

If we can rule out the possibility of arbitrage in securities or asset markets, then we can use this information to price an asset that is a cash flow substitute for another asset. That is, if two assets will produce the same cash payoff tomorrow, then the two assets must cost the same today. Specifically, the no-arbitrage condition of asset pricing requires that the price of the two assets mentioned above must be the same. As an example, assume that the cash flows and payoffs are as below for Asset A and Asset B:

- Payoff of Asset A tomorrow is $10.
- Payoff of Asset B tomorrow is $10.
- Cost of Asset A today is $6.
- Cost of Asset B today is $7.

It is easy to see that B is over priced relative to the price of A. An arbitrageur could put on the following arbitrage trade to profit from the relative mispricing:

- Sell Asset B short today for an inflow of $7.
- Buy Asset A today for an outflow of $6.
- Net inflow today is $1.

Tomorrow, the arbitrageur would do the following an instant before the two assets made their respective cash payouts:

- Repurchase Asset B for $10.
- Sell Asset A for $10.
- Net cash flow tomorrow is $0.

The net benefit of the arbitrage trade was a $1 cash inflow today with a guaranteed neutral cash flow tomorrow for the arbitrageur. This meets the second definition of arbitrage mentioned above.

In the above example, the arbitrageur would continue to put on the arbitrage trade until the arbitrage no longer existed. Note that the trade that the arbitrageur puts on will cause the price of Asset A to increase and the price of Asset B to decrease. The arbitrageur will continue to trade until both prices are equal, thereby removing the arbitrage opportunity.

What Arbitrage Is Not

Often times traders will identify a trade that depends on certain events occurring, which will make the trade extremely profitable. However, if the future happens to take an unanticipated course then the profitability of the trade is much lower or even unprofitable. Such a trade is not an arbitrage trade. An arbitrage opportunity requires that there be no risk concerning the cash flows as well as no cost today (initial investment) for the portfolio. This means that if there is any chance that the payoff for owning the portfolio (or combination of assets) will not be constant under any circumstances, then there is no arbitrage opportunity available. In the prior example, let's assume that the cost and payoff for Asset A remains the same but only the payoff for Asset B is slightly altered. That is, Asset B now has a 90% probability of producing a $10 cash flow tomorrow and a 10% probability of producing an $11.50 cash flow tomorrow. Let's assume that the same arbitrage trade is put on by an arbitrageur. It is easy to see that the cash flows to the arbitrageur will have a 90% probability of being just as we calculated in the earlier example. However, let's examine the cash flows for the trade the other 10% of the time:

- Today, the cash flow will be just as before.
- Sell Asset B short today for an inflow of $7.
- Buy Asset A today for an outflow of $6.
- Net inflow today is $1.

However, 10% of the time the cash flows will be as follows:

- Repurchase Asset B for $11.50.
- Sell Asset A for $10.
- Net cash outflow tomorrow is $1.50.

Now we have introduced the possibility that the arbitrageur will have to pay out $1.50 tomorrow. Therefore, the payoff is not guaranteed to be the same in all circumstances.

Consequently, the set of cash flows for Assets A and B do not provide an arbitrage opportunity since the payoff of the constructed portfolio is not constant and does not therefore meet the qualifications of either type of arbitrage. In fact, given the second example setup, it is entirely possible that the relative prices of Assets A and B are completely arbitrage free. To reiterate, for a trade opportunity to be an arbitrage opportunity, it must meet two criteria: (1) a trade opportunity must involve a riskless or guaranteed profit and (2) it must involve a nonpositive investment.

No-Arbitrage Conditions

As mentioned earlier, arbitrage profits are either available for very short periods of time or not at all. Such a no-arbitrage condition, therefore, yields the ability to price derivative instruments in a fairly precise manner. That is, if two portfolios will generate the same cash flows tomorrow, regardless of the state of the world, then they must have the same cost today. Since derivative instruments derive their payoff from some underlying security, then we are usually able to construct a portfolio of derivative instruments whose payoffs can be duplicated by owning some amount of a market-priced underlying security. If the payoffs of these two portfolios are the same, then their market prices must also be the same. From that point, it is a simple matter of deducing the no-arbitrage market-determined price of each derivative instrument.

—L. Wendell Licon

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ARCHER DANIELS MIDLAND

Founded in 1902 and incorporated in 1923, Archer Daniels Midland (ADM) is one of the largest agricultural processors in the world. It supplies many of the inputs for agricultural production, buys the crops from the field, processes them into food for humans and animals, fuels, and chemicals, and sells them all over the economy—and lobbies, very successfully, to obtain and retain the legislation that makes the entire operation profitable.

It *is* profitable. In the fiscal year ending June 30, 2005, ADM reported net earnings of $1,044 billion, or $1.59 per share, compared with $495 million, or $0.76 per share, in the previous year. Profits were up in Europe, South America, and Asia. So the board of directors declared a cash dividend of $0.085 per share on the company's stock—ADM's 315th cash dividend and 295th consecutive quarterly payment, 73 years of uninterrupted dividends. Clearly, they are doing something right.

In addition to being profitable, ADM tries to be environmentally friendly, and often succeeds. In the same fiscal year, ADM won two United States Environmental Protection Agency Presidential Green Chemistry Awards for a way to reduce volatile toxins in paints and a way to lower trans fats and oils in vegetable oils.

It is not always easy to be good. ADM stands at the heart of an enormous network of companies and activities, owning or controlling the entire agricultural enterprise through direct ownership or joint ventures with other companies. Its position entails that it controls the entire food chain, from the decision on what to plant, from the seed, through the machine that plants the seed and the pesticides and herbicides that help that seed to prosper, through the tending and harvest of the crop, through all processing and distribution of the products, to the very shelf in the supermarket (or repose in the chuckling fat of the fast-food French fries cooker). In the course of its vertically integrated enterprises, it is often difficult to discover the market price of a product that, for instance, is created from crops on an ADM farm and immediately sent back to another ADM farm to feed hogs. Just such a product is lysine, a corn-based dietary supplement for farm animals that is widely used across several countries. Yet it turns out to be possible for one to cheat, and price fix, on this product, for that's just what ADM was caught doing in 1996; they ended up paying a record fine of $100 million for price-fixing. That wasn't the end of their problems: Two years later the government brought separate criminal charges against three top executives for conspiring in the crime, collected more fines, and sent the executives briefly to jail. Later, the European Union added its own penalties; in all, ADM had to budget over a quarter of a billion dollars for all expenses connected to the price-fixing incident.

ADM has maintained its agenda in Washington largely through very generous political contributions to both parties, amounting to some $2 million per year. A large part of its Washington lobbying agenda has been to urge, as the petroleum resources decline, the adoption of a provision requiring that ethanol should be a part of every gas station and oil reform. (The concern for oil scarcity has a lot to do with the fact that ethanol is produced from corn; at this point ADM controls more than 50% of the ethanol capacity in the world.) Conservatives and liberals alike have objected to this huge subsidy, but it continues.

—Lisa H. Newton

See also Agribusiness; Agriculture, Ethics of; Factory Farming

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Arendt, Hannah (1906–1975)

Hannah Arendt is best known for her writings on political philosophy, most specifically her analysis of the 20th-century totalitarian regimes. Born in Hanover, Germany, Arendt studied philosophy with Martin Heidegger, and later with Karl Jaspers. In 1933, Arendt fled Germany for Paris, surviving a brief internment en route. Although Arendt was neither religious nor a Zionist, the rise of the Nazi party and the rapid spread of anti-Semitism through Europe provoked in Arendt a strong consciousness of her Jewish identity. In her intellectual writings of the 1930s, she argued that conditions of freedom and citizenship should never require repudiation of one's ethnic or cultural identity.

Emigrating to New York in 1941, Arendt gained recognition among political theorists and philosophers as a bold and controversial intellectual. She was University Professor in Political Philosophy at the New School for Social Research and a visiting fellow at the University of Chicago. Her major works include *The Origins of Totalitarianism*, *On the Human Condition*, and *The Life of the Mind.*

Most relevant to the field of business ethics is Arendt's authoritative analysis of the trial of Nazi leader Adolf Eichmann, *Eichmann in Jerusalem: A Report on the Banality of Evil.* Arendt attended the trial in Jerusalem to report the proceedings in a series of articles for the *New Yorker* magazine. As she listened to Eichmann's defense of his own motives and actions, Arendt concluded that Eichmann was not a monster but an ordinary man, following orders and doing his job to the best of his ability. He asserted that he bore the Jews no particular ill will and that in different circumstances he wouldn't have taken actions that ultimately killed millions of Jews—he just happened to be the person in that role, a role any number of Germans might have filled as well as he did. It was precisely this inability to think about the moral implications of his actions that led Arendt to characterize Eichmann's evil as banal. This characterization was a radical departure from previous sociological, philosophical, and psychological analyses of evil. Furthermore, Arendt asserted that the Holocaust could not have happened without the collaboration of Jewish organizations. In this, she was not blaming the victims but describing an essential component of the Nazi strategy to force cooperation and thereby undercut Jewish resistance solidarity. For these views, she was accused of insulting Jewish victims of Nazi genocide and including them as blameworthy in accounting for the atrocities of World War II.

In contemporary social analysis, the term *the banality of evil* has come to generally indicate the ease with which immoral actions, such as lying, stealing, falsifying records, and violating rules, are accepted into daily life. Indeed, the term *Eichmann* has come to represent that potential in each of us to be blind to the moral impact of our actions.

—Robbin Derry

See also Civil Rights; Freedom and Liberty; Human Rights; Jewish Ethics; Kantian Ethics; Machiavellianism; Pluralism; Political Theory; Religious Discrimination; Roles and Role Morality

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Aristotle (384–322 BCE)

A Greek philosopher who lived in the fourth century BCE, Aristotle was long referred to as "*the* Philosopher" and the master of those who know. He was a student of Plato and the teacher of Alexander the Great, and he is widely credited with having been one of the most comprehensive, influential, and profound thinkers ever to have lived. His books were numerous and their topics wide-ranging. Including but not limited to writings on natural science, psychology, logic, ethics, metaphysics, rhetoric, and the art of poetry, Aristotle's corpus also included works treating the investigations at the heart of this encyclopedia.

Three general characteristics of his work help to distinguish Aristotle from other ancient philosophers: (1) he was greatly concerned with empirical evidence, so when studying politics, for example, he compiled data on many actual constitutions; (2) he attended to the opinions of other thinkers, so he offered explicit criticisms of Plato, for example, and of the atomists and Pythagoreans; and (3) he stressed the importance of focusing on the end or purpose (*telos*) of things, so in discussing causality, Aristotle stressed the final cause or purpose, whereas both his predecessors and his followers show more concern with material or formal causes.

Widely studied by scholars of the history of thought, Aristotle is also turned to as a thinker with contemporary relevance, especially when it comes to his treatment of ethics and politics. His teleology helps him to argue that the city-state is natural, for example, and has the purpose of helping human beings reach their natural end or fulfillment. This natural end requires that we live well as human beings, and this in turn entails exercising the virtues he examines in his *Nicomachean Ethics.* Different political arrangements should thus be judged in light of their ability to foster this ethical end. As he makes this case, Aristotle even seems alert to modern temptations such as relativism, hedonism, and communism (which he knew in its Platonic variety). Along with his empiricism, which helped limit any tendency toward utopianism, his teleological approach led him to take a stand against these still vigorous intellectual currents, and this in turn has helped him to continue to find enthusiasts even in recent centuries.

As regards business, ethics, and society, note first that Aristotle gave the word "ethics" its prominence. Related to the Greek words for habit (*ethos*) and for a sustained disposition or characteristic (*ēthos*) of a person, Aristotelian ethics develop the view that the human good is happiness, that a person's happiness proceeds from activity in accord with virtue, and that the virtues are identified especially by examining the specific endowments of human beings as such. Aristotle thus rejects the view that happiness is the mere gratification of desire, while he also opposes the view that duty or obligation is fully defensible without regard to its contribution to the happiness of the dutiful person. In more technical language, his approach to ethics is neither hedonist nor deontological; rather, it helps give shape to what is now known as "virtue ethics," where the focus is on possessing and exercising virtues, not on an external criterion of right action.

A second way in which Aristotle is important for business ethics is that his treatment of "business" (or, more precisely, "the art of acquisition," *chrematistikē*) is focused on the question of whether acquisition should be limited or not. Late in Book I of his *Politics*, he appears to develop the view that acquisition that is not limited by a proper purpose is "unnatural," while natural acquisition is limited by reasonable goals. While Aristotle's criticisms of various sorts of utopianism serve in advance as cautions against important features of Marxism, he also advances principles that do not sit well with the acquisitiveness of modern capitalism. His teleological view of acquisition is one such principle; his teaching that things have inherent value also discourages a complete surrender to the market as the determinant of worth.

—Wayne Ambler

See also Deontological Ethical Systems; Hedonism, Ethical; Hedonism, Psychological; Utilitarianism; Virtue Ethics

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Arms Trade

The arms industry is a massive global business enterprise that never seems to lack suppliers and customers. For better or worse, an armament is a product or system designed to maim, kill, or destroy. The arms trade is the sale or barter of armaments (weapons) between two or more parties for profit. Such exchanges are generally (but not exclusively) conducted by sovereign governments and by private contractors around the world and subject to various regulations. Most of the biggest sales are state-to-state transfers of highly sophisticated weaponry, but the bulk of sales involve smaller arms and light weapons (SA/LWs).

Basic Information

The international trade in weapons is currently worth in excess of $35 billion per year. Some weapons producers are state owned. But advances in international communication and the end of the Cold War helped consolidate manufacturing across national boundaries in private hands, now dominated by a small number of Western multinational corporations. America and Europe currently account for about 94% of arms sales. In fact, the United States is the world's leading arms exporter—with a 63% market share that is more than all other competing nations combined. Other major arms exporters include Russia, France, the United Kingdom, Germany, Canada, China, and Israel. Nations such as Iran are often portrayed in the news media as a major supplier of arms to militant Islamic groups, but this role is often as an intermediary since many of those weapons were originally produced in other countries.

The figures above are informed estimates because of the failure to create an effective international system to mark or trace exchanges, especially for small and light arms. Unlike a jet fighter, SA/LWs have many legitimate buyers including individuals and police forces in addition to military clients. As unpleasant as it might be to think about, law enforcement needs armored vehicles, CS and pepper gas, electric shock batons and leg irons, execution equipment, guns and ammunition, rubber bullets, security and surveillance equipment, water canons, and so on. There are also many participants in the arms system, with SA/LW production occurring in over 90 countries and with more than 1,200 companies involved in some aspect of the trade (from production to repair). Putting controls on the arms market is further complicated by the lack of transparency in most such deals. SA/LWs are especially easy to hide, pass along, smuggle, steal, and capture from the enemy. In the conventional weapons category alone there are also multiple (and often conflicting) sources of data for the many levels of trade. The bottom line is that weapons are very easily available from a variety of different sources.

Illegal Transfer of Weaponry

One area of concern is the illegal transfer of weaponry. Although unlawful, an active and highly profitable underground armaments marketplace exists. Ironically, the vast majority of small arms on the black market were originally manufactured and marketed legally before being diverted into an illicit network. This diversion occurs via a number of ways, including the following:

- "Straw purchases" in countries such as the United States without limitations on the number of weapons a person can legally buy or own at one time, and the illegal resale of some of those arms either domestically or in other nations where gun laws are more restrictive
- Theft from civilian gun owners
- Accidental loss and misplacement by governments
- Theft from government weapons stockpiles
- Looting of military and police arsenals during periods of instability
- Soldiers selling their weapons because they haven't been paid or have sympathy to a rebel cause
- Violating arms embargos by bribing officials in one country not on a debarred list to allow transshipments to a sanctioned country

Weapons might be sold for cash; bartered for hostages, drugs, or any marketable commodity; or countertraded for oil or food. The deals can be transacted by unscrupulous go-betweens who are equally comfortable in shipping toxic waste to the horn of Africa, smuggling illegal immigrants to the United States, or trafficking in counterfeit computer chips to Europe. This trade requires access to cargo ships typically registered in a "flag-of-convenience" nation noted for its openness to corruption through low registration costs, dummy commercial ownership rules, and banking secrecy. Ultimately, the money payments and commodity sales are moved through international networks of so-called ghost companies and coded bank accounts in tax haven countries, which benefit by protecting all financial transactions against prying regulatory scrutiny. Constantly attempting to keep ahead of investigators (usually successfully), these clandestine networks thus are conduits for an incredible variety of goods and services.

Lack of International Controls

Unfortunately, these black market sales/resales operate outside of any viable international system of law enforcement. The Organization of American States and the Organization for Security and Cooperation in Europe are largely ineffective in terms of legal armaments monitoring, let alone clandestine trafficking. Even the United Nations (UN) has no mechanism for ensuring that its rules are followed. This impasse may arise out of the fact that the five permanent members of the UN Security Council (the United States, France, Russia, China, and the United Kingdom) are among those responsible for more than 80% of global arms sales.

Instead, many arms sales are subject to stringent national and bilateral export/import controls. Such restrictions tend to work fairly well on large weapons and systems. Nevertheless, loopholes are plentiful even there. Products that have both military and civilian applications (especially electronics and other dual-use equipment) often escape export restrictions. Even when arms agreements are in place, still another ambiguity is encompassed in weapons brokering. Unlike the direct trade in armaments, brokering involves the legal selling of weapons to what turns out to be an intermediary without reporting the actual destination customer for the goods (typically an oppressive rogue regime or insurgency). A variation occurs when an arms manufacturer issues a license for its weapons to be built overseas in a country with low wages and lax export rules. Because this activity creates local employment in the recipient nation, such licensed production also serves as an incentive for the purchase of additional weapons.

Even the question of what actually constitute armaments is subject to nuance. Arms products typically include various types of guns, ammunition, disabling gases, explosive devices, tanks and other vehicles, ground-to-air and air-to-air projectiles, aircraft and naval ships for military use, integrated weapons systems, and associated consumable items (clothing, body armor, helmets, food rations, etc.). Despite organized opposition to private weapon ownership in many countries and although their use can prove to be lethal, guns and knives carried for self-protection and those used for hunting/sport purposes (as compared with military specification) are generally not regarded as "arms" in most analyses.

SA/LWs are considered a subcategory of "conventional weapons," which make up the bulk of the arms trade. In 1997, a UN panel developed working standards to define SA/LWs that are now widely accepted. In essence, a small arm is one that can be fired, maintained, and transported by one person; a light weapon requires a crew of two or more people and is transportable on a light vehicle or pack animal. Small arms include revolvers, self-loading pistols, rifles and carbines, smaller machine guns, and related ammunition. Light weapons range from heavy machine guns, grenade launchers, shoulder-fired antitank missiles, and other portable antiaircraft guns, to mortars of less than 100 mm caliber.

A major weakness is that there are no binding international treaties or other legal instruments dealing with establishing universal arms export criteria, brokering standards, creating arms identification marks, or tracking of conventional weapons. On the other hand, weapons of mass destruction (WMD), such as nuclear, biological, and chemical weapons, are banned through a variety of global agreements. But even in the case of WMD, there is an illicit market that is especially worrisome to antiterrorist authorities in the United States and Europe.

The U.S. Perspective

Historically, Americans have been suspicious of arms manufacturers, fearing that those who had the most to benefit from weapons sales also had an incentive to stir up conflict. As far back as George Washington's day he warned against getting involved in entangling military alliances. In the 20th century, the U.S. Senate established a committee to investigate the industry and war profiteering. After hearings lasting from 1934 until 1936, the committee published a series of studies reporting a strong link between lobbying by munitions industry representatives ("merchants of death") and the American government's decision to enter World War I. Committee members were also highly critical of the way the nation's leading bankers operated, arguing that their role at the center of the American economic system made war inevitable.

Nearly 25 years later as his last term neared its end, President Dwight D. Eisenhower, in his farewell address, also warned against giving too much power to this military-industrial complex, but his concerns like those of the Senate committee have largely been ignored. Today, just 12 firms dominate American weapons production (AAI Corporation, BAE Systems Inc., Boeing, Carlyle Group, Colt's Manufacturing Company, General Atomics, General Electric [primarily through GE-Aviation], General Dynamics, Honeywell, Lockheed-Martin, Northrop Grumman Corporation, and Raytheon Corporation). They are generally working hand in hand with the Department of Defense and the Congress, the so-called iron triangle.

Most of these companies are household names, since many also produce a diversity of civilian products and services (including ownership of major media). Such interconnection raises questions about information control and propaganda. Other firms not on the list, such as Bechtel and Halliburton, benefit by providing services in the aftermath of military conflict, as has been in the case of the American occupation of Iraq beginning in 2003.

Ethics of International Arms Sales

Are any forms of international arms sales ethical? Businesses do not operate in a vacuum. Their activities inevitably lead to a series of social and environmental impacts, especially when the product created is designed to maim, kill, and destroy. Proponents, however, argue there are tangible benefits to the arms business. These positive impacts include the following:

- Providing domestic and overseas employment
- Contributing to balance of trade surpluses
- Helping governments maintain stability and defend themselves against attack
- Gaining influence in other countries through military foreign aid
- Securing access to overseas military facilities
- Further rewarding allies when engaged in conflicts such as the current actions in Afghanistan and Iraq

Critics suggest the price for such strategic partnerships and coalitions is steep, with the United States taking the brunt of the blame over weapons proliferation and the cynicism engendered. A number of nongovernmental groups have been monitoring developments and agitating for better monitoring tools and stronger treaties to beef up international control and enforcement. Many of these groups say that bribery, insider deals, and political back-scratching characterize today's arms trade so that any participation is morally repugnant. Opponents further argue that U.S. arms transfers often end up fostering a climate of violence by adversely

- diverting expenditures that otherwise would go to health, education, and other social programs,
- empowering undemocratic regimes,
- enhancing surveillance of dissidents and minorities,
- contributing to torture and internal repression,
- exacerbating other human rights abuses,
- fueling external aggression/wars (especially when supplying both sides of a conflict),
- obstructing relief programs,
- contributing to child prostitution and labor (with some even forced into service as soldiers), and
- fostering war crimes.

Worse, instead of securing the regional stability they were supposed to ensure, weapons sales frequently undercut global security. This ironic result has been cynically called in Orwellian fashion a perpetual war for perpetual peace by historians such as Harry Elmer Barnes.

According to the United Nations, there are over 635 million SA/LWs in circulation worldwide. These SA/LWs alone account for over a half million deaths annually, including 300,000 in wars and related unrest. Cluster bombs and land mines are widely used and continue to be dangerous well after a conflict winds down. Lack of funding too often precludes removal. So when properties remain mined they cannot serve a productive use, such as the raising of animals or growing of crops.

The majority of arms are sold to developing nations, which by definition tend to have serious problems of poverty, hunger, and governance. Not surprisingly, fully 80% of the world's poorest countries have suffered from a major armed conflict in the past two decades. By way of example, of the 49 major conflicts occurring in the 1990s, small arms were the weapons of choice in all but two instances. The AK-47, a very effective and durable machine gun first created in the Soviet Union, is plentiful and can be bought for under $10 in some countries. The almost $25 billion spent on arms each year by developing nations is considerable. However, the arms expenditures in turn are a drop in the bucket compared with the nearly $600 billion Third World nations owe to the United States, members of the European Union, and other creditors. One problem compounds another.

Maintaining controls on what happens to legal sales is also increasingly difficult over time. This dilemma is exacerbated when governments change policies or fall from power as arms provided to friendly forces end up in the hands of potentially ruthless adversaries. For example, U.S. M16 machine guns were used in 1991 to murder peaceful demonstrators in East Timor. Following the Gulf War, Saddam Hussein used Soviet and Western-made arms in the domestic slaughter of thousands of Iraqi Kurds and Shiites. Stinger missiles that the United States supplied to the mujahedeen in Afghanistan in the 1980s were used against American forces in the war with the Taliban. Even weapons dating back to the intervention in Vietnam are still in circulation.

The illicit trade and trafficking in small arms is of particular concern for nations subject to rebellion and which have poor law enforcement. For far-flung countries with extensive coastlines, they face particular challenges involving transfer of nonsanctioned SL/LWs by sea. Police and intelligence authorities have detected the involvement of international organized criminal groups in the trade in small arms. Such firearms are not only used by insurgents, but end up in the hands of civilians and linked to crimes, especially armed robberies.

—Richard Alan Nelson

See also Amorality; Barter; Black Market; Capitalism; Cartels; Collusion; Colonialism; Communism; Consequentialist Ethical Systems; Darwinism and Ethics; Deontological Ethical Systems; Developing Countries, Business Ethics in; Developing World; European Union; Extortion; Foreign Corrupt Practices Act of 1977 (FCPA); Free Market; Global Business Citizenship; Global Codes of Conduct; Hedonism, Ethical; Human Nature; Human Rights; Industrial Revolution; Kantian Ethics; Internal Revenue Service (IRS); International Business Ethics; International Trade; Machiavellianism; Multinational Marketing; Nongovernmental Organizations (NGOs); Public Interest; Regulation and Regulatory Agencies; Self Interest; Tax Havens; Terrorism; Truth Telling; United Nations; Utilitarianism; Wealth; World Trade Organization (WTO)

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Arrow, Kenneth (1921–)

Born August 23, 1921, in New York City, Kenneth J. Arrow was awarded the Royal Bank of Sweden Prize in Economic Sciences in Memory of Alfred Nobel (widely known as the Nobel Memorial Prize) in 1972 with Sir John R. Hicks for their contributions to general economic equilibrium theory and welfare theory. Arrow is one of the major representatives of the neoclassical school of economics. His main contributions were devoted to the fields of social choice theory—which includes his famous Arrow impossibility theorem—general equilibrium theory, growth theory, and economics of information and organization.

He graduated in 1940 with a B.S. in social science with a major in mathematics at City College of New York. He received an M.A. in mathematics in 1941 from Columbia University. During World War II, he served as an officer in the Weather Division of the Army Air Corps, conducting research. After the war he returned to graduate study at Columbia. In 1947, he joined Jacob Marschak as a research associate at the Cowles Commission, University of Chicago, where he became Assistant Professor of Economics during 1948 to 1949. His work on social choice dates from this period. In 1949, he was appointed Acting Assistant Professor of Economics and Statistics at Stanford University where he has been working ever since, except for the period 1968 to 1979. In 1968, he moved to Harvard University as Professor of Economics, becoming the James Bryant Conant University Professor in 1974. In 1979, he returned to Stanford as Joan Kenney Professor of Economics and Professor of Operations Research. He retired in 1991 when he was designated Emeritus Professor. Among other high honors, he received the John Bates Clark Medal of the American Economics Association in 1957.

A desired objective of economists is to formulate a "social welfare function." This function—the relationship between the well-being of the society at large and the utility of the individuals comprising that society—would determine the best possible social situation stemming from individual rankings of alternatives. Is it possible to achieve a social situation that satisfies all individuals? What does this achievement entail? Arrow endeavored to achieve this objective under minimal ethical conditions: the function should include all the possible orderings, decisions should be coherent, and no individual would have a privileged position in determining the solution. Arrow's conclusion was that this social ordering was logically impossible. The result, called Arrow impossibility theorem, was part of his doctoral dissertation at Columbia—published in 1951 as *Social Choice and Individual Values*—which states that it is impossible to formulate a social preference order corresponding to individual rankings satisfying a set of minimal acceptable conditions. Instead, it seems plausible for Arrow that a "dictator" imposing an order of preferences is required. This conclusion gave rise to a lot of academic work on welfare economics. Amartya Sen's "Paradox of Impossibility of a Liberal Paretian," which states that it is impossible to obtain an acceptable distribution on the basis of liberal minimal conditions, constitutes an example of this line of inquiry.

As stated above, Arrow also contributes to the economics of information. Although neoclassical economic theory is based on the presupposition of complete information for every economic agent, actually different individuals have often unequal knowledge of relevant information. This situation of "asymmetric information" engenders a number of problems to economics: misguiding incentives and decisions and the generation of unnecessary or avoidable costs—for example, the setting of wages in labor markets and employer's preferences for the existing employees (productivity levels of potential employees is unknown to the employer). Asymmetric information before a contract is signed is called "adverse selection," and after contracts, "moral hazard." A typical example of moral hazard is the negligible behavior of insured car drivers. The insurance company ends up with an adverse selection of people and rising the premium for all kind of consumers. A nonoptimal allocation of resources results from this divergence between the private marginal cost of an action and the social marginal cost of the same action. This notion of moral hazard was developed by Arrow in a 1963 paper about medical insurance.

Arrow has always expressed a concern for the ethical aspects of economics. This concern always reflected the kind of topics he addressed (i.e., welfare economics, information problems). He advocates for an ethical repair of market failures.

It is impossible to encompass all his outstanding, thought-provoking, and pathbreaking contributions in a short entry. He is one of the most fruitful and respected living economists.

—Ricardo F. Crespo

See also Arrow's Impossibility Theorem; Asymmetric Information; Equilibrium; Methodological Individualism; Moral Hazard; Public Choice Theory; Welfare Economics

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Arrow's Impossibility Theorem

Arrow's impossibility theorem is a proposition that it may be impossible to create a consistent collective decision-making rule. Consistent collective decision making treats individuals fairly and equitably and increases the likelihood that people will accept the outcome of a social decision. The theorem provides insights into the complexities of social decision making and the difficulties inherent in improving the voting process.

Difficulty in achieving consistent collective decisions is particularly evident when society is made up of more than one person and there are at least three choices being considered. Nobel Prize–winning economist Kenneth Arrow postulates that a voting scheme should satisfy six exhaustive axioms. First, the voting scheme should produce the same result regardless of the configuration of individual voter preferences. If pairwise voting (Choice A vs. Choice B, and the winner goes up against Choice C) is used, a different result may occur depending on which vote is held first (A vs. B or B vs. C).

This voting process may not lead to a single result if the pairwise voting process is allowed to go on indefinitely. This vote cycling is often referred to as the "paradox of voting." If the voting process is not allowed to go on indefinitely, the one who sets the agenda (voting order) may be able to manipulate the outcome of the election. Neither scenario is desirable for group decision making.

Second, the voting rule should be able to rank all outcomes at the end of the voting process. Third, the ranking of outcomes should be responsive to the individuals in society. Social welfare must be a function of the welfare of the individual in society. Fourth, the outcome of the vote should not violate the law of transitivity. If Choice A is socially preferred to Choice B and B is preferred to C, then A should also be preferred to C. The social voting rule should produce a consistent outcome. Fifth, the outcome should be independent of irrelevant alternatives. If society is ranking Choices A, B, and C, only individual preferences of A, B, and C are relevant. Where individuals would rank Choice D is irrelevant because it is not included in the vote. Preferences concerning Choice D should not influence the vote on Choices A, B, and C. Last, the voting rule should not be solely based on the preferences of one individual in society. The social welfare function should not be determined by a dictator.

Each of these axioms is intuitively pleasing and seems very reasonable. A voting rule that satisfies all these criteria would most likely be accepted by society. However, when grouped together these axioms imply that it is unlikely that a society would be able to create a consistent decision-making rule. The results of collective decisions cannot be expected to be as consistent as the results of individual decisions. Social decision-making consistency is only possible for some patterns of individual preferences. For example, if all voters have identical preferences for Choices A, B, and C, a voting rule is likely to produce consistent results. According to the theorem, it is not completely impossible for consistent decisions to be made collectively, it is just highly unlikely.

A body of academic literature has evolved as a result of Arrow's work. Social scientists have given mathematical proofs of the theorem and have written papers on the implications of possibly relaxing one or more of the criteria. A collective decision-making rule has not been developed that can stand up to all the axioms of the theorem. It is widely accepted that majority (the winning choice has more than 50% of the votes) and plurality (the winning choice has more votes than the other choices) voting are very good ways to make social decisions. Kenneth Arrow and John Hicks shared the 1972 Bank of Sweden Prize in Economic Science in Memory of Alfred Nobel for their contributions to general economic equilibrium theory and welfare theory.

Welfare theory is a branch of economic theory where resource allocations are assessed. Resource allocation simply means "who gets what" in society. Positive theory is concerned with how an economy operates, while normative (welfare) theory is concerned with what should be. The findings of welfare theorists can be used to establish criteria for government intervention in private markets and for the establishment of mechanisms for making collective decisions. Arrow's impossibility theorem helps social scientists better understand the voting process. The theorem indicates difficulty for economists attempting to create a social welfare function, as ranking alternatives often appears to be impossible for society as a whole. This well-known theorem has found applications in mathematics, political science, and many subfields of economics such as public finance and public choice theory.

Arrow's impossibility theorem is not a condemnation of the democratic process. It is not correct to conclude that the theorem implies that all voting methods are fundamentally unfair and that a dictatorship is the best way to make collective decisions. While a dictatorship may be able to produce consistent results, it is generally not considered preferable to majority voting or other voting schemes. In fact, a lack of unanimity may lead to political debate where alternatives can be tested. Inconsistency may be good for the political process, even though someone will always be disappointed by a collective decision. The theorem points out fundamental difficulties in trying to make improvement in our current voting processes. Arrow's impossibility theorem gives insight into the complexities of collective decision making.

—Charles Kroncke

See also Arrow, Kenneth; Normative Theory Versus Positive Theory; Public Choice Theory; Resource Allocation; Welfare Economics

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Arthur Andersen

Arthur Andersen was the largest public accounting firm in the 1990s, with more than 85,000 employees operating in 84 countries. During the last decade of the partnership's life, auditors at several regional offices failed to detect, ignored, or approved accounting frauds for large clients paying lucrative consulting fees, including Enron and WorldCom. In 2002, the partnership was found guilty of obstruction of justice for destroying documents related to the Enron audit, a decision later unanimously overturned by the United States Supreme Court.

Consulting Schemes

For more than half a century, Arthur Andersen, founded in 1913 by Arthur Andersen, who had a reputation for acting with integrity, was primarily an auditing firm focused on providing high-quality standardized audits. But a shift in emphasis during the 1970s pitted a new generation of auditors advocating for clients and consulting fees against traditional auditors demanding more complex auditing techniques. The problem worsened when Andersen's consulting division began generating significantly higher profits per employee than the auditing division. Auditing revenues had flattened and growth came primarily through consulting fees. Consulting schemes publicly praised by Andersen partners included the following:

- Using highly qualified consultants from other regional offices to market their services during client presentations and then not including them on the project team after the contract was obtained
- Determining the client's budget for consulting services and then selling as many consulting services as possible up to that budget limit, even if the services were unnecessary
- Charging clients a partner's high billable hour rate and then assigning most of the work to lower paid, and less qualified, staff

The Enron Audit

The combination of more complex financial statements, more aggressive accounting techniques, greater concern for customer satisfaction, greater dependence on consulting fees, and smaller cost-effective sampling techniques created many problems for auditing firms. Andersen's Houston office was billing Enron $1 million a week for auditing and consulting services, and David Duncan, the lead auditor, had an annual performance goal of 20% increase in sales. Duncan favorably reviewed the work of Rick Causey, Enron's chief accounting officer and Duncan's former colleague at Andersen. Duncan let Enron employees intimidate Andersen auditors, such as locking an Andersen auditor in a room until he produced a letter supporting a $270 million tax credit. Andrew Fastow, Enron's chief financial officer, successfully lobbied for the removal of an Andersen accountant for questioning his aggressive accounting schemes.

The Indictment

In June 2001, the Securities and Exchange Commission (SEC) issued a cease-and-desist order against Andersen regarding any securities violations for its role in a $1.7 billion accounting fraud at Waste Management. Andersen partners were forewarned that any future violation would result in an extreme penalty from the Justice Department.

By late September 2001, Enron insiders knew the firm would publicly announce on October 16 a third-quarter operating loss, its first ever, along with an after-tax nonrecurring charge of more than $1 billion. Both Enron and Arthur Andersen went into a crisis management mode to prepare for an anticipated SEC investigation. On October 12, Andersen's in-house lawyer requested that the director of Andersen's Houston office comply with the company's documentation retention policy—all extraneous documents should be destroyed.

As expected, the SEC requested Enron audit information on October 17. Six days later, Duncan ordered his audit team to destroy documents at a pace quicker than required by the documentation retention policy. Within 3 days, an unprecedented amount of material had been shredded, and e-mails and computer files deleted, in Houston and several other regional offices. The shredding stopped on November 8 when the SEC formally subpoenaed Andersen for Enron-related material.

CEO Joseph Berardino immediately notified the SEC on finding out about the excessive document shredding, and he fired Duncan following the public uproar. Andersen's response was considered inadequate given that three other major corporations for whom Andersen recently issued unqualified or clean audit opinions—Global Crossing, WorldCom, and Qwest—were either being investigated by the SEC, drastically restating previous financial statements, or abruptly declaring bankruptcy.

On March 14, 2002, the Justice Department indicted Andersen for obstruction of justice. Clients wanting to ensure investors that their financial statements could meet the highest accounting standards abandoned Andersen for its competitors. They were soon followed by Andersen employees and entire offices. Berardino was forced to resign and 4,000 employees were laid off.

In early April, Duncan pleaded guilty to one felony count of obstruction of justice. Andersen requested and received a speedy trial because of the mass client defection. On June 15, 2002, Arthur Andersen was found guilty of shredding evidence and lost its license to engage in public accounting. Three years later, Andersen lawyers successfully convinced the United States Supreme Court to unanimously overturn the obstruction of justice verdict based on faulty jury instructions. But by then there was nothing left of the firm beyond 200 employees managing its lawsuits.

—Denis Collins

See also Accounting, Ethics of; Conflict of Interest; Enron Corporation; Fraud; Manipulation, Financial; Sarbanes-Oxley Act of 2002, WorldCom

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Aspen Institute's Business and Society Program

As a highly visible part of the Aspen Institute—a global forum and cultural institution gathering leaders in reflection and dialogue to create enlightened policy and practices—the Business and Society Program seeks to develop business leaders for a sustainable global society. Since 1999, through its seminars, research, awards, and publications, the Program has sought to disseminate information, promote change, and develop leaders and networks in business and society.

The Program's Web sites provide sources of innovative curriculum, notably through www.caseplace.org and www.beyondgreypinstripes.org. *CasePlace.org* is a free, online service for business school faculty, students, and businesses. It provides some of the best cases, references, and commentary published by and for business educators and business executives. Materials incorporate social impact management (the field of inquiry examining interdependency between business needs and societal concerns), corporate social responsibility, and business ethics.

Beyond Grey Pinstripes is a joint project between the Business and Society Program and The World Resources Institute (WRI), which in 1998 created *Grey Pinstripes with Green Ties*, a report that examined the inclusion of environmental management topics in 37 MBA programs. In 1999, WRI partnered with the Aspen Institute's Business and Society Program to balance the report by examining MBA programs for the teaching of social impact management. Today, *Beyond Grey Pinstripes* has grown in influence and has been used by tens of thousands of students, academics, and major corporations. The current Web site contains detailed information on 130+ global MBA programs. It is the only global survey that evaluates MBA programs for their efforts to prepare graduates on social and environmental stewardship in business. This biennial publication accounts for the majority of articles and press releases about the Business and Society Program. The most recent edition was published in 2005 and notes that an increasing number of schools surveyed (54%, up from 34% in 2003) require one or more courses in ethics, sustainability, business and society, or corporate social responsibility.

In addition to rating leading MBA programs, *Beyond Grey Pinstripes* also identifies "Faculty Pioneers." These are exceptional scholars and excellent teachers (one includes *Encyclopedia* editor Sandra Waddock) who are leading the way in incorporating social and environmental issues into their teaching and research both on and off campus. Faculty are nominated by their peers and selected from a pool of finalists by a panel of corporate judges.

As one of 15 policy programs supported by the Aspen Institute, the Business and Society Program periodically explores topics of current interest and importance, in service to the larger Institute's mission of lifting people out of their usual selves. Some critics of the Aspen Institute consider it more of a social club for the cultural and corporate elite. This charge comes from the Institute's heritage, as a "hobby" of wealthy Chicago businessman Walter Paepcke (1896–1960), who was influenced by the University of Chicago's Great Books program and the humanism inspired by the work of Professor Mortimer J. Adler. Paepcke was a believer in the necessity of business leaders to have time out from commerce to contemplate values and experience the broadening power of the arts. The Aspen Institute is currently managed by Walter Isaacson, noted author and former CEO of CNN and managing editor of *Time* magazine, who exemplifies the Institute's continuing interest in harmonizing business and ethics. A mixture of political and corporate leaders continues to manage the Institute, including Madeleine Albright, Jack Valenti, Henry Kissinger, Micheal Eisner, and Brent Scowcroft. With values training seminars, 1-week in duration, costing almost $10,000, the Institute reaches top-tier business and political leaders but must contend with charges of elitism. By working with university faculty and graduate students, the Aspen Institute's Business and Society Program seeks to provide practical services to balance the more esoteric gatherings at its Aspen and Wye River, Maryland, campuses.

In addition to its case Web site and Beyond Grey Pinstripes study, the Business and Society Program conducted a multiyear survey of 1,700 MBA students at 12 leading international schools of business. The study published in 2003 as *Where Will They Lead?* examined student attitudes about the role of business in society. Another effort was the Corporate Governance and Accountability Project, a study of prevailing models of corporate governance and theories of the firm as taught by business school faculty. The Program was formerly known as The Aspen Institute's Initiative for Social Innovation through Business.

—*LeeAnne G. Kryder*

See also Business Ethics Research Centers; Business for Social Responsibility (BSR); Corporate Citizenship; Corporate Governance; Corporate Social Responsibility (CSR) and Corporate Social Performance (CSP); Ethical Role of the Manager; Global Business Citizenship; Humanities and Business Ethics; Leadership; Management, Ethics of; Virtue and Leadership

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Association for Computing Machinery (ACM)

The Association for Computing Machinery (ACM) was founded on September 15, 1947, as an organization for computer and information professionals. At that time, there was growing interest in the commercial applications of both mechanical and digital computers, although there was little more than speculation that computing technology would become a primary means of global change within the following 50 years.

The ACM publishes an academic journal, *Journal of the ACM*, which was a primary outlet for computer science research. The group also publishes several magazines for practitioners and students.

Another function of this organization was to promulgate a set of professional standards as the discipline of computer science grew into a plethora of subdisciplines, including software engineering, information security, and others. The organization has 34 special interest groups (SIGs), each devoted to a specific area of practice. There is a strong emphasis and focus on computer hardware and end-user applications. Several of these SIGs hold annual conferences, which have become important venues for presenting research and innovations in related fields. Several of these fields each have an ACM academic journal. These are called the *Transactions.*

At the association's founding, computing technology had already been used as a powerful military weapon. Computer scientists in the United States, the United Kingdom, and Germany had participated in a variety of projects to develop faster, more reliable automated equipment for use in cryptography, ballistics, weapons targeting, and other military applications. Computing technology allowed the bureaucracies of the industrialized world's governments to process and store far more information than ever before, more accurately, and at less cost.

On October 16, 1992, the ACM Council adopted a code of ethics and professional conduct, which was developed by a task force of 13 members. (This document replaced a previous code of professional conduct, which was adopted by the ACM in 1982.) The primary purpose of the ACM Code is educational. Thus, the code is normative, with a strong emphasis on deontology and stakeholder theory. The 1992 Code contains 24 statements of personal responsibility for information professionals. These statements are presented as moral imperatives and distributed in four sections: general imperatives, specific imperatives, leadership imperatives, and compliance imperatives.

The general imperatives focus on basic obligations to society. In many ways these principles draw from common laws and professional norms, including intellectual property, trust, privacy, and the avoidance of both personal harm and discrimination.

The second section provides more specific rules for addressing the previous section, including the need for professional competency. The ongoing review of work and performance is a critical area. This includes a professional obligation to honor contracts and agreements.

The third section drew heavily from a draft version of the International Federation for Information Processing (IFIP) Code of Ethics. The imperatives for organizational leadership emphasize the duties of executives, managers, and leaders. At the heart of this section is the tension between the limitations and possible uses of computer systems. Users must understand and abide by a statement of acceptable practices that is specific to the organization and its external environment. A special emphasis is placed on the dignity of users and anyone who is affected by each computing system. In this regard, the code appears to acknowledge a stakeholder view of professional and social responsibility.

The final section addresses the voluntary nature of the Code. Members of the association pledge to abide by its imperatives and to support other members and professionals in their own compliance efforts.

—William A. Sodeman

See also Business Ethics; Codes of Conduct, Ethical and Professional; Deontological Ethical Systems; Normative Ethics; Stakeholder Theory

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Association of Community Organizations for Reform Now (ACORN)

The Association of Community Organizations for Reform Now (ACORN) is an independent grassroots network of neighborhood organizations whose members engage in direct action to win political, social, and economic benefits for low- and moderate-income people in communities throughout the United States. While many advocacy groups appeal to a single constituency or focus on a single issue, ACORN is committed to organizing communities around a variety of issues. Whether fighting for better schools, affordable housing, new libraries, or more favorable banking practices, they identify winnable goals that have broad appeal across racial, gender, geographic, economic, political, or employment status boundaries. Using an approach that combines electioneering, legislative lobbying, legal action, peaceful protest, and in-your-face confrontation, their coalitions fight for, and often win, tangible benefits for their members and their communities.

Critics of ACORN contend that ACORN's tactics are counterproductive and that they are motivated by a left-wing political agenda that is out of step with the communities that they represent. In addition, in March 2003, the National Labor Relations Board found ACORN in violation of some of the same labor laws that they challenge in other organizations.

ACORN is structured into local chapters, which are democratically run by dues-paying members. Leaders are elected to fill roles in community, city, state, and national ACORN offices. The national president of ACORN since 1990 has been Maude Hurd.

Chapter members identify local issues that people care about and around which they can organize. ACORN staff members do not select community-organizing goals.

Seventy-five percent of all funding comes from members and from member activities, including dues and fund-raising events. ACORN also accepts government funding for specific community programs.

History, Growth, and the *People's Platform*

ACORN grew as an offshoot of the National Welfare Rights Organization (NWRO). The NWRO leadership realized that, as a single-issue organization, they would be unable to organize broader constituencies to obtain a wider array of benefits. With the support of the NWRO leadership, community organizer Wade Rathke founded ACORN in 1970 as the Arkansas Community Organizations for Reform Now.

ACORN expanded beyond Arkansas in 1975 by adding offices in Texas and South Dakota, and by 1980, they had opened offices in 20 states. In 2004, ACORN opened their first international offices in Canada and Peru, and in 2005, they opened additional offices in Mexico and the Dominican Republic. At the time of this writing, ACORN reports that there are 175,000 member families in 850 neighborhood chapters in 75 cities throughout the United States. ACORN continues to add offices and chapters both inside and outside the United States.

In 1979, ACORN adopted their *People's Platform.* The *Platform* is both a vision statement and a detailed list of goals and demands. The *Platform* addresses affordable housing, living wages, accessible health care, better schools, fair utility pricing, the preservation of family farms and family owned businesses, community development, tax relief, industrial and toxic waste cleanup, safe neighborhoods, civil rights, communication rights, community representation in government, and community representation in big business. More recently, ACORN has added immigrant rights to their list of goals and demands.

Through the years, ACORN has created or affiliated with a number of allied organizations. The ACORN Housing Corporation, founded in 1986, builds or restores housing in low-income neighborhoods. The Living Wage Resource Center promotes and supports the living wage movement. Project Vote registers low-income people to vote.

While remaining true to their roots in community organizing, ACORN leaders also organize state and national campaigns around issues that affect all communities. Issues such as fair taxation, living wages, and social security protection are better suited for political action directed at higher levels of government.

ACORN and Business

Early in ACORN's history, the primary targets of their actions were governmental agencies. Over the years, they have also found fertile ground in organizing challenges to corporate activities that they judge to be unfair or abusive.

For example, ACORN has used protests, regulatory challenges, and class action lawsuits to attack predatory lending practices. Loans are considered predatory when lending institutions offer only higher-interest loans to people whose credit histories would justify more favorable terms. Minorities and people living in poor or transitional neighborhoods are often victims of predatory lending. ACORN brought and settled a class action suit against Household Finance in 2003. In 2004, they reached an agreement with Citigroup for fair banking and credit services for low-income households. They also helped to pass California's Predatory Lending Law in September 2001 and similar legislation in other states as well. ACORN continues to pursue legislative protections and legal remedies to challenge predatory lending practices by banks and other lenders.

ACORN also challenged predatory practices associated with refund anticipation loans (RALs). RALs are short-term loans, secured by an income tax refund, commonly offered by tax preparation services. The fees associated with RALs can be several hundred percent when calculated as an annualized effective loan rate. In 2005, ACORN reached an agreement with tax services company H&R Block for better disclosure and reduced fees. They are currently pursuing similar action against other tax preparation companies.

ACORN does not always have to challenge a business practice to win benefits for their communities. In 2005, the Forrest City Ratner Companies (FCRC) enlisted the support of ACORN in the early planning stages of a mixed-use real estate development project in

Brooklyn, New York. As part of their plan, FCRC guaranteed thousands of low- and middle-income housing units, jobs and job training, minority development contracts, and community use of a new professional basketball arena. By addressing ACORN's concerns early in the planning stages, the FCRC proposal received ACORN's endorsement.

Criticism

Several critics remind us that ACORN's roots lie within a left-wing ideology. Even today, the *People's Platform* speaks about the struggle of the masses to share the wealth. Yet, at the same time, ACORN coalitions are composed of people across the political spectrum.

By drawing attention to class differences and making a direct challenge to American political and economic institutions, these critics argue that ACORN's rhetoric may be seen as divisive, not embracing. Conservative participants in ACORN coalitions may participate only to the extent that the action benefits them and addresses their local issues. Critics also wonder what would happen if a local chapter pursued a conservative agenda that was out of line with ACORN's ideals.

In its defense, ACORN does manage to form and maintain coalitions, one issue at a time, and win benefits for their communities. However, the potential conflict between ACORN's goal-oriented activism and their left-wing ideals should not be overlooked.

—Steven Birnbaum

See also Boycotts; Consumer Activism; Nonprofit Organizations; Predatory Pricing and Trading; Public Interest; Social Activists

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Association of Trial Lawyers of America (ATLA)

As the world's largest trial bar, the Association of Trial Lawyers of America (ATLA) is a broad-based, international organization of attorneys, judges, law professors, paralegals, and law students. The ATLA is dedicated to promoting justice and fairness for injured persons, safeguarding victims' rights (especially through the right to trial by jury), and improving the civil legal system through education and disclosure of the information to the public.

Started in 1946 by a group of plaintiffs' attorneys involved in workers' compensation litigation, the then named National Association of Claimants' Compensation Attorneys (NACCA) was founded to protect the rights of victims of industrial accidents. Shortly thereafter, the NACCA attracted personal injury, admiralty, and railroad lawyers, eventually opening the organization to all areas of trial advocacy.

With continued growth and expansion of its advocacy, the NACCA changed its name to ATLA in 1972 to reflect the broadening membership base. In 1977, ATLA moved its headquarters from Boston to Washington, D.C., to more effectively lobby and advocate on behalf of its membership. With approximately 60,000 members worldwide, ATLA provides attorneys with information and professional assistance to better serve their clients successfully in trial advocacy and support ATLA's goal of protecting the democratic values inherent in the civil justice system. ATLA is a voluntary professional organization governed by the membership.

In recent years, ATLA has become one of the most influential and well-funded political lobbying groups in the country. ATLA is very active in the legislative arena on behalf of matters of concern to its members and their clients, focusing primarily (but hardly exclusively) in the area of tort and judicial reform. ATLA is major contributor to politicians and political campaigns, especially to those in the Democratic Party.

—Stephen R. Martin II

See also American Bar Association; Campaign Finance Laws; Litigation, Civil

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Association to Advance Collegiate Schools of Business (AACSB International)

AACSB International, the Association to Advance Collegiate Schools of Business (formerly American Assembly of Collegiate Schools of Business), is a not-for-profit corporation of educational institutions, corporations, and other organizations devoted to the promotion and improvement of higher education in business administration and accounting. AACSB, which is the oldest and largest business accreditation organization, was founded in 1916 by the deans of 17 business schools in an effort to establish and maintain minimum accreditation standards. In 1980, to address the needs of the accounting profession, AACSB adopted additional standards for undergraduate and graduate degree programs in accountancy.

Many business school constituents have continually criticized the AACSB for not enforcing standards relating to public policy, moral philosophy, social values, and other humanities in curriculum development. In 1925, the first detailed AACSB curriculum standards were approved, requiring a reasonable amount of work in at least five groups of study, including business law. In 1949, new standards required that at least 40%, but not more than 60%, of a student's education consist of nonbusiness courses. Critics of the AACSB argued that too many business programs violated this standard and that the educational requirements of humanities were inadequate.

Going into the 1960s, the business school reform movement called for increased business and society study because business students needed to understand the connection between business and nonbusiness studies. Both the Ford and Carnegie Foundations maintained that the content of business law courses, intended to inform students of the broader societal concerns, was too narrow. The Ford Foundation recommended that the business law course be replaced with a course that taught the legal environment of business or a more broad-based course that dealt with the social, political, and other dimensions of business environment. The Carnegie report recommended that business law be replaced with a class about political and legal factors of business in addition to six credits in business policy and social responsibilities. In 1967, the AACSB revised its standards requiring business programs to include in their curriculum the economic and legal environment issues and social and political influences that affect both profit and nonprofit organizations. In 1974, this standard was expanded to include ethical considerations. As a result, the teaching of business and society topics became a growth activity throughout the 1970s and into the 1980s.

The loss of public confidence as a result of corporate scandals of the early 2000s renewed the demand for ethics education. Despite the growing support by constituents to require stand-alone ethics coursework, AACSB failed to require it in the accreditation standards adopted in 2003 and revised in 2005. Ethics continues to be excluded from the list of accredited subjects. Accredited institutions can choose to address the subject matter by either incorporating it in other required coursework or as a separate course.

—Lois S. Mahoney

See also Business Ethics; Business for Social Responsibility (BSR)

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Asymmetric Information

Neoclassical economics is founded on the assumptions of complete and symmetric information. Information is complete when all parties to a transaction know, or have access to, all information that ought to be relevant to their activities. Information is symmetric when all parties know all relevant information possessed by others involved in an exchange. However, most economic activities involve some failure to meet these conditions. People often do not possess full information related to decisions they make, and more important, some people usually have better information than others. When two or more individuals interact, asymmetric information exists when at least one individual possesses relevant knowledge that others do not have. Asymmetric information pertains only to situations involving interactions of two or more people.

Asymmetric information is best understood in the context of an exchange between buyers and sellers. A classic example involves the selling of a used car. The owner of the car knows its quality, but the buyer does not. If it is difficult, costly, or even impossible for a buyer to determine the quality of the car, then we say the seller possesses private information. Asymmetric information is a problem because people who possess the superior information may have an incentive to intentionally misrepresent the product and defraud others, while people who do not possess the superior information may incur costs trying to obtain better information or to protect themselves from being harmed. For example, in the case of used cars, the seller might try to convince the buyer that the car is of better quality than it actually is to obtain a higher price for the car. Knowing this, the buyer might pay a mechanic to inspect the car; or the buyer might hire a lawyer to draft a bill of sale that stipulates that the seller is obligated to issue a refund to the buyer if serious mechanical problems arise with the car within a stated period of time.

There are several reasons why asymmetric information exists. First, acquiring information is costly. This is because it usually takes time to search for and identify relevant information. Thus, some people may find that the cost of acquiring information may not be worth the expected benefits from possessing it. Second, some information is difficult to transfer, such as scientific knowledge or firm-specific knowledge. Knowledge is difficult to transfer if it cannot be easily quantified or articulated explicitly. Related to this is the fact that people are boundedly rational, meaning they have a limited capacity of acquiring, processing, and storing information. People are also forgetful. Thus, even if information were freely available, cognitive limitations will prevent people from being able to integrate all relevant information into the decisions they make. The implication is that some people will inevitably have better or more complete information than others possess.

Asymmetric Information Problems Manifested as Adverse Selection or Moral Hazard

Asymmetric information problems can arise either before or after an exchange is established. *Adverse selection* is the term used to describe problems of asymmetric information arising before an exchange occurs. *Moral hazard* is the term used to describe problems of asymmetric information occurring after an exchange is established.

Adverse Selection

Adverse selection is the process by which bad products or outcomes are "selected," and it occurs when people opportunistically exploit private information they possess. The classic study on adverse selection is by the Nobel Prize–winning economist George Akerlof (1940–). In his article, "The Market for Lemons," Akerlof elaborates on the problem of buying and selling used cars. The term *lemon* refers to a defective car. Akerlof argues that if a used car market consists of good cars and lemons, and if sellers have private information about car quality, then buyers would be willing to pay at best a price equal to the average quality of cars. Because an average price is less than the value of good cars, owners of good cars might pull out of the market, resulting in a market that either collapses or consists only of lemons.

Another example Akerlof offers is medical insurance for people aged more than 65 years. Companies offering medical insurance do not know the true health risks of applicants, but applicants know their personal medical conditions. That is, buyers of medical insurance possess private information. Therefore, insurance companies would offer a price for insurance reflecting average health risks of applicants. People who believe they are relatively healthy may find this average price too high and opt out of the medical insurance market. As healthy people begin to do this, the average health risk of applicants increases. This causes the insurance company to increase premiums, resulting in even more people seeking to self-insure. The result is that the cost of medical insurance becomes so large that no medical insurance sales take place for people over age 65. As a contrast, Akerlof says the market for group insurance for employed workers functions because there is no asymmetric information. If health is a precondition for employment, then medical insurance companies will know that people who are employed are relatively healthy. As a result, they can offer prices for their policies that are low enough for the healthy and employed to be willing to pay. Akerlof suggests that his "lemons principle" provides an insight into the true cost of dishonesty. If sellers can either honestly represent or misrepresent their products, or if buyers can either honestly represent or misrepresent their true types, then dishonest dealings tend to drive honest dealings out of the market.

Because the root problem of adverse selection is information asymmetry, solutions generally involve some form of either signaling or screening. Signaling is the process by which people with superior information credibly communicate their true types to others. Screening is the process by which people without superior information infer the true types of others based on their observed behavior. For example, education can be an effective signaling and screening device. Suppose employers want to hire hardworking employees, but they cannot determine which workers who apply for employment will work hard and which applicants will shirk. According to Akerlof's lemons principle, employers would only be willing to offer a wage reflecting the average quality of workers, resulting in hardworking applicants withdrawing from the labor force, because these workers would find this average wage less than what they believe they are worth. However, suppose applicants who would have been hardworking employees could take an action that signals their true quality, such as earning a college degree. If a college education is challenging enough so that shirking workers would be unable or unwilling to complete a college degree, then a college education would be an effective signal of worker quality in this sense: People who have college degrees are expected to be hard workers, while those without them are not. Employers can infer which workers would work hard and which would shirk by observing whether applicants have a college degree. Moreover, employers could screen job applicants by requiring a college degree or by hiring workers who obtain college degrees from certain universities.

Moral Hazard

Moral hazard refers to the risk one party carries because of the behavior of others. Like adverse selection, it exists because of asymmetric information. Moral hazard occurs when, after an exchange takes place, one party to the exchange changes his or her behavior or acquires information unbeknownst to the other party, thus increasing risk for the other party. For instance, without an insurance policy, drivers must bear the full cost of an auto accident. This will usually give them an incentive to drive carefully. However, if drivers purchase an auto accident insurance policy that pays in the event of an accident, they will have less of an incentive to drive carefully, thus increasing risk to the insurance providers. Another example occurs in employment. People who are paid a fixed salary may have less incentive to work hard than people who are paid on commission, thus affecting the productivity of the employer.

Moral hazard problems are manifested as consequences of hidden action or hidden information. Hidden action refers to situations in which the person taking an action knows what the action is, but those affected by the action cannot observe or infer at low cost what the action is. The insurance and employment examples are representative. In the case of insurance, insured drivers know if and how their behavior changes as a result of the insurance policy and, most important, if an auto accident is a result of careless driving. The insurance company, however, might not be able to determine if an accident is the result of chance or careless driving. In the case of employment, an employer might not know if the poor performance of workers is the result of shirking or other factors outside of their control, but workers would know how hard they work.

Hidden information refers to situations in which people who have entered into an agreement acquire specialized knowledge as a result of completing their duties that would be valuable to their trading partners. For example, lawyers, physicians, and accountants will often learn information that would be beneficial to their clients because of the work they perform for them. Similarly, persons in sales might learn about market conditions or the activities of competitors, knowledge that would be valuable to their employers. Hidden information is a problem because persons with the private knowledge might have an incentive either to fail to fully or truthfully disclose knowledge they have to others who may be entitled to that knowledge or to use that knowledge for their own benefit at the expense of others. For example, physicians might know the true health of their patients but may order unnecessary medical tests or procedures that benefit them financially, or accountants and auditors might know the true financial status of a corporation but report false or misleading information to affect stock prices.

Asymmetric Information and Ethical Behavior

Asymmetric information is at the heart of most unethical behavior in business. Whether manifested as adverse selection or moral hazard, people who possess superior information will often have an incentive to use their private knowledge for their own benefit at the expense of others. Insider trading, corporate accounting scandals, deceptive advertising, shirking, and employee theft are examples of problems that arise in business because some people possess or have access to private information.

Ethical problems arising from asymmetric information are not just confined to business, however. They pervade all aspects of life. Family, social, and political life are often disrupted or complicated because people take advantage of or fail to disclose relevant, private information. For example, consider the case of courtship and marriage. Presumably, potential marriage partners want to find the best person they can marry. Courtship is a time in which potential partners learn about each other. However, partners are often reluctant to disclose all information about themselves or their past, such as how many previous partners they may have had or what illicit behaviors they may have participated in as a youth. Marital strife and even divorce can result when partners learn things about their spouses that they did not know about before marriage. In the case of politics, many people have a cynical view of politicians. The reason is in part related to the problem of asymmetric information. People know that politicians possess information that the average citizen does not, and people believe that many politicians use that information to enrich themselves at the expense of the tax-paying public.

If asymmetric information is at the heart of unethical behavior, then solutions to unethical conduct involve efforts to create private and public institutions that attempt to make that information more public, symmetric, and transparent. Examples of such institutions include private investigators, government regulators, and rules regarding the disclosure of financial information by companies. When private information is transparent, the incentive to exploit such information is often reduced or eliminated. All said, when asymmetric information persists, principles of ethics suggest that people ought not to use private information they possess to benefit themselves at the expense of others.

—Harvey S. James, Jr.

See also Adverse Selection; Bounded Rationality; Incentive Compatibility; Information Costs; Moral Hazard; Perfect Markets and Market Imperfections; Signaling; Transparency

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Auction Market

Auctions are a form of trade, a mechanism to match a buyer and seller for any item of value. The valuation of items is usually subjective and is usually achieved through a bidding process that finally ends after the last bid is accepted by the seller. Historical evidence suggests that auctions have been around for about 10,000 years. Auctions have been used to sell items to consumers, auction off assets such as treasury bonds and transmission bandwidths, and for many other types of sales. An auction market is a place for off-line auctions or a virtual space for online auctions that facilitates auctions.

The main function of a good auction market is to facilitate an efficient and fair trade. *Efficiency* could be defined as generating the best valuation for the seller with the least cost of the auction process itself. *Fairness* could be defined as eliminating any advantage to buyer(s) or seller(s) that could be derived through a variety of unethical, illegal, and other means. Over the long history of auction markets, many different auction mechanisms have been designed to increase efficiency and fairness. Different types of auction markets (or mechanisms) and efficiency and fairness issues related to those are presented next.

The number of identical items for sale, number of sellers, and number of buyers are the factors that are relevant in designing appropriate auction markets. For example, if all the items being sold are one-of-a-kind items, and the auction has multiple buyers and one seller, we will have a traditional *English auction.* Here, each bidder would successfully bid higher and the final price is settled once there are no more bids. If the seller has several of the same items the auction would be a *Dutch auction*, where the bidders will still continue to bid higher and higher. However, in this auction, the bidders will have the choice of indicating the number of items they are committed to buy at their price. If there are many sellers and a single buyer the auction results in a *reverse auction.* For example, a state government interested in buying aluminum sheet could invite several sellers to the auction, the sellers bid against each other by continually lowering their sales price and the final price is reached when there are no more bidders at a lower price.

Auctions can also be *open bid*, where everyone in the market knows the value of the bids of other participants, or *closed bid*, where the bids are not disclosed. Auctions can also be classified based on the type of participants as consumer to consumer, business to consumer, government to business, and so on. Auctions can also be classified as off-line or online. In an off-line auction, the most common auction before the explosive growth of the Internet, all potential buyers and the seller(s) would congregate in one location (a physical place), the buyers would examine the items being auctioned off and develop an initial valuation for the item, and then start bidding for the item at a preset time and continue to bid until there are no more bids. In contrast, online auctions are held in a virtual space on the Internet and buyers and sellers can be anywhere in the world. An example of the most successful online Internet auction market is eBay.

If a participant is purchasing an item in an auction to derive some personal value, such as buying a bottle of 100-year-old wine to consume at a special occasion, then the value of the item is considered a *private value.* However, if all the buyers perceive the same use for the item, like buying a certain transmission bandwidth for developing cell phone networks in a certain location, the value generated will be *common value.*

In any auction market the efficiency increases as more buyers and sellers participate as there will be more competition. Efficiency also increases when there is information transparency, that is, all participants have access to all the information necessary to assess the value of the items. In an open-bid auction, the information generated through the bidding process increases the efficiency. This transparency is lacking in the sealed-bid process. A variation of the sealed-bid auction is a multiple-stage process, where the bid details of each stage are revealed to all participants to improve the efficiency of the bidding process in successive stages. In eBay auctions, where there is a preset time for the closing of the auction, it is possible for the bidder with the most information about the item to wait until the last minute to start bidding. This reduces the information available to other bidders in the bidding process and leads to information asymmetry and a reduction in the efficiency of the auction market. This last-minute bidding, to obtain a valuable item for a cheaper price, is sometimes known as *sniping.* Auctions on Amazon .com compensate for this by not having a firm preset close for an auction. These auctions close only when there are no bids for a 10-minute period after the last bid before the flexible preset close time. This reduces the possibility for sniping and provides more valuation information to all participants. In some auctions, sellers may bid in their own auctions early in the bidding process to provide wrong information about the value of the items to other bidders thus potentially increasing the value of the final bid. This is called *shilling.* Some auction markets, both off-line and online, try to eliminate this unfair practice by requiring the participants to register and by monitoring for shilling activity. Inaccessibility of the auction, whether technological or otherwise, to many potential participants also results in reduced efficiency of the auction market.

With the explosion of the Internet, many successful, and possibly more efficient and fair, online auction markets have been created. The trend appears to favor growth of online auction markets.

There are some social and ethical issues that must be considered in designing auction markets. In electronic auction markets, the digital divide, the unavailability of communication and information technologies to individuals and organizations, can have a negative social impact on participants by restricting entry through unavailability and increased cost of technologies and through lack of understanding of appropriate technologies. An ethical issue that should be carefully monitored, in both off-line and online auctions, is the presence of collusion by participants to reduce the final bid price, thus decreasing the fair payoff to the seller.

—Hindupur V. Ramakrishna

See also Asymmetric Information; Collusion; Transparency; Trust

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Austrian School of Economics

The Austrian School of Economics is an economic school initiated by Carl Menger (1840–1921). Menger's first disciples were Eugen von Böhm-Bawerk (1851–1914) and Friedrich von Wieser (1851–1914). Joseph Schumpeter (1883–1950) is sometimes associated with the Austrian School. Although he was a student of the last two, he departed early from Austrian ideas. The Austrian current was continued by Ludwig von Mises (1881–1973) and Friedrich A. Hayek (1889–1992). Other representatives were Murray N. Rothbard (1926–1995), Ludwig M. Lachmann (1906–1990), and Israel M. Kirzner (1930–). The School is still alive and universally active, though concentrated mostly in the United States.

The Austrian School is more than an approach to economic theory. It also deals with matters of political philosophy, social ontology, and social science epistemology. It supposes, and sometimes explicitly speaks about, an anthropological conception. It is generally associated with classical liberalism or libertarianism, though this is not necessarily a particular trait of the Austrian School. Most Austrians are vigorous advocates of the cause of political freedom, free markets, private enterprise, and individualism. Mises and Hayek were paradigmatic in this respect. They opposed totalitarianism in all its forms. Hayek's *Road to Serfdom* (1944) is still today a necessary point of reference on this issue. They both engaged in the "socialist calculation debate," arguing that government planning cannot achieve the efficient results of a free market system.

Main Characteristics

We may summarize the characteristics of the Austrian School in five main items:

1. Economic explanations rely on human purposive action. "Purposive" means that it stems from an individual decision aiming at an end or goal—a "subjective" decision. Hence, subjectivism is a relevant trait of Austrian economics. One difference with neoclassical marginalism, stemming from Austrian subjectivism, is its stress on the opportunity cost theory: This theory emphasizes the necessarily subjective role of personal demand preferences in the determination of prices. Austrian economics refuses mathematical and mechanical explanations, considering them inadequate for dealing with purposive human actions. One consequence for businesses of this trait is that Austrians strongly support a market system absolutely free, without governmental controls.

2. Methodological individualism—the explanation of social phenomena as resulting from purposeful individual subjective actions—is the method of Austrian economics. Hayek developed this issue. A typically Austrian nuance of this perspective is depicted next.

3. Individual actions have unintended consequences. The traditionally considered unintended consequence is a tendency toward market equilibrium. However, Austrian economics does not focus on equilibrium outcomes. For Austrians the market is a process that tends toward equilibrium. These last two characteristics reinforce the relevance of freedom in economic actions in the Austrian approach.

4. A fourth trait—although arguable—is value neutrality as a condition of scientific knowledge. It was defended by Menger, Mises, and Hayek and, despite some dissent, is still defended today. This is relevant for business ethics because value neutrality entails putting aside ethical concerns within economics.

5. Specifically, economic ideas include concrete approaches to the concept of cost (as mentioned above); a theory of business cycles based on monetary overinvestment; a time-theoretic theory of interest and capital; and the special relevance of the price system for coordinating decentralized, subjective individual preferences to achieve a spontaneous and harmonious order. Kirzner has developed a theory of entrepreneurship in which entrepreneurial alertness has a significant role. For him, entrepreneurial discoveries propel the market process.

The Austrian School Versus Neoclassical Economics

From its beginnings, the Austrian School has been differentiated and opposed in several points to the neoclassical school. The causes of these differences may be found in the Austrian School's ontological, anthropological, and epistemological premises. Concerning ontology, while neoclassical economics has a determinist or closed social ontology, Austrians take an open view of society as always subjected to unexpected change. The neoclassical anthropology entails a mechanistic vision of man and of human action, while Austrians are open to freedom in a teleological conception of human action. Both schools have different epistemological assumptions appropriate to those philosophical positions. The Austrian School, rather than supporting neoclassical naturalistic or mechanistic frames, leaves room for an epistemological special framework for social sciences, where human interpretation enters the game. This has been for Austrians a source of continuous criticism of neoclassical economics.

A Nonmonolithic Doctrine

The Austrian School is not a closed system—it has been far from static. It has made room for different philosophical influences—from Aristotle to Immanuel Kant, Max Weber, Alfred Schutz, and scholastic thinkers as well. The common idea is subjectivism and a conception of all that is economic as human action. Another common trait is the search of an economy that respects individuals and their freedom from totalitarian and socialist regimes.

Austrian subjectivism has expanded since its creation. The first step was Menger's application of subjectivism to human needs. The second was the extension of subjectivism to means, while ends are given. Hayek considers the conveying problems that subjectivism has to overcome. Lachmann, following the British economist George Shackle (1903–1992), introduces hermeneutics: We do not only have information but we also have interpretation influenced by imagination and desire, as well as by rationality. This process draws on expectations and broadens rationality. Subjectivism reaches ends, which are a creative result of people's imagination, thus making the future unpredictable.

An epistemological tension within the Austrian School can be expressed in the question, "How can we explain the unpredictable?" For Kirzner, the resolution of this dilemma would become the future research program of the Austrian School. This tension has not yet been fully resolved and has prompted the development of two positions. One position prefers equilibrium over uncertainty, despite relaxing the firmness of equilibrium. The other position prefers uncertainty over equilibrium, where unintended consequences cannot be foreseen.

This last position has been challenged by the Austrian orthodoxy as being nihilistic: We cannot develop science from unpredictable or unmanageable actions or processes. We should choose: We must retain either unpredictability or coordination. We cannot have both and consider that plans coordinate unpredictable actions by the intervention of miracles. A possible solution is a profound social shaping of human beings that makes them act individually, while taking into account that they are social beings. However, this solution will be always limited because an Austrian must acknowledge the creative character of human beings. This tension between subjectivism/nihilism and coordination/scientific predictability leads

Austrians to try a solution in a position located between the absolutely open position of a radical hermeneutics and the closed position of social determinism.

Conclusion

What is the essential message of the Austrian School for business, business ethics, and society? Austrians' strong support of free markets ultimately translates into an ethical mandate. Since businesses must develop in a free market environment, the ethical principle of freedom becomes paramount.

—Ricardo F. Crespo

See also Methodological Individualism; Spontaneous Order

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AUTHENTICITY

When we refer to documents, works of art, or historical artifacts as authentic, we mean that it is the "real thing," or that it is what it claims to be. For example, to claim that a Picasso painting is authentic, art dealers would have to determine that it was truly painted by Picasso. Similarly, in providing attest services, auditors verify that a company's financial report reflects the true state of the company's financial affairs and is therefore authentic. You can see that in all these examples, when one calls something "authentic," one is making a truth claim. When it comes to attributing authenticity to a person, we also refer to the extent to which a person is true to himself or herself. This definition assumes that each individual has a unique identity and unique values and habits and that authentic persons would display these beliefs and traits in their everyday behavior. A person who claims to be honest, but conducts dishonest business activities, cannot be called authentic.

Ironically, as a result of the idea that authenticity entails "being true to yourself," it became associated with moral subjectivism. If individuals make moral decisions based solely on their own individual beliefs or interests, we lose the ability to criticize individual acts that may be considered morally problematic from the perspective of the shared values and beliefs existing in society. Charles Taylor, a communitarian, finds the roots of the individualist understanding of authenticity in the Cartesian motto of *I think therefore I am*, and traces it through the history of modern philosophy to Sartre's existentialism and the individualism found in John Locke's political philosophy. Taylor argues that it is a mistake to define authenticity in individualistic terms, because it tends to result in narcissism and self-indulgence. He argues that individuals only develop a sense of self in interaction with others in society. Beliefs derive moral significance because human beings assign value to certain things in interaction with one another. In the process, we develop shared horizons of significance, which inform individual values, beliefs, and habits. The notion of self-determining freedom to "be yourself," which is so influential in popular conceptions of authenticity, acknowledges the creative nature of individual construction of meaning, but it underestimates the importance of shared horizons of significance. Taylor points out that one cannot have a sense of self without also taking into consideration the dialogical setting within which your sense of who you want to be originates. An authentic moral response would be one that displays an awareness of how one's unique ethical response is formed by or interacts with the norms and values existing in society. For example, being an authentic auditor will therefore mean that one displays the norms and values that society associates with auditors—objectivity, veracity, due care, and so on. If one fails to display these traits, one cannot be an authentic auditor. Poststructuralism would concur with the communitarian critique of the individualism and instrumentalism that characterize modern notions of authenticity. However, poststructuralist perspectives on authenticity would depart from the communitarian dialogical understanding at various points. Heidegger's notion of authenticity differs from other definitions of authenticity in that it does not measure it in terms of a person's compliance with certain normative standards of behavior. In fact, Heidegger would argue against a representational account of values and morality in general. Representing the "moral" in terms of a set of rules, or defining it in instrumental terms, that is, whatever would facilitate a balance of benefits over harms, would be to sacrifice the possibility of an authentic life. An authentic existence in Heidegger's terms lies in the phenomenological idea of "world openness," which entails resisting the instrumental considerations that allow us to objectify and categorize everything that we encounter in our attempt to survive. We orientate ourselves toward certain end results and therefore degrade everything else as unimportant, or inessential. Authenticity entails the ability to remain open to the possibility of emergence of the world out of hiddenness. This requires a new type of openness. The characteristic mode of being that allows for this openness is that of a "lingering attentiveness," that is, pausing to consider how what we are doing or saying is both hiding and revealing certain aspects of our existence.

Heidegger's critique of instrumentalism has direct implications for the definition of business objectives. Heidegger seems to be making a strong argument against a business model that would focus only on extrinsic, instrumental motivations such as mere profit. The intrinsic value of being human beings in the world would problematize the way in which meaningful work is often defined in instrumental terms. Heidegger describes our everyday existence as filled with restlessness, which is the result of always being driven toward a specific end. He argues that, as a result, we find ourselves in a perpetual state of homesickness. We feel homesick because we no longer have access to those conditions that provide us with access to an authentic humanity.

However, business life can be a space that allows for an authentic life if it could provide the space within which an openness toward the world can be realized in and through one's everyday work. Business creates the objects and services that frame our experience in particular ways. Technologies such as jugs, bridges, cell phones, and so on can distract us from certain aspects of being in the world, or they could serve to facilitate our openness toward different modes of being. In choosing certain product lines or new services, business should consider how it may assist or hamper our authentic existence. That means giving some consideration to how these objects or concepts may facilitate a "lingering attentiveness" to what it means to be human.

—Mollie Painter-Morland

See also Accounting, Ethics of; Existentialism; Meaningful Work; Relativism, Cultural; Relativism, Moral; Truth Telling

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AUTHORITY

Authority is defined as the exercise of legitimate influence by one social actor over another. There are, of course, many ways that an actor can influence another to behave differently, and not all of them have equal claim to authority. To differentiate the term from other forms of influence, consider a simple hypothetical: Imagine that a person wielding a club forces another person to hand over his or her money and possessions. This act might be considered coercive—the exercise of brute power, which in many instances would be criminal. However, if the person with the club is a bailiff, a person occupying a legitimate role in a society, and menaces the other person in the process of repossessing goods, the act of influence may well be legitimate and constitute the exercise of authority.

This classic hypothetical illustrates the basic distinction between authority and coercion by physical force. As the psychologists French and Raven point out, however, these are only two of the common bases of social power, and the distinctions between authority and the other forms of social influence are somewhat more subtle. For example, if the person no longer held a club but instead offered the other person a toaster to hand over all of his or her money, we might see this reward (i.e., the toaster) as a source of power but probably not authority. The banker, who rewards a client with future interest payments (and sometimes a toaster) for doing exactly this has no authority over the client, for the client is always free to decide not to give the money and, later, to require the money's return. The same might be true of peer pressure, a good argument, or any other form of influence for which one cannot say, "Person B has an obligation to obey Person A and hand over all of his or her money." Indeed, it is in this sense that there exists some normative relationship between A and B, some duty that B has to obey A, which constitutes authority.

Governments are, perhaps, the most familiar example of an authoritative social actor, as by most accounts, they generally possess a monopoly on the legitimate use of physical force to compel obedience to their mandates in a given geographical area. It is easy to imagine our hypothetical Person A using the club legitimately to quell a riot or to subdue a fleeing prisoner. The soldier or police officer serves as an extension of state authority and shares its legitimacy. However, even these familiar forms of political authority as exercised by the state have limits, and a police officer who uses the same club to compel a confession or to extort money steps outside the limits of the legitimate authority usually accorded to the police and thereby engages in coercion, which is the opposite of authority where the presence of a normative relationship is concerned.

Of course, the exercise of authority, thus defined, is neither limited to the state nor confined to the use of physical force. Instead, the concept of authority extends to cover a variety of social interactions and resides with a variety of social actors. Through the mechanisms of corporate governance, shareholders and their boards of directors exercise authority over the executives of publicly held corporations. They have, for example, the right to hire and fire the chief executive, to set his or her wages, and to review important corporate policies. Business firms create rules to regulate and, thereby, exercise authority over employees. Indeed, the very notion of hierarchy that characterizes most complex organizations rests on the exercise of authority by superiors over subordinates. Much of the early scholarship in organization theory centered on questions of why authority dynamics arise in organizations and how these dynamics facilitate the coordination of organizational action.

As a central concept in the study of societies, states, and organizations, authority has drawn the attention of several very different fields of study. The nature of authority and what makes the exercise of authority legitimate is a central question for political philosophers. "When," they ask, "may a state legitimately compel its citizens to act?" And, conversely, "When may citizens legitimately refuse to obey state mandates?" For sociologists and political scientists, the more pressing questions concern the antecedents and effects of de facto state authority (existing state authority, especially as it actually exercises its power rather than how it's supposed to do so, according to the constitution or the Federalist Papers or a philosopher, for example). They ask, Why do individuals, groups, and organizations submit to authority? How do broader social institutions serve to legitimate this authority? How does the form of authority exercised by a state affect society and its members? For social psychologists, the more fundamental question concerns individual reactions to the exercise of authority. Why do individuals obey authority? And what are the limits of this obedience, especially where other normative considerations are concerned? Each of these three very different sets of questions has clear implications for understanding the role of business in society.

Authority as Normative Question

To the political philosopher, the central question concerning political authority is under what conditions state action can be considered legitimate. After all, we can agree that authority requires some clear appeal to a higher sense of legitimate state function, but agreement on this point does not imply agreement either on the principles that define what is legitimate or on the limits of this legitimacy. When, for example, are citizens obliged to obey laws that either imperil their own lives (i.e., the problem of Socrates) or conflict with other important moral considerations (i.e., the problem of Thoreau)? Such questions have occupied political philosophers for centuries and have inspired important contributions by philosophers such as Thomas Hobbes, David Hume, and John Rawls.

In recent years, commentators such as Robert Paul Wolff have placed such questions in starker terms, considering authority to present a paradox: If legitimate authority requires an actor to act in ways contrary to their own judgment and if moral autonomy (i.e., the right to exercise reason on moral questions and act according to one's reason) is a fundamental human right, then the exercise of authority is always a violation of the other person's moral autonomy and is immoral. This has given new life to the discussion of normative justifications for legitimacy.

For those interested in applying insights from political theory to the conduct of business, one avenue is a direct analogy of the state-citizen relationship to that existing between the state and the firm. After all, the question of when and why a firm should obey state mandates is particularly important given the magnitude of social consequences when it fails to do so. Moreover, to the degree that the corporation (a popular form of business organization) relies on the legitimacy of state mandate for its very existence, one might expect a higher rather than a lower degree of obedience.

More interesting is the question of whether insights from political theory apply to the actions and mandates of the business firm itself. If we can say that a firm exercises authority over its employees (or any other stakeholder groups), then we must also ask whether the boundaries ascribed by political philosophers to state legitimacy apply equally well to organizational action. For example, do notions of consent that underpin theories of democracy at the state level necessitate similar notions of employee or stakeholder democracy at the firm level?

The relationship between political philosophy and organizational ethics is controversial, not least because some political philosophers (e.g., John Rawls) have specifically excluded private associations from the scope of their thinking. Business ethicists disagree about the need for an organizational ethics separate from political philosophy, with some arguing for the direct application of philosophical insights about authority, while others argue that organizations are sufficiently different from states so that few of these philosophical insights apply with any precision.

Authority as a Sociological Question

To the sociologist, the legitimacy that distinguishes between coercive power and authority rests not on some theoretical normative foundation but rather on de facto social convention (actual social convention, meaning here that legitimacy is not whether an actor's behavior satisfies some ideal ethical norm but whether it fits with social norms held in common by real people in society).

Society confers on certain actors the right to influence others and to expect their obedience. A community member who stops another on the street and searches his or her possessions against his or her will is a vigilante, exercising coercive power; a police officer who engages in the same behavior in accord with legal procedures, validated by social convention, is exercising authority. Max Weber identifies three inner justifications, or sources of legitimacy, for the exercise of authority: traditional norms sanctified by long-standing convention; charisma, which attracts the personal confidence and devotion of followers; and rational-legal considerations supported by belief in the validity of legal statutes and functional competence. Much of the authority cited in business and other organizations today rests on a rational-legal source of authority. It is the combination of a manager's position relative to statutory and rational structures that constitutes the right to expect obedience from subordinates. Stockholders share a similar type of authority in their dealings with the corporation via governance mechanisms.

For organization theorists, it is Chester Barnard's so-called consent theory of authority that lays the foundation for thinking about the relationship of business with its stakeholders, despite its focus only on intrafirm relationships between executives and subordinates. Contrary to top-down notions of authority (such as that of Weber), Barnard held that an executive's order would have authority only insofar as a subordinate judged it acceptable, falling within a *zone of indifference* that would keep the subordinate from questioning the executive's authority. From this, one might infer that the responsibility of the executive is to maintain employer-employee relations on a sufficiently positive basis that could sustain authority necessary for the efficient functioning of the organization.

Extending this notion of authority to multiple stakeholders, one might also argue that much of an organization's treatment of its stakeholders rests on some level of authority. When a firm proscribes certain behaviors from customers (e.g., behaviors when standing in line), employees, and local communities, it often rests not on a direct market exchange but on the willingness of stakeholders to accept the authority of a firm's managers. In this sense, the conflicts that companies often face at the hands of stakeholder groups represent the breakdown of organizational authority.

The extreme example of how a firm might exercise authority, on a consent basis, among its stakeholders is the increasing trend toward self-regulation, in which even the state cedes some authority to firms (individually and collectively) to determine right behavior. For example, the Motion Picture Association of America participates in a voluntary rating scheme in which, in lieu of federal regulation, the Association assigns content ratings to films. In this sense, the association exercises not only direct authority over filmmakers but also indirect authority over the movie theaters that show the films and even the moviegoers who can be turned away from seeing the films if they do not meet certain age restrictions.

Authority as a Psychological Question

To the psychologist, the interesting issue concerning authority is how it can overcome other considerations in compelling individuals to obey orders, especially basic considerations such as survival and basic morality. In the latter half of the 20th century, this question took on particular importance as social scientists struggled to make sense of the nightmares of World War II, particularly the willingness of ordinary German citizens and soldiers to take part in the extermination of Jewish and other minorities in the concentration camps. Stanley Milgram, a social psychologist at Yale University, conducted the most famous (and infamous) of these studies designed to understand the limits of a person's willingness to obey authority. Milgram discovered, as he later wrote in his book *Obedience to Authority*, that adults would do almost anything when commanded by an authority. He traced this willingness, in no small part, to the division of labor that characterizes modern society and alienates individuals from the consequences of their own actions.

In organizational terms, this willingness of individuals to authorize others to control them raises a serious dilemma. On the one hand, this willingness to obey represents one of the key psychological underpinnings of the complex organization. The reason companies adopt hierarchies rather than leaving every exchange to the market is that it is more efficient and less costly for a person to obey his or her superior rather than engaging in constant negotiations. On the other hand, many of the most infamous moral lapses in recent organizational history have involved individuals who were willing to follow authoritative commands rather than questioning their morality. For Hannah Arendt, commenting on the behavior of Adolf Eichmann during World War II, this banality of evil represents the ultimate horror of bureaucracy, in which even unspeakable acts can become normal and routine through the exercise of authority.

—Michael E. Johnson-Cramer

See also Anarchism; Autonomy; Hobbes, Thomas; Hume, David; Rawls, John; Stakeholder Theory; Statism

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AUTONOMY

Since the early 1970s, the concept of autonomy has become increasingly important within discussions of business ethics. For example, it plays a key role in discussions of the ethics of advertising, where much of the debate centers around the question of whether or not persuasive advertising undermines consumer autonomy. It also plays a key role in discussions of the morality of sweatshops, where it is often alleged that the use of sweatshops is unethical insofar as the labor conditions that exist within them evince a failure on the part of their owners fully to respect the autonomy of their employees. Respect for autonomy also plays a key role in grounding ethical objections to fraud, coercion, and even bluffing in business situations. More recently, persons have argued that respect for the autonomy of consumers requires that businesses provide as much information as possible about the products that they offer, including such information as the place of manufacture, whether sweatshop labor was involved, and (in the case of foodstuffs) whether they include genetically modified ingredients.

Given that the concept of autonomy plays such a central role in so many discussions of business ethics, it is important to be clear as to what exactly it is for a person to be autonomous or to lack autonomy. Such clarity is especially important because there are two distinct approaches to understanding autonomy: the Kantian approach, which is based on the work of the 18th-century philosopher Immanuel Kant, and the Millian approach, which draws on the approach to autonomy that was taken by the 19th-century philosopher John Stuart Mill.

Kantian Autonomy

The proponents of both the Kantian and the Millian approaches to autonomy draw on the etymology of the term, which stems from the two Greek words *autos* and *nomos*, meaning "self" and "rule." However, the proponents of these two approaches to analyzing autonomy have very different understandings of what it is for a person to be self-ruled. For Kant, a person is self-ruled only if his or her decisions and actions are unaffected by any factors that could be said to be external to his or her self. As such, on a Kantian understanding of autonomy, a person lacks autonomy, and is thus heteronomous, to the extent that his or her decisions or actions are the result of factors that are not essentially his or hers. For the Kantian, then, a person will be heteronomous with respect to his or her decisions or actions if they are the products of any factors that are merely contingent on his or her situation. This is important, for people's desires can be contingent on the situation that they find themselves in. A person in 18th-century France, for example, would not have the desire for a new Mercedes, whereas a person in 21st-century America would not have the desire to wear a powdered wig. More fundamentally, even if people's desires are not the product of their social environment but are, instead, the product of their physiology, they are still not essential to them. For example, a person who liked chocolate ice cream simply because it affected his or her palette in certain ways would not be a different person if he or she were to lose this taste and acquire one for vanilla instead.

Since people's desires are thus not essential to who they are but are merely contingent factors that might influence their decisions and actions, a Kantian holds that those who act on their desires are not acting autonomously, for in doing so, they would not be guided by their essential self. Instead, for a Kantian, since a person is essentially rational, he or she will only be autonomous with respect to his or her decisions or his or her actions if they are directed by his or her rationality. Kant is clear that this does not mean that a person is autonomous if he or she acts instrumentally rationally to achieve some end. To act in this way is merely to act on a hypothetical imperative—that you will perform a certain action if you wish to achieve a certain goal. Actions that are the result of hypothetical imperatives would be performed to secure some goal that would be dictated by the person's desires. Thus, since these desires would not be essential to the person's self, the actions that they lead to would not be ones that the person was autonomous with respect to. Rather, for a Kantian, to act rationally in the sense that grounds ascriptions of autonomy to a person, he or she must act in accord with a categorical imperative—one that must be followed by every rational individual regardless of his or her desires or inclinations. For Kant, such a categorical imperative is to act rationally without being affected by the contingencies of one's desires or inclinations; you must recognize that all other persons could, without logical contradiction, perform the action that you are contemplating performing were they to be in the same situation as you are in. Acting out of respect for this maxim, for Kant, would be an act of respect for the moral law, for the actions that it would allow would be moral ones. Thus, for example, a person whose actions were guided by this categorical imperative could not lie to gain an advantage. This is because were this person to will that everyone lie when it is to their advantage, no one would trust the word of anyone else, and so no one would be able to reap the advantages of lying that would motivate this. Lying, then, cannot be consistently willed to be a universal law.

For Kant, then, a person is autonomous to the extent that he or she acts out of respect for the moral law. Moreover, for Kant, the moral law also shows why autonomy is important. Insofar as persons must, to be moral, act on maxims that they can consistently will to be moral law, and insofar as they consider themselves to be intrinsically valuable as rational agents, they must also recognize that other rational agents are intrinsically valuable, too, for there is no relevant difference between their rational agency and that of others. As such, for Kant, persons must always treat rational humanity, whether in their own person or that of another, as an end in itself (i.e., as intrinsically valuable) and never as a mere means (i.e., as merely instrumentally valuable). This Kantian claim that we must always respect the autonomy of other persons is frequently used to ground claims concerning the ethical conduct of business. It is, for example, often used to ground the claim that persons should not be coerced into employment and that businesses should not defraud those they interact with, on the grounds that such practices would be examples in which persons were not treated as ends in themselves, and so their autonomy was not respected, but only as mere means. This Kantian claim has also been used to ground the view that multinational enterprises should not exploit workers in the developing world but should, instead, not only adhere to local labor laws but also ensure that they provide good working conditions to their employees and pay them fair wages. Were these multinationals not to do so, it is argued, they would be treating their workers merely as means to their own profits and thus would fail to respect their autonomy in the way required by Kantian ethics.

Millian Autonomy

The Millian view of autonomy is very different from the Kantian one. For Kant, a person is autonomous if he or she acts out of respect for the moral law, with no concern for his or her contingent desires or inclinations. In contrast, for Mill, persons are autonomous to the extent that they rule themselves and are not ruled by others. For Mill, autonomy was closely connected with the idea of individuality; indeed, in his seminal work *On Liberty*, Mill used the latter term in preference to the former. For Mill, persons are autonomous if they choose their plan of life for themselves. A person is autonomous to the extent that he or she directs his or her actions in accord with his or her own values, desires, and inclinations—the polar opposite of the impersonal account of autonomy offered by Kant.

This Millian account of autonomy has been more widely adopted within discussions of applied ethics in general and business ethics in particular than its Kantian rival, for three reasons. First, the Millian account of autonomy appears to be more empirically accurate. Very few persons explicitly act out of respect for the moral law, yet it does not seem that autonomy is a rare phenomenon. Second, insofar as its focus is on persons acting in accordance with their own desires and values, the Millian account of autonomy is well suited to discussions of business ethics, especially when considering whether or not persons are, for example, autonomous with respect to their decisions to gratify their desires to purchase an advertised product. Third, the application of the Millian approach to autonomy in discussions of business ethics has benefited from a recent flourishing of analyses of what it is for a person to be autonomous in this desire-based sense of autonomy. This discussion was started by the philosopher Harry G. Frankfurt's seminal article "Freedom of the Will and the Concept of a Person," in which he outlined a hierarchical analysis of what it is for persons to be autonomous with respect to those of their desires that actually move them to act.

Hierarchical Analyses of Autonomy

Frankfurt's early hierarchical account of what it is for persons to be autonomous with respect to those of their desires that actually move them to act has been enormously influential and is no doubt in large part responsible for the popularity of the Millian, rather than the Kantian, approach to autonomy in discussions of business ethics. Frankfurt offered an account of autonomy that was able to accommodate the intuitively plausible claim that persons might not act autonomously even though they were, in a sense, doing what they wanted to do. For example, persons who are addicted to a drug but who do not want to be so addicted would still be doing what they want to do when they take the drug to which they are addicted, even though it is plausible to hold that they are not fully self-directed, not fully autonomous, when they do so. To accommodate the intuition that such unwilling addicts would not be autonomous with respect to their taking of the drug to which they are addicted even though they do so to satisfy a desire that they have for the drug, Frankfurt claimed that it was necessary for a person to endorse his or her first-order desires for him or her to be autonomous with respect to them. Thus, to be autonomous with respect to his or her taking of the drug, the unwilling addict would have not only to have a desire for the drug but also to have a desire to have that desire for the drug. Yet even if the addict has such a second-order desire (a desire about another desire whose intentional object is not a desire), he or her might still not be autonomous with respect to his or her taking of the drug. This is because he or she might want to have the first-order desire for the drug but not want it to move him or her to act. (He or she might, for example, want to know what it feels like to be addicted but might not want to take the drug to which he or she is addicted.) To be autonomous with respect to his or her effective first-order desire for the drug, then, this addict would, for Frankfurt, have to both endorse his or her effective first-order desire and want it to move him or her to act. In Frankfurt's terms, then, persons are autonomous with respect to their effective first-order desires if they volitionally endorse them, if they both want them and want them to move them to act.

This Millian account of autonomy developed by Frankfurt has been subject to three criticisms. First, it is not clear why a person would be autonomous with respect to his or her second-order volition. If the answer is that this was endorsed by a third-order volition, then a regress is entered into, for the same question can arise with respect to this third-order volition. If, however, the answer is that the person is autonomous with respect to it for some other reason, then Frankfurt's account is incomplete. Second, it is not clear why a person's higher-order desires should be considered to be more genuinely his or hers, those that he or she is more autonomous with respect to than his or her first-order desires. A person's second-order desires might, for example, be the products of socialization, with his or her first-order desires being those that are more autonomously his or hers. Finally, Frankfurt's Millian account of autonomy seems vulnerable to what is termed the *problem of manipulation*. A person might implant both a first-order desire into another person and a corresponding endorsing second-order volition, and the implantee would, on Frankfurt's original account, be autonomous with respect to him or her, resulting in implanted first-order desire. But this seems implausible. These three objections have led Frankfurt to revise his account of autonomy. Most recently, Frankfurt holds that to be autonomous with respect to an effective first-order desire, a person must not only reflectively endorse it but also be satisfied with his or her endorsement of it, where such satisfaction consists in his or her having no interest in altering the desire in question. This revision of his account appears to meet the first two objections stated above. However, it does not appear to meet the problem of manipulation, for a person could still be manipulated into being satisfied with an implanted desire. To avoid this problem, the philosopher John Christman has developed a historically based version of Frankfurt's account. For Christman, to be autonomous with respect to an effective first-order desire, a person must not have resisted its development when attending to this and when his or her attention to this matter was uninhibitedly reflective.

The analyses of Millian autonomy and their subsequent revisions in light of criticisms are not, however, only of interest to autonomy theorists: They are of crucial importance to those areas of business ethics in which the concept of autonomy plays a central role. If, for example, Frankfurt's original hierarchical account of autonomy is accepted, then it would not, from the point of view of someone who held autonomy to be morally valuable, necessarily be morally objectionable to defraud consumers. This is because, on Frankfurt's original account of autonomy, provided a person volitionally endorsed his effective first-order desire then he was autonomous with respect to it. Thus, if a person was fraudulently sold defective goods, his or her autonomy would remain inviolate, since he or she would have volitionally endorsed his or her effective first-order desire to purchase them. If, however, Christman's Millian account of autonomy is accepted, then a person who held autonomy to be morally valuable would have grounds for objecting to fraud, for its victims would have resisted the development of their desires for the fraudulent goods had their reflection on them not been inhibited by those who intended to defraud them.

Judgmental Relevance

The question, then, of which theory of autonomy to accept will be in part guided by what the philosopher Gerald Dworkin has termed *judgmental relevance*—the degree to which each theory matches our pretheoretical intuitions as to when a person is autonomous with respect to her actions and her desires and when she is not. Thus, if we believe that fraud is an affront to autonomy we would endorse either a Kantian account of autonomy or else a Millian account of the sort developed by Christman. That different conceptions of autonomy fit with our pretheoretical intuitions concerning the scope of this concept in particular cases does not, however, imply that they should all be accepted. Instead, it shows that to arrive at a core analysis of autonomy we should pay particular attention to cases in which there is disagreement over whether or not a person is autonomous with respect to her actions. Such cases will show us either that when we disagree we do so because we are talking about different, but related, concepts (such as autonomy and authenticity), and we can then refine our discussions accordingly, or that if we agree on the concept at hand, we can refine our analysis of it to accommodate all our intuitions about its extension. As such, discussions of the ethics of persuasive advertising, bluffing, and sweatshops should play a role in our discussions of autonomy, since by providing real-life examples of cases in which a person's autonomy is in question they can help us to identify the appropriate scope of this concept.

—*James Stacey Taylor*

See also Advertising, Subliminal; Advertising Ethics; Global Business Citizenship; Kant, Immanuel; Kantian Ethics; Mill, John Stuart

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B

Bait-and-Switch Practices

The term *bait-and-switch* is most commonly used to refer to an advertising practice that is both unethical and illegal. While the term has been used since the 1920s, the practice is likely to be much older. It typically involves an advertiser luring customers into the store by offering a product at an unrealistically low price (the bait). The customer is then told that the advertised goods are (1) not available or (2) of inferior quality and/or not suitable for the customer's needs. The goal is to "switch" the customer to another, more expensive product or one that has a higher profit margin. What sets bait-and-switch apart from other advertising practices is that the store does not intend to sell the advertised product—the advertised product is intended to attract customers, who are then persuaded to buy another product.

It is not only retailers who use bait-and-switch techniques. This technique could be used by any provider of goods or services, such as companies providing financial services and products, recruitment agencies, and travel agencies. Even governments have been accused of using bait-and-switch strategies.

An Example

The following example highlights the issues raised by bait-and-switch practices. Suppose a product is advertised at a very attractive price and customers arrive at the store to buy it. Customers are convinced by the salesperson that the advertised product is not value for the money, is unreliable, and has few features that most people think essential. The customers are persuaded to spend significantly more on an alternative product.

The advertisement that drew customers to the store was an alluring but insincere offer to sell the product advertised. The intention was to entice potential purchasers into the store and then sell them the more expensive item. The claim is that what has taken place is fraudulent. As soon as customers decided to visit that particular retailer rather than another (in other words, they "took the bait"), they have made an investment of time, money, and effort; so, even if they do not end up purchasing from that store, they have nonetheless been deceived. Once in the store, the salesperson aims to convince customers not to buy the product they came in to purchase. However, once they are in the store, that store has a competitive advantage over other retailers of similar products. This is why the "switch" is often successful. The present and actual product to which customers have been switched is more attractive than hypothetical products at other retailers, making it more likely that the salesperson will complete the sales of the more expensive model. In this example, the appealing offer was not what it seemed. The advertised product was simply an enticement to get customers to identify themselves as being interested in the type of product advertised, thereby providing the sales staff with an opportunity to sell a model that was more advantageous to the store.

The Law and Bait-and-Switch Practices

In the United States, the Federal Trade Commission (FTC) regulates against deceptive practices.

Bait-and-switch practices are considered deceptive and therefore unlawful. The federal court interpretation of bait-and-switch practices is usually consistent with the FTC guidelines, and reference is often made to them. Many state courts have adopted the Uniform Law version of Consumer Protection Laws, in which bait-and-switch practices are identified as deceptive.

According to the FTC, advertisements for products must be bona fide efforts to sell the product advertised. It is illegal to advertise goods or services that the company has no intention of selling, intending instead to sell to the customer another, usually higher-priced product or service.

Advertisements are not bona fide offers if, for example,

- the advertiser refuses to show, demonstrate, or sell the advertised product or service;
- the product or service is disparaged by the salesperson;
- there is insufficient stock to reasonably meet anticipated demand;
- the advertiser refuses to take orders for advertised goods to be delivered in a reasonable time frame;
- the advertised product fails to fulfill the purpose represented or implied in the advertising; or
- sales staff are penalized if they sell the advertised product.

Even though bait-and-switch practices are illegal and those involved risk federal and state prosecution or lawsuits from competitors, from a practical perspective, the time and expense involved in establishing injury is prohibitive.

Ethics and Bait-and-Switch Practices

There is a connection between autonomy, deceit, and coercion. For most people, autonomy is a value. This means that autonomy is something that is intrinsically good or worth having for its own sake and anything that erodes autonomy is bad. To be autonomous is to be in command of one's own life, to be in a position to review alternatives for action knowing exactly what they involve and what their consequences are. Autonomy can be eroded by false or misleading information. Bait-and-switch practices are not consistent with a commitment to the value of autonomy. If a customer was influenced to purchase an alternative product by information that was deceptive and if the customer would not have bought the product except for the information provided, then he or she has been coerced into buying it. This is exactly what happens in a successful bait-and-switch.

The effect of bait-and-switch practices is harm to consumers and to honest competitors. Moreover, it is often the poor and less well educated who are most susceptible to the "hard sell" techniques employed to switch a customer from the bait product to another more expensive one. In the following sections, a brief ethical analysis of bait-and-switch practices is provided from three different perspectives: the golden rule, utilitarianism, and Kant's ethics.

The Golden Rule

The golden rule of doing unto others as you would have them do unto you is a widely accepted moral principle. It is an ethical norm that is a cornerstone in (almost) all the major religions. Clearly, anyone who subscribed to the view that we should treat others as we would like to be treated ourselves would have a problem with bait-and-switch practices. It is implausible that anyone would seriously claim that he or she would not object to being treated in the way that victims of bait-and switch practices are treated. According to the golden rule, bait-and-switch practices are unethical.

Utilitarianism

For the utilitarian, there is only one ultimate moral principle. This is the requirement to act so as to produce the greatest happiness for the greatest number. When there are more than one alternative courses of action, the right action is the one that produces the greatest net happiness. A distinction needs to be made between *rule* and *act* utilitarianism. Rule utilitarianism is concerned with identifying a set of moral rules that satisfies the principle of utility better than any alternative set of moral rules. Particular actions are judged right or wrong according to whether they conform to the chosen set of rules. Act utilitarianism, on the other hand, requires a utilitarian calculation to be undertaken for each possible action in order to identify what is ethically required.

How would bait-and-switch practices be evaluated against the utilitarian criterion? First, a rule utilitarian would identify the general rules of conduct that maximize utility. Arguably, any such set of rules would include injunctions to act honestly (or not act dishonestly). To see why this is the case, we only need consider two societies, one in which there is a rule requiring honesty and one in which there is not. We then consider whether people will be better off in the first or the second society. The first society is preferable from the point of view of utility. Since bait-and-switch practices deceive consumers, the rule to act honestly is violated, and a rule utilitarian would judge the practice wrong.

An act utilitarian analysis of bait-and-switch practices requires that everyone affected be identified and taken into account, together with the extent of the impact. First, consider those who benefit from bait-and-switch practices (i.e., those for whom the consequences are good). Clearly, the company engaged in the practice will benefit financially, with a flow-on effect to that company's owners and employees. However, long-term consequences also need to be taken into account. If there is legal action or adverse publicity as a result of the bait-and-switch practices being made public, then any short-term financial benefit could be outweighed.

Next, we turn to those who are harmed by bait-and-switch practices (i.e., those for whom the consequences are bad). Most obviously, it is the customers who have been victims of successful bait-and-switch practices who are harmed. Honest competitors who do not engage in deceitful practices are also harmed because potential customers have been lured away from them. Moreover, a whole sector could be damaged by publicity relating to questionable practices. For example, if it becomes common knowledge that many automobile dealerships use this technique, then even honest operators' reputations can be harmed. When all the consequences of bait-and-switch practices are considered, it is impossible to conclude that the practice maximizes long-term utility.

Kant's Ethics

In contrast to utilitarianism, Immanuel Kant believed that moral principles can be identified by the exercise of reason alone, without having to know anything about the consequences of actions. Kant believed that it is only when a person acts from "goodwill" or duty that the action has moral worth. At the core of Kant's moral theory is his categorical imperative. In answer to the question "What makes an action right?" the categorical imperative states that an action is morally right only if the maxim (or principle) represented by the action can be accepted as a universal law. The categorical imperative is binding on all rational agents regardless of their specific goals or desires and regardless of the consequences.

There are two other ways to understand or interpret the categorical imperative. First, an action is right only if the agent would be willing to be treated in this way if the positions of the parties were reversed. This formulation of the categorical imperative is a variation of the golden rule discussed previously. Second, people should always be treated as ends, never merely as means to others' ends. This formulation of the categorical imperative is sometimes referred to as respect for persons. The requirement to act from a sense of duty and the three understandings of the categorical imperative can be used as tests to evaluate actions.

Bait-and-switch practices would be judged unethical from a Kantian perspective. First, those who are involved in these activities act from a sense of self-interest and not duty, so their actions cannot be morally praiseworthy. Second, rational agents could not accept the principle underlying the action as a universal law. To do so would require accepting a principle that said something like "It is acceptable to deceive customers in order to benefit financially." Third, those who employ bait-and-switch practices would not be prepared to change places with the customers who are victims of these practices. Finally, customers are being used simply as a means to generate profits.

Conclusion

Bait-and-switch practices can be used in many contexts; however, what makes them all legally and ethically problematic is that their success relies on deceit. Bait-and-switch practices are deceptive and therefore unlawful. The golden rule, utilitarianism, and Kant's ethics all support the claim that bait-and-switch practices are unethical.

—Josie Fisher

See also Advertising Ethics; Consumer Fraud; Consumer Rights; Deceptive Advertising; Federal Trade Commission (FTC); Marketing, Ethics of

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Bankers' Trust

In the mid-1990s, BT Securities Corporation, now part of Deutsche Bank, was involved in two landmark legal cases that helped clarify the duties and responsibilities of swap dealers and their customers.

The first case involved Gibson Greetings, Inc., a manufacturer of greeting cards and related products. Gibson sued BT for losses on two swap transactions where BT was the dealer. The contracts in dispute represented the cumulative position resulting from 27 earlier transactions. Of the 29 transactions between Gibson and BT, many involved the termination of one position in exchange for entering into another position. This process requires agreement between the parties as to the terms that will equate the market value of the terminated swap (or swap portion) to the value of the new position (or amendment) received in exchange.

The dispute between Gibson and BT centered on the duties of each party in determining the termination value of the swaps. Gibson alleged that an advisory relationship existed between BT and Gibson, meaning that BT was supposed to be acting on Gibson's behalf. BT argued that their transactions with Gibson were strictly arm's-length deals and that the swap master agreement did not establish any advisory or fiduciary relationship. BT argued that termination values they quoted were simply that—quotations at which BT stood ready to terminate a swap. BT argued that Gibson was free to shop for better deals in the market. The suit was settled out of court in November 1994, with Gibson paying BT only $6.2 million out of the $20.7 million owed under the terms of its swap agreements.

In a second case, Procter & Gamble (P&G) sued over its similar experience with BT. P&G accused BT of misleading statements about the terms of two interest rate swaps. The swap agreements included some complicated option features designed to allow P&G to lock in a favorable interest rate even if interest rates rose.

The pricing of the deals relied on BT's proprietary valuation models. P&G had placed itself in a position in which it had to rely on the computations of BT, without understanding how the results were reached. In large part, this was due to the complex option provisions of the swaps. P&G claimed that it relied on BT's models to value the swaps but that BT would not share the specifics of their models. P&G claimed that it was the victim of a financial fraud, a charge that BT strongly contested. BT argued that P&G was fully aware of the risks when it had agreed to the swaps and was free to get a second opinion on swap values from another dealer. The case was settled out of court with P&G paying BT $35 million of the more than $200 million BT claimed it was owed.

As a result of these two cases, swap dealers are careful to enumerate the duties of the dealer and the responsibilities of the dealer's customers. Swap dealers are also careful to abide by these duties once established.

—James A. Overdahl

See also Financial Derivatives; Scandals, Corporate

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Bank of Credit and Commerce International (BCCI)

The Bank of Credit and Commerce International (BCCI), a large private bank founded in 1973, engaged in various lines of illegal activities, ultimately leading to its demise. Its name is associated not only with illicit practices and financial scandals (e.g., fraud, money laundering, fund diversions, account falsification, deceitful management) but above all with the fact of having worked as a front to cover up other dirty business on the margins of banking activity, including drug trafficking and international terrorism, among others.

The BCCI, founded by the Pakistani Agha Hassan Ahbedi, had its headquarters in Luxembourg and was controlled by the Emirate of Abu Dhabi. In its day, it was considered the seventh largest private bank in the world, with a turnover of more than $30,000 million and offices in 70 countries. However, to the surprise of many, the bank was closed by judicial order in 62 countries on July 5, 1991.

The BCCI was more than a bank; it was a type of state within the state. It had its own intelligence service, an army, and, naturally, its own central bank. Due to this, although the banking business was important, it only represented a small part of the entirety of its activities. The so-called "Black Network" stands out, a clandestine division comprising 1,500 employees in charge of carrying out espionage, selling arms, trafficking in drugs, as well as perpetrating bribes and extortions at an international level. A few of the well-known clients of the bank were, among others, Manuel Noriega, Abu Nidal, Saddam Hussein, and Ferdinand Marcos. The BCCI was also the bank used in the dubious Iran-Contra affair.

The police siege of the BCCI started to bear fruit in October 1988, when customs agents apprehended seven financiers related to the bank in Florida. Three days later, another 40 directors were arrested in Europe under charges of laundering money proceeding from drug trafficking for the value of $14 million. As subsequent investigations revealed, the BCCI had also clandestinely controlled for years the capital of First American Bankshare, whose president was former Secretary of Defense Clark Clifford. It maintained total financial duplicity to secretly manage other banks in the United States and to organize its business in third-world countries.

As the investigations progressed, the BCCI began to appear more and more like an empty shell. In December 1991, the bank was found guilty of fraud and money laundering. A New York court indicted Sheikh Khalid bin Mahfouz, a top officer of Saudi Arabia's National Commercial Bank, a BCCI subsidiary, to be able to recover a fine of $170 million. Clark Clifford and his partner Robert Altman were also accused of being conspirators and of having hidden important facts related to the fall of BCCI.

—José-Luis Fernández-Fernández

See also Corruption; Fraud; Scandals, Corporate; Terrorism

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Bankruptcy, Ethical Issues in

Bankruptcy occurs when an individual or a corporation that has insufficient assets to pay all debt obligations is subject to laws that provide some protection from creditors and permit an orderly distribution of assets to satisfy creditors' claims. There are two broad kinds of bankruptcy. In "liquidation" or "straight" bankruptcy, the assets of an individual or a corporation are turned over to a trustee, who liquidates them and distributes the proceeds to the creditors. An individual who goes through liquidation bankruptcy is absolved of many debts and is free to make a "fresh start." A corporation that is liquidated goes out of business. The second kind is "reorganization" bankruptcy, in which a corporation obtains temporary relief from debt obligations while it seeks to reorganize and regain solvency. Individuals may also use reorganization bankruptcy to work out a repayment schedule with creditors. In the United States Bankruptcy Code, liquidation bankruptcy is governed by Chapter 7 and reorganization bankruptcy by Chapter 11.

Bankruptcy is vital for a well-functioning economy. Without it, indebted individuals may suffer a lifetime under debt burdens that keep them from enjoying a rich, full life. The prospect of possible ruin without promise of relief is likely to deter individuals from risky, but potentially profitable, business ventures. Without the possibility of an orderly liquidation of a failed business, suppliers would be less willing to extend goods on credit or make capital available. Most important, reorganization bankruptcy permits potentially profitable businesses to recover from temporary adversity and remain going concerns. This kind of protection enables business organizations to continue to provide jobs and serve customers and to keep productive assets employed during difficult times. Overall, bankruptcy increases the wealth of any society.

Despite these benefits, bankruptcy poses some ethical issues. One ethical issue in bankruptcy concerns the moral justification of bankruptcy laws. Laws that absolve individuals and corporations from paying debts they have incurred or else allow them to defer payment might appear to violate the ethical principle that all debts should be paid. Alternatively, very stringent bankruptcy laws might be viewed as unjustifiably punitive, especially when they force individuals to pay heavy debts or prevent corporations from reorganizing and returning to profitability.

A second ethical issue is the possible abuse of bankruptcy laws. Individuals might be accused of abusing bankruptcy, for example, when they incur large debts just before filing for bankruptcy. In corporate bankruptcies, all creditors should be treated fairly with respect to their claims. However, in bankruptcy proceedings, it is possible for some creditors to get more than they deserve and others, less. In particular, when corporations reorganize and emerge from bankruptcy, those parties that control the process have an opportunity to enrich themselves at the expense of some creditors and other groups, such as employees. Bankruptcy also affords corporations the opportunity to enter bankruptcy in order to achieve strategic ends, such as avoiding legal judgments or strengthening their negotiating position with creditors. Such "strategic bankruptcy" is often criticized as an abuse of the law.

The Justification of Corporate Bankruptcy

When a corporation is unable to pay its debts, the moral imperatives are that the remaining assets be used to satisfy the creditors' claims to the fullest possible extent and that all creditors be treated fairly, with each receiving a proper share. Sometimes, creditors are best served by liquidation, in which the corporation is dissolved and its assets distributed to the creditors. In liquidation, no assets are lost; they are merely put into different hands. At other times, however, the creditors are better served when an insolvent corporation is allowed to reorganize and return to profitability. This occurs when a corporation's assets have greater value kept together in an ongoing entity rather than dispersed to the creditors. Not only creditors but also employees and the rest of society benefit when potentially profitable firms are allowed to reorganize.

From an economic perspective, a bankruptcy code that allows for either liquidation or reorganization maximizes the value of a corporation's assets. Since the creditors are the major beneficiaries in bankruptcy, they can decide themselves whether to liquidate an insolvent firm or permit its reorganization. However, creditors, who in bankruptcy replace shareholders as owners of a corporation, typically have different, competing interests. Unlike shareholders, who have a single objective—namely, profit maximization—creditors are more diverse due to their different kinds of claims. Bondholders, for example, may have interests that differ from those of unpaid suppliers; and some creditors may be secured, while others have unsecured debt. The challenge of any bankruptcy code, then, is to force creditors to act collectively in making wealth-maximizing decisions. In short, the code should force creditors to act like shareholders, who have the single objective of wealth maximization, instead of individual claimants whose only objective is the payment of particular debts.

One way of justifying an ideal bankruptcy code is by employing the "creditors' bargain." This justification asks the hypothetical question, What system would all creditors agree to in advance of any bankruptcy proceedings? The answer would be a system that maximizes a corporation's assets, from which their claims will be satisfied. Although individual creditors, especially those with secured claims, might collect more of what they are owed in one case by liquidation, say, they might collect more in another case by reorganization. In any event, creditors as a group will collect more under a bankruptcy code that maximizes the value of a corporation's assets. Such a code is likely to allow for both liquidation and reorganization and to force creditors to act collectively. The creditors' bargain thus justifies any particular bankruptcy code by employing a hypothetical contract argument of the following form: This code is justified because it is one that would be agreed to by all creditors in advance of any particular situation.

Although any bankruptcy code that is justified by the creditors' bargain is in the creditors' interest, it remains to be shown that it also serves the interests of society as a whole. However, an argument that such a code serves society's interests can be constructed along the lines of the argument for shareholder control. Bankruptcy can be understood as corporate governance under conditions of insolvency. As long as a corporation is solvent, shareholders ought to have control, and such control, according to the standard argument, serves all other interests because shareholders will make wealth-maximizing decisions. When a corporation becomes insolvent, creditors rather than shareholders assume control because all remaining corporate assets should be used to satisfy their fixed claims, which have priority over shareholders' residual claims. By forcing creditors to act like shareholders, though, a well-designed bankruptcy system ensures that creditors, like shareholders, will make wealth-maximizing decisions that benefit everyone.

Abuse of Corporate Bankruptcy

The bankruptcy code in the United States has been used by companies to avoid or reduce the payment of heavy legal judgments in suits over defective products and contract breaches and to void or renegotiate collective bargaining agreements and other onerous contracts. Some solvent corporations have entered bankruptcy to gain additional leverage with employees, creditors, and other groups as part of a reorganization. In such situations, bankruptcy is a strategic choice rather than an unavoidable condition.

Is there anything wrong with such "strategic bankruptcy"? Critics charge that it abuses the bankruptcy code by enabling corporations to avoid their moral and legal obligations. However, the obligations to pay legal judgments or fulfill contracts are no different from the obligations to pay other creditors; they are all debts. And the bankruptcy code is designed to enable companies that are insolvent—or would become insolvent if forced to pay a legal judgment or fulfill a contract—to maximize the value of their assets. Moreover, bankruptcy does not permit corporations to avoid their obligations entirely but only to negotiate the terms under which they will be fulfilled. And if not all obligations can be fulfilled, then every claimant must settle for only partial payment. In many cases, successful litigants and contract holders end up being well served by the outcome of bankruptcy proceedings. A well-designed bankruptcy code should permit companies to renegotiate ruinous legal judgments and onerous contracts if fulfilling these obligations would prevent them from fulfilling other obligations to creditors, employees, and other parties. Morality requires that all claimants be treated fairly, and preventing strategic bankruptcy might allow some claimants to take priority over others.

Another objection to strategic bankruptcy is that claimants who receive their claims under one set of rules must fight for them again under another set of rules. Thus, victims of defective products who receive awards in court suits are forced to win their case all over again in bankruptcy proceedings. Workers who negotiate a labor contract in good faith can find themselves back at the bargaining table, this time before a bankruptcy judge. Strategic bankruptcy might be compared to a game of poker in which a dealer with bad cards is able to stop the game, rearrange some of the hands, and resume the game under different rules.

It can be argued in response that the situation for victims of defective products and workers with contracts is no different from that for other creditors. Every claim includes a provision for default. Thus, bondholders and suppliers must expect to go to court if their claims are not paid. If a company is insolvent, then not everyone can be paid, and some way must be found for all claimants to receive a fair share of a firm's assets. Moreover, the poker game to which strategic bankruptcy might be compared is not unfair if the dealer's option is understood at the beginning of play. All creditors should be aware of the possibility of strategic bankruptcy and play their hands accordingly.

A third objection to strategic bankruptcy is that it might enable managers to enrich themselves at the expense of creditors and even shareholders. American law permits easy access to bankruptcy protection because a company need not demonstrate that it is insolvent but only that it would face insolvency without protection from its creditors. The bankruptcy code also permits managers to retain control during the reorganization process. With such easy access, managers have the opportunity to "play games" at the creditors' expense. If bankruptcy is an acceptable risk, managers might be willing to pursue more risky strategies that benefit themselves and shareholders since creditors will also lose if the strategy fails (which is an instance of moral hazard). Managers' pursuit of exceptionally risky strategies in an effort to keep their positions might also lead to greater losses for shareholders as well. There is some evidence that since the American Bankruptcy Code was liberalized in 1978 to allow easier access to bankruptcy protection, both bondholders and shareholders have lost proportionately more in bankruptcy proceedings.

The crucial question, then, is not whether to allow strategic bankruptcy—it can serve to benefit all claimants of a corporation—but how easy the access to bankruptcy protection should be. If this question is answered by the creditors' bargain, then creditors, as well as shareholders, might prefer a system with relative restrictive conditions for receiving bankruptcy protection.

Personal Bankruptcy

The standard justification for personal bankruptcy, which allows individuals to discharge their debts and have a fresh start, is based on welfare and justice. At one time, when individuals were unable to pay their debts, they were cast into prison. Even without the threat of imprisonment, people with heavy debts might spend a lifetime of economic struggle with consequences not only for themselves but the whole of society. Everyone, debtors and creditors alike, are better off in a society that allows personal bankruptcy because even creditors might find themselves with debts they cannot pay. Although there is an obligation to pay one's debts, the benefit of fulfilling this obligation may be outweighed by the loss that results when people are unable to live full, productive lives. In addition, it is unfair for people to suffer crushing debt loads that are caused, in many cases, by adversities beyond their control.

However, a liberal system of personal bankruptcy creates opportunities for abuse. Easy access to bankruptcy protection with little stigma or inconvenience might lead individuals to be less restrained in incurring debts. When facing bankruptcy, individuals might incur all the debt they can, knowing that it will soon be discharged, and seek to shield other assets from creditors by improper means (such as transferring the title for property to a relative). In the United States, creditors, most notably banker lenders and credit card issuers, whom critics accuse of enticing customers into unmanageable debt loads, have protested against this abuse and sought changes in the law to prevent it.

The main issues in the debate over changes in the law of personal bankruptcy are as follows: (1) Should individuals above a certain income level as determined by a "means test" be required to pay off a certain portion of their debts (in reorganization) instead of having them discharged completely (in liquidation)? (2) Should some assets (such as a home or pension savings) be shielded from creditors during bankruptcy proceedings? (3) Should certain debts be nondischargeable (e.g., those for luxury goods or large cash advances obtained just prior to seeking bankruptcy protection)?

Opponents of more stringent personal bankruptcy laws argue that abuse is committed by only a small portion of those seeking protection and that the vast majority of personal bankruptcies are due to job loss, divorce, illness, and business failure. For such people, a fresh start will often enable them to resume successful lives, whereas requirements to pay off a portion of their debts will mire them in cycles of indebtedness. Opponents also claim that bankruptcy due to the failure of a business is more common than is generally recognized and that more stringent laws will strongly deter individuals from starting new businesses, thus damaging a vital engine of economic growth.

—John R. Boatright

See also Fairness; Finance, Ethics of; Justice, Distributive; Moral Hazard; Product Liability; Shareholder Model of Corporate Governance; Shareholder Wealth Maximization; Social Contract Theory; Wealth; Wealth Creation

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Barings Bank

Barings Bank, PLC, was a British merchant bank founded in 1763 and known as the "Queen's Bank." The bank was one of the world's most highly regarded financial institutions before it suddenly collapsed due to the actions of a 28-year-old rogue trader, Nick Leeson, operating from the bank's Singapore affiliate. The sad tale of Barings highlights the need for financial institutions to adopt strict internal control procedures to monitor the positions established by traders on the institutions' behalf.

Leeson was supposed to be conducting stock index arbitrage between Japanese stock index futures contracts traded in Japan and similar futures contracts traded on the Singapore exchange (SIMEX). Such trading involves buying the cheaper contract and simultaneously selling the more expensive one, then reversing the trade when the price difference has narrowed or disappeared. The strategy seeks to capture small and temporary pricing discrepancies between markets. Theoretically, stock index arbitrage is risk free, and properly executed arbitrage transactions involve very low levels of actual risk. The risk is limited, because of the close relationship between a stock index futures contract and the underlying stock index itself.

However, Leeson apparently strayed from his strategy in late 1994 and early 1995. Through the futures markets and using options on futures, Leeson made very large one-sided bets that Japanese stocks would rise. The Kobe earthquake in January 1995, however, rocked the entire Japanese economy and led to a dramatic drop in the Japanese stock market. The highly leveraged bets on a rising Japanese market turned out to be giant losers. These losses completely exhausted the capital of Barings, which declared bankruptcy and was acquired by the Dutch investment bank ING for one pound British sterling on March 3, 1995.

When Barings filed for bankruptcy in February 1995, it was discovered that Leeson, in the name of Barings, had established (and concealed in an error account) outstanding notional futures positions on Japanese equities of $7 billion. In addition, Leeson had outstanding notional futures positions on Japanese bonds and euroyen totaling $20 billion. Leeson had also sold Nikkei put and options with a nominal value of about $7 billion. The reported capital of Barings at the time was $615 million. In a short period, Leeson's trades lost about $1.4 billion. Leeson's actions were overlooked because of poor risk oversight and poor internal controls at the bank. The bank had allowed Leeson to be both a risk taker and a risk monitor. The bank had ignored internal warnings about this conflict of interest, perhaps because it appeared on paper as if Leeson's trades were highly profitable. After the losses became public, Leeson was arrested, convicted, and sentenced to a 6½-year prison term in Singapore. By 1999, Leeson was out of prison, giving speeches on the dangers posed by rogue traders at $100,000 per appearance, appearing in commercials on behalf of brokerage firms, playing celebrity online poker, and receiving numerous job offers in risk management. In 1999, a movie appeared, titled *Rogue Trader*, based on Leeson's autobiography of the same name. In 2005, he took a marketing job with an Irish football team.

Leeson's rogue trading, while spectacular, is hardly an isolated incident. The 1990s witnessed a steady stream of staggering losses caused by rogue traders. In the mid-1990s, Daiwa and Sumitomo Corporation each lost over $1 billion from rogue traders in their employ. In 1997, Codelco lost $200 million, allegedly because of a rogue trader. In February 2002, Allied Irish Banks (AIB) announced a $750 loss attributed to rogue trading, a further reminder of the need for financial institutions to adequately address issues related to internal control procedures.

—James A. Overdahl

See also Scandals, Corporate

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Barriers to Entry and Exit

Entry and exit barriers limit the number of firms competing in a product market or industry. Entry barriers lessen the degree of competition by imposing hurdles that decrease the ability of new entrants to operate profitably. One result is that firms operating in an industry protected by strong entry barriers tend to benefit from higher prices, and thus profits, than do firms operating in an industry without strong entry barriers. In contrast, exit barriers increase the degree of competition within a product market or industry by imposing obstacles that make exit difficult or costly. The rivalry between firms in an industry with strong exit barriers tends to be more intense than the rivalry between firms operating in an industry where exit is easy or relatively costless. One result is that firms in an industry with strong exit barriers tend to suffer lower prices and, thus, profits.

What entry and exit barriers have in common is their strong impact on the nature of competition: In the case of entry barriers, competition is lessened, while in the case of exit barriers, competition is magnified. This relationship between competition and entry and exit barriers has important ethical implications associated with erecting and maintaining various forms of entry and exit barriers. Competition benefits consumers; it ensures that firms operate efficiently and share the resulting gains by lowering prices, boosting innovation, improving quality, and/or further increasing profitability. Firms can also benefit from competition; consider the case of Pepsi and Coke, whose rivalry has significantly increased cola consumption. However, all else being equal, firms prefer to erect and maintain barriers to entry that furnish them some level of protection from highly competitive forces. Different barriers will benefit consumers versus firms in different ways. Some forms of barriers to entry and exit are more likely to engender a sense of commutative justice, where both consumers and firms benefit equally. Other types of barriers may justly favor one over the other, creating an undercurrent of distributive justice. Finally, some barriers may unjustly benefit one group at the expense of the other. Understanding how barriers to entry and exit affect the distribution of benefits between consumers and firms is crucial to comprehending their ethical implications.

Entry Barriers

Entry barriers can be broadly classified according to whether they are internally based or externally based. Internally based barriers to entry appear when managers make investments that give their firm a competitive advantage, thus allowing them to charge above-average prices, capture high market share, and/or benefit from an extraordinary cost position. Such investments develop into entry barriers when they become costly enough to discourage potential new firm entrants. Externally based barriers to entry appear when managers successfully influence key external stakeholders to impose policies that render entry by potential competitors into the industry impossible or unreasonably complex.

Internally Based Barriers to Entry

There are two categories of internally based barriers to entry—explicit and tacit. First, explicit, internally based barriers to entry are tangible and easily measurable. The costs and benefits that emerge from these barriers to both firms and consumers are clear. High fixed costs are one of the main types of internally based barriers to entry. For example, the costs involved in exploring for oil and then constructing the pipeline infrastructure to bring oil, once discovered, to a port or a refinery are enormous, even when oil is found quickly. It is very difficult for potential new firms to enter oil and gas production because of the massive capital investment required to bring the product to market.

Strategic lock-in, in which a firm attempts to retain customers in the long term, is another example of an explicit, internally based barrier to entry. For example, commercial airline frequent-flyer programs are designed to “lock in” passengers on future flights; a customer is more likely to remain brand-loyal if he or she needs only a few more flights in a year to qualify for free upgrades. This lock-in of future customer purchases raises the cost of entry to new firms in the product market or industry by increasing the switching costs customers face in transferring their business from existing firms to new firms.

Similarly, some firms erect barriers to entry with the intent of creating a form of strategic “lock-out.” The recent consolidation in the telephone industry illustrates this. When Baby Bell SBC acquired the weakening long-distance firm AT&T, it gained the best long-distance carrier in the industry—that is, the firm with the best assets and a national reputation for quality in the long-distance market, where many of the Baby Bells are weak. Thus, SBC may have locked out its long-distance rivals from competing effectively against it in the future by taking the best-asset long-distance carrier (AT&T) off the market and by leaving weaker acquisition targets (such as MCI) for rival acquirers. A similar pattern occurred in global commercial airlines following deregulation.

Explicit, internally based barriers to entry provide relatively equal benefits to both consumers and firms. Firms benefit from a limited level of competition, thus allowing them to enjoy higher payback levels against their initial investments. Consumers benefit from greater access to the product in the case of the oil refinery, lower prices in the case of frequent-flyer programs, and higher quality in the case of SBC and AT&T. Explicit, internally based barriers to entry engender commutative justice for both firms and consumers, since both parties benefit fairly from having the barriers in place and both are left better off as a result.

The second category of internally based barriers to entry consists of tacit barriers. The characteristics of tacit barriers are often intangible or vague. The costs and benefits for firms and consumers are difficult to track. Super brands—brands with global recognition—such as Coke or Pepsi provide the most well-known example of tacit, internally based barriers to entry. Any firm entering the markets in which Coke or Pepsi operate, for example, would face great difficulty in credibly challenging the products of those two firms. Many customers will buy only Coke or Pepsi soft drinks. The Coke or Pepsi brand is a form of tacit barrier that has come into existence over time, with millions of dollars of investments in all facets of marketing. It has taken decades for Coke and Pepsi to develop their brand identities and consumer loyalties; such a resource is almost impossible for a competitor to duplicate quickly, and thus, many potential competitors do not enter those markets.

The brand, a tacit barrier to entry, is a costly endeavor for a firm. When successful, it allows firms to recoup significantly above-average returns by charging the consumer substantially high prices. However, consumers who purchase these products often do so with the belief that they are high-quality products and/or represent an image with which they wish to be associated. This reciprocal relationship between firms and consumers, although measurably benefiting firms more than consumers, seems to satisfy the argument for commutative justice—that is, where benefits are distributed to both parties, not necessarily equally but reasonably enough to warrant future exchange.

In the case of super brands, they tend to dominate their particular industry segment by dominating advertising media, distribution channels, and retail shelf space, thus enjoying monopolistic power. Super brands such as Pampers, Coke, and Kleenex are good examples. The risk inherent in super brands is that they often become powerful enough to decrease consumer choice, thus violating the norms of distributive justice in favor of benefits to the firm. Although many anticompetitive agencies attempt to rein in violators, super brands sustain their power by purchasing other strongly branded products. This maintains the pretence of fair competition while increasing the super brand's power over competition; Coke is a key example, selling beverages with over 500 different brand names globally. Adidas recently acquiring Reebok or Starbucks acquiring Seattle's Best Coffee are examples of brands increasing their market power while maintaining the pretence of competition.

Externally Based Barriers to Entry

Similar to internally based barriers to entry, externally based barriers can also be divided into two categories. The first category consists of externally based barriers to entry that have the goal of producing a public good. These are typically the result of an agreement between specific firms in the industry and a particular stakeholder, typically from the government. The second category consists of barriers that have the goal of producing a private good.

Best-known in the category of barriers with the goal of producing a public good are public policies that restrict competition in a product market or industry. For example, patents, a form of an externally based barrier to entry, allow pharmaceutical firms enough time to earn a payback on their research and development (R&D) costs. For successful drugs, it takes 7 years to bring a drug along the various phases of R&D and can cost hundreds of millions of dollars. By sanctioning monopoly status for the drug, both firms and consumers benefit. Pharmaceutical firms are encouraged to continue investing in innovation and scientific discovery, and consumers benefit from access to new lifesaving technologies. Of course, some pharmaceutical firms use patent protection solely for private gain. For example, some firms seek patents for minor changes to existing drugs (so-called cosmetic changes that do not result in a therapeutically new or distinct drug) whose patent protection will shortly expire, simply to erect entry barriers for generic drug companies.

Other industries where we see legally sanctioned monopolies are telecommunications, banking, cable, electricity, gas, water, and transportation. These industries are also often the ones in which scale economies are so high that only one firm can profitably recoup the costs of infrastructure investment. This was the rationale for telephone service in the United States being provided solely by AT&T until 1984; constructing phone lines nationwide was so costly that one firm needed the entire national market to recover its infrastructure costs profitably. Without a legally sanctioned monopoly in the early phases of the telephone service industry, its growth would have been much slower, leaving consumers and firms alike to suffer the consequences. During their protected phase, legally sanctioned monopolies can earn very high levels of profits. Some would argue that this skews the distribution of benefits in favor of firms. We suggest that the payback risk assumed by firms such as pharmaceutical companies undertaking R&D or companies engaging in infrastructure development is very high. Therefore, although they may reap significant benefits, these are fair and warranted. We suggest, therefore, that barriers to entry that have the goal of producing a public good benefit firms and consumers by meeting the threshold for distributive justice.

When barriers to entry are intended to produce a private good, they benefit firms more than they benefit consumers. A typical example is tariffs and other types of trade restrictions, such as quotas, that prevent entry to foreign (exporting) firms in a product market or industry. They do so by raising the price of the foreign product (the import) relative to the price of the domestically produced price (by the amount of the tariff), thus deterring the entry of foreign firms. Subsidies also dampen competition by giving subsidized firms a cost advantage over nonsubsidized firms, which must be proportionally more efficient than their subsidized competitors to be able to meet the price of the subsidized firm and still recover their costs. Despite these higher levels of efficiency, nonsubsidized firms are unable to pass on the benefits of their efficiencies to consumers, while subsidized firms are disincentivized to become more efficient. Under these circumstances, consumers experience measurable losses in terms of paying higher prices and supporting inefficient, and often underperforming, industries. Agriculture is probably the most frequently subsidized industry internationally, but subsidies are also paid to high-technology industries, such as the highly visible public underwriting of Airbus Industrie's R&D costs by a consortium of European governments.

Similarly, many developed nations require occupational licensing; in the United States, there are over 500 occupations that require licensing. Occupational licensing is an externally based barrier to entry that effectively limits economic opportunity by restricting access to many occupations to those individuals able to pay for the required training and testing.

In contrast to the above example, which focuses on public policy to restrict entry, there are certain private agreements that restrict entry by potential competitors. The best example of this occurs in distribution channels. Retail stores, for example, have only a limited amount of shelf space on which to display products. If a drugstore has already committed half its shelf space for one brand of cosmetics, for example, then the odds of a competing cosmetics manufacturer receiving access to critical retail distribution channels is lessened. Many potential entrants are discouraged in industries with a relatively fixed supply of distribution. Apart from retail industries, commercial airlines face a similar bottleneck in airport gates. Departure/arrival gates are critical to being able to offer air transportation, yet almost all gates at most airports are already fully booked or owned by existing carriers. The existing contracts that govern access to gates are a steep obstacle for any potential new airline to overcome. In both these examples of private agreements that restrict entry, firms benefit at the expense of consumers. In both examples, competition is limited in a way that allows the protected firms to behave in a monopolistic manner by raising prices; consumers lose, and an unjust distribution of benefits prevails.

Exit Barriers

The main impact of exit barriers is to increase competition among the firms in a product market or industry by increasing the costs of leaving the industry during hard times. Firms within an industry typically seek to erect barriers to entry to protect them from outside competition, allowing them to earn above-average profits. However, firms are unlikely to erect barriers to exit intentionally since they impede mobility, increase competition, and encumber profitability.

There are two main kinds of exit barriers—operational and reputation based. First, operational exit barriers are firm characteristics such as high fixed costs or highly asset-specific investments that are required for the firm to operate within the industry. An example of a high fixed-cost exit barrier is a new

Table 1 Main Types of Entry and Exit Barriers and Their Ethical Implications

	Consumer Benefits	*Firm Benefits*	*Ethical Implications*
Explicit internally based barrier to entry	High	High	Commutative justice
Implicit internally based barrier to entry	Low	High	Distributive justice tending toward injustice
Externally based barriers to entry intended to create a public good	High	High	Commutative justice
Externally based barriers to entry intended to create a private good	Low	High	Injustice
Exit barriers	High	Low	Injustice

semiconductor fabrication plant, which costs about $5 billion. Even if the price of semiconductors drops dramatically and margins are adversely affected, most firms having made this large capital investment would remain in business in the hope that prices would increase and they could recoup their investment. The profitability threshold for exit decisions tends to be greatly altered when there is a costly and highly asset-specific investment involved.

Second, reputation-based barriers prevent easy exit from an industry when a firm encounters difficult macroeconomic or firm-specific conditions. Consider the case of a business school that has faced steeply declining student enrollment for years. Most managers when faced with such circumstances would seriously consider closing the business. No university administrator would seriously contemplate this, however, because the negative impact on the remaining schools and divisions in the university would be severe. Who would feel comfortable attending a school that might pull the rug out on the program at any moment and thereby devalue the degrees of all alumni? Similarly, consider relationship spillover effects: two firms may benefit from a long-standing joint venture that is highly profitable. Then, something changes for one or both partners to render the venture unprofitable; firms in such relationships are often reluctant to exit because they do not want to earn a reputation for being unable to maintain business-to-business relationships. Finally, managerial pride or arrogance often serves as a reputation-based exit barrier. For example, managers will be so committed to a strategy that they will escalate the strategy, despite clear signals to exit the product market or industry. In all these examples, an underperforming segment of a business is retained when it should not be to preserve the broader reputation of the entity. Exit barriers, thus, lock firms into industries even when expected returns fall short of a breakeven point. When exit barriers are high, firms often become fixated on contributing to their margins and drop prices significantly. In the short term, consumers benefit from unusually low pricing, and firms often experience losses. Over the long term, these industries typically experience a great deal of shakeout and sometime collapse. Indeed, the distribution of benefits engendered by exit barriers is unjustly skewed in favor of consumers at the expense of firm benefits.

In summary, entry and exit barriers influence competition and, thus, the distribution of benefits between firms and consumers (see Table 1). Different types of entry and exit barriers influence this distribution in different ways, sometimes achieving the goal of commutative justice or distributive justice and sometimes resulting in an unjust distribution.

—Ariff Kachra and Karen Schnietz

See also Brands; Commutative Theory of Justice; Competition; Copyrights; Corporate Political Advocacy; Cost-Benefit Analysis; Economic Efficiency; Economic Incentives; Economic Rationality; Economies of Scale; Enron Corporation; Justice, Distributive; Perfect Markets and Market Imperfections; Profits; Public Goods; Rawls, John; Regulation and Regulatory Agencies; Rents, Economic; Subsidies; Tariffs and Quotas; Transaction Costs

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BARTER

Barter is the direct exchange of goods or services without the use of money as an intermediary. It is often assumed that bartering is an exchange system limited to nonliterate societies, collapsing states, and the margins of official economies, but it is important to recognize that bartering plays a role in any economic system. Adam Smith famously asserted that it is part of human nature, removed from any utilitarian motivation, to truck, barter, and exchange one thing for another. According to a strict definition, barter demands both that each exchange is balanced and that the exchanged goods are actually desired by the acquiring parties. The first postulate assumes that each meeting results in a trade that both parties deem fair and that neither party walks away with any debts or obligations. In practice, delayed transactions and various forms of credit are often worked into barter systems. The second postulate assumes that the parties are trading to meet some demand or, in other words, that the traded goods have an immediate use-value for their recipients. When one party acquires goods that are not needed with an eye toward retrading them at a future date, such goods are basically functioning as a unit of exchange. For example, in a black market economy such as the one in a prison, a pack of cigarettes may function simultaneously as a commodity and as a medium of exchange. In such cases, multiple commodities can potentially act as media of exchange. Anthropologists often define barter as a purely economic transaction, to distinguish it from other forms of nonmonetary exchange that have more of a social than an economic function, the most widely cited example being the exchange of gifts.

The term *countertrade* refers to modern agreements where goods or services are reciprocally exchanged without pure cash transactions. *Countertrade* has become an umbrella term that encompasses a number of practices in addition to simple bartering, including bilateral clearing, compensation arrangements, counterpurchases, offsets, production sharing, switch transactions, and technology transfers. Estimates of countertrade as a percentage of world trade differ widely, ranging from 5% to 40%. Countertrade was a standard component of Soviet-bloc trade, especially in the 1980s, and continues to play a major role in trade with developing nations. The primary motivations for countertrade are large debts, hyperinflation, a lack of hard currency with which to import goods, and a desire to promote exports in new markets. Less scrupulous companies have used countertrade to avoid or minimize taxes. The tax codes of most countries consider the value of what is changing hands the equivalent of a cash purchase, but the complexity of many of these transactions allows for "creative" accounting practices in determining revenue. Countertrade can be risky and quite complex, but many companies see a willingness to engage in countertrade as a competitive advantage. Countertrade has been criticized as running contrary to the principles of free trade by fostering bilateral agreements and tampering with markets.

—Clark Farmer

See also Black Market; Developing World; International Trade; Underground Economy

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Bayesian Approach

Named after the 18th-century English cleric Thomas Bayes, the Bayesian approach refers to a distinctive framework for decision making. Accepting the dictum that "probability is the guide to life," the Bayesian approach provides a model for rational choice in which the expected utility of an action is determined in relation to a person's notions of the probabilities and utilities associated with the potential outcomes of the action under consideration. In considering alternative courses of action, the Bayesian principle is to choose an action with the greatest expected utility. The Bayesian approach has been widely influential in the development of rational choice theory and has been used in the study of rational choice in diverse disciplines, including management science and economics. Three elements central to the Bayesian approach include the Bayesian account of belief, rationality, and learning.

Bayesian Belief

There are two key aspects involved in the epistemology of the Bayesian approach toward belief. The first is that beliefs come in varying degrees of strength. According to Bayesians, beliefs are probabilistic in nature rather than all or nothing. Thus, in the Bayesian approach, we can assign probabilistic values, represented by numbers between 0 (no confidence) and 1 (full confidence), to beliefs, based on the degree of strength that persons have in those beliefs. In the Bayesian approach, the strength of a belief corresponds to the level of confidence that a person has in the truth of the proposition expressed by that belief, which, in turn, can be determined by a consideration of what gamble that person would be willing to accept as fair on the truth of that proposition. Most Bayesians now admit that it is unrealistic to think that most persons can assign numerically precise values to the strength of their beliefs. Bayesians, generally, now only hold that we can represent the beliefs of people in terms of some confidence measure, which orders their beliefs on the basis of their comparative confidence in those beliefs.

Second, since the Bayesian approach takes the strength of a belief to represent the actual conviction that a person has in the truth of that belief, Bayesians endorse a subjectivist approach to probability. Since people do often disagree on the degree to which they believe a given proposition, such a subjective view of probability denies that there are objectively correct probability values that attach to individual beliefs. For instance, if Smith believes Proposition p to Degree x, but Jones believes Proposition p to Degree y, there is, according to the Bayesians, no objective fact about which value is closer to the truth. This subjectivism about belief in the Bayesian approach has been the subject of much criticism, since it seems to imply that it is rational for individuals to assign any degree of probability whatsoever to their beliefs. In response, however, Bayesians point toward their account of rational coherence and rational learning as ways of mitigating the force of such a criticism.

Bayesian Rationality

Although the Bayesian approach places no restrictions on people's assignment of probabilities to individual beliefs, it is not the case that any numerical assignment that agents assign to their beliefs is acceptable within Bayesianism. The Bayesian approach requires that the assignments that persons give their beliefs must obey the axioms of the probability calculus. That is, while Bayesians place no restrictions on the assignment of individual probabilities, they do place important restrictions on the assignments that persons can place on their beliefs taken as a set. In this regard, the Bayesian approach can be seen as offering a type of coherence theory of rational belief formation, since it requires that a person's assignment of probabilities be internally consistent.

Not only does the Bayesian approach require that a person's assignment of probabilities conform to the probability calculus, but it also offers a notable justification for this requirement, known as the Dutch Book argument. The argument attempts to show that anyone whose beliefs violate the laws of the probability calculus is practically irrational. Informally, a Dutch Book is made against a person whenever that person accepts a series of bets such that this person will lose no matter what turns out. Such a situation will arise when a person assigns a degree of belief to a statement (or statements) that conflicts (according to the probability calculus) with the degrees of belief that the person assigns to other statements. For instance, according to the probability calculus, if a person assigns the probability .5 to some statement X, then he or she ought to assign the probability .5 to the statement not-*X*. If a person who assigned the value .5 to *X* violated this condition and assigned a probability of, say, .8 to not-*X*, then there would be some series of bets that such a person would consider as being fair on *X* and not-*X*, given the probabilities he or she assigned these statements, on which, nonetheless, he or she would lose money no matter whether *X* or not-*X* turned out to be true. Building on this idea, the Dutch Book theorem is meant to show that persons who violate the laws of probability will end up performing actions that make them less well off, on their own terms, than some available alternative when they attempt to maximize their expected utility. Thus, the Dutch Book argument shows that agents who violate the laws of probability will be practically irrational in committing themselves to actions that, according to their own preferences, will make them worse off.

The Bayesian approach to rationality is particularly connected to the classical notion of economic rationality, since it supposes both that rationality involves maximization and that the relevant values of outcomes are subject to numerical quantification. As to the first point, Bayesians generally accept that a rational agent should choose the act that has the greatest subjective expected utility, a principle standard to classical economic thought and one that has close ties to typical forms of cost-benefit analysis. With regard to the second point, the Bayesian approach has obviously been seen as particularly fecund in analyzing behavior in economic contexts in which the outcomes in question can be assigned numerically ordered values, such as dollar values. While both of these points have made the Bayesian approach especially attractive to those working in the classical economic tradition, they have also, and for the same reasons, attracted criticisms with regard to the adequacy of the Bayesian approach in providing a foundation for rational choice. On the first point, critics have raised concerns as to whether the notion of rationality as subjective maximization is compatible with respect for moral rights, since actions of maximal expected value may well often involve the violation of individual rights. As to the second point, some critics have concerns about the supposition that all relevant outcomes can be given numerically ordered values in the way that the Bayesian approach supposes. Such critics have been particularly concerned with the tendency in economic thinking to use dollar values to rank all outcomes, especially when those outcomes involve noncommercial goods, such as human lives or environmental damages.

Bayesian Learning and Bayes's Theorem

The Bayesian approach also maintains that although the initial assignments that different persons give to a particular belief may differ initially, their degrees of confidence will converge as they take in new evidence. In this vein, Bayesians argue that as new evidence arises, people will move toward intersubjective agreement in their assignment of probabilities. This convergence is because the Bayesian approach sees learning as conditionalization, in which persons update their prior beliefs conditional on new information. Bayes's theorem, which can be deduced from the probability calculus, stipulates that where *E* represents some new evidence and *H* represents an initial hypothesis, the posterior probability of *H* conditional on *E*, or $\Pr(H/E)$, can be calculated by the following formula:

$$\Pr(H/E) = [\Pr(H) \times \Pr(E/H)]/\Pr(E).$$

Thus, even if two different persons start out with widely different prior probability assignments to *H*, as they both accommodate new evidence, the posterior probabilities they assign to *H* will begin to merge together. This Bayesian notion of learning through conditionalization has been widely appealed to in other contexts as well, including the development of spam-filtering programs for e-mail.

While the Bayesian account of internal consistency and intersubjective learning may allay some of the worries about the subjective nature of the Bayesian approach, some critics still see the Bayesian approach to rational choice as too internalistic in nature. They argue that a plausible theory of rationality must also be supplemented by the use of some external principles of rational choice to properly evaluate and justify an individual's prior belief formation. In this regard, and as previously noted, the Bayesian approach has been seen by many as central to the economic notion of rationality, and the criticisms of the Bayesian approach are akin to more general concerns about whether the economic notion of rationality is too narrow in its scope.

—Daniel E. Palmer

See also Cost-Benefit Analysis; Economic Rationality; Expected Utility; Rational Choice Theory; Rationality; Utility, Principle of

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BENEFITS, EMPLOYEE

Employee benefits are the noncash compensation offered by employers to their employees as part of the total compensation package. The benefits offered by employers generally reflect a basic care and concern for the well-being of employees and the importance of that well-being to employee productivity. For the most part, employee benefits may be placed in one of three categories: health-related insurance, financial insurance, and quality-of-life benefits.

Health-related benefits, which include health, dental, vision, and disability insurance, are designed to provide for the health care needs of employees and, in many instances, may be extended to include their spouses and/or dependent children. The purpose of financial insurance, which includes retirement and pension plans, life insurance, and flexible spending accounts, is to help employees become more financially secure. Quality-of-life benefits, which have grown increasingly important to employees in recent years, help employees live less stressful lives by maintaining a healthy work-life balance. Quality-of-life benefits includes personal and parental leave time, on-site child care, day care subsidies, paid holidays, flexible work schedules, employee assistance programs (EAP), concierge services, and a plethora of additional elective benefits, such as insurance for their homes, pets, and long-term care.

Employee benefits may be further classified as voluntary or mandatory. Mandatory benefits are those that employers are required to provide by law and include social security, Medicare, and unemployment and disability insurance. Voluntary benefits are health care and retirement plans, as well as other elective benefits that employers provide above and beyond what is required by the government.

Employee benefits as an essential feature of the total compensation package grew out of the U.S. labor movement. The Norris-LaGuardia Act of 1932 and the Wagner Act of 1935 guaranteed employees the right to join unions and required employers to engage in good faith collective bargaining. In 1949, labor unions won the right to include employee benefits in the bargaining agreement.

The rapid growth throughout the 1950s and 1960s in the number of employers that offered benefits as part of the total compensation package reflected an expanded social consciousness in which employers felt increasingly obliged to invest in the total well-being of their employees. The growth in employee benefits was further facilitated by a strong economy and the tax incentives that the government made available to firms that provided benefits. Subsequently, by the 1970s, almost all employers offered some type of employee benefits to their regular full-time employees, primarily health insurance and retirement plans.

With so many individuals now dependent on employee benefits programs for their health care and retirement, legislation was enacted to safeguard their rights as participants in these programs. The Employee Retirement Income Security Act (ERISA) of 1974 established minimum standards for most voluntary pension and health care plans in private industry to provide protection for the employees participating in these plans. ERISA requires employers to provide employees with detailed information including the benefits plan features and funding, defines the fiduciary responsibilities of those who manage and control plan assets, requires plans to establish a grievance and appeals process for participants to get benefits from their plans, and gives participants the right to sue for benefits and breaches of fiduciary duty.

Today, few view employee benefits as optional; they are largely perceived as an essential part of the employee's total compensation package. A strong benefits package that meets the broad array of needs of a diverse workforce is critical for most employers to recruit and retain the best talent. Most employers are legitimately concerned about the physical and financial well-being of their employees; however, the rising costs of health care and retirement benefits and the continued pressure to improve existing benefits while remaining competitive in a global economy present a significant challenge.

Benefits now encompass a significant portion of the total human resources budget. In 2003, U.S. employers spent $1.18 trillion on voluntary and mandatory benefits programs, including $569.1 for retirement benefits, $501.4 for health care benefits, and $114.1 for other types of benefits. The dramatic growth in the cost of health care benefits, which is projected to soon surpass the cost of retirement benefits, may be most alarming for employers. As a result, employers have taken various steps to rein in the costs.

Many employers, for example, have shifted their retirement programs from defined benefit to defined contribution plans. In a defined benefit plan, the employer guarantees that employees will receive a specified sum on retirement and as such is required to pay this sum regardless of the actual financial performance of the retirement fund investments. Employers offering defined benefit plans have also seen an increase in the financial burden of funding these programs due, in part, to the increase in the average life span of retirees and the mandatory cost-of-living adjustments these plans require.

In a defined contribution plan, the employers specify the amount of money they will contribute to employees' retirement savings; however, the employees assume all the investment risk. Employees are generally responsible for determining how to allocate the savings among various investment options, and the dollar value of the benefits received on retirement is dependent on the financial performance of their investments. In many instances, the employer's contribution to the plan depends on the amount that the employee contributes; if the employee opts not to contribute, he or she does not receive the benefit.

Another step employers have taken to control their benefits costs is to pass more of the expense on to employees, particularly the cost of health care insurance. Many employers require employees to absorb an increasingly greater portion of the insurance premiums, as well as to make larger copayments for doctor visits, medical procedures, and prescription drugs. As a result, there has been a dramatic rise in the number of workers who go without health care insurance, even though their employers offer it, because they cannot afford it.

Controlling benefits costs is a key factor driving many companies to fill vacated or new positions with temporary or contract employees, who are not entitled to receive the same benefits as regular, full-time employees, or to outsource functions to external providers. Many have resorted to relocating operations to countries where benefits costs are comparatively low or are not required as part of the compensation package. Still others have opted to reduce or eliminate the benefits offered to retirees.

Some are predicting that within the next 10 years, the costs of providing benefits will cause many employers to move away from covering benefits for employees. Benefits advocates argue that the costs of the health, financial, and quality-of-life benefits offered by employers is offset by reduced costs in other areas such as worker's compensation, greater ease in recruiting and retention, and increased productivity due to reduced absenteeism and employee stress. Many who take a paternalistic view of the relationship between the organization and its employees contend that organizations that exist to serve people should also serve the needs of their own employees.

Many employers contend that the benefits from offering comprehensive benefits packages to their employees are being outstripped by the costs. Employers increasingly argue that the best way to control the costs is to make employees more accountable for managing their own benefits. Just as defined contribution retirement plans have replaced traditional defined benefit plans as the prevailing choice for retirement insurance, many are predicting that defined contribution health plans, in which employers contribute a specific sum to each employee's health spending account and empower the employee to determine how to spend those dollars for health care, will one day become the standard for health-related benefits. Opponents of these plans argue that they will shift more of the burden of paying for health onto those who are less healthy. Critics also worry that individuals will be poor purchasers of care on their own and susceptible to scam artists. Most agree that society in general benefits from a healthier and more financially secure citizenry; however, the debate as to who should be responsible for providing these benefits—employers, the government, or individuals themselves—is likely to increase as the costs continue to escalate.

—Carmen M. Alston

See also Business Ethics and Health Care; Employee Assistance Programs; Employee Retirement Income Security Act of 1974 (ERISA); Employee Stock Ownership Plans (ESOPs); Family-Friendly Corporation; Health Maintenance Organizations (HMOs); Norris-LaGuardia Act of 1932; Outsourcing; Pension Benefit Guaranty Corporation (PBGC); Pensions; Work and Family; Work-Life Balance

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Benevolence and Beneficence

Many problems in business ethics involve questions about the obligations and motives of beneficence. Diverse examples are obligations to protect Internet users from obscene materials, responsibilities for human subjects in pharmaceutical research, paternalistic policies of consumer protection, government actions to control markets in the public interest, policies to improve the welfare of farm animals, benefit packages for employees, ideals of corporate philanthropy, obligations for poverty-related ill health, programs to benefit children and the incompetent, preferential hiring policies, and many environmental protection programs.

The Concepts of Beneficence and Benevolence

The term *beneficence* connotes acts of mercy, kindness, and charity, and perhaps even altruism, love, and humanity. In ordinary language, the notion is broad, but it is understood even more broadly in ethical theory, to include effectively all forms of action intended to benefit other persons. The language of a *principle* or *rule* of beneficence refers to a normative statement of a moral obligation to act for the benefit of others, helping them further their important and legitimate interests, often by preventing or removing possible harms. Many dimensions of business ethics appear to incorporate appeals to beneficence in this sense, even if elliptically. For example, when cigarette manufacturers are criticized for the way they market their products, the ultimate goal is the beneficent one of removing conditions that cause harm to persons. Similarly, when apparel manufacturers are criticized for not having good labor practices in factories, the ultimate goal is to obtain better working conditions, wages, and benefits for workers.

Whereas *beneficence* refers to an action done to benefit others, *benevolence* refers to the socially valuable character trait—or virtue—of being disposed to act for the benefit of others. An account of moral *motives* is often connected to a theory of the virtues, and benevolence has sometimes served as the prime example—for example, in the ethical theories of Francis Hutcheson and David Hume. Benevolence has seemed to these writers close to the essence of morality itself.

Acts of beneficence may be done from obligation, but they may also be performed from nonobligatory moral ideals, which are optional. However, not all exceptional beneficence rises to the level of the moral saint or moral hero. Saintly beneficence and benevolence are at the extreme end of a continuum of beneficent conduct and commitment that exceeds duty. A celebrated, though fuzzy, example of beneficence that rests somewhere on this continuum is the New Testament parable of the "good Samaritan." In this parable, robbers have beaten and left half-dead a man traveling from Jerusalem to Jericho. A Samaritan takes compassion on him, tends to his wounds, takes him to an inn, and stays with him. The Samaritan's actions are clearly beneficent and the motives benevolent. However, they do not seem—on the information given—to rise to the level of heroic or saintly conduct. The morally exceptional, beneficent person, then, may be laudable and worthy of emulation yet neither a moral saint nor a moral hero.

Historical Place in Ethical Theory

Celebrated writings in the history of ethical theory suggest that there is no one correct way to think about beneficence and benevolence. Several landmark ethical theories embrace these notions, in assorted ways. Utilitarianism is the most notable example, because its principle of utility is, in effect, nothing but a strong and demanding principle of beneficence. Other distinguished theories, such as Hume's moral psychology and virtue ethics, are not as demanding as utilitarianism but nonetheless make benevolence and utility their centerpieces. All such theories closely associate the goal of benefiting others with the goal of morality itself.

Many other writers in the history of ethics make beneficence even less of a centerpiece yet maintain that obligations to confer benefits, prevent and remove harms, and weigh and balance an action's possible goods against its costs and possible harms are central to the moral life. In a renowned theory, Immanuel Kant argued that everyone has a duty to be beneficent—that is, to be helpful to others according to one's means and without hoping for any form of personal gain thereby. Benevolence he regarded as unlimited, whereas beneficence done from duty should not be viewed as placing unlimited demands on persons. Kant abstractly anticipated what, as noted below, have become several key issues about beneficence.

Predictably, deep disagreements have emerged regarding how much is demanded by *obligations* of beneficence and also about whether these obligations have anything to do with business. An impressive body of work has been done in recent years on Adam Smith's moral psychology and economic model for business ethics. His views about the role and place of benevolence in business have interesting implications for how we should understand the roles and obligations of businesses. Smith says that the wealth of nations is dependent on social cooperation but is not dependent on the benevolence that characterizes moral relations. Market societies, he argues, depend heavily on cooperation, yet it would be vain for us to expect benevolence when interacting in market societies. In commercial transactions, he says, the only successful strategy is to appeal to personal advantage: Never expect benevolence from a butcher, brewer, or baker; expect from them only a regard to their own interest. Market societies operate not by concerns of humanity but rather from self-love.

Mixed and Pure Beneficence

Several key problems in business ethics today can be framed as attempts to come to grips with Smith's view. Discussions of the role of the corporation in society and the very purpose of a corporation as a social institution are examples. It is not disputed today that the purpose of a for-profit corporation is to make a profit for stockholders, but there has been an intense debate about whether maximizing stockholder profits is the *sole* legitimate purpose of a corporation—as Milton Friedman and others have notoriously argued—and whether beneficent corporate conduct is justifiable. This is a normative question, but there is also the question of moral psychology raised by Smith: Is it reasonable to expect benevolent acts from the business community?

Some corporate social programs appear to involve a *mixture* of limited beneficence and self-interested goals such as developing and sustaining relationships with customers. An example is found in public utilities programs to help customers pay for electricity, gas, oil, phone service, and the like. These programs often decrease rather than increase corporate profits. They are, in effect, a form of corporate philanthropy. The programs locate and attempt to remedy the root causes of bill nonpayment, which typically involve financial distress. The programs also seek to rescue people in the community who are in unfortunate circumstances because of industrial injury, the ill health of a spouse or child, drug dependency, and the like. The company may even pay for consumer advocates, who are social workers trained to deal with customers and their problems. These programs, by design, make life much better for various unlucky members of the community. They therefore have a strong appearance of beneficence, but they may not be entirely motivated by benevolence because they may also be designed to achieve a positive public image as well as payment of overdue bills.

In contrast, some firms have charitable programs that seem to be cases of pure beneficence (not admixed with some form of outreach that will help the company). Money is taken directly out of profits, with no expected return benefits. It has been questioned, however, whether even programs of this description are instances of pure benevolence. In the precedent U.S. case of *A. P. Smith Manufacturing v. Barlow* of 1953, a judge determined that a beneficent charitable donation to Princeton University by A. P. Smith Co. was a legitimate act of beneficence by responsible corporate officers. However, the judge acknowledged that such beneficence may not be pure beneficence but rather an act taken in the best interest of the corporation by building its public image and esteem. In effect, the judge suggests that such a gift, while beneficent, may not derive from entirely benevolent motives.

If beneficent acts by corporations are actually nothing more than clever ways to maximize profits, then these actions seem to satisfy Friedman's demands. However, such a simple reconciliation of Friedman and corporate beneficence accounts does not reach down to the question of proper moral motive. Most moral philosophers have insisted that a morally meritorious act of beneficence must come from true benevolence—that is, purely benevolent motives. Apart from this problem, it is unlikely that an easy reconciliation of Friedman's views and beneficence-oriented ones is possible. Consider stakeholder theory, which arose, in part, as an effort to broaden our horizons regarding who should legitimately benefit from corporate profits. In the classical profit-to-stockholder view, stockholders' interests were supreme, but what about the interests of other stakeholders, particularly those whose efforts are necessary for a firm's survival and flourishing? Who deserves to benefit?

Even beyond stakeholders, might there be obligations of beneficence to some larger community? In a statement of "The Johnson and Johnson Way," in the Johnson and Johnson Company credo, it is said that Johnson and Johnson is responsible to the communities in which it thrives, indeed to the world community. The company asserts an obligation to be good citizens, including the support of charities, the encouragement of civic progress, the bettering of public health, and the improvement of education. Johnson and Johnson and many other companies assert that they have obligations to these ends, but to many writers in business ethics, this claim of obligations seems misguided: The moral demands here seem more like ideals or commitments, especially if they reach out to the world community. This takes us to a critical distinction between obligatory and ideal beneficence.

Obligatory and Ideal Beneficence

Some ethical theories insist not only that there are obligations of beneficence but that these obligations demand severe sacrifice and extreme generosity in the moral life. In some formulations of utilitarianism, for example, it appears that we may have obligations to give our job to a person who needs it more, give away a substantial part of our income, devote much of our time to civic enterprises, and so on. Few societies, it appears, have ever operated on such a demanding principle, but it does seem embraced, at least abstractly, by a large number of moral philosophers, including many utilitarians and Kantians.

Predictably, many other moral philosophers have denied that we have such demanding obligations, and some have argued that we have no general obligations of beneficence at all—only obligations deriving from specific roles and assignments of duty. A decisive example of the latter is found in the contemporary moral theory of Bernard Gert, who maintains that there are no *moral obligations* of beneficence, only *moral ideals* of beneficence. For Gert, the general goal of morality is to minimize evil or harm, not to promote good. Rational persons can act impartially at all times with regard to all persons with the aim of not causing evil, he argues, but rational persons cannot impartially promote the good of all persons at all times.

Philosophers such as Gert who reject the principles of obligatory beneficence draw the line at obligations of *nonmaleficence.* That is, they embrace rules that prohibit causing harm to other persons, even though they reject all principles or rules that require *helping* other persons or acting to prevent harm. Thus, they accept moral principles such as "Don't kill," "Don't cause pain or suffering to others," "Don't incapacitate others," "Don't deprive others of the goods of life," and the like. However, the mainstream of moral philosophy has been to make *both* not-harming and helping to be obligations while preserving the distinction between the two.

Some philosophers defend an exceedingly demanding principle of obligatory beneficence. In a widely discussed theory of "the obligation to assist," Peter Singer distinguished—in his early work on the subject—between preventing evil and promoting good. He contended that if it is under our control to prevent something bad from happening, without our having to sacrifice anything of comparable moral importance, then we are morally obligated to do it. In other words, we ought to donate time and resources until we reach a level at which, by giving more, we would cause as much suffering to ourselves as we would relieve through our gift. This claim implies that morality sometimes requires us to make large sacrifices. In the case of corporations, the wealthier the corporation, the larger its contribution should be to assist others in need.

Singer's proposals struck a number of critics as far too demanding. The requirement that persons or corporations must seriously disrupt their life plans to benefit the poor and underprivileged seemed to these critics to exceed the limits of common moral obligations. They argued that Singer proposes as obligatory what is actually supererogatory—an aspirational moral ideal but not an obligation. In reply, Singer attempted to reformulate his view so that his principle of beneficence does not set too high a standard. He concluded that his principle requires a more guarded formulation using the notion of a level of assistance. In particular, he argued that we should strive for a round percentage of income, around 10%, which means more than a token donation yet not so high as to make us a moral saint. This he proclaimed the minimum that we ought to do to conform to obligations of beneficence.

It is difficult to assess whether such a percentage of income—for a person or a corporation—states one's obligation. But wherever the line of precise limits of obligatory beneficence is drawn, the line is almost certain to be a revisionary one, in the sense that it will draw a sharper boundary on our obligations than exists in ordinary morality. Singer's proposals represent a revision of our ordinary moral outlook, despite its faint presence in the history of Western morality, where it is found primarily in religious obligations of tithing.

Liberty-Limiting Beneficence: The Problem of Paternalism

An important issue about beneficence descends historically from John Stuart Mill's classic work *On Liberty*, in which he argued that paternalism is an indefensible moral position. Paternalism involves an attempt to benefit another person when the other does not prefer to receive the benefit. Paternalism may be defined as the intentional overriding of one person's known preferences or actions by another person, where the person who overrides justifies the action by the goal of benefiting or avoiding harm to the person whose preferences or actions are overridden.

Paternalism is often found in the practices of business and in government regulation of business. For example, many businesses require employees to deduct money from their salary for a retirement account; they may likewise deduct salary money to pay for a life insurance policy. If employees do not want these "benefits," they are not free to reject them. Paternalism is here assumed to be an appropriate liberty-limiting principle. Another commonplace example comes from the construction industry and the chemical industry. If an employee does not wish to wear a particular suit, mask, or other protective device, the company (and also the government) will compel it anyway, often (though not always) for paternalistic reasons.

A much-discussed example at present is the restriction of various pictures, literature, or information—often pornography or violent depictions—on the Internet, in bookstores, and in video stores. Many customers may wish to purchase or receive information about these products, but paternalism often prevails. Arguments are put forward maintaining that those exposed to pornography will harm *themselves* by such exposure—for example, pornography might reinforce their emotional problems or render them incapable of love and other distinctively human relationships.

A classic problem of paternalism derives from the principle, often mentioned in business ethics, of *caveat emptor*—Latin for "let the buyer beware." This property-law-derived principle can here be taken as a general principle governing sales: A buyer is responsible for determining any unfitness in a product and is not due any form of refund or exchange unless the seller has actively concealed the unfitness. The buyer is free to either make the purchase or not make it. Many paternalistic restrictions on purchasing have arisen with the objective that buyers will not harm themselves or will not fail to receive benefits that they otherwise might not receive. For example, the control of pharmaceutical products and all controlled substances—through government policies and licensed pharmacies—has often been justified by appeal to paternalism. Many believe that the Food and Drug Administration (FDA) in the United States is fundamentally a paternalistic agency.

As the marketplace for many products has grown more complex and the products themselves more sophisticated, buyers have become more dependent on salespersons to know their products and to tell the truth about them. An engaging question in business ethics is whether a salesperson's role should be viewed as that of paternalistic protector of the buyer. Suppose, for example, that a consumer wants a sprinkler system in his yard to water his grove of evergreens; he loves the sound and look of sprinklers. However, these sprinklers will be worthless for appropriate watering of the roots of his evergreens: The owner needs drip-hose for his large collection of pine, spruce, cedar, and cypress. Should a salesperson insist on selling only drip-hose, refusing to sell sprinkler heads, or should the salesperson acquiesce to the customer's strong preference for sprinklers? Traditionally, salespersons have not viewed their obligations of beneficence in this way, but perhaps paternalistic beneficence would here be a commendable change of practice?

—Tom L. Beauchamp

See also Altruism; Business for Social Responsibility (BSR); Charity, Duty of; Corporate Citizenship; Corporate Social Responsibility (CSR) and Corporate Social Performance (CSP); Corporate Social Responsiveness; Cost-Benefit Analysis; Developing Countries, Business Ethics in; Economics of Well-Being (Post-Welfarist Economics); Income Distribution; Invisible Hand; Justice, Distributive; Living Wage; Paternalism; Profit Maximization, Corporate Social Responsibility as; Public Goods; Redistribution of Wealth; Stewardship; Strategic Philanthropy; Supererogation; Utilitarianism; Virtue Ethics; Welfare Economics

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Bentham, Jeremy (1748–1832)

Jeremy Bentham was born in London, and in 1760, he entered Queen's College, Oxford. When he graduated in 1764, he started the study of law at Lincoln's Inn, London. Bentham never practiced law, although he was qualified to do so, preferring instead to write in favor of both legal reform and the reform of social institutions such as prisons. Indeed, one of Bentham's main projects was the design of the "Panopticon," a model prison where the prisoners could be observed at all times by the guards—who could not themselves be seen by the prisoners.

Drawing on both the English tradition of empiricism and his belief in the power of reason, Bentham held that human behavior could be described scientifically. Some of his major works based on these principles include *A Fragment on Government, Plea for the Constitution*, and *On the Liberty of the Press and Public Discussions.* Bentham believed that all human behavior could be explained by reference to the twin motivations of pleasure and pain.

The theory of psychological hedonism formed the basis of Bentham's account of utilitarianism, the moral view that he helped found and that he famously described in his major work, *Introduction to the Principles of Morals and Legislation.* Utilitarianism was based on the principle of the greatest happiness for the greatest number. According to its proponents, an act was right insofar as it produced the greatest happiness for the greatest number and wrong insofar as it failed to do so. For Bentham, it was not only the happiness of people that mattered morally, but the happiness of all sentient beings counted as well.

This does not mean, however, that Bentham (or other utilitarians, such as James Mill, John Stuart Mill, and, more recently, Peter Singer) believed in “animal rights.” This is because Bentham did not believe that anyone, animal or human, possessed any natural rights at all. That is, Bentham did not believe that any being possessed any rights by nature. Indeed, Bentham is famous for claiming that such rights are nonsense on stilts. Bentham’s rejection of natural rights was informed by his legal philosophy, in which he held that laws are simply commands expressing the will of the sovereign. (This approach to the philosophy of law is termed *legal positivism*, and Bentham had a great influence on 20th-century legal positivists such as J. L. Austin and H. L. A. Hart.) As such, for Bentham, there is no such thing as natural law—and hence no such things as natural rights. All rights are simply legal rights, created by the law. On his death, Bentham was, at his own request, dissected, embalmed, dressed, and placed in a chair at University College, London University, which institution he helped finance through a large bequest.

—James Stacey Taylor

See also Animal Rights; Hedonism, Psychological; Mill, John Stuart; Rights, Theories of; Utilitarianism; Utility; Utility, Principle of

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Berle-Dodd Debate

The Berle-Dodd debate of the early 1930s, between specialists in corporation law, was the opening exchange in the still-raging controversy about shareholder versus stakeholder views of the firm. This controversy concerns the primary purpose of the publicly owned corporation. Adolf A. Berle Jr. proposed that public policy should define a strict fiduciary duty for management. E. M. Dodd Jr. replied in favor of public policy safeguarding multiconstituency and community responsibilities. Dodd may be regarded as a forerunner of stakeholder and corporate social responsibility theories. The debate itself had an important impact on the U.S. securities acts of 1933 and 1934.

The Debate

The debate originated in the perceived problem of separation of investor ownership and management control. Adolph Berle and Gardiner C. Means, then an economics doctoral student at Columbia University, where Berle taught, argued this thesis in *The Modern Corporation and Private Property.* Separation effectively destroyed the traditional property rights basis for shareholder control of business decisions. The shareholder had become purely a “rentier.” Berle’s proposed solution was for public policy to define a strictly fiduciary duty for management. Berle’s article drew on the established legal doctrine of trusts to argue that the manager should be strictly a trustee for assets owned by investors.

Dodd replied that the business corporation had in addition a vital social service function. Dodd made three points. He drew a distinction between the equity (i.e., money) capital of investors and the “capital” of other constituencies defined in terms of their cares and concerns invested in the firm. Dodd argued that the common law had earlier treated business as a public profession; this view had subsequently been limited to businesses deemed to have some public interest. The 19th century was a judicial reversal of the previous common-law tradition. Dodd argued a case for public policy explicitly strengthening customers’ and employees’ rights. Dodd basically agreed with Berle that managers could not be trusted with discretion concerning multiple responsibilities.

Berle responded in a rejoinder that Dodd’s position was an expression of theoretical rather than practical principles. Berle's concern was that weakening of a strict fiduciary duty for managers would prove dangerous in practice. Berle conceded that Dodd had won the debate (at least temporarily) in the sense that social fact and judicial decisions had over time come to support Dodd's general viewpoint against strict fiduciary duty.

Historical Background of the Debate

This debate between two legal experts had roots in the development of corporation law. In the United States, a corporation exists artificially and only in contemplation of the law, according to Chief Justice John Marshall in the 1819 U.S. Supreme Court case *The Trustees of Dartmouth College v. Woodward.* The Michigan Supreme Court addressed the basic elements of the Berle-Dodd debate in 1919 in the case of *Dodge v. Ford Motor Co.* Henry Ford had paid a double dividend for some years (i.e., a regular dividend and a special dividend). He announced his intention not to continue the special dividend in order to reduce prices to customers and increase wages to employees. The Dodge brothers filed suit in state court for continuation of the special dividend. The Michigan Supreme Court ruled that the primary purpose of the investor corporation was investor wealth and supported continuation of the special dividend. The opinion also articulated the business judgment rule, holding that managers and directors are not expected to have perfect judgment but only to exercise business acumen reasonably for the goal of profit seeking. Ford did not use a line of defense that arguably might have proven successful. He could have argued that reducing prices and increasing compensation was a reasonable strategy under the business judgment rule for increasing sales and labor productivity.

In the 1883 case of *Hutton v. West Cork Railway Co.*, Lord Justice Bowen considered whether a company could properly provide gratuities to employees. He concluded that liberal dealing with employees could ease friction and thus benefit the company. This opinion accords with Dodd's view that, in the long run, management consideration of employee welfare would increase shareholder profits.

Effect on Securities Legislation

The Berle-Dodd debate had important impacts on the content of the U.S. securities acts of 1933 and 1934. Berle had significant influence on the drafting of the legislation. Because shareholders did not control management, control must rest on full disclosure of information. Disclosure follows from either Berle's view of the separation of ownership and control or Dodd's view of constituency and social responsibilities. Such disclosure and transparency remain the fundamental philosophy of the securities acts.

Modern Concern With the Debate

The modern version of Berle's thesis was famously stated by the Nobel Prize–winning economist Milton Friedman. He explicitly characterized discretionary corporate social responsibility by managers as theft from the primary stakeholders (customers, employees, and investors alike). In addition to invoking a primitive stakeholder model of the firm, Friedman also noted an irreducible role for customary ethics as well as for public policy. He admitted that companies might need to engage in prudential altruism to forestall even more burdensome public policy developments. In contrast to Friedman, subsequent authors have tended to omit ethics and reduce limitation on managerial conduct strictly to law. The formal version of this line of reasoning is principal-agent theory. Any managerial behavior other than maximizing shareholders' wealth, up to the limits imposed by law, arguably reduces social wealth due to increased agency costs.

The debate continues to this day. Justice Bowen's line of reasoning was rejected decades later in the 1962 case *Parke v. Daily News Ltd* on the basis that enlightened industrial relations do not meet the standard of short-term profit calculation. This opinion accords with Berle's and Friedman's concerns that it is not practical or wise to deviate from strict fiduciary duty. The two U.K. decisions noted above simply place business strategy and company law in plain conflict. There may be no strong empirical evidence of any definite relationship among corporate social responsibility, stakeholder management, and profitability.

U.S. corporate governance law, enacted at the state rather than the federal level, is bifurcated. Some 29 states have adopted corporate constituency statutes that permit or require director attention to the interests of one or more stakeholders other than investors. Available evidence suggests that these statutes effectively do nothing to increase stakeholder influence or interests; rather, they simply increase managerial discretion at the expense of shareholder control for no tangible gain by other stakeholders. The evidence tends to support Berle's contention. It has been argued that managers can handle only one objective at a time, so that objectives must be ordered hierarchically—meaning wealth seeking primacy (within the law) and stakeholder considerations being secondary. A strategic view suggests, however, that managers would be well advised to practice enlightened stakeholder management: Since employee sentiments can affect employee morale and hence productivity, consideration must be given to those sentiments.

The general case for constituency or stakeholder attention rests on the experiences of European and Japanese industrial relations in contrast to the U.K.-U.S. legal doctrine. German industrial democracy, in effect since 1920, includes dual boards (a supervisory board including employee representatives appoints the management board) and works councils at establishments. Japanese business operated after World War II on the basis of management–labor cooperation. Both Germany and Japan, as examples of employee-oriented industrial relations (they may or may not be beneficial to consumers in the long run), reflect a scheme of industrial conflict management. It is difficult to see that these approaches are truly multiple-constituency models—everything depends on whether one believes that the approaches are in the long run in the public interest. European unemployment is structurally much higher than U.S. unemployment (reflecting more flexible labor markets and higher economic growth rates), and while Japanese unemployment is considerably lower, there is some evidence that it has risen and that lifetime employment practices are deteriorating. Evidence suggests that stakeholder management practices in Europe are measurably costly.

During the 1980s and 1990s, U.S. corporations—following the lead of General Electric (Jack Welch, CEO), for example—pioneered in shareholder value maximization (or wealth seeking) practices. The long success story (until tarnished by the dot.com bubble burst and recent corporate scandals) seemed to indict stakeholder or multiple-constituency theory. The Dey Report from Toronto in 1994, the Hampel Report from London in 1998, and the Peters Report from Amsterdam in 1997, issued by stock exchanges, all attempted to increase the weight of shareholder orientation without reducing the existing weight of stakeholder orientation.

Critics of stakeholder theory have returned to Berle as a touchstone—arguing why Dodd was wrong despite Berle's tentative concession. The general lines of argument run as follows: (1) investors have property rights that should not be reduced; (2) U.K.-U.S. corporate governance law should emphasize shareholder primacy; and (3) efficient, competitive markets generate social wealth without the need for governmental regulation or discretionary corporate social responsibility.

This reasoning tends to ignore the Berle and Means separation thesis. Principal-agency theory suggests imperfect control by investors and substantial discretion for managers. It is more likely that directors and executives emphasize corporate wealth, defined as corporate assets under discretionary managerial control rather than shareholder primacy. The latter remains a legal and economic ideal, if not a fiction, rather than the functioning reality.

Biographical Information on Berle and Dodd

Both Berle and Dodd were Harvard graduates, lawyers, and ultimately university professors. Dodd spent most of his career at Harvard, while Berle went into government service and returned to Columbia after World War II. Both Berle and Dodd practiced and taught in the field of corporation law.

Adolf Augustus Berle Jr. (1895–1971), born in Massachusetts, graduated from Harvard College and then Harvard Law School. His parents were active in the Social Gospel approach to progressive reform and politically connected. He first worked in the Boston law firm of liberal justice Louis D. Brandeis. Later, he provided legal services for the Henry Street Settlement House on Manhattan's Lower East Side. He formed his own law and Wall Street firms with specialization in corporation law. He commuted from New York to teach at the Harvard Business School. Resigning from the American delegation to the Paris Peace Conference in protest against the terms of the Versailles Treaty, Berle returned to practice law in New York City and, in 1927, began teaching "law of corporation finance" at Columbia, where he met Means. Berle became a member of Franklin D. Roosevelt's (FDR's) New Deal "brain trust" and an adviser to New York City Mayor Fiorella La Guardia. As assistant secretary of state for Latin American affairs (1938–1944), Berle was spokesman for FDR's Good Neighbor Policy. During World War II, he was the head of State Department intelligence activities.

After serving (1945–1946) as ambassador to Brazil, when the Vargas dictatorship was toppled, he resumed his professorship at Columbia and was a founder and chairman (1952–1955) of the Liberal party. In 1951, he became chairman of the board of trustees of the Twentieth Century Fund. During the Kennedy administration, Berle chaired a task force on Latin America that originated the Alliance for Progress.

Edwin Merrick Dodd Jr. (1888–1951), born in Rhode Island, also graduated from Harvard College and then Harvard Law School, several years ahead of Berle. He practiced law in Boston and then joined the Washington and Lee School of Law for 1 year, resigning to join the War Industries Board. After World War I, Dodd returned to legal practice in Boston and then in 1922, to teaching and scholarship on the law faculties successively of Nebraska, Chicago, and from 1928, Harvard. He died untimely in an automobile accident.

—Duane Windsor

See also Agency, Theory of; Business, Purpose of; Corporate Social Financial Performance; Corporate Social Responsibility (CSR) and Corporate Social Performance (CSP); Fiduciary Duty; Fiduciary Norm; Friedman, Milton; Stakeholder Theory

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Better Business Bureau (BBB)

The Better Business Bureau (BBB) is a network of private, nonprofit organizations concerned with fair business practices and consumer protection. The BBB has no policing powers, does not give legal advice or assist in breaking legal contracts, and does not make collections or give credit information. The BBB, under the leadership of the Council of Better Business Bureaus, collects and disseminates information about companies based on unanswered or unsettled complaints. In this endeavor, the BBB depends on the input and feedback from consumers. In addition, the BBB provides buyer-seller mediation and arbitration services and monitors advertising and selling practices.

Historical Background

Consumer activism is not a new phenomenon. Its roots can be traced back to early political economists such as John Stuart Mill and Adam Smith, who recognized that consumption was linked with politics and social organization. The modern consumer movement in the United States dates to the 1930s, to the period between the World Wars, when consumers lobbied for a more equitable tax system, price control, social security, and more stable labor-management systems. Writers such as Kathleen Donohue point to the establishment of the Consumers Advisory Board of the National Recovery Administration and the Office of the Consumers Counsel General within the Agricultural Adjustment Administration during the presidency of Franklin D. Roosevelt as a mobilization and institutionalization of a wave of citizen consumers. It is within this overall consumer context that the BBB is situated.

From the inception of the BBB, its major concern has been the issue of business ethics. One area of concern was that of advertising, which until 1880 was completely unrestrained. Some advertisers were making unbelievable claims, and the first acknowledgment of the overinflated claims made by advertisers first appeared in the *Farm Journal* in October 1880. The publishers of the *Farm Journal* declared that they would make every effort to ensure that advertisements that appeared in its pages were signed by trustworthy persons and went further by stating that they would make good on any losses suffered by a consumer as a result of a published advertisement. At the turn of the 20th century, the infant advertising industry established its own self-regulating organization known as "Vigilance Committees," which was devoted full-time to eliminating abuses and creating advertising codes and standards. Within a year, vigilance committees were established in Boston, Milwaukee, Atlanta, Des Moines, Seattle, and Denver. The Advertising Club Volunteers operated the vigilance committees, examining newspaper ads and contacting those suspected of making false claims and attempting by moral persuasion to appeal for voluntary ethical business practices. The publication of information called the attention of the public to those companies that were not willing to voluntarily reform their advertising. Within a few years, consumer complaints included demanding refunds and repairs or replacement of products or services. Eventually, the work expanded to consider the ethical issues involved in consumer complaints. If companies failed to resolve complaints, public reports were issued, resulting in an increased awareness among the public of the unethical activities of businesses. With the increased public awareness of the vigilance committees, it was inevitable that a consumer would inquire about the reliability of a company with whom the consumer was considering a business relationship. Thus the Reliability Reporting service of the BBB was initiated.

Better Business Bureau Structure

All BBBs provide a common set of core services and offer optional programs and services that reflect their local preferences, all provided for within the governance and structural makeup of the BBB system. BBBs share the same mission and values but are locally governed. Each BBB is an independent nonprofit corporation organized and governed by its business members. Members derive no financial benefit from the operation of the BBB but do have a vote (one per member) in the election of the board of directors and the officers of the corporation. Members are invited into the organization by membership representatives and are approved by the organization. Members pay annual dues, usually based on the size of the company. They may be removed from membership if they fail to abide by the BBB membership standards. The board of directors provides financial and policy oversight. The CEO, appointed by the board of directors, conducts business under procedures established under the bylaws of the corporation. BBB members provide the financial support that enables the BBB to offer services. The BBBs in the United States and Puerto Rico are organized into five regions. The BBBs in each region conduct an annual regional conference, organize other staff-training conferences, encourage effective communications within the region, and elect representatives to serve on the Council of Better Business Bureaus board and committees. The Council receives financial support from its member BBBs, from its national members, and from fees paid for national program services. The Council is organized as a nonprofit business membership organization that provides a national leadership voice for the BBB and protects the use of the registered Better Business Bureau name and its torch logo. It also provides services to BBBs ranging from consumer education materials and training to computer programming and support and membership marketing support.

Programs and Services

The BBB is concerned with ethical issues, a moral test that goes beyond the legal standard. Promotion of ethical advertising is a core service of the BBB. The BBB has developed an advertising code that establishes a set of guidelines that reflect the ethical advertising standards fostered by the BBB system. The BBB provides reliability reports that are designed to provide consumers with an informative, accurate, and unbiased summary of information documented in the BBB records. BBBs provide reliability reports but do not endorse or recommend any company, product, or service. The BBB provides dispute resolution services. Complaints are usually reported to the BBB in writing, many online. At the first level, the objective of the

BBB complaint process is to present the complaint to the business for a response and settlement of the issues. Most complaints are resolved at this level. If the complaint is not resolved, the BBB provides mediation services. Mediation involves helping the parties reach their own agreement to settle a dispute. The third level is arbitration, a process in which two parties allow a third party to make a legally binding decision to settle a dispute. The Better Business Bureau Auto Line is a very successful national dispute resolution program. Auto Line is a mediation and arbitration program designed to settle warranty disputes between auto manufacturers and customers. The BBB provides consumer education materials, information that helps identify quality features of products and services. BBBs provide information that helps businesses maintain ethical advertising and selling practices and effective customer relations. Most BBBs maintain some form of charity review program. The model program was developed by the Better Business Bureau Wise Giving Alliance, which operates as a service of the Council of Better Business Bureaus. Its objective is to establish wise giving guidelines and to gather information from national charities and present the information to potential donors in its Better Business Bureau Wise Giving Reports.

—Marilynn P. Fleckenstein

See also Accountability; Advertising, Subliminal; Business, Purpose of; Business Ethics; Charity, Duty of; Codes of Conduct, Ethical and Professional; Consumer Activism; Consumer Fraud; Consumerism; Consumer Product Safety Commission; Consumer Rights; Global Codes of Conduct; Marketing, Ethics of; Mill, John Stuart

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Bhopal

The Bhopal disaster—night of December 3, 1984—was the worst industrial disaster in the history of the world: the leakage of 40 tons of methyl isocianate (MIC) recorded at the plant that Union Carbide India, Limited (UCIL) had in Bhopal, the capital of Madhya Pradesh, one of the poorest and most overpopulated states in India. There were 6,903 dead, approximately 20,000 injured, and almost another 850,000 seriously affected in different ways.

Union Carbide Corporation occupied third place in the ranking of the chemical sector in the United States. It had assets of over $10,000 million and around 110,000 employees. Nevertheless, it underwent the worst financial situation in recent years: Net profits plummeted from $310 million in 1982 to $79 million in 1983.

Why did the disaster occur? The causes are related to diverse and complex factors. On the one hand, they were attributable to technical aspects and shortcomings detected in the safety mechanisms of the industrial plant, and the management was aware that it did not have adequate plans in place to resolve possible contingencies and accidents. On the other hand, they were related to the human factor: The morale of the workers was low, and it seems that there was not enough staff, technical training was rare, and the director did not have the required experience—excessive rotation of directors is apparent if we keep in mind that there were eight different general directors in 15 years. As regards the remaining reasons—and without wanting to annul the moral responsibility of the company for what happened—the insistence of the Indian authorities in keeping operative control of the subsidiary in the hands of nationals may have also contributed to the disaster by somehow removing the parent company from direct control of the plant.

The most noteworthy consequences of the disaster in Bhopal were the following: loss of human lives, illnesses, lack of confidence in the sector, more regulations, lawsuits, indemnities, loss of image, lack of worker motivation, and economic losses—in one week, the market value fell by almost $1,000 million. Months later, Union Carbide had to implement a restructuring plan: the closing of different plants and the dismissal of over 4,000 workers. It also had to defend itself against a hostile takeover attempt by GAF Corporation. Although the company managed to dodge problems successfully during this period, Union Carbide was no longer even a shadow of what it once had been. In the end, the company had to refocus its business and center it on the manufacturing of plastics and chemical products. It carried out a staff reduction program until only a little more than 12,000 employees remained, who were under pressure to declare that they were committed to the environment in the face of public opinion.

—José-Luis Fernández-Fernández

See also *Exxon Valdez*; Multinational Corporations (MNCs); Silkwood, Karen; Social Costs; Toxic Waste

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Bilderberg Group

A subject of much speculation, the Bilderberg Group is one of the more secret forums for high-level interaction by key business and political insiders from the principal nations of Europe and the United States. Formed in 1954 under the auspices of Prince Bernhard of the Netherlands, who hosted the first meeting at the Hôtel de Bilderberg near Arnhem, the group over time has served to promote collaboration between the European Union and the United States, including support for the North Atlantic Treaty alliance (NATO). Although claiming to have no formal charter, organization, or Web page, it has a chairman and a steering committee.

The Bilderberg conferences feature about 100 eminent financiers, corporate heads, government officials, media owners, intellectuals, and other political movers. The 4-day meetings are held once or twice a year, generally at out-of-the-way hotel and resort locations (always five-star) with strict security to keep away the uninvited. Camaraderie is created by all participants arriving without their spouses to live, talk, and dine together without being on the record. There is an unwritten rule that anyone attending a Bilderberg conference should be able to later, in a private capacity, contact other attendees, who over time form a virtual "who's who" of influence. Press coverage is discouraged, and participants are pledged not to repeat publicly what was said in the discussions. So despite the presence of many leading media figures over the years, very little is reported about these gatherings.

Ethical decision making and communication generally are enhanced by transparency and openness. So understandably, any largely autocratic and unaccountable means for those in the seat of power to meet clandestinely will give rise to concern. There are those who see the Bilderberg conferences as a type of secret society in which agreements are made to pull strings to clandestinely dictate government policies. In this respect, the Bildebergers are often grouped by conspiracy analysts with the Council on Foreign Relations, the Trilateral Commission, the United Nations Organization, the Vatican Bank, and other entities. The argument is that they are part of an overt/covert so-called shadow government having interlocking connections with major business interests, media, educational foundations, think tanks, and other powerful organizations.

Unless one is an insider, it is hard to evaluate these negative claims about such elite groups. There is no doubt about their influence, but many proponents argue that meetings such as the Bildeberg conferences help build personal contact, promote understanding, and serve the public good.

—Richard Alan Nelson

See also Council on Foreign Relations; Globalization; International Business Ethics; Trilateral Commission; United Nations; Vatican Bank

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Biocentrism

Biocentrism ("life centered") is an ethical perspective holding that all life deserves equal moral consideration or has equal moral standing. While elements of biocentrism can be found in several religious traditions, it was not until the late decades of the 20th century that philosophical ethics in the Western tradition addressed this topic in a systematic manner.

Much of the history of environmental ethics can be understood in terms of an expanding range of moral standing. Traditional Western ethics has always been anthropocentric, meaning that only presently living human beings deserve moral consideration. As environmental issues such as nuclear waste disposal, population growth, and resource depletion came to the fore, many ethicists argued that moral standing should be extended to include future generations of human beings. The animal welfare and animal rights movement argued for an extension of moral standing to, at least some, animals. Arguments followed to extend moral standing to plants and then to such ecological wholes as ecosystems, wilderness areas, species, and populations.

The philosophical challenge throughout this process was to articulate and defend a nonarbitrary criterion by which the question of moral standing could be decided. On what grounds do we decide that objects deserve to be considered in moral deliberation? Supporters of extending moral standing to future generations argued that temporal location, like geographical location, was an arbitrary ground for denying equal moral status to humans not yet living. Defenders of animal rights cited characteristics such as having interests, sentience, being conscious, and being the subject of a life as the most appropriate criteria for moral standing.

Biocentric ethics argues that the only nonarbitrary ground for assigning moral standing is life itself. Biocentric ethics extends the boundary of moral standing about as far as it can go. All living beings, simply by virtue of being alive, have moral standing and deserve moral consideration.

Roots of biocentric ethics can be found in a number of traditions and historical figures. The first of the five basic precepts of Buddhist ethics is to avoid killing or harming any living thing. The Christian saint Francis of Assisi preached to animals and proclaimed a biocentric theology that explicitly included animals and plants. Some Native American traditions also held that all living things are sacred. The romantic movement of the 18th and 19th centuries defended the intrinsic value of the natural world against the tendency of the technological age to treat all nature as having mere instrumental value.

In the 20th century, preservationists such as John Muir held that the intrinsic value of natural areas, and in particular of wilderness areas, created responsibilities on our part. Preservationists argued that the intrinsic value of nature imposes duties on us to respect and preserve natural objects.

But the preservationist ethic can go beyond biocentrism in that it is not life itself that always carries moral value. Wilderness areas and ecosystems, after all, are not alive. Similarly, Christopher Stone's famous argument that trees should have legal standing would not strictly be biocentric in that Stone also advocated standing for mountains and rivers. This observation suggests that biocentrism is essentially an individualistic ethic. Life would seem an attribute of individual living things. Many environmentalists argue that holistic entities such as ecosystems, wilderness areas, and species all deserve moral consideration. To the extent that such entities are not alive, strictly speaking, environmental holism differs from biocentrism.

Albert Schweitzer was another early-20th-century thinker who argued that it was life itself that was the decisive factor in determining moral value. Working in the most remote areas of Africa, Schweitzer experienced the diversity, complexity, and multiplicity of plant and animal life forms there, rarely seen within industrialized societies. Schweitzer used the phrase "reverence for life" to convey what he took to be the most appropriate attitude we ought to take toward all living beings. Life itself, in all its mystery and wonderment, commands our respect, reverence, and awe.

Only in the final decades of the 20th century did philosophers attempt to develop a more systematic and scholarly version of biocentric ethics. Paul Taylor's 1986 book, *Respect for Nature*, was perhaps the most comprehensive and philosophically sophisticated defense of biocentric ethics. Taylor provided a philosophical account for why life should be accepted as the criterion of moral standing, and he offered a reasoned and principled account of the practical implications of biocentrism.

Taylor claimed that the reason why life itself is a nonarbitrary criterion for moral standing is that all living things can be meaningfully said to have a good of their own. Living things have a good because they are "teleological centers of life." The Aristotelian notion of a *telos* calls attention to the fact that living things have characteristic activities that are goal directed. Living beings aim toward ends; they have directions, purposes, and goals. Pursuing these characteristic and natural goals—essentially what is the very activity that is life itself—constitutes the good for each living being.

As a normative theory, biocentrism has practical implications for our behavior. Taylor argued that the good of all living beings creates responsibilities on the part of human beings. Taylor defended four basic duties of biocentric ethics: nonmaleficence, noninterference, fidelity, and restitutive justice. The duty of nonmaleficence requires that we do no harm to living beings, although it does not commit us to the positive duties of preventing harm from happening or of aiding in attaining the good. The duty of noninterference requires that we not interfere with an organism's pursuit of its own goals. The duty of fidelity requires that we not manipulate, deceive, or otherwise use living beings as mere means to our own ends. The duty of restitutive justice requires that humans make restitution to living beings when they have been harmed by our activities.

While Taylor offers a careful explanation and defense of biocentric ethics, serious challenges remain both for his particular version and for biocentrism in general. Examining these challenges can provide a helpful overview of the present state of biocentric ethics.

Numerous practical challenges suggest that biocentrism is too demanding an ethics that requires too much of us. Taylor's alleged duties to do no harm to living beings and to refrain from interfering with the lives of other beings asks a great deal of humans. It is difficult to understand how any living being, and especially humans, could survive without doing harm to and interfering with other living beings. Not only would abstaining from eating meat seem to be required, but even vegetables would seem to be protected from harm and interference.

The more general point is that any biocentric ethics would seem to face a dilemma. On the one hand, the commitment to biocentric equality could be taken seriously, and every living being is understood to have equal moral standing. This option would appear to create a very demanding ethical world of constant moral tragedy. We have ethical duties not to harm beings with equal moral standing, yet we need to eat those beings to survive. On the other hand, we could acknowledge situations in which strict equality can be abandoned. As Taylor himself argues, we can make a distinction between basic and nonbasic interests to provide guidance in cases where the interest of living beings conflict. In such a case, one would conclude that basic interest should trump nonbasic interests. For example, the interest in remaining alive should override the interest in being entertained. Thus, it is unethical to hunt animals but ethically justified to kill an animal in self-defense. But this second alternative quickly threatens the consistency of biocentric equality.

Consider the interest in remaining alive that might be attributed to a bacterium, a mold, or an insect and compare that with any of a number of relatively trivial human interests and actions that would result in the deaths of countless bacteria, molds, or insects. Either the basic/nonbasic interest distinction is applied equally across species, or human interests are given priority. In the first case, biocentrism again seems to require a level of ethical care that is unreasonably demanding. In the second case, we would seem to abandon biocentric equality by granting human interests a privileged standing.

In response to such concerns, defenders of biocentric ethics often argue for a principle such as Taylor's restitutive justice. When inevitable harms do occur in the conflicts between living beings, a duty to make restitution for the harms is created. Thus, I can compensate for the harms I do in harvesting trees or crops by restoring the forest or planting more crops. But this response raises the second major challenge to biocentric ethics.

An important environmentalist perspective, identified as "ecocentrism" to distinguish it from biocentrism, holds that ecological collections such as ecosystems, habitat, species, and populations are the central objects for environmental concern. This more holistic approach typically concludes that preserving the integrity of ecosystems and the survival of species and populations is environmentally more crucial than protecting the lives of individual elements of an ecosystem or members of a species. In fact, ecocentric environmental ethics often would condone destroying the lives of individuals as a legitimate means of preserving the ecological whole. Thus, we can be justified in culling members of an overpopulated herd or killing an invasive nonnative plant or animal species.

Thus, a strictly biocentric ethics will conflict with a more ecologically influenced environmentalism. Protecting individual lives may actually harm rather than protect the integrity of ecosystems and species. It is, of course, always open for the biocentric approach to accept this conflict by simply denying the value of ecological wholes. Biocentric ethics would thus only incidentally have overlapping concerns with environmental ethics. But as Taylor's reliance on restitutive justice suggests, biocentric ethics may need the value of ecological wholes to solve its serious practical problems. The beneficiaries of biocentric restitution and compensation, after all, are the nonliving ecosystems and other species members that replace and compensate for the harmed individuals.

Finally, challenges remain to the fundamental claim that life itself is the nonarbitrary criterion of moral standing. The biocentric perspective relies on a problematic teleological hypothesis. Living beings are said to have an intrinsic moral value because each living being has a good of its own. They have this good in virtue of the fact that living things are goal-directed (teleological) beings. But this teleological assumption that being goal directed entails having a good may be unwarranted.

The biological sciences do commonly refer to an object's purpose, goals, or function, and in this sense, they seem to adopt a teleological framework. But the challenge is whether all goal-directed activity implies that the goal must be understood as a "good." Such an inference was made in the Aristotelian and natural law traditions, but it is not obviously valid.

Consider the clear example of a human action that aims for some goal. Why do we assume that a human goal is a good thing? The obvious explanation is that we assume that any intentional act by conscious agents is undertaken because that agent believes that the goal is, in some sense, good. By definition, a rational person wouldn't choose to do something unless he or she believed that it was a good thing to do. Aristotle himself argued that all acts aim for some good. But, if the subject is nonconscious and nonintentional, can we still conclude that its goal is a good?

In contrast, consider the following examples from biology: "The purpose of the kidney is to remove waste from the blood" and "The goal of brightly colored plumage on male birds is to attract females." Assuming that kidneys and bright plumage do not consciously and intentionally choose the goals they serve, it is not at all clear that attaining these goals does accomplish even a perceived good. Only if some other value component is elsewhere assumed (e.g., that blood free from waste is good for the body in which the blood circulates or that attracting female birds is good for the preservation of the species) can one conclude that attaining the goal is good. Ecocentric environmentalism might argue that life is goal directed, but like bright plumage, the good associated with this goal is the good of something other than the object itself—for example, the good of ecosystem integrity or of species survival.

The fundamental philosophical challenge to biocentric ethics thus involves two questions. Is the activity of living really goal directed in itself, even when nonintentional? Even if it is goal directed, why assume that a living thing serves its own good rather than, like kidneys and bright plumage, the good of something else?

Perhaps one way to revive biocentrism is to learn from elements of Aristotle's ethics other than his teleology. One might think of biocentric ethics as more congenial to a virtue-based ethics than to a rule- and principle-based ethics. Biocentric ethics will always face difficult challenges when it seeks to provide a decision-making rule or principle by which we can resolve conflict and make unequivocal decisions. But Aristotle warned against seeking more exactitude than a subject matter allows and rightfully reminded us that ethics is not mathematics.

Consider biocentrism not as a set of rules to follow but as an attitude or character trait with which to approach life. Aristotle would have called such an attitude a virtue, and this is more a description of an ethical person than it is an action-guiding rule. Interestingly, both Schweitzer and Taylor allude to similar ideas. Schweitzer characterized the reverence for life more as a profound feeling of awe that one develops in the face of the mystery of life. Reverence is a virtue. Taylor refers to a "biocentric outlook" as an ultimate moral attitude toward life.

In this way, biocentric ethics advises us to develop a set of habits and attitudes with which we interact with living beings. Approaching any and each living being with awe and with humility will help make our own human life more meaningful and significant. A sense of bereavement and loss in the face of death would be an equal part of biocentric ethics, even when we recognize that death is both inevitable and necessary.

—Joseph R. DesJardins

See also Animal Rights; Animal Rights Movement; Anthropocentrism; Deep Ecology; Environmental Ethics; Environmentalism; Environmental Protection Legislation and Regulation; Gaia Hypothesis; Green Values; Land Ethic; Wilderness

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BIODIVERSITY

Biodiversity is a term used to represent the total number of all life forms on our planet. This term includes all existent varieties of microbes, plants, animals, and fungi and all the genetic information they represent. Biodiversity entered into popular use with the publication of a volume edited by E. O. Wilson in 1988, titled *Biodiversity*, and is a contraction of the term *biological diversity*. While there is no comprehensive global database of all species, there are descriptions of between 1.4 million and 1.75 million documented species (depending on your source), with estimates of as few as 2 million to as many as 50 million more species yet to be identified and classified. While this disparity in estimates testifies to our limited understanding of the ultimate extent of biodiversity, it is even more surprising to note that some experts believe that as many as three species per hour are being lost largely due to human activity. Ecologists generally agree that species loss is happening at a historically unparalleled rate and could claim as many as one third of all organisms over the next 50 years. Given the estimates, it is possible that more species could be lost over the next century than are currently known and described. The awareness of our lack of deep knowledge of biodiversity raises many questions for humanity on both philosophical and practical levels.

Comprehension of biodiversity is critical to a proper understanding of the concept of sustainability (see entry) in the immediate and abstract sense. Biodiversity is an ecological demonstration of W. Ross Ashby's law of requisite variety, introduced in 1956, which states that the greater the variety possessed by a system the greater the number of disturbances that system can absorb without failure. Ashby observed that as variety is reduced below a requisite level, systems begin to fail. Because all life on the planet is part of the same biosphere, or interconnected ecological system or ecosystem, the variety of life-forms, or biodiversity, helps ensure the sustainability of all life on the planet by helping absorb the disturbances encountered within our ecological system. As has been observed and demonstrated, the existence of life helps create the conditions to support life, a notable example being the production of oxygen by trees and of carbon dioxide by animal respiration, each required to support life for the other.

As biodiversity decreases, the law of requisite variety predicts that the resilience of the ecosystem will also decrease until at some point the ecosystem will fail. In isolated regional ecosystems, such as island ecologies, this prediction has been demonstrated: As the biodiversity falls below the requisite variety, the ecosystem fails for life-forms related to that specific system, and especially harmed are those life-forms higher up on the food chain and therefore dependent on a greater number of other life-forms for their continued existence. Biodiversity has particular impact for human populations because our species is dependent on many other species of plants, animals, fungi, and microbes. At this point, scientists and ecologists have no clear idea of what number of other species constitutes the minimum *requisite variety* in terms of the global ecosystem's ability to provide ecological services to the global population of living creatures. The United Nations Environment Programme (UNEP) has estimated ecosystem services to be worth between $16 trillion and $54 trillion annually. What is clear is that the human population, and our ability to adapt to most biological niches, has made species survival for many other life-forms on this planet increasingly difficult. In the expert opinion of some scientists, our planet is experiencing the greatest rate of species extinction in 65 million years. By all indications, human activity is either directly or indirectly the cause of this massive reduction in biodiversity.

Humanity's collective need to maintain biodiversity presents some business organizations with contentious dilemmas. Organizations such as resource extraction industries that disturb or destroy habitat, such as mining, oil extraction, and logging to name a few, are often the focus of these dilemmas. The global population creates demand for power, lumber, and materials for goods, yet it also requires a planet with a sustainable ecosystem. It is well known that species diversity is most concentrated in areas such as rain forest and other undisturbed wilderness areas, and these are often the places where resource extraction companies find their raw materials. Regulations, both national and international, have provided one solution to this dilemma, but population pressure and a desire for continued and unimpeded economic growth continues to challenge the ecological necessity to keep some places wild. In some cases, even what some advocates represent as minimally invasive resource extraction technologies contribute to habitat fragmentation and species loss. Another example of human activity affecting biodiversity can be found in the fishing industry's management of common fishery resources (see the entry "Tragedy of the Commons") where once seemingly inexhaustible fisheries have been driven to collapse because of overfishing and habitat destruction. Examples of this exist in the Atlantic cod fishery, the Pacific and Atlantic salmon fishery, and the Chilean bass fishery in the south Pacific. Even fish farming has its dark side. Once thought to be the answer to world hunger, introduction of alien species into occupied habitat and disease caused by monoculture and reduced genetic diversity have created many unintended ecological problems, resulting in new threats to biodiversity. Finally, commercial farming or agribusiness in pursuing economies of scale through the use of monoculture farming and agricultural chemicals creates situations that deplete soil and reduce native plant stock variety, again having the unintended consequence of reduction in biodiversity.

Citizens, governments, and businesses must come to terms with the new realities that attend increased understanding of our planet and its limitations. Destruction through ignorance is tragic, but continued degradation of shared resources such as biodiversity becomes a societal and moral failure once the peril of such behavior is exposed. As more people understand, or in the worse case feel the effect of loss of biodiversity, business may find society less willing to allow free markets to function when self-regulation has the biosphere heading for a collapse due to loss of biodiversity (see entry on market failure).

Some positive steps have been taken. UNEP has been carefully monitoring global environmental health, while efforts are being made by some corporations to adopt more ecologically friendly practices. A number of management tools have been suggested for business organizations to help improve their environmental performance, including triple bottom line, balanced scorecard, *natural capital* (see entry), industrial ecology, the natural step, Zero Emissions Research Initiative, ecological footprint, and eco-effectiveness (cradle-to-cradle model). All these approaches represent an opportunity for management and governments to recognize that bottom line and the ecological baseline are not inextricably at odds.

By limiting our impact on the environment, including reducing our impact on habitat and pursuing sustainable management practices, society is making a statement about intergenerational justice and the intrinsic right of other species to share this impossibly rare inhabitable planet. Whether the arguments are based on enlightened self-interest, social justice, ecological theory, or systems theory, it is becoming abundantly clear that action must be taken to avert the dire consequences. Climate change and levels of ultraviolet radiation can have a devastating effect on species diversity. While action on global warming has been slow to muster, action on ozone depletion has been achieved, and the results have been dramatic. The damage to the ozone has begun to reverse. In the United States of America, the Endangered Species Act, for all of its detractors, has been a demonstration that concerted action can reverse the damage done through ignorance and greed. The experience gained from the Endangered Species Act has taught us that a species-by-species approach is inefficient and that global society must address habitat destruction and climate change. Yet this experience has also shown that progress can be made and that concerned and active citizens can make meaningful contributions to maintaining a balance between other species and human activity as part of a policy of sustainability.

The science of ecology informs us that maintaining biodiversity is not a luxury to achieve if possible or as budgets allow. It has provided us with evidence that biodiversity is the requisite variety needed to ensure the resiliency of our ecological system and ultimately secure the future of humanity.

—David H. Saiia

See also Agribusiness; Consumerism; Corporate Ecology; Deep Ecology; Environmentalism; Factory Farming; Market Failure; Natural Capital; Sustainability; Tragedy of the Commons

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Bioethics

Bioethics is the study of ethical issues in the practice of medicine and biomedical research. The field of bioethics has flourished for 30 years, and bioethicists have made significant progress on ethical issues in clinical medicine—that is, on "bedside" issues in the delivery of health care. More recently, significant attention has been paid to the just distribution of scarce health care resources. At the forefront of contemporary bioethics are issues tied specifically to for-profit health care such as the ethical development and marketing of pharmaceuticals.

The field of bioethics is one of the closest allied areas of research to business ethics. Bioethics and business ethicists deal with many similar issues, such as the appropriate use of ethical theory in dealing with practical ethical questions, obligations to conflicting stakeholders, and the scope and limits of professional codes of conduct. However, health care providers have generally welcomed the advances made by bioethicists regarding the ethical delivery of health care, and most hospitals now have an ethics committee, the task of which is to adjudicate difficult ethical issues that arise in the practice of medicine. In addition, ethical training is now routinely incorporated into medical school and nursing school curriculums. In contrast, businesspeople have not welcomed advances made by business ethicists in the same way, and business ethics education is not typically a required element of business school curriculums. Part of the explanation for this difference in attitudes lies in the fact that physicians and nurses regard themselves as having *ethical* duties to patients, whereas managers and directors typically regard themselves as having *fiduciary* duties to the owners of the business. It is also the case that in the United States, physicians and nurses have self-governing licensing boards that enforce ethical standards, whereas business managers and directors do not have equivalent layers of self-governance and ethics enforcement.

Clinical Biomedicine

One of the most important and influential ethical frameworks for examining problems in bioethics is known as principlism. Developed by Tom Beauchamp and James F. Childress, this approach derives principles from common morality and medical traditions. This approach to bioethics is not "top-down" in the sense of consistently applying principles derived from ethical theory to the practice of medicine. Rather, the approach grants that prima facie principles can and should be modified in light of a variety of sources of justification such as case judgments and rules of practice. The four principles identified by Beauchamp and Childress are (1) respect for the autonomous choices of individuals; (2) nonmaleficence, or do no harm; (3) beneficence, or the prevention of harm and the promotion of good; and (4) justice in the allocation of health care resources. Physicians and nurses who conduct their professional lives in a manner consistent with this approach, it is argued, do much of what is necessary for the ethical practice of medicine. Critics of principlism argue that this approach to bioethics fails to provide an adequate means for resolving cases in which principles come into conflict. They also argue that the "common morality" that principlism invokes is often inconsistent and as such cannot provide an adequate basis for an approach to bioethics.

In part due to the influence of Beauchamp and Childress but also because of the work of many other normative bioethicists and because of the transformation of medical training, concepts such as respect for autonomy, nonmaleficence, and beneficence have become commonplace among medical practitioners. The actual practice of medicine has been transformed from one dominated by the paternalistic judgment of physicians to one in which respect for patient autonomy is regarded as a core value. There is less agreement among bioethicists, practitioners, and U.S. policy makers regarding the just distribution of health care resources. This is the case despite the progress scholars such as Norman Daniels have made in articulating and defending a systematic account of just health care.

Profit-Driven Biomedicine

The 20th century saw major shifts in the provision of health care. These shifts include the transformation of the professional practice of medicine from a service orientation to a market orientation; the emergence of powerful pharmaceutical and health care corporations; and the development of new, innovative, and expensive biomedical technologies by for-profit enterprises. These changes have been accompanied by the emergence of a range of ethical issues that have not historically been discussed by bioethicists. One set of issues that is receiving increasing attention concerns the purposes and functions of HMOs, insurance companies, and physician practice groups, such as pricing, capitation, resource scarcity, and appropriate standards of care.

A second, more prominent range of ethical issues concerns the pharmaceutical industry. Critics of pharmaceutical companies such as Marcia Angell allege that direct-to-consumer marketing campaigns manipulate consumers into requesting unnecessary or inferior drugs from physicians; that pharmaceutical representatives provide incomplete and erroneous data regarding the efficacy of particular drugs to physicians; that pharmaceutical companies develop and aggressively market expensive "me too" drugs rather than developing truly innovative drugs; that most of these companies do little to provide the affordable, life-savings drugs most needed by people in the developing world; and that the companies are unjustly profitable. In reply, pharmaceutical companies and their representatives argue that they do not engage in marketing to consumers or to physicians but instead provide educational services, that all their drugs are intended to provide innovative benefits to consumers, that companies such as Merck have spent hundreds of millions of dollars to help eradicate diseases such as river blindness (onchocerciasis) and elephantiasis (lymphatic filariasis) in the developing world, and that they are for-profit enterprises with obligations to their owners to be profitable. In addition, they point out that their industry trade group, PhRMA, provides voluntary guidelines for ethical marketing and a range of other areas of concern.

In the 21st century, these issues concerning profit-driven medicine have begun to take a more prominent place in both bioethics and business ethics. However, since bioethicists normally focus on the obligations of individual clinicians on the one hand and the provision of health care by governments on the other, they are typically not in a position to address the obligations of for-profit enterprises. Similarly, business ethicists do not normally have expertise in biomedicine and so may not be well positioned to address the distinctive obligations of for-profit health care companies. It is likely that work at the intersections of these two fields of applied ethics will be collaborative and will be produced by senior scholars with broad professional experience. Normative ethical scholarship in this area has just begun and is likely to become much more sophisticated.

—Denis G. Arnold

See also Autonomy; Benevolence and Beneficence; Business Ethics and Health Care; Deontological Ethical Systems; Dignity; Justice, Distributive; Marketing, Ethics of; Medicaid; Medicare; Merck & Co., Inc.; Moral Reasoning

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Birth Control

Birth control remains a highly controversial topic throughout the world. Birth control is any method that prevents birth; as such, it includes not only contraceptives and contragestives but also abortion—both chemical and surgical—and sterilization. Contraceptives are birth control methods that prevent fertilization of an egg by a sperm (conception). Contragestives are methods that prevent the implantation of a fertilized egg (embryo) after conception. Abortion is the removal of an embryo or fetus from the uterus. Sterilization is a surgical procedure by which the male vas deferens or the female fallopian tubes are severed or removed. This entry will focus on the ethical dimensions of each type of birth control, as well as some of the issues that arise between birth control and business.

Different ethical dilemmas regarding birth control come to the forefront depending on when and where it is discussed and by whom. People of higher social class and/or from developed countries generally have more birth control options than those of lower social class or from developing countries. Birth control is also more of an issue for women since they can become pregnant. This difference is evident in the number of birth control options that involve female activity compared with those available for men.

Birth control generally is viewed in two ways: as population control and as a means to control when pregnancy occurs. Generally, the issues of birth control with regard to population control are discussed and regulated by government. For example, in China, women are forced to undergo surgical sterilization after giving birth due to the one-child policy the government has imposed in the hope of controlling the country's population growth. Governments may also adopt policies against birth control to ensure national survival. For example, abortion was banned in post–World War I France to encourage the birth of more French children.

The discussion on using birth control as a means to control when a woman will get pregnant occurs in many different venues. For example, the Roman Catholic Church is against most methods of birth control because it views controlling pregnancy as an attempt to thwart God's plan, thus attributing birth control to a lapse in Christian values. Viewing birth control as a means by which women can control when they will become pregnant has caused many feminist thinkers to support its use. Feminists believe that a woman should have the right to choose when she will become pregnant. The right to choose the timing and method of birth control can allow women more control over their life plan. Of course, a woman can be disempowered if the decision to use birth control is taken from her. To the extent that men exercise control over women's birth control choices, feminists see a pattern of patriarchal dominance.

There are many ways in which birth control issues affect businesses. These are some of the ethical questions companies may need to answer: Is it ethical to produce and sell birth control products? Is it ethical for some birth control methods to be easily available to minors or unmarried women? Is it ethical to provide birth control through health insurance paid for by the company? Is it ethical to cover some birth control options through company health insurance but not others? As will be discussed later, some businesses have been criticized by public activists for their answers to such questions.

Contraceptives

Female Contraceptives

"The pill" is the most widely used female birth control method. The ethical concerns regarding the use of oral contraceptives are their health risks and their potential to act as contragestives.

Barrier methods are another form of female contraceptive, but these methods are no longer popular due to the advent of oral contraceptives. Barrier methods include diaphragms, sponges, cervical caps, and female condoms. While these methods do not introduce hormones into the body, and therefore do not carry the same risks as oral contraceptives, there are other potential risks associated with their use: they are difficult to use properly, there is the risk of developing a potentially fatal toxic shock syndrome, and most do not protect against sexually transmitted diseases (STDs). The continued emphasis on oral contraceptives over safer barrier methods that protect against STDs, such as the female condom, exposes women to health risks from introducing hormones into the body and from STDs and HIV/AIDS.

Other female contraceptives introduce hormones into the body through a vaginal ring, dermal patch, injection, or subdermal implant. Each has similar potential health risks as oral contraceptives since hormones are used. Each also has different degrees of risk based on the method of delivery. Injected hormones cannot be reversed quickly, thereby decreasing a woman's choice to restore her fertility. In contrast, implants, pills, and the patch can be removed from the body, thereby restoring fertility relatively quickly. Injectable contraceptives also have a great potential for abuse. A woman can be injected without her consent or knowledge, as has happened in refugee camps and psychiatric hospitals.

Male Contraceptives

Currently, there are only two methods of male contraception that have a high rate of success: condoms and sterilization. Sterilization is a radical contraceptive choice. Some would argue that it is not used to prevent pregnancy but rather reflects the desire to never have children. The male condom has the added benefit of helping prevent transmission of STDs, including HIV/AIDS. There is great potential for the advent of a male form of oral contraceptive within the next 5 years. Strides toward developing a reversible, nonbarrier male contraceptive have been made recently, and research shows that men are receptive to the idea of an oral contraceptive. Oral contraceptives for men would most likely interfere with the maturation of the sperm.

Contragestives

Contragestive or interceptive methods of birth control intervene after fertilization by causing the destruction of the embryo. Contragestives can affect the embryo either before implantation or after, but the user of a contragestive cannot determine when the embryo is destroyed. Contragestives include intrauterine devices (IUDs), emergency "morning after pill" contraceptives such as Plan B and Mifepristone (also known as RU-486), and menstrual extraction. Contragestives bring up many of the same ethical issues as abortion because they can be viewed as abortifacients, depending on one's definition of abortion and when personhood begins.

Abortion

While there is little evidence that people view or use abortion as a form of birth control, technically it is one. Abortion ends a pregnancy, thus controlling when a woman gives birth. Elective, surgical abortion brings up a multitude of ethical problems. While the debate about abortion is too complex to fully discuss in this entry, here are a few of the issues. When does human life begin? When does personhood begin, and what are the rights of a fetus? Does the extent of these rights increase as the fetus approaches viability inside or outside the mother's womb? What are the morally acceptable reasons for deciding to have an abortion? When and how should abortion be made available? Who can decide whether or not to have an abortion? Should the fetus's right to life take precedence over the mother's right to privacy? Should the mother's right to privacy include her autonomous control over decisions that affect her own body? Should the health of the mother be considered in evaluating an abortion option? Should abortion be made available to all women, since all women are morally equal? What constitutes a good parent? Governments, religious groups, and other organizations around the world have taken a stance regarding abortion. These positions have polarized many people.

Sterilization

Sterilization is currently a surgical procedure that involves the cutting, sealing, tying, or removal of the male vas deferens and the female fallopian tubes. Abuses of surgical sterilization abound. Such abuses have in common the assumption that sterilization is justified by the needs of society. Eugenic sterilizations have been imposed all over the world on persons considered undesirable due to their race, ethnicity, sexual orientation, nationality, and mental or physical condition. In the past, U.S. courts have imposed sterilization on an unknown number of men sentenced for fathering children that they do not support or for being convicted as sexual predators. Women in China and India are often encouraged or required by the government to have the procedure after giving birth to their first child. "Fetal protection" policies have also forced sterilization on women so that they can get certain jobs that could be dangerous to an unborn fetus. These policies will be discussed further in the next section of this entry.

Birth Control and Business

There are many ways in which issues of birth control and business intersect. Below are brief synopses of four cases where business operations and birth control issues have conflicted.

The Dalkon Shield

The Dalkon Shield is a form of IUD that was introduced in the United States with a high level of serious side effects, including uterine infection and death. When the Dalkon Shield was taken off the market in 1975, 14 deaths and 223 spontaneous abortions had been related to its use. The company that made the Dalkon Shield, A. H. Robins, then sold large quantities of the product to the U.S. Agency for International Development's Office of Population. The Dalkon Shield was distributed to women around the world despite the known health risks. It is unknown how many women were given this product or how many deaths it caused, but in 1985 A. H. Robins declared bankruptcy due to numerous lawsuits.

"Fetal Protection" and Johnson Controls

"Fetal protection" policies have forced sterilization on women so that they can get certain jobs that could pose mutagenic risks to an unborn fetus. These jobs generally have higher pay than others in the same industry and expose the worker to toxins. In 1991, the U.S. Supreme Court ruled that Johnson Controls' fetal protection policies were a form of sexual discrimination. While this ruling can be viewed as a victory for women's rights, the language of the decision causes a mother who exposes her fetus to toxins in the workplace to be criminally liable for any harm to the fetus.

Plan B and Wal-Mart

In March 2006, Wal-Mart reversed its stand on Plan B, deciding to stock the product. Wal-Mart had refused to carry the product, citing not ethical reasons but rather low demand for the product. Women in Illinois and Massachusetts sued the company, claiming that Wal-Mart outlets were the only pharmaceutical option available in some communities. Plaintiffs claimed that as a part of the national health care system, Wal-Mart pharmacies should carry Plan B. After losing both suits, Wal-Mart changed its policy and began stocking Plan B. Wal-Mart continues to have a "conscientious objection" policy allowing employees to refuse to distribute items they find ethically objectionable; however, the employee must direct the customer to another employee or store that will service the request.

Insurance Coverage of Contraceptives

In recent years, most insurance companies and employers have decided to cover oral contraceptives, largely due to intense lobbying by female employees and women's groups. This coverage excludes women who cannot take the pill due to health issues or who prefer another method of contraception. Recent innovations offer women alternatives that have fewer side effects and are easier to use (the patch, vaginal rings, etc.). The newer methods, however, tend to be far more expensive for insurance companies that have negotiated discount rates for birth control pills with the many manufacturers vying for their business. For example, the cost of the patch to insurance companies can be 10 times the cost of the pill, because the patch is made by one company. Insurance companies and employers argue that because these alternatives are less popular, limiting access is a way to reduce health care costs without affecting many people. It is probable that costs will decrease and insurance policies will cover these methods as they become more popular and/or are produced by multiple companies. For now, this issue is unresolved.

—*Amy Parziale*

See also AIDS, Social and Ethical Implications for Business; Autonomy; Benefits, Employee; Bioethics; Business Ethics and Health Care; Coercion; Dalkon Shield; Employment Discrimination; Feminist Ethics; Feminist

Theory; Gender Inequality and Discrimination; Health Insurance Portability and Accountability Act; Human Rights; Patients' Bill of Rights; Population Growth; Women in the Workplace; Women's Movement; Work and Family

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Black Market

The black market refers to any economic activity that is illegal, unrecorded, unreported, or in violation of the law. Other terms used to describe this illegal activity include *underground*, *shadow*, *subterranean*, *informal*, *parallel*, or *irregular economy*. Another related term is the *gray market*, but this describes goods that are sold and not manufactured under patent, trademark, copyright, or exclusive distribution laws. The term *black market* derives its name from economic activities conducted in the dark or shadow, since it is hidden from the law.

Black markets exist so that individuals may evade taxes or restrictive government controls, sell illegal goods or services, or obtain goods through unsanctioned channels. Examples of black market activities include trading stolen goods such as illegal drugs, offering illegal services such as prostitution, paying someone cash who will not pay taxes, manufacturing a banned substance such as anabolic steroids, or bartering goods or services to circumvent being taxed for them. Bartering occurs when you exchange goods or services without entering into any monetary transactions. For example, instead of paying a dentist for the cleaning of your teeth, you would change the oil in the dentist's automobile. Without monetary exchange, such transactions cannot be tracked for tax purposes.

Economic Implications

There are several economic factors that may prompt the emergence of a black market economy, including an increase in taxes, high unemployment, illegal immigration, lack of strong unions, or a government embargo. An embargo is imposed when a country outlaws sale of a product within its national borders, such as the U.S. embargo of Cuban cigars. The black market can affect the economy in a variety of ways. First, if a product or income is untaxed, the brunt of the taxes will fall on those who legally report their transactions. Second, the cost of the goods offered on the black market is usually higher since the demand is high or the supply may be scarce. For example, the price for banned substances is substantially higher for goods such as fireworks, which may not be legally sold in several U.S. states. The same is true for exotic animals, which may only be purchased by professionals in limited venues, such as zoos. However, the prices may be lower if they have circumvented normal, more costly channels. If stolen goods are offered for sale on the black market, then law-abiding business owners lose out to the dishonest ones. Third, black market transactions affect the measurement of economic growth. Estimates of the extent of black market economic activity range from 9% of the gross domestic product (GDP) in the United States to 76% in Nigeria. GDP refers to the total market value of the final goods and services sold within a given country in 1 year.

One method to estimate the extent of the black market is to compare the amount of personal income declared on tax returns with the amount of money that is actually spent. Two other methods include measuring the changes in currency supply and gauging the velocity of money (how many times money circulates in a given period).

History

The origins of the black market economy extend back to the first time governments intervened in the commercial transactions of commodities. However, the black marketing of slavery in the United States began sometime after January 1, 1808, after importing slaves was officially outlawed. This practice continued until the end of the Civil War in 1865, which was the same year in which the Thirteenth Amendment to the Constitution abolished slavery in the United States. Alcohol products were black market goods illegally sold in the United States during the 1920–1933 prohibition era. During World War II, when the U.S. government imposed rationing or price controls on meat, sugar, automobile parts, penicillin, and gasoline, a black market emerged. After the Cold War, the United States and the Soviet Union dismantled 40,000 nuclear warheads. Fears have been expressed that at least some of these nuclear materials may have been offered on the black market for weapons of war and terrorism.

Illegal immigration also has been connected to black market activity. In 2006, as many as 12 million illegal immigrants, according to some experts, may now reside in the United States. Since black market employment goes unreported, this can cost the U.S. government over $30 billion in uncollected income taxes. In addition, these immigrants are underpaid, lack any medical benefits, and often work in unsafe or unhealthy conditions. Such black market activity creates a higher unemployment rate for those who might otherwise have been employed and paid legal minimum wages. Unethical subcontractors gain a competitive advantage if they can pay below minimum wages.

Ethical and Practical Concerns

Although economic activities conducted in the black market are illegal, a 2003 survey by the Internal Revenue Service reveals that 17% of respondents believe that cheating on taxes is acceptable. However, many individuals will not purchase commodities from the black market because they believe it is unethical, because they prefer purchasing from the legal suppliers given that there could be a problem honoring the warranty, or because they could face a punishment or a fine.

There are some possible approaches to discouraging a black market economy in the United States, but these raise other practical or ethical concerns. Illegal products could be legalized, but this would make banned substances such as cocaine or heroin readily available. Increasing Customs Service enforcement of restrictions on importation of banned substances could be another solution. Another possibility is President George W. Bush's proposed 2006 "guest worker program," which requires illegal immigrant workers to register for a temporary work visa and then return to their home country within 6 years of this registration. Many Republicans oppose this proposal, believing that the government is too lax and that this proposal would encourage even more illegal immigrants to enter the United States. Consequently, black market activities appear to be extremely pervasive and cannot be easily obliterated from the economy.

—Martin J. Lecker

See also Barter; Economic Growth; Gross Domestic Product (GDP); Immigration Policy; Tax Ethics; Underground Economy; Unemployment

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Blue Sky Laws

Blue sky laws are state laws regulating securities. They gained their unusual name from concerns that fraudulent securities offerings were so brazen and commonplace that issuers would sell building lots in the blue sky. In general, these laws predate the Securities Act of 1933 and the Securities Exchange Act of 1934 and were not preempted by those federal acts. In the 20-year period between 1911 and 1931, 47 of the existing 48 states adopted such laws.

Blue sky laws typically require the registration of any securities sold in the state, regulate broker-dealer and investment advisers, impose liability for false and misleading information relating to securities, and establish administrative agencies to enforce the laws. The registration requirements often include a "merit review" that gives the administrative agency the power to prohibit the sale of securities that it considers not to be "fair" or "equitable." This is in contrast to the federal securities law approach that relies on the market to determine a fair price after ensuring full disclosure of relevant information. It should also be noted that blue sky laws do not regulate interstate trading of securities.

Although the majority of states have adopted the Uniform Securities Act (USA), these states have made variations to the USA, which creates significant differences from state to state. In addition, judicial interpretations of the USA can also vary significantly from state to state. Thus, actions that may be considered fraudulent under the USA in one state may not be fraudulent under the USA in a different state.

In an attempt to achieve greater uniformity between the states and thus reduce the burden on issuers and broker-dealers, Congress passed the National Securities Markets Improvement Act (NSMIA) of 1996. The NSMIA classifies certain securities as "covered securities," which are exempt from state registration or merit review requirements. The covered securities include securities listed on a national stock exchange, mutual funds, and other offerings. Certain types of intrastate and small-scale securities offerings continue to be regulated by the states.

In addition, Congress passed the Securities Litigation Uniform Standards Act (SLUSA) of 1998 to place limits on state court jurisdiction over securities fraud lawsuits. Under the act, federal courts have exclusive jurisdiction over class actions alleging fraud. This subjects the plaintiffs to the reforms of the Private Securities Litigation Reform Act of 1995, which has significantly more difficult procedural hurdles than typical blue sky laws. It is unclear, however, to what extent the SLUSA requires nonfraud class action claims, such as a breach of a fiduciary duty claims, to be heard only in federal courts.

The SLUSA does not prohibit state and local governments (and their pension funds) from bringing securities fraud claims. The importance of this exception became clear in 2002, when the New York attorney general used the state's blue sky law (known as the Martin Act) to reach a settlement with Merrill Lynch that required Merrill Lynch to make significant changes to its operating and disclosure practices. This settlement became a leading example of regulation by prosecution. Subsequently, other states have amended their blue sky laws to increase their attorney general's prosecutorial powers, and Congress has considered new legislation in an ongoing attempt to find the appropriate balance between federal and state powers in securities regulation.

—David Hess

See also Fiduciary Duty; Finance, Ethics of; Scandals, Corporate; Securities and Exchange Commission (SEC)

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Bluffing and Deception in Negotiations

Deception can be defined as intentionally causing someone to have false beliefs. Bluffing in negotiations involves attempting to deceive others about one's intentions or negotiating position. In the United States, it is common, often a matter of course, for people to misstate their intentions during business negotiations. For example, suppose that Bob is selling a house and tells a prospective buyer that $350,000 is absolutely the lowest price that he will accept, when he knows that he would be willing to accept as little as $320,000 for the house (in this case, $320,000 is his "reservation price"). Such statements are lies according to standard dictionary definitions of lying—they are intentional false statements intended to deceive others. (See Carson, 1993, for an alternative definition of lying, according to which it is not so clear that such statements are lies.)

In a business negotiation, there is typically a range of possible agreements, any one of which each party would be willing to accept rather than reach no agreement at all. For instance, Bob might be willing to sell his house for as little as $320,000. His range of acceptable agreements extends upward without limit—he would be willing to accept any price at or above $320,000 rather than fail to make the sale. Suppose that a prospective buyer is willing to spend as much as $335,000 for the house. (He or she prefers to buy the house for $335,000 rather than not buy it at all.) The buyer's range of acceptable agreements extends downward without limit—he or she would be willing to purchase the house for any price at or below $335,000. In this case, the two reservation prices overlap, and an agreement is possible. No agreement is possible in a negotiation unless there exists a "bargaining range"—that is, unless the buyer's reservation price is greater than or equal to the seller's reservation price.

If there exists a bargaining range between the positions of negotiators, then the actual outcome depends on the negotiations. Consider again our example of the negotiation over the sale of the house. Whether the house sells for $320,000, $335,000, or somewhere between $320,000 and $335,000, or whether it sells at all will be determined by the negotiations. In this case, it would be very advantageous for either party to know the other person's reservation price and disadvantageous for either party to reveal his or her reservation price to the other. It can sometimes be to one's advantage to mislead others about one's own reservation price. In the present case, it would be to the seller's advantage to cause the buyer to believe that $335,000 is the lowest price that the seller will accept.

Attempting to mislead the other person about one's reservation price can backfire and prevent a negotiation from reaching an agreement that both parties would have preferred to no agreement at all. For example, suppose that the seller tells the buyer that he or she won't accept anything less than $375,000 for the house. If the buyer believes the seller (or believes that the seller's statement is close to the truth), the buyer will break off the negotiations, since, by hypothesis, the buyer is not willing to pay more than $335,000 for the house. Since negotiators typically don't know the other party's reservation price, it is risky for them to engage in such deception.

It is possible to bargain aggressively and engage in the give and take of negotiations without making any false claims about one's reservation price. One can withhold information about one's reservation price and engage in the process of making offers and counteroffers without making any false claims about one's reservation price and, thus, without doing anything that might constitute lying or deception.

Is It Morally Permissible to Misstate One's Negotiating Position?

Clearly, it is permissible for a person to protect his or her interests by withholding information about the reservation price. One is not obligated to reveal this information to others or answer questions that ask one to reveal it. No one who writes on the topic claims otherwise. The literature on deception and bluffing in negotiations focuses on the question of whether it is permissible for one to attempt to gain an advantage in a negotiation by making deliberate false statements about one's reservation price.

A Defense of Bluffing

Carr argues that misstating one's reservation price is morally permissible. Business, he argues, is a game like poker—a game in which special norms apply. The moral norms appropriate to the game of business or the game of poker are different from those appropriate to ordinary contexts. Carr claims that bluffing (misstating one's reservation price) is morally permissible because it is legal and a common practice that is regarded as permissible by conventional morality. Carr's argument presupposes the following principle: Any practice engaged in by businesspeople in a given society is morally permissible provided that it is consistent with both the society's conventional ethical principles governing the practice and the laws of that society. This principle is most implausible. Conventional morality and the law are not infallible moral guidelines. In the past, many immoral practices, most notably slavery, were condoned by the conventional morality and legal codes of many societies.

There is a second, more plausible, argument that *may be* implicit in Carr. This argument can be stated as follows: People who play poker know that the rules of the game permit deception. Thus, they consent to being deceived when they play poker. If they object to being deceived, then they shouldn't play poker. Similarly, people who negotiate consent to have others attempt to deceive them by means of false statements; therefore, it is morally permissible for negotiators to attempt to deceive others by means of false statements. Often, consent makes it morally right for people to do things to others that would otherwise be wrong for them to do—for example, enter their house, drive their car, operate on their knee, or caress their body. However, this argument fails for several reasons. First the (conventional) rules for negotiations are not as clear and widely known as the rules for poker; it is not clear what, if anything, one knows to expect when entering into a negotiation with a stranger. Second, negotiations are not purely optional in the way that playing poker is. Those who refuse to negotiate economic transactions pay a high cost. A person who wants to purchase a home or car has very limited options if he or she refuses to negotiate with others (or refuses to negotiate with those who engage in deception).

No one else who writes on this topic gives the same blanket endorsement of deception in negotiations. Recent literature on this topic focuses on cases in which one has reason to suspect that the other party is attempting to deceive one about his or her reservation price.

Two More Qualified Defenses of Bluffing

Dees and Cramton argue that the law and conventional business practice make a sharp distinction between deception about one's reservation price and deception about other matters. For example, in a personal injury lawsuit, statements about the amount of money one is willing to accept are expected to be deceptive, and the law permits this; however, statements about the extent of physical injuries suffered are not expected to be deceptive and are not permitted by law. Typically, negotiators have no grounds to trust the other party's claims about his or her reservation price. Negotiators often risk suffering significant disadvantages by refraining from making false claims about their reservation price. In such cases, Dees and Cramton contend, negotiators have little moral obligation to refrain from lying/deception about their reservation price. However, they claim that it is wrong for negotiators to engage in lying or deception about other matters.

Like Dees and Cramton, Strudler makes a sharp distinction between deception about one's reservation price and deception about other matters. He argues that given the uncertainty and lack of trust endemic to negotiations, lying and deception about one's reservation price can be useful devices to signal one's intentions and reach mutually beneficial agreements. Given their usefulness in serving this function and given the general understanding that such statements are not to be trusted, such lying and deception usually do not cause other people significant harm. Thus, according to Strudler, there is no moral presumption against such lying and deception, and those who engage in this sort of lying and deception shouldn't feel moral regret or embarrassment.

The View That Bluffing Can Be Justified (Only) on Grounds of "Self-Defense"

Carson argues that it is usually permissible to misstate one's reservation price when one has good reason to think that one's negotiating partner is doing the same, and it is usually impermissible to misstate one's reservation price if one does not have good reason to think that the other party is misstating his or her price. He contends that there is a moral presumption against attempting to deceive others about one's reservation price (whether or not it counts as lying). However, when others attempt to deceive us and thereby gain an advantage over us, we are often justified in deceiving them in "self-defense." Similarly, it is at first view very wrong to use violence or deadly force against another person, but when doing so is necessary to protect ourselves from the violence or deadly force of others, then it is morally permissible. Carson defends what he calls a generalized principle of self-defense. Roughly, this principle says that even if a certain action is ordinarily morally wrong, it can be morally justified if it is necessary to defend oneself against others who are doing or trying to do the same action to oneself. (Alternatively, and a bit more precisely, the ordinary moral presumption against doing a certain harmful act to someone else does not hold if doing that action to another person is necessary to prevent that person from harming one by doing the same action.) Carson claims that rational people can follow this principle and maintains the view that people can defend themselves and refuse to be prey for others.

According to Carson, misstating one's reservation price is permissible in cases in which one has reason to think that others are doing the same and thereby gaining an advantage over one. He also holds that there is a strong presumption for thinking that this is wrong otherwise. Dees and Cramton hold a somewhat more permissive view. They don't require that one have positive reason to think that the other party is misleading one and thereby harming one. They think that misstating (or lying about) one's reservation price is justified provided that one lacks a positive reason to trust the other party and there is a *risk* that deception by the other party will significantly disadvantage one.

Dees and Cramton, Strudler, and Carson all think it is wrong to deceive others about other matters in negotiations. Among other things, they claim that it would be wrong to deceive someone about the properties of a house whose price is being negotiated and wrong to deceive someone about the extent of injuries suffered in negotiations over damages for a personal injury.

—Thomas L. Carson

See also Consent; Deceptive Advertising; Deceptive Practices; Ethics of Persuasion; Honesty; Integrity; Reciprocity; Trust; Truth Telling

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Boesky, Ivan (1937–)

Ivan Frederick Boesky, born on March 6, 1937, in Detroit, Michigan, is most well known for his involvement in a Wall Street insider trading scandal in the mid-1980s. The son of a Russian immigrant who became a top Detroit restaurateur and graduate of the Detroit School of Law, Boesky landed on Wall Street in 1966 as a stock analyst. With the assistance of his father-in-law, the real estate magnate Ben Silberstein, Boesky started his own arbitrage firm in 1975.

Throughout the early 1980s, Boesky, working as an arbitrage specialist and known affectionately as "Ivan the Terrible," amassed a fortune estimated at approximately $200 million by betting on corporate takeovers and mergers. Boesky, along with other corporate financiers such as T. Boone Pickens and Sir James Goldsmith, took advantage of the gap between public and private market values to raid corporate targets, a legal enterprise as long as the trading in the targets securities was based on public knowledge of the imminent acquisitions. During this time, the U.S. Securities and Exchange Commission (SEC) investigated Boesky for engaging in certain investments based on tips received from corporate insiders regarding potential takeover targets. Boesky acquired securities in various companies based on insider tips, often with significant purchases made only days before a corporation publicly announced a takeover, resulting in substantial returns for Boesky when the news of the pending takeover was released.

While use of such insider information to trade in public securities was illegal, the SEC until this point had rarely engaged in enforcement proceedings for insider trading. In November 1986, Boesky, as a result of an SEC investigation into illegal insider trading on Wall Street, pled guilty to one felony count of manipulating securities and agreed to cooperate with the SEC in its ongoing investigation. Boesky, in return for leniency, allowed the SEC to secretly tape his conversations with various corporate insiders and takeover specialists, including junk bond trader Michael Milken. Boesky's cooperation led to an insider trading probe of Milken and his firm Drexel Burnham Lambert, resulting in both Drexel and Milken later entering guilty pleas to securities law violations.

As a result of his plea agreement and cooperation with the SEC, Boesky received a sentence of 3½ years in prison, a $100 million fine, and a permanent ban from working in the securities industry for the remainder of his life. Boesky, who served his time at the Lompoc Federal Prison Camp in California, was released from prison after serving 2 years.

The actions by Boesky and others (including Milken) are viewed as emblematic of the greed and excesses critics argue marked the 1980s on Wall Street. Prior to his guilty plea, Boesky gave an infamous speech at the University of California in 1986 extolling the positive aspects of greed, stating that he thought greed was healthy. Boesky's statements inspired the key speech by the fictional character Gordon Gekko (played by Michael Douglas) in the 1987 movie *Wall Street* claiming that greed was good.

—Stephen R. Martin II

See also Arbitrage; Insider Trading; Manipulation, Financial; Milken, Michael Robert; Securities and Exchange Commission (SEC)

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Bottom of the Pyramid

The term *bottom of the pyramid* (BoP) refers to the lower two thirds of the economic human pyramid, those 4 billion people living in abject poverty. More broadly, it refers to a market-based model of economic development that promises to simultaneously alleviate widespread poverty while providing growth and profits for multinational corporations (MNCs). The approach is also known as base of the pyramid (avoiding the negative connotations of the earlier term) and as sustainable livelihood business. It is increasingly adopted by firms in different industries (e.g., household goods, energy).

Alleviating global poverty was identified as a top priority in the United Nations Millennium Goals. Unlike traditional aid-based models of economic development, BoP approaches recast poverty as an economic opportunity for MNCs. The basic argument has three premises: (1) the world's poor constitute massive growth opportunities and profit potential for multinational enterprises, (2) such companies are uniquely qualified to unlock the economic potential of these difficult to access markets, and (3) bringing the poor into the global economy will simultaneously generate fortunes for firms while solving the problem of global poverty.

Critics of BoP approaches note two crucial challenges, governance and sustainability; neither challenge is currently well addressed. Effective governance mechanisms and bodies are needed to regulate, monitor, and oversee the development of markets and effective competition, and like MNCs, they must transcend national sovereignties. Raising the consumption levels of the world's 4 billion poor dramatically requires radically new business models and technologies to avoid disastrous impacts on the earth's ecosystems; governance mechanisms are needed to enforce the adoption of radical resource efficiency measures and clean technologies across a multinational playing field.

Four billion poor people constitute a staggering market opportunity, but without buying power (income) and transaction capacity (credit, infrastructure, distribution systems, and other institutional frameworks), the poor are locked into poverty. BoP approaches contend that MNCs in particular have the incentive (growth opportunities), the financial resources, and the capabilities (low-cost mass production, marketing expertise, international experience) to produce and distribute appropriate, affordable products at high volumes and razor-thin profit margins. Working with political actors, small businesses and entrepreneurs, and aid organizations to overcome self-reinforcing poverty traps, MNCs supply goods and services, provide credit and social engineering, help reduce corruption, and facilitate growing empowerment. Engaging in BoP demands significant innovation, new business models, and organizational learning and offers opportunities for sustainable entrepreneurship. Once initiated, economic activity becomes the engine for continuing wealth generation and growth.

Bringing the poor into a global economy as active participants in consumption and production has significant implications for the notion of sustainable development, which depends equally on healthy social, ecological, and economic systems. To the degree that BoP approaches can empower the poor and alleviate poverty, they strengthen economic and social systems. Raising consumption levels of 4 billion people currently living at or below subsistence levels, however, massively increases the demand for energy and resources while producing pollution and waste. The strain on the natural environment will be devastating unless increases in consumption are achieved through radical improvements in resource-efficient, clean technologies, as well as effective regulatory schemes.

—Monika I. Winn and Manfred Kirchgeorg

See also Accountability; Corporate Governance; Empowerment; Sustainability; Transparency

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Bounded Rationality

Bounded rationality argues that a decision agent is as rational as its limited resources and other conditions will permit. This theory recognizes that, contrary to neoclassical decision theory, decision makers are not purely rational, optimizing individualistic outcomes. Rather, bounded rationality suggests inherent limits on rational thought and decision making.

Neoclassical economic theory unrealistically suggests how rational consumers *should* behave. However, bounded rationality describes what imperfect human beings *actually* do, allowing better explanation or prediction of their decisions.

Bounded rationality is a central theme in *behavioral economics*, which studies how the imperfections of actual decision making influence those decisions. Thus, behavioral economics departs from one or more neoclassical assumptions regarding rational behavior. By considering nonmonetary costs, the limitations of human perception, and altruistic motivations, bounded rationality theory demonstrates that seemingly irrational behavior often can be fully justified. Nonetheless, the fact that buyers are less than perfectly sovereign raises controversial social and ethical issues for marketers.

Rational Decision Making and Economic Rationality

Many social sciences behavioral models assume human "rationality." Rational deliberations are described by *rational choice theory,* used by practitioners in economics, management, philosophy, psychology, and other behavioral science fields. The theory explains deliberations among alternative courses of action, assuming motivation by the pursuit of individual usefulness or happiness—that is, *utility.*

Rationality suggests that decision makers select *optimal* options—the best possible or most preferred alternatives for each agent, given their resource constraints and knowledge of their environment. Decision makers maximize personal utility by carefully quantifying, weighing, and comparing all relevant information.

Rational decision making has been studied extensively in *neoclassical economic theory* under the theories of (1) the consumer and (2) the producer. Decision agents—households and firms—are conceptualized as rational actors maximizing *subjective (expected) utility* via the "self-interest standard." Given their knowledge of utilities, alternatives, and outcomes, they calculate the alternative yielding the greatest subjective utility for the costs incurred.

The *neoclassical (microeconomic) theory of the firm* studies individual business choices. Business organizations face the *profit maximization problem*, deciding which price and output alternatives maximize earnings.

The *neoclassical theory of consumption* (*consumer decision making*) analyzes individual consumer choices regarding quantities of various products (goods and services) to be purchased at particular prices. Consumers derive needs and wants satisfaction (*utility*) from the consumption of products. They face the *utility maximization problem:* how to maximize satisfaction by spending their scarce money. Buyers possess *omniscient rationality*—they make highly informed optimal decisions based on self-interested economic calculations, maximizing their expected utility per dollar spent.

This theory proposes a *utility function* providing a mathematical representation of an individual's preferences over alternative bundles (market baskets) of commodities purchased during some discrete time period. Personal preferences are defined to be rational and can be represented by a utility function if they are (1) *complete* (any two bundles can be compared, and all combinations of goods can be ranked), (2) *transitive* (logically consistent), (3) *reflexive* (more utility is preferred to less), and (4) *stable* (unchanging over a particular time period).

Two applications emerge. First, observers can normatively *describe* optimal economic behavior by explaining what the best decision *should* be in a given situation. Second, they can *explain* and *predict* what actual economic behavior *will* be.

Bounded Rationality and Satisficing

Neoclassical economic theory is based on several key but highly questionable assumptions from an empirical, behavioral perspective. Fundamentally, it assumes that people possess perfect and costless information. Specifically, the theory presumes the following:

- Individuals have precise information (or else a reliable probability distribution) regarding the outcomes of a particular decision.
- Persons are fully aware of all possible alternatives and their prices.
- Consumers are cognizant of the personal utility yielded by each item, fully understanding their needs and wants.
- People have the time and ability to compare all alternatives.

That such assumptions are usually unrealistic is embraced by the concept of *bounded rationality.* The computer scientist and psychologist Herbert A. Simon (1916–2001; Nobel Prize for Economic Sciences, 1978) of Carnegie Mellon University formulated bounded rationality theory during the 1950s. Simon pointed out that most people are only partly rational and are otherwise irrational. He noticed that in a complex and uncertain world, humans make decisions under the constraints of limited resources, knowledge, and time. Yet economics' rational decision-making models largely ignore information and time constraints. Consequently, Simon proposed "bounded rationality," suggesting that people are usually unable to calculate optimal strategies.

Another problem is that neoclassical economic theory is *prescriptive* (*normative, evaluative*), explaining how rational consumers *should* behave, assuming that they are fully informed, accurate, and rational. Hence, economics often seems moralistic, judgmental, and unrealistic.

The theory is based strictly on *deductive (inferential) reasoning*—deriving logical conclusions regarding optimal behavior. Conversely, bounded rationality is a *positive* (*descriptive*) approach—founded on *inductive (empirical) investigation* of actual behavior (the behavioral perspective), allowing decisions to be better explained or predicted.

In Simon's view, people's decisions are *unboundedly rational*—always the best, given their available evidence. Individuals are partly rational in that they try to logically understand things and make sensible choices. However, they lack the capacity and time to understand a large and complex world. Hence, bounded rationality models are more psychologically plausible than neoclassical economic theory without giving up completely on the idea of reasoned decision making.

Simon indicated that perfect (deductive) rationality breaks down for two reasons. First, there are *cognitive limitations*—restrictions of knowledge and cognitive capacity. People are constrained by their *schemas*—mental structures used to organize and simplify information. Furthermore, people cannot rely on others to behave perfectly rationally, and so they must guess their behavior.

A second cause of bounded rationality is *time limitations.* Computational difficulties make it difficult to make optimal decisions within a reasonable time.

Consequently, consumers formulate and resolve problems in satisfactory rather than completely optimal ways. In Simon's parlance, *satisficing* is behavior attempting to achieve at least some minimum level (rather than a maximum possible value) of an outcome: profitability for the firm and utility for consumers. Hence, people are only "rational enough," that is, they are *boundedly rational*—rational within certain limits.

Rational Ignorance Theory: Count the Costs

By extending the concept of "cost" to include these two nonmonetary factors—*cognitive effort* and *time*—almost every purchase maximizes the ratio of satisfaction to cost to some degree. As an example of effort, consider that classical economists regard *brand loyalty*—purchasing the same brand regularly due to a strong preference without considering competitive brands—as foolish due to the possibility of overlooking new and better alternatives. However, brand loyalty is rational if the shopper feels that the expected benefits of seeking out a better brand are not worth the effort and time.

As an example of time, consider patronizing convenience stores even though product prices are relatively high. Such patronage seems perfectly rational when the *opportunity cost*—the next best use of the consumer's time—is accounted for.

According to *rational ignorance theory*, ignorance about an issue is "rational" when the cost of educating oneself to make an informed decision outweighs any potential expected benefit from that decision. Even where information is available, its acquisition can be costly in terms of effort, time, and money. As postulated by *information economists* such as George Stigler, the rational consumer searches for marketplace information until the expected marginal costs of the search exceed the anticipated additional gains.

To save time, effort, and money, "cognitive misers" use *decision heuristics*—quick, easy shortcut mental decision rules derived from experience—to exploit reasonably consistent environmental patterns. Examples: "Purchase the brand your friend recommends," "Choose the brand rated highest by *Consumer Reports*," and "Buy the brand your spouse likes."

Often such heuristics entail a single buying criterion to simplify decision making, speed decisions, and overcome information overload. Examples: "Buy the brand with the lowest sodium content," "Pick up the lowest-cost brand," or "Purchase the best-known brand."

Search costs explain why, in the absence of easily acquired and understood gauges of product quality, consumers sometimes rely on a decision heuristic called *surrogate indicators.* These are readily discernable product attributes that consumers use, often erroneously, to make probabilistic inferences on product characteristics that are less easily comprehended, such as a product's composition, quality, or performance. Surrogate indicators serve as a product *signal*—a quick, easy way to deduce product quality. For example, reasonable buyers might assume that high price indicates high quality or that heavily advertised brands are better.

Such *market beliefs*—assumptions about how product signals connote quality or performance—are not always correct, thereby leading to *nonoptimal* choices. Market beliefs are most likely to be used where buyers have insufficient product category information, are unable to intelligently select, are rushed, and lack motivation to make a careful decision.

As the economist Gary Bauer has observed, heuristics-using consumers are nonetheless rational. Heuristics are rational since they help buyers reduce *perceived risk*—their beliefs about the uncertainty of possible negative product purchase and use consequences.

The Limitations of Human Perception

Perception is the process whereby people are exposed to, attend to, and comprehend information. Two characteristics of perception hinder acquisition of perfect information: *selectivity* and *subjectivity.*

The boundedly rational buyer's information intake is *selective* in two instances: (1) when it is not worth spending sufficient resources to obtain perfect information and (2) due to cognitive human limitations—people perceive only a tiny fraction of the surrounding sensory stimuli.

The stimuli people most likely notice are determined by (1) their *perceptual (mental) set*—what they expect to perceive based on prior experiences—and (2) their *perceptual predispositions*—desires, interests, values, beliefs, and attitudes. Individuals exhibit *perceptual vigilance*, being more likely to notice stimuli relevant to their needs. Humans also selectively perceive stimuli consistent with their predispositions to achieve *cognitive consistency*—uniform predispositions. Consequently, consumers seek advertisements affirming their purchase decisions, thereby alleviating *cognitive dissonance* (postpurchase doubt). In addition, consumers tune out stimuli that they find psychologically threatening or contradicting their predispositions (*perceptual defense*).

A second perceptual limitation is *subjective* perception—information acquisition is biased and distorted due to individual interpretations based on personal past experiences and predispositions. Hence, people generally perceive what they expect or desire. Consequently, marketers enhance brand perceptions via perceptual cues such as color (cigarette ads featuring lush green imply healthiness and freshness), euphemisms ("bargain priced" vs. "cheap"), and shapes (oval is feminine).

Subsumed under subjectivity is an issue ignored by neoclassical economists—*emotional satisfaction.* Traditional economists believed that it is irrational to purchase based on *emotions*—uncontrollable feelings (e.g., fear, anger, excitement). However, fulfilling emotional motives yields satisfaction, so rationality should be broadly interpreted to include them.

Simon explained that a full account of human rationality must include emotions' influence on choice behavior. Contrary to Simon's early writings, subjective, emotional criteria are not irrational because irrationality implies failure to maximize utility. However, consumers nearly always attempt to select alternatives that, in their estimation, maximize their satisfaction, including emotional or hedonic fulfillment. For instance, a product might be selected based on its promise to enhance the user's sex appeal, thereby bolstering the consumer's self-confidence. Hence, rational and emotional motives can both underlie a given purchase. In fact, the opposite of rational is not emotional but *nonrational* or *irrational*, while the opposite of emotional is not rational but rather *nonemotional.*

One type of emotional purchase is *impulse purchasing*—buying without deliberate, careful planning. People display *time inconsistency*—when deciding about the future they are reasonably rational. However, when facing a decision on whether to gain consumption pleasure now or defer gratification to maximize their long-term best interests, they can be as impulsive as wild animals (e.g., grabbing a package of junk food in the supermarket checkout aisle). Impulse purchasing appears economically unwise and irrational. However, such consumers also might have short time horizons, deriving much more utility from current pleasure than from the possible long-term gain realized by abstinence.

The Paradox of Altruism

Simon and others have questioned the classical economics assumption of the "self-interest standard." Consider *altruism*—caring for one's fellow humans, leading to maximizing others' interests while sacrificing one's own self-interest. Altruists practice self-sacrifice for general causes such as the public good or the environment.

Economists have traditionally viewed helping behavior as a paradox since it fails to enhance one's own well-being. For instance, *empathy*—feeling compassion for others—leads to selfless behavior (e.g., parents sacrificing time, money, and energy for their children). Other examples include philanthropy—acts of charity—and voluntary deeds of duty, such as serving in the armed forces during wartime or purchasing environmentally friendly but expensive products.

However, usually underlying all these forms of altruism is self-interest since they usually give a "warm glow" and a sense of moral satisfaction. Indeed, traditionally, moral philosophers have accentuated "constrained self-interest" over pure self-interest.

The Limitations of Consumer Sovereignty

Simon also questioned the neoclassical assumption of *consumer sovereignty*—buyers being in reasoned control of their decision making and not malleable by outside forces. In perfectly competitive markets, where both buyers and sellers have freedom of choice and good (if imperfect) information, consumers are sovereign—uncontrollable by external forces.

However, modern psychology, communication theory, and marketing practice recognize that marketing efforts, peers, and society can influence buyers. Moreover, the assumption of consumer sovereignty can be very flawed. These are so-called *free-market failures*—marketplace exceptions to the classical economic assumption that informed consumers make optimal decisions.

Four such marketplace circumstances relate to bounded rationality and have clear ethical/social implications:

1. *Consumers lack "perfect" (or even "good") information.* For instance, for hi-tech and health care products, technology, complexity, or the pace of change has outpaced the learning ability of most buyers. This *information asymmetry* between buyers and sellers means that purchasers are at a disadvantage relative to knowledgeable sellers who can take advantage of their ignorance.

2. *Deception and other unethical behaviors occur.* Consumers cannot make intelligent decisions if they are misled into believing something false. Deception arises from marketing communications creating a divergence between perception and reality, resulting in marketer manipulation of consumers.

3. *Vulnerable groups exist.* Certain categories of consumers fail the "reasonable man" test—they are more easily misled. These groups include children, people with mental disabilities, the emotionally disturbed, the recently bereaved, some recent immigrants, those of low education levels, addicts, and some elderly people.

4. *Consumers have latent needs. Latent* (subconscious) wants are those that buyers are unaware of—they lack conscious knowledge of what they need. Latent needs characterize "unsought goods"—products satisfying functional needs but yielding delayed gratification (e.g., life insurance, cemetery plots, estate planning). Consumers therefore ignore information on these products. Marketers who are accused of trying to "manufacture demand" are actually often simply trying to tap into these subconscious needs.

Often, private market solutions to these problems will not work, and instead, government intervention is recommended (e.g., providing consumer information, punishing deception, and protecting vulnerable groups).

Social and Ethical Issues

The theory of firm and consumer rationality is grounded in neoclassical economics and capitalism, stemming from the work of the 18th-century moral philosopher Adam Smith, who emphasized that a free-market economy should occur within a legal and moral framework. Smith argued that the capitalist system is based on managers' honesty and integrity, without which the "invisible hand" would not work.

However, modern economics during the 20th century became an "amoral" science, presupposing "value-free" market exchanges. It focused on how things *actually* work *materially* rather than on how they *should* work *morally*. However, Smith never envisioned a value-free pursuit of wealth ignoring moral judgments or ethical consequences.

Neoclassical economists merely explain market participants' choices, considering it beyond their discipline to morally judge these choices. Economists do suggest that for business activity to benefit society, observance of *minimal moral restraints* is necessary (avoiding theft and fraud, observing contracts, etc.). Beyond this, they say, business managers need concern themselves only with maximizing profits.

However, increasing profits via means such as pollution, bribery, tax evasion, and price-fixing harms society. Consequently, the firm's economic objective can be framed in boundedly rational terms as a *constrained optimization problem*: Maximize profits subject to qualitative ethical/social responsibility constraints (e.g., considering employee, environmental, and consumer welfare).

Archie Carroll outlined four levels of *corporate social responsibility*—the second through fourth might entail sacrificing corporate profits:

1. *Economic responsibilities:* Being profitable for shareholders while providing economic benefits to other corporate stakeholders (e.g., fair-paying jobs for employees and good-quality, fairly priced products for customers)

2. *Legal responsibilities:* Complying with business laws

3. *Ethical responsibilities:* Going beyond the law by avoiding social harm, respecting people's moral rights, and acting justly

4. *Philanthropic responsibilities:* Voluntarily "giving back" time and money to good works enhancing various stakeholders' well-being

Since sellers deal with buyers possessing imperfect information, several controversial social and ethical issues arise. Readers can delve more deeply into these:

- There is the economic argument that producing whatever the buying public wants is good. However, satisfying buyers' desires assumes that their wants are moral and they know what is in the best interests of themselves and society. What about controversial products such as handguns, pornography, and even "unhealthy" fast food and junk food? But disallowing them would rob consumers of choice, further eroding consumer sovereignty.
- Whose moral responsibility is it to educate consumers so that they can make better-informed decisions: the firm, the consumer, the government, or some combination thereof? How can this education be best implemented? Can and should sellers strive to reduce consumers' time, money, and energy costs in gathering this information? Is the fact that people selectively screen information a justifiable excuse for not providing full disclosure?
- Do marketers sometimes create artificial brand loyalty by increasing *switching costs*—psychological, physical, and economic costs that buyers face in switching between technologies or products, such as learning new tax preparation software?
- Is encouraging impulse purchasing through tactics such as enticing in-store displays and samples ethical? After all, these can be very emotional decisions, and consumers often feel temporarily out of control.
- Might the use of surrogate indicators by marketers in signaling quality to uninformed consumers sometimes be misleading? For example, if a product is of comparable quality with its competitors, is it ethical to charge a higher price to create a high-quality image?
- Are "impression management" and "spin control"—selectively and positively reporting information to make one's firm look good—morally justifiable in light of subjective and selective perception?
- Can perceptual cues, such as appetizing artificial colors in food, and euphemistic language, such as "gaming" (for *gambling*), be deceptive?
- Might the use of strong emotional advertising and selling appeals such as fear, guilt, and fantasy confound consumer decision making?
- Where do advertisers and salespeople cross the line between exaggeration ("puffery") and deception?
- What extra precautions, if any, should be taken with vulnerable groups? For instance, are children more susceptible to impulse purchasing, perceptual cues such as attractive packaging, emotional appeals, and puffery?
- Is it legitimate to conduct *motivational research*—marketing research tapping into buyers' latent needs through techniques such as depth interviews and indirect questions, with a view to appealing to those needs?
- Is it preying on consumers' altruistic sensibilities to use appeals such as cause-related marketing (donating money to a charitable cause for each unit of a brand purchased)?
- Can corporate social responsibility activities become a public relations ploy?

—Geoffrey P. Lantos

See also Altruism; Consumer Sovereignty; Corporate Social Responsibility (CSR) and Corporate Social Performance (CSP); Economic Rationality; Economics, Behavioral; Information Costs; Opportunism; Rational Choice Theory; Rationality; Satisficing; Smith, Adam; Strategic Corporate Social Responsibility; Utility

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Boycotts

A boycott occurs when one or more parties (e.g., consumer advocacy groups, activist organizations, local municipalities) ask that consumers refrain from making certain purchases to achieve desired goals. Boycotts target businesses directly and governments indirectly via boycotts of businesses operating under an offending government's jurisdiction. The boycott of Shell, Coca-Cola, and other companies for their operations in South Africa under apartheid is an example of such a boycott, sometimes called a surrogate boycott. Note that although some boycotts occur in an effort to meet consumer aims, successful boycotts are often used to achieve essentially non-market-based goals of primarily moral import. Boycotts have been used to combat discrimination, improve labor conditions, and raise the bar on corporate policies concerning the environment and animal welfare.

The term *boycott* dates back to a dispute between a British estate manager in Ireland, Charles Cunningham Boycott, and his workers. After years of leaving the workers in deplorable living conditions, Boycott decided to pay his tenant farmers a fraction of their usual wage to bring in the harvest. When they refused, Boycott had his family attempt to bring in the harvest. When his wife pled with the workers, they agreed to return to work but were evicted on rent day. The workers vowed to ostracize Boycott completely, urging all his servants to quit and promising that his name would go down in infamy. Although today's boycotts still engage in economic ostracism, they rarely involve the same degree of social ostracism.

Contemporary boycotts are generally employed alongside other forms of consumer activism such as shareholder activism, socially responsible investment or divestment, and direct lobbying of the offending institution. Since boycotts generally occur in tandem with other strategies for effecting social accountability, it may be difficult to determine the boycott's effectiveness in isolation. That said, it should be noted that boycotts have been important to institutional reform. It should also be noted that the efficacy of contemporary boycotts often depends more on media publicity than on actual loss of sales. Damage to the corporate image is generally perceived as the greater threat.

Boycotts may be implemented in several ways. Commodity boycotts ask that consumers refrain from the purchase of all brands and models of a particular product or service. A boycott of meat would be an example of a commodity boycott. Other boycotts target a single brand name or a firm along with all its brand name subsidiaries. In 1981, the Interfaith Center on Corporate Responsibility launched a boycott against Nestlé for its marketing of formula that led to countless infant deaths in the developing world. This would be an example of a brand name boycott since all Nestlé brand products were targeted.

Perhaps the most well-known boycotts are the antisegregation bus boycotts in the American South during the 1950s. At the time, buses were segregated by race. If the whites-only section of the bus were to fill up, blacks were expected to give up their seats. In March 1953, black community leaders in Baton

Rouge successfully lobbied for passage of an ordinance allowing blacks to be seated on a first-come, first-serve basis. Drivers, unwilling to enforce the measure, went on a 4-day strike. A suit was filed; the Louisiana attorney general sided with the drivers since the Baton Rouge ordinance violated state segregation laws. In June 1953, a majority of the black population, who had originally accounted for about two thirds of all riders, boycotted local buses. Eventually, a compromise was struck allowing black riders to be seated on a first-come, first-serve basis so long as the rear seat of the bus was reserved exclusively for blacks and the two side front seats for whites.

This boycott was followed by the renowned Montgomery bus boycott. On December 1, 1955, Rosa Parks refused to give up her seat to a white man, in violation of segregation law. Parks had long been involved in local politics, serving as a secretary for the local National Association for the Advancement of Colored People between 1943 and 1955. This was not the first time that Parks had violated segregation laws, but this time local leaders decided to launch a boycott in protest. Local leaders elected to have Martin Luther King Jr. take over leadership of the 382-day boycott. As in the Baton Rouge boycott, the organizers were successful because they were able to arrange alternate transportation through the formation of the Montgomery Improvement Association. More than 90% of black riders stayed off the buses until the case made its way into the federal courts for an antisegregation ruling.

African Americans are not the only group to have used boycotts in the fight against racism. American Jewish communities organized a boycott of German goods during World War II. By April 1939, a Gallup poll showed that 64% of Americans were willing to join the movement to boycott German-made goods. Later, in March 1992, American Indians were outraged when the Hornell Brewing Company introduced Crazy Horse Liquor. Many felt that the liquor's name was insensitive and demeaning given the alcohol abuse problems facing American Indian communities. Moreover, the revered Lakota leader was known to have vehemently opposed the consumption of alcohol by American Indians. Two other organizations joined the American Indian Movement in calling for a boycott.

Boycotts have been a key strategy for defenders of human rights in other arenas as well. ACTUP (AIDS Coalition to Unleash Power) initiated a boycott of Philip Morris in the early 1990s, citing the company's campaign donations to Senator Jesse Helms, an opponent of gay rights. The boycott ended in June 1991, when Philip Morris said that it disagreed with Senator Helms on gay rights but that it may still donate to his campaign. Lest the company be seen as opposed to gay rights, Philip Morris promised to give at least $2 million to gay and AIDS support organizations annually. Feminists have also launched prominent boycotts. The National Organization for Women, for instance, called for tourism boycotts of states that refused to pass the Equal Rights Amendment in the 1970s.

Although labor organizers typically rely more on strikes to effect change, labor has strategically used boycotts when scarcity of labor was difficult to control. This was especially true during the late 1800s and early 1900s in the United States. The Knights of Labor, who represented easily replaceable, largely unskilled workers, launched strategic boycotts of necessities and inexpensive luxury items. The Knights of Labor also engaged in secondary boycotts—that is, the boycott of businesses selling items produced by the offending companies. During the mid-1890s and in 1908, the American Federation of Labor published a "We Don't Patronize List" in a similar attempt to get business to meet labor demands. After the Supreme Court decisions of *Loewe v. Lawker* and *Buck's Stove* made boycotts more difficult, the American Federation of Labor stopped printing the list. The Taft-Hartley Act of 1947 banned secondary boycotts as an unfair labor practice, and the Landrum-Griffin Act of 1959 outlawed secondary boycotts as coercive.

More recent labor boycotts include an initiative advanced by the United Farm Workers Organizing Committee in California led by Cesar Chavez during the 1960s. The boycott of grapes picked by migrant workers was launched when the National Labor Relations Act denied migrant farm workers the right to organize. Within 6 months of launching the boycott, there was a 30% drop in grape shipments to New York City, the United States' largest urban market for grapes. Another recent labor boycott was led by the Coalition of Immokalee Workers (CIW). Their 4-year boycott of Taco Bell ended in the spring of 2005. CIW, representing primarily Guatemalan and Mexican tomato workers, demanded that Taco Bell pay one penny more per pound of Florida tomatoes and adopt a code of conduct allowing Taco Bell to cut ties to suppliers who abuse farm workers. Taco Bell announced that it would pay growers an extra $100,000 per year for tomatoes. Taco Bell also agreed to help farm workers persuade other fast food chains and tomato retailers to increase pay and monitor conditions to ensure that workers are not beaten or forced into indentured servitude.

Environmentalist and animal welfare organizations have launched numerous boycotts. These boycotts are especially likely to be part of a broader strategy to change standard practices in entire markets rather than targeting the policies of a single supplier. Often, industry leaders are subjected to the first boycott in the hope that other members of the industry will follow suit in a domino effect. Rainforest Action Network (RAN) led a 9-year boycott of Mitsubishi, which ended in 1998 after the company agreed to stop using old growth timber and to use almost all non-wood-based paper by 2002. In 1997, Greenpeace, RAN, the National Resources Defense Council, Forest Ethics, and others formed the Coastal Rainforest Coalition (CRC). This group first targeted the Home Depot, as an industry leader in the home supply chain industry, asking the company to stop purchasing timber from ancient forests. In 1999, Home Depot agreed to a progressive wood-sourcing policy. After a successful campaign with Home Depot, CRC moved on to Lowe's, Menards, Wickes Lumber, and 84 Lumber, all of which agreed to make substantive changes. People for the Ethical Treatment of Animals (PETA) has implemented a similar strategy. PETA launched a campaign against McDonald's in 2001 asking the company to allow announced and unannounced slaughterhouse audits of all its livestock suppliers, stop purchasing from suppliers who failed the audits, increase space for laying hens, and change feeding and catching standards. In September 2002, McDonald's agreed. PETA launched a similar campaign against Burger King, which agreed after 5 months of the boycott to make the requisite changes. PETA has since moved on to a boycott of KFC, in the hope that the fast food industry will follow the lead of companies like McDonald's and Burger King. It is interesting to note that in these examples, media exposure was highlighted more than the refusal to purchase products.

The aforementioned environmental and animal welfare boycotts are led by professional organizers that are likely to see boycotts as fundamentally instrumental, one step in a long-term strategy to effect positive policy changes. This stands in contrast to expressive boycotts where the organizers' primary aim is to express dismay with corporate policy. Punitive boycotts employ aspects of both instrumental and expressive boycotts. A punitive boycott is designed both to express public outrage concerning perceived policies of wrongdoing as well as to effect future changes. For example, the American Family Association and Christian Leaders for Responsible Television boycotted Chlorox, Mennen, and Burger King in an effort to punish the companies for supporting television shows with sex, violence, and profanity. This sort of boycott both expresses moral disapproval of corporate policy and seeks specific policy changes. In 1990, due to the boycott, Burger King promised to support programming that promoted "family values." It should be noted that even the more instrumental boycotts employed by professional environmental and animal welfare organizations may involve punitive aspects as well.

—Mary Lyn Stoll

See also Consumer Activism; Consumer Preferences; Consumer Sovereignty; Corporate Accountability; Shareholder Activism

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BRANDS

A brand is the unique, ownable identity of a business, enterprise, company, or undertaking. It includes the name of the entity and its logotype or any identifying design by which the enterprise is known and recognized, and it conveys what the enterprise stands for, its products and services, and ultimately its role and significance for the customer, consumer, user, or perceiver in its respective society, culture, or civilization.

Increasingly, a brand is any carefully articulated identity.

During the late 20th century, corporate brands rose to a level of strategic significance within the world of modern business and enterprise. Growing from their humble origins as an indicator of ownership or a source of goods, brands became the primary tool used to create and orchestrate enterprise identity, a major factor in setting corporate strategy, and an important asset in developing enterprise value and creating wealth. As such, brands became the most important and the most strategic and monetarily valuable asset in successful organizations, be it a commercial enterprise, a nonprofit organization, a governmental agency, a nation, or even an international body,

Concurrent with this rise to previously unprecedented social and economic power, brands, with their ability to determine perception, drive behavior, and influence public markets, have become the focus of a number of ethical debates regarding the nature of capitalism, consumerism, and corporate social responsibility.

The Power of Brands

Although they have existed since the earliest days of urban civilization and commerce, brands made their debut, in the modern sense, during the European Renaissance as the "trade names" of businesses and enterprises.

However, it wasn't until during the 17th and 18th centuries that brands began to be used commercially as "brand names" to market goods and services and thus to have an increasingly commercial existence. It was with the arrival of their use for commercial purposes that brands began to achieve their modern significance as a valuable enterprise asset. By the end of the 19th century, with the passage in the United States of the federal trademark legislation of 1870, "trademarks" acquired rights similar to those of real property, and these early brands became formally acknowledged and protectable under the law.

Throughout the 20th century, brands became recognized for their ability to distinguish one product or service from another, impart intangible value, convey quality, and eventually, in a world increasingly populated with brands, enable consumer choice in the marketplace. Most notably, during the 20th century, with the rise of marketing as a business discipline, it became clear that branded products and services commanded higher prices and delivered greater margins to their enterprises, as consumers often chose one nearly or actually identical product over another because of what its respective brand stood for in their minds.

By the end of the 20th century, business leaders and corporate executives had become aware of the power of brands to deliver competitive advantage and build wealth. Thus, "branding," now understood as the articulation of a compelling identity and the successful positioning of an enterprise within a market, became a theory of brands that formalized the principles of creating and strategically deploying these powerful new assets.

It was only as the brand, understood as a powerful asset of the organization, began to be deployed to drive markets by maximizing consumption that questions emerged regarding the ethical use of brands within society. As it became clear that brands could instill desires where they hadn't previously existed and otherwise increase consumption, especially within easily persuaded audiences such as children, the elderly, or the less educated, the negative concept of "consumerism" emerged along an ethical spectrum of increasingly questionable enterprise behaviors that were suggestive of greed and exploitation.

For many, the apparent manipulation of audiences and populations to drive corporate profits became questionable and, for some, morally reprehensible. Brands had been a benefit to society in building and segmenting markets, in differentiating goods and services, and in the eventual discovery of intangible assets as powerful creators of wealth. However, as corporations sought and investors came to expect unending growth from their commercial enterprises, aggressive forms of marketing evoked ethical questions about the propriety of creating unnecessary desires and driving consumption beyond natural need, the effect of omnipresent advertising and the overall commercialization of society, the possibly unsustainable toll on natural resources and the environment incurred by unnecessary manufacturing and the consumption of raw materials, and the effect on society of creating a worldview that equates personal happiness and self-image with shopping, consuming, and owning material possessions.

The Theory of Branding

Largely developed through the 1990s and into the first decade of the 21st century by management consultants, marketers, and corporate executives within the pages of well-established professional business publications such as the Harvard Business Review, the California Management Review, and the Wall Street Journal, brand theory has only recently become aware of itself as a discipline.

Brands have been defined by theorists as the primary identity vehicle for products, services, initiatives, and entities transacted within the economy and society. In the most formal sense, brands are understood as highly successful commercial or public entities with well-orchestrated identities that consist of complex sets and hierarchies of meanings and attributes and that are broadly and instantly recognized, accurately perceived by specific constituencies, and associated with a name, a trademark, and often a symbol.

From the perspective of an enterprise, brands are an intellectual capital asset that organizes and gives meaning to an undertaking. From the perspective of management, a brand is that for which all activities are undertaken, the *raison d'etre* for the development and marketing of various products or services. And strategically, a brand is that which is leveraged to achieve strategic results and, most essentially, to provide competitive advantage and create often substantial monetary value.

Uniquely, brand theory holds that brands *distill* intellectual, monetary, and moral value from other organizational intangible assets, such as intellectual property, knowledge, human capital, corporate culture, innovation, core competencies, or the social capital that is unique to a respective organization. Accordingly, brands, by their nature, put a face on products, services, and other intangibles or knowledge-based assets and organize them into an expression of a more complex set of meanings. This process is called "branding" and is based on defining what the brand stands for, articulating its values, identifying its audiences, and ultimately creating its personality. Such organizing is what creates or produces the economic value chains that turn ideas and innovation into products and services and, eventually, into brand assets that drive wealth.

In this sense, intangible assets, such as an intellectual property portfolio of patents, may be very valuable economically, but brand theory suggests that whatever that value may be, it is likely to be worth exponentially more when it is advanced commercially under a brand that provides more complex and organized meanings.

Therefore, in brand theory, well-articulated brands (1) communicate the meaning of an enterprise; (2) identify its goods, attract consumers, and differentiate the company from other players in the marketplace; (3) create trust and repeat purchase, increase interaction, and encourage brand loyalty; (4) possess extraordinary economic value, convey that value, and deliver profitability; and (5) become intellectual capital assets of the respective organization—all of which benefit the individual enterprise and, possibly, society.

The Practice of Branding

It is with the "practice" of branding that we can begin to see ethical issues arise. With the advent of the 21st century, branding became a highly formalized practice that was applicable across all organizations, products, and services in all the major industries and sectors within the economy and society, and it was a well-defined professional discipline practiced by management consultants and corporate executives.

The strategic thinking behind a brand is captured by the concept of a *brand strategy*, whereby what the brand stands for is thoroughly articulated, its position within the marketplace is analytically identified, and a marketing strategy that implements and realizes that brand strategy is defined.

To this end, practitioners developed methodologies to define the enterprise to be branded, stating the justification for the brand, its relevance to the consumer, its promise, and some summary brand philosophy that defines what a brand stands for in the minds of its consumers. Also, the most influential brands have determined how they will be expressed, dimensionalized their "brand personalities," and created a brand identity to incarnate their respective brand. When thought of this way, every brand needs a strong creative and imaginative idea at its center that brings it to life and provides it with relatively unlimited possibilities for growth and expansion.

In addition, every brand is assumed to be a true expression of the enterprise for which it stands. Thus, brands, in their nature, possess an ethical core, character, or agency from which they may or may not diverge. Brands that evoke the greatest levels of trust and marketplace success are frequently those that are founded on and expressive of the authentic nature of their respective enterprise. In contrast, those brands that are founded or deployed purely on motives of greed and exploitation and are embarked on only for commercial gain are those that invoke the least trust, are frequently seen as mere façades, and are deemed to be those that most characterize "commercialism" in its worst sense. Such brands exist not to express the abiding nature of an enterprise but solely to capitalize on and exploit yet another target audience or to maximize consumption beyond need, and they are seen by individual consumers and society to violate the trust society expects between business and its markets. Society expects a business to deliver legitimate products and services, and the potential trickery that marketing is capable of delivering to entice unnecessary consumption and to sell yet another unit or service to make the numbers that will drive earnings and stock prices is increasingly seen to be in bad faith and thought to be socially irresponsible.

Others, in contradistinction, believe it is the prerogative of business to sell products and make as much money as possible for itself and its shareholders by whatever legal means exist. They argue, in juxtaposition to the social responsibility argument, that their responsibility lies in delivering earnings and gains to their shareholders and that rather it would be "bad faith" to investors not to maximize their returns, even at the expense of aggressive marketing technique.

Both schools of thought seek their respective maximal profits but draw the line differently between the maximum allowed under a social conscience and the maximum allowed under the law. In either case, the operational deployment of a brand, referred to as "building the brand," involves marketing programs that are designed to enhance the image and vitality of a brand or brands. Increasingly, and in virtue of the sophisticated brand valuation tools developed at the turn of the 21st century, enterprises are regularly able to benchmark the monetary value of their brand to obtain a baseline against which to measure the ability of a brand or marketing program to build brand equity.

The implicit code of ethics that stands behind the modern practice of branding is grounded in the assumption that brand building builds or develops brand equity, thus contributing to enterprise value, and that commercialization understood as exploitation destroys brand equity but may drive enterprise revenues. The primary strategies driving the development of brand equity at the beginning of the 21st century are marketing strategies such as (1) niche marketing, (2) integrated marketing, (3) lifestyle marketing, (5) permission marketing, and (5) corporate social responsibility initiatives.

Historically, the first impact of the rise of brands was the shift from traditional marketing, which was designed to create desire in mass populations, to niche marketing. By the late 20th century, markets had become flooded with brands. Across the consumer products industries alone, over 20,000 products per year were entering the marketplace, and by the end of the decade of the 1990s, many segments of the consumer marketplace were reaching saturation. Consumers were swamped with innumerable advertising messages each day, and only the most highly differentiated brands could cut through the media clutter to be perceived and engaged by consumers. Well-branded products became essential to enabling the shopping process, and soon only those products that had identified a "niche" in the marketplace for their message could be expected to survive. Thus, marketing became "niche marketing," and "positioning" products for consumer apprehension became de rigueur.

Soon, driven by the globalization of commerce and the proliferation of channels of trade such as the Internet, modern branding also became characterized by "integrated marketing." Branding started to involve the creation of one coherent identity that was well articulated and able to be communicated in each of the various internal and external communications that each enterprise needed to deploy in each of its respective markets and channels of trade. In daily business, this meant that each dimension of a brand was defined and mapped against the needs of the respective consumers to ensure that a consistent and well-integrated brand was presented at each communication opportunity. Because the expressions and communications about a brand needed to be orchestrated and blended to achieve synergy and because research demonstrated that perceiving the same identity or same brand through multiple media and channels of trade increased credibility and brand awareness, marketing became "integrated marketing."

Further, because research had demonstrated that the most successful brands became part of the consumer or end-user's "lifestyle," marketing also focused on positioning products within the lifestyles, usage occasions, and consumption patterns of target audiences. By the end of the 1990s, brands had become a part of the identity of individual lives, and they were implicated within the individual consumer's self-discovery in such a way that they became an expression of an individual's inner spiritual and personal search. Thus, too, marketing became "lifestyle marketing."

While each of these approaches, per se, grew out of the evolving dynamics within markets, as markets became more saturated and competition increasingly fierce, what became the commercialization of society began to emerge. Soon, everything was an advertising medium. Coupons, deals, direct mail, telemarketing, broadcast media advertising, in-store marketing, online spam and pop-ups, in-store radio, and cell phone advertising all combined to reach a crescendo culminating in the branding of university and civic buildings in return for monetary considerations of one form or another. For many, business was overstepping its proper bounds, invading personal privacy, destroying culture, and undermining civilization by commercializing every space and moment as a selling opportunity.

Concurrently, brand marketing, in an effort to regain its ethical character as a discipline and the respect of consumers, adopted an approach known as "permission marketing." Assailed by sophisticated marketing strategies, constant advertising, intrusive direct marketing efforts, and new online promotional vehicles, consumers reacted in various ways to filter out the ongoing onslaught of marketing and advertising messages. Permission marketing appeared to characterize those endeavors that marketed only to receptive targets that were interested in the offered goods.

The most recent evolutionary development of brand strategy has been the trend toward corporate social responsibility. Oversaturated markets and omnipresent advertising messages were driving high levels of market fragmentation and a consumer backlash against marketing per se and the companies that used it the most. Many brand strategists began to see a need to take an entirely different approach to building their brands through a focus on corporate reputation, which became known as corporate social responsibility. With a commitment to favorably influencing or solving social problems that were frequently complementary to enterprise markets, brand strategists found a new way to build important levels of brand equity while at the same time being instrumental in ameliorating many of society's ills. However, in many cases, even corporate social responsibility became hollow rhetoric, just another marketing tactic, without sincere motivation. Fortunately, for many businesses, corporate social responsibility predominantly became an ethical brand-building response to the greed, exploitation, and abuse of their markets.

While probably any approach to branding and marketing could be abused, the dynamics of markets and competition, compounded by the demands of investors, creates a complex ethical situation. Investors expect their investments to grow and demand steadily increasing quarterly earnings, and thus, businesses must find ways to deliver the unending growth that is becoming more impossible in saturated markets. Thus, business and enterprise must turn to marketing and branding to drive new levels of consumption and market penetration.

However, because branding and marketing as disciplines and business practices are ethically neutral as methodologies, careful attention to the development of socially responsible brand strategies, coupled with approaches to brand marketing that build brand equity, typify the modern practice of branding and its ability to orchestrate values and meanings to create notable monetary value. Increasing sophistication among professional practitioners and the realization that intangible, intellectual capital assets such as brands are driving significant new levels of enterprise market capitalization and societal wealth are working together to enhance the strategic significance of brands in the modern world.

The Financial Dimensions of Brands

Because brands have become valuable assets that are readily improved by intelligent development and wise exploitation, they have also caught the attention of accountants, financial analysts, investors, and capital markets.

Worldwide, there are hundreds of thousands of brands, with thousands more entering the public marketplace every year. In the United States alone, over 245,000 trademark applications are filed each year with the Patent and Trademark Office. Combined, these many brands constitute a major economic force in the world. During 2005, estimates place U.S. market capitalization at nearly $15 trillion, with over $11 trillion of that amount being contributed by brands and other intellectual capital assets. Such calculations highlight the enormous opportunity to be realized by businesses, the economy, and society through the astute leveraging of assets of such tremendous value.

For these and similar reasons, the branding of products and services has emerged to occupy a place of paramount concern within businesses, often becoming *the* corporate or enterprise strategy. By the end of the 1990s, branding had become the *uber*-discipline for CEOs, corporate executives, and marketers. Articles and books on the subject of branding appeared daily, and numerous branding consultancies emerged, specializing in creating every aspect of a dominant, winning identity in the marketplace. Brands moved to the center of business strategy, and prestigious business and financial publications such as *Financial World, Fortune,* and *BusinessWeek* began printing annual tabulations of the "top 100 brands" and their specific monetary values.

Showcasing the monetary value of brands has helped financial analysts and executives recognize them as their most valuable assets and, thus, develop correspondingly sophisticated strategies designed to leverage these intangible intellectual assets to drive corporate valuations and market capitalization in much the same way that traditional physical and financial assets have long been leveraged to deliver enterprise performance. The simple axiom that leveraging your most valuable assets is the essence of good management applies no less to intangible intellectual assets and brands, as their paramount instantiation, than it does to plant, property, equipment, and financial assets.

However, complex ethical issues arise with the valuation of intangible intellectual assets that frequently go undetected because of both the complexity of setting such valuations and that of the financial transactions that surround such assets.

The primary market for intellectual assets such as brands and intellectual property is that of mergers and acquisitions. Since the early 1990s, such assets have increasingly determined pricings in such transactions. Brands were quickly recognized as the primary source of value in such dealings, and soon brand valuation methodologies emerged to set values. However, their complexity militated against transparency, opening the door to min-maxing tactics that led to substantial balance sheet write-downs that hurt investors and their respective businesses. The volatility and difficulty in defining the metes and bounds of such assets has often spawned unscrupulous activity that is only recently beginning to be policed through new Financial Accounting Standards Board regulations and rules that minimize conflicts of interest and encourage enhanced impartiality.

The Future of Brands

The concept of branding, while quickly spreading around the world, has also spread beyond the world of business into nonprofit organizations and society, into government and nongovernmental organizations, into the world of personalities and celebrities, and into every area where complex created identities operate. Thus, the future of brands is tied up with business and the economy, society and culture, governments and civilization, worldviews, and the entire zeitgeist. Brands have laid an intellectual foundation that, like the ripples from a pebble falling into a still pond, is spreading outward across the dimensions of our world and influencing the creation and management of identity in diverse respects.

Most obviously, in the 21st century, brands have become the future of business in every form because they have extended the paradigm of business from the product or service itself to its meaning in our minds and our society. As a result, brands have enlarged the economic capacity of our global economies, allowing them to hold thousands upon thousands of individual products that wouldn't otherwise exist and all the while concurrently creating vast amounts of new wealth out of ideas and meanings.

Brands, with their miraculous economic contributions, convey the promise of a bright economic future. Yet the brands of the future, if they will fulfill such a promise, face theoretical and practical challenges that are inherent in their nature and their dynamics.

As brands become more global, many face problems of brand elasticity and diminishing returns as they seek to encompass ever greater ranges of meaning and significance. The meaning of an individual brand can only be stretched so far before it begins to lose it significance and becomes empty and meaningless. Consequently, in the future, brand elasticity will remain a problem as brands struggle to orchestrate global meanings without overextending themselves.

In addition, as the number of brands in existence continues to increase, many may find it difficult to carve out differentiated brand positions in their respective markets as they grapple with the finitude of possible brand positions. Many early-21st-century markets are already becoming saturated, and a market can only be parsed and segmented so far before meanings collide and become inconsequential.

Both issues of brand elasticity and those of brand positioning are leading to increased instances of unfair competition, trademark infringement, trade dress infringement, misappropriation, piracy, and counterfeit goods as legitimate enterprises and illegitimate enterprises collide. While many such matters are illegal and are handled in due course through litigation and indictment, many are also ethical problems requiring enhanced professional ethics and enterprise codes of conduct for their amelioration.

Brand lifespan may also emerge as a problem for markets and consumers, as some brand strategists strive to create brand vitality and fail, leaving their efforts to clutter the commercial landscape with diluted meanings, creating consumer dissatisfaction, and frustrating legitimate commercial aspirations. Waves of brands that come into and go out of existence create confusion and undermine trust in all brands—for trust is of the essence for a brand, and the most successful brands are always those that inspire the greatest trust, the ethical sine qua non for brands. Correspondingly, the entire role of marketing and the overcommercialization of society will continue to be debated, putting pressure on brands to have meaning, legitimacy, and authenticity and to avoid creating social problems of excess, insincerity, and exploitative intention.

Further, to meet the challenges of the future, many thinkers believe that brands will need to productively marshal an ongoing commitment to successful innovation in order to ensure their continuing relevance with an ongoing stream of "new" products or services. In this respect, much will depend on the talent and skill with which brand propositions are articulated and expressed and structural issues such as whether brands can remain relevant beyond their native audiences, their generation, and their nationality without losing critical mass with those constituencies.

Brands are also deeply implicated in fulfilling the ongoing need of society for prosperity, and because of their power to organize other intangible assets, synergize their value, and constellate higher-order sets of meaning, brands are likely to play a determining role in the future creation of wealth. For many, their evident impact on the development of prosperity at the end of the 20th century portends the creation of new wealth beyond that ever yet produced through traditional physical or financial assets. This paradigm shift to a new era of intellectual capital assets, with the brand—because of its distilling nature—as the intellectual capital asset par excellence, brings with it a whole new momentum that promises new value, based not on supply and demand but on meaning and significance.

—Lindsay Moore

See also Advertising, Subliminal; Advertising Ethics; Authenticity; Bait-and-Switch Practices; Conflict of Interest; Conspicuous Consumption; Consumerism; Corporate Citizenship; Corporate Moral Agency; Corporate Social Responsibility (CSR) and Corporate Social Performance (CSP); Deceptive Advertising; Economics and Ethics; Ethics of Persuasion; Financial Accounting Standards Board (FASB); Human Capital; Intellectual Capital; Intellectual Property; Mergers, Acquisitions, and Takeovers; Piracy of Intellectual Property; Social Capital; Trademarks; Transparency; Unfair Competition; Wealth Creation

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Bretton Woods Institutions

The Bretton Woods Institutions—consisting of the International Monetary Fund (IMF) and the World Bank (the Bank)—were created in 1944 to help promote the economic health of the world economy. The Bretton Woods Conference, officially called the United Nations Monetary and Financial Conference, was held in Bretton Woods, New Hampshire, at the Mount Washington Hotel on July 1–22, 1944, as World War II was coming to a close.

Delegations from 45 governments agreed on a framework for economic cooperation designed to avoid a repetition of the disastrous economic policies that contributed to the Great Depression of the 1930s. During the 1930s, as economic activity in the major industrial countries weakened, these countries attempted to support their own economies by increasing restrictions on imports. Unfortunately, increased restrictions led to a downward spiral in world trade, limited economic output, increased unemployment, and worsening living standards in many countries.

At the close of World War II, various plans to restore order to international monetary and financial relations led to the creation of the Bretton Woods Conference and the Bretton Woods Institutions. The British economist John Maynard Keynes and the U.S. Treasury international economist Harry Dexter White were the intellectual founding fathers of the Bretton Woods Institutions. Keynes and White shared a belief that powerful, multilateral institutions could prevent future depressions while helping build a strong, global economy. John Maynard Keynes, the father of Keynesian economics, in particular, actively advocated for a strong government role in developing interventionist policies to mitigate economic recessions, depressions, and booms. As the father of macroeconomic theory, Keynes argued for an interventionist role of governments in alleviating unemployment, stirring investment, and increasing savings rates by focusing on aggregate consumption and investment.

Initially, the IMF and the Bank were designed to help rebuild Europe after the war. The IMF was charged with promoting global economic growth through international trade and financial stability, with stable currency exchange rates initially tied to gold reserves. The Bank made its first loan of $250 million to France in 1947 for postwar reconstruction. Over the intervening decades, with the increased international integration of markets, the IMF and the Bank have increased their responsibilities to coordinate, assess, and promote international cooperation for continued monetary stability. Expanding memberships and a strategic focus on poverty and debt reduction have led to new initiatives by the Bretton Woods Institutions.

Headquartered in Washington, D.C., the IMF and the Bank are governed by their member countries. As specialized agencies of the United Nations, the IMF and the Bank are related but have different purposes.

The IMF promotes balanced expansion of world trade, stability of exchange rates, avoidance of competitive currency devaluations, and orderly correction of balance of payment issues. Balance of payment issues occur when a country starts running short of money and credit by buying more goods and services abroad than it can sell or as a result of investors taking their capital abroad. The IMF provides temporary financing to ease the balance of payments crisis provided the country agrees to implement policies addressing the cause of the problem and ensuring that the IMF is repaid. Member countries provide money (called quota subscriptions) to the IMF. The IMF then lends to members in financial difficulties. Quotas, based predominantly on the country's economic size, determine the voting power and the amount of funds a country can borrow. A 24-member executive board provides oversight to the managing director, his or her deputies, and an international staff that carries out the IMF's work. The finance minister and other high officials of all member countries comprise the board of governors, the overall authority for the IMF.

The Bank focuses on promoting long-term economic development and poverty reduction. By financing specific projects, the Bank assists countries by focusing on longer-term development issues. Owned by 184 member countries, the Bank has become a Group composed of five closely related institutions: the International Bank for Reconstruction and Development (IBRD), the International Development Association (IDA), the International Finance Corporation (IFC), the Multilateral Investment Guarantee Agency (MIGA), and the International Centre for Settlement of Investment Disputes (ICSID). The Bank Group focuses on poverty reduction and improvement of living standards around the world. The IBRD focuses on middle-income and creditworthy poor countries, while the IDA focuses on the poorest countries of the world. Low-interest loans, interest-free credit, and grants are provided for education, infrastructure, communications and other initiatives. The Bank Group works to help countries' governments take the lead in preparing and implementing development strategies to reduce poverty in their own countries. The Bank's Comprehensive Development Framework, adopted in 1999, guides its assistance by focusing on four key components: (1) comprehensive and long-term vision is emphasized, (2) strategies are "owned" by the country with local stakeholders shaping them, (3) countries lead the management and coordination of aid programs, and (4) performance is evaluated through measurable results.

While the IMF might be called in an emergency for a financial crisis brought on by balance of payment issues, for example, the Bank is the world's largest source of development assistance and is heavily involved in reducing poverty in low-income countries. Every year, nearly 40,000 contracts ranging in size from a few thousand dollars to multimillion-dollar contracts are decided for delivering goods and services around the world. The Bank also provides an extensive array of advice and facilitates private sector investments in developing countries to promote growth and opportunity.

In recent years, the Bretton Woods Institutions have been subjected to severe and significant criticisms on their globalization policies, with allegations that the IMF and the Bank promote poverty and inequality. Following the disrupted talks of the World Trade Organization in Seattle in 1999, protesters have annually demonstrated at the combined IMF and World Bank boards of governors meetings. In 2000 at Prague, Czech Republic, the board of governors was forced to cut short its annual meeting after protests, lobbying, and workshops denouncing globalization. In 2001, 20,000 protestors convened for an often raucous demonstration in Washington, D.C., preventing the boards from meeting.

—Jennifer J. Griffin

See also Developing World; Development Economics; Globalization; International Monetary Fund (IMF); Poverty; World Bank; World Economic Forum; World Trade Organization (WTO)

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BUDDHIST ETHICS

Buddhist philosophy originates with the teachings of the Buddha (566–486 BCE), which are framed by the goal of eliminating suffering. Buddhist ethics aims at providing the path to achieving this goal. The teachings of the Buddha were preserved as an oral tradition for 400 years until they were compiled by monks in the Pali canon around the first century BCE. (There are many schools of Buddhist thought, but they share the same core teachings.) No separate discourse for Buddhist ethics exists in the ancient sources. Rather, a sophisticated and profound ethical theory is found throughout the canon and is inseparable from the rest of the philosophy. Works devoted explicitly to Buddhist ethics are recent, blending material from various sources into a more well-defined moral theory.

The Foundation of the Theory

Buddhist ethics is grounded in a theory of the nature of reality. It is logically embedded in Buddhist causality and the concomitant notion of nonsubstantiality. The presumption is that everything has a cause, that something cannot arise out of nothing, and that all phenomena thus fall under causal law. It follows that everything depends on something, indeed everything, else. This is known as the principle of dependent origination, and it lies at the heart of Buddhist philosophy.

On a physical level, every object obviously depends on a variety of causes and conditions. For instance, a table is made of wood, which comes from trees, and trees depend on water, earth, and sunlight. The table comes into existence because of the carpenter, who also depends on food, air, water, and so on. No element in nature can be conceived of as not connected to myriad others. We can also understand this principle conceptually. That is, this is a table by virtue of our definition of it; at other times, the wood may be firewood, a chair, or a bat. No element or object possesses an intrinsic, independent identity.

The principle of interdependence naturally leads to the conclusion that there is no separate self or soul either. In addition, if everything is subject to causation, then everything is also constantly changing and is impermanent. According to Buddhist philosophy, a person is a combination of five fluctuating aggregates (body, sensation, perception, dispositions, and consciousness). We cannot claim that any of these constitutes an intransigent self.

The concept of dependency entails significant moral implications. From our dependency and interconnectedness with others follows a sense of obligation and concern about the well-being of others. Since we are ultimately dependent on every aspect of the universe, ethical consequences follow regarding social philosophy, attitudes toward animals, and environmental ethics. Thus, understanding interdependence brings with it respect for nature and all living things.

Further moral implications ensue from the view of "no self." Without a permanent, fixed self-identity, one is not invested in one's own ego. Selflessness and other-directed actions follow. That is, without being preoccupied with oneself, a selfless concern for the well-being of others becomes possible. Egoism is replaced by the idea that distinction between self and others is an illusion.

The most important manifestation of the Buddhist view of causality is the law of karma, which is a natural law. *Karma* literally means *actions*. The principle that every effect has a cause means that actions have consequences for oneself and others. Karmic effects can be twofold, external and internal. One's actions affect others and accordingly accumulate merit or demerit. Immoral actions, such as killing, stealing, and lying, result in bad karma; good deeds result in good karma. Accepting a belief in reincarnation, people are reborn according to the moral ledger of their actions. The family one is born into, one's professional life, one's character, and even one's physical appearance may manifest past karma. The second aspect of karma is psychological, the way in which karma affects the agent. Here, karma is a psychological law, the law of causation applied to mental events. Immoral actions have negative effects because they are embedded in states such as anger, resentment, and violence. Negative thoughts and emotions lead to anxiety, even depression; they cause internal turmoil, and they are in themselves forms of suffering. By harming others one harms oneself. Positive thoughts and emotions lead to calm and satisfaction. Belief in reincarnation is not necessary for appreciating the psychological aspect of karma.

Karma is also a moral law. Unlike the system of rewards and punishments in monotheistic religions, in Buddhism, without a god, responsibility for one's destiny lies within oneself. By understanding how character and events come about, we learn to redirect the course of our lives, as the Buddha outlined in presenting his Four Noble Truths.

The Four Noble Truths

The core of Buddhist teachings is expressed in the Buddha's Four Noble Truths, his first sermon. The Four Noble Truths sketch a moral path. The assumption is that all beings wish to avoid suffering and attain happiness. Buddhist ethics begins with the desire to end suffering, and Buddhist concepts of right and wrong follow. The Four Noble Truths provide an analysis of what causes suffering on the one hand and what brings peace and happiness on the other.

The first Noble Truth is the truth of suffering. The point is to identify the nature of suffering as a problem in order to eliminate it. The principle is that suffering pervades human existence. Buddhism identifies a broad spectrum of phenomena as suffering, and areas causing psychological and moral problems are broader than what we find in Western moral theories. Birth, sickness, old age, death, as well as pain, grief, and sorrow are all forms of suffering, but even pleasurable experiences can cause suffering because of their transient nature. A new car, a new promotion, or a new relationship are only new for a short while. If our well-being depends on these highlights, we are subject to constant ups and downs. Not getting what one wants is suffering. Here, the Buddha is referring to the idea that whenever there is a gap between what we have and what we want or who we are and who we want to be, we will suffer. Expectations embedded in ignorance of the principle of dependent origination lead to suffering. Assuming a fixed, permanent self makes one a slave to the demands of the ego; one's social status and material possessions become central, and we try to satisfy aspects of an existence that cannot be satisfied because it does not exist per se.

The second Noble Truth identifies the origin of suffering. Desire and attachment cause suffering. Craving and attachment refer not only to pleasure and to material goods but also to ideals, theories, and beliefs. Desires are viewed as insatiable, and thus in principle they cannot be satisfied. All forms of suffering, from personal problems to political struggles such as poverty and war, can be viewed as rooted in selfish cravings and desires and in attachment to material goods, ideologies, or religions.

The three roots of evil are greed, hatred, and delusion. Here, the principle of causality and karma applies not only to action but also to intentions, thoughts, and feelings. Negative thoughts give rise to offensive speech and violent actions, just as sympathetic and compassionate thoughts give rise to kind words and actions. Thus, thoughts and feelings have karmic effects as well. Wishing someone ill is not morally neutral. In this sense, Buddhist philosophy offers a deeper analysis of morality by including human psychology as a cause of our behavior. This link between psychology and ethics is a central feature of Buddhism. The second Noble Truth shows that what causes psychological suffering also causes immorality. As the goal is to eliminate suffering, one must consider one's state of mind.

The third Noble Truth concerns the cessation of suffering and the possibility of attaining nirvana. Nirvana is mostly described in negative terms as it is impossible to convey this transcendent state rationally. Several Buddhist scholars refer to nirvana as a moral state because it includes the cessation of the causes of immorality—that is, greed, hatred, delusion, desire, and attachment. Negative emotions or mental states are eradicated as well. The goal is to eliminate the cycle of birth and death, although, as mentioned previously, this point is not essential to the moral theory.

The Fourth Noble truth is the truth of the Eight-Fold Path. The Eight-Fold Path lies at the core of Buddhist practice. It embodies the main principles of Buddhism and represents the middle way prescribed by the Buddha between asceticism and self-indulgence. The path entails three aspects: wisdom, morality, and meditation. Wisdom pertains to understanding the true nature of reality, that suffering is grounded in ignorance. Moral conduct is a way to purify one's actions, which also purifies one's motives. Meditation creates awareness and mental discipline. This path also embodies one of the main principles in Buddhist philosophy—nonviolence.

The Eight-Fold Path entails the following: (1) right view—that suffering originates in ignorance, hence understanding the true nature of reality is necessary for liberation; (2) right resolve—after understanding the causes of suffering, one needs to intend to change them; (3) right speech—one's words should be used only constructively, not destructively; one's speech should be honest and nonviolent; (4) right action—one should act in nondestructive, nonviolent ways; (5) right livelihood—one's livelihood should not involve harm to others, sentient beings, or the environment; (6) right effort—one should recognize that this path is not easy and requires work; one needs to replace negative emotions by positive ones, selfish motivations by selfless ones, unwholesome mental states by wholesome ones; (7) right mindfulness—this creates self-awareness, essential for combating aggression and negative motivations; and (8) right concentration—meditation and stillness allow deeper insights. The Eight-Fold Path underscores how ethics is essential to eliminate suffering.

Virtue Ethics

In philosophy, virtue ethics concerns one's character. Beyond analyzing the causes of immorality, Buddhist ethics proffers positive reasons to behave ethically and to resist unethical tendencies. There are four cardinal virtues: loving kindness, compassion, sympathetic joy, and equanimity. These are incompatible with their opposites and serve as antidotes to their negative counterparts. Loving kindness, the aspiration for another's well-being, is incompatible with hatred for others. Compassion, the hope that others be free from suffering, is incompatible with cruelty. Sympathetic joy, the ability to truly rejoice in another's success, is incompatible with envy. Equanimity, being serene and of an even mind, helps dissolve desire and aversion. Cultivating these virtues, then, is an important part of Buddhist morality. Practicing virtues leads to thinking about others, identifying with others, and experiencing selflessness. Considering the positive effects of these virtues, we can see that by helping others one also helps oneself.

Ethical Precepts

Buddhist ethics also includes a normative component, and there are several sets of precepts governing action. Five basic precepts pertain to the lay person: no killing, no stealing, no lying, no sexual misconduct, and no intoxication. Additional sets of 8 and 10 precepts guide lay persons in deepening their practice. There are over 200 precepts for monastic life.

Classification of Buddhist Ethics

Buddhist ethics is an ethics of enlightenment and compassion. As a nonauthoritarian philosophy, clinging to scriptures or theory is viewed negatively. Truth can only be attained by one's own authority. Tolerance follows this antifundamentalist approach, with wisdom and compassion inseparably linked. In contrast, in Aristotle, for instance, morality is a means to an end, to happiness. The Buddhist concept of nirvana as a moral state indicates that morality is not merely a means to enlightenment but an end in itself as a feature of enlightenment.

Buddhist Economics

Economic teachings are scattered throughout the Buddhist scriptures. "Right livelihood" is one of the requirements of the Eight-Fold Path. In applying the principles of nonviolence and not harming others, right livelihood means that one should refrain from making one's living through any profession bringing harm to people, sentient beings, or the environment. Therefore, the Buddha denounced professions that trade in weapons, drugs, or poisons; violate human beings; or kill animals. It follows that Buddhist economics cannot be a discipline separate from other aspects of life, notably from Buddhist ethics. Economics becomes a subset of morality and a normative social science, with moral considerations providing the framework for economic thought. From this perspective, and given the principle of interdependence, economic decisions cannot be made without taking into consideration individuals, society, and the environment. One cannot consider costs alone. If economic decisions are made solely on the basis of profit and loss, they become the source of social and environmental problems rather than positive solutions.

Given the goal in Buddhist philosophy of liberation, well-being cannot be defined by consumption or the accumulation of goods. Nevertheless, Buddhism is by no means adverse to wealth. On the contrary, wealth prevents poverty, about which the Buddha claims that hunger is the greatest illness. The concept of the middle way rejects the extremes of poverty or seeking riches for their own sake. Moderation, simplicity, nonviolence, and nonexploitation are the watchwords for economic activity, and the accumulation of wealth must also be carried out without violating any of the five precepts against killing, stealing, lying, sexual misconduct, and taking intoxicants. Being born into wealth is considered the result of good karma, and wealth provides an opportunity to practice generosity. Sharing wealth supports individual well-being and the community.

The goal of liberation implies that wealth is only a means to an end. If greed, craving, and attachment cause suffering and if one's attitude toward wealth includes these dispositions, wealth will bring suffering rather than enjoyment or solutions to the problem of suffering. In addition, economic activity motivated by greed will yield different results than when motivated by the desire for well-being. Greed leads to overconsumption and needless accumulation of goods, whereas the desire for well-being leads to moderation, balance, and sustainability. Distinctions between right and wrong consumption and use follow, given these attitudes toward wealth and its pursuit.

Buddhist philosophy consistently addresses the motivation behind human activity, and in the end the causes of suffering, unethical behavior, and immoral economic activity are the same. Thus, ethics and economics are integrated through causal analysis and consequently provide guidelines that aim at both individual and social transformation.

Business Ethics

Although Buddhist philosophy was forged during an agricultural era and before the rise of modern capitalism, the main tenets of Buddhist theory are applicable to business ethics today. From a Buddhist perspective, practical questions pose themselves for people engaged in business and commercial activities. Given the principle of right livelihood and that certain trades are denounced altogether, the first question one has to ask is what is being produced? For example, from a Buddhist point of view, there is no way to morally justify a multibillion-dollar weapons industry (enabling war, massacres, genocide, and other atrocities). The second question that arises is how is the product being produced? Does it involve harm to people, sentient beings, or the environment? Then, given the principle of interdependence, because businesses are integral parts of the community, decision making cannot be reduced to profits without considering the impact on people and the environment. Moreover, given that materialism is not the ultimate goal in Buddhism but only a means to an end, profits cannot be considered in isolation; they ought to be subservient to the moral path rather than dominate and compromise it. Finally, the goal in Buddhism is to eliminate suffering, so allowing businesses to profit while exploiting people and polluting the environment increases the amount of suffering and is counterproductive to the overall goal.

—Karin Brown

See also Confucius; Deep Ecology; Ethics of Care; Feminist Ethics; Jainist Ethics; Taoist Ethics; Triple Bottom Line

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Bureau of Land Management

The Bureau of Land Management (BLM), part of the U.S. Department of the Interior, administers more federal land than any other federal agency: over 264 million acres of land (about one eighth of all land in the United States). Also, it manages 700 million additional acres of subsurface mineral resources and has responsibility for wildfire management and suppression on 388 million acres. The bulk of these lands are located in the western United States and include a variety of terrain, such as rangelands, forests, high mountains, arctic tundra, and deserts. Within these public lands, commercial, cultural, recreational, and wilderness resources abound; the responsibility for management and multiple uses of these resources puts the BLM in challenging public-private debates.

The mission of the BLM is to sustain the health, diversity, and productivity of public lands for the use and enjoyment of present and future generations. BLM functions include preparing land-use plans and assessing environmental impacts; issuing leases and other use authorizations; identifying and protecting significant natural, cultural, and recreational resources; managing and suppressing wildfires; and monitoring resource conditions.

The roots of the BLM can be traced back to the early years of the United States, with the Land Ordinance of 1785 and the Northwest Ordinance of 1787. By the late 19th century, a shift in federal land management priorities was marked by creation of the first national parks, forests, and wildlife refuges. Public lands were valued for more than simple commodity extraction and population settlement. By 1934, a U.S. Grazing Service was established to manage the public rangelands. In 1946, this Grazing Service merged with the General Land Office to form the modern BLM within the Department of the Interior.

In 1976, Congress enacted a unified legislative mandate for the BLM, with passage of the Federal Land Policy and Management Act of 1976. Congress confirmed the value of public lands and charged the BLM to practice "multiple-use" management: These lands and their various resource values should be used in a combination best meeting the present and future needs of the American people. Balanced use of public lands is increasingly a challenge, since most of the public lands are in the Western states, which experience intense population growth. Traditional land uses of grazing, mining, and timber production continue to be in high demand. The BLM increasingly is the target of lawsuits initiated by both citizen and commercial organizations.

The American public wants access for recreational and cultural activities. Oil and gas interests, along with ranching and timber interests, lobby for access to harvest resources from these public lands. These commercial and recreational activities must be balanced in an environmentally responsible manner. Further, the BLM must not only balance these varied interests but must also ensure future enjoyment of public lands by future Americans.

—LeeAnne G. Kryder

See also Natural Resources; Resource Allocation

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Bureau of National Affairs

The Bureau of National Affairs (BNA) is a leading print and electronic publisher of more than 200 books, journals, and newsletters providing news, analysis, and commentary regarding legal, economic, and regulatory matters. BNA is especially known for its publications on federal and state regulatory activities, corporate law, labor and employment law, tax law, banking, bankruptcy, health care law, and business finance. Due to its long history of reliable publishing of authoritative material in these areas, it is regarded as an original source for researchers, government, and businesses.

Founded in Washington, D.C., in 1929, where it is still based, BNA was incorporated as a wholly employee-owned company in 1946. It reports that it is the oldest organization in the United States to be wholly employee owned. It received the *Business Ethics Magazine* Employee Ownership Award in 2000, which noted that BNA had continued to maintain employee ownership despite recent offers to purchase the company. All employees can own stock, and no employee owns more than 3% of the stock of BNA. Employees and retirees represent 10 of the 15 positions on the board of directors, with the other 5 positions filled from outside the company. There are no special stock options for senior management. It has also been previously honored by *Fortune Magazine* as one of America's 100 Best Companies to Work For, which recognized BNA for its family-friendly policies.

The American Bar Association has partnered with BNA to produce various legal reference books and jointly publishes with BNA the *Lawyers' Manual on Professional Conduct*. The Society for Human Resource Management has also partnered with BNA to survey trends in human resources.

BNA has acquired other media enterprises and provides a variety of services today, which include document delivery, regulatory monitoring, and custom research for its clients. BNA has become heavily involved in electronic delivery of its services and publications, and select material is available through LexisNexis.

—David D. Schein

See also American Bar Association; Employee Stock Ownership Plans (ESOPs)

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Bureau of Reclamation

Established in 1902, under Teddy Roosevelt, the Bureau of Reclamation is part of the Department of the Interior. Its presence in the four regions made up of the 17 Western states concerns water resources. Dubbed "Reclamation" because of its initial purpose to provide irrigation in order to "reclaim" unusably arid land for human benefit, Reclamation is best-known for dam and canal projects, including the Hoover and Grand Coulee dams. More recently, however, Reclamation is known for its construction and maintenance of hydroelectric power plants. Emphasis at Reclamation has shifted from that of construction to maintenance of those facilities and environmental water concerns.

Although it is a federally funded agency, Reclamation's projects were in part supposed to be financed by those who benefited from them. Repayment to Reclamation prior to the 1960s often fell short due to terms favorable to consumers and unfavorable to the agency. Since the 1960s, new Reclamation contracts have been written so as to be less one-sided.

The 1980s saw a further shift at Reclamation. Due to changes in the running of the federal government, Reclamation changed from a construction agency to a maintenance one. Now well established as a natural resource management agency, Reclamation's mission is to deal with water and water-related resources in ways that are both environmentally and economically beneficial to American interests.

Reclamation's effect on business has been profound since its beginning. Through its irrigation and power plant projects in the West, Reclamation has made vast areas of arid land economically viable. In addition, Reclamation has had an effect on the use and management of water resources to control water hoarding and infringement on water rights.

Reclamation must balance national interests with state and tribal water rights and environmental concerns. As the population in the West grows, these concerns about water, power, and their appropriate use also grow. Reclamation faces new water-related challenges due to changes in the economy, population, and industry in the area.

Reclamation also has an international presence through its research and scientific and economic studies concerning water. Reclamation's economic impact in farming; ranching; residential, commercial, and industrial power and water; and the development of new economic units is enormous. This development includes water conservancy districts, also known as irrigation districts, for which many Reclamation projects have been undertaken.

Some might ask what business a federal agency has in this arena. To answer that, we can think of Reclamation as similar to those agencies that construct highways, railroads, and other infrastructure that contributes to the overall economic growth of the nation, as it has contributed to the Western expansion of previous centuries.

The Bureau of Reclamation serves the public good in its management of water resources in the West as well as its construction and maintenance programs concerning electric power. Charged with reclaiming the usefulness of the arid West, Reclamation is important to the vital needs of both citizens and business in the areas of its operation.

Still, though, Reclamation is not without its critics. Significant criticisms come from environmentalists who are concerned about the reliance on water levels to which the Western states have become accustomed. Some water resources that Reclamation has exploited for development are nonrenewable at the current rates of use, such as the reclaiming of groundwater. This casts a questionable light on many Reclamation projects in that it seems that via Reclamation some economic and development enterprises in the West rely on water that will not be there in the long run to support the projects. So while the initial purpose of Reclamation was to make the West usable, it may have done its job too well—making the West more usable than the water resources can really sustain.

—Ellen M. Maccarone

See also Bureau of Land Management; Environmental Ethics; Environmentalism; Environmental Protection Agency (EPA); Environmental Protection Legislation and Regulation

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Bushido

Bushido is an ethical system based on the relationship between a samurai warrior and his overlord. The essential feature of this ethic is the relationship between master and vassal, with allegiance owed to the master by the samurai and care owed to the vassal warrior by the master. The master-vassal association, the core of *Bushido*, is reflected in the Japanese model of corporate management—that is, the spirit of devotion by employees for the sake of the company culture while the company (the master) shows the employees mercy and sympathy in ways such as lifetime employment, the seniority-centered employment system, and the "*ringi* system" of decision making. The latter is based on the rule of consensus, which encourages employee teamwork and unity in spirit. Furthermore, it leads employees to share fundamental values of "mutual trust and mutual responsibility" as if the company were a feudal domain. It should be noted, however, that Japanese corporate management and governance are evolving, embracing both *Bushido* and Anglo-American models of corporate management and governance.

The term *Bushi*, or samurai, can be traced back to the middle of the Heian period (782–1191). However, there was no such term *Bushido.* The ethics of the samurai in the Japanese medieval world (1192–1603) and the word *Bushido* (*Bu* = military, *shi* = knight, *do* = ways) were coined during the early times of the Tokugawa Shogunate (1603–1867). And the moral path that the *Bushi*, the warriors, were required to observe has been passed on for more than 800 years.

There are three key components of the master-vassal relationship, or the Japanese samurai's system of vassalage, usually called *Shuju Kankei*, that are important to understand what *Bushido* is:

1. From the perspective of followers in the master-vassal relationship, the master is required to possess three qualities: (1) "master with high fighting skills," (2) master with "benevolence or mercy," and (3) master with "sympathy or pity" having the tenderness of a warrior. Only when these three qualities are fulfilled will followers be convinced that they share the same destiny with their master and convince themselves to commit their lives to the master. This interpretation is what Hikozaemon Ohkubo writes in his *Mikawa Story*.

2. Tetsuro Watsuji called the samurai master-vassal relationship "absolute subordination" and "the ethic of devotion." For the core of the ethic of devotion, Watsuji says that the very fundamental spirit of the samurai is to overcome self-love. The master ignores his self-interest for the sake of his vassals, and for such masters, their followers serve them with absolute readiness to risk their own lives—that is, selfless devotion. Submission to authority, the sacrifice of all private interest, and risking life in battle for the master are essential. Watsuji argues that the ethic of devotion is the central value and denies the interpretation of a mutual benefit relationship such that *go'on* (debts) to the lord must be repaid by *ho-ko* (service).

3. Sokichi Tsuda contends that the central essence of the master-vassal relationship is based on mutual benefit. Master and follower are united by the exchange of interest, the foundation of their relationship. When the essence of this mutual benefit is damaged or lost, it ends the relationship.

As observed above, *Bushido* is not a fixed idea, and there are various teachings and interpretations related to it. As for the ethical underpinnings of *Bushido,* the teachings of Confucius provided the most significant foundation, while Buddhism furnished a sense of calm trust in fate, and the tenets of Shintoism thoroughly imbued *Bushido* with loyalty to the sovereign.

Historically, *Bushido*'s precepts are represented by *Shido, Hagakure*, and *Meiji Bushido*:

1. *Shido*, the way of the samurai, is based on the well-known "Yamaga Gorui" written by Soko Yamaga (1622–1685), who emphasizes the samurai's legitimate social role in governance through moral leadership. The personality of a great man was the single most important component of his notion of the perfect samurai, and it implied, above all, courageous and self-enhancing conduct in the pursuit of moral ideals. *Shido* is united with neo-Confucianism, which emphasizes five moral relations between master and servant, between father and son, between husband and wife, between older and younger brothers, and between friends. The important elements that support the five moral relationships are benevolence, justice, politeness, wisdom, and sincerity.

2. *Hagakure* means hidden leaves. Bravery, loyalty, filial duty, and benevolence are the fundamental values of *Hagakure.* The precepts, as set forth by Tsuramoto Tashiro, are based on what Tsunetomo Yamamoto (1659–1719) told about his ideal of the samurai. Although *Hagakure* was dedicated to Mitsushige Nabeshima, the lord of Saga Han (the Domain), it is the most famous and aggressive evocation of *Bushido,* a manifesto of protest against the majority of samurai who accepted their destiny of domestication.

Tsunetomo Yamamoto rejects the exchange aspect of vassalage—the pattern of *go'on* (debt) and *hoko* (service). Instead, he emphasizes absolute devotion on the part of the followers without any expectation of an appropriate reward from the master. In *Hagakure,* the way of the samurai is found in death. When it comes to either/or, there is only one choice, and that is death. One should be determined and advance in the face of opposition.

Only through learning how to die honorably could a man attain the mind-set of a true samurai, in peacetime as well as during war. Avoiding *haji* (shame) was a central moral precept in *Hagakure*; it was a matter of inner dignity. Readiness to die meant courage in fighting, *chu*, absolute loyalty to the lord, and *ko*, the virtue of filial piety to one's parents. *Hagakure* proposed to rescue the moral autonomy of the samurai while simultaneously protecting the absolute authority of the lord. Absolute loyalty to the lord was redefined as the moral choice of the samurai vassal, who entered on the difficult path of devotional service through "secret love" without expecting any reward.

3. *Meiji Bushido* includes especially the *Bushido* written by Nitobe and published in 1899 in America. The greatest contribution Nitobe made was the idealization of the traditional *Bushido*, the ethical system, and this view has been widely disseminated among the people. The central points of Nitobe's *Bushido* are the following. Rectitude or justice is a twin brother to valor, another martial virtue. Courage, the spirit of daring and bearing, is doing what is right. The spiritual aspect of valor is evidenced by composure—calm presence of mind. Benevolence, love, magnanimity, affection for others, sympathy, and pity are also recognized to be supreme virtues. Benevolence is a tender virtue and motherlike. Politeness (propriety) springs as it does from motives of benevolence and modesty and is actuated by tender feelings toward the

sensibilities of others. It is a graceful expression of sympathy. Without veracity and sincerity, politeness is a farce and a show. Confucius teaches that sincerity is the beginning and the end of all things; without sincerity, there would be nothing. The sense of honor, implying a vivid consciousness of personal dignity and worth, characterizes the samurai, born and bred to value the duties and privileges of their profession. "You will be laughed at" and "Are you not ashamed?" are the last appeals to correct behavior on the part of a delinquent youth. Finally, the duty of loyalty is central to *Bushido* feudal morality. It shares other virtues in common with other systems of ethics, with other classes of people, but this virtue—homage fealty to a superior—is its distinctive feature.

It was the ideal to embrace "the morality of the East" (*Bushido*) and "the art of the West" (science and technology) that Shozan Sakuma (1811–1864) and many other leaders in the last days of the Tokugawa Shogunate held up for the future of Japan. Eiichi Shibusawa (1840–1931), a great contributor to modern Japanese capitalism in the late 19th and early 20th centuries, believed that harmony between profit and righteousness is an immortal principle common to the Orient as well as to the Occident. He writes in his well-known book *Rongo to Soroban* (*The Analects and the Abacus*), "*Bushido* sunawachi Jitsugyodo nari" (the ethics of the samurai is same as "the ethics of business"). The term *Sikon Shosai* (embracing the samurai spirit and business acumen) was coined during the Meiji era (1868–1912). The central values of the *Bushido* spirit, such as "contribution," "devotion," "gratitude," "untiring efforts for improvement," and "team work united in spirit," are inherited in the corporate philosophy as well as the corporate culture of Japanese companies.

—Akira Saito

See also Benevolence and Beneficence; Buddhist Ethics; Business Ethics; Confucianism; Confucius; Decision-Making Models; Employee Relations; Ethical Culture and Climate; Fidelity; Honesty; Human Capital; Integrity; *Keiretsu*; Loyalty; Moral Education; Moral Leadership; Shame; Taoist Ethics; Trust; Virtue; *Zaibatsu*

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Business, Purpose of

The word *business* derives from the Middle English terms for *busy* and *ness*, and its primary meaning is to engage in purposeful activity. Thus, the notion of the purpose of business is in one sense redundant since in its generic meaning, business means having a purposeful activity. However, there is a secondary meaning of the word *business*, which denotes activities that involve the production and exchange of goods for economic purposes, primary among which is the generation of profit. Consequently, business is often defined as economic activity engaged in for the sake of profit. For that reason, business engaged in for the profit motive is distinguished from other "busy" activities, such as those carried on by nonprofit enterprises such as schools, hospitals, government bodies, and nongovernmental organizations. So those businesses generating profit are a species of organizations unto themselves and are concerned with generating enough profit to continue to exist in a competitive marketplace. Because of this specific difference from other organizations engaged in productive activities, it appears that the profit-making feature is the specific differentiating factor, and consequently, it is thought that the generation of profit is the primary purpose of business. However, despite this account, the question remains as to whether this is the correct way to characterize the purpose of business activity. There are alternative accounts of the purpose of business that can be articulated.

The Importance of the Question of Purpose

There are two reasons why determining the purpose of any organization or institution is important. The first is that the purpose of anything determines whether the activities of an entity are appropriate. Given the ethical maxim "Good is to be done and harm avoided" and given the fact that the purpose determines what counts as good, the purpose of any entity will determine when activities within that institution or entity are appropriate. In other words, the purpose of an entity furnishes us with the criteria of evaluation. For example, a knife has an end or a purpose. What makes a knife a good knife is how well it "fulfills its purpose"—that is, cuts. Analogously, a business is designed for some purpose, and what makes it a good business is determined by whether and how well it fulfills that purpose. If the main purpose is to maximize profits, then a business with a good bottom line that maximizes profits is a good business. But some businesses that maximize profit can act in an unethical fashion. This means that if there is a purpose over and above the maximization of profit, or shareholder wealth, we would need to determine what this purpose is in order to determine whether the pursuit of profit needs to be overridden by ethical considerations.

The second reason that determining the purpose of an object or entity is important is that the purpose furnishes criteria for determining whether the object or entity is well designed. Again, using the knife analogy, a knife is designed well if on account of the design, it is able to perform its function most effectively. Through experimentation, people have realized that a knife cuts well if it is designed with a strong handle and a sharp blade. In the case of business, if the purpose is to make a profit, the organization will be well designed if it fulfills that purpose and maximizes profit. It is evident how this purpose will greatly influence many diverse aspects of the organization, including perhaps the manner in which employees are treated and the allocation of resources. Further, the purpose of the business also determines and prioritizes the responsibilities of the people who are charged with managing the business. If the purpose of business is to make a profit, then the "excellencies" of the managers will be those qualities that enable them to improve the bottom line. However, if there are other purposes of business besides profit making and wealth creation, they need to be determined in order to be able to ethically evaluate business activities.

The Societal Roots of Business

While it is true that what distinguishes business from other activities is that it is activity that is motivated by the hope for a profit, and that profit-making activity designates the specific property or necessary condition of business, that specific property of profit generation is not sufficient to encompass the entire notion of the purpose of business, particularly if one looks at the place of business in society, in a capitalist society.

Human beings are social animals, which means that they exist and thrive in and depend on society for their existence. They develop conventions, institutions, systems, and/or forms of life to fulfill the purposes of their social communities. Business is one of those institutions. Consequently, it is important to look at what purpose business fulfills in a modern capitalist society.

Anthropologists and economists point out that for time immemorial, human beings have produced goods as well as developed means to exchange and barter surplus goods. Since this tendency to produce and exchange runs through the entire period of human history, markets are a standard feature of society. These instincts are evidenced time and again, whether it is a couple of kids on the playground with a few baseball cards or hundreds of men and women on the floor of the New York Stock Exchange or at the local shopping mall. Before there was any formalized government, law, or even state, people who had a proficiency in producing one of the necessities of life were trading with someone else who had a proficiency in the making of another needed item. This informal market and the informal division of labor it produced benefited society, and therefore, society permitted and encouraged entrepreneurial activity since it worked out for the betterment of all the members of a community.

In the early stages of human history, before the invention of money, instead of trying to accumulate a profit, people accumulated goods that were not perishable. The introduction of money allowed not only the accumulation of nonperishable goods but also the possibility for capital to be invested. With the introduction of capital, the notion of how much property it was appropriate for people to own changed. Rather than the prevailing rule of justice that superabundant goods were owed to those in need, the prevailing belief changed so that it was thought that it was permissible to save and invest superabundant monetary goods. If goods were not perishable and could be accumulated without loss, it was possible to set up capital markets, and these two developments altered the beliefs concerning how much property people were entitled to own and affected the conception of distributive justice.

Political economists such as Adam Smith pointed out that since most people only rarely produce for the sake of others and mostly produce out of their own self-interest, production could be enhanced and society would benefit if markets were set up in such a way as to incentivize this self-interest. The incentive became known as profit. The self-interested pursuit of profit would lead to the whole society being better off. Smith's recognition of human behavior was codified in the well-known doctrine of the invisible hand. However, there was a constraint on this pursuit of self-interest. It was permitted as long as it did not violate the rules of justice.

Society has developed since the origin of the human community and cooperation, but the nature of human motivation remains the same. People want to promote their best interest and consequently are motivated to act in ways that will make them better off than they were before the action was performed. People trade goods and services because they believe that they will be better off trading than not, and the fact that human trade continues on a massive scale demonstrates that human beings today are in that respect the same as their original forbearers. There are no significant differences between the original traders and contemporary traders, only modest ones. The introduction of money, of course, obviated the need to have a good or a service to participate in an exchange—that is, barter. I only have to bring a wallet to the food market, and I can leave my pigs at home. The second difference is that people produce goods and services in collectives, rather than as individuals, and these collectives can vary in size from just a few people to hundreds of thousands of people working together to provide a good or a service (or a series of goods and services). In addition, there is a greatly increased variety of goods and services for sale on account of human ingenuity. Nevertheless, despite the changes, the basic motive to barter, truck, and trade remains, and this is on account of the fact that it improves the lives of the people who participate in the great exchange.

Nevertheless, it is important to note that society's permitting the appeal to self-interest and profit, and consequently providing great incentives for productivity, does not thereby abrogate the societal purpose of business. Self-interest is an individual motivator. But business is a societal institution, and as a societal institution, it has a social purpose.

Beneficial Goods and Services

The societal view of business's purpose must ask how any business activity is beneficial to society. Throughout history, it seemed clear that while production and trade are good, unbridled and unfettered exchange is not good for society. Communities, and the governments that represent them, have always insisted on the right to regulate trade for the maintenance and promotion of the good of society. At times, this has meant that certain goods were declared illegal, then legal, and then illegal again, depending on consensus of the populace. Other goods have been regulated in certain places and unregulated in others. With some products, regulation is accepted readily and even sought after, and with other products, regulation is fiercely debated. But, whatever its applications, regulation has remained the unchallenged prerogative of governments, as representatives of the people, to prevent the activity of exchange and the institution of business from harming the society it has done so much to help.

Consequently, the very existence of pervasive regulation clearly entails that the purpose of business from a societal point of view must be something to the effect that business exists in the way that it does so that it can increase production and facilitate exchange in a way that makes people better off—that is, in a way that promotes the common good, the general welfare, or the public interest. Therefore, business practices that do not fulfill this purpose are irresponsible.

Maximizing Profit and Creating Shareholder Wealth

However, as was noted, there are those who maintain that the societal notion of the purpose of business as the creation of goods and services to promote the general welfare is naive and simplistic. This view maintains that the primary purpose of business is to create wealth or generate maximum profits. The maximization of profit and the notion of shareholder value and shareholder wealth are structurally similar, if not identical, since they hold that the primary purpose of business is to serve the interest of the individual owner of a business rather than the interest of society.

This view is developed by Max Weber, who defines capitalism as a system where there is pressure for ever-increasing profits, and continued by those who see capitalism as an economic system of free markets, such as Milton Friedman, who believes that the system works best when each person, *homo economicus* (economic man), pursues his or her own interest. In such a system, the primary and only responsibility of a corporation is to maximize profits for those self-interested individuals who have invested their capital in the system, subject to laws and fundamental ethical customs. Since this view must define a primary responsibility as a function to be performed in the face of desired ends, it implicitly recognizes the purpose of business as maximizing profits. Other proponents of this theory change the description of the end and outcome from maximizing profit to increasing shareholder wealth or shareholder value, but structurally, increasing wealth and value are the same as the goal of maximum profit.

The evidence for this view rests on the fact that most investors enter into the market with the intention of increasing their wealth rather than with the intention of directing or controlling the behavior of firms so that they act in accordance with the goals of society in enhancing production and exchange. Hence, in this view, profit maximization or wealth generation or shareholder value generation must be the goals of management. In this view, managers who deviate from acting in accordance with the interests of the shareholders—that is, providing them with maximum return on investment—are failing in their fiduciary duties by misappropriating what does not belong to them.

This point is further supported by the court findings in the well-known case of *Dodge v. Ford Motor Company*, argued at the beginning of the 20th century. In that case, presented before the Supreme Court of Michigan, Justice Ostrander, writing the majority opinion, claimed that the benefits of lower-priced automobiles for customers could not take priority over the interests of the shareholders. It had been Henry Ford's plan, which was not formalized, even though it was publicly known, to continually decrease the price of his automobiles while increasing the quality of the cars. So Ford determined that he would neither issue dividends to his shareholders that accurately reflected Ford's record profits nor lower the price of the automobiles that year. Rather, he would hold onto the profits of that year to raise enough capital to better expand and improve Ford's production faculties in order to produce a higher-quality product for consumers at a lower price. The shareholders argued that Ford was no longer running a business but instead was running a quasi-charitable institution. The justices agreed and ordered Ford to pay the higher dividends. In his opinion, Justice Ostrander stated that it was one thing to engage in charitable activities for the benefit of one's employees, such as constructing an employee medical center for their use, but it is another thing entirely to fundamentally change the ends and purposes of business, which he identified as increasing shareholder value. To do otherwise is to disregard what is legitimately owed to the shareholders.

Proponents of this view also claim that since the firm is the property of the shareholders, the managers are the agents of the investors and are therefore required by a fiduciary duty to act in a manner that promotes their interests. A fiduciary relationship is defined as one in which one person, a principal, justifiably has confidence in another, an agent, whose help or advice is sought in some manner. The agent is obliged to act with loyalty in advancing the client or principals' interest. Doctors are fiduciaries of their patients, and lawyers are fiduciaries of their clients. Similarly, managers are agents of the shareholders and should act with loyalty in advancing the interests of the shareholders for two reasons: first, a shareholder is not involved with—that is, does not control—the day-to-day operations of the business, and second, the shareholder lacks information about those day-to-day operations of the business.

Concerning the first reason, in the same way that patients cannot refer themselves to a specialist for a treatment that they may very much need, individual shareholders (for the most part) cannot enforce their will in terms of their own ideas and proposals on the organization. Concerning the second reason, which is lack of information about the status of the organization, even if this information were provided to them, the shareholders would still be unsure if the information they have received is complete and how to understand the information they have been presented. Finally, in the same way as the doctor and the lawyer can cause great harm to the patient or the client, whether through deliberate actions or through inattention, the manager can cause financial harm to the owner either through deliberate action or inattention. Therefore, it is on account of the fact that property owners could have their property harmed through the actions of others (whether deliberate or not) that they are owed a fiduciary obligation by the managers who are in their employ. It is this fiduciary obligation that requires that the purpose of the business is to be run for their financial benefit. Since agents are to act on behalf of a principal, in this case the owners, they need to determine what the point of their activity is, and if it is defined as profit making, the managers and directors have an obligation to pursue that profit, as much as possible, for the shareholders, unless the shareholders say otherwise.

Responses to the Profit-Maximizing Account

There are two problems with the belief that profit maximization or increasing shareholder value or wealth is the primary purpose of business. This view does not take into account the great variety of businesses, many of which have no shareholders, where there is no separation of ownership and control. Furthermore, it fails to take into account the differences between small businesses and large corporations. A small business can be run by its owner, and the owner can be in the business because one likes what one does or likes independence and merely wants enough profit so that one can live modestly from the profits of the business.

Such a business is privately owned and managed by the owner. As a business, it is still interested in profit, but it is not under pressure for ever-increasing profits, which Weber characterized as the spirit of capitalism. Rather, the small entrepreneur can be interested not in the maximization of shareholder wealth, since there are no shareholders, or in the maximization of profit, since one doesn't always need maximum income, but only in making enough money to live comfortably. Such owners are in business and producing goods and services that society needs and increasing their assets and profit, but they are not pressured to maximize profit. The fact that the defenders of profit maximization and shareholder wealth do not often reflect on privately owned and/or small businesses indicates that there is an entire area of business that they have not considered or that they are using profits as a measurable tool for monitoring agency behavior. But monitors for agent behavior are not purposes but measurable outcomes.

The second problem with the alternative account is that it confuses or conflates two quite different things, motives for actions (subjective causes) with purposes for the action (objective justificatory reasons). If one distinguishes between motives (which explain) and purposes (which justify) one is logically impelled to reject the view that the primary purpose of business is the pursuit of profit.

There are two different answers to the question "Why?" when addressed to human actions: the justificatory and the explanatory. To cite a purpose for doing something is to attempt to justify it and give it a legitimating reason. To cite a motive for doing something is to give it a psychological explanation. Hence, the question "Why did you make the bread?" can be answered by the justifying purpose, "To alleviate hunger," or by the psychological motive explanation, "Because I can sell it and buy things I want and need."

Confusing motives with purposes is similar to confusing the engine of a train with the destination of a train. The goal or purpose of the train may be to get to London, but it is the engine that gets it there. While the engine may be necessary to help us get to London, it is not the goal. The purpose of being a brewer is to make beer, while the motive for making the beer might be that it enables the brewer to make a good living. After the initial love of beer making wears off, it is not from altruism that a brewer makes beer but from his own self-interest. Nevertheless, the outcome of the profit-making venture is the manufacture of beer.

Thus, those who argue that profit maximization is the primary purpose of business have put the cart before the horse. They would have to argue, for example, that the purpose of baking is to make money and the secondary purpose is to provide food for the hungry.

Furthermore, this way of viewing the situation, which turns the self-interested motive for an action into the purpose of an action, opens a Pandora's box because it legitimizes or justifies the unfettered pursuit of self interest. If self-interest is the purpose and the purpose determines what activities are acceptable, the self-interested "rational maximizer" needs to do whatever is necessary to gain profit. But such unfettered self-interest is greed. It begets and legitimates the greedy, grasping, acquisitive, profit-motivated, bottom-line-oriented entrepreneur who feels no responsibility to the public welfare and for whom business ethics is indeed an oxymoron.

Recent Perspectives on the Social Purpose of Business

It should be noted that business as a social institution, convention, or form of life is different from a natural entity that has its own *telos* or purpose. As an institution or convention, it is created by society for societal purposes. It would be contradictory for society to create an institution that has the seeds of its own destruction. Hence, in creating and allowing business to exist, society must have in mind the general welfare. The fact that governments create laws that incentivize and appeal to self-interest does not make self-interested motives the purpose.

The granting to the corporation the status of a person, to protect the individual from liability, generated the needed capital investment and as a law must be justified by an appeal to the public interest. Laws developed to be of benefit to individuals at the expense of the public interest are unjust laws. Thus, a legal perspective must look at the purpose of business as not being for the benefit of any specific individual but to encourage individual enterprise for the sake of society's well-being. Any incentives, such as the introduction of corporate laws protecting individual investors, have always been to incentivize the individual for the sake of society. The principle is that because business—that is, the production and exchange of goods—is good for society, government ought to develop ways to incentivize productive market behavior. The profit motive and government-created incentives to make a profit are beneficial because they spur businesses on to generate and exchange more and more goods, which benefits the public interest.

This kind of thinking becomes more manifest in more recent court findings that more and more clearly articulate the public purpose of business. It begins with the case of *AP Smith Manufacturing Company v. Barlow et al.*, which was filed in 1953, in which the court provided something like legal permission to perform actions that primarily promote the public good, as long as there is a demonstrable secondary benefit to the shareholders.

AP Smith Manufacturing Company was incorporated in 1896 and produces equipment for the water and gas industries. The company is located in New Jersey and had around 300 employees, and furthermore, the company had a history of donating funds to local educational institutions. The subject of the case was a $1,500 donation to Princeton University, which was approved by the board of directors and authorized by the president of the company. The shareholders of AJ Smith disputed this allocation of corporate funds as disadvantageous to their interests and filed suit. The president of the company argued that the donation was a good investment for the business for the following reasons: (1) donating money to educational institutional promotes goodwill among members of the community, who have an expectation that their local corporations will act in socially responsible ways, and (2) contributing to educational institutions will help secure an able and efficient workforce in the future. In addition, the chairman of Standard Oil, writing as a friend of the court, also argued that corporations are expected to acknowledge their responsibilities to support the system of free enterprise (and since free enterprise depends on educated workers, supporting free enterprise means supporting educational institutions). Furthermore, the chairman argued that it is not good business to disappoint a societal expectation, and finally, he contended that businesses, as a whole, should not take from the community without giving back.

The court agreed with the arguments of the plaintiff and, in the majority opinion, offered the following thoughts. When wealth was primarily in the hands of individuals, they discharged their responsibilities by donating their wealth for charitable purposes. However, on account of the fact that wealth has been largely transferred to the corporation and that individuals now suffer under an increasing tax burden, individuals are no longer able to support charitable causes in the same manner as they used to, which is troubling since the need is even greater now than it was before. Therefore, individuals have turned to corporations to assume the modern obligations of good citizenship in the same way that humans do. Moreover, corporate contributions in the area of education are really an investment in the business since corporations will be an important beneficiary of a well-run and well-funded educational system.

In contrast to the *Dodge v. Ford Motor Co.* case, legal opinions that offer a defense of activities more beneficial to society while taking the shareholder into account become an important milestone for advocates of the doctrines of stakeholder theory and corporate social responsibility. Generally, those doctrines would hold that businesses have responsibilities above and beyond those to the shareholders. Businesses are entities that act like citizens in a community and have a range of duties to all those who have a stake in the business.

—Ronald F. Duska and Julie Anne Ragatz

See also Business for Social Responsibility (BSR); Capitalism; Collective Choice; Collective Punishment and Responsibility; Corporate Accountability; Corporate Citizenship; Corporate Moral Agency; Corporate Philanthropy; Corporate Rights and Personhood; Corporate Social Responsibility (CSR) and Corporate Social Performance (CSP); Friedman, Milton; Social Contract Theory

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Business Ethics

Although defining business ethics has been somewhat problematic, several definitions have been proposed. For example, Richard De George defines the field broadly as the interaction of ethics and business, and although its aim is theoretical, the product has practical application. Manuel Velasquez defines the business ethics field as a specialized study of moral right and wrong. Unfortunately, a great deal of confusion appears to remain within both the academic and the business communities, as other related business and society frameworks, such as corporate social responsibility, stakeholder management, sustainability, and corporate citizenship, are often used interchangeably with or attempt to incorporate business ethics. Relative to other business and society frameworks, however, business ethics appears to place the greatest emphasis on the ethical responsibilities of business and its individual agents, as opposed to other firm responsibilities (e.g., economic, legal, environmental, or philanthropic).

A Brief History of Business Ethics

The subject of business ethics has been around since the very first business transaction. For example, the Code of Hammurabi, created nearly 4,000 years ago, records that Mesopotamian rulers attempted to create honest prices. In the fourth century BCE, Aristotle discussed the vices and virtues of tradesmen and merchants. The Old Testament and the Jewish Talmud discuss the proper way to conduct business, including topics such as fraud, theft, proper weights and measures, competition and free entry, misleading advertising, just prices, and environmental issues. The New Testament and the Koran also discuss business ethics as it relates to poverty and wealth. Throughout the history of commerce, these codes have had an impact on business dealings. The U.K. South Sea Bubble of the early 1700s, labeled as the world's first great financial scandal, involved the collapse of the South

Sea Company. During the 19th century, the creation of monopolies and the use of slavery were important business ethics issues, which continue to be debated until today.

In recent times, business ethics has moved through several stages of development. Prior to the 1960s, business was typically considered to be an amoral activity; concepts such as ethics and social responsibility were rarely explicitly mentioned. During the 1960s, a number of social issues in business began to emerge, including civil rights, the environment, safety in the workplace, and consumer issues. During the late 1970s, the field of business ethics began to take hold in academia, with several U.S. schools beginning to offer a course in business ethics by 1980. From 1980 to 1985, the business ethics field continued to consolidate, with the emergence of journals, textbooks, research centers, and conferences. From 1985 to 1995, business ethics became integrated into large corporations, with the development of corporate codes of ethics, ethics training, ethics hotlines, and ethics officers. From 1995 to 2000, issues related to international business activity came to the forefront, including issues of bribery and corruption of government officials, the use of child labor by overseas suppliers, and the question of whether to operate in countries where human rights violations were taking place. From approximately 2000 until today, business ethics discussion has mainly been focused on major corporate scandals such as Enron, WorldCom, and Tyco, leading to a new phase of government regulation (e.g., the Sarbanes-Oxley Act of 2002) and enforcement.

This current "scandal" phase of the business ethics field has tremendously enhanced its popular use. For example, a search in Google using the term *business ethics* (as of November 2005) generates over 88 million hits. Hollywood continues to portray important business ethics issues or dilemmas in movies such as *Wall Street, Quiz Show, Boiler Room, Erin Brockovich, The Insider*, and *Jerry Maguire* and even in children's films such as *Monsters, Inc.*

Moral Standards and Business Ethics

Although the field of business ethics covers a broad range of topics, the core of the field is based in moral philosophy and its use of moral standards (i.e., values, principles, and theories) to engage in ethical assessments of business activity. A literature review indicates that five moral standards have been applied in the field of business ethics to a greater extent and with greater consistency than others. Two moral theories are particularly dominant in the business ethics literature: utilitarianism and deontology. Utilitarianism, often expressed as a teleological or consequentialist framework, is primarily based on the writings of Jeremy Bentham and John Stuart Mill. Deontology (i.e., duty-based obligations) is often expressed in terms of "Kantianism" (or more specifically as the principle of the categorical imperative), being primarily based on the writings of Immanuel Kant. In addition to utilitarianism and deontology, two other moral theories (typically considered deontological in nature) have been used extensively in the business ethics field: moral rights and justice (e.g., procedural and distributive). The fifth moral theory receiving attention appears to be moral virtue, being primarily based on the writings of Aristotle. The predominant use by business ethicists of these moral theories points toward their importance in the field. Other important moral standards that are also used (although to a somewhat lesser extent) in the field of business ethics include moral relativism, ethical egoism, and religious doctrine.

There have been several means by which moral standards have been applied in business ethics. Some of the more apparent ways are (1) individual ethical decision making; (2) organizational ethical decision making (e.g., policies and practices); (3) the moral evaluation of business systems (e.g., capitalism) and the marketplace (e.g., competition); (4) the relationship between business and society (e.g., corporate social responsibility); and (5) specific issues in business (e.g., affirmative action and discrimination, conflicts of interest, privacy, whistle-blowing, executive compensation, consumer protection or marketing, and international business). In conjunction with the above are the uses made of moral standards with respect to both teaching and research in business ethics.

Business Ethics as an Academic Field

Richard De George might be considered the first to attempt to distinguish business ethics as a separate field of study. De George suggests that business ethics is a field to the extent that it deals with a set of interrelated questions to be untangled and addressed within an overarching framework. He argues that the framework is not supplied by any ethical theory (e.g., Kantian, utilitarian, or theological) but by the systematic interdependence of the questions, which can be approached from various philosophical, theological, or other points of view.

Despite business ethics being a relatively recent distinct field of study, several typologies have emerged. There appear to be five general approaches: (1) a normative and descriptive approach, (2) a functional approach, (3) an issues approach, (4) a stakeholder approach, and (5) a mixed approach. For example, in terms of the normative/descriptive approach, academic business ethics research is often divided into normative (i.e., prescriptive) and empirical (i.e., explanatory, descriptive, or predictive) methodologies. A functional approach attempts to divide the subject of business ethics into separate functional areas such as accounting, finance, marketing, or strategy. Others attempt to categorize business ethics by using an "issues" approach—in other words, by discussing issues such as the morality of corporations, employer-employee relationships, or other contemporary business issues. Another approach attempts to discuss the subject of business ethics from a stakeholder perspective (i.e., in relation to which stakeholder is most directly affected). For example, business ethics issues might be framed based on the following stakeholders: owners, employees, consumers, suppliers, competitors, the government, the natural environment, and the community. Finally, a mixed approach draws on aspects of several of the approaches (e.g., normative/descriptive, issues, and stakeholder) and appears to be the most popular approach used by business ethics academics. For example, quite often business ethics textbooks will commence with a normative discussion of moral theory and business systems. The discussion will then turn to a more mixed normative/descriptive discussion of the specific issues. In addition, many of the issues are tied to stakeholders, typically involving employees and customers.

In terms of business ethics research, in a review of the first 1,500 articles published in the *Journal of Business Ethics* from 1981 until 1999, Denis Collins found the presence of the following major business ethics research topics: (1) prevalence of ethical behavior, (2) ethical sensitivities, (3) ethics codes and programs, (4) corporate social performance and policies, (5) human resource practices and policies, and (6) professions—accounting, marketing/sales, and finance/strategy.

Major Early Contributors to Business Ethics

Several important early contributors to the field of business ethics, mainly through their initial textbook publications, include Norman Bowie, Richard De George, Manuel Velasquez, Thomas Donaldson, W. Michael Hoffman, Patricia Werhane, John Boatright, and many others too numerous to mention. John Fleming conducted a study in 1987 to determine among other things the most referenced authors, books, and articles in business ethics. The top five referenced authors were (1) Milton Friedman, (2) Christopher Stone, (3) Thomas Donaldson, (4) Peter French, and (5) Alasdair MacIntyre. The top three referenced books were (1) Christopher Stone, *Where the Law Ends*; (2) Thomas Donaldson, *Corporations and Morality*; and (3) John Rawls, *A Theory of Justice.* The top three referenced articles were (1) Brenner and Molander, "Is the Ethics of Business Changing?"; (2) Peter French, "The Corporation as a Moral Person"; and (3) Milton Friedman, "The Social Responsibility of Business Is to Increase Its Profits."

Business Ethics Today

Based on early efforts, the field of business ethics continues to flourish in both academia as well as the business community. For example, a search (as of November 2005) using the database ABI/Inform for the term *business ethics* found in scholarly journal articles generates over 11,000 hits. Several important academic journals now exist, including *Journal of Business Ethics, Business Ethics Quarterly, Business & Society, Business Ethics: A European Review,* and *Business & Professional Ethics Journal*, among others. Business ethics conferences are held annually, including those conducted by the Society for Business Ethics and the European Business Ethics Network. Every 4 years, the International Society of Business, Economics and Ethics organizes a World Congress on Business Ethics, often portrayed as the "Olympics of Business Ethics." Research centers such as Bentley College's Center for Business Ethics, Wharton's Zicklin Center for Business Ethics Research, or the Ethics Resource Center based in Washington, D.C., continue to support research efforts in the field of business ethics. Surveys suggest that approximately two thirds of the top U.S. business schools now teach business ethics as either a mandatory or an elective stand-alone course. In the corporate world, the growth of ethics officers as well as the Ethics & Compliance Officer Association, ethics programs (e.g., codes of ethics, ethics hotlines or helplines), ethics audits and reports, ethical investment, and even corporate business ethics awards highlight the growing practical importance of the field. Consulting efforts in the business ethics field appear to have grown significantly as well due to the various corporate scandals and the desire of firms to avoid them in the future.

Yet despite the growth of business ethics and the apparent acceptance of its importance among many, several issues are being debated. For example, can business ethics be taught? What factors actually influence ethical behavior? What should a firm's ethical obligations (i.e., beyond the law) consist of? Does ethical behavior actually improve the firm's financial performance? Is a firm capable of being held morally responsible, or only the firm's agents? How can business ethics best be integrated into a firm's corporate culture? These issues, as well as many others, remain to be examined and debated by those active in the business ethics field.

—Mark S. Schwartz

See also Business Ethics Research Centers; Business Ethics Scholarship; Descriptive Ethics; Dilemmas, Ethical; Ethical Decision Making; Ethics, Theories of; Ethics & Compliance Officer Association (ECOA); Justice, Distributive; Normative Ethics; Professional Ethics; Rights, Theories of; Situation Ethics; Teaching Business Ethics; Utilitarianism

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Business Ethics and Health Care

The health care industry faces several aspects of ethical considerations in the business aspects of their practice. The challenges facing the industry are first outlined, followed by some ethical frameworks and guidelines that might be helpful in resolving these issues. A practical checklist of questions that health care providers should try to address as they face various ethical dilemmas in the business aspects of their profession is finally outlined.

Challenges in the Health Care Industry

The following are some of the major challenges facing the health care industry today.

Clinical Health Care Ethics

These are issues that deal with the practice of clinical medicine that physicians and their patients encounter as they work together to diagnose and receive treatment, respectively, for the disease. For example, who has the right to keep or stop the life-supporting devices? Does a badly wounded patient have the right to refuse medical care? Should euthanasia be considered legal? Who is eligible for an organ transplant, and how should the decision be made? Should the health care system encourage assisted reproduction or abortions?

Scientific Bioethics

This relates to the ethical questions associated with medical progress. For example, should humans be used as experimental research subjects? Should genetic and neuroscience research be allowed to progress? Are cloning and stem cell research ethical? Should the use of randomized trials—that is, studies in which the patient is randomly assigned to either the experimental or the control group—raise ethical problems?

Cultural Ethics

Does the fact that there are different cultural norms for ethical behavior imply that all ethical norms are relative to the cultures in which they are found and are valid only in that time and place? Does it assume that there are no universal ethical norms that transcend the borders of culture, tradition, and history? This happens more acutely when persons from one cultural tradition encounter the health care of another culture. For example, how do people of a particular country view the authority of physicians? How do people of specific religious denominations feel about abortion or about life support technology? Should a doctor inform a patient that he or she has cancer, even if it is inappropriate according to the patient's culture? How should a gynecologist from a Western country react to genital mutilations of young African patients, especially when their mothers vigorously defend the practice as holy and good for women?

Religious Freedom Versus Patients' Rights

Health workers and patients have clashed when service providers have refused to give care that they feel violates their beliefs, resulting in an intense and complex debate over religious freedom versus patients' rights. On the one hand, those who believe in a "right of conscience" for health workers argue that there is nothing more dutiful and courageous than protecting individuals from being forced to violate their moral and religious values, while patient advocates and others point to a long tradition in medicine of having an ethical and professional responsibility of putting patients first.

Should an ambulance driver refuse to transport a patient for an abortion because of his or her beliefs? Should fertility specialists rebuff a gay woman seeking artificial insemination? Should a pharmacist turn away a rape victim seeking the morning-after pill? Should anesthesiologists refuse to assist in sterilization procedures? Should gynecologists be allowed to decline prescription of birth control pills? Should doctors be allowed to reject requests for Viagra from unmarried men?

After the historic 1973 *Roe v. Wade* decision, many states passed laws protecting doctors and nurses who do not want to perform abortions. Oregon's monumental 1994 legalization of physician-assisted suicide, however, allowed doctors and nurses an opportunity to decline to participate.

Marketing Practices in the Health Care Industry

The ethical aspects of the marketing practices of the health care industry are best studied under the rubric of the four Ps—that is, product, price, promotion, and place. Each of these Ps raises its own characteristic set of ethical questions as discussed below.

Product

The word *product* raises questions about product safety, availability, and efficacy. Are medical products and services available in the market truly effective? Is it ethical to sell products to patients under false pretenses if they are likely to be better off without it? Should pharmaceutical companies focus more of their research development efforts on "life-enhancing" drugs versus "life-saving" drugs?

Promotion

The health care industry has used extensive promotional tools, such as advertising, personal selling, and publicity and public relations to market their products to medical professionals as well as consumers at large. In many cases, marketers and advertisers work side by side with major researchers in positioning new drugs as potential bestsellers. One such technique is to employ ghostwriters to write articles for medical journals that tout the benefits of the new products. They also recruit other doctors with expensive fees, whose opinions are valued, to speak to peers about the drugs' benefits.

Drug companies are prohibited from promoting their products before the approval of the Federal Drug Administration or from promoting them for unapproved uses. Critics also contend that advertisers are also influencing the clinical drug trials, while the latter disagree and note that they are tightly regulated.

Price

Over 12% of the gross national product of the United States is spent on health care, and there is a lot of debate on how health care costs can be contained and made affordable for the common citizen. Other issues include the appropriateness of bundling of medical services through physical-hospital organizations and the appropriate pricing of life-saving drugs for diseases such as AIDS in the poorer regions of the world.

Placement

Placement issues refer to the "distribution channel" aspect of marketing: the possible avenues through which customers gain access to the product or service. The following are some salient issues. Is rationing of health care ethically defensible? Who makes rationing decisions? How should access to health care be structured based on whether it is offered through private insurance or government programs?

The Ethical Frameworks

According to a report by the *Woodstock Theological Center,* health care professionals have three different but interrelated sets of responsibilities. The first and foremost responsibility of physicians, nurses, hospital executives, therapists, health educators, and other health care professionals is to attend to the health needs of the individuals in the communities they serve. This includes taking appropriate and reasonable measures to prevent serious illness or injury in the healthy, curing and alleviating the suffering of the sick, and comforting the dying. The next level of responsibilities is to administer and use wisely the physical, technological, financial, and human resources available to health care professionals in meeting the needs of the communities they serve. The final set of responsibilities is for continued enhanced research, education, and scientific advancement so that the quality of care available for patients and the efficiency and efficacy with which those resources are used can be improved gradually.

Health care professionals typically have to face all the above responsibilities in various shapes and forms. The following section presents the benchmarks for ethical decision making by health care professionals as they undertake these responsibilities.

Compassion and Respect for Patients

Health care professionals must be committed, first and foremost, to the welfare of their patients. Respect for human dignity forms the basis for compassion, honesty, integrity, and confidentiality. It is unethical for individual health care providers to exploit the vulnerability of the patient and benefit monetarily. Institutional health care providers have a primary responsibility to serve the patient and to ensure adequate facilities, equipment, supplies, support staff, and services, while executives and trustees are responsible for fostering institutional cultures that focus on patient care.

Commitment to Professional Competence

Health care providers have an obligation to keep up with the latest developments in their field and the benchmarks for "best practice" in their respective fields. Inadequately trained, misinformed, or inexperienced physicians and practitioners can not only cause harm to the patients but also drive up costs by misdiagnosis, administrating inappropriate treatments, or ordering unnecessary tests. "Competence" by executives and trustees also involves creating a climate that rewards delivery of quality care and encourages cost-saving innovations and an efficient, yet flexible and realistically designed, system.

Commitment to Spirit of Service

Given the exorbitant costs of medical care and the vast number of people who are unable to afford it, health care providers should be mindful of the high standards required by the social covenant and exercise their community responsibilities by providing uncompensated or reduced fee service to needy patients and by implementing public policies that allow poor and uninsured people to receive adequate care. The "not-for-profit" institutions should particularly be cognizant of these obligations to serve the community, given the tax benefits received by them.

Honesty

Health care professionals also have an ethical obligation to be honest and truthful about a patient's condition, appropriate treatments, and related costs and provide this information to the patient or an appropriate guardian. They are also obliged to keep accurate and truthful medical records and also to provide truthful and accurate information to third-party payers. The executives of hospitals and managed care organizations are also obligated to foster a culture that avoids deceitful practices. Finally, intellectual honesty enhances professional competence. Professionals should acknowledge their doubts, be open to new ideas, and seek second and third opinions from colleagues when they are unsure of a diagnosis or a proposed path of treatment.

Confidentiality

Health care professionals have an obligation not to divulge intimate details of a patient's illness or condition without the individual's permission, except as required by law. The only exceptions are in extreme cases when there is a threat of serious harm to the patient or to other individuals at risk by exposure to the patient. Third-party payers, such as insurance companies, should only be provided information that is legally required. Newer patients should be provided a thorough explanation of what information is recorded, how it is used, who has access to that information, and what the rules may mean to the patient.

Good Stewardship and Careful Administration

Even though the primary responsibility of the health care industry is to take the best care of the patient, they must also be aware of their gatekeeper role in managing costs. Professionals should carefully balance the relative costs with the potential of benefits of alternative therapies for their patients, counsel the latter about these issues, and work with third-party payers to encourage treatments that are the most cost-effective. It is also imperative to maintain detailed and accurate records as well as assist public health authorities in gathering information on issues such as the effectiveness of new therapies and the spread of diseases. Executives are responsible for a wide range of administrative, financial accounting, providing useful information about services, costs, and patient outcomes to various stakeholders, such as physicians, patients, third-party payers, and government regulators.

Health care ethics is not just about patient-related decisions but about decisions made by executives and in boardrooms, as these people play their roles as various stakeholders, such as health care providers, employers, community service organizations, and citizens of the community. Health care industry professionals face the day-to-day challenges of making sound decisions on the basis of ethical guidelines and criteria based on the understanding that the health care organization is committed to patients' rights, the careful use of resources, just working conditions for the employees, and service to the community.

—Abhijit Roy

See also AIDS, Social and Ethical Implications for Business; American Medical Association (AMA); Americans with Disabilities Act of 1990 (ADA); Bioethics; Birth Control; Ethics of Care; Genetics and Ethics; Health Insurance Portability and Accountability Act; Health Maintenance Organizations (HMOs); Human Genome Project; Patients' Bill of Rights; Stem Cell Research; World Health Organization (WHO)

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Business Ethics Research Centers

Business ethics research centers are organizations dedicated to the study of what is good or right for individuals and groups of individuals engaged in business activity. Since business ethics is a form of applied ethics (a branch of philosophy), the work of these centers is concerned with taking theoretical ethical concepts and principles and applying them in the real world. More particularly, business ethics research centers investigate and analyze the application of such concepts and principles to business decision making and action and consider the ramifications across the entire range of business functions, including the management of legal compliance, risk, stakeholder relationships, and business reputation, to name just a few. This investigation and analysis usually has the aim of developing greater awareness and understanding of ethical issues in the business environment and promoting best practices to address them. Accordingly, business ethics centers are most effective when they bridge theoretical inquiry and practical application and guide organizations in the development of ethical business cultures.

Business ethics centers are generally not-for-profit organizations, and although most have been established within business schools and universities, some exist independently. Funding and support for institution-based centers are usually provided by the host institution or by corporate and individual donors, government grants, revenue-generating activities (such as executive education programs, conferences, and publishing), and sometimes by all these sources in combination. There are some institution-based centers that derive funding from consulting activities. Independent centers may generate funding from similar sources, with consulting revenues likely to contribute a proportionately greater share in many cases. Typically, centers are small with a full-time director, one or more research and consulting staff members or associates, and several full- and part-time support staff. In the university setting, it is common for faculty members to be affiliated with such centers. They are often charged with teaching business ethics within a broader discipline-based curriculum and, especially now in business schools, integrating the subject into students' general education.

History and Geographical Distribution

Significant active research in business ethics began in the mid-1970s as the field became more widely recognized as a legitimate subject for study and teaching. Demand for such research was driven by the heightened social and ethical consciousness that emerged in the wake of a decade of civil unrest, environmental concern, and consumer enfranchisement—and especially after a series of high-profile scandals such as Watergate and the aerospace industry bribes.

There are over 200 centers worldwide, more than 120 of which are in the United States alone. The majority have been established in an academic setting, but most centers are characterized by an outward focus and a desire to provide practical assistance to business communities around the world. The earliest business ethics centers were established in the United States in the 1970s, with Europe, Canada, and Australia following in the 1980s. Among the oldest business ethics centers are the Center for Business Ethics, founded in 1976 at Bentley College in Waltham, Massachusetts, and the Olsson Center for Applied Ethics, which became active around the same time in the Darden Graduate School of Business Administration, at the University of Virginia. Countries and regions that became significant for interest in business ethics in the 1990s, and that saw the creation of research centers, include Latin America, South Korea, Hong Kong, Japan, and South Africa.

The Work of Business Ethics Research Centers

The particular focus of individual centers varies widely but, in general terms, all are concerned to stimulate, support, conduct, and disseminate research related to business ethics and corporate social responsibility (see the next section). Very few centers now concern themselves solely with conducting or collecting research. Even when the majority of a center's time and resources are used in this way, it is likely that there will be subsidiary activities such as organizing occasional conferences or publishing reports. Most centers have multiple functions, often a combination of research with teaching and the preparation of teaching materials, organizing conferences and seminars, and the provision of speakers and scholars for media interviews. A growing number of centers offer advisory and networking services to corporations and other organizations. Some centers are repositories for books, journals, videos, and corporate ethics materials. Among centers that publish business ethics newsletters or magazines, the trend is toward online publications to enable more timely and cost-effective dissemination of ideas and information. The Ethics Resource Center in Washington, D.C., and the Institute of Global Ethics in Camden, Maine, have been notable trendsetters in this regard.

Centers differ in the degree of specialization within the field of business ethics, ranging from an interest in business generally to a specialist focus on particular industries or professions. Prominent centers in the former category include the Zicklin Center for Business Ethics Research at Wharton, University of Pennsylvania; the Center for Business Ethics at Bentley College; and the Institute of Business Ethics in London. At the other end of the spectrum is the Isbell Center for Hospitality Ethics at Northern Arizona University and the Silha Center for the Study of Media Ethics and Law at the University of Minnesota.

Widening Research Focus

Since the mid-1990s especially, the field of business ethics research (which, as noted below, has always been an interdisciplinary pursuit) has widened further to place greater emphasis on matters external to business organizations. While it remains important to study the design and implementation of internal corporate strategies, policies, and structures to ensure legal compliance and ethical conduct, corporations have become increasingly concerned with the obligations, relationships, and risks associated with outside stakeholders, including shareholders, customers, suppliers, strategic partners, communities, the media, and the environment. This wider definition of business ethics has led research centers to recognize and embrace a blurring of the boundaries with fields such as corporate social responsibility (CSR)—sometimes now called corporate responsibility—and corporate governance. This has happened in Europe and elsewhere to a greater extent than in the United States, where CSR is generally less advanced and tends to focus on philanthropic issues, as opposed to more strategic concerns such as sustainable development and the integration of economic, social, and environmental issues (the so-called triple bottom line).

Effect of Major Corporate Ethics Scandals

Numerous high-profile corporate scandals occurring between 2001 and 2004—especially in the United States—and the forceful regulatory response to them have done much to reinvigorate discussion and inquiry about ethical best practices in business. Inevitably, this has focused attention on existing business ethics research centers, as recognized experts in the field, and led to the establishment of new ones. The unprecedented magnitude and frequency of the corporate ethics scandals, involving corporations as large and ostensibly successful as Enron, WorldCom, Parmalat, and Tyco, is having at least two significant consequences for the field of business ethics and for the research centers that study it. First, while the short-term effect of the scandals (in the United States, at least) was the introduction of comprehensive, compliance-focused legislation such as the Sarbanes-Oxley Act of 2002—designed primarily to ensure greater accountability, responsibility, and transparency in the financial reporting of public corporations—there seems to be a longer-term consequence with possibly greater significance: an accelerated and widespread realization that a rules-based approach to business ethics is a necessary but insufficient requirement for ensuring ethical behavior in organizations. More than this, there needs to be an underlying commitment, embraced at the highest level of the organization, to operating in a manner that is consistent with clearly defined and appropriate organizational values, which will guide ethical decision making and positively influence the corporate culture.

The second significant development, arising largely out of the first, is the wider recognition of the critical influence of organizational culture in either promoting or discouraging ethical business conduct. A notable indication of these developments, and the fact that they are already shaping public policy and legislation, was the U.S. Sentencing Commission's amendment, in November 2004, of the Federal Sentencing Guidelines for Organizations to include the word *ethics* for the first time, as distinct from rules-based "compliance." Furthermore, the amended Guidelines emphasize the importance of organizational culture and the responsibility of senior management and the board of directors for positively influencing that culture.

Research centers have been advancing the understanding of values-driven management techniques for some time, and considerable research has been carried out on the importance of corporate culture. Centers are likely to redouble their efforts in these areas. Thus, although currently in the United States a compliance-led, legalistic approach continues to predominate, there are some obvious signs of a changing emphasis, and business ethics research centers are likely to be a driving force, as corporations look to the results of empirical research in shaping best practices.

Influence of Centers on Business Ethics Teaching

The frequency and magnitude of corporate scandals occurring since 2001 prompted questions to be asked (especially in the United States) about the adequacy and rigor of business education—specifically, whether business schools properly address the ethical dimension when educating tomorrow's managers and business leaders. This is a debate in which business ethics centers have participated energetically. The debate has focused not only on whether business schools have been including sufficient ethics-related material in their courses but also whether they are integrating business ethics throughout the curriculum. The Association to Advance Collegiate Schools of Business (AACSB) has promoted the teaching of business ethics in business schools since the 1980s; indeed, ethics education has been included in AACSB's accreditation standards since 1991. Although the standards issued by AACSB in 2003 do not contain specific ethics course requirements, there are concerns that many business schools are taking a minimalist approach, including just sufficient ethics content in their MBA programs to satisfy the AACSB mandate, with ethics courses disappearing slowly as programs have been redesigned. This situation is not peculiar to the United States, because a 2004 study in the United Kingdom concluded that business ethics occupied a more marginal position within the curriculum than previous studies had suggested. Furthermore, there is evidence in Australia that business ethics is still sidelined in business schools' curricula and is not yet a mainstream subject in business management programs.

Universities that host business ethics research centers are clearly at an advantage when it comes to establishing credentials in this critical area of business education. A number of centers located on university campuses have begun initiatives that aim to infuse discussion, teaching, and learning about business ethics throughout the curriculum and the campus community. Some, such as the Center for Business Ethics at Bentley College, have been successful in educating a broad range of faculty members on how to explore the ethical dimensions of business in their own classes, as opposed to bringing in specialist ethics professors. Other centers, such as the Center for Ethics and Business at Loyola Marymount University, have used strategies such as intercollegiate ethics case competitions to raise the profile of business ethics teaching.

Relationships With the Business Community

The renewed focus on business ethics in recent years has led many corporations to look for ways to demonstrate a visible commitment to promoting ethical business practices. One way in which some companies have tried to do this is by aligning themselves with business ethics centers and providing funding for them. Some centers have taken their sponsor's name, such as the Prudential Business Ethics Center at Rutgers University. In some cases support has taken the form of a philanthropic venture, such as the Merck Company Foundation's financial support for a number of business ethics centers, including the Ethics Resource Center (Washington, D.C.), the Gulf Center for Excellence in Ethics (Abu Dhabi, U.A.E.), and the Ethics Institute of South Africa (Pretoria). In other cases, corporate support has occurred through strategic alliances, as in the case of the LRN-RAND Center for Corporate Ethics, Law and Governance, founded in 2004 to study the ways in which businesses can best conduct operations ethically, legally, and profitably at the same time. Another notable development has been the establishment of the Business Roundtable Institute for Corporate Ethics at Darden Graduate School of Business Administration, University of Virginia. Here, an association of 160 chief executive officers of leading U.S. corporations has linked with a business school with the expressed intention of building and sustaining public confidence in the marketplace, in the wake of corporate misdeeds.

The funding of ethics centers by corporations, which—as previously noted—can involve naming them or their programs after the sponsor (or one of its executives), is considered problematic by some. To be sure, such partnerships can be enormously valuable to nonprofit centers with limited sources of funding and can enable resources, facilities, and programs to be expanded, generally making the centers more effective in their work. However, when a center takes a corporation's money or its name, it can present ethical issues that both partners need to address carefully. The questions that may need to be considered include the following. Are the values and missions of the two partners properly aligned, and is this really a good fit? What conditions, if any, are attached to the funding? What safeguards are in place to ensure that the center's research objectivity is not compromised? Are there actual, potential, or perceived conflicts of interest? If the corporate sponsor should subsequently attract bad publicity, what contingencies are in place to prevent or minimize damage to the center's reputation and credibility by association? In that event, could or should the center change its name or return the money received previously? Clearly, there are advantages to the business ethics movement both in improving ethics centers' access to funding (especially when they operate on a nonprofit basis) and in bringing about greater interaction with the private sector, since both increase the opportunities for advancing knowledge and learning and facilitating dialogue and the exchange of ideas. Nevertheless, there is a balance to be struck between these laudable objectives and the risks inherent in pursuing them in particular ways. Such risks (actual, anticipated, or perceived) need to be identified, quantified, and addressed.

Research Methodologies

A feature of business ethics research is that it draws on other disciplines and contributes to them, and therefore, business ethics research centers are, by necessity, interdisciplinary in their approach. Richard De George, a leading business ethics scholar, has observed that this field of study derives its descriptive component from the work of economists and those who study business and corporations from sociological, psychological, and other social scientific perspectives; it requires the theory of organization, management, and business activity provided by professors of business; and it requires the systematic development and application of moral norms and normative theory provided by philosophers and theologians. The field is essentially interdisciplinary because all the above disciplines (and more) are necessary for the study of business ethics, and each discipline is to some extent changed by its union with the others.

Research methodologies employed at centers differ widely, depending on the nature of the subject matter, the research objectives, and the resources available. Some centers conduct empirical research to investigate, evaluate, and explain companies' practices, using qualitative methods such as case studies and interviews, as well as quantitative analysis of large-sample survey data that might have been gathered with the assistance of a specialist survey firm. Research is also carried out using secondary sources, such as companies' annual reports and accounts and other corporate publications, public filings, media coverage and directories, as well as other academic research that has already been published. The work of some centers requires a greater degree of theoretical abstraction, grounded in the discipline of philosophy.

There is a trend toward cooperation in business ethics research, with the establishment of numerous alliances, especially between business and academia. This may help strengthen the base of the field, especially in parts of the world where business ethics is still a relatively new formal discipline.

The Future

In the early years of the 21st century, business ethics research centers have achieved greater prominence than previously, as the value of their work to society has been more fully recognized. There are encouraging signs that perceptions of ethics as "soft" and peripheral to the real challenges of business may be on the wane. There is certainly heightened awareness—in the business community, the marketplace, academia, government, and society generally—of the potentially savage economic and social consequences of unethical business conduct. This has shone new light on the need for greater understanding of ways to align our thinking and actions with appropriate values and promote business cultures in which ethical conduct will flourish. As business ethics research centers seek to drive this pursuit forward, they are likely to face at least three significant challenges: (1) in overcoming the still widespread misconception that ethics is a matter of legislation and enforcement, and what might be termed the "check-box" mentality that pervades many corporate efforts to ensure integrity; (2) in more fully exploring the relationship of business ethics to other disciplines and fields, so that business can more easily see the benefits and opportunities of an integrated approach to addressing its evolving responsibilities in contemporary society; and (3) in finding increasingly innovative and engaging ways to sample, analyze, and present data such that the relevance of ethics to business is understood by all and disputed by none.

—Mark Rowe and W. Michael Hoffman

See also Business Ethics; Business Roundtable; Corporate Governance; Corporate Social Responsibility (CSR) and Corporate Social Performance (CSP); Enron Corporation; Ethical Decision Making; Federal Sentencing Guidelines; Parmalat; Sarbanes-Oxley Act of 2002; Stakeholder Theory; Triple Bottom Line; Tyco International; WorldCom

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Business Ethics Scholarship

Business ethics scholarship is usefully divided into three distinct categories of research: conceptual, normative, and descriptive. Conceptual scholarship seeks to advance our understanding of certain mental concepts that inform our understanding of business. Normative scholarship seeks to clarify the purposes of business and the ethical constraints under which businesspeople should operate. Descriptive scholarship seeks to explain and predict business practices.

In the 1970s, philosophers working in normative ethics found that more specialized attention to the practice of business was necessary to assess the ethical status of specific business practices and provide guidance to ethical managers. This increase in specialization paralleled a similar increase in specialization by philosophers working on normative questions in bioethics and seeking to counsel physicians. Since that time, both business ethics and bioethics have become increasingly specialized as fields of applied ethics. Historically, normative business ethicists have approached the subject from distinct theoretical perspectives, such as Kantianism, libertarianism, and contractarianism. Descriptive business ethicists have approached the subject using lenses such as cognitive developmental psychology and institutional theory. In recent years, both normative and descriptive business ethicists have begun to specialize in specific areas of inquiry and research, such as ethics and financial services, marketing ethics, ethics in human resources, ethics in information technology, international business ethics, and business ethics and the natural environment.

Conceptual Scholarship

To properly understand and assess the practice of business and to prescribe specific constraints on businesspeople and business organizations, philosophers and social theorists have analyzed key concepts and defended particular understandings of those concepts. For example, there is an extensive literature on the ontological status of organizations that seeks to clarify our knowledge of concepts such as corporate intentionality, corporate personhood, corporate agency, corporate moral responsibility, moral imagination in business, and both negative and positive deviancy in business. It is only after such concepts are clarified that questions concerning the moral status of organizations can be understood. For example, if a corporation is properly understood as a moral agent, then it is possible to praise or blame corporations and not just the directors, executives, managers, and workers of a corporation at a particular time. Punishment of the corporation, and not just the corporate personnel, is thereby justified when corporate intentions are morally objectionable. Without such conceptual scholarship, such judgments would be difficult to render.

Another important area of conceptual scholarship concerns stakeholder theory. The notion of a stakeholder was initially developed by R. Edward Freeman in response to the stockholder conception of the corporation. The stockholder conception holds that a corporation is an organization whose function is to serve the interests of shareholders. In this view, the obligation of the manager is to increase value for shareholders. Freeman has argued for more than 20 years that the stockholder conception of the corporation fails to accurately capture the purposes of the modern corporation. He argues that all corporations have stakeholders, persons who are helped or harmed by corporate actions and whose rights are either respected or violated by corporate managers. Stakeholder theorists seek to identify and prioritize stakeholders and thereby clarify the purposes of the modern corporation.

These are just two examples of the sort of conceptual work undertaken by business ethics scholars. All concepts related to business ethics are open to conceptual analysis by business ethicists. Such conceptual analysis typically lays the groundwork for more sophisticated work in normative and descriptive business ethics.

Normative Scholarship

Normative business ethics scholarship is distinct from both conceptual scholarship and descriptive scholarship in that such scholarship argues for or against particular business practices and thereby attempts to establish *norms* for the ethical conduct of business. One theory that is commonly associated with business is utilitarianism. This theory, whose most famous proponent was the 19th-century philosopher John Stuart Mill (1806–1873), holds that when actions promote overall welfare, they are right and when they do not promote overall welfare, they are wrong. According to utilitarianism, then, if business activities maximize the overall welfare of society, then those activities are justified. However, utilitarianism has been criticized for being unable to account for basic moral concepts such as the dignity of individual persons and justice. This may explain why utilitarianism is typically not used by business ethicists to defend or justify business practices and why there are few active research streams in utilitarian business ethics.

There is a range of other normative ethical theories that business ethicists use to inform their work. It is not possible to canvass each of these theories, or perspectives, in the space of this entry. Instead, this discussion focuses on three of the most active areas of research within normative business ethics: libertarianism, integrative social contracts theory (ISCT), and Kantianism.

Libertarianism

Libertarian theorists of the corporation hold in common the view that it is the obligation of publicly held corporations to maximize profits for shareholders within the bounds of certain moral side-constraints. The most well-known defender of a libertarian conception of the corporation was Milton Friedman, whose stockholder theory of the corporation remains influential despite having been subjected to significant criticism. Prominent 20th-century libertarian theorists, such as Friedrich Hayek, Robert Nozick, and Friedman, defended a core set of libertarian doctrines. These included the ideas that individual persons, rather than the community, should be regarded as the basic unit of social analysis; that individuals should be free to decide what is best for themselves so long as they respect this same freedom in others; and that government intervention in market exchanges should be minimized in the interest of freedom and economic prosperity.

Libertarian theories of the corporation are grounded in these ideas and hold in common the view that it is the responsibility of publicly held corporations to return profits to shareholders within the bounds of certain moral side-constraints. Moral side-constraints are blocks or restrictions against actions, and they may be either weak or strong. A weak-side-constraints view will require relatively few restrictions on corporate actions, whereas a strong-side-constraints view will require significantly more restrictions. Proponents of weak side-constraints ground these constraints in the rules or norms presupposed by the activity itself. In this view, moral side-constraints are grounded in notions of fair play. For example, in *Capitalism and Freedom*, Friedman argued that the normative function of the corporation is to use its resources and engage in activities designed to increase its profits so long as it stays with the rules of the game—that is, engages in open and free competition, without deception or fraud. The rules are determined by the will of the majority of citizens in democracies. Actions that do not violate the rules of the game are permissible, whereas actions that violate those rules are not.

This view has been widely criticized on numerous grounds. For example, it has been argued that this view cannot justify the negative impact of externalities produced by business. It has also been pointed out that this view presupposes the existence of a form of democracy that exists almost nowhere in the world. Denis Arnold has argued that the view is incoherent when applied in a global context, since many nations in which corporations operate, such as China and much of the Middle East and Africa, are undemocratic. Furthermore, he argues that even if such a democracy were found to exist, one that acted always in a manner consistent with the will of the people and never at the behest of corporate lobbyists, basic ethical norms would still need to be adhered to, irrespective of the will of the people. For example, one's right not to be enslaved should trump the collective will of a majority of citizens in a democratic society that approves of slavery.

This is a view shared by many libertarians. Proponents of strong side-constraints, such as Nozick, ground side-constraints in fundamental rights. Rights may be either negative or positive. Negative rights constitute shields against the unjust violation of individual freedoms. Positive rights, on the other hand, constitute entitlements to things that are necessary for the exercise of individual freedom. Libertarians famously embrace negative rights while rejecting positive rights. The possibility of defending such a position has proven difficult for libertarians in light of the criticisms leveled against the distinction by philosophers such as Henry Shue. Even Nozick admitted toward the end of his career that his arguments in this regard were unsuccessful. Libertarian business ethicists have also been criticized for failing to address in any serious manner the ways in which business interests exercise a coercive influence over governments and thus undermine democratic institutions.

Integrative Social Contracts Theory

One influential view among business ethics scholars is ISCT, developed by Thomas Donaldson and Thomas Dunfee. While ISTC owes much to contractarian ethical theory, it introduces a variety of new concepts, such as hypernorms and microsocial contracts, and as such is properly understood as the first new normative theory to be developed by business ethics scholars. Donaldson and Dunfee defend a pluralistic account of economic ethics. They reject extreme universalism on the grounds that it is incompatible with the toleration of a variety of diverse moral beliefs. They reject relativism on the grounds that it may sanctify inhumane ethics. Instead, they defend a social contract model that is tolerant of diverse ethical practices while ruling some practices out of bounds.

The social contracts approach for determining the ethical norms for economic ethics favored by Donaldson and Dunfee has three core components: hypernorms, macrosocial contracts, and microsocial contracts. At the global level, there are hypernorms. These are the fundamental principles or norms by which lower-order norms are to be derived. The sources of these hypernorms are intentionally left unspecified. That is, Donaldson and Dunfee are agnostic with respect to the ultimate source or sources of hypernorms. Hypernorms are divided into three distinct categories: procedural, structural, and substantive. Procedural hypernorms set the terms for contracting microsocial contracts implied in the macrosocial contracting situation. The terms specified are the right to exit the microsocial community and the right to exercise one's individual voice within the microsocial community. Structural hypernorms are described as the principles that support the core background institutions of society. These include the right to property, the right to fair treatment under the law, and necessary social efficiency. Finally, substantive hypernorms specify fundamental conceptions of the right and the good, especially with respect to economic activity. These hypernorms are derived from outside the macrosocial contracting situation. Substantive hypernorms such as prohibitions against bribery and gender discrimination are said to emerge from the convergence of religious, cultural, and philosophical beliefs around certain core principles.

Hypernorms are identified and validated by macrocontractors, who are imagined to convene in a sort of parliament of humanity. These rational global contractors would, according to Donaldson and Dunfee, derive the following macrosocial contract with the following terms for economic ethics:

1. Local economic communities have moral free space in which they may generate ethical norms for their members through microsocial contracts.
2. Norm-generating microsocial contracts must be grounded in consent, buttressed by the rights of individual members through microsocial contracts.
3. To become obligatory (legitimate), a microsocial contract norm must be compatible with hypernorms.
4. In cases of conflicts among norms satisfying macrosocial contract terms 1 to 3, priority must be established through the application of rules consistent with the spirit and letter of the macrosocial contract.

The hypernorms agreed to by macrosocial contractors are necessarily general and lack specific moral guidance. It is here that Donaldson and Dunfee believe that microsocial contracts can be useful. By microsocial contracts, they have in mind the extant agreements, both formal and informal, that exist within companies, industries, and other economic groups. These "microcontracts" are to be regarded as legitimate so long as they are consistent with hypernorms and authentic local norms.

ISCT has been criticized on numerous grounds. For example, several theorists have argued that it is relativistic with respect to substantive hypernorms and thereby fails to meet the theory's own internal standards of viability. In an even more penetrating critical assessment, John Boatright and others have argued that Donaldson and Dunfee have omitted too much ethical theory in their account of ISTC for it to be viable. They argue that by invoking religious and cultural norms as a basis for hypernorms, while eschewing traditional ethical theory, ISTC fails to provide reasonable grounds for businesses operating on the global stage to adhere to any one set of hypernorms.

A significant secondary literature on ISCT has been developed. Most of the constructive literature has been produced by social scientists who were persuaded by the efficacy of ISCT. Given the ambitiousness of the theory and its lack of theoretical foundations, the theory has not been taken up as a viable project by many philosophers. In defending ISCT against criticism, Donaldson and Dunfee rightly point out that they are the first business ethicists to examine the relevance of microsocial contracts in everyday economic life. This remains undisputed.

Kantian Business Ethics

One of the most significant traditions in ethics is derived from the work of the 18th-century German philosopher Immanuel Kant (1724–1804). Kant scholarship and Kantian ethics are two of the most important research streams in 21st-century philosophy. Kant scholars study the written works of Kant and attempt to advance our understanding of his work. For example, many Anglo-American readers of Kant take him to believe that it is always unethical to lie, even if doing so would save an innocent life. The Kant scholar Allen Wood has recently shown that this counterintuitive view is not Kant's view. This provides some indication of the ongoing importance of Kant scholarship.

Kantian ethics is a flourishing field in which contemporary philosophers advance the key insights of Kant while at the same time avoiding the difficulties that may be found in some of Kant's original arguments. Such work is increasingly used to provide a theoretical foundation for business ethics. For example, contemporary Kantian ethicists seek to better understand what duties are entailed by the Kantian doctrine of respect for persons. One prominent view holds that a proper understanding of the duty to respect persons yields a core set of managerial obligations. Such a view has important implications for business ethics. In particular, such a view suggests that corporate managers have specific duties to employees regarding health, safety, and working conditions, as well as to other stakeholders.

One of the most influential Kantian business ethicists is Norman Bowie. In his work, Bowie combines contemporary work in Kantian ethics with contemporary work in organizational theory and strategic management to advance discussion of the ethical practice of business. Bowie argues that managers have basic duties to respect their stakeholders and that such duties are compatible with the pursuit of profit. He argues that Kant's first formulation of the categorical imperative provides the basis for a theory of the moral permissibility of market transactions. The first formulation of the categorical imperative requires that actions be universalizable—that is, that everyone in like circumstances should be able to perform the action without self-contradiction. For example, deceiving investors about the financial condition of a firm is self-contradictory in the sense that if every business did this, faith in stock markets would collapse, investment in publicly held companies would stop, and publicly held companies would cease to exist. Market transactions that are consistent in this sense are morally permissible, whereas market transactions that are not are prohibited.

Bowie argues that managers have a duty to protect and promote the welfare of their employees. This duty is grounded in the second formulation of Kant's categorical imperative, which holds that one must always treat other persons as ends in themselves and never as only a means to an end. This means that managers must respect their employees. To do anything less would be to fail to properly respect the dignity of human beings. Examples of respecting employees include refraining from deceit, providing a living wage, and providing meaningful work. Arnold and Bowie argue that the Kantian doctrine of respect for persons also entails that managers of multinational corporations have the following duties in their off-shore manufacturing facilities: to ensure that local labor laws are followed, to refrain from coercion, and to meet minimum health and safety standards.

Bowie argues further that a proper understanding of the duties of managers regarding employees and other stakeholders requires that managers cultivate firms as moral communities. Some of the principles that he argues should guide the moral firm are as follows.

- The firm should consider the interests of all the affected stakeholders in any decisions it makes.
- The firm should have those affected by the firm's rules and policies participate in the determination of those policies and rules.
- It should not be the case that for all decisions, the interests of one stakeholder should trump the interest of all the others.
- When stakeholders come into conflict, the humanity of some stakeholders cannot be sacrificed merely because there are a greater number of stakeholders in the other set.
- Only principles that are universalizable may be adapted.

Unlike ISCT, the Kantian approach to business ethics is not susceptible to the criticism that it lacks sufficient theoretical foundations. Rather, critics argue that because of its theoretical foundations, the Kantian view is susceptible to all the criticisms that have been mounted against both Kant's ethics and Kant's metaphysics. Since this is the case, they argue, Kantian business ethics is not a viable research project. Kantians normally respond in one of two ways. First, they argue that the resurgence in work by Kantian scholars and Kantian ethicists in recent years has reinvigorated Kantian ethics and disarmed many traditional criticisms. Second, they argue that elements of Kantian ethics, such as the doctrine of respect for persons, can be assessed independently of other elements of Kant's philosophy and have been shown to merit allegiance in their own right.

Descriptive Scholarship

In contrast to normative business ethics, descriptive business ethics is not (or less) concerned with determining the moral status of an act in the business realm. Instead, it is concerned with explaining and potentially predicting the commission (or omission) of that act. Accordingly, descriptive business ethics adopts a social scientific perspective to business ethics topics. The social scientist who studies business ethics relies on factual evidence to make neutral descriptions of behavior related to morality and ethics and to support or refute theoretical explanations of the relationships between concepts. A social scientist might, for example, gather evidence about the role of tenure in embezzlement or the relationship between an organization's size and its propensity to overstate earnings and use such findings as a basis for a more general explanation of embezzlement or disclosure. While many believe that the descriptive and normative elements operate in parallel domains and that any interaction between the two threatens to violate the naturalistic fallacy (deriving an "ought" from an "is"), many business ethics researchers assume that empirical findings on business ethics can be integrated with normative implications in a perpetual cycle of learning that requires ongoing theoretical development, empirical validation, and the refinement of normative prescription.

The Scientific Method

The social scientific study of business ethics normally follows a generalized format. First, the researcher identifies a phenomenon of interest or a research question to be answered. Generally speaking, business ethics researchers are concerned with the phenomena of moral and/or socially responsible behavior as they relate to business practices or policy, but typically the phenomenon of interest or the research question itself is focused on a very specific practice or policy. Those who study whistle-blowing, for example, might ask what leads an individual to become a whistle-blower or what kind of treatment individuals might receive after they have reported unethical behavior in a company. Once the researcher has identified the research question, a theory is put in place to answer that question. The central concept of social science is the theory, a generalized statement about the relationship of two or more concepts. A theory might be developed through intuitive reasoning, grounded experience with the phenomenon (e.g., a case study, participation, observation), evidence from previous empirical work on related topics, or a combination of all three. The researcher then selects a methodology for testing that theory. In some cases, a theory will implicitly dictate the kind of methodology to be employed. If a theory, for example, purports causality, a methodology that establishes causality, such as an experiment in the lab or the field, is not only suitable but perhaps also required. If a theory simply argues that two concepts are associated with each other, the researcher might be justified in selecting a survey or the analysis of archival data to find evidence of a correlation (or a lack thereof) between the two. Similarly, if the phenomenon being studied is a process, the methodology will require repeated measures to establish patterns of behavior and changes over time. Some research questions are amenable to qualitative approaches, or perhaps combined approaches that meld many different kinds of methodologies into an overall program of research. Ultimately, the research relies entirely on a methodology to gather data that support or refute the theories involved and illuminate the original research question.

Social scientific research on business ethics is often categorized according to the level of analysis. While some work has been conducted on groups, industries, and market-level issues, the vast majority of business ethics research has focused on the individual and the organization. Within these two very large categories, researchers have attempted to explain individual and organizational behavior in the context of generally accepted moral norms and social obligations.

Individual-Level Research

Much of the individual-level research is tied to the cognitive developmental approach to moral behavior. This field is most appropriately summarized by James Rest's four-stage model of moral behavior. According to Rest, moral behavior is the result of a four-stage process wherein the individual (1) recognizes the moral issue, (2) makes a moral judgment, (3) establishes the intention to act morally, and (4) finally behaves morally. Researchers have conducted numerous studies to better understand all the possible factors that might shape these four stages of behavior. For example, a great deal of research has considered the role of gender in each of these four stages; some of this work has found differences between the genders (i.e., women are more aware of moral issues and are more likely to behave morally), while others have found no evidence of a gender effect.

The cognitive developmental approach has dominated the field for decades and has spurred a great deal of research on why and how individuals act morally or immorally. Nevertheless, this research has also demonstrated the shortcomings of a cognitive approach, and as a result, there are growing movements to explore other kinds of frameworks or approaches as a basis for explaining individual moral behavior. Several researchers, for instance, have proposed emotions and intuition as a basis for moral decision making and moral behavior.

Within this large stream of literature, the field has recognized that individual moral behavior is influenced not only by individual factors (gender, age, intelligence, personality traits, etc.) but also by contextual factors. Some of the more well-researched areas related to contextual factors include the characteristics of the issue itself (moral intensity), elements of the immediate environment in which the individual works, and characteristics of the larger culture in which the individual lives. Research on organizational ethical climates, for example, has demonstrated that organizations develop shared norms about what is done and how it is done and that these expectations influence individual moral decision making and behaviors. Research has also demonstrated that both immediate factors, such as peers, bosses, and reward systems, as well as more distant factors, such as codes of conduct, ethics training, and other institutional mechanisms, can affect individual moral decision making and behavior.

A substantial proportion of descriptive business ethics research has focused on the organization as a level of analysis. Perhaps most prominent among such approaches has been the stakeholder approach to management discussed above. The stakeholder approach argues that the organization exists in a network of relationships with primary and secondary stakeholders and that by developing and managing these relationships the organization can garner and develop financial and moral legitimacy in the marketplace. While much of the stakeholder literature is theoretical in nature, empirical research has quantified variables related to the theory to test some of these arguments. For example, there is empirical evidence to suggest that stakeholders who are powerful and legitimate and have urgent claims receive more attention from the organization as opposed to other stakeholders who are less powerful and less legitimate and have less pressing claims.

Organization-Level Research

Other research focusing on the organization as a level of analysis has generally focused on the social performance of the organization. This literature typically seeks evidence of the causes and effects of an organization acting beyond its financial responsibilities toward more socially oriented obligations. Within this literature, researchers have identified the factors that increase the likelihood that an organization will act in a socially responsible manner, the factors that increase the likelihood that such socially responsible behaviors will be successful, and the consequences of an organization acting in accordance with social expectations. A great deal of the research in this area is aimed at identifying a relationship between the financial performance of the firm and its social performance. As a matter of empirical evidence, recent meta-analyses along these lines suggest that while financial and social performance are correlated, an organization that conducts itself in a socially responsible manner is not necessarily more successful financially, though it may reap intangible rewards that facilitate the long-term survival of the organization.

Challenges

Conducting business ethics research involves several challenges. While many of these challenges are inherent in any social science research, others are unique to the study of business ethics. One of the most common challenges faced by business ethics researchers involves a fundamental methodological concern: measurement. To conduct empirical research, the researcher must determine the means for measuring the concepts in question. Subsequently, if a researcher is interested in studying moral behavior, it is undoubtedly required that the researcher employ a measure of moral behavior. As with many social scientific constructs, a measure such as this is difficult to create because the researcher must establish the validity of the construct and provide evidence that that measure measures what it claims. Such a task is dramatically more difficult in the business ethics realm, however, because of what many view as the subjective nature of morality. Whether a behavior is moral or not might be relative, and even the most universal of behaviors might be considered immoral under specific conditions. For example, if the researcher is interested in moral behaviors and chooses to focus on dishonesty, does withholding information constitute lying? Furthermore, does dishonesty sufficiently represent the concept of immoral behavior? In the face of such difficulties, the researcher must rely on the norms and traditions of social science and conduct the research in accordance with those standards but must also be mindful of the underlying philosophical concerns that might invalidate his or her measure. Clearly, measurement is a significant challenge for the business ethics researcher.

Another challenge that affects the business ethics researcher, perhaps more so than any other social scientific researcher, is that studying how individuals and organizations act in the context of moral norms might require or threaten the violation of those or other relevant moral norms. When studying the impact of light, for example, it would be useful from a scientific perspective for a researcher to create an environment where light is low or absent. Creating an environment where morality is weak or absent, though, could in and of itself be considered an immoral act because of the harm it might do to the participants of the research. For this reason, the business ethics researcher is at all times both an observer and a subject of business ethics phenomena. The difficulty of operating in such conditions was perhaps never more apparent than in Stanley Milgram's famous studies. Milgram asked very poignant questions about the role of authority in individual moral behavior. His studies employed deceit to examine how completely individuals would follow authority. Although his studies were informative, the methodology that they used posed a threat to the psychological well-being of the individuals and violated some of the very moral norms the experimenters were exploring. Of course, any study involving subjects contains an element of inconvenience and perhaps a risk to the subject. Descriptive ethics studies, however, must take special care to consider the risks of their studies to ensure that the studies themselves do not violate moral norms of behavior. Over the years, human subjects guidelines have evolved, and expectations about how subjects are treated during the research process have become institutionalized, and these guidelines are particularly salient to business ethics research. Nevertheless, they do not encompass all the moral concerns that the study of morality entails.

A final challenge for business ethics research is to effectively define the unique elements and status of business ethics issues in order to sufficiently justify the existence of business ethics research. In other words, business ethics researchers have at some level an obligation or a requirement to explain what is inherently or effectively unique about moral topics. For example, training is an important part of organizations and has been studied extensively from many different perspectives. In recent years, ethics training has received increased attention, but researchers might ask, Is ethics training somehow distinct from other forms of training, and if so, what is the nature and implications of those differences? If ethics training is not unique and different from other training, then there is little to no value in studying and explaining ethics training other than to make incremental contributions to a larger body of knowledge on training. One area of study that is most subject to this kind of concern is that of individual moral decision making. A considerable amount of research has been conducted on moral decision making, but there is some question about how moral decision making is different from other more generalized forms of decision making. Are the processes of moral decision making unique, do they involve factors not included in other forms of decision making, or is moral decision making merely a specialized form of decision making? To the extent that researchers can identify the unique aspects of moral decision making, they have the potential to better understand the topic of concern, to more fully legitimate the field, and to more fully contribute to society.

One approach to justifying the study of business ethics and, perhaps paradoxically, establishing the unique position of moral topics is to suggest that every topic has an ethical dimension. While such an approach is philosophically debatable, from a practical perspective, it justifies the integration of a much larger circle of social scientific research. There are many areas of study that lie outside the traditional business ethics realm that are nevertheless at some level conceptually related to ethics, and research in these areas might have much to offer more traditional business ethics topics. The most obvious of such areas is that of justice. Researchers have identified at least four principal forms of justice (distributive, procedural, interactional, and systemic) as psychological constructs. A host of research in a wide variety of social scientific settings has subsequently measured these different forms of justice and has identified relationships to various different variables. The question that remains, though, is to what extent is justice a business ethics topic? This question is critical because descriptive ethics is in constant tension with normative ethics, with an assumption of some interplay between the two. If justice is considered to be a business ethics topic, then there is a secondary analysis to be conducted that could dramatically inform our understanding of this topic. The same could be said for other areas of research, including whistle-blowing, deviance, corporate governance, the environment, and others. These topics have strong ethical undercurrents, yet they are not always identified as business ethics topics per se, and thus there is some question about the social scientific identity of these issues. On the one hand, arguing that there is an ethical dimension to every decision provides an avenue for integrating these kinds of topics into business ethics research. On the other hand, doing so also threatens to dilute business ethics more generally as a unique field of social inquiry.

In sum, descriptive business ethics is an attempt to explain and predict the occurrence of moral behavior in business settings. Most descriptive business ethics research has been focused on individuals and organizations, but regardless of the level of analysis, business ethics researchers face common methodological and institutional challenges. To develop valid and useful work, they must follow a general scientific method that adheres to the norms of established social science and is consistent with the underlying philosophical principles.

Looking Forward

To date, much of what has been produced by business ethics scholars has focused on large, publicly held corporations and the managers and employees who populate them. We expect that as in other similar academic fields, business ethics scholarship is likely to become more diverse and more specialized. For example, a literature on the ethics of entrepreneurship and on the ethical issues confronting small and medium-sized enterprises has begun to emerge. Similarly, it is more common for scholars to focus on specific subfields, such as accounting ethics or marketing ethics. This increased specialization produces knowledge that is more relevant to professionals in the various business disciplines. As the field matures and develops, we expect that more attention will be paid to these kinds of elements, producing a richer and much more comprehensive body of knowledge, and ultimately business ethics will more fully represent all those concerns with which the term *business* is associated.

—Denis G. Arnold and Scott J. Reynolds

See also Cognitive Moral Development; Consequentialist Ethical Systems; Corporate Moral Agency; Deontological Ethical Systems; Duty; Ethics, Theories of; Integrative Social Contract Theory (ISCT); Kant, Immanuel; Kantian Ethics; Liberalism; Libertarianism; Mill, John Stuart; Moral Imagination; Rights, Theories of; Social Contract Theory; Universalizability, Principle of; Utilitarianism

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Business for Social Responsibility (BSR)

Business for Social Responsibility (BSR) is a global organization that helps member companies achieve success in ways that respect ethical values, people, communities, and the environment. Its mission is to create a just and sustainable world by working with companies to promote more responsible business practices, innovation, and collaboration.

BSR began in 1992 as an association of approximately 50 companies dedicated to helping businesses be both commercially successful and socially responsible. Many of these founding companies were small and medium-sized businesses—such as Ben and Jerry's, Patagonia, and Tom's of Maine—which themselves strongly believed in and pursued responsible business practices.

During the past years, corporations are becoming more aware that to compete successfully, they need to develop responsible business policies and practices and make them an integral part of their mission, values, strategy, and operations. Along with this increasing importance of corporate social responsibility (CSR), the world has witnessed the growth of a network of national organizations that promote awareness of CSR and provide business leaders with tools and opportunities to collaborate with innovative managers across all industries, geographies, and functions. BSR, as part of this network, provides information, tools, training, and advisory services to make CSR an integral part of business operations and strategies.

BSR helps address a broad spectrum of CSR issues: business ethics, community investment, environment, governance and accountability, human rights, marketplace, mission, vision, values, and workplace.

To fulfill its mission, BSR works mainly in four specific areas. First, it provides advisory services on matters such as CSR reporting and implementation, stakeholder engagement, working groups, supply chain management, CSR strategy and structure, and CSR assessment and policy development. Second, BSR sponsors a series of conferences, including the BSR Annual Conference, which has become the largest forum for CSR practitioners, bringing together over 1,000 business leaders from more than 40 countries and their colleagues in the independent and public sectors. In the course of 4 days, executives, economists, analysts, academics, nongovernmental organizations, and public policy leaders can participate in training sessions and instructive breakout sessions covering business action in the areas of economic development, governance and accountability, human rights, and the integration of CSR into core operations. Third, BSR provides a collection of resources on responsible business practices, mainly online tools and guidelines. Fourth and finally, its store contains a number of books and reports that enhance the knowledge and promotion of CSR.

In addition, being a nonprofit organization, BSR promotes cross-sector collaboration and contributes to global efforts to advance the field of CSR: BSR connects its members to a global network of business and industry peers, partners, stakeholder groups, and thought leaders, mainly because cross-sector dialogue and collaboration have become the essential ingredients of a successful CSR strategy. Working in partnership with these groups, BSR is expanding its capacity to serve its members' global business needs and to achieve the mission of the BSR Education Fund. BSR has established formal partnerships with Global Compact, Ethos Institute (Brazil), CSR Europe (Belgium), MAALA (Israel), Business in the Community (United Kingdom), and Acción Empresarial (Chile). BSR is also a founding member of EMPRESA, the Forum on Business and Social Responsibility in the Americas. BSR has established additional links with other business organizations with similar interests in the United States, Canada, Europe, Latin America, Asia, and Africa.

BSR also acts as an intermediary between business and civil society. While understanding business and serving its needs, BSR maintains strong relationships with other key stakeholders and opinion leaders in the civic and public sectors. Through these relationships, BSR provides companies with alternative viewpoints and engagement opportunities that help them better formulate decisions, positions, and actions.

Today, BSR member companies have nearly $2 trillion in combined annual revenues and employ more than 6 million workers around the world. Even though the organization was started by medium-sized companies and membership is open to all companies regardless of size or sector, nowadays BSR's members consist mainly of large corporations such as American Express, Coca-Cola Company, Ford Motor Company, General Motors Corporation, IBM, McDonald's, Nike, Procter & Gamble, UPS, and Walt Disney Company. On its Web site, BSR lists what it describes as an "illustrative" list of members, implying that some prefer their identity not to be publicly disclosed. Membership provides the previously mentioned extensive set of practical resources.

—Marcelo Paladino, Amalia Milberg, and Florencia Sánchez Iriondo

See also Business Ethics; Canadian Business for Social Responsibility; Corporate Social Financial Performance; Corporate Social Responsibility (CSR) and Corporate Social Performance (CSP); Nonprofit Organizations

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Business Judgment Rule

The business judgment rule serves to shield an officer or director from civil liability when sued for a breach of a fiduciary duty, with the highest fiduciary duty owed to shareholders. Under corporation law, the business judgment rule is the classic defense used by directors and officers of corporations when they are sued, usually by shareholders. While the business judgment rule presumes that an officer or director has behaved reasonably, that presumption can be overcome by evidence of a negligent or disloyal act. The courts of Delaware, where more than 60% of Fortune 500 companies are incorporated, have largely defined and applied the rule through case law, not through statutory law.

Impact

The business judgment rule prevents courts from second-guessing management decisions and from interfering with management prerogatives. This is especially important in a capitalistic system as a way to provide an incentive to officers and directors to take the necessary risks preferred by shareholders and to create wealth for society. Mistakes sometimes occur when taking risks, but officers and directors would avoid risk taking entirely if they were to suffer personal liability from any mistake. They would then operate fearing litigation at every step.

Historically, Delaware courts have accorded more protection to management than to shareholders, especially during the wave of takeovers during the 1980s. It is more difficult today, however, for directors to invoke the veil of protection of the business judgment rule, due to recent judicial applications that have tightened the legal demands on officers and directors. Courts today more closely scrutinize potential violations of fiduciary duty by officers and directors.

Elements of the Business Judgment Rule

The elements of the business judgment rule are loyalty, candor, care, and good faith. The business judgment rule presumes that officers and directors abide by these elements, but the presumption is rebuttable and can be overcome by evidence in court. These are the elements of fiduciary duty, and the breach of any such duty can create personal liability for an officer or director. While good faith is an element of other duties, such as loyalty and care, courts increasingly see it as a separate duty, especially as corporate charters have eroded the significance of the duty of care.

Loyalty

Officers and directors must believe in good faith that their actions serve the best interests of the corporation, not their own personal interests. Loyalty stands as a barrier to conflicts of interest and demands that officers and directors exercise independence of judgment. It prohibits officers and directors from engaging in self-dealing and using their position to their own personal financial advantage. If a director, for instance, would benefit from the sale of land or real estate to the corporation, the deal must be an economically prudent deal for the corporation. The director must not promote such a real estate transaction if only the director benefits, while the corporation would gain more from an alternative transaction.

Corporate codes of conduct often extend and reinforce the duty of loyalty by requiring that all employees refrain from conflicts of interest. Often such codes require that an employee disclose any conflict of interest to either the board of directors or the corporate legal counsel. Even without such a code, however, officers and directors owe a common-law duty to the corporation to refrain from any conflicts and to disclose them.

Related to the duty of loyalty is the independence of judgment that directors should exercise. To honor their fiduciary duty, directors should not act in a self-interested manner; this issue has been prominent in cases involving mergers, takeovers, and takeover defenses. So long as a takeover defense is designed not to entrench managers in their positions but rather to protect the independence of judgment of officers and directors to make the best decision for shareholders, a takeover defense will be consistent with the business judgment rule.

The independence of judgment required to fulfill one's fiduciary duty to shareholders and to remain loyal to the corporation may go beyond the avoidance of self-interest and conflicts of interest. Independence can also be jeopardized by social relationships and loyalties to other institutions. For instance, directors employed by a university that receives substantial philanthropic contributions from a company might not be able to independently judge the merits of a legal dispute with the university or with officers who have ties to the university.

Candor

Officers and directors also owe a duty of candor to investors and in their own deliberations. Officers should not hide bad news from the board of directors, and the board should share an honest description of the company's conditions and prospects with investors and regulators. Officers and directors should disclose any conflicts of interest, and they should freely exchange their own views in a culture of open dialogue.

This common-law duty is reinforced by Securities and Exchange Commission (SEC) regulations and other government regulations. It also relates to the ethical duties of honesty and disclosure.

Care

Breach of the duty of care is the first step in proving a negligence action against an officer or a director. To fulfill their duty of care, officers and directors must be diligent, act rationally, and make informed decisions. In establishing a standard for the duty of care, courts apply an "ordinarily careful and prudent director" standard. Some decisions have held that directors violate their duty of care only when gross negligence can be shown. Most states have also enacted statutes specifying the degree of care consistent with prevailing judicial decisions.

In determining the nature of an informed decision, courts have held that officers and directors are not liable for good-faith reliance on a consultant's report, so long as they behaved reasonably in selecting the consultant and discussed the accuracy of the report's information and conclusions. However, when a board spends only 2 hours on a Sunday afternoon deliberating and then approving a major leveraged buyout of the firm based on a biased report, as in one landmark case, courts have found that it does not constitute an informed decision.

The duty of care includes the duty to actively monitor corporate performance through a corporate information and reporting system. In the case In re Caremark International Inc. Derivative Litigation, 698 A.2d 959 (Del. Ch. 1996), the Delaware Chancery Court held that although a board of directors cannot be expected to know about all wrongdoing in a company, it nevertheless has a duty to exercise adequate oversight as part of its duty of care as well as its duty of good faith.

One major legal erosion of the duty of care has occurred. The Delaware General Corporation Law now allows companies to adopt charter provisions exculpating their directors from the need to fulfill the duty of care. However, directors are not exculpated from honoring other fiduciary duties, including the duty of good faith. For that reason, courts are beginning to breathe more life and significance into the duty of good faith than it has heretofore enjoyed, as explained next.

Good Faith

Courts in the past tended to doubt whether a duty of good faith exists separate and apart from the duty of care or loyalty. Increasingly today, however, courts have elevated that duty to a separate status in situations where the duties of care and loyalty have not been violated. This is especially important given that corporate charters increasingly contain exculpatory clauses that relieve directors of liability when they fail to exercise due care.

To find a lack of good faith, a court must find the director's decision so irrational that it cannot be explained except for bad faith. Bad faith would also include recklessness or intentional wrongdoing. For instance, if a chief executive officer demanded a bribe from an acquiring company as a condition for the completion of a merger, a director who approved the merger might be held liable for demonstrating lack of good faith.

Even though the directors of Disney were not found liable for violating their fiduciary duties in approving the $140 million severance payment for the former president Michael Ovitz, a judge denied a motion to dismiss the charges at an earlier stage based on a conscious and intentional disregard of director responsibilities, which constituted bad faith. Disney itself had a charter provision that exculpated directors from any liability due to breach of due care, so the case moved forward on the basis of a possible breach of the duty of good faith.

If board members engage in a "sustained and systematic failure" to monitor a firm's compliance with pharmaceutical safety regulations, that can constitute bad faith. If a corporate officer fails to disclose a blatant conflict of interest to the board or to the chief counsel, as required by a corporate code, that failure can also constitute bad faith.

Current Legal Interpretations

The SEC has acted in parallel to the evolving standards of the business judgment rule in some of its recent enforcement actions. Failure of oversight has been important in bringing action against some directors for securities fraud. For instance, if a director ignores a decision by top management to fire the company's outside auditor for charging the company with improper accounting, the director's failure could breach the duty of care as well as violate SEC regulations. The SEC is also pursuing directors for failing to maintain adequate information and reporting systems, as articulated in the Caremark case.

There are two other aspects to the role of the SEC in these enforcement actions. First, even when a director might be exculpated under a charter provision from liability for breach of the duty of care, the director might still be subject to SEC penalties for the same duty of care violation. Second, and much to the chagrin of states' rights advocates, the SEC is using standards of fiduciary duty established under state corporation law in its own body of federal regulations. Critics of the Sarbanes-Oxley Act complain that the law federalizes principles of corporate governance, which have been the focus of state law and court decision throughout American business and legal history.

Under recent interpretations of the business judgment rule, and especially of the separate good faith standard, it is becoming more important for directors to take the initiative and to more actively monitor corporate performance and for boards to focus more on process issues. While the details of a reporting system are a legitimate question of business judgment, it is at least important for the board to ensure that there is a sufficient system of reporting and internal controls in place. That should include financial, operational, and compliance controls. Such controls are also important in complying with the provisions of the Sarbanes-Oxley Act, so they serve multiple purposes.

Directors also protect themselves from charges of intentional and reckless wrongdoing when they pay more attention to red flags or warning signals. They need to pay attention to both internal reports and such external signals as lawsuits and negative media reports. This is especially true when the gravity and duration of the alleged wrongdoing are greater.

Directors can further protect themselves from liability, and also demonstrate care and good faith, by ensuring compliance with the standards set by both government agencies and self-regulatory organizations, such as the New York Stock Exchange. Being proactive and going even further to study and adopt the best practices developed by other companies, especially in such challenging areas as compensation and executive succession, would also be prudent.

—John M. Holcomb

See also Business Law; Conflict of Interest; Corporate Governance; Directors, Corporate; Due Care Theory; Due Diligence; Fiduciary Duty; Loyalty

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Business Law

Law can be defined as rules set by society to govern behavior; thus, business law refers to those rules of behavior that govern business. To govern behavior efficiently, law must be both predictable and flexible. It must be predictable so that people can plan their behavior, and it must be flexible so that it can be applied in a wide variety of different situations.

Law is directly related to ethics, especially in a business context: Much of business law amounts to the formalization of "good business practices" or ethics, and neither ethics nor law can be meaningful without each other. Ethics without the authority and enforcement of law is a mere aspiration. The reverse is also true: Mere law, if it does not mirror societal expectations of behavior at least to some extent, is not likely to be enforced. For example, although there was contract law in place shortly after the dissolution of the former Soviet Union, that law was often not effective because post-Soviet society was not used to expecting people to keep their promises.

When a community is appalled by an ethical violation, that violation may drive the development of law, whether through legislation, judicial decision, or both. For example, the Enron and WorldCom scandals of 2001 to 2002, which involved deceptive and fraudulent accounting practices, led to the prosecution of those involved and also led directly to the Sarbanes-Oxley Act (SOX), which created new duties and accountability for corporate officers and accounting firms. Much of the unethical behavior involved, however, was illegal before both these scandals and the act. Thus, the ultimate lesson of those scandals may well be that law alone cannot prevent such acts. In these cases, short-term business pressures led companies first to stretch the laws of accounting practice and then violate them in an effort to present a positive picture and preserve the stock market value of the companies involved. The legal scandals that developed from these dishonest acts ultimately resulted in the demise of those companies. In the aftermath, it has been posited that law by itself is an insufficient deterrent for unethical practice, because under pressure of competition, companies will continue to look for ways to abide by the letter, rather than the spirit, of the law. Businesspeople must not only abide by the law, but they must also realize that unethical behavior ultimately leads to the destruction of a business, and they must be aware of the business virtue of absolute moral conviction.

To make the relationship between law, business, and ethics still more complex, while there are times when societal mores and ethics lead to the enactment of law, there are also times when morality and business law diverge. For example, it is a long-standing principle of common law that there is no duty to rescue, so that if you see a man about to step in front of a fast-moving car, you have no legal obligation to reach out and stop him—though most of us would feel we had a moral obligation to do so. To begin with, enforcing a duty to rescue would be contrary to a free society and the principle that individuals have the freedom to pursue their own individual good as long as they do not attempt to deprive others of theirs or impede their effort to obtain it. Creating a legal duty to rescue would imply a society that focuses on a group good rather than individual good. Moreover, creating a legal duty to rescue would be impractical. When would such a duty arise? How would it be enforced? If there were a crowd of people, on whom would the duty fall?

The same divergence between ethics and law can be found in business. For instance, Henry Ford once wanted to forego increasing dividends for his shareholders and instead wanted to use the money for philanthropic purposes. He felt that his company was rich enough and the ethical thing to do at that time was to lower the price of cars and increase the size of his company so that he could hire more workers and pay them the same good wages he was paying his current employees. However, in a famous opinion, the Michigan Supreme Court disagreed: The court found that Ford Motor Company's primary duty was to its shareholders and to make a profit and did not justify the charitable steps he was planning.

In addition to being driven by ethics, business law is also driven by society's need to foster commerce, because a strong commercial environment is directly related to the health of a nation's economy and the welfare of its citizens. The United States Constitution was influenced by the concern that commerce be fostered, as seen in the Commerce Clause, which has been interpreted as prohibiting states from discriminating against products from other states. The creation of the Constitution, however, was also driven by the nation's need to raise taxes, and this taxing power has led to a symbiotic relationship between business tax laws and new forms of business entities such that business forms are designed to take advantage of tax laws.

Some of the topics most often discussed that display the interplay between business law, commercial need, and ethics include contracts and sales, business torts and products liability, environmental protection, workers' remedies (safety, antidiscrimination, privacy, and whistle-blowing), and trade law (fair trade, intellectual property, and anticorruption laws).

Contracts and Sales

For businesses to thrive, they must be able to rely on commitments. Sometimes, business is successfully concluded merely on a handshake ("my word is my deed"), such that neither party feels the need to verify that the commitment will be enforced by the law should the other party fail to keep his or her word. However, if the commitment is a large one, if the parties are strangers, or even if they are just cautious, either or both of them may want to verify that the agreement will be enforced by a court should something go wrong. Parties need to be free to contract according to their own best interest, but they also need to be free from being obligated unless they specifically intend to be obligated and they understand those obligations. Contract law systems attempt to balance these ethical and practical considerations.

Common Law of Contracts: Offer, Acceptance, and Consideration

Traditionally, in common law—the law derived from centuries of cases decided by English courts and used in 49 of the United States—an enforceable contract requires proof of just three things in addition to the intent to be bound: offer, acceptance, and consideration. An offer must be sufficiently precise and complete such that the other party's merely saying "yes" to that contract means that a contract will be formed. However, if some of the necessary information or terms are missing, then the statement is not an offer. For example, "Would you like to buy six widgets at $12.00 per widget?" constitutes an offer for the sale of six widgets and indicates that if a buyer agrees, then the seller intends to be bound to the resulting contract. In contrast, the statement "Widgets for sale, $12.00 per widget" is not an offer because merely saying "Yes" would not complete a contract—neither party would know how many widgets were being sold. Instead, this kind of statement is called an "invitation to negotiate." As with most advertisements, the purported seller is simply trying to interest potential buyers; he is not making a formal offer for sale.

An acceptance, in concept, is similarly simple. It signifies the other party's intent to be bound by the terms of the contract: "Yes, I'll buy six widgets for a total of $72.00." However, if the buyer were to say, "Will you accept $8.00 each for six widgets?" then no contract would be formed because the buyer has not accepted the original offer. Instead, he has implicitly rejected it and made a new offer, a *counteroffer,* instead.

The third concept required by common law is *consideration,* which refers to the thing that each party receives in exchange for his or her agreement to perform the obligation or obligations indicated in the contract. This requirement of mutual consideration means that there is some indicia that each party *bargained for* what he or she is receiving under the contract. *Bargained-for consideration* is merely another way of verifying that the parties intend to be bound by the terms of their agreement. Civil law, the law used in 90% of the world (including Louisiana), does not recognize the concept of consideration but uses instead a related principle, termed *cause: cause* is the reason why one obligates oneself to a contract. Both *consideration* and *cause* serve to verify that the parties intend to be bound.

When a party to a contract fails to perform his or her obligations, the other party may sue for breach of contract. Thus, if the buyer pays the $72.00 for the widgets, but the seller fails to deliver them, the buyer has a legal remedy: the buyer can demand the return of the $72.00 or demand that the widgets be delivered, and the court will order the seller to do one or the other. Similarly, if the widgets are defective, the buyer can sue under various warranty theories. Finally, if the seller delivers the widgets but does so in such an unfair and unethical way that the buyer cannot enjoy their use, then the buyer can sue for a breach of the *duty of good faith and fair dealing.*

All these basic contract concepts are the legal embodiment of a basic ethical principle: One should not make promises lightly, and one should deliver what one promises to do, and no less. They are also basic good business practice because they encourage win-win agreements. Where businessmen keep their word and deliver a good and useful product at a fair price, they are likely to be successful. If, on the other hand, they fail to keep their promises, deliver a poor product, or otherwise make their customers miserable by behaving unethically, their businesses will eventually decline and they will have trouble attracting new customers. Thus, basic contract law is based on centuries of experience about what constitutes both good ethics and good commercial practice.

Statutory Contract Law

Statutory law builds on these basic principles, setting standards and specifics for commercial contracts involving the sale of goods (Uniform Commercial Code, Article 2 [UCC-2]), contracts involving e-commerce (the Uniform Electronic Transactions Act), negotiable instruments (Uniform Commercial Code, Section 9), and others. In addition to providing remedies for unethical conduct, these statutes are designed to improve communication and efficiency and prevent disagreements by setting standard terms for commercial contracts and providing directions for what should be done if the parties' contract fails to provide for some contingency. For example, under the UCC-2, if commercial parties fail to mention a price for the sale of a good, then as long as they intend to be bound to the contract, a court can imply a "reasonable" price as determined by the local market.

International Contract Law

In addition to common law and state and federal statutes, some contracts are governed by multinational treaties signed and ratified by the United States: the Vienna Convention on Sales, the Electronic Signatures in Global and National Commerce, and others may be *mandatory* law (law a court must follow) if the parties to the contract are residents of different countries. Most, if not all, of these treaties state the basic requirements of the type of contract at issue and incorporate the same fundamental concepts of offer, acceptance, cause or consideration, and the duty of good faith. In addition, parties to a contract often stipulate which state, country, or international law they want to govern their contract in the event that they come to some disagreement; and they often stipulate that their disagreements will be resolved out of court, through mediation or arbitration, both of which methods of alternate dispute resolution are governed by still more law.

Business Torts and Products Liability

The most fundamental purpose of law and government is to stop people from hurting each other, or at least to punish them or force them to make recompense when they do. The difference between a tort and a crime is that a tort is a civil wrong: One party sues another. A crime is a societal wrong such that government sues (i.e., *prosecutes*) the malfeasor on behalf of the people as a whole. Businesses have long been held civilly liable for the intentional or unintentional torts of their agents and employees. Although they can be held criminally liable as well, this section will deal only with businesses' civil liability for torts. An intentional tort is one where the tortfeasor specifically intends to commit a wrong—for instance, where an employee wrongfully restrains a customer he suspects of shoplifting (committing the tort of *false imprisonment*). Businesses are allowed by statute to restrain customers they reasonably suspect of shoplifting but must do so within certain limitations. If they restrain a purported shoplifter for too long a period prior to contacting the police or if they restrain him or her under improper and overly punitive conditions, then that person may sue for false imprisonment.

Vicarious Liability for Unintentional Torts

In addition to being held vicariously liable for intentional torts, businesses may be held vicariously liable for the unintentional torts of their employees. For example, if a pizza deliverer causes an accident while delivering pizza, the injured person can sue both the pizza deliverer and his or her employer. Similarly, if a business fails to properly maintain its premises, it can be held liable for negligence when a customer is injured as a result—these are the well-known "slip and fall" cases, where a grocery store is liable for a customer's slipping in a puddle of water on the floor.

Liability for Third-Party Crimes

Thus, businesses are often held liable for the misdeeds and negligence of their employees, but until recently, they had not been held liable for the misdeeds of third parties while on their premises. As with the lack of any duty to rescue, businesses traditionally had no duty to prevent third parties from committing crimes against customers on their business premises, for several reasons: It would be unfair to hold a business liable for criminal conduct it could not predict; such liability would place an undue economic burden on commercial enterprise and the consuming public; protecting citizens is a function of the government that should not be shifted to the private sector; merchants should not become insurers of customer safety; and one can reason that the criminal's act is what caused the harm, not the merchant's purported failure to protect the customer from the crime.

This is changing, however. Generally, a business still has no duty to protect customers from the criminal acts of third parties that occur on its premises. The business is not the insurer of its customers' safety, and it has no absolute duty to implement security measures to protect them. However, a number of states now impose a duty on businesses to take reasonable precautions to protect customers from foreseeable criminal acts. The question then becomes how to define *foreseeable.* Although different courts use different definitions, the trend now is to define foreseeable in terms of a balance between the likelihood and gravity of the risk as opposed to the economic burden preventative measures would place on the business. If the risk is low and the cost is high, a business is found not liable for a particular criminal act. On the other hand, if the risk and the gravity of the harm are great (as when a customer is abducted from a business's parking lot where a number of crimes have already taken place, so that one would logically expect more crime) and the burden of preventing such crimes would not be too onerous (a security guard could have been hired for a reasonable rate), then the crime is foreseeable and the business is liable for the damages caused by the crime.

In setting these new standards, courts try to strike a balance between the policy reasons that originally denied such a duty and practical considerations. Courts recognize that the economic and social impact of requiring businesses to provide security on their premises is significant. Security is a significant monetary expense for any business and further increases the cost of doing business in high-crime areas that are already economically depressed. Moreover, businesses are not responsible for the endemic crime that plagues society, a problem that even law enforcement and other government agencies have been unable to solve. At the same time, while acknowledging that businesses do not cause the crimes committed on their premises, in imposing a limited duty to protect customers, courts recognize that business owners are often in the best position to both appreciate the crime risks that are posed on their premises and take reasonable precautions to protect against those risks.

Strict Products Liability

Another area of business tort law in which courts and legislatures have had to strike a balance between ethics and economic reality is products liability. Originally, only the direct buyer of a product could sue the manufacturer if a product was defective. If the product was sold to the injured consumer by anyone other than the manufacturer, then the manufacturer was not liable because it had no contract with the consumer. As the 20th century advanced, bringing ever more industrialization and faced with increasingly serious claims by consumers injured by factory-made products, courts began to stretch negligence theory to cover such situations, but this also proved unsatisfactory because it is very difficult for an injured consumer to obtain the information needed to show that the manufacturer thousands of miles away, and not the wholesaler, the retailer, or some other handler, was responsible for the injury-causing product defect.

Finally, courts developed the theory of strict products liability to cover such situations, and this theory has been widely adopted by state legislatures as statutory law. Under strict products liability, the injured consumer need only prove that a defect in the product made it unreasonably dangerous, and this defect caused his injury. The manufacturer, distributor, and seller of the product can then together be held liable for the consumer's injury, unless they can show that the product was not defective or they had no part in the defect. This change means that the law favors the consumer rather than the manufacturer.

There are three kinds of defects possible: (1) manufacturing defects, (2) warning defects, and (3) design defects. A manufacturing defect occurs when the product is dangerous because it was not made the way it was supposed to be made. For example, assume that weak screws securing an electric saw fail, causing the tool to fly apart, and the flying pieces then strike and injure the operator. The injury is caused by a manufacturing defect because the screws were not as strong as originally designed. In contrast, a warning defect occurs when a court finds that the product is dangerous by its own nature and the manufacturer should have warned the consumer about that danger. One famous (or infamous) example of a warning defect case is the one involving an older woman who suffered burns when she spilled McDonald's coffee on herself—the jury found that the warning on the cup was not large enough. The third kind of defect is a design defect, which is when the manufacturer should have used a safer design rather than the one that injured the plaintiff. In design defect cases, courts use the same kind of risk/burden analysis used in determining whether a crime committed on business premises was foreseeable. In the case of a design defect, the question is one of balancing the gravity of the danger posed by the existing design against the cost and feasibility of an improved design. If the danger of the harm is greater than the cost of an improved design, then the design is defective and the manufacturer is liable.

In developing the doctrine of strict products liability, courts balanced the interests of individuals of limited means and sometimes serious, debilitating injuries against manufacturers' economic interests. Three policy reasons justify the doctrine: (1) the cost of the medical injuries may be overwhelming to the consumer, and the manufacturer is better able to bear that cost; (2) of the two, the manufacturer is better able to prevent the defect, and the possibility of facing liability for consumer injuries encourages manufacturers to do so, and (3) the costs of such awards and increased insurance premiums bought by manufacturers can be distributed to the public through higher prices.

Environmental Protection

Another legal and ethical concern of business is its effect on the environment. In 1970, the U.S. Congress created the Environmental Protection Agency (EPA) and passed a series of laws protecting the environment. Over the years, federal, state, and local laws have added to this basic structure, creating the most comprehensive system of environmental protection laws in the world. Some of the other major federal acts include the Clean Air Act (setting standards for air quality), the Clean Water Act (designed to gradually end the discharge of pollutants into navigable waters), the Resource Conservation and Recovery Act (controlling the disposal of hazardous waste), and the Comprehensive Environmental Response, Compensation, and Liability Act (creating a federal superfund to finance the cleanup of toxic waste sites).

Originally, many of these regulations primarily employed injunctions and penalties to force businesses to reduce or stop emissions deemed unacceptable. However, over time, critics criticized the network as complex, expensive, inflexible, and unproductive. They argued that the costly regulation, focused on punishing businesses it perceived as polluting, was making American firms less competitive globally and was inefficient. The same critics further argued that the goal of reducing pollution would be better met by encouraging companies to reduce emissions through profit motives rather than purely through penalties that become incorporated into the cost of doing business. In the case of sulfur dioxide emissions, this criticism led to the creation of a trade-reliant permit system used to encourage companies to reduce emissions rather than a penalty system. Companies can purchase allowance permits for emissions at an auction held by the EPA and then sell these permits to other companies. The market in emissions permits has encouraged those companies that are most able to reduce their emissions to do so, and they then sell their allowances to less able companies for a profit.

Environmental concerns are complex, the problems difficult to remedy and sometimes difficult to balance with commercial development. Therefore, the debate continues over the best way to address them. As shown by the emissions allowance permit system, some environmental problems may be best addressed by encouraging technological development.

International Environmental Protection Treaties

The balance between commerce, the environment, and effective law is an international concern, not just a domestic one. In the international context, the United States has ratified some international environmental treaties and rejected others. Thus, while the United States has long adopted and enforced the Cites treaty protecting wildlife around the world, it rejected the Kyoto Accord on climate change. Under the Kyoto Protocol, which went into effect on February 16, 2005, industrialized nations are required to reduce their emissions of greenhouse gases, which are the product of fossil fuels. Developing nations such as

China, India, and Brazil, however, are not so required. Although the Protocol was originally proposed with the backing of the United States, the Senate refused to ratify it because of a perceived ethical concern—the disparity in treatment between industrialized and developing nations—and President Bush similarly refused to support it. Nevertheless, it came into effect for the signing countries in February 2005.

The Protocol, as originally proposed, requires industrialized nations to reduce their emissions of carbon dioxide to 5% below the 1991 levels by 2012. Complying with the requirements of the Kyoto Protocol presents serious difficulties to some industries. For example, Canada, in switching from utility plants powered by fossil fuels to hydroelectric power, may endanger indigenous sturgeon, a fish once endangered by water pollution and carefully brought back. However, as enacted in 2005, the treaty includes provisions for emissions trading markets, enabling industries to buy and sell emissions credits in much the same way that the sulfur dioxide permits operate. As a result, global investors are beginning to develop new insurance products to handle the risks created by global warming and also developing investments in clean technology because they see its profit potential.

Workers' Remedies

A great deal of law has been developed to protect workers from ethical violations in the workplace: There are laws to protect against unsafe working conditions, workplace discrimination, and invasion of privacy and now a ban on retribution for whistle-blowing.

Safety in the Workplace and Workers' Compensation

Traditionally, there has been little consensus in the United States regarding the appropriate balance between risk and security in the workplace. Overregulation stifles competition and detracts from efficiency, yet because of the excesses of unethical business practices in the latter part of the 19th century, the state now has some role in mandating that employers compensate workers injured in the workplace. In addition to the workplace safety standards set by the Occupational Safety and Health Administration of the U.S. Department of Labor, workers' compensation provides a way to compensate workers who are accidentally injured on the job, through a no-fault recovery system. Under such state systems, employers regularly pay a certain amount into the system, and their injured workers then receive compensation quickly without having to prove that the employer was at fault. In exchange, the employer is assured that the injured worker is limited to compensation under the state workers' compensation act and may not sue the employer for more. The workers may receive less than they would from litigation, but they are assured of receiving it. However, while worker's compensation schemes limit employer liability, an injured worker is still free to sue other potential defendants, such as the manufacturer of the equipment that caused the injury, under strict products liability.

Antidiscrimination Law

Discrimination is another legal and ethical concern in the business world. In addition to laws mandating safety standards, federal law also bans discrimination on the basis of race, color, religion, sex, or national origin. The equal protection provision of the Fifth and Fourteenth Amendments to the United States Constitution prohibits governments from denying any person within their jurisdiction the equal protection of law and is the foundation for antidiscrimination laws. These amendments require the government to treat different groups of people similarly situated in the same way; however, they do not require the same of private citizens and businesses. After the protests against segregation in the 1960s, Congress passed comprehensive civil rights legislation that addressed discrimination on the part of private businesses and individuals. It outlawed discrimination in public accommodations (hotels, motels, restaurants), housing, public education, federally assisted programs, and employment. Title VII, the provision dealing with employment, bans not only outright differential treatment but also practices that appear to be neutral but that disproportionately disadvantage members of one race, sex, or religion.

Sexual Harassment

Laws against sexual harassment have identified two types of illegal sexual harassment: quid pro quo and hostile environment. Quid pro quo refers to demands for sexual favors with threats attached: The victim either gives in and provides the favors or loses a tangible job benefit. Hostile environment refers to behavior that creates an intimidating or abusive workplace atmosphere. The Supreme Court, in 1999, held that Title VII protects men as well as women and that the fact that both plaintiff and defendant are of the same sex does not necessarily prevent a claim of sex discrimination. While sexual harassment is unethical and illegal, as a practical matter, society must recognize that the workplace is a realm that can be alive with personal intimacy and sexual energy. People who work together come into close personal contact, and close personal contact can lead to interactions with sexual overtones without constituting either discrimination or harassment. Thus, the law is structured in an effort to sort between legitimate claims of sexual harassment and nonoffensive interactions.

The Age Discrimination in Employment and Americans with Disabilities Acts

Since the passage of Title VII, additional types of discrimination have been made illegal, specifically discrimination on the basis of age or disability. The Age Discrimination in Employment Act (ADEA) protects individuals who are 40 years of age or older from employment discrimination based on age. The ADEA's protections apply to both employees and job applicants, making it unlawful to discriminate against a person because of his or her age with respect to any term, condition, or privilege of employment, including hiring, firing, promotion, layoff, compensation, benefits, job assignments, and training. The Americans with Disabilities Act makes it illegal to discriminate against an individual who with reasonable accommodation can perform the essential functions of an employment position that the individual either holds or desires. Reasonable accommodation can include making the existing facilities used by employees readily accessible to and usable by individuals with disabilities and restructuring the job to accommodate the individual. In determining whether an individual with disabilities can perform the job, consideration is given to the employer's judgment as to what functions of the job are essential and can be determined by any written job description.

Wrongful Discharge and Whistle-Blowing

Traditionally, most employment is considered to be *at will,* meaning that either the employee or the employer can terminate the employment at any time for a good reason, a bad reason, or no reason whatsoever. Thus, in the United States, as opposed to other countries, there are very few grounds for wrongful discharge. One exception to this rule is quid pro quo gender discrimination. A new exception is whistle-blowing: the SOX prohibits any publicly traded company from discriminating against any employee who lawfully provides information or otherwise assists in an investigation of conduct that the employee "reasonably believes" constitutes a violation of federal securities laws. The intent of this new law is to encourage corporate insiders to report fraud and help prove it in court. However, the practicality of this new provision has been questioned. To begin with, the new law cannot guarantee shelter for whistle-blowers: It may be difficult for the whistle-blowing employee to prove indirect retaliation. In addition, the statute affords protection only for whistle-blowers who report securities fraud, and while this is a very broad area because it refers to any falsity on any public statement or document filed with the SEC, other kinds of whistle-blowing remain relatively unprotected. Under the new Sarbanes-Oxley provision, winning a reprisal lawsuit against an employer has risen, but only to between 25% and 33%, which means that a corporate employee is still unlikely to win such a lawsuit. In general then, in deciding whether or not to blow the whistle, an employee is still likely to face a difficult choice between his or her conscience and continued employment with that particular company.

Privacy Concerns

Because of past unethical behavior, laws prohibit certain unsafe conditions in the workplace, prohibit discrimination and sexual harassment, protect whistle-blowers, and provide no-fault compensation when employees are injured on the job. A current issue that may lead to new law concerns employee privacy. Employers want to find out if their workers are productive and loyal, but employees need a degree of privacy to thrive. Companies want to know the preferences of potential customers or the strategies of competitors, but customers may not want their preferences sold from company to company, and competitors will want to protect their trade secrets. Tension between privacy and the need to know is increased as a result of computer technology, because information gathering has never been so fast, efficient, or omnipresent.

Employees' Expectations of Privacy

The Constitution does not expressly protect a right to privacy. The Fourth Amendment protects citizens from "unreasonable searches" by the government, but there is no constitutional protection against searches or surveillance by private corporations. However, intellectual property laws and contracts protect individuals' and companies' property rights in inventions (patents), creative products (copyright), and trade secrets. In contrast, however, employees may have a hard time objecting to employers monitoring their workplace e-mail messages. Employees may claim that electronic monitoring by their employers amounts to an intrusion—the tort of invasion of privacy; however, this tort requires that the means used to intrude must be an obnoxious deviation from the normal, accepted means of discovering the relevant information and the reasons for the intrusion must be unjustified. Courts have held that employees do not have a reasonable expectation of privacy in e-mail communications voluntarily made by them over the company e-mail system, especially when the communication is made to a supervisor. Similarly, an employer may legally film its employee to demonstrate that the employee is fit and able when that employee is suspected of filing a fraudulent workers' compensation claim.

Consumers' Privacy Expectations

Like employees, consumers' privacy rights can be limited in some respects as well. For example, in the United States, consumers' ability to prevent companies from selling information about them may be limited, even if the company promises not to sell information about its customers to nonaffiliated third-party vendors. For example, in one case, Chase Manhattan, despite its commitment not to do so, sold information about its customers' names, addresses, telephone numbers, account or loan numbers, credit card usage, and other financial data. The third-party vendors then used this information to create lists of Chase customers who might be interested in their products or services and contacted them by telemarketing and direct mail solicitations. Chase customers sued under New York's business law, claiming that Chase had violated their privacy and its own promises as well as deceived them. However, because the plaintiffs could not prove that they were actually injured, they lost the suit.

While U.S. law is concerned with protecting citizens from government intrusions, European law is much more concerned with protecting citizens from intrusions by private parties. Under the 1995 European Directive on the processing of personal data, companies must guarantee that the personal data gathered are accurate, up-to-date, relevant, and not excessive. Moreover, the information collected may be used only for the purpose for which it was collected and can be processed only with the consent of the subject. Furthermore, under the 2002 Directive on Privacy in the Electronic Communications Sector, which builds on the 1995 legislation, companies doing e-commerce with citizens in the European Union must protect their customers' data, erase the data automatically, and obtain their customers' consent before using the data to market electronic communication services. Thus, in Europe, selling information about customers the way Chase did would be unlawful. Because of the difference between U.S. and European privacy law, under a bilateral treaty designed to resolve this difference, U.S. companies doing business with European customers must comply with *safe harbor* provisions: Among other requirements, they must notify their customers if they are collecting information electronically, give customers the option not to have that information sold, and take measures to ensure the accuracy of the information transferred.

Securities, Trade, and Antitrust Law

Much of the previous discussion has been focused on how individuals in a business can be affected by law. However, companies themselves can be held liable for unethical, illegal, and even criminal behavior as it relates to other companies or individuals. Securities, trade, antitrust, and intellectual property laws hold companies to certain legal standards of ethical business behavior.

Securities Laws

Securities laws, developed after the stock market crash of 1929, require that publicly traded companies provide shareholders and potential shareholders a substantial amount of financial and other information about themselves. The underlying rationale is that the required transparency discourages fraudulent behavior by companies, gives potential investors some rational basis on which to decide to invest, and creates public confidence in the stock market so as to avoid similar widespread market failure. Since the creation of the securities laws and the Securities and Exchange Commission in the early 1930s, publicly traded companies have been subject to ever-increasing levels of corporate compliance, and hence increasing costs, as new laws, such as the SOX, are passed in reaction to new scandals. In the long term, such requirements may become so cumbersome that companies may decide not to go public. For example, the pre-SOX annual cost of compliance was approximately \$91,000 per company. After SOX, the average cost of compliance increased to approximately \$3,507,000. As a result, a number of companies, both U.S. and foreign, delisted themselves from American exchanges, choosing to be traded on the London or Hong Kong exchanges instead. In the future, to avoid such consequences, policy makers may consider the potential effect of any additional compliance requirements on the various American exchanges.

Trade Law

Trade law is focused on two goals of public policy: first, that competition is to be encouraged because it leads to more and better products and, second, that technological developments can be encouraged only if the developer is allowed to make a profit before competition ensues. Under the international standard set by the 140 members of the World Trade Organization (WTO), freer trade and importation, as demonstrated by the lowering of customs duties and other barriers, are encouraged. However, under U.S. and international law, an industry can ask that customs duties be raised, thereby discouraging competition from imported products, when it has been subjected to unfair trade practices and thereby rendered unprofitable. Specifically, customs duties may be raised when an imported product's low price is the result of dumping (selling below the cost of production) or subsidization (artificially low production costs caused by governmental grants in the home country) or when a weak or fledgling industry needs to be temporarily protected and safeguarded from foreign competition until it can strengthen itself.

Antitrust Law

A monopoly or trust is a concentration of wealth and power over an industry in one company or group of companies that have agreed to maintain certain price structures for their products or have otherwise taken steps to minimize competition. Because these kinds of arrangements minimize or obliterate normal marketplace competition, they cause markets to stagnate and discourage development of new products and services. To prevent the creation of such monopolies, Congress passed the Sherman and Clayton Antitrust Acts. When a company has become so powerful that it prevents competition from developing, it may be broken up or otherwise prohibited from certain business practices under these Antitrust Acts. In 2001 to 2002, Microsoft faced major antitrust litigation in both the United States and Europe. The U.S. claim was that Microsoft illegally tied its Web browser software to its operating system software, thus preventing competition from other browsers. The suit was eventually settled. Similar claims in Europe and South Korea resulted in rulings that Microsoft had abused its dominant position and must change its business practices by allowing competing media players and servers to interface with its operating system. As of 2006, Microsoft has agreed to uniformly license its operating systems and allow manufacturers to include competing software.

Intellectual Property

One of the reasons why the Microsoft cases were both intriguing and difficult to decide is that they revolved around copyright law. Patents, copyrights, trademarks, and trade secrets are all forms of intellectual property, which provides inventors and developers with a monopoly over their invention for a certain period of time. The reason such monopolies are tolerated is because such innovations are unlikely to be made without a profit incentive. Especially with patents or software, the development of a new invention may involve a great deal of research and development cost. Intellectual property laws allow the owner to recoup research costs and make the first profit before allowing other parties to compete.

Trade secrets include information that helps keep a business competitive and are protected only if the company that developed them takes specific measures, such as nondisclosure agreements, to protect them. Examples of trade secrets include customer identities and preferences, vendors, product pricing, marketing strategies, company finances, manufacturing processes, and other competitively valuable information.

While trade secrets are protected under state law, patents, copyrights, and trademarks are registered and protected under federal law. A patent gives an inventor the right to exclude all others from making, using, importing, selling, or offering to sell the invention for up to 20 years without the inventor's permission, though there are some exceptions and extensions. Patents protect technological inventions, such as pharmaceuticals. Copyrights protect works of authorship, such as writings, music, and works of art that have been tangibly expressed. The Library of Congress registers copyrights, which last for the life of the author plus 70 years (95 years from publication in the case of works made for hire). Trademarks protect words, names, symbols, sounds, or colors that distinguish goods and services. One example of a trademark is the Nike "swoosh." Unlike patents and copyrights, trademarks can be renewed forever as long as they are being used in business. Software, such as Microsoft's browser system, is copyrighted. Thus, in the 2002 case, the claims were that Microsoft had manipulated its copyrights in such a way as to prevent all competition and, in so doing, had become monopolistic.

International Trade Law

As has been seen, the tension between encouraging competition and encouraging innovation has resulted in two bodies of law, antitrust and intellectual property. Writ large, the same tension has been taken into the international arena through various treaties. The WTO, founded by the General Agreement on Tariffs and Trade (the GATT treaty), is aimed at increasing competition worldwide by encouraging countries to lower duties and taxes so as to allow imports to compete in domestic markets, thus forcing domestic products to lower prices and improve quality. In conjunction, the World Intellectual Property Organization encourages countries to protect the copyrights, patents, and trademarks of imported products. Both organizations recognize that these goals are more difficult for developing countries than for already industrialized nations.

—Nadia E. Nedzel

See also Age Discrimination; Antitrust Laws; Business, Purpose of; Business Ethics; Civil Rights; Common Law; Confidentiality Agreements; Emissions Trading; Employee Protection and Workplace Safety Legislation; Freedom of Contract; Free Trade, Free Trade Agreements, Free Trade Zones; Gender Inequality and Discrimination; Greenhouse Effect; Individualism; Intellectual Property; International Business Ethics; Kyoto Protocol; Loyalty; Price-Fixing; Relativism, Moral; Restraint of Trade; Sarbanes-Oxley Act of 2002; Securities and Exchange Commission (SEC); Shareholder Wealth Maximization; Tax Incentives; Virtue; Virtue Ethics; WorldCom; World Trade Organization (WTO)

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Business Roundtable

The Business Roundtable is the leading association representing the interests of big business in the United States. Founded in 1972, the Roundtable derives its strength from its organizational structure. As opposed to most other Washington, D.C.–based industry and trade associations, the Roundtable maintains a very small staff. Its policies and activities are driven by its membership—in this case, chief executive officers (CEOs) of 150 to 200 of the largest corporations in the United States.

The Roundtable was the result of a merger of three other big business associations. The Construction Users Anti-Inflation Roundtable and the Labor Law Study Group represented major U.S. corporations in the late 1960s and early 1970s, when the foremost concerns of big business were the increasing costs of labor (particularly in construction) and the political activities of labor unions, which were attempting to strengthen their protection under federal labor law. Following the passage of a series of laws and the creation of new federal regulatory agencies in areas such as consumer protection, environmental protection, worker safety, and employment discrimination, a third association—the March Group—was formed to counter what CEOs perceived to be a decline in business political power.

The consolidation of these three groups was intended to (1) decrease fragmented political power among conflicting industries, (2) educate big business on the new politics of regulation in the 1970s, and (3) coordinate big business political activities. It achieved these goals by restricting Roundtable membership to CEOs of only the largest companies and maintaining the locus of the decision-making and political activities in the hands of the CEOs themselves.

Within a few years, the Roundtable had demonstrated its organizational and political success by leading the efforts to defeat a proposed Consumer Protection Agency, to rebuff labor efforts to amend federal labor law, and to reduce corporate taxes. In the early 1980s, the Roundtable devoted its energies toward reducing federal regulation and addressing the concerns of increasing federal budget deficits. By the mid-decade, corporate CEOs found themselves under attack by agency theorists, who blamed the decline in the U.S. economy on the strategic decisions of U.S. corporations. Aided by institutional investors and armed with a politically accepted finance theory, leverage buyout companies formed to challenge CEOs in the "market for corporate control" by threatening to take over and dismantle corporations. The Roundtable counterattacked by lobbying state legislatures and acquiring protection from what they characterized as "hostile" takeovers and testifying before Congress that these takeover threats posed real dangers to the U.S. economy.

In the mid-1990s, the Roundtable found its political power waning in the midst of Republican congressional victories. Congress, the House of Representatives in particular, was more politically in tune with the interests of small rather than big business. The Roundtable was displaced by the National Federation of Independent Business as the leading pan-industrial political association. Responding to this weakening of its political power, the Roundtable refocused its activities to support the policies of the congressional leadership and the Bush administration. In doing so, it reacquired its political status and success.

The Roundtable was not only heavily involved in the political debates over corporate governance in the 1980s and 1990s, but it played an important role in the philosophical debates as well. In 1981, the Roundtable advocated what became the definitive stakeholder model of the corporation, with managers balancing the interests of the various corporate constituencies. By 1997, the Roundtable's CEOs had redefined their "paramount role" as serving the interests of shareholders, whom they now claimed were the "owners" of the corporation.

—Ernie Englander

See also Leveraged Buyouts

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CAFE Standards

See Corporate Average Fuel Economy (CAFE) Standards

Campaign Finance Laws

Campaign finance laws govern the amounts of money candidates or parties may receive from individuals or organizations and the cumulative amounts that individuals or organizations can donate. These laws also define who is eligible to make political contributions and what sorts of activities constitute in-kind contributions.

There have been three major periods of campaign finance regulation in the past century: the era before the Federal Elections and Campaigns Act (FECA) of 1971 and its subsequent amendments; the era from 1974 to 2002, when FECA regulated campaigns; and the current era, following the enactment of the Bipartisan Campaign Reform Act (BCRA) of 2002.

Before FECA, campaign finance laws were mainly addressed to particular types of contributors. By 1947, federal employees, corporations, and labor unions were barred from making contributions to candidates. Unions and corporations responded by forming political action committees (PACs), which aggregated voluntary contributions by individual members or employees.

The FECA of 1971 established limits on candidate spending; on the contributions of individuals and PACs to candidates, parties, or political committees; and on the amount of money candidates could spend on their own campaigns. FECA also established a public funding system for presidential campaigns, financed through a voluntary income tax checkoff. FECA created the Federal Election Commission (FEC) to enforce and clarify campaign finance laws.

In its 1976 *Buckley v. Valeo* decision, the Supreme Court ruled that restrictions on candidate spending and candidate self-financing violated the First Amendment. The Court allowed the limits on spending in presidential campaigns to stand because these limits were contingent on receipt of public funds. And the Court upheld the limits on contributions from individuals or PACs; thus, from the passage of FECA in 1971 until 2002, individuals were limited to contributing no more than $1,000 to a candidate, up to a total of $25,000, and PACs were limited to contributing no more than $5,000 to a candidate.

Many have contended that FECA abetted the development of PACs and increased the reliance of congressional candidates on PACs. FECA has also been said, however, to have reduced the reliance of candidates on individual donors or organizations. That is, because of the contribution limits, it is unlikely that any one donor or organization will contribute enough to a candidate to have an influence on that candidate's campaign. At the presidential level, FECA also restrained spending. All major party nominees abided by FECA's spending limits in their primary campaigns from 1976 through 1996, and public funding of general election campaigns ensured that candidates could not outspend each other.

During the 1990s, two major developments took place that, according to many politicians, undermined FECA's restrictions. First, although corporations and labor unions cannot make direct contributions to candidates, FECA did not prohibit them from contributing to political parties as long as this money was used for “party-building” activities. During the 1990s, political parties began to solicit “soft money” donations from corporations, labor unions, and wealthy individuals. Because these funds were not distributed by the parties to candidates or used to advocate the election or defeat of a candidate, they were not subject to contribution limits. Second, recall that FECA limited the ability of individuals and organizations to spend money in a coordinated fashion with a campaign. The FEC has interpreted this as a prohibition on advocacy that explicitly encourages voters to vote for or against a candidate. Yet, during the 1990s, several advocacy organizations began to advertise heavily on television, describing candidates in a manner virtually indistinguishable from a candidate’s campaign advertisement but without using “magic words” such as “support” or “oppose.”

The BCRA of 2002 was a response to both developments. The two major components of BCRA are a ban on soft money contributions to the national parties and severe restrictions on so-called electioneering advertisements by advocacy groups. These restrictions prohibit organizations that receive corporate or labor funding from broadcasting advertisements that refer to a candidate for election within 30 days of that candidate’s primary election or within 60 days of the general election. BCRA also doubled individual contribution limits and indexed them to inflation. BCRA took effect the day after the 2002 election. In *McConnell v. FEC*, the Supreme Court upheld all the major provisions of BCRA.

As to the soft money ban, some students of campaign finance make a distinction between “pushed” and “pulled” money. “Pushed” money is contributed voluntarily by donors who wish to advance an ideological cause. “Pulled” money is contributed somewhat reluctantly, as a consequence of pressure exerted by politicians on donors. Even prior to the passage of BCRA, many corporations reported that they were becoming reluctant to give soft money contributions to the parties but felt pressured to do so by members of Congress. As a consequence of BCRA’s prohibition on soft money, giving by many corporations, particularly publicly held corporations, declined substantially in 2004. Many individual business CEOs contributed large sums to “527” organizations, organizations independent of the parties that engage in advertising, voter registration, and voter-mobilization activities. Business PACs also grew, though not at a rate larger than the increase across previous election cycles.

BCRA’s advertising restrictions would have prohibited millions of dollars in advertising by peak business organizations, such as the Chamber of Commerce and the Business Roundtable, and industry-specific organizations, such as Citizens for Better Medicare and the United Seniors Association, had they been in place from 1996 to 2002. By 2002, however, the broader peak organizations had already begun to limit their advertising, citing the fragmented television market and the increasing efficiency of using the Internet to communicate with employees.

—Robert G. Boatright

See also Interest Groups; Political Action Committees (PACs)

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Canadian Business for Social Responsibility

Founded in 1995, Canadian Business for Social Responsibility (CBSR) is, according to its Web site, a nonprofit, business-led, national membership organization of Canadian companies that have made a commitment to operate in a socially, environmentally, and financially responsible manner, recognizing the interests of their stakeholders, including investors, customers, employees, business partners, local communities, the environment, and society at large. Its vision statement is to be Canada’s leading voice for corporate social responsibility (CSR), harnessing the power of business to create positive change. Its mission statement is to offer practical services and tools to assist Canadian businesses to improve their performance in support of CSR. CBSR members have three guiding principles: (i) implementing and acting on socially, environmentally, and financially responsible policies and practices; (ii) ensuring shared prosperity of shareholders, staff, the environment, as well as local and international communities; and (iii) fostering an exchange of ideas and information within the business communities.

There are three types of members of CBSR: founding members, sustaining members, and regular members. CBSR currently has more than 140 members representing many of Canada's largest corporations, small businesses, and entrepreneurs. The members vary in location across Canada, as well as in size and sector.

One of CBSR's primary activities is the provision of advisory services to help organizations achieve their CSR goals. Different advisory areas that are worked on by CBSR include the following: board and senior executive engagement, research and benchmarking, CSR assessments, stakeholder engagement, CSR strategy and planning, training and education, management tools and systems, and policy and program development. CBSR's advisory services attempts to help companies answer the following four questions: (1) How do you engage your employees in CSR, from frontline staff to senior executives? (2) How do you develop your "random acts of goodness" into a strong and cohesive CSR strategy? (3) How do you communicate your CSR achievements internally and externally? (4) How do you develop the business case for CSR in your company?

CBSR also engages in a number of other projects and activities each year, including the hosting of conferences developing CSR tools and methodologies, as well as the provision of CSR research reports. Examples of some of CBSR's current or past projects include the following: Human Rights: Everyone's Business, Building Sustainable Relationships: Aboriginal Engagement and Sustainability, and the Small and Medium Size Enterprises Program.

The organization takes a collaborative approach to its activities and has entered into partnerships with a number of other CSR-related organizations from around the world including international CSR networks, government agencies, industry associations, educational institutions, the media, and nongovernmental organizations. For example, CBSR considers the U.S.-based Business for Social Responsibility to be one of its many partners. CBSR has offices in both Vancouver, British Columbia, and Toronto, Ontario.

—Mark S. Schwartz

See also Business for Social Responsibility (BSR)

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Canadian Business for Social Responsibility (CBSR) [Web site]. Retrieved from www.cbsr.bc.ca

Capabilities Approach

In general, organizational capabilities are categorized in one of three different ways. First, capabilities reflect an ability to more efficiently perform a basic business function (e.g., distribution, marketing activities, operations, logistics, etc.) compared with rivals. For example, Nike has significantly better global brand management than its competitors and has developed extensive competitive capabilities around its brand. Continuously improving the dynamics of interactions is a second type of capability—dynamic capabilities. These types of capabilities focus on the learning associated with repeated and recurring activities. For example, going beyond expectations in customer service responses by anticipating questions or designing next-generation products/services from information gleaned from customer responses is a dynamic capability. Another dynamic capability is the rapid development of bringing ideas to the marketplace. The third category of capabilities enables firms to recognize intrinsic value or develop novel strategies before others. Schumpeter's creative destruction is an example of the third type of capabilities, which is closely tied to cognitive and creative abilities of management and leadership.

Each of these three types of organizational capabilities (static, dynamic, creative) deploys resources to effectively compete against rivals and create a new vision of the future. The ability of competitors to learn and duplicate a firm's existing capabilities depends on the sustainability of the competitive advantage of the capability. A highly imitable capability such as outsourcing to lower-wage countries is not likely to create an advantage for a long period of time. Highly inimitable capabilities, such as personal networks among the top management with elite politicians or understanding the political relationships of employees or the commitment of retirees for effective grassroots lobbying, on the other hand, may create longer-term sustainable advantages. Overall, capabilities based on rare, valuable, or inimitable resources are best for creating sustainable competitive advantages.

For example, when John Deere, Caterpillar, or Komatsu are developing contracts with governments in developing countries, a capabilities approach for these manufacturers of large, earth-moving machines might emphasize infrastructure development. Infrastructure development reflects dynamic and creative capabilities. Dynamic capabilities can be derived from the web of networks and relations with rivals, nongovernmental organizations, and governmental officials for concomitant development of banks, legal systems, regulatory oversight, utilities, telecommunication systems, and so on. By creatively providing inimitable capabilities in addition to earth-moving tractors, John Deere, Caterpillar, or Komatsu can add value, distinguish themselves from competitor's bids, and bring better long-term consequences by creating and managing relationships with outside stakeholders. Rather than competing as manufacturers of earth-moving machines, these firms can extend their product offerings with relational and creative capabilities. Likewise, Cisco Systems or Microsoft uses a capabilities approach by building literacy and computer skills in local neighborhoods and by making computers and software systems available to developing countries. By extending their product offerings by building literacy and computer skills and interacting with policy makers on contentious topics such as privacy, Microsoft and Cisco Systems have the ability to improve living conditions, help eliminate poverty through jobs, and potentially increase demand for future generations of their products/services while creating more stable business conditions and employment opportunities.

By focusing on what firms do extremely well, a capabilities approach encourages development of those activities, processes, and inimitable resources in related areas. Extending the processes executed efficiently and creatively to new contexts, new audiences, and new products can create new markets and improve the long-term economic rents of firms. New contexts might be to different countries or different regions of the world. New audiences might include disadvantaged consumers, the public sector, not-for-profits, or nonprofit trade associations. New products could be extensions of existing product line or unrelated diversification.

Capabilities are embedded within the routines of business activities. That is, a capability cannot be readily isolated and removed from the business. An added value of the product/service is the firm's capability, and the capabilities are a result of the ongoing learnings from the creation, distribution, or consumption of the product/service. Unfortunately, capabilities are often seen as the way to get the product/service sold rather than as a distinguishing feature requiring resources and thoughtful management.

The more valuable the capability the less likely the capability can be exactly duplicated in another firm. For example, Toll Brothers' ability to build seemingly similar large-scale houses in a short time frame is a capability that is currently being duplicated by its competitors in tract housing. As demand for new houses based on a limited number of choices continues, this new capability will likely become more widespread. Easy duplication of Toll Brothers' track-housing skills (a static capability) renders their initial advantage obsolete. Similarly, readily available and cheap worldwide labor sources capable of reproducing accurate data entry/data management activities are changing the competitive structure of many industries. Data management and international call centers are currently core capabilities in some firms operating in low-cost, labor-rich countries.

—Jennifer J. Griffin

See also Developing Countries, Business Ethics in; Global Business Citizenship; Strategic Corporate Social Responsibility; Sustainability

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Capabilities Approach to Distributive Justice

One of the central claims of the capabilities approach is that when people are situated differently and have different levels of needs and expectations, certain rights-claims can be better understood as claims regarding equal level of capabilities to function than simply, for example, the equal rights to resources, which may turn out to be unequal in real terms. Thus, one important idea of this approach to distributive justice is to enrich the discourse on equality by reframing the notion of human rights from being empty rhetoric of entitlements to ideas concerning institutional and material arrangements that are conducive to achieving a certain measure of a full human life. The approach has been developed by Harvard economist and philosopher Amartya Sen and later endorsed and expanded by the University of Chicago law professor and ethicist Martha Nussbaum. For Sen and Nussbaum, seeing rights as capabilities has some helpful advantages in that it indicates that all human rights have broader economic and social dimensions because the capabilities approach emphasizes the actual ability to do or to be. The rights talk in itself does not clarify what is needed to make those rights a reality unless they are understood as securing effective measures to make people capable of appropriate functioning in those areas involving needed material and institutional support. It is thus not helpful to rely on the usual distinction between political and civil rights on the one hand and economic and social rights on the other. Another advantage of the capabilities language over rights talk is that because functioning of the central human capabilities is culturally neutral and sufficiently universal, cross-cultural agreement on basic entitlements is easier to obtain than when the politically and culturally loaded concept of rights is used.

The capabilities approach agrees with John Rawls in not accepting the amount of material wealth for a country (the analog of the gross national product per capita as the model for a country's development or prosperity) or the utility principle for assessing quality of life or human development, as these measures fail to adequately account for the fairness issues in distributive justice. John Rawls, the Harvard political philosopher, is credited with the most influential formulation of the notion of distributive justice in recent times. Rawls defended liberal egalitarian principles of justice among fellow members of a single society as the social contract that would result from hypothetical deliberations in which members of a society assumed to be self-sufficient seek to pursue their individual interests in ignorance of the nature of their goals and resources. This conception of justice, known as justice as fairness in contemporary political philosophy, stipulates that in a just society people should have equal access to social advantages that, in Rawlsian terminology, are primary social goods such as liberty, opportunity, and wealth, unless an unequal access or distribution is to everyone's advantage. Because capabilities approach specifies that capabilities are integrated together for maximal human functioning, both Sen and Nussbaum claim that the Rawlsian primary goods should be understood in terms of central human capabilities. This way, it gives the Rawlsian conception the latitude it needs without making it too thin or abstract.

Nussbaum goes on to argue that the capabilities approach provides a better account of the need, dependency, and vulnerability of many real people than the account of needs conveyed by the notion of primary goods of imaginary contracting parties in the Rawlsian scheme. Accordingly, though Nussbaum's position is close to Rawls's in many ways, she claims that her capabilities approach can overcome certain deficiencies in the Rawlsian notion of social justice. Sen, on the other hand, claims that because capabilities are certain indicators of individual functioning and opportunities only, they cannot adequately account for the fairness or equity of the process involved in justice. Accordingly, for Sen, the bigger arena of justice, where priority of liberty and procedural equity matters, is outside the reach of the capabilities approach.

Nussbaum is more optimistic about the justice implications of her capabilities approach, and this is where she challenges Sen over the issue of endorsing a list of basic capabilities as essential requirements of social justice. Sen is reluctant to endorse a predetermined set of basic capabilities that is not context specific because the capabilities approach allows significant latitude in interpretation and implementation. Underlying this difficulty on his part is his insistence on the need for public reasoning for the validation of rights as capabilities. Given the importance of unobstructed public reasoning in a democracy and the open-ended nature of capabilities, Sen would not like to see a fixed list of capabilities unduly influence the tone and direction of civic discourse that is vital for the evolving social judgment and policy assessments in a democracy. The discourse should be open and have as broad a reach as possible, both for objectivity and fairness. For Sen, public discourse is vital for democracy. Capabilities themselves depend on it, emerging from and being shaped by it, so any theoretical list shouldn't be allowed to preset the tone of the debate.

Unlike Sen, Nussbaum is more insistent on listing a core group of capabilities as valid and applicable through all cultures. Instead of regarding such a list as a denial of the reach of democracy, she believes that her list should be a challenge to all democratic regimes to take rights talk seriously. Nussbaum claims that her capabilities approach offers great potential in deciding on the fundamental constitutional entitlements for citizens in a just democratic state—entitlements that can be put together in constitutional guarantees. It starts with the broad idea of human dignity—an idea that is foremost in many modern liberal democratic constitutions—and then goes on to include a list of 10 capabilities as key ingredients of a rich plurality of life activities that constitutes a life with dignity. The list includes the central human capabilities such as life, bodily health, bodily integrity, emotions, practical reason, social and political affiliations, leisure, and material resources, which, for Nussbaum, better convey the sense of a flourishing human life than a list of negative and positive rights that do not take into account the totality of a full life. A just society must secure for all its citizens each of the 10 capabilities up to a threshold level as constitutionally guaranteed basic entitlements. Nussbaum's list of fundamental entitlements broadly covers the same domain of liberties that features prominently in the discourse on human rights in international politics. Also, Nussbaum views her list of central capabilities as essential requirements of justice, in the sense that the denial of any one of the capabilities on the list is a matter of urgent concern and subject to appropriate judicial review.

Nussbaum thinks that there is considerable tension between Sen's insistence on a strong priority of certain capabilities as fundamental entitlements of all people everywhere and his generic endorsement of capabilities as freedom, without saying which freedoms are important and which ones lack merit, which are socially desirable and which not. Nussbaum acknowledges that public reasoning is crucial in understanding and implementing the range of capabilities in different cultures, and she leaves room for that discourse in her list, which is thick but left open-ended regarding the viability of specific functionings. Just as the broad language of human rights justifiably leaves room for latitude in local interpretation and implementation beyond a certain threshold level, Nussbaum likewise asserts that the threshold levels of the fundamental capabilities are set in different constitutional traditions according to their own history and current possibilities. She nonetheless is left wondering how Sen can avoid evaluating human freedoms and not endorsing a core list of capabilities if he were to embark on a coherent social and political conception of justice. If a constitutional democracy tries to pursue a reasonably just political order, its constitution has to specify, as a minimum requirement of justice, certain freedoms or capabilities as basic entitlements for its citizens.

Firms operating abroad cite the beneficial effects of their business on the country's economy, including opportunities for economic growth. However, the message of the capabilities approach for these companies would be that they need to be concerned with the capabilities of their workers to lead a good measure of meaningful human life, which is the best guarantor of productivity consistent with the well-being of the workers and the society in which they live. This means that international business should operate on a different notion of productivity than the one understood only in terms of material resources and utility. From a capabilities perspective, firms doing business at home and abroad need to include a growth model in their business operations that would emphasize sustainability rather than just material productivity. Otherwise, the global acceleration of a consumer culture would endanger environmental qualities, clash with cultural values, and widen the gap between the rich and the poor. All this is detrimental to an equitable approach toward distributive justice.

—Deen K. Chatterjee

See also Capabilities Approach; Development Economics; Human Rights; Justice, Distributive; Rawls, John

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CAPITALISM

Capitalism is a system of economic organization, based on private property and freedom of enterprise and contract, in which decisions are coordinated not through coercive mechanisms but through the market. "Economic systems" is the name we give to the different ways in which economic decision making may be organized in a society. Such systems try to answer questions such as what goods and services to produce, how much of each good or service to produce and in what way to produce it, how to distribute the output among all those who have contributed to producing it, how to ensure that the standard of living of the population steadily improves, and so on. And all that has to be done under the real-life conditions of scarcity, ignorance, and uncertainty.

Throughout history, various economic systems have been developed: the tribal economy, feudalism, the planned economy or communism, capitalism, and so on. Intermediate types, displaying features of different systems, have also appeared, such as the war economy and many varieties of mixed economies. Following the crisis of communism, the dominant system has been capitalism.

The Capitalist System

The above definition encapsulates the distinguishing features of capitalism: (1) private property (above all, private ownership of the means of production); (2) the market as the mechanism for coordinating decisions; and (3) freedom of exchange and enterprise for the economic agents vis-à-vis the State and other agents, which implies decentralization of decision making, so that all decisions are made by those most directly affected by them.

The combination of private property and economic freedom gives rise to the incentives that are needed for the agents to base their decisions on criteria of efficiency—efficiency being understood as the achievement of the best possible outcome given the scarce resources available or, alternatively, as the achievement of the desired result using the least possible resources. Under certain conditions, this will lead to a social optimum, by which we mean an efficient allocation of scarce resources to serve goals such as those the agents themselves have freely decided.

The task of coordinating individual decisions is entrusted to the market and the price mechanism. It is assumed that prices contain all, or at least a large part of, the information that the agents need for their decisions to be efficient. Thus, the market performs three broad functions:

1. It is a mechanism for gathering, storing, processing, and transmitting, at minimal cost, information that is scattered among millions of agents who are not even aware that they have it and would not know how to use or share it—a task that no central planning office could ever perform.
2. It promotes and orients incentives so that the agents act as efficiently as possible, minimizing their costs and optimizing their outcomes.
3. It coordinates the decisions of those millions of agents so that their demands and supplies are reasonably well satisfied in time and space, without wastage of resources.

Varieties of Capitalism

The outline given above is the core of the theory of the capitalist system. But just as the market is the product of human action, but not of human design (i.e., it is a "spontaneous" order that arises informally and is continually evolving), capitalism, too, has developed in accordance with specific geographical and historical circumstances: through spontaneous evolution, through reactions to the incentives that have been created, and through the deliberate efforts of the agents.

That is why, in the real world, "pure" capitalism does not exist. Instead, we find numerous variants of capitalism, reflecting the various factors that influence the way in which different societies organize their economic activities. In a sense, it would be fair to say that there are as many capitalisms as there are human communities and historical periods: The capitalism of Germany is not the same as that of Taiwan or Brazil, nor is the U.S. capitalism of the 1950s the same as the U.S. capitalism of the 2000s.

Nowadays, it is common to distinguish between different forms of capitalism. One of them—perhaps the most genuine—is Anglo-American capitalism, represented by the United States, the United Kingdom, Canada, Australia, and New Zealand. Anglo-American capitalism is more individualistic (it assumes that the agents make their decisions based exclusively on their own individual preferences and interests) and more competitive (relations between the agents are more adversarial than oriented toward consensus and negotiation), leaves the agents (persons or organizations) to make their own basic decisions about their future (i.e., it allows only a limited role for the State), puts the emphasis on short-term financial results (as the key to economic efficiency), and concedes an important role to the capital markets.

Another prominent model, which tends to be set in opposition to Anglo-American capitalism, is the continental European model, represented by Germany, Austria, and Switzerland. This model puts the emphasis on the social dimension of decisions (relying on negotiation, agreement, participation, and coresponsibility in decision making), stresses long-term results and social security safety nets that guarantee protection for all citizens (the paradigm for this would be the social market economy, introduced in Germany after World War II), seeks to moderate the free market through a broad array of regulations, and seeks a financial system in which banks play a bigger role than the capital markets. But not all continental European countries fit that model: There are marked differences between, say, France and Germany. There are differences, also, between the Mediterranean countries (Italy, Spain, Portugal, Greece) and the Nordic countries (Sweden, Norway, Denmark, Finland), in which the social security system is far more comprehensive (from cradle to grave), the State plays a much greater role, and incentives also function differently (e.g., when seeking employment).

There is also a Japanese model, which, in its pure form, would include close coordination between economic policy and corporate interests; a system of cross-ownership, forming business groups made up of large companies, their suppliers, and banks; and stable industrial relations, which ensure low labor costs, less conflict, lifetime employment, high productivity, and strong employee loyalty. However, this model is rapidly changing, especially since the 1990s.

It has often been debated which of the various models is the best. There is no one criterion by which to establish an order of preference, so no ranking will be accepted by everyone. In continental Europe, for example, protection of the employment relationship and extension of the welfare state are considered nonnegotiable, so that the apparent advantage of the Anglo-American model in terms of productivity growth is not a conclusive argument.

On the other hand, the ranking of the different models has varied over time. Taking economic growth as a criterion, for example, Europe held the lead in the 1960s, while in the 1980s Japan seemed the model to follow. Since 1995, having achieved only mediocre results in the 1970s, the United States has seen a strong recovery in its growth rate. And now, at the start of the 21st century, China is experiencing tremendous progress. But China is not a pure capitalist economy (nor communist, for that matter); its advantage has a lot to do with the transition from an underdeveloped economy to an industrialized one, although some of its progress is undoubtedly attributable to the introduction of capitalist institutions, markets, and incentives, and the same can be said of some of its problems, such as the growing inequality in the distribution of income and wealth.

Ethical and Social Dimensions of Capitalism

Each generation needs to reach its own conclusions about the social legitimacy and ethical validity of its economic system. Therefore, the fact that the debate on the moral and social aspects of capitalism has been continuing for centuries should come as no surprise. What's more, the same arguments have been put forward time and again. The debate is further complicated when, as often happens, the features of the theoretical or pure model are mixed up with those of capitalism as actually practiced in particular countries and periods.

First of all, it should be pointed out that capitalism is not morally neutral: It is not a purely technical, amoral form of organization but has far-reaching ethical implications. It is possible to describe more or less aseptically how a system works, but moral judgment is somehow inevitable. And from that judgment there derives a set of rules for the system's organization, operation, and results.

To orient our analysis, we must situate the capitalist system within the broader system of society, of which the economic system is a part, whose ideas, values, and attitudes sustain it and whose laws, social norms, ethical precepts, and institutions it shares. In practice, it is impossible to understand capitalism without reference to the society in which it develops. That is why it may be helpful to distinguish between at least four components of any economic system:

1. A complex of ideas and values, from the most elevated (on nature, man, society, happiness, the good) to the popular views and conceptions of daily life, including historical, artistic, scientific, and technical ideas. It is a disordered and often incoherent set in which diverse, even contradictory, ideas and values may coexist. Some are likely to be dominant, but they will change over time in line with trends in the "values market," in which these ideological and axiological sets are forever competing with one another.
2. Prominent within that complex of ideas and values are the philosophical, economic, sociological, and political theories of how the system works or, better, a set of not always consistent theories, based on certain interpretations of man and the community, that explains the incentives, role divisions, and coordination mechanisms in society. Any such explanation will obviously help us to understand the system, but its assumptions will be simplifications of reality, so criticisms of those assumptions cannot be extrapolated to the system.
3. A body of norms and rules (legal, administrative, and social; customs, practices, and cultures) and institutions (market, private property, contracts, money, credit, etc.), which together constitute the formal and informal fabric of society, reflecting its history and its ideas.
4. A system of formal or informal, explicit or implicit incentives that motivate the agents to act in such a way as to achieve their objectives within the framework of norms and institutions.

In an economic system such as capitalism the web of ideas and values, together with certain aspects of the environment (geography, history, endowment of resources, etc.), specifies the norms and institutions. The norms and institutions, in turn, shape the incentives and coordinate the agents' decisions so that they achieve the goals they have set themselves, individually or in groups. Norms and institutions are products of human action, but they may or may not be the result of human design. Insofar as they are the result of human design, a specific role is assigned to collective decision-making mechanisms, especially the ones we know as the State. Now, we are in a position to analyze the problems of social legitimacy and ethical evaluation of capitalism.

The Foundations

As we said earlier, the foundations of capitalism are private property, economic freedom, and coordination through the market. Clearly, our ethical assessment of those foundations will decisively influence our moral and social attitude toward the system as a whole.

1. Capitalism does not flourish in a vacuum but within a legal and institutional framework. A key element of that framework is recognition of the right to private ownership of goods, factors of production, and ideas. Any debate on capitalism starts, therefore, with how to justify that right.

That can be done, for example, by appealing to the principles of justice: People have ownership rights to goods that they have obtained through their own labor or entrepreneurial initiative, or they have ownership rights to goods that they have purchased and possessed peacefully or goods that they need to survive, and so on. Or it can be done by appealing to the principle of freedom: Exercise of private ownership is an indispensable condition for the agent's autonomy. It can also be done by citing natural law, utilitarian arguments, or other reasons that stress the role of efficiency and social welfare: Private property is the best way to conserve and increase material goods and motivate the agents to take personal and social responsibility for their future.

Some authors criticize the individualistic content of the right to private property, as recognized in capitalism, while others accept that right, albeit with limitations (emphasizing the social role of property). In that case, what they are criticizing is not the foundation of the capitalist system as such, but the inadequacy of its legal and institutional system to define property rights appropriately. And there are, of course, those who radically reject the system. Karl Marx, for example, argues that private property constitutes, on the one hand, the right of the capitalist to appropriate the labor of others (the product of their work), and, on the other, the impossibility for labor to appropriate its own product. Therefore, it is a means of abuse of power and, as such, should be abolished.

And Pierre-Joseph Proudhon, on the other hand, declares that all property is theft.

2. The various freedoms that form the foundation of capitalism (freedom of exchange, initiative, labor, contract, etc.) are justified by a variety of principles—freedom, efficiency, moral duties, natural law, and so on.

The freedom that takes center stage in the economic agents' decisions is freedom of choice. Attacks on capitalism are not usually targeted at the principle of freedom as such but at this particular interpretation of freedom, as reflected in legislation, institutions, and the theoretical interpretation of the system. Some authors say that this limited conception of freedom is reductionist and incomplete. Others, while accepting the conception of freedom as being centered in choice, criticize the conditions and limitations imposed on the exercise of that freedom in practice—for example, because the unequal power of the economic agents effectively limits the freedom of those who lack resources or because the huge power of companies and the distortions created by advertising effectively prevent consumers from exercising the sovereignty that the system supposedly grants them.

3. As pointed out earlier, in capitalism the agents' decisions are coordinated through the impersonal market mechanism, not by any planning agency. Efficiency is the main argument used to justify the market. For example, the economic theory of welfare shows that under certain (fairly restrictive) conditions the competitive equilibrium in a free market economy is a paretian optimum, as shown by Arrow and Hahn; that is to say, agents acting to satisfy their personal preferences in competitive markets achieve the efficient coordination of all their decisions, guided by the "invisible hand" invoked by Adam Smith.

And yet the idea of coordination by the market is often criticized. Most of the criticism is technical. In practice, the conditions that must be satisfied for that social optimum to be achieved are indeed very strict: perfect competition in all markets (including cost-free perfect information); existence of perfect markets for all goods, present and future; absence of external effects and public goods; the agents' decisions must be based exclusively on their personal preferences and must not include those of other agents, and so on. Given that those conditions are never met, the capitalist system does not, in practice, yield the excellent results it promises, which is not to say that the alternative systems do any better.

In any case, capitalism operates within a legal, regulatory, and institutional framework, whose task is to channel the agents' decisions so as to achieve economic efficiency, coordinate the agents' decisions, and correct any negative effects that arise when reality does not coincide with the assumptions of the theoretical model. For example, in the absence of perfect competition, it is the task of the legal and institutional system to remedy that shortcoming by promoting "sufficient" competition or by correcting the effects of the lack of competition. Any shortcoming of the system is, above all, a shortcoming of the legal and institutional framework.

The Role of the State

The criticisms of capitalism on the grounds of efficiency demonstrate the need for precisely such a legal and institutional framework to foster the necessary incentives so that agents achieve their goals, their decisions are sufficiently coordinated, and economic efficiency is obtained. This means that in the capitalist economic system there is a role for the State. That role consists, basically, of four tasks:

1. Promoting the legal, regulatory, and institutional framework, that is, formulating laws, regulations, and standards; adhering to them; and ensuring that they are adhered to. That includes developing the institutions that depend on the law. For example, to develop the institution that we call "contract," a legal system has to be created that favors freedom of contract (certainty, legal guarantees, impartiality, etc.) and a judicial system that encourages compliance with those requirements. Note that this is an ethical duty of the State: If the capitalist system is incapable of generating that framework, it will be failing not only in its economic but also in its moral function.

2. Providing public goods. Public goods are goods that may be consumed by one citizen without excluding their being consumed by others. (For example, if police officers patrol a particular street, all the people living in the street will benefit from that service; none can be excluded.) Precisely because nobody is excluded, nobody wants to pay for that good (everyone will think that if the others pay the police to patrol the street, each will be able to enjoy that service at no cost to him or her). That is why, ultimately, the State must take responsibility for providing public goods,

financing them through coercive taxes levied on all citizens. And that, again, is a duty of the State and, therefore, an ethical requirement of capitalism.

3. Correcting external effects. External effects or externalities are the effects that one person or organization's behavior has on another with whom it has no direct relations in the market. For example, the pollution caused by a factory harms local people because the company offloads onto them part of the costs deriving from its activity. In such cases, the State must intervene to limit that external effect by taxing the polluting activity, imposing physical limits on the amount of pollution, and so on. Once again, that is a duty of the State and, therefore, an ethical requirement of the capitalist system.

Obviously, we could draw up a much longer list of possible interventions by the State. The three points mentioned above should be seen as the essential minimum to correct the deficiencies of the market system (so-called market failures) as a mechanism for coordinating decisions aimed at efficiency. Some of the other functions attributed to the State are similar to those just mentioned—for example, provision of infrastructure, roads, railroads, schools, and so on, which have at least some of the characteristics of public goods or help correct external effects. Others, meanwhile, are part of what the State needs to perform its functions—for example, creating the necessary administrative services for the State to carry out its tasks of international representation, justice, defense, public order, and so on. There is one more function, however, that is also very important.

4. Providing a minimum income for citizens. The reason for this function is that agents come to the market to obtain certain goods that they do not possess in exchange for goods and services that they do possess and that they have obtained through natural endowment (their labor, for example), inheritance, or donation or through an earlier exercise of their capacity for work or entrepreneurial initiative. Obviously, the agents' capacity for exchange will be limited by their initial endowments, which may be insufficient to guarantee them a minimum standard of living. Therefore, there will be equity (and also efficiency) reasons for ensuring that each agent has a minimum income, although many authors dispute this argument.

Of course, one may also require the legal and institutional framework to contribute to the redistribution of wealth, and there are ethical principles to support that view, though they are not universally accepted. In any case, any effects that such redistribution has on efficiency will also have to be taken into account (if, e.g., the possibility of receiving transfers from the State reduces the incentive to work or act entrepreneurially). This also has a moral dimension, insofar as it affects not only the well-being of society but also the fulfillment of the individuals' responsibilities toward their own future and their contribution to the common good.

The Ethical Limits of Capitalism

Probably the strongest charge against the capitalist system, from the moral point of view, concerns its anthropological assumptions. However, any discussion of these issues lends itself to confusion because it is not always clear what we are talking about: (1) the characteristics that the agent must have for the capitalist system to work, (2) the anthropological characteristics identified by the theoretical model, or (3) the characteristics of real men and women in existing capitalist societies.

1. What the capitalist system demands is that the agents be resourceful, evaluating, maximizing persons. *Resourceful* means capable of improvement, not passive, filled with a desire for what is best. It means that the agents are capable of developing their tastes, preferences, and capabilities, so as to open up new opportunities, thus broadening the variety of agents and their capacity for specialization. *Evaluating* means that the agents do not look at the world through indifferent eyes but analyze, order, and compare states of the world to choose between them. And *maximizing* means that the agents always try to obtain the best they can from the scarce resources at their disposal. Provided the agents have these characteristics, even if only to a partial and limited extent, the system will work. And it seems reasonable to assume that real-life men and women do indeed have those characteristics, or at least a lot of them do.

2. The theoretical model of capitalism is quite a different matter. It tends to specify those characteristics much more closely, depending on the need for detail and precision of conclusions. It is assumed, for example, that the agents are driven exclusively by self-interest and often that they are selfish. It is assumed, also, that the agents are rational, in the sense that they have a preference function with certain conditions (continuity,

internal consistency, divisibility of goods, etc.). Often, it is further assumed that their calculation ability is perfect and that they have all the necessary information (all these being assumptions that are criticized by those who believe that rationality is bounded).

Obviously, though, those specifications are not required for the capitalist system to work. For example, the agents must be capable of identifying the goals of their actions, which as a rule will be their own personal goals but which may also be oriented toward the interests of other agents (altruism, solidarity). Self-interest means simply that each person is capable of identifying the goals of his or her actions. And needless to say, people's goals do not have to be "selfish," in the sense of ignoring the effects that their actions have on others or not including other people's interests in their preference function. It does not seem legitimate, therefore, to criticize capitalism for the assumptions on which the theoretical models are based or for the implications of those models—although it is not always easy to identify which assumptions are part of the theoretical apparatus and which are relevant to the capitalist system in practice.

It should also be pointed out that the economic optimum, which economics tells us is achieved in a system of private property and free enterprise, is not devoid of ethical content. In effect, what is achieved is a Pareto optimum, that is, a situation in which no change can be made without benefiting one party to the detriment of another. An optimum, thus defined, is not ethically neutral, however. It is based on utilitarian assumptions that have been widely debated. It is only natural, therefore, that the situation achieved under a capitalist system should be considered ethically unacceptable under other moral assumptions.

3. Last, we must consider the set of ideas and values of the flesh-and-blood agents who actually make decisions in the capitalist system. We already pointed out that these ideas and values are plural, disordered, sometimes contradictory, and always changing. What is often criticized about the capitalist system is precisely that set of ideas and values.

That criticism may be important, but it is unfair. It may be important insofar as capitalism, because of the way it works, promotes values that, at least from certain ethical viewpoints, may be described as immoral, because they are individualistic, selfish, uncaring, and so on. In a word, the theoretical model does not take into consideration the mechanisms of moral learning (acquisition of virtues or vices) at work in people's lives. But it may also be unfair insofar as those values are provided by society (the "values market" mentioned earlier), which offers or imposes them on the agents and on the economic system.

The problem becomes even more complicated if we consider that individual and social ideas and values are channeled through laws and institutions. From the moral point of view, it would seem natural to expect society to set up the legal and institutional framework so that it encourages ethically correct and economically efficient behavior and discourages undesirable behavior. But that is not the function of the economic system. The invisible hand referred to by economists is an economic, not an ethical, mechanism. It works to harmonize the decisions of millions of agents acting in accordance with their—selfish or altruistic—personal interests. But the result is an economic, not an ethical, harmony. In capitalism, as in other economic systems, there is no "ethical invisible hand" that works automatically to bring about the improvement of people and the achievement of higher social goals.

Ultimately, the final moral evaluation of the economic system is a moral evaluation of the society of which the economic system is a part. The economic system is not self-sufficient: It needs the above-mentioned legal and institutional, and through them, moral mechanisms that lead society toward an ethically better situation.

All this becomes clearer if we consider the purpose of the economic system, which we have identified as efficiency. In economics, efficiency is defined as a comparison of the resources actually used with the goal pursued: It is always efficiency "for something," for a particular purpose. How that goal or purpose is defined will, in a way, give us the key to the morality of the system whose efficiency we are trying to evaluate. Capitalism efficiently produces weapons, food, drugs, and textbooks, and the moral value of its production will have to be assessed from outside the system.

The thoughts set out in the preceding paragraphs help us to better understand some of the criticisms commonly leveled against capitalism, for example, the criticism that puts the emphasis on how limited the market is—many activities are completely omitted, such as friendship, family, religion, artistic creation, culture, and so on. That is obviously not a shortcoming of the capitalist system, however, but an acknowledgment that a mechanism whose purpose is to achieve efficiency in the use of scarce resources cannot possibly account for every facet of human activity. And the fact that, in recent years, people have developed economic theories of the family, art, religion, altruism, culture, and so on does not alter that argument, because in every human decision involving the use of scarce resources to achieve alternative goals there is room for economic reasoning. That is not to say, however, that such a decision is exclusively economic.

To end this section, it will do no harm to recall that the capitalist system also develops—and demands—moral values such as honesty, integrity, trust, keeping one's word, respect for the law, and many others, and it fosters an entrepreneurial spirit, generosity, risk taking, vision of the future, personal responsibility for building one's own life, and so on. And it also demands values. For example, many economists say that the social responsibility of a company manager is to conduct the business in accordance with the owners' desires, which generally will be to make as much money as possible while conforming to the basic rules of the society, both those embodied in law and those embodied in ethical custom. Ethical ideas and values, embodied in legislation, regulations, institutions, and social culture, are necessary for capitalism to work efficiently.

The Results

The last block of criticisms and defenses of capitalism concerns the actual results. The following are some of the arguments:

- Capitalism is more efficient than other systems in that it has achieved higher rates of economic growth and, therefore, a higher standard of living for the population. In fact, the rapid economic growth of the last two centuries is directly related to the spread of capitalism. But that is true only if we consider material well-being. Higher living standards may have promoted other private or social goods, such as moral quality, cultural development, artistic activity, and so on, but that need not necessarily be so. As pointed out earlier, the economic system aims to achieve efficiency, not to provide those other goods.

- In promoting freedom of enterprise and the entrepreneurial spirit, capitalism has promoted technological progress and innovation. Others, meanwhile, point to the costs of progress, in terms of unemployment, regional underdevelopment, and so on. Once again, this topic brings us back to the legal and institutional framework in which capitalism moves and the incentives it promotes.

- In capitalism, economic growth has been accompanied by an unequal distribution of wealth. The usual response to this criticism is that growth generates opportunities for all: When the tide comes in, all the boats go up. Once more, our judgment will depend on the rules and institutions, above all on the treatment given to those who lack the resources demanded in the market, the opportunities they have to improve their endowment (e.g., through education), social security policy (unemployment and health insurance and retirement pensions), and so on.

- Many years of experience of economic cycles, especially during the Great Depression of the 1930s, led many people to believe that the capitalist system was essentially unstable, prone to boom and bust cycles, high unemployment rates, periods of high inflation, and so on. In the second half of the 20th century, however, governments learned to handle economic policy much better, smoothing the cycles and mitigating the effects of recessions. Moreover, we now have a better understanding of the causes of unemployment and inflation, and the appropriate policies to combat them, so that today these problems are not usually considered to be endemic to capitalism. Nevertheless, failures of market coordination, of the kind mentioned by John Maynard Keynes, still occur, though it does not seem practicable to resolve them by means of planning mechanisms. In any case, insofar as any economic system must protect decision-makers' freedom, such problems of coordination will always exist.

- Environmental deterioration was considered a defect of capitalism. Yet the results achieved by other systems have been no better. Again, the problem is one of institutions, policies, and incentives, and introducing market mechanisms—environmental ownership rights, pollution markets, and so on—is part of the solution to that problem.

- Many critics of capitalism still see it as containing deep cultural contradictions, including promoting contradictory values and life styles (e.g., the work ethic as opposed to the ethic of consumption); the need for trust while creating incentives to violate it (opportunism); the alienation of workers and consumers; the exaltation of work as the key to building a family, while work effectively could destroy the family; the defense of consumer sovereignty and its negation via the manipulation of consumer preferences through advertising; the insistence on the need for competition and the continuous incentive to destroy such competition; the defense of long-term profitability as key to economic efficiency and the predominance of very short-term profit as the guide for financial decision making, and so on. In recent years, other defects have been identified in the framework of a globalized economy. They include irrational bubbles in the financial and real estate markets, job destruction as a means of value creation for shareholders, value chain manipulation as a means of profit maximization, and so on.

- On a sociological and ethical level, the unequal distribution of power, especially between large and small companies, between multinationals and governments, and so on. Once again, it becomes apparent what an important role the legal and institutional system plays. That system cannot be taken as a given; rather, it is something that has to be continuously earned and improved, precisely because the incentives to manipulate it are always there.

- As opposed to these arguments, capitalism is also seen as a system based on freedom. As Milton Friedman pointed out, freedom is one and indivisible, and economic freedom is key to the creation of a space for individual autonomy, mainly vis-à-vis the State. Ultimately, the defense of capitalism is based mainly on two arguments: efficiency and freedom.

The debate on economic systems tends to be impassioned, because it brings into play crucial aspects of the underlying conception of the human person and society. Opinions are very unlikely to converge when the starting paradigms are so different. Nevertheless, study, reflection, and dialogue may help find points of agreement and identify the reasons for disagreement. This entry has offered an outline that may help identify, first, what is essential in the capitalist system and, second, what aspects of the capitalist system are most criticized.

—Antonio Argandoña

See also Altruism; Bounded Rationality; Economic Efficiency; Economic Incentives; Economics and Ethics; Externalities; Freedom and Liberty; Freedom of Contract; Free Market; Friedman, Milton; Globalization; Liberalism; Market Socialism; Marxism; Mixed Economy; Pareto Efficiency; Public Goods; Smith, Adam

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CARNEGIE, ANDREW (1835–1919)

Andrew Carnegie was born in Dunfermline, Scotland, in 1835 and died in Lenox, Massachusetts, in 1919. He was a leading industrialist, investor, and philanthropist who shaped the railroad, bridge-building, and iron and steel industries in the United States. Carnegie moved with his family to Pittsburgh, Pennsylvania, in 1848, where he literally rose from rags to riches, starting at age 13 with a factory job. After his retirement in 1901, he became known popularly as the richest man in the world.

Carnegie's aggressive business strategies and benevolent acts were well known. He is considered one of the industrialist robber barons, 19th-century capitalists who used ruthless business methods to attain great wealth. He was a contemporary of Herbert Spencer, admiring Spencer's ideas of survival of the fittest and social evolution. Carnegie favored the monopolistic concentration of industry among a few owners freely competing, and he thought his individual success uplifted society. He also felt a mandate to give away his money for the public good, and Carnegie's outspoken criticism of idle wealth spurred philanthropy among his contemporaries.

Carnegie as Businessperson

The management techniques Carnegie developed for handling complex organizations were adopted widely. His trademark style used new technology to drive industrial development, returned profits to the firm to enhance its capitalization, and continuously sought ways to cut costs of production, labor, and distribution. Although these techniques enabled the United States to harness its resources and establish itself as an industrial power, many facets of them became the epitome of bureaucracy, such as a rigidly hierarchical reporting structure, decisions solely made on the basis of cost accounting, and using purely quantitative criteria for performance-based promotions.

Figure 1 Carnegie (Bearded Figure, Center) at the 1911 Founders Day Celebration at Carnegie Institute of Technology

Source: Photograph used courtesy of Carnegie Mellon University Archives.

Carnegie's record as an employer was mixed. He saw himself as a friend of the working man, but he treated labor as an abstract cost to be reduced. He used his good rapport with workers to encourage them to run the mills 7 days a week for 12-hour shifts under dangerous working conditions. Although he did not oppose unions overtly, he hired upper-level managers with antilabor reputations. An infamous strike at his Homestead Steel Works in 1892 erupted in violence when replacement workers arrived. The strike's resolution eventually became a significant defeat for the labor movement in the United States, when his workers were forced to accept wage concessions and give up their union.

Carnegie as Philanthropist

Carnegie gave away an estimated $350 million, creating foundations for world peace, education, and research. Perhaps his best-known philanthropic activity was the creation of more than 2,500 libraries in the English-speaking countries, but he also donated to a range of other concerns. The organizations he created include the Carnegie Corporation of New York, the Peace Palace at The Hague, Carnegie Endowment for International Peace, Carnegie United Kingdom Trust, Carnegie Endowment for the Advancement of Teaching, Carnegie Hero Fund, Carnegie Institute of Technology (later Carnegie Mellon University), and the Carnegie Museums of Pittsburgh.

—Adele L. Barsh

See also Labor Unions; Spencer, Herbert

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Carrying Capacity

Carrying capacity is the ability of an environment to provide the resources for life-forms to survive and reproduce indefinitely. Every species or organism has needs that must be met for it to survive, but if any population gets too large in relation to the environment's ability to provide for those needs, the ecosystem becomes overloaded and cannot provide basic needs to every organism. Human beings, for example, need space, clear air and water, food, and other essentials to survive and maintain a certain quality of existence, but if the human population gets too large relative to its environment and resource availability, the carrying capacity of the ecosystem may be overtaxed with adverse effects on human welfare. An ecosystem does have limits relative to the size of various populations it can support, whether one is talking about human beings or animal populations.

Below the carrying capacity, populations will tend to increase, while they will decrease above the carrying capacity. Population size decreases above the carrying capacity due to either reduced survivorship because of insufficient space or food or reduced reproductive success because of insufficient food or behavioral interactions. The carrying capacity of an ecosystem will vary for different species in different habitats and can change over time due to a variety of factors including trends in food availability, environmental conditions, and space. The field of population ecology, which deals with the dynamics of species populations and how these populations interact with the environment, attempts to predict the long-term probability of a species persisting in a given habitat.

William Rees (1996) has defined human carrying capacity "as the maximum rates of resource usage and waste generation that can be sustained indefinitely without progressively impairing the productivity and functional integrity of relevant ecosystems wherever the latter may be located." The size of the corresponding population that can be maintained is a function of the technology employed and the per capita material standard of living. Regardless of the state of technology, however, humankind depends on a variety of ecological goods and services provided by nature. For sustainability, these goods and services must be available in increasing quantities from somewhere on the planet as per capita resource consumption and population increase.

Humans have developed technologies to grow more food and dispose of the wastes that we create. These technologies have extended the carrying capacity of earth. However, there is still a limit to the human population that the earth can support. This carrying capacity is a function of the number of people, the amount of resources each person consumes, and the ability of the earth to process all the wastes produced. Sustainability is about finding the right balance point among population, consumption, and waste assimilation at any point in time given the existing technologies.

This same concept of carrying capacity applies to certain elements of the environment such as air and water. Every such medium has a certain ability to absorb waste material without serious harm done to the quality of that medium. Thus, air, for example, can absorb a certain amount of waste material without serious harm being done to its quality. But if the carrying capacity of the air is exceeded, the air starts to become fouled by certain pollutants and the quality of the air is affected. Its natural dilutive capacity is violated and human health is affected as a result of exposure to harmful pollutants.

The concept of carrying capacity is related to the idea of natural capital. While "capital" is most often used to refer to money and material goods, natural capital refers to the functions the ecosystem provides for the sustainability of human life, including natural resources, air, water, and other such functions. A community that is living within its means and caring for its natural capital is living within the carrying capacity, while a community that is degrading and destroying the ecosystem on which it depends is using up its natural capital and living unsustainably. In this case, natural capital is being used up faster than it is being replenished or replaced.

Related to the concept of carrying capacity is the idea of a limiting factor, that the population size of a species is constrained by whatever resource is in shortest supply. For example, the availability of water is a limiting factor for human populations living in desert conditions. While other resources necessary for sustainability may be available, the unavailability of one critical resource means that the carrying capacity of that ecosystem may be exceeded. Organisms may, however, substitute a closely related substance for one that is required but is deficient in the environment, or they may be able to alter the conditions in which they are living so as to reduce their requirements.

While in the abstract the concept of carrying capacity makes sense, measuring the carrying capacity of the earth is fraught with difficulty. One of the debates in the population literature centers on what the maximum carrying capacity of the earth is at present and whether we are below or above that level. Doomsayers think that the earth has already exceeded its carrying capacity, while some of their critics seem to believe that the carrying capacity of the planet is infinite. Some question the practical usefulness of the concept, while others focus on ecological footprint analysis to get a handle on the carrying capacity of the earth. Such an analysis approximates the amount of land and sea area it takes to sustain a population and is widely used as an indicator of environmental sustainability. There is thus some controversy about the concept of carrying capacity and its usefulness in helping formulate policies for individual countries.

—Rogene A. Buchholz

See also Biocentrism; Bioethics; Deep Ecology; Environmental Ethics; Environmentalism; Natural Capital; Natural Resources; Pollution

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Cartels

A cartel typically consists of a voluntary and temporary agreement among firms in the same industry to follow common policies instead of competing with each other. These policies can include agreements on prices, market shares, quota systems (limiting production to certain quantities), and conditions of credit. From the perspective of these firms, the main reason for the voluntary formation of cartels is to avoid excessive competition that can lead to price wars that decrease profits for all firms in an industry. This is a departure from the conventional understanding that a competitive market of unfettered supply and demand is the most efficient and fair way of establishing prices and quantities of production. While prices and quantities of production are variable under conditions of free competition, cartels may adapt production to meet demand quotas. Because of this, they can also be used as tools of industrial policy by governments.

The use of cartels was established in Germany at the end of the 19th century. During this period, for example, the coal cartel of Westfalia-Renania formed in 1893 and acted as a sales agent for the majority of mines in Ruhr. Later, in 1925, German chemical companies merged to form IG Farben. It is estimated that there were 3,000 or so cartels in Germany in the 1930s, which the Nazis used to control the German wartime economy. Cartels have also existed in other countries, such as Austria, England, Switzerland, France, Italy, Scandinavia, and Japan, often as a result of government policies aimed at providing incentives for corporate development.

After World War II, cartels fell out of favor with many theorists. Presently, there seems to be a consensus in many camps that cartels are neither efficient nor fair. The adverse implications for social welfare include unused production capacity, higher prices for consumers, and the maintenance of inefficient companies to the detriment of efficient ones. Even so, it is important to note that forms of noncompetition have long existed in market economics. Besides cartels, these include monopolies, oligopolies, trusts, vertical integrations (consolidations of supply chains), and *zaibatsus* or industrial groups that once dominated the Japanese economy. Furthermore, cartels are generally thought to be unstable in that member firms have incentives to cheat on agreements and sell more than the production quotas set by their cartels.

—José-Luis Fernández-Fernández

See also Antitrust Laws; Free Market; Industrial Policy; Laissez-Faire; Market Failure; Monopolies, Duopolies, and Oligopolies; Organization of Petroleum Exporting Countries (OPEC); Perfect Markets and Market Imperfections; Unfair Competition; *Zaibatsu*

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Casuistry

Casuistry is a case-based method of reasoning used in business ethics, bioethics, and the ethics of various professions. Casuistry typically uses general principles in reasoning analogically from clear-cut cases, called *paradigms*, to vexing cases. Similar cases are treated similarly. In this way, casuistry resembles legal reasoning. Casuistry may also use authoritative writings relevant to a particular case.

Practitioners in various fields value casuistry as an orderly yet flexible way to think about real-life ethical problems. Casuistry can be particularly useful when values or rules conflict. For example, what should be done when the duty to meet a client's expectations collides with a professional duty to protect the public? Casuistry also helps clarify cases where novel or complex circumstances make the application of rules unclear. Should e-mail receive the same privacy protection as regular mail? If someone develops an idea while working for one employer, is it ethical to use that idea to help a subsequent employer? Casuistry seeks both to illuminate the meaning and moral significance of the details in such cases and to discern workable solutions.

How Casuistry Works

Consider the following scenario: A maintenance supply vendor visits the manager of a large apartment building and demonstrates the advantages of switching to energy-efficient light bulbs. The vendor adds, "We're having a special promotion right now. Everyone who orders 10 cases of bulbs gets a free emergency radio." Is it ethical for the manager to order 10 cases and accept the gift?

A casuist might approach the scenario by identifying its morally significant features. Those features might include

- the value of the gift,
- the quality of the product being offered for sale,
- the availability of similar products from other vendors at a lower price, and
- the timing of the gift offer relative to the timing of the manager's decision about whether to buy.

The casuist might next identify any generally accepted rules or values involved in the case. A rule in the case of the manager might be, "Get the best value for the building owner's money."

At this point, the casuist might look for analogous paradigm cases. One paradigm would involve a clearly unacceptable gift, such as an expensive piece of luggage offered to promote a shoddy, overpriced product. A second paradigm would involve a generally acceptable gift, such as an inexpensive ballpoint pen given as a thank-you for purchasing a competitively priced, high-quality product.

The casuist would compare the building manager's case with the two paradigms. A closer resemblance to the paradigm involving an acceptable gift would argue in favor of letting the manager accept the radio. A closer resemblance to the opposite paradigm would argue against accepting the radio.

Casuistry's attention to the details of cases can help open up a range of options for those caught in ethically murky situations. In the case of the building manager, possibilities might include demanding a discount instead of the radio, asking for a delay to allow competitors' products to be evaluated, or simply rejecting the radio. The moral and practical advantages and disadvantages of the options would then be discussed.

When examining complex issues, casuists may arrange and sort many cases to create a resource called a *taxonomy.* Treating similar cases similarly, casuists use taxonomies to develop general guidelines or policies.

History of Casuistry

Biblical writers, Greek and Roman philosophers, rabbis, Christian preachers and teachers, and Muslim jurists have used casuistry to solve real-life moral puzzles. The Roman orator and philosopher Cicero wrote the first known "case book" on situations where duties seemed to conflict.

In Europe between 1556 and 1656, members of the Society of Jesus (Jesuits), a religious order in the Catholic Church, produced an extensively developed form of casuistry that became known as "high casuistry." The "Provincial Letters" by the French religious philosopher and mathematician Blaise Pascal criticized the misuse of casuistry as sophisticated excuse making. Following Pascal's critique, casuistry fell into disrepute.

The rise of professional ethics led to renewed interest in casuistry. Contemporary casuists recognize the potential of self-interest and other forms of bias to corrupt casuistry. At the same time, many authors affirm casuistry's usefulness in helping people with diverse beliefs to reach workable agreements in difficult moral cases.

Casuistry and Other Methods in Ethics

Casuistry departs from ethical approaches that work deductively from rules thought to have clear applications in all circumstances. Casuistry takes rules into account but begins with the moral and practical features of each case.

Casuistry also departs from approaches to ethics that rely solely on good character or virtuous motives. Instead, casuistry demands deliberation about how to put good character and virtuous motives into practice.

Some authors classify casuistry as a subset of "applied ethics." Others restrict the term *applied ethics* to deductive reasoning from principles to cases. Accordingly, these authors view casuistry as an alternative to applied ethics.

Like casuistry, "situationism" or "situation ethics" focuses on cases. Unlike casuistry, situationism uses no paradigm cases and views principles as "guidelines" at most. Situationism also departs from casuistry by viewing circumstances as unique and isolated rather than as continuous with broader moral experience.

—David P. Schmidt

See also Common Law; Dilemmas, Ethical; Ethical Decision Making; Moral Reasoning

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Cato Institute

The Cato Institute, founded in 1977, is a nonpartisan research organization based in Washington, D.C. The mission of the self-described market liberal think tank focuses on traditional American principles of limited government, individual liberty, free markets, and peace. In keeping with these free market principles, the Institute accepts no governmental funding or endowments, instead relying on private donations to support its $14 million annual budget.

The Cato Institute keeps its intellectual forebears in the forefront, as evidenced by its naming, after *Cato's Letters*. Advocates rely on the values propounded in these revolutionary pamphlets, along with the written works of the founding fathers. While embracing modern individualist philosophers such as Robert Nozick and Ayn Rand, the Institute demonstrates a special attachment to Friedrich Hayek. Hayek argued that freedom for all would allow genius and innovation to emerge from any sector or strata of society, ultimately leading to social benefits for all.

Cato researchers explore market-liberal positions on diverse domestic topics such as education policy, labor law, homeland security, and tobacco. Indeed, the Institute has been looked to by a series of presidential administrations as the leading source of research and analysis on the privatization of social security, a research program that it formalized in 1995 with the founding of its Project on Social Security Choice. The Cato Institute also addresses global issues. While critical of the International Monetary Fund's and World Bank's fostering of financial dependence among developing economies, the Institute is a strong advocate of free trade, as evidenced by the Cato Center for Trade Policy Studies.

The Institute's market-liberal economic position is accompanied by an equally libertarian social position. The Cato Institute's goals include the pursuit of liberty for all citizens, primarily in the form of equal freedom from governmental intervention. Their positions often align with "socially liberal" politics, in that the Institute supports sexual and racial freedoms and decries the "war on drugs." The Institute also disagreed vocally with the Bush administration's decision to invade Iraq, arguing that the military should instead focus on its legitimate role as defender of homeland soil.

The Cato Institute's critics claim that it is a front for corporate interests and foundations anxious to benefit from these antiregulatory advisers in Washington. Others argue that it is misleading to label the Institute *nonpartisan*, a term that may describe its relationship to the two leading political parties in the United States, but that belies its strong philosophical position.

The Cato Institute publishes books and policy studies, along with their regular publications *Cato Journal*, *Cato Policy Report*, *Regulation* magazine, and the free quarterly *Cato's Letter.* In addition to holding regular policy and book forums in Washington, D.C., the Institute also hosts conferences in major cities around the world.

—Lori Verstegen Ryan

See also Cowboy Capitalism; Freedom and Liberty; Free Market; Friedman, Milton; Hayek, Friedrich A.; Individualism; Libertarianism; Nozick, Robert; Rand, Ayn; Smith, Adam

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Cause-Related Marketing

Cause-related marketing (CRM) refers to a marketing activity that involves a company forming a relationship with a particular cause or causes for mutual benefit. CRM can be characterized as a strategic marketing tool employed to achieve both social and corporate objectives; it simultaneously benefits the company and a charity or similar cause. The cause could be general, for example, a concern for the environment, or specific, for example, when a percentage of the sales of a particular product are donated to an identified charity. From the company's perspective, the benefits include the opportunity to enhance their reputation, differentiate themselves from the competition, boost employee morale, raise brand awareness, increase customer loyalty, build sales, and attract positive publicity. From the perspective of the "cause," the benefits include increased revenue and public awareness of their activities.

CRM originated in the United States, where corporate philanthropy is typically characterized as "enlightened self-interest" or as "doing well by doing good." American Express is credited with being the first company to launch a CRM campaign in the early 1980s. Increasingly, companies are moving away from "no strings attached" donations toward joint ventures in which commercial sponsorship of charities is included within overarching corporate objectives, and it is becoming common for contributions to social causes to be funded by the marketing budget rather than a central philanthropic fund.

There are several concerns raised by CRM. Neither the short-term nor long-term effects of CRM on charitable income are known. While CRM campaigns appear to result in increased funding for the social causes involved, there are fears that traditional sources of income may be harmed by CRM. There is concern that CRM will undermine traditional donations as companies come to expect a return for their contributions. Moreover, individuals may be less likely to spontaneously donate to particular charities if the products they buy support social causes. There is also a question relating to the sustainability of income for social causes from CRM. When a company feels it has exhausted CRM's benefits it will move to more profitable campaigns leaving the social causes they previously supported to find alternative ways of generating income. If CRM does undermine spontaneous donation, then after the campaign ends the charity may be badly affected. This possibility raises the question of what, if any, ongoing responsibility companies ought to have to the social causes they have entered into CRM relationships with after the campaigns end.

On a more theoretical level, the concern is that CRM marks a shift from an intrinsic motivation for companies supporting social causes (i.e., supporting them because it is the right thing to do) to an instrumental or prudential reason for doing so (i.e., supporting them to derive a benefit). At an individual level, CRM may undermine consumers' commitment to social causes because it is mediated through a market transaction that could lead to a sense of moral disengagement from social issues.

—Josie Fisher

See also Corporate Citizenship; Corporate Philanthropy; Marketing, Ethics of

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Caux Principles

The Caux *Principles for Business* were first presented to the business community in 1994. The authors of the *Principles* are members of the Caux Round Table (CRT), which was organized in 1986 by 28 senior business executives from Japan, Europe, and the United States. The group meets in various nations but often in Caux, Switzerland, hence their name.

To have efficient and fair markets, CRT executives recognized the need for worldwide ethical principles. Some members also belonged to the Minneapolis-St. Paul Minnesota Center for Corporate Responsibility, now called Center for Ethical Business Cultures, which had already forged global ethical principles. CRT discussed those principles and decided to adopt them with a few changes. CRT added two basic principles to their *Principles for Business.* The first, from the Eastern tradition, is the Japanese principle of *kyosei*, which means living and working together for the common good, enabling cooperation and mutual prosperity to coexist with healthy and fair competition. The second principle, from the Western tradition, is *human dignity*, which refers to the sacredness or value of each person as an end, not simply as a means to the fulfillment of other's purposes. The *Principles* include a preamble, seven general principles, and six more specific sets of stakeholder principles, covering customers, employees, owners/investors, suppliers, competitors, and communities.

—Gerald F. Cavanagh

See also Codes of Conduct, Ethical and Professional; Global Codes of Conduct; Missions and Mission Statements; Transparency International; Triple Bottom Line; United Nations Global Compact

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CERES

See Coalition for Environmentally Responsible Economies (CERES)

Certified Public Accountants (CPAs)

A certified public accountant (CPA) is an individual who has been certified by a state examining board as having passed the Uniform CPA Examination and met that state's additional requirements with respect to education and work experience. Most states also require that licensed CPAs obtain a specified number of hours of continuing professional education every 3 years to maintain the license to practice as a CPA.

Professional ethics plays an important role in the public accounting profession. Every state society of CPAs has its own code of professional ethics, and its members are expected to adhere to that code. Alleged violations are investigated by the state board or its designee, and those deemed to be in violation are subject to penalties ranging from censure to license revocation.

The Uniform CPA Examination was recently changed to a computer-based format that is administered two out of every three months during the year at test centers across the United States. Individual state boards of accountancy determine if candidates meet their jurisdictions' requirements to sit for the examination. The revised exam is divided into four sections—auditing and attestation, financial accounting and reporting, regulation, and business environment and concepts—and takes a total of 14 hours to complete. Candidates may take as many sections of the exam as they choose during each examination window, but must pass all four parts during a rolling 18-month period, beginning on the date that the first section has been passed.

Educational and experience requirements for CPAs vary somewhat from state to state. However, at present, most states require 150 hours of postsecondary education at an accredited college or university and 2 years of experience in public accounting or internal auditing. A useful resource summarizing the requirements by state is the *Digest of State Accountancy Laws and State Board Regulations* published jointly by the American Institute of Certified Public Accountants (AICPA) and the National Association of State Boards of Accountancy.

The largest national, professional organization representing CPAs in the United States is the AICPA. With approximately 328,000 members, the AICPA works with state CPA organizations, giving priority to those areas where public reliance on CPA skills is most significant. AICPA membership is not mandatory for CPAs, but it is estimated that three out of every four CPAs are members of the AICPA.

CPAs pursue careers in public accounting, private industry, governmental agencies, and not-for-profit organizations. CPAs in public practice engage in a broad range of services, including auditing, tax, and consulting activities for their clients. However, the Sarbanes-Oxley Act of 2002, passed partially in response to accounting scandals at Enron and WorldCom, prohibits public accounting firms from performing consulting and certain other services for those clients whose financial statements they audit. The firms, however, are permitted to perform these services for other, nonaudit clients. A primary function of CPAs is the audit of financial statements of public and privately held companies, as well as other business entities. This assurance function has become an important component of the U.S. economic system, as it provides potential investors and creditors with independent verification that a company's financial statements have been prepared on a consistent basis in accordance with generally accepted accounting principles. This verification process supports the overall economy by effectively lowering the overall cost of capital.

There has been a rapid increase in the number of CPAs specializing in forensic accounting as a result of the recent accounting scandals. Forensic accountants investigate alleged white collar crimes, such as securities fraud and embezzlement, as well as other criminal financial activities, such as asset misappropriation and financial statement fraud. Forensic accountants combine their knowledge of accounting, law, and investigative techniques to determine if illegal activity has occurred. Often, forensic accountants serve as expert witnesses during trials, presenting the results of their investigations.

CPAs in private industry often hold the title of chief executive officer, chief financial officer, controller, and/or treasurer. They record and analyze financial information of the companies for which they work and are involved in budgeting, performance evaluation, product costing, cost system design, and asset management. CPAs in private industry also pursue careers as internal auditors, verifying the accuracy of their organization's internal records and checking for mismanagement, waste, or fraud. They also evaluate their firms' financial and information systems, evaluate management procedures, and assess whether internal controls are adequate.

CPAs also work in the public sector for governmental agencies and not-for-profit organizations, maintaining and examining records of government agencies and charitable organizations. CPAs employed by federal, state, and local governments guarantee that transactions are recorded in accordance with laws and regulations. They also work as Internal Revenue Service agents or in financial management, financial institution examination, and budget analysis and administration.

Multiple career options are one of the many attractive qualities of a career as a CPA. In addition, the implementation of the Sarbanes-Oxley Act of 2002 has greatly increased the demand for auditors and, particularly, forensic accountants. These new-age accounting jobs require more than simply crunching numbers. Rather, they require a detail-oriented mind and solid communication skills to converse with clients and upper-level management. Along with the variety of career paths available to CPAs comes a very work-oriented life style. CPAs usually work between 40 and 50 hours a week during the regular year, with the number of hours increasing dramatically during the traditional busy season during the first calendar quarter.

The job outlook for CPAs is bright. It is predicted that 2005 hiring for entry-level accounting positions will increase by 13% over 2004, according to a new survey from the National Association of Colleges and Employers.

—Sharon L. Green and Robert J. Kollar

See also Accounting, Ethics of; American Institute of Certified Public Accountants (AICPA); Chief Executive Officer (CEO); Chief Financial Officer (CFO); Codes of Conduct, Ethical and Professional; Fraud; Internal Audit; Professional Ethics; Public Interest; Sarbanes-Oxley Act of 2002

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CFA Institute

CFA Institute is the global, nonprofit professional association that administers the Chartered Financial Analyst curriculum and examination program worldwide and sets voluntary, ethics-based professional and performance-reporting standards for the investment industry. As of June 2005, CFA Institute had 76,000 members in 119 countries. Its membership includes the world's 64,000 CFA charterholders, as well as 131 affiliated professional societies and chapters in 52 countries and territories. CFA Institute is headquartered in Charlottesville, Virginia, USA, with additional offices in London and Hong Kong.

Mission and Membership

The mission of the CFA Institute is to establish a direction for serving its members and setting a higher standard within the global investment community. CFA Institute has adopted a formal strategic planning process and a set of values around which all its programs, services, and initiatives revolve. It strives to be the organization for investment professionals who are dedicated to meeting the highest standards for ethical behavior, education, and ongoing professional development and excellence of practice in the profession. CFA Institute provides a range of products and services to its members, other investment professionals, and the investing public, and it aims to fulfill its mission and vision through effective use of volunteers, good stewardship of resources, and effective use of technology. Therefore, the core values of excellence, integrity, strength of community and cooperation, and volunteer service have been adopted.

Formerly the Association for Investment Management and Research, CFA Institute offers three membership categories: CFA charterholder, regular, and affiliate. To qualify as a CFA charterholder member, an individual must have satisfied the requirements to become a regular member and the requirements of the CFA program established by the CFA Institute. As a regular member of CFA Institute and a local society, an individual must (1) hold a bachelor's degree from an accredited institution or have equivalent education or work experience, (2) have passed Level I of the CFA exam or the Self-Administered Standards of Professional Practice Examination and have 48 months of acceptable professional work experience in the investment decision-making process, and (3) agree to adhere to and sign the Member's Agreement and Professional Conduct Statement. An affiliate membership applicant must adhere to the Member's Agreement and Professional Conduct Statement.

Code of Ethics and Asset Manager Code of Professional Conduct

The CFA Institute code of ethics states that its members shall act with integrity, competence, dignity, and in an ethical manner when dealing with the public, clients, employers, employees, and fellow members. The Code encourages members to practice in a professional and ethical manner that will reflect credit on members and their profession, while striving to maintain and improve their competence and the competence of others in the profession. Moreover, the Code asks members to use reasonable care and to exercise independent professional judgment.

Recently, the Asset Manager Code of Professional Conduct has been revised and new standards are expected to be included in the 2006 exam year. This Code addresses six areas: (1) loyalty to clients, (2) the investment process and actions, (3) trading, (4) compliance and support, (5) performance and evaluation, and (6) disclosures to clients. The Code compels management firms to, among other things, place clients' interests first, have a reasonable basis for investment decisions, and act according to clients' or funds' objectives. Firms must also fairly allocate trades among clients and give priority to client trades over self-interest; appoint a compliance officer to implement policies and investigate complaints; use fair-market prices when necessary; and ensure that performance information is complete, accurate, and timely. Last, the Code calls on companies to make all necessary disclosures to clients in a truthful and timely manner.

An integral part of the CFA Institute is the *Financial Analysts Journal*, which circulated its inaugural issue to about 700 subscribers in January 1945. Despite having different governing bodies, the publication adheres to the same standards and principles as CFA Institute.

—Paula J. Thielen

See also Certified Public Accountants (CPAs)

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CHAEBOL

A *chaebol* is a family-controlled South Korean conglomerate. While the founding families do not own majority stakes in the companies, Korean culture allows them to maintain control out of respect for their long associations with the businesses. Among major *chaebol* are Samsung, LG, Hyundai, and SK Group. *Chaebol* produce nearly two thirds of South Korea's exports and attract 70% of foreign capital inflows.

South Korean government-*chaebol* cooperation has been termed an unholy alliance, with rampant favoritism and corruption and little transparency. While that cooperation has been credited with fueling the nation's growth and transformation, critics say it also has led to monopolistic and oligopolistic concentration of capital and economically profitable activities. The *chaebol* culture is now accused of stifling creativity, amassing political power for leading families rather than maximizing profits, providing an unfair playing field for small and medium-sized enterprises, and excluding women and divergent voices from management. *Chaebol* payoffs to former South Korean presidents Chun Doo Hwan and Roh Tae Woo were estimated to be in the hundreds of millions, and perhaps billions, of dollars, subsequently leading to the convictions of those leaders.

Webs of cross-shareholdings enable families running the *chaebol* to covertly transfer funds from healthy companies to weaker ones in the group. As a result, investors in high-performing companies in the *chaebol* are forced to subsidize survival of frail members. In addition, the South Korean government has pursued a "too big to fail" doctrine, with government-owned banks regularly rescuing large firms despite continuing huge losses, resulting in *chaebol* acquiring massive debt. Foreign investors have long applied a "Korea discount" of 20% or more to Seoul-traded shares, showing reluctance to pay high valuations on companies that may be secretly controlled by insiders.

In 1997, following devaluation of the Korean *won*, the International Monetary Fund bailed out South Korea with an aid package worth almost $60 billion. That aid came with strict conditions that South Korea reform its economy and the *chaebol.* The *chaebol* situation was the key issue in the 2002 South Korean presidential race, with Roh Moo Hyun, a crusading civil rights lawyer, riding into office on a wave of reformist sentiment.

A variety of reformative measures have been taken. For example, Chey Tae Won, chairman and CEO of SK Group and heir to the company's founding family, was arrested in 2003 and jailed on misappropriation charges. He was convicted of accounting fraud and breach of his fiduciary duties and sentenced to 3 years in jail. Nevertheless, he served just 3 months in prison and remains at the head of the *chaebol.*

Laws implemented in 2004 limit the amount conglomerates may loan or invest in their affiliate companies, require disclosure of shares held by members of the top executives' families, and permit the Bank of Korea to investigate the assets of owners' family members to prevent concealment of assets. Largely because of reform efforts, 12 of Korea's top 30 *chaebol* prior to 1998 no longer exist as coherent entities.

Nevertheless, some critics argue that reform has been slow, tentative, and incomplete, hampered in part by recent scandals surrounding Roh Moo Hyun's aides and donors. Reform may also face opposition since forced closure of loss-making *chaebol* businesses would result in cutting 200,000 or more jobs and because of the still massive power of the *chaebol.*

—Ramon J. Aldag

See also Cartels; International Monetary Fund (IMF); *Keiretsu;* Monopolies, Duopolies, and Oligopolies; Scandals, Corporate

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Challenger Disaster

The *Challenger* Disaster refers to the accident in which the Space Shuttle *Challenger* exploded barely a minute after liftoff and killed all seven people on board. This incident is cited as an example of what can happen when members of an organization fail to blow the whistle on what they recognize as a potential problem.

The Space Shuttle *Challenger* flew nine successful missions prior to the incident in 1986. This mission was unique in that, on this flight, *Challenger* was scheduled to carry the first teacher to fly in space, Christa McAuliffe. The mission was also unusual in that, from the start, it was plagued by anomalies. Although liftoff was originally set for January 22, weather delays and equipment servicing issues delayed liftoff until January 28.

A subsequent investigation identified the cause of the disaster—the failure of an O-ring seal. It was determined that the O-ring was not designed properly. Regardless, had the shuttle lifted off on January 22 as originally planned, it is likely that the launch would have been successful. It was the abnormally low temperature on January 28 coupled with the design defect that caused the disaster to occur.

In fact, engineers and managers at Morton Thiokol, the manufacturer of the O-rings, were not entirely surprised by what happened. On the night before the fated day, several of them protested the launch because of the impending bad weather predicted for the next morning. First, they believed that choppy sea waters might make it considerably difficult to recover the shuttle boosters after the launch. Second, they feared that ice in the booster support troughs might interfere with the shuttle orbiter. Third, they were openly concerned about the weather—they admitted that they could not predict the behavior of the O-rings that sealed the booster joints, because the O-rings had not been tested at temperatures below 50°F (degrees Fahrenheit). The temperature was predicted to be about 30°F at the time of the scheduled launch.

Thiokol signed off on the launch over the objections of the engineers. Managers at Thiokol saw their first priority as to execute the launch. Since there had been 24 successful launches prior to this one, they did not see any reason this launch would not be successful as well. Moreover, the engineers could not prove that the O-rings and shuttle orbiters would not function at temperatures below 50°F. The engineers did not blow the whistle—they did not report their concerns to anyone other than their managers. On January 28, 1986, at 11:39 EST, Space Shuttle *Challenger* disintegrated, 73 seconds into its flight.

Many lessons were learned on this day. Manned space flights did not resume in the United States for more than 2 years after the *Challenger* Disaster. Only after technical modifications were made and after NASA management implemented stricter regulations regarding quality control and safety did the space shuttle program resume on September 28, 1988, with the flight of Space Shuttle *Discovery*.

—*Tara J. Radin*

See also Professional Ethics; Roles and Role Morality; Whistle-Blowing

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Chamber of Commerce of the United States

The idea of forming a national organization to represent the unified interests of U.S. business first took shape under the presidency of William Howard Taft. On April 12, 1912, his vision for the organization became a reality when a group of 700 delegates from various commercial and trade organizations came together to form the U.S. Chamber of Commerce to represent business interests at the national level. More than 90 years later, the Chamber has grown to include more than 3 million business organizations, 2,800 state and local chambers, 830 associations, and 102 American Chambers of Commerce abroad.

The U.S. Chamber focuses on national issues at the federal level that affect business interests. The Chamber tries to influence these issues through lobbying or talking with government leaders, testifying before Congress on behalf of business, going to court, keeping track of the legislative agenda, speaking out for business, and other means to make sure business interests are taken into account by the federal government. Its influence has grown over the years as it has become more sophisticated in its ability to affect the public policy process and make its voice heard in Congress and other parts of government. It has been a leader in fighting government regulation thought to be too onerous on business and pressing hard for legislation that is supportive of individual opportunity and the free enterprise system.

The Chamber has a number of programs that provide services to its members. The National Chamber Foundation, for example, is an independent, nonprofit public policy think tank that promotes discussion of cutting-edge issues affecting business. The Institute for Legal Reform helps reduce excessive and frivolous lawsuits while restoring fairness and balance to the nation's civil justice system. It does this by promoting civil justice reform through legislative, political, judicial, and educational activities at both national and local levels. Another legal program focusing on litigation is the National Chamber Litigation Center, which plays a major role in shaping public policy on important legal questions of concern to American business while achieving long-range improvements in the legal system as a whole.

Access America focuses on women and minority-owned business leaders and entrepreneurs and tries to open doors to networks and markets and fosters strategic alliances and investments for these groups. The Center for Corporate Citizenship works with public and private sectors to enable and facilitate corporate civic and humanitarian initiatives. The Center for Workforce Preparation elevates the quality of a community's workforce by participating in grant-based programs. The Institute for Organization Management and the Institute for Advanced Management offer continuing education opportunities and professional credentialing for chamber and association professionals. There is also a Homeland Security program that recognizes the stake American business has in a strong national defense and homeland security policy that safeguards Americans while also promoting their mobility and freedom.

With regard to trade and international programs, the U.S. Chamber has an International Division that tries to improve the ability of U.S. business to compete in the global marketplace by providing its members tools and resources as well as promoting cutting-edge events that bring world leaders to its membership. The Center for International Private Enterprise is an independent, nonprofit affiliate of the Chamber that promotes democratic and market-oriented economic reform by working directly with the private sector in developing countries. The Space Enterprise Council represents businesses with a commercial interest in space by providing a forum for space-related companies. Finally, TradeRoots is a national trade education program dedicated to building grassroots support for trade in the U.S. Congress and stopping antitrade protectionism.

The Chamber has a number of publications and e-newsletters for its membership. The Member magazine keeps its readers alert and up-to-date on legislation that will affect business. Whether it is taxes, energy, or transportation, the magazine claims to tell it membership what it needs to know. *SmartBrief* is an e-newsletter that provides an inside track to business best practices to help chamber and association members lead their organizations. The *Workforce Preparation News* provides information about current workforce development projects in support of workforce training and education. And finally, *The Corporate Citizenship* is a monthly e-publication that provides insight on current trends and policy developments that have an impact on the active role of business in society.

The Chamber of Commerce of the United States is one of a number of organizations that work at the federal level to promote business interests. The National Association of Manufacturers (NAM), for example, was formed before the Chamber and claims to be the voice of American industry. The Business Roundtable was formed to represent the largest companies in the United States who felt they had different interests that were not being adequately represented by the Chamber and NAM because these organizations covered such a broad range of business organizations from the smallest to the largest. Finally, the National Federation of Independent Business was formed to represent the interest of smaller companies. Nonetheless, the Chamber is one of the premier organizations representing business at the federal level and is likely to remain so in the future.

—Rogene A. Buchholz

See also Corporate Political Advocacy; Nongovernmental Organizations (NGOs); Trade Associations

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Charity, Duty of

Charity is the act of giving something of value, usually money, physical property, or time, to a worthy cause or to a person or people in need. Generally, charity is extended to those whom the giver views as less fortunate or those whose cause the individual considers worthy of receiving charity. People living in chronic poverty, suffering from disease, abuse, or other misfortune, and victims of crime or natural disaster are sometimes viewed as especially deserving of charity.

Some social theories posit that the duty of charity is part of the social contract that allows individuals to live together in relative harmony. Each person helps others in times of adversity, knowing that their good deeds will be reciprocated when, or if, necessary. At a minimum, the social contract implies a duty to provide aid in times of emergency. In this regard, charity is a form of social insurance in which a person gives so that others will give to them at appropriate and beneficial times.

Historically, it has been considered a social duty and a moral obligation of the affluent social classes to provide charity to the poor, the sick, the indigent, and others in chronic and acute need. Thus, charity has taken many forms, from cash contributions to charitable organizations, financial endowments of schools and other facilities, to performing many kinds of volunteer work. Involvement in charity work was based on the knowledge that there were others less fortunate than the benefactor and the awareness that those who are more affluent, better educated, or in a higher social class have a specific obligation to behave charitably toward those with fewer resources or a lower social standing.

While charity is seen as a duty, it is not, from a secular perspective, an absolute duty; the social contract does not obligate people to give at all costs. The duty of charity should not place an intolerable burden on a person. Sometimes it is morally impossible to fulfill the charitable obligation—individuals cannot give what they do not have. People are not expected to practice charity when doing so compromises their own survival or that of their families, nor are they obliged to perpetrate immoral or illegal acts in the name of charity.

In the Abrahamic traditions (Judaism, Christianity, and Islam), charity is the root and foundation of all moral behavior. These major world religions equate charity with mercy and love, while also stating that every other virtue relies to some degree on the ability to behave charitably. They further identify forgiveness as an act of charity toward a person who has done wrong. Charity is an individual responsibility and a form of ministry through which observant Jews, Christians, and Muslims may express their faith.

Charity is one of the principle tenets of Judaism. Jewish theology equates charity with mercy and graciousness. It is expressed by the Hebrew word *yadid,* combining two Hebrew characters—*yad* (hand) with *dod* (loved one). The definition of charity in the Jewish tradition is extending a hand of friendship to another for one's own good and for the benefit of others. Charity is a *mitzvah* (pl. *mitzvoth*), a commandment, good deed, and source of joy, which blesses both the giver and recipient. *Mitzvoth* are pleasing to God and beneficial to the world at large. Judaism emphasizes *mitzvoth* as a way to achieve self-improvement.

Jewish religious practice offers many opportunities for *mitzvoth.* A charity box is found at the entrance of many synagogues. Its purpose transcends fundraising. Contributing to the charity box before entering the synagogue to pray encourages observant Jews to consider the needs of others before their own. It is a special *mitzvah* to observant Jews to extend charity before *Pesach*, otherwise known as Passover, so that Jews with insufficient resources may participate in the celebration. Charity at other times in the Jewish religious year is also a *mitzvah.* It is customary to make a contribution to the synagogue or another charitable cause on the day before Rosh Hashanah, the start of the Jewish calendar. At the Feast of Purim, which celebrates Esther's intervention in a plot to assassinate innocent Jews, it is customary to give gifts of money, food, and other goods to the poor.

The custom of *Kapparot* takes place in preparation for Yom Kippur, the Day of Atonement. In ancient times, *Kapparot* was the ritual sacrifice of a rooster (for men) or a chicken (for women), with the meat being distributed to the poor. In the modern *Kapparot* ritual, observant Jews make a monetary donation to the synagogue or a charitable organization of their choice. Charitable acts at other important times are also *mitzvoth.* In ancient times, it was the custom for a Jewish bride and groom to set aside a table at their wedding feast to feed the poor or indigent; the modern equivalent is a contribution to the couple's favorite charity. When an observant Jew dies, it is the custom during *shivah*, the 7-day mourning period, to make a donation to the departed's synagogue or favorite charity, instead of sending gifts of food or flowers to the bereaved family. In terms of monetary charity, Jewish teaching also advocates tithing, wherein 10% of one's earnings is given to charity. The tithe should be paid before any other financial obligations are met, in keeping with the *first fruits* teaching found in the Bible in Deuteronomy, Chapter 14.

The duty of charity follows observant Jews into their roles as sole proprietors or owners of privately held corporations, but it is not clear that the duty of charity extends to their roles as officers of publicly traded companies. As corporate officers, their primary duty is to act as agents of the shareholders, so they may practice giving with corporate profits only if directed to do so by the shareholders.

Like Jewish teaching, Christian theology advises believers to tithe. Charity is viewed by theologians as the root of Christianity. Jesus's death on the cross to redeem mankind's sins is perceived as the ultimate act of charity. Throughout Christian wisdom literature, the terms *charity*, *mercy*, and *love* are often used interchangeably. In the Christian tradition, the interdependence of people living in community requires each to work for the safety, growth, and well-being of others. This ideal is expressed in the Great Commandment given by Jesus to his followers—to love God with all one's heart, soul, and strength and one's neighbor as oneself. This is the most basic teaching of Christianity.

In addition to charity, The Baltimore Catechism, which is recognized in both the Catholic and the Protestant traditions, identifies specific charitable acts that faithful Christians are obligated to perform when the need arises; these are called the corporal and spiritual works of mercy. The corporal works of mercy are feeding the hungry, giving drink to the thirsty, clothing the naked, sheltering the homeless, visiting the sick and imprisoned, ransoming the captive, and burying the dead. The spiritual works of mercy are instructing the ignorant, counseling the doubtful, admonishing sinners, bearing wrongs patiently, forgiving wrongs willingly, comforting the afflicted, and praying for the living and the dead.

Charity is one of the Five Pillars of Islam, called *zakat* (purification or growth) in Arabic. Islamic charity is based on the teaching that all things belong to God (Allah) and are held by people in trust. One's possessions are purified by setting aside a portion for those in need; this pruning action encourages new growth. Each Muslim calculates his or her own *zakat*. Generally, this may represent 1.5% to 2% of one's capital, though more or less may be given, depending on individual circumstances. In addition to *zakat*, Islamic teaching on charity includes *sadaqa,* voluntary charity. While this may be interpreted as monetary charity in excess of *zakat*, *sadaqa* are much broader.

At a minimum, *sadaqa* instructs observant Muslims to refrain from wrongdoing and uncharitable behavior. It further directs them, to the degree they are able, to urge others to behave charitably and to work to aid the poor and needy. According to the Prophet Mohammed's teaching, even greeting a neighbor is an act of charity. Islamic hospitality is another custom that corresponds to *sadaqa*. Muslims are instructed to entertain guests generously, as their station in life allows. In particular, women, children, those who are sick, and travelers, especially those on religious pilgrimage, are deserving of hospitality.

The practice of *waqf* is also an Islamic teaching on the duty of charity; in Arabic, the word means tying up or dedication and is used similarly to the English words bequeath or bequest. Under *waqf*, personal or business assets are used to endow charitable or benevolent activities. Generally, *waqf* are permanent arrangements—donors relinquish the right of ownership over their donated property, and managers of *waqf*, called *mutawalli,* act as agents of Allah, not of the original owner or the charitable organizations who may receive funds from the proceeds of the *waqf*.

What distinguishes *zakat* and *sadaqa* from other forms of charity is the Islamic emphasis that the observant Muslim seeks Allah in the performance of charitable acts, so any act of charity must be in keeping with Islamic teaching and law. Muslims are expected to perform charitable acts circumspectly, without thought of payment or acknowledgment. In addition, *sadaqa* explicitly precludes uncharitable behavior. During his lifetime, the Prophet Mohammed taught that to receive Allah's charity faithful Muslims must behave charitably by doing for others what they desire for themselves, contributing to the needs of the poor, dealing honestly in business transactions, caring for animals and the physical world, and behaving modestly and circumspectly.

There are two major differences between the secular and spiritual perspectives of charity. First, secular thought holds that charitable giving involves something of tangible value and presumes that the giver is more able to give than the receiver may be. While the spiritual perspective recognizes such giving as charitable, it expands the definition of charity to include good deeds that may be extended to an affluent person by a poor one. Second, secular thought views charity as an imperfect duty, that is, people should behave charitably, but choosing not to do so is an acceptable course of action. In the spiritual view, charity is not voluntary—it is mandatory, though people are not coerced into giving. Regardless of status, wealth, or social standing, all are capable of giving and must do so to the degree they are able. Judaism, Christianity, and Islam have charity as a prime foundation of their respective faiths. While none of the Abrahamic traditions require charity from those who are unable to give, they all state that every person of conscience is capable of giving something, and each should give as much as they are able when circumstances require it.

—Cheryl Crozier Garcia

See also Altruism; Christian Ethics; Corporate Philanthropy; Empathy; Fiduciary Duty; Islamic Ethics; Jewish Ethics; Metaethics; Moral Agency; Normative Ethics; Ought Implies Can; Profit Maximization, Corporate Social Responsibility as; Strategic Corporate Social Responsibility

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Chernobyl

On April 26, 1986, an accident occurred at Unit 4 of the Chernobyl nuclear power plant in the former Ukrainian Republic of the Union of Soviet Socialist Republics, near the present borders of Belarus, the Russian Federation, and Ukraine. The accident destroyed the reactor, contaminated large areas surrounding the reactor, and led to an increase in radiation levels over practically the whole of the northern hemisphere.

The Chernobyl power station consisted of four Soviet-designed light water–cooled graphite-moderated (RBMK) reactors of 950 MW each. These units used graphite to moderate the nuclear reaction and used water flowing through channels holding the fuel elements to cool it. There was no containment structure. The immediate causes of the accident were a flawed reactor design coupled with serious mistakes made by the plant operators during a test procedure when many control systems had been deliberately overridden. There had been little communication between those responsible for the test and the plant operators, formal safety approvals were either bypassed or given perfunctory attention, and the experiment carried out on a less well-resourced night shift when it had been scheduled as a daytime activity.

The greatest doses of radiation were received by 200,000 workers, called *liquidators*, who participated in the cleanup. Thirty-one people died almost immediately; 237 occupationally exposed individuals were admitted to hospital with clinical symptoms attributable to radiation exposure, of whom 14 died over the next 10 years. This was the only time when radiation-related fatalities occurred in a commercial nuclear power plant.

Those in the affected areas learned about the nature of the event and its hazards not from authoritative reports but from hearsay and international reports. This lack of transparency lowered public confidence. Some contemporary media reports emphasized the potential dangers, and thousands of mothers-to-be aborted unborn children. Evacuation of residents began the day after the accident and continued into August. The 116,000 people who were evacuated and those who remained living in the less affected regions will, over their lifetimes, receive doses of radiation comparable with doses they would receive from natural sources. Demographic indicators in the "contaminated" regions have worsened as people have been resettled or have migrated. Economic activity has also been limited.

A significant increase in the incidence of thyroid cancer among those in the affected areas, who were children in 1986, is directly linked to the accident, and continued incidence among exposed residents is expected. These cancers are not usually fatal if diagnosed and treated early. Other health effects have been reported but none have been confirmed as directly related to the accident.

Some radiosensitive local ecosystems received lethal doses in the first few weeks after the accident. Within 3 years the natural environment in these localities had begun to recover and no sustained severe impacts on animal populations or ecosystems have been observed. Long-term genetic effects remain a possibility, and some groups attribute many thousands of deaths to the accident. A concrete shell or sarcophagus was constructed around the destroyed reactor, which has provided protection since its construction. Its stability and the quality of its confinement are in doubt.

Thus, a series of seemingly inconsequential operational decisions led to an event that had a significant impact on the availability of electric power (and hence economic development) in the Soviet Union and has had lasting consequences on the attitude toward nuclear energy well beyond the region.

—Howard Harris

See also Bhopal; *Exxon Valdez*; Kyoto Protocol; Nuclear Power; Pollution

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Chicago School of Economics

The Chicago School of Economics refers to the free market approach to economics advocated by members of the Department of Economics at the University of Chicago. The Chicago School approach began in the 1930s under Frank Knight and persisted for decades producing multiple Nobel Prize winners. In addition to Knight, some of the leading and more well-known figures include Gary Becker, Ronald Coase, Aaron Director, Milton Friedman, Merton Miller, Richard Posner, and George Stigler. The Chicago School of Economics is also associated with the law and economics approach to jurisprudence developed at the University of Chicago Law School.

At the heart of the Chicago School approach are neoclassical price theory and a belief in free markets. Simply stated, the Chicago School approach stands for the belief that markets without government interference will produce the best outcomes for society (i.e., efficient outcomes). A primary assumption of this school of thought is the rational actor (self-interest maximizing) model of man. Under this view, all decision makers will act to maximize their self-interest and will, therefore, respond to appropriately designed price incentives. At the society level, free markets populated by rational actors will cause resources to be distributed based on their most valuable uses (allocative efficiency).

The Chicago School's approach to antitrust law in the area of regulatory policy provides an excellent demonstration of its general principles and approach. The traditional approach to antitrust regulatory policy is to limit concentrations of market power, such as by breaking up a firm that has monopoly power. The Chicago School approach, on the other hand, argues that consumers are best protected by competition, even if that is only between a few large firms in an industry. Those large firms may have gained their dominant market positions through efficiency advantages that provide greater benefits to consumers than a market forced by the law to include many smaller firms. Even if a firm gains monopoly power, the Chicago School approach prefers to allow the market to correct the problem rather than rely on government intervention, which may cause greater harms to efficiency.

The Chicago School's price theory and rational maximizer approach has been applied to a wide variety of areas, including both market- and nonmarket-based activities. For example, Gary Becker extended this analysis to areas such as crime, racial discrimination, marriage, and family life. In the realm of law and economics, the Chicago School approach argued that legal rules and court decisions should be based on the promotion of efficiency. The role of the law is simply to alter the incentives of individuals and organizations to achieve that end. For example, in the area of tort law, the goal should not simply be the minimization of costs from accidents but also the minimization of the costs of preventing such accidents. If liability rules require individuals to take precautions against accidents that are more costly than the accidents themselves, then the outcome is allocatively inefficient.

There are many criticisms of the Chicago School approach. For example, behavioral law and economics scholars challenge the assumption that humans are rational, self-interest maximizers. Instead, they argue that certain decision heuristics and biases prevent people from being the ideal decision makers assumed by the Chicago School approach. Others argue that the goal of efficiency comes at the cost of justice and equality in society.

—David Hess

See also Antitrust Laws; Austrian School of Economics; Economic Efficiency; Economic Rationality; Efficient Markets, Theory of; Friedman, Milton; Pareto Efficiency; Perfect Markets and Market Imperfections; Pollution Externalities, Socially Efficient Regulation of; Rational Choice Theory

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Chief Compliance/Ethics Officer (CCO)

The chief compliance/ethics officer (CCO) typically has responsibility for oversight of a company's ethics initiative and compliance activities, including its code of conduct, guidance and reporting system, and ethics and compliance training. The CCO works with senior-level management to develop strategies and tools that are designed to integrate ethics, values, and compliance into all levels of the organization. To succeed, the CCO must have a deep understanding of the nature of the business, its policies and procedures, and its unique ethics and compliance risks.

The CCO is a relatively new position that is evolving in terms of role and job responsibilities. Larger companies are more likely to create such a position, or give more visibility to a preexisting position, as a result of the major corporate scandals of the early 2000s and increased regulation that requires public companies to institute better corporate governance and strongly encourages all companies to adopt effective ethics and compliance programs. Although some companies may make a distinction between a compliance officer and an ethics officer, others do not. In fact, many companies that have both titled functions assign these responsibilities and titles to one individual.

Origin of the CCO Position

The CCO is a newcomer to the executive suite who owes his or her position primarily to a more demanding regulatory environment. Of particular importance are the following laws, regulations, and guidelines: the Foreign Corrupt Practices Act (1977) (making it a crime for American companies or their agents to bribe foreign officials or politicians to gain or retain business), the Defense Industry Initiative (1986) (the agreement of major U.S. defense contractors to promote sound management practices and comply with regulations), the U.S. Federal Sentencing Guidelines for Organizations of 1991 (building on the Defense Industry Initiative principles to outline a framework for corporate compliance programs), the Sarbanes-Oxley Act of 2002 (mandating stronger corporate governance, integrity, and transparency in financial reporting and effective internal controls for public companies), and the Amended Federal Sentencing Guidelines for Organizations of 2004 (expanding and clarifying the framework for effective corporate compliance and ethics programs).

In the wake of the corporate scandals of the early 2000s, companies came under regulatory pressure to centralize ethics and compliance responsibilities under one officer. For example, in a speech to the American Society of Corporate Secretaries in 2002, Securities and Exchange Commissioner Cynthia Glassman stated that it was important for companies to designate a corporate responsibility officer so that someone within the company had ownership of corporate compliance and ethics issues.

Ms. Glassman's remarks proved to be a precursor to the U.S. Sentencing Commission's revisions to the Federal Sentencing Guidelines in 2004. The Guidelines, as originally drafted, made clear that an effective compliance and ethics program could lead to greatly reduced fines and penalties for a company convicted of a crime. The amendments to the Guidelines highlighted the criticality of a company having a knowledgeable governing authority (board of directors) to provide reasonable oversight of the program and designating overall responsibility for the program to a high-level executive or executives.

The Shared Role: A Different Approach to Ethics and Compliance Leadership

Although many companies have centralized responsibility for ethics and compliance under one officer, other companies, both public and private, have resisted this trend. Historically, these companies have considered responsibility for ethics, compliance, and governance to reside in the offices of the general counsel, the corporate secretary, and elsewhere and have seen little benefit in altering their structure. According to a 2006 chief compliance officer survey of nearly 400 companies conducted by The Society of Corporate Secretaries & Governance Professionals and *Corporate Secretary* magazine, nearly half of the companies surveyed did not have a dedicated CCO position. Many of these companies, instead, assigned compliance and ethics responsibilities to either the general counsel or the corporate secretary.

Companies have given various reasons for allocating multiple responsibilities to one function or individual, including the fact that much of the work in ethics, compliance, ethics and compliance risk management, and governance is overlapping. For example, in the interest of efficiency, Nike has designated one individual as corporate secretary and senior governance counsel, with the added responsibility of corporate compliance. Other companies have combined these roles to avoid excessive bureaucracy or because they are not highly regulated and see little need for a compliance position apart from the general counsel. Many smaller companies have chosen not to designate a separate compliance officer due to insufficient work, limited staff, and lack of resources.

The CCO and Compliance Program Reporting Structure

The reporting structure for a company's ethics and compliance program is often tied to the company's history and culture. For example, if the general counsel has had responsibility for the compliance function in the past, a recently appointed CCO may report to the general counsel. According to the chief compliance officer survey, 28% of CCOs or chief governance officers report to the CEO, 17% report to the general counsel, and 15% report to the audit committee. Other reporting options include the chairman, the board of directors, a compliance or governance committee of the board of directors, and the corporate secretary.

Regardless of the precise reporting structure, a company is well-advised to give the CCO access to executive management (in particular, the CEO, the CFO, and the general counsel) and to the audit committee or an independent committee of the board of directors. Granting the CCO a direct or dotted reporting line and direct access to the board of directors is particularly important in light of the Amended Federal Sentencing Guidelines, which place ultimate responsibility for knowledge about and oversight of the compliance and ethics program with the board of directors.

In larger organizations, the CCO is often supported by a mid-level manager and other staff, often located in different business units, who are responsible for the program on a day-to-day basis. The Amended Federal Sentencing Guidelines make it clear that the individual or individuals responsible for daily operation of the program should report periodically to the CCO or other high-level personnel in charge of the program and should also have direct access to the board of directors.

Another element of the reporting structure for some companies is a cross-functional compliance committee—often made up of high-level managers from departments such as human resources, legal, internal audit, and line operations—that meets regularly to discuss compliance issues throughout the company. At Dupont, for example, the chief ethics and compliance officer manages the Ethics and Compliance Central organization and chairs its Corporate Compliance Committee.

Role and Responsibilities of the CCO

The role and responsibilities of the CCO vary from company to company. According to the chief compliance officer survey, in 2006, only 39% of companies with a designated CCO had a specific job description. Generally speaking, the CCO is accountable for developing, directing, and providing oversight to the organization's ethics and compliance program, including its code of conduct, related programs and policies, communication, training, and guidance/reporting system. He or she is often recognized as an expert and a leader, working with executive and line management to establish and sustain an ethical culture.

The Ethics & Compliance Officer Association (ECOA), a professional association for managers of ethics, compliance, and business conduct programs, which was founded in 1992, has outlined the chief responsibilities of the CCO. These include accountability for all program activities related to standards of conduct, including ethical relationships with employees, customers, shareholders, suppliers, and other stakeholders; development of a compliance risk management program; responsibility for a confidential reporting program; ethics and compliance training and regular communication on corporate values, ethics, and compliance; integration of new acquisitions into the program; conducting investigations into alleged violations of the company's code of conduct and making recommendations regarding discipline; assessing the effectiveness of the program; and providing reports to top management and the board of directors.

In some companies, however, some of the responsibilities listed by the ECOA as belonging to the CCO may be allocated to other functions. For example, the legal department may retain responsibility for compliance risk assessment and risk management; human resources may lead or partner with the CCO on the ethics and compliance training initiative; human resources, internal audit, the legal department, and the security organization may conduct investigations of alleged wrongdoing, depending on the nature of the violation; and recommendations as to discipline for violations of the code of conduct may fall within the jurisdiction of the human resources and line functions.

Although the public often perceives that a company's corporate social responsibility (CSR) or corporate citizenship initiatives are linked to its ethical culture, the CCO rarely is assigned responsibility for the CSR function. For example, General Electric's citizenship strategy is managed primarily by the vice president of corporate citizenship.

Background and Job Qualifications

Because the CCO is a relatively new position, those who fill the role come with a wide variety of backgrounds and experience. Most commonly, the CCO will have previously served in positions in the legal, human resources, finance, or internal audit department. Some companies require CCO candidates to have a J.D. or master's degree, a given number of years of managerial experience, and expertise in domestic and international laws and regulatory compliance.

The ECOA lists common characteristics of CCOs as including strong communication skills; ability to establish and maintain credibility and trust throughout the organization at all levels; ability to assimilate information on complex issues; political savvy; organizational knowledge; working knowledge of applicable laws and regulations; experience with training and development; broad management skills; ability to protect confidential information; ability and willingness to take on a difficult or unpopular position, if necessary; and common sense, objectivity, maturity, rationality, and integrity. One might add to this list independence and strong influencing skills.

Benefits of Creating a CCO Position

Companies that have established a CCO position report generally favorable results, according to the chief compliance officer survey. Some respondents suggest that the position is more form than substance and others comment that the role is still not clearly defined or understood within their company. Other respondents, however, observe that the centralized position has enhanced the company's focus on compliance, governance, and ethics and enabled both the company and regulators to more effectively regulate and monitor compliance. Other benefits reported in the survey include better anticipation of compliance risks, establishment of a climate of ethical conduct, help in setting the "tone at the top," and companywide acceptance of the program, with the backing of the CEO and board of directors.

Major Challenges for the CCO

According to a Compliance Program and Risk Assessment Benchmarking survey conducted by the

Association of Corporate Counsel (ACC) and Corpedia, Inc. in 2005, the top challenges for CCOs when planning or implementing their company's compliance and ethics function have been dealing with the complexity of the regulatory and legal environment, the complexity of the company's own compliance processes, and staffing issues. Other problems listed by the respondents to this survey include the perception that compliance is not a strategic function, organizational resistance to change, lack of adequate financial resources, inadequate technology, inadequate senior executive support, and inadequate peer support.

Top management support is generally regarded as critical to the success of the CCO and the company's ethics and compliance program. A CCO may have to report bad news or investigate alleged wrongdoing by a senior executive. He or she may face pressure to ignore misconduct or may be overruled by high-level managers in deciding how to address it. In such cases, senior executive backing is critical to the CCO's effectiveness and survival.

For CCOs of companies with international operations, partners, and suppliers, there is the additional complexity of overseeing a global ethics and compliance program that is consistent in principle but flexible enough to be effective in different cultures. Some companies have adopted a fairly broad, values-based code of conduct that makes reference to specific policies (relating to matters such as gifts and entertainment, conflicts of interest, discrimination and diversity, and political contributions) that vary, somewhat, on a country-by-country basis.

CCOs of global companies must also ensure that their program's reporting system is effective and legal in all countries in which the company operates. For example, in some cultures, employees are much more reluctant to report improprieties via a helpline than is the case in the United States. In France, Germany, and other countries, anonymous reporting channels (which are mandated for public companies by the Sarbanes-Oxley Act of 2002) have been banned unless they meet certain standards that may be inconsistent with the act. In addition, the CCO who oversees training on the code of conduct and compliance must often ensure delivery of training in the local language, tailoring of the message to address cultural differences, and adaptation to circumstances in which technological or staffing resources are limited.

Supporting Organizations and Their Role

Although one problem reported by CCOs in the ACC/Corpedia survey is a lack of peer support, several organizations have begun to fill this gap. Primary among these in the United States is the ECOA, which holds an annual conference focusing on the trends and issues faced by those with responsibility for ethics and compliance in their organizations. More recently, the Open Compliance and Ethics Group, the Society for Corporate Compliance and Ethics, the Society for Corporate Secretaries and Governance Professionals, and various consultants have begun to offer resources and advice to compliance professionals.

—Francy Stewart Milner

See also Business Ethics; Codes of Conduct, Ethical and Professional; Corporate Ethics and Compliance Programs; Corporate Governance; Directors, Corporate; Ethical Culture and Climate; Ethics & Compliance Officer Association (ECOA); Ethics Training Programs; Federal Sentencing Guidelines; Foreign Corrupt Practices Act of 1977 (FCPA); Global Codes of Conduct; Sarbanes-Oxley Act of 2002; Scandals, Corporate

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Chief Executive Officer (CEO)

A chief executive officer (CEO) has responsibility for developing and implementing a strategic plan to achieve goals and objectives of the corporation. The corporation's board of directors selects and oversees the CEO and the executive team. Historically, the majority of U.S. CEOs have also been the chairman of the board, although this practice has diminished in recent years. In publicly held organizations, shareholders elect the board of directors.

The functions of the CEO include figurehead, spokesperson, leader, resource allocator, monitor, liaison with outside groups, disseminator of information to internal stakeholders, crisis manager, entrepreneur, and negotiator. All these functions involve managing various stakeholders. The following sections describe planning, reporting, and behavioral imperatives that CEOs face.

Reporting

Securities Exchange Commission and Other Governmental Agencies

CEOs of firms with publicly traded stock have regular financial reporting responsibilities to the Securities and Exchange Commission (SEC). CEOs and chief financial officers (CFOs) are ultimately accountable for the accuracy of these reports, as signified by their signature. Individual penalties may occur if information in these reports is later found to be untruthful.

While they do not personally develop them, CEOs are also responsible for other reports that are made regularly to government agencies, such as the Internal Revenue Service, the Occupational, Safety and Health Agency, the Environmental Protection Agency, and the Department of Labor. In addition, CEOs are responsible for compliance with a number of acts and regulations that affect how business operates, such as the American with Disabilities Act, the Employment Retirement Income Security Act, and the Sarbanes-Oxley Act.

Sarbanes-Oxley Act

The Sarbanes-Oxley Act has had perhaps the largest impact on CEO behavior since the Securities Acts of the 1930s. It is an extremely complex piece of legislation. Sections 302 and 906 are particularly relevant to CEOs because of the individual accountability imposed on them. Following Sarbanes-Oxley, CEOs and CFOs must certify the effectiveness of internal controls and the fair and accurate representation of financial reports. Section 302 of the Sarbanes-Oxley Act addresses the fairness of financial statements, and Section 906 addresses the adequacy of internal control.

While both Sections 302 and 906 have similar requirements, Section 302 is less stringent because it allows certification based on the officer's knowledge. In contrast, under Section 906, the CEO needs to acquire whatever expertise is necessary to attest to the quality of internal control; the CEO cannot rely on other people's knowledge.

While faulty Section 302 certification does not have specific penalties, faulty Section 906 certification can result in criminal penalties and/or imprisonment for individuals. Criminal penalties under Section 906 include fines up to $5 million and/or imprisonment of up to 20 years. In addition, CEOs who are found guilty may be temporarily or permanently barred from serving as an officer or director of another firm.

For certification under Section 906, CEOs rely on documents produced in compliance with Section 404 of the Sarbanes-Oxley Act. Section 404 requires companies to oversee the documentation, testing, and issuance of a report on the effectiveness of internal controls. External auditors then must attest management's report on internal control. While there are no penalties or sanctions for poor internal control, the strength of the internal control system affects the amount and scope of work that needs to be completed by the external auditors before they can determine an audit opinion. Material weaknesses in internal control must be reported to the audit committee and the board of directors.

Section 406 of the Sarbanes-Oxley Act requires that companies disclose the code of ethics applicable to their CEO and other top officers throughout the organization. The purpose of the code of ethics is to promote honest and ethical conduct and deter wrongdoing by top corporate officials. The requirements under Section 406 underscore the importance and enforceability of corporate codes of ethics.

Section 1102 of the Sarbanes-Oxley Act states that tampering with evidence, witnesses, victims, or informants may result in fines and/or imprisonment. Document shredding and whistleblower retribution fall under this section of the Sarbanes-Oxley Act. While not specifically aimed at CEOs, corporate codes of ethics are approved by CEOs and must clearly state that these tampering practices will not be tolerated.

Federal Sentencing Guidelines

As part of the Sarbanes-Oxley Act, effective January 25, 2003, Congress granted emergency authority to the United States Sentencing Commission to increase penalties significantly for corporate fraud and other white-collar fraud offenses. Sentences were enhanced for white-collar offenses that affect a large number of victims or endangered the solvency or financial security of publicly traded corporations, other large employers, or 100 individual victims. Officers and directors of publicly traded corporations were particularly targeted for substantial increases in penalties for the abuse of a position of trust. In most cases sentence length was increased by 50% and financial penalties enhanced by five times or more.

Corporate Social Responsibility (CSR) Reports

Over the past decade, the reporting responsibilities of the CEO have expanded greatly and moved beyond traditional financial reporting. One prominent example is the growth of reporting on corporate social and environmental responsibility. Unlike financial reports and attestation by licensed accounting professionals, there is no common format or auditing process for these reports. This has made the tasks of creating and certifying these reports much more complex. Similar to financial reports, CEOs sign CSR reports as a symbol of their accepted responsibility for the report contents. At this time, there are no penalties for CEOs who file false CSR reports, although there may be negative reputation effects for both the CEO and the company for false or incomplete reports.

Planning

Planning Horizon and Scope

The typical CEO remains on the job for less than 5 years. Because of this short horizon, CEOs may be motivated to focus on short-term objectives. Incentive plans for top corporate officers that focus on achievement of long-term strategic goals are less likely to encourage short-term aggressive earnings management.

The planning function of CEOs is extremely complex. The traditional economic view of the firm is that the CEO's job is to maximize shareholder value. The CEO is an agent of the owners of the corporation. The CEO has a fiduciary responsibility to make corporate investments that enhance the shareholders' investments and periodic returns. Shareholders may consider corporate investments in nonshareholder stakeholder initiatives to be undesired "philanthropy" that is best left to the personal desires of shareholders because corporations are inefficient mechanisms for altruism. CEOs who make investments for social objectives such as improving the environment may be taxing owners by undemocratic procedures.

Contemporary political philosophers argue, however, that wealth maximization can negatively affect nonshareholder constituencies. Even in organizations that embrace the importance of including stakeholders in their strategic planning process, there is controversy about how broadly a firm defines stakeholders and to what extent the stakeholders should affect the goals and objectives of an organization even if they do not have a financial interest in the firm.

The most common stakeholders are shareholders, employees, customers, communities, suppliers, and the government. Corporate decisions can affect persons far removed from the firm that nonetheless can affect the firm's reputation in both negative and positive ways. CEOs must be prepared to publicly address the impact of the organization on its many stakeholders as well as their fiduciary duty as an agent of shareholders. The CEO's obligation to serve shareholders and other stakeholders will be one of the chief ethical dilemmas he or she will face on a routine basis.

Organizational Structure

Part of strategic planning involves organizational design and structure. CEOs must select an organizational structure that facilitates achievement of the corporation's goals and provides accountability. Organizational structures vary across industries and over time have become less hierarchical. Without a good fit between structure and strategy, it is difficult for companies to achieve their corporate goals.

The CEO's choice of organizational structure influences the speed in which decisions are made, the extent of cross-functional integration of ideas and personnel, and the allocation of resources. Organizational structure evolves and expands with the size and scope of an organization. It is the CEO's responsibility to recognize when organizational structure is impeding strategy and to implement an appropriate restructuring response.

Behavior

The "tone at the top" is reflected in the CEO's and key officers' day-to-day behavior. "Walking the talk" is one indicator of the CEO's commitment to the values of an organization. Several companies have sustained substantial financial losses following a decline in corporate reputation. As a result, CEOs now play the role of "chief reputation officer" in addition to having many other job responsibilities. Positive corporate reputations are important because they have been linked to increased profitability from higher employee retention, improved product quality, and increased customer loyalty.

Conflict of Interest

CEOs face a wide range of challenges that may fall under the heading of conflict of interest. These relationships can be social as well as financial. For example, a CEO may have a personal relationship with another employee, which may be a violation of the corporate code of conduct. A CEO may use corporate assets for personal expenditures, such as a private aircraft for personal travel, or receive loans that are forgiven over the period of employment. Both these examples illustrate lack of separation between personal and corporate assets. In firms with publicly traded stock, business and personal assets must not be commingled.

Another potential conflict of interest is when CEOs receive personal tax services or other accounting services from their companies' external auditors. Companies can also no longer extend credit or make personal loans to CEOs, unless this is the company's line of business.

Insider stock trading is another example of conflict of interest. CEOs have access to competitive information that may encourage them to sell stock in advance of general knowledge of this inside information. One way that CEOs can avoid possible accusation of insider trading is through participation in a routine stock purchase and sale program. There are also restrictions on how and when CEOs can trade stock. For example, CEOs may not buy or sell stock during retirement plan "blackout" periods. A blackout period is a period of more than 3 days where more than 50% of U.S. participants cannot purchase or sell company stock.

Compensation

Historically, CEO compensation has been controversial. Many view U.S. CEOs to be greatly overpaid. However, "reasonable" compensation depends on the person making the evaluation. In the past, informal rules concerning the multiplier between the highest and lowest paid employees were measures of fairness. For example, in Japan, the average CEO's salary is 11 times greater than the average worker's salary. In the United States, the average CEO's salary is 475 times greater than the average worker's salary. Today, consultants working with the compensation committees of the board of directors use market rates that can distort historical multiplier rates.

Of greater public concern appears to be the appearance of CEO compensation plans that are not tied clearly to performance, as are compensation plans of other employees. Golden parachutes are coming under increased scrutiny as CEOs leave companies with large severance and benefits packages. In an attempt to address some of these issues, the Sarbanes-Oxley Act now states that incentive-based compensation paid to CEOs based on earnings that are later restated downward must be returned to the company.

In addition, the SEC is requiring increased disclosure for top executives' total compensation rather than the piecemeal approach that has been used in the past. Disclosure should include pay for performance, deferred compensation, retirement benefits, and other special perquisites. CEO incentives may be influenced by their departure packages, whether it is a takeover, termination, or retirement scenario. Expanded disclosure of CEO compensation will provide better visibility to investors and is key to responsible corporate governance.

Recruiting

The CEO must handle employment arrangements carefully. CEOs should be careful of nepotism and violation of noncompete agreements. Hiring former employees of significant competitors must not be contingent on the employee's sharing of confidential competitive information with the new employer.

Bribery

CEOs are also responsible for international operations where acceptable local practices may differ from the country in which the organization is headquartered. Section 104 of the Foreign Corrupt Practices Act forbids bribery of foreign officials to secure an improper advantage. However, company officials may pay a foreign official to expedite or secure the performance of a routine government action. Routine governmental actions include obtaining permits, processing visas, providing police protection, and providing utility services. Corporate officers, including CEOs, who participate in bribery may incur penalties of fines up to $25,000,000 and 20 years imprisonment. In addition, questionable local practices as reported by the media can impair corporate reputation and affect a firm's long-term profitability.

Product Safety

CEOs, who become aware of problems associated with product safety, need to take swift action to avoid significant reputational loss that can easily exceed any costs associated with removing the product from distribution channels. Johnson & Johnson's speedy response to the Tylenol product tampering, spearheaded by the CEO, staved off reputational damage due to the Tylenol poisonings.

Conclusion

CEOs have a large amount of responsibility to direct an organization and can have a tremendous impact on the corporation's success. However, they are under increased scrutiny in all areas of their planning, reporting, and personal behaviors. Clearly, the days of the imperial CEO are numbered, as an increasing number and variety of stakeholders monitor CEOs closely. The Sarbanes-Oxley Act and revised Federal Sentencing Guidelines provide clear incentives for CEOs to behave ethically or suffer severe personal and professional consequences.

—Cathleen Burns and Naomi Soderstrom

See also Accountability; Agency, Theory of; Altruism; Codes of Conduct, Ethical and Professional; Conflict of Interest; Corporate Social Responsibility (CSR) and Corporate Social Performance (CSP); Dilemmas, Ethical; Executive Compensation; Federal Sentencing Guidelines; Foreign Corrupt Practices Act of 1977 (FCPA); Friedman, Milton; Insider Trading; Sarbanes-Oxley Act of 2002; Securities and Exchange Commission (SEC); Stakeholder Theory; Trust

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Chief Financial Officer (CFO)

A chief financial officer (CFO) is the most senior executive official within a company to have responsibilities for leading the organization's financial affairs, including the direction of its financial and managerial accounting and control functions, and often its treasury functions. He or she oversees the recording, analysis, and reporting of financial information internally and externally; administers its system of internal accounting control; counsels the organization's leadership on financial matters; and represents the organization to external auditors, tax and financial regulatory authorities, capital markets, and contracting entities.

The complex regulatory frameworks that govern the work of a CFO and his or her organization call for (1) principled leadership in conformity with relevant financial, legal, and ethical standards and the organization's mission and identity; (2) prudential decision making and independent professional judgment in assessing, balancing, and managing risks; and (3) a demonstrable commitment to safeguarding and enlarging the organization's financial resources so that it will be capable of growth that can benefit the diverse stakeholder constituencies that contribute these and other resources.

Official Role, Reporting Relationships, and Qualifications

The CFO, as an executive officer of a corporation, is among its chief administrative leaders, and he or she serves at the discretion and pleasure of the chief executive officer (CEO) and the board of directors. By law, the corporate charter, and prudent business practice, the CFO and other officers join with the board of directors to guide the organization's strategic direction and provide important oversight regarding the integrity of its operations and financial reporting and control processes. Officers owe the corporation fiduciary duties of care, loyalty, and good faith in overseeing its affairs. For tax-exempt organizations, these fiduciary duties include as well a duty of conformity to the purposes and activities that form the bases for their exemption before federal and state tax authorities.

The CFO often reports to the CEO or to a chief operating officer. In the case of a large, multisegment organization, each business unit may have a CFO, or the equivalent, who reports to its CEO. Because of the CFO's rank and portfolio of responsibilities, it is common for corporations to confer authority on their CFOs to enter into contracts on their behalf.

Many CFOs have a background in accounting, finance, and related fields, although in the United States this is a matter of business practice and preference rather than a legal or professional requirement. Many large entities select professionals with extensive experience in relevant fields, especially public accounting, and/or service in similar capacities at other business units or organizations for this role. Because of the diversity of recruitment practices, the Sarbanes-Oxley Act of 2002 § 407 requires companies that list securities in public capital markets to disclose whether at least one member of their board audit committee qualifies as a "financial expert." If a company cannot disclose at least one such expert, it must disclose why this is not the case.

The CFO's Scope of Responsibilities: Accounting, Control, and Treasury Functions

The CFO's responsibilities include leading the financial affairs of the organization and administering its related processes, principally the accounting and control functions. Depending on the organization, the CFO's portfolio may include treasury functions as well. Within the accounting and control functions, professional staff oversee managerial and financial accounting roles, the former relating to the collection, analysis, and reporting of financial information about an entity to aid managerial vigilance and decision making and the latter having to do with preparing financial statements in accordance with applicable public- and private-sector standards, including generally accepted accounting principles (GAAP), primarily for external users.

When the CFO's role includes treasury responsibilities, he or she leads corporate processes and systems for safeguarding assets, managing cash and investments, and securing capital resources to maximize the organization's return on investment so that it can grow and add value for shareholders and other stakeholders. In this last role, the CFO often devotes significant time to shareholder relations and to being a public face for the organization.

Accounting and Control Responsibility Functions

The four main accounting and control responsibility functions that typically report to the CFO are general accounting, accounts payable, payroll, and budgeting. The size and complexity of the organization will influence whether these functions reside within dedicated departments. The first three of these functions often report through a "controller," or other chief accounting officer.

The general accounting function coordinates the organization's entries into its financial journals in conformity with a system of internal accounting control; executes regular "closings" of these records to post them to general and subsidiary ledgers; reconciles discrepancies and imbalances; notes variances; prepares consolidations of financial results in multisegment entities; prepares financial statements and other reports; maintains related databases, including schedules of fixed assets; and performs physical inventories, financial account analyses, and other procedures to assist the external auditors in their testing and review procedures.

These financial reporting processes make it possible for the controller to prepare financial statements in accordance with GAAP and enable the CFO to discharge his or her role of taking express written responsibility on behalf of the organization for the representations in the financial statements. This provides the basis for the distinct role of the independent external auditor to express an opinion regarding the fairness of these representations. In a similar way, the CFOs and CEOs of corporations that file quarterly and annual financial information with the Securities and Exchange Commission (SEC) rely on the work of their controllers' staffs in preparing the financial statements when they certify under § 302 of the Sarbanes-Oxley Act that, among other things,

- they have read the statements,
- the statements are free of material untrue statements or omissions, and
- the statements fairly present the financial condition and results of operations for the organization for the applicable dates and periods.

The accounts payable function is responsible for exercising control over the disbursement of funds to pay an organization's obligations, through documentation procedures regarding the identity of the payee, the date of the purchase of the good or service, the amount of the expenditure, the business purpose, and the authorization by the requester and the approver to remit the payment. For payments for personal services, the accounts payable function normally will require documentation of the worker's independent status, for example, in the form of an executed contract, to ensure that the organization does not use the accounts payable system to pay for services by employees, and risk failing to withhold appropriate income and payroll taxes.

In cooperation with the human resources function, the payroll function is responsible for exercising control over the disbursement of funds to compensate an organization's employees for their services through its payroll system, through documentation procedures regarding the following for each employee:

- Identity and employment eligibility
- Job title and salary information
- Social security number or tax identification number
- Tax status for the jurisdiction(s) in which he or she works and lives, and the number of personal exemptions for calculating the withholding of income taxes
- The employee benefits elections that he or she has made

The payroll function also calculates, withholds, and remits to tax authorities income, payroll, and other taxes, and it complies with court orders to garnish wages, for example, for delinquent child support obligations of employees.

Some organizations locate additional accounting and control functions under or alongside the scope for the controller's authority, for example, accounts receivable, fixed asset accounting, and tax compliance services. In addition, large, multisegment organizations may create a controller within each business unit with one or more of the aforementioned functions reporting to him or her to help the organization operate more responsively.

The role of the budget function is to guide the process for assembling information from throughout the organization to compose a financial plan for the entity that will be sufficiently detailed to enable realistic planning for the year and to form a basis for evaluating performance. The financial budget constitutes one of the primary measures of individual and organizational performance and accountability, while the forecasts that budget officers and staff may help prepare throughout the year normally serve as dynamic planning documents.

The internal audit function within an organization generally should *not* report to either the CFO or the treasurer, because the purpose for this role is to provide a level of oversight and control over the operations of these areas. The internal audit staff cannot function effectively, exercise independent professional judgment, or render meaningful oversight if they report to the very people about whose work they must maintain professional skepticism in their testing and review procedures. In the majority of cases, organizations will avoid this conflict by requiring the internal audit function to report to the audit committee, risk management and compliance committee, or governance committee of the board of directors, or perhaps to the board, in its entirety, for small organizations.

Treasury Responsibility Functions

The treasury responsibility functions within an organization, including cash management and investment management services, technically report to the entity's treasurer but, in practice, the person who serves as the CFO may perform the role of treasurer as well. These treasury functions include the following:

- Managing the organization's cash and investment accounts through internal specialists and external investment management firms to preserve and increase their value
- Raising capital sufficient for the organization to achieve its strategic objectives in a cost-effective manner
- Promulgating and enforcing policies and procedures throughout the organization for the secure collection, custody, transfer, and disbursement of cash and other assets

Whether as a dedicated treasurer, or simultaneously in his or her role as CFO, the incumbent will work closely with the leadership of risk management, internal audit, legal counsel, and other key responsibility portfolios within the organization, and likely will solicit feedback from the external auditors as well, to ensure that there are adequate controls in place to protect the entity's assets.

The treasury functions also include efficiently and effectively procuring and managing capital resources for the organization. The most significant source for such capital typically consists of retained earnings, the cumulative store of value that the organization has generated through its operating activities. (This prominent role for retained earnings, and the diversity of constituencies that contribute to this resource, help justify stakeholder theory.) When retained earnings are not sufficient to finance a company's capital needs, then the CFO can help/advise senior leadership regarding alternative sources for capital, including various classes of common stock, preferred stock, bonds, and revolving credit arrangements. For a tax-exempt organization, the analog to retained earnings is the total of "net assets," or the "fund balance," that is typical of fund accounting, and alternative sources for financing include endowment and other investment income; royalty income; program services revenue; and grants and contributions from government agencies, private institutions, and the public.

In seeking such capital resources, a company's leadership must make a credible case to participants in public and private capital markets that the organization will be able to earn a rate of return in excess of its weighted average cost of capital, that is, the blended cost that it incurs for these resources. In performing such an outreach, the leader of the treasury function often must involve himself or herself directly in shareholder relations and serve as an important public face for the corporation, explaining its plans within the limits of corporate confidentiality and eliciting the trust of markets to minimize the organization's cost of capital.

It is in demonstrating the corporation's capacity to earn this *excess* over the weighted average cost of capital that treasury leadership makes the case for the organization's fundamental capacity to *grow.* Regardless of its market share, number of employees, revenues, or scope of activities, if a company is not growing in this basic financial sense, it will not be able to continue as a going concern over the long term. Only if the company is capable of protecting the interests of its sources of capital—a set of constituencies much broader than shareholders, as the discussion above indicates—will it be in a position to benefit other stakeholders.

In this role, treasury leadership assists the rest of senior corporate leadership in evaluating its progress in this process and in assessing alternatives to help it succeed. For the person serving as treasurer to locate and secure sources of capital that are demonstrably conducive to the financial growth of the company, he or she routinely seeks counsel from internal and external advisers, including financial analysts, economists, investment bankers, marketing strategists, accountants, and attorneys. This is particularly the case when dealing with complex transactions or new forms or sources of domestic and international capital.

The CFO's Role in Managing the Risks of Fraud and Misconduct

A key theme for the CFO's stewardship of an organization's resources, and a primary requirement for him or her to discharge the aforementioned statutory and fiduciary duties, is his or her role in implementing policies and procedures to safeguard the organization against the risk of fraud and misconduct by its employees and agents. The traditional taxonomy for fraud in this context has relied on the accounting profession's elements of material misstatements in financial statements and misappropriations of assets. However, it has become common as well to include in the definition of fraud a legal dimension that encompasses material misstatements by employees or agents of an organization that induce reliance by others, to the substantive detriment of the others' financial, legal, reputational, and other interests.

In addition to recognizing these traditional accounting and legal dimensions, organizations increasingly are construing the scope for fraud and misconduct to include behavior that violates standards of the organizations themselves, applicable professional guidelines, or ethical principles and qualities to which members of relevant stakeholder constituencies, including the general public, commonly assent, including honesty, fairness, and transparency.

Examples of recent practices that implicate the role of the CFO and that reflect all three of these dimensions of fraud are the massive financial reporting scandals of the early 2000s involving Enron, WorldCom, Andersen, and other organizations; the secret backdating of stock options to increase executive compensation without authorization; and secret kickbacks from mutual fund administrative vendors to mutual fund advisers in exchange for continuing favorable referrals (a diversion of mutual fund investors' money to the advisers without authorization).

In the context of the increasingly complex regulatory frameworks affecting accounting, finance, and legal professionals, and corporate governance practices, the CFO has had to join with other members of corporate leadership, including legal counsel and ethics and compliance officers, to assume a significant role in managing organizational risk, particularly the risk of fraud and misconduct. In addition to complying with GAAP in reporting financial information, CFOs for companies that fall under the de jure or de facto requirements of the Sarbanes-Oxley Act must take a leading role in preparing reports on their internal controls for their annual reports and in providing the bases for management to recite its responsibility for "establishing and maintaining an adequate internal control structure and procedures for financial reporting" (§ 404). These reports also must contain management's "assessment of the effectiveness of the internal control structure and procedures" of the organization, an assessment to which the external auditor must attest as part of its examination.

On March 9, 2004, the Public Company Accounting Oversight Board (PCAOB) promulgated Auditing Standard No. 2, *An Audit of Internal Control Over Financial Reporting Performed in Conjunction with an Audit of Financial Statements*, to provide guidance for this process by reciting standards for auditors to follow in making such attestations according to the framework of the Committee of Sponsoring Organizations of the Treadway Commission. In response to widespread concern among companies that comply with the Sarbanes-Oxley Act, their auditors, and other interested parties regarding the absence of a materiality standard for discerning a practicable scope for issuing and attesting to such assessments, the SEC announced in May 2006 that it would propose changes to the rules of the PCAOB that would tailor the burdens and effects of complying with these requirements, with particular attention to the size and complexity of the organization under audit. The SEC later signaled the issuance of these proposed changes for public comment and review in late 2006.

The Sarbanes-Oxley Act § 406 also requires that companies that issue securities in public capital markets disclose whether they have adopted a "code of ethics" for their senior financial officers, including their CFOs. These companies similarly must disclose on SEC Form 8-K "any change in or waiver of the code." In the statute, the expression *code of ethics* refers to

> such standards as are reasonably necessary to promote . . . honest and ethical conduct . . . including . . . handling of . . . conflicts of interest . . . ; full, fair, accurate, timely, and understandable disclosure in . . . periodic reports . . . ; and compliance with . . . governmental rules and regulations.

While the legislative intent in drafting such language was admirable for the objective of promoting a culture of integrity and compliance within corporations under Sarbanes-Oxley requirements, the expression *code of ethics* is problematic in that it conflates a feature of legal authority and compliance—a "code"—with ethics, a normative discipline for deliberatively evaluating and reflectively justifying practices on the basis of articulable principles and argumentation. A more descriptively meaningful term in this context would have been *code of conduct*.

In addition to the Sarbanes-Oxley Act, the federal organizational sentencing guidelines for white-collar crime, the listing standards for the New York Stock Exchange and the NASDAQ, and other public sector and private sector frameworks around the world help prescribe practices that CFOs and other members of organizational leadership should follow to

- assess a practicable scope for the risks of fraud and misconduct that the organization faces;
- evaluate, design, and implement antifraud programs and controls, including ethics and compliance programs; and, thereby,
- seek to prevent, detect, and respond to instances of such fraud and misconduct, in a manner that is consistent with, and ideally integrated into, the organization's mission and identity to create value for the entity and to protect the articulable financial, legal, reputational, and ethical interests of its stakeholders.

The Essential Normative Dimension of CFO Leadership

An integral normative element for the executive authority and professional oversight that the CFO contributes to an organization is the principled leadership that he or she demonstrates as an adviser to the CEO and the board and as a guide to others in his or her unit or entity. The profile of the CFO includes not only technical competencies in finance, accounting, and related disciplines but also capacities for strategic thinking, independent professional judgment, and courageous and prudential decision making.

In particular, the CFO, as an executive adviser and a principled leader, must take an intellectually sophisticated and experientially informed approach to assessing the aforementioned dimensions of risk. The CFO's role is not to recommend whether to take risks but rather to make the case for the risks that are worth taking. There is no such thing as zero risk and a wise CFO will not seek to achieve it. Rather, these aforementioned capacities will enable him or her thoughtfully to assess, balance, manage, and advise others regarding the various forms of risk facing an organization, including regulatory, litigation, financial, reputational, and ethical risks.

The CFO monitors the financial and related dimensions of an entity's status and operations, captures this information in the idiomatic—even arcane—language of accounting and finance, and communicates it to the organization's senior leadership, participants in capital markets, and other relevant constituencies. In doing so, he or she discharges not just the aforementioned legal duties but also ethical duties, including *vigilance* in keeping abreast of key trends, issues, and developments that affect the financial and other dimensions of the organization's life, and *respect* for the moral autonomy of the stakeholders who have placed their trust in him or her as a steward of the organization's resources. The CFO abides by these ethical duties by demonstrating in his or her actions qualities of honesty, care, good faith, prudential judgment, courage, fairness, and even temperance, for example, when it comes to promulgating and enforcing policies for reimbursements of expenditures.

At the same time, the CFO remains aware that he or she offers only one of many authoritative voices within the organization and that the decisions that senior leadership makes require balancing the risks and options for action that correspond to the messages that emerge from these channels. Others communicate similarly urgent information regarding the entity's status and operations to senior leadership on matters of litigation and regulatory compliance; information technology; competitive standing and marketing matters; engineering, technological, and operational matters; human resources matters; and other issues. The CFO saliently demonstrates his or her professional judgment and prudential decision making by balancing the duties to (1) remain within his or her sphere of competency and yet (2) act in the best interests of the organization and its stakeholders generally, even when the latter course may mean raising questions or principled objections with the CEO and/or the board of directors over broader organizational policies and practices.

The CFO will maximize his or her effectiveness in balancing these duties and will sustain the conceptual clarity and meaningfulness of his or her recommendations and other contributions to the organization and its stakeholders regarding accounting, financial, and fraud risk management matters, when he or she speaks out of a demonstrable posture of principled leadership, independent professional judgment, and moral autonomy, and integrates this guidance with the ethical principles that underwrite the entity's organizational mission and identity.

In this way, the CFO can exercise oversight commensurate with an executive scope of responsibility in a corporation according to legal, managerial, and ethical guidelines; deploy and support a credible apparatus for a system of internal accounting control and other antifraud measures that will minimize the risk of misappropriation of the organization's assets or misrepresentations on its financial statements; and preserve and enlarge the organization's cash and investments, procure capital resources at the lowest weighted average cost, and create a foundation for the organization's financial growth so that it can continue as a going concern and be capable of benefiting its diverse stakeholder constituencies.

—Lester A. Myers

See also Accounting, Ethics of; Arthur Andersen; Autonomy; Certified Public Accountants (CPAs); Chief Executive Officer (CEO); Chief Operating Officer (COO); Contracts; Employment Contracts; Enron Corporation; Ethics of Care; Fiduciary Duty; Finance, Ethics of; Fraud; Internal Audit; Leadership; Moral Leadership; Public Company Accounting Oversight Board; Sarbanes-Oxley Act of 2002; Securities and Exchange Commission (SEC); Stakeholder Engagement; Stakeholder Responsibility; Stakeholder Theory; Stewardship; Virtue; Virtue and Leadership; Virtue Ethics; WorldCom

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Chief Operating Officer (COO)

A chief operating officer (COO) reports to the chief executive officer (CEO) and usually has responsibility for the daily internal operations of the company. COO is primarily a function, because other titles are sometimes used to designate substantially the same role: chief administrative officer, chief of staff, executive vice-chairman, and president without any further designation. A study in 1964 of 433 large companies in the United States showed no use of the title. By the 1970s, it was gaining popularity.

Although reporting lines in companies vary with their organizational structures, commonly most business units and some staff areas (e.g., information technology, marketing, human resources, and procurement) report to the COO. In a company with operating subsidiaries that have their own presidents, sometimes the presidents of the most significant entities report directly to the CEO.

In organizations that have a CEO/COO structure, the CEO is generally said to be responsible for external matters and for broad corporate issues such as vision, strategy, long-range planning, acquisitions, and corporate governance. In contrast, the COO's role is to function internally as the operational head of the company. As will be discussed later, the COO could also have a significant role in developing a climate of ethical conduct in the company. All this is not to say that the COO has an entirely internal job, because there are situations where he or she must deal with external customers and suppliers. However, these are generally limited to matters that have a significant bearing on operational issues.

Some observers maintain that a stark distinction between external and internal roles does not accurately characterize the actual working team relationship between the two top officers in most companies. Rather, they are more likely to be partners in most things.

Being a COO is sometimes said to be the most difficult job in a corporation because the level of responsibility is high, yet the most senior level of authority still resides with the CEO. This power imbalance can be the source of friction, especially if the COO was hired as the CEO-in-waiting, not a permanent number two in the hierarchy. Many of the qualities that are sought when the COO is recruited are precisely the characteristics that can lead to being impatient or jealous of the CEO.

Given the potential for a mismatch between the CEO and COO, it is important that the recruiting process give due consideration to the need for an alignment of competencies, values, and strategic orientation between the two top executives. As well, the selection process must result in giving the new COO a clear set of expectations with respect to succession planning for the CEO. Since the CEO is normally responsible for recruiting the COO, some commentators recommend that members of the board be involved to provide some independent judgment on the likely fit between the two executives.

An Executive Team as COO

Increasingly, the role of COO is being performed by an executive team that is sometimes called office of the CEO, or office of the chairperson. The composition of the team can vary widely, but frequently it is made up of the heads of the most significant units (e.g., divisions and subsidiaries) and functional areas (e.g., finance, legal, human resources, and marketing). The executive team supports the CEO in providing strategic, operational, and institutional leadership. A well-functioning team is interdependent and interactive. As the surrogate COO, the team can bring synergies to the office by providing improved coordination across units and functional areas. The growth in popularity of the executive team model reflects the increasing complexity of organizational life stemming from globalization, the technology revolution, evolving organization forms, and the increasing pace of change.

Some CEOs favor the executive team model because it both removes the expense of a highly paid senior officer and eliminates a management layer between the CEO and the operating units. As well, it does away with what some think is an artificial distinction between strategy formulation and implementation.

Critics of the executive team model point to the conflict that can arise from bringing together individuals whose prior success in corporate life has come from the ability to lead as an individual, not a team member. Group decision making can be fraught with difficulty if trust, openness, and collaboration give way to self-interest and an absence of concern for the overall corporate good. This is sometimes referred to as cosmetic teamwork—the trappings of teamwork are prominently displayed, but real team decision making is not occurring.

The COO and executive team models both share the CEO succession issue. In fact, the team model is sometimes used precisely to set up a competition for CEO succession. Proponents of the team model point out that it may not be the best approach in all cases, but maintain that where it is appropriate successful teams need to have the right composition of members, work to achieve consensus in decision making, be open and forthright in critiquing the positions taken by other members, and maintain loyalty to the team as a whole.

Ethics and the COO

Not everyone believes that the senior executives of a corporation should explicitly attempt to develop strategies around building a socially responsible and ethically sound organization. However, for those who support the ethical mandate, one question is, "Who should take the managerial lead?" Usually, it is the CEO who is said to be ultimately responsible for setting the moral tone, and it is the job of all managers to ensure good conduct. But because the COO is at the nexus of all daily operations, being a key figure would seem to be reasonable.

From an operational perspective, ethical conduct is driven to a large extent by the myriad laws, regulations, industry standards, and codes of conduct with which the company and its employees must comply. For instance, in many countries there are statutory requirements that cover parts of the ethical terrain such as environmental preservation, workplace health and safety, product safety, whistleblower protection, and privacy. And, there are many regulatory strictures that flow from legislation requiring adherence. Although they can vary by industry, common examples are the requirements in public companies for audited financial statements and financial filings to securities commissions and stock exchanges. In addition, some industries have self-regulatory standards, such as professional codes of conduct for lawyers, accountants, engineers, and architects. Finally, many companies have their own codes of conduct covering prescribed relations between employees and with the company's stakeholders.

In some organizations, the COO devolves responsibility for compliance to other executives. For instance, dealing with complaints or concerns about employee issues, such as privacy, might be delegated to a chief privacy officer, ombudsperson, or vice president, human resources. Alternatively, some organizations employ an ethics officer. A compliance officer, or in-house legal counsel, might be given responsibility for regulatory compliance such as dealing with the securities commission; and the chief financial officer could look after the audit compliance. Whatever the specific organizational arrangement, the COO is ultimately in charge.

Some writers maintain that regulatory compliance is an essential part of being a socially and ethically responsible organization, but only at a base level. Rules and regulations, they say, deal with what we must or should do, but not with what we could do. In their view, simply following the rules does not capture what a company might aspire to do as a socially responsible organization.

According to this view, a company should strive to attain organizational integrity. Such an entity is one in which employees have a sense of responsibility for the way they deal with others; are honest, open, and truthful; keep promises; avoid malicious gossip; and come to the assistance of others when there is no personal gain. Equally, those working in the organization need to feel as though they belong and that they subscribe to the mission and values. The centrality of the COO in bringing this about partly resides in having control over processes such as hiring, promotion, annual review, establishing of objectives, employee development, and compensation. Through these, the COO can set the criteria that reinforce and reward integrity.

This view of the COO's role in developing organizational integrity rests on a theory of the firm that places corporate social responsibility as an important obligation of both the organization and its management. Sometimes, it is argued that because of the enormous size of modern corporations, they have the power to affect the lives of people, not only within the organization but also in communities and society as a whole. With this power comes a responsibility to act in ways that support societal objectives, or at least avoids harming them.

In opposition is the classical theory of the firm that views the corporation merely as an economic entity, which should only be evaluated on the basis of economic criteria, such as efficiency and growth in production of goods and services. Profit is its primary motivation, and the role of management is to increase profits for the benefit of stockholders. Proponents of the theory maintain that efficiently run corporations benefit employees, suppliers, customers, the economy, and society as a whole. There is no room in the theory for management legitimately to engage in non-wealth-generating activities such as pursuing social or ethical objectives. This is a role for other social institutions. Indeed, one of the theory's most famous proponents, Nobel Laureate Milton Friedman, maintains that to spend company funds on social programs is the equivalent of taxing stockholders.

Critics respond by saying that the classical theory is overly restrictive in viewing the corporation as exclusively an economic entity. Rather, they maintain that there are other stakeholders (e.g., employees, customers, suppliers, and communities) to whom it has responsibilities. While governments and other social agencies may have the primary obligation to ensure public well-being, a corporation should lend a hand where needs in close proximity are urgent and where the corporation has the capacity to respond while others do not.

A theory that goes some way to bridging the gap between programmatic agendas of corporate social responsibility and the socially skeletal classical theory is the moral minimum of the market. This position holds that corporations must at least conform to the elementary principles of face-to-face civilized behavior. As one commentator has noted, this leaves a lot of room for virtues such as honesty, openness, fairness, and avoidance of harming others. When taken together, these values come very close to the characterization given to integrity above.

This theory ties back into the role of the COO because it points to another means of fostering integrity that does not involve the more elaborate establishment of ethics programs that use corporate resources. It is the leadership shown by the COO in terms of personal integrity. As the most senior operations officer, this is the person who employees expect to embody the qualities and characteristics that define integrity in their organization. If the COO is not seen to be a leader in this regard or, worse, acts without integrity, ethical language found in mission statements, policies, and codes has little traction.

—A. Scott Carson

See also Chief Executive Officer (CEO); Chief Financial Officer (CFO); Chief Privacy Officer (CPO); Corporate Social Responsibility (CSR) and Corporate Social Performance (CSP); Corporate Social Responsiveness; Ethical Culture and Climate; Ethical Role of the Manager; Integrity; Ombudsperson

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Chief Privacy Officer (CPO)

The chief privacy officer (CPO) is an executive officer responsible for the balance between consumer and employee demand for privacy and the organizational need for information. The position is generally high-ranking and often reports directly to the chief executive officer (CEO). Depending on the size of the organization, the CPO may need to put together a team of experts and stakeholders in the form of a privacy board. It is not limited to the private sector, and it can also be found in governmental organizations. The position is a recent development in the organizational structure with the first corporate CPOs having been hired in the late in 1990s.

The CPO's job essentially revolves around satisfying the needs of privacy stakeholders and avoiding privacy-related risks while enabling reasonable data collection by the organization. The main deliverables of the job are the so-called privacy policy and the resulting privacy program. Finally, the CPO must conduct periodic audits of the organizational compliance with the privacy policy and laws, the organization's implementation of the privacy program, the media and political environments, and the state of organizational technology. The CPO position is interdisciplinary in nature and involves expert knowledge of legal matters and information systems (IS), especially in the area of security. In addition to understanding these two fields, the CPO must also communicate with marketing, human resources (HR), and public relations (PR) departments.

Privacy Stakeholders

The primary stakeholders that the CPO has to consider in developing the privacy policy and program are the individual consumers, the employees, and business-to-business (B2B) customers.

Individual Consumers

The organization's customers represent an essential source of its marketing data. For example, consider the implementation of grocery store membership card programs. The programs require customers to use their membership cards to get the advertised savings. When the customer scans the card at the checkout stand, the entire purchase list is stored for future analysis. The stores can use the obtained information for marketing trend analysis and to tailor specific offers for that particular customer. Most grocery store customers consider the programs fairly innocuous to their privacy since the system stores only a list of their purchases. However, as additional information, such as credit card numbers and prescription medications, are added to the database, customers might see the program in a different light. Changes in how customers see the organization is of concern to CPOs of both physical and virtual store fronts. After all, while collecting and analyzing such information may be legal, consumers may not always agree that it is ethical. The resulting decrease in trust toward the organization may then not only negatively impact its image but also its revenue.

B2B Customers

Organizations that cater to businesses may face data protection concerns from these types of customers as well. Business clients are primarily concerned about the sharing of insider data and corporate trade secrets. Consider the following service option offered by several companies providing server software for applications such as enterprise performance monitoring. These software makers are offering an option for the customer's server to be linked to the software maker's so that the software maker can quickly analyze problems found on the customer's side. Some software makers have even packaged this option as default on installation. Although the potential for rapid troubleshooting was lucrative, many business customers were concerned about an external source having access to their data. The involvement of the CPO on the software maker's side in such a marketing plan may not only have advised the marketing and the research and development departments on the external perception but may also have helped develop a privacy policy targeted to potential customers of the option, assuring them that their data would not be used by the software maker and that preventative measures would be taken to ensure the safety of the data. In addition, the business customers' CPO may need to be involved to verify that new software installations comply with the privacy policy.

Employees

The CPO must also consider the privacy of the organization's employees. There are a number of U.S. legislative items that regulate the means and the extent of employee surveillance and monitoring in both private and public sectors. In addition, the employees may feel that they have rights to privacy in the workplace although these rights may not be protected legally. When dealing with employees, the CPO must communicate with the HR department to make sure that the organization's privacy policy is in compliance with applicable laws. Otherwise, employees dissatisfied with the surveillance and the use of the surveillance data may sue the organization, leading to negative impacts in terms of finances and PR. In addition, the CPO must make sure that employees in contact with sensitive customer data understand its criticality and do not abuse their access.

Privacy-Related Risks

The discussion of the privacy stakeholders above has alluded to a number of privacy-related risks that the CPO must mitigate. The most obvious risk is that of litigation both by customers and by employees. For example, two U.S. laws have had a very high impact on the privacy of customer information in the financial and health care industries: the Health Insurance Portability and Accountability Act and the Financial Modernization Act (aka the Gramm-Leach-Bliley Act). Businesses with Internet presence have also been affected by the Children's Online Privacy Protection Act, which regulates the online collection of information from children less than 13 years of age. The organization may also come under fire from employees based on the violation of the Fourth Amendment to the U.S. Constitution, which protects against unreasonable searches and seizures, as well as the Electronic Communication Privacy Act (ECPA), which regulates access, use, disclosure, privacy protection, and the interception of electronic communication. If the company does not properly protect itself from litigation it may face severe financial risks as the costs of litigation rise. Finally, the negative information that spreads about the organization in the media poses a significant risk in the areas of PR, customer development, and, finally, sales.

Privacy Policy

A privacy policy states how the organization obtains data, how the collected data are used, and how an individual can access and alter (including withdraw) personal data, as well as what security measures the organization is taking to protect the collected data. In creating the privacy policy, the CPO must communicate with members of the legal, HR, finance, IS, and PR departments. The individuals from these departments can assist the CPO in addressing their departments' unique privacy issues and help with policy decisions in line with the current legal, political, and media environments. The PR department is especially important in this part of the CPO's job as the organization's privacy policy must be communicated to the privacy stakeholders. In communicating the policy, the CPO and the PR personnel must focus on (1) gaining trust toward the organization and (2) training customers and employees with regard to necessary privacy actions. A variety of means can be employed in communicating the policy and its implications, including press releases, meetings, and presentations. In the area of gaining trust among employees, the town hall meeting format can be especially useful as the CPO and other key personnel involved with the privacy policy can answer questions in person with regard to the policy. In training users and employees with respect to privacy-policy-related actions, the CPO, together with the IS and the PR departments, may chose to provide guides via the World Wide Web. This is an especially useful method for organizations with strong Internet and intranet presences.

Privacy Program

The natural next step after creating the privacy policy is the design of the privacy program. A privacy program is essentially the implementation plan for the privacy policy. In designing and implementing a privacy program, U.S. CPOs may follow the Federal Trade Commission's Fair Information Practice Principles. These are notice, choice, access, integrity, and enforcement. In implementing the privacy program and following the above principles, the CPO must communicate with the legal, information technology (IT), and security groups of the organization. The legal group must be involved in phrasing the notice and in creating valid options for notification of consent to the notice and the policy it represents. Such notice may need to be given and consent may need to be received for both customer data collection and for employee surveillance. For example, employees must be informed that they are monitored via closed-circuit television (CCTV), and customers should be told if the data collected about them during their transactions may be sold to third parties.

The CPO must work closely with the organization's IT group to implement the access, integrity, and enforcement principles. The IT group can create a Web site where customers can view, alter, and withdraw their data from the organization's database. The group is also responsible for maintaining the integrity of the data and avoiding unauthorized access to the databases, as well as for enforcing data-monitoring practices such as database audits on employees viewing and altering sensitive data. In resolving situations where the privacy policy was violated, the CPO must work closely with the legal and HR departments to prevent any repercussions to the organization as the violators are apprehended and to ensure that the victims are redressed accordingly.

Auditing

To asses how well the privacy policy is being followed and the extent to which the privacy program has been implemented, the CPO must perform periodic audits. First, the CPO must conduct audits of policy compliance. This audit must cover the communication of the policy to the stakeholders and how well the stakeholders have been trained on the policy. Such an audit should include a review of the company's Internet and intranet Web sites to find out whether the privacy policies have been stated there. In addition, the CPO may need to know whether there are proper notices of CCTV activity and whether any unlawful or undisclosed employee surveillance practices are in place. The CPO should also audit the information stored about customers to identify whether the information is personally identifiable, sensitive, or related to specific statutory requirements. With the help of the legal department, the CPO should audit the privacy policy and program to verify that they are in compliance with the applicable laws. If not, change management programs should be implemented to bring the organization into a state of compliance. The PR department can help the CPO conduct an audit of the media and political environments. For example, if the PR department notifies the CPO that the media has been increasing its watch of companies selling customer data, the CPO may find that the privacy policy needs to be altered to preemptively accommodate the upcoming changes. Finally, the CPO must audit the technology for data collection and protection currently employed by the organization. Technology must be up-to-date and in compliance with the latest legal standards. If necessary, the privacy program may be updated to include new technology to ensure technological compliance.

Conclusion

The CPO must continuously follow the changes in the organization and its environment as new stakeholders, legal requirements, and technological advancements emerge. Continuous communication with the legal, HR, marketing, finance, IT, and PR departments keeps the CPO and the privacy team abreast of new developments and helps them make quick adjustments to the company's privacy policy, keeping it relevant and up-to-date. Updates to the privacy policy must flow through to the privacy program, ensuring that the necessary tools and technologies are employed for the organization to fully comply with the policy.

—Zoya A. Voronovich and Kai R. Larsen

See also Employee Monitoring and Surveillance; Health Insurance Portability and Accountability Act

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Child Labor

Child labor is a complex phenomenon that has been complicated further by definitional difficulties. Traditionally, many government officials, union representatives, and social reformers have used the term *child labor* to refer to any wage work by children in the labor market. Oftentimes, they have argued that all such work is harmful to children and, therefore, "child labor" should be prohibited. In recent years, increasing numbers of commentators have come to define child labor more narrowly as that work that is harmful to children as distinct from other forms of work either not harmful or beneficial to their development. The present article uses the terms *child work* or *child employment* to refer to children's engagement in any economic activity with the term *child labor* reserved for their participation in those that are harmful.

Work by children has undoubtedly existed throughout human history. However, it first emerged as a public issue in the early stages of the Industrial Revolution as the locus of their work moved outside the family and into the factory. Changes in technology created jobs requiring few skills in a number of industries, most notably textiles, and mill owners often sought to employ poor children in their factories. The owners, of course, benefited from this cheap labor, but many others also welcomed the growing demands for child factory workers. Poor families viewed their children's wages as vital to their welfare. The upper classes feared the potential for social disruptions by numerous idle children and regarded their employment as preparation for productive roles as adults. It was also argued that nations depended for their welfare on a disciplined, skilled, and healthy population.

Early governmental efforts focused on regulating conditions and hours of factory work rather than prohibiting children from working. Steps were often taken as well to provide schooling for young workers. The measures drew support both from those concerned with children's welfare and others intent on improving conditions for adult workers. Over the course of the 19th century, growing resistance to work by children and concerns about the idleness of many others led many Western nations to adopt compulsory school requirements. These laws enabled states to monitor all children's educational, physical, and psychological development while limiting their access to jobs.

If the Industrial Revolution provoked the earliest debates about children's work, globalization has rekindled old conflicts and posed new problems. Growing exports from developing countries have led to concerns about trade deficits and the loss of jobs in many industrialized countries. Government officials and union leaders attribute part of the problem to the lax labor standards in the developing countries and cite the pervasive employment of children. However, concerns regarding the ethics of work by children are evident as well. Many consumers in the developed world wince at graphic reports of children working under hazardous conditions to produce clothes, rugs, furniture, and other products for their use. Activists have demanded governmental action on humanitarian grounds to ban imports of goods made by children and have pressured retailers such as Nike, Wal-Mart, and the Gap to monitor their foreign contractors' labor practices.

Efforts by governments and activists in the developed world to end work harmful to children in the developing countries have often been taken in concert with the United Nations and its agencies. Founded in 1919, the International Labour Organization (ILO) has, as its mission, the development and promulgation of labor standards including those pertaining to the employment of children. The ILO functions through "conventions" or proposed standards, which nations may voluntarily agree to adopt. One of the most fundamental is the Minimum Age Convention of 1973 (#138), which updated earlier conventions and provides much of the ILO's framework for defining "child labor." For children less than 12 years, any economic activity is taken to be child labor. For those between 12 and 14 years, an economic activity is considered child labor when it is hazardous or the child performs it for more than a few hours per week. For those between 15 and 17 years, child labor is defined as hazardous work. Based on these definitions, the ILO estimated that in 2002 about 186 million 5- to 14-year-olds (about 15% of this cohort) were child laborers plus 59 million 15- to 17-year-olds. The vast majority are found in developing areas, especially Asia and Sub-Saharan Africa. Most work for their families in agriculture or small businesses engaged in commerce or light industry. Significant numbers of girls work in the households of others as domestic servants. Although highly visible in the media, only a small percentage, less than 5%, are found in export industries, most notably apparel, carpets, shoes, textiles, and furniture. Even with some flexibility for poor nations (e.g., children can work full-time at 14 rather than 15 years of age), the aim of this convention to prohibit nearly all work by children has led many developing nations to withhold ratification.

In 1989, with the support of about 140 nations, the General Assembly of the United Nations adopted the Convention on the Rights of the Child. This convention is widely regarded as more child centered and tolerant of cultural and national diversity than the ILO's Minimum Age Convention. It specifies a host of children's rights including the right to be protected from work that harms them, the right to an education, and the right to participate in the formulation of public policies affecting them. Article 3 stipulates that such policies must be based on the best interests of the child rather than those of adult stakeholders. The recognition that not all work is harmful has made this convention more congenial with the perspectives of many developing nations.

Ten years later, the ILO continued efforts to develop global labor standards acceptable to all nations with the Worst Forms of Child Labor Convention (#182). This commits signatories to "take immediate and effective measures" to eliminate child slavery and other forms of forced labor, prostitution, and involvement in drug trafficking as well as "work which . . . is likely to harm the health, safety or morals of children" as determined by the national authorities in consultation with the children involved. Indicative of the widespread support for this convention, 156 nations have already ratified this convention by 2005.

Despite progress in the formulation of global agreements regarding work by children, significant conflicts remain between those seeking universal standards for regulating work by children and those advocating flexible implementation in light of differences in culture, capacity of political institutions, and level of economic development among nations. Many officials, reformers, and unionists in industrialized nations demand adherence to the Minimum Age Convention on the grounds that work typically harms children directly or through reduced time for education. Many representatives of government and civil society in developing countries regard such demands as forms of ethical and cultural imperialism that mask protectionist interests. They are joined by increasing numbers of officials from international agencies (e.g., UNICEF), representatives of nongovernmental organizations (e.g., Save the Children Sweden), and child development specialists who advocate child-centered national policies grounded in the best interests of the children. They contend that blanket prohibitions against all forms of employment by children fail to recognize the diversity of jobs they perform and contexts in which they work. While the worst forms of child labor clearly harm children, other working conditions and contexts, including many formal apprenticeship programs and much work supervised by parents, provide substantial benefits and contribute to their development. However, many and perhaps most jobs performed by children combine a variety of actual and potential benefits with some clear costs and possible risks.

Advocates of regulatory flexibility and child-centered policies argue further that the best interests of children require that the circumstances of working children inform public policies pertaining to their work. Poverty, tradition, poor schools, and governmental incapacity may well justify certain kinds of work by children that, to outside observers, might appear undesirable or even harmful. Because these determinations are complex and because some consequences of work depend on children's interpretation of their experiences, many argue that child workers must participate in policy deliberations regarding their work. Such participation provides a more nuanced view of the workplace, the benefits children derive from it and the hazards they encounter. As a result, authorities may find the option of eliminating harmful practices a better alternative than prohibiting children from working altogether. Finally, child-centered advocates argue that children develop through their participation in the world of work. Through work experiences appropriate to their level of maturity, they encounter problems that challenge them to learn how to cope with risks and protect themselves.

Disputes between those demanding universal standards and those advocating flexibility have stimulated increasing research on work by children. Family poverty has been the most widely adopted explanation for children's work in developing areas. The poor quality of schooling in poor communities is often cited as another explanation for families to seek work for their children. Research by economists suggests that work may reduce children's efforts in school and poor-quality schools may increase the attraction of work.

Whether children find jobs depends on their opportunities to work. Parents with land or businesses often employ their own children, and research in developing areas suggests that most children do, in fact, work for their families. Some analysts argue that globalization forces many businesses in developing nations to compete internationally on lower costs, which some achieve by employing children. However, the few studies to date do not appear to support this thesis.

Cultural explanations of work by children are also advanced. Many argue that traditional cultures regard work by children as fundamental to their socialization. Research does suggest that illiterate parents are more apt to seek jobs for their children. Others attribute work by children to their efforts to escape traditional obligations to perform unpaid domestic work. Similarly, some argue that children's exposure in developing areas to modern, consumer cultures, via the mass media, creates desires for youth-oriented consumer items that they can only purchase by paid employment.

Far less attention has been devoted to the consequences of work by children in developing areas. Available studies focus largely on the implications of work for education and derive from economists' concerns that early work involvements reduce the time available for school and, consequently, the store of human capital available to the society. Their research often reveals that the educational performance of working children is lower than that of nonworkers. However, the rival hypothesis—that children performing poorly in school are more likely to work—is equally plausible. In addition, this literature fails to distinguish between different forms of work that have different implications for child workers' education. Far less research has been done on the implications of work for children's attitudes, values, behavior, and physical or mental health.

Efforts to deal with child work by public policy makers have focused largely on its elimination through legislative means. This approach rests on two controversial assumptions. The first is that much child work is undesirable and should be eliminated because it not only harms children but also undercuts adult employment and wages. The second is that legalistic means are feasible because child work is visible and that government has substantial capacity to monitor employer behavior and apprehend violators. The persistence of work by children throughout the developing world testifies to the insufficiency of this approach. Part of the problem stems from the fact that many in developing nations, including child workers, believe that the benefits to children from working often exceed the costs. In addition, much of the work by children occurs within small, family-run operations that are difficult to monitor. Finally, governments in many developing nations lack the capability to enforce employment laws.

The failure of legal prohibitions on children's work has led to experimentation with other approaches. Because inadequacies in schools often drive children to work, many efforts are being made to make them more attractive to students and their families. Some programs focus on improving the schools themselves—their availability, location, physical structures, materials and equipment, and the teachers. Another approach is to reduce the costs to students of uniforms, books, and other items that sometimes require children to work to be able to afford. A third involves more flexible schedules and curricula better adapted to working children.

Poor families with children working in particularly harmful circumstances are the targets of other programs designed to reduce the opportunity costs of attending school by providing cash transfers to offset income lost by children when they stop work to devote more time to education. Consumers have been the focus of efforts to end work by children by affecting purchasing decisions. Boycotts have followed extensive publicity of child employment by foreign contractors of Nike and other retailers. Other efforts, such as the Rugmark campaign to end child work in the Bangladesh carpet industry, have used labels on products to indicate that no child work was involved in their production. Such labeling initiatives facilitate consumer efforts to apply pressures on producers to end child work.

Difficulties in mobilizing consumers have often led activists in industrialized nations to advocate trade sanctions that would restrict imports of products from industries employing children. Opponents of such policies cite the potential for adverse unintended consequences from such sanctions. In particular, they note the cases of the Bangladesh garment industry and Pakistani soccer ball manufacturers who, when threatened with trade sanctions, fired large numbers of children. Unfortunately, very few returned to school. Most sought work elsewhere with some reportedly becoming prostitutes and others trafficking in drugs. Thus, as with many other efforts to curb child labor, the results of this intervention were different from those intended.

At the core of much of the controversy about child work are ethical considerations. The immediate response of most people in developed countries to work by children is that it is immoral and ought to be eliminated. However, a deeper understanding of the many forms and contexts of such work suggests that the moral issues are more nuanced and complex. Clearly, certain forms of child work are morally indefensible. These are the so-called worst forms of child labor, which include activities such as bonded child labor, drug trafficking, soldiering, and prostitution. These are so dangerous and degrading that no one even attempts to offer a defense for them. The widespread adoption of the ILO convention targeting these forms of child labor bears testament to this.

Opponents of attempts to outlaw work by children have generally supported their position with utilitarian arguments. Thus, even if there are some harms to the child worker, these would be offset by benefits to the child, his or her family, and the society as a whole. These would include providing much needed financial benefits to the child and his or her family, enhancing job skill and character development, keeping the child occupied and out of trouble, and promoting economic and social development nationwide. Yet other defenders of child work (especially so-called child liberation advocates) contend that children should be free to decide for themselves whether or not they want to work in formal work settings.

The ethical case against work by children is usually argued in terms of violations of rights of child workers. Many people feel that children have basic rights of access to adequate shelter, health care, security, education, and other basic amenities of life until they achieve some designated level of maturity. Within this context, work by children is viewed as incompatible with education and, thus, inconsistent with the basic rights of children. Moreover, some forms of child labor are hazardous and further impinge on these basic rights.

Given the many forms, contexts, and consequences of work by children, blanket condemnations or defenses seem inappropriate. Moral judgments on child employment would thus benefit from an in-depth understanding of the nature of the work, its societal context, and the consequences of the work to the children themselves as well as how these relate to basic rights of children. Moreover, children's own views on these matters should be taken into account.

Looking forward, discussions of the ethics of child work and child labor will benefit by more thorough attention to three issues. The first of these has to do with how children develop and, more specifically, how much protection and, conversely, exposure to risk they need to become capable adults. The second has to do with the nature of work and, specifically, the need to acknowledge that invisible and devalued domestic work often poses as many hazards to children as jobs in the labor market. Third and most important is the development of a more balanced view that recognizes the value of some forms of work by children as well as the harm caused by other types.

—J. Lawrence French and Richard E. Wokutch

See also Fair Labor Association (FLA); Nike, Inc.; Rights, Theories of; Sweatshops; Women in the Workplace; Worker Rights Consortium (WRC); Working Conditions

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CHILDREN, MARKETING TO

The marketing of products to children is not a new phenomenon, and certainly, the historical record is rife with examples of popular product campaigns geared toward children. However, recent decades have seen an unprecedented expansion in marketing efforts aimed at children. Such efforts involve both direct and indirect forms of marketing to children. Direct marketing to children involves advertising and related activities geared toward soliciting children's awareness of and interest in specific products. Indirect forms of marketing to children involve similar efforts devoted to creating consciousness of products designed for younger persons among parents and others responsible for purchasing products for children. The average child now views tens of thousands of television and print advertisements every year, and magazines, television shows, and Web sites aimed exclusively at children provide a fertile medium for marketers to appeal to this audience directly. Indeed, the line between entertainment and advertisement is now routinely blurred in the television programs and movies viewed by children, which are often closely connected to marketing campaigns that sell toys, games, and other products centered on the characters and themes of these shows. Furthermore, marketing departments have become increasingly sophisticated in the their attempts to appeal to children, often making use of extensive market research on the buying habits of children and the expertise of child psychologists in developing marketing strategies.

Essentially interconnected with the expansion of marketing to children is the increased disposable wealth of children, who now directly spend billions of dollars every year on toys, games, and other products. Children are also indirectly responsible for influencing billions of dollars in adult expenditures on food, clothing, vacations, and assorted goods and services. There is, thus, no doubt that children represent an important element in the modern consumer economy. In this sense, some have seen the expansion in direct marketing to children as simply responding to the increased purchasing power of this segment of the population. Nonetheless, this proliferation in the number of products marketed to children as well as in the techniques used to market these products has raised a number of concerns about the ethical status of many of these efforts. While some of the concerns raised about marketing efforts directed at children reflect more general questions about marketing ethics, others rest on more specific concerns with the practices of marketing to children. Ethical concerns of the latter type often stem from considerations of the differences between adult and children consumers. Because of these differences, most ethicists argue that higher ethical, and often regulatory, standards are appropriate for the marketing of products to children.

Suitable for Children?

A number of the concerns raised by marketing directed at children turn on the kinds of products that such marketing involves. Questions of an ethical nature have been raised in this direction about marketing campaigns that involve products that are dangerous, inappropriate, or useless. While it may be legitimate to assume that adult consumers have the capacity to rationally evaluate the relative merits and risks of products on their own, children, particularly those of a younger age, lack the understanding and experience necessary to independently judge the worthiness of many products. There is good reason for, thus, believing that even in a market economy children should be provided additional protection against the marketing of harmful products. Differences exist though in terms of the marketing of products of questionable suitability for children and, thus, as to which products, and to what extent, marketers should be restricted or regulated in appealing to children.

The clearest cases of ethically problematic marketing campaigns directed at children are those that involve products that are inherently dangerous. The most notorious cases involve products such as cigarettes and alcohol, which are not only harmful but which children are not legally permitted to purchase either. Despite such legal restrictions, there have, nevertheless, been several cases of marketing campaigns involving such products that were apparently directed toward children and teen-aged youth. A particularly notorious example of such a case was the advertising campaign used to market Camel brand cigarettes through the use of the "cool" cartoon figure Joe Camel. Critics argued the use of this Disney-like cartoon figure to market cigarettes was designed to purposely appeal to a younger audience. Eventually, under pressure from the Federal Trade Commission (FTC) and various interest groups such as the American Medical Association, R. J. Reynolds agreed to discontinue use of the Joe Camel character. In a similar vein, critics have contended that marketers often appeal to children of unsuitable age in advertising movies, video games, and other media that contain sexual and violent content of an age-restricted nature. Certainly, any company that does purposefully market such products to children is engaging in an ethically dubious practice. At a minimum, if a product has been deemed to be inappropriate for persons under a certain age by law or regulation, marketers have a moral and legal responsibility not to target younger persons in their advertising campaigns.

Controversy also exists concerning the marketing of products to children that pose less direct harms. For instance, a number of groups have expressed concerns over the extensive marketing of soft drinks, snacks, sweets, and fast-food products to children. Given the poor nutritional value of most of these products, these critics argue that children are being encouraged to adopt unhealthy eating habits that can have long-term health consequences. Other marketing efforts directed at children have been targeted by critics for selling products that present unhealthy or unrealistic images to children. For example, some critics have argued that many of the dolls marketed to girls present them with a female body image that is unrealistic and that in doing so contribute to the self-image problems that are widespread among young females. Finally, some critics simply express concern over what they see as the widespread marketing of products to children that, while not harmful, have no positive educational, social, or personal value either. These critics argue that high-pressure advertising campaigns often exploit the naivety of children in marketing worthless products to them.

Advertising Techniques

Questions of the last-mentioned sort raise further considerations about the means by which products are marketed to children and, in particular, to the methods of advertising. Here, two issues have been given particular prominence in discussions of marketing to children. One involves the pervasiveness of advertising to children and the other the means by which advertising appeals to children. As to the first point, a number of ethicists have expressed worries about the extent to which advertising has infiltrated nearly every childhood activity. They argue that, on a daily basis, children are bombarded with advertisements on television, the Internet, in public spaces, and even at schools and other community institutions. Defenders of the marketing industry have traditionally pointed to the role of parents in filtering what children see and argued that the primary responsibility for monitoring the consumer habits of children belongs with the family. However, critics suggest that the strength of this argument is weakened by a consideration of the ubiquitous nature of advertising to children in contemporary society that makes it nearly impossible for parents to adequately monitor and counter these commercial influences.

The second issue turns on the kinds of methods that advertisers use to appeal to children. Here, many critics worry about the extent to which emotional appeals and image advertising can influence younger consumers who can be expected to have less maturity and less developed judgment than adult consumers. The FTC, which is responsible for protecting consumers from deceptive advertising practices, has generally recognized this in applying more stringent standards to advertisements directed at children than to those aimed at adults. Despite this more strident regulation by the FTC of advertising to children, a number of critics argue that much of the advertising that is directed at children still makes use of emotionally manipulative techniques in appealing to younger consumers. For example, some critics have charged that advertising directed at children often plays on the fears, insecurities, and unrealistic expectations of children to influence their decisions about products. To the extent that children are more easily swayed by purely emotional appeals, such advertising can be seen as unduly manipulative.

Advances in technology have also raised concerns about the ethics of marketing to children. Of particular prominence here have been questions about the various methods by which marketers target children online, a number of which have come under scrutiny in recent years. Sophisticated marketers have the capability to track the online activities of children and to develop advertising personalized to individual users. Interactive advertising sites for children often also blend entertainment and advertising in a near seamless fashion, and various banner advertisements redirect children who click on them to company-sponsored sites. Such practices tend to intensify questions as to what extent children have the capacities to identify the advertising appeals intermixed with such online activities and to resist their influence. Online marketing techniques can involve the solicitation of various forms of information from and about children and their online habits as well. The collecting and selling of such information raises further ethical questions about protecting the privacy of children online, who are less appreciative of the importance of informational privacy.

Regulatory and Industry Responses

A number of efforts have been made by the government, industry groups, and individual companies to initiate regulations and policies that address some of the specific ethical concerns raised above. At the federal level, the Children's Television Act of 1990 can be seen as a response to the increasing commercialization of children's television programming. The act requires that television stations carry a designated amount of programming for children that contains an educational and information component. In 2000, the Children's Online Privacy Protection Act was also passed. This act requires that commercial Web sites that are aimed at children less than 13 years of age obtain parental permission before collecting personal information from a child. At the industry level, the National Advertising Review Council, an organization formed through the auspices of a number of national advertising trade associations and the Better Business Bureau, established the Children's Advertising Review Unit (CARU) in 1974 to review and evaluate advertising directed toward children. The CARU has developed a set of self-regulatory guidelines to promote honesty and responsibility in advertising to children and also has included special provisions directed toward protecting children in the online environment. Some companies and marketing firms have also sought to adopt specific policies and codes of ethics with regard to marketing to children as well, including a few large corporations that have traditionally had a significant role in marketing their products to children. For instance, in 2005, Kraft Foods announced the adoption of a set of standards for marketing to children that included setting nutritional standards for foods advertised to children between 6 and 11 years of age.

Broader Social Issues

Issues surrounding the proliferation of advertising to children and the uses of associative advertising also spill over into larger debates about the social impact of marketing to children. In this vein, some commentators worry that the tendency by marketers to target younger and younger children and to do so in increasingly numerous and sophisticated ways poses a more general threat to human flourishing and important social values. First, critics of this stripe contend that by inculcating desires for unnecessary and potentially harmful products in children from an early age, particularly through associative and image advertising, marketers threaten the ability of children to develop as fully rational and autonomous persons. Second, some have tied concerns over marketing to children to more general concerns with consumerism. By encouraging children to become fervent consumers at an early age, some contend that rampant marketing efforts directed at children stymies the development of personal virtue and the appreciation of noncommercial social goods.

Others have argued, however, that such social critics overestimate the influence that advertising has on individuals as well as the extent to which the values inherent in such practices are necessarily enemies of human flourishing. They believe that blanket assertions about the manipulative nature of such advertising are overstated and claim that advertising plays an important role in allowing children to become reflective decision makers by providing them with information about available products. In doing so, such defenders argue that advertising can actually aid children in formulating a sense of their own wants and preferences, as well as introduce them to the workings of a free market economy.

Debates over such broader social issues will no doubt continue into the foreseeable future. In attempting to sort them out, though, further research is called for in at least three directions. First, further empirical investigation into the effects of advertising on the psychological and social development of children is needed for a proper evaluation of claims concerning the scope and strength of its influence. Second, from the normative point of view, parties on all sides of the debate need to further explicate and defend the views of human values and social goods that underlie their positions. A complete treatment of the ethics of marketing to children will necessarily depend on a robust account of the nature of personal and social value. Finally, even with regard to unethical marketing practices, care must be taken to distinguish between those cases that pose a serious enough threat to children as to warrant government regulation from those practices that while perhaps ethically dubious are not sufficiently problematic as to call for regulatory restrictions.

—*Daniel E. Palmer*

See also Advertising, Subliminal; Advertising Ethics; Child Safety Legislation; Commodification; Consumerism; Consumer Product Safety Commission; Consumer Protection Legislation; Deceptive Advertising; Federal Trade Commission (FTC); Marketing, Ethics of; Paternalism; Product Liability; Truth Telling

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Child Safety Legislation

A child is a person who has not reached the age of majority or the age at which a person attains full legal rights. In the United States, this is also the age of capacity defined by statute as 18 years for legally being able to agree to a contract, 16 years for agreeing to marriage, and 14 years for knowing right from wrong. Safety implies freedom from danger, damage, injury, or harm. Safety is security. Legislation refers to an enacted body of laws. Legislation may create agencies and competent authorities that administer regulations pertaining to the law. Regulations are rules that have the force of law. Child safety legislation includes any law or regulation created to protect a child from danger or harm.

Child safety legislation encompasses the categories of health, medicine, and physical safety; family and education; employment; and exploitation. According to human rights advocates, children's status as human beings automatically entitles them to all human rights, including safety. The business legislation on child safety is generally a part of regulations established for the protection of larger classes of people such as workers, consumers, and citizens.

In the United States, child safety regulation is often initiated by public interest groups. Public interest groups lobby in favor of safety regulations in the administrative processes of government agencies such as the Food and Drug Administration (FDA) and the Consumer Products Safety Commission (CPSC). This type of activity resulted in the establishment of product safety standards in child restraint systems, bans on children's jewelry containing lead, and multiple voluntary recalls of products.

Because of their physical and mental immaturity, children are seen as members of a dependent group that needs special safeguards and care, including appropriate legal protection before as well as after birth. However, since the beginning of the 20th century, society's principal concern has been with the physical protection and security instead of the recognition or guarantee of rights. Rather than using a basis of equality, rights here are based on the concept that children are significantly different from adults. They are vulnerable, at risk, and require nurturing and special protection from the adult world. This calls for extra measures from society in law and in practice.

U.S. Legislation

The earliest legal provisions for children in the United States dealt with labor and health issues in the food supply. The following sections address child labor and prominent legislation for food, drugs, and consumer products.

Child Labor

Indenture was an early means of caring for orphans in the United States, dating back to the 1600s in Massachusetts. However, indenture was more often a source of free labor than child protection. In 1866, Ohio established the first law providing public funds for a county orphan's home. In 1935, Congress passed the Child Welfare Provisions of the Social Security Act. In 1938, a key piece of business legislation was passed in the United States. The Fair Labor Standards Act (FLSA) forbids the use of oppressive child labor by restricting employment to nonhazardous jobs, by limiting working hours for those under the age of 18 years, and by forbidding employment for those under the age of 14 years except as newspaper deliverers or child actors. The FLSA establishes minimum wage requirements that apply to children.

Although adults have the capacity to bargain with employers, children generally are not in a position to discuss or negotiate terms of employment. Child work such as delivering newspapers or household chores is differentiated from child labor or waged labor in which a child is exploited by third parties for profit. Exploitation occurs when a child starts work at too early an age, works too long, works in jobs with dangerous or excessive physical demands, works for inadequate remuneration, or is delegated too much responsibility.

Food and Drugs

Regulation of food in the United States dates back to food statutes concerned with bread and meat in early colonial times. Federal controls over the drug supply began in 1848 with a national law requiring inspections and banning the importation of adulterated drugs.

Public outcry over deaths from a poisonous sulfa drug (elixir sulfanilamide) put on the market for children was a major impetus for the passage of the 1938 Food, Drug, and Cosmetic Act. The act is administered by the FDA. The law prohibits false therapeutic advertising. It requires labeling and directions for safe use and premarket approval for new drugs. FDA approval requires that manufacturers prove that the new drug is safe and effective before it can be sold. Amendments to the law in 1962 protected unborn infants in the United States from the risk of deformities produced by the drug thalidomide.

Children are not expected to have the same capacity for judgment as adults. Therefore, they are especially susceptible to the lure of harmful and dangerous products such as alcohol, tobacco, chemicals, and drugs. Legislation bans dispensing these products to children. The FDA also finds that children's developmental processes are easily disrupted, making pesticide content in fruits, vegetables, and juices a concern.

Consumer Products

In 1972, Congress created the CPSC, which took over several programs pioneered by the FDA. The CPSC enforces the Flammable Fabrics Act (1953), the Refrigerator Safety Act (1956), the Child Protection Act (1966) banning hazardous toys and articles for which adequate warning labels cannot be written, the Child Protection and Toy Safety Act of 1969, child safety measures in the Poison Prevention Packaging Act of 1970, and the Toy Safety Act of 1984.

Children are easily influenced by marketing and advertising ploys. For example, medical research has found that the brains of adolescents function in different ways than adult brains in that they underestimate risks, overvalue short-term benefits, and act more impulsively than adults. The American Academy of Pediatrics (AAP) considers advertising to children under the age of 8 years inherently deceptive and exploitative. In addition, developmental processes occurring in children, but not adults, require protection. The AAP already recommends that children between the ages of 0 to 2 years not watch television because early television watching is associated with attention problems at the age of 7 years.

International Legislation

In 1889, the British Parliament passed the "Children's Charter" for the prevention of cruelty to children. However, it was not until after World War II that the matter of the human rights of children, an idea that originated in the West, was recognized as an international issue. The United Nations Convention on the Rights of the Child acknowledges that every child, generally defined as any person under the age of 18 years, has certain basic rights including the right to life, the right to his or her own name and identity, and the right to be reared by parents in a family or cultural group.

The United Nations General Assembly adopted the Convention into international law in 1989. It was the world's first international legal instrument on children's rights. The Convention forbids capital punishment for children. The Convention has been ratified by 191 countries. The laws of several states, authorizing execution as a punishment for crimes committed by minors, have been a barrier to ratification by the United States. However, the 2005 Supreme

Court decision in the case of *Roper v. Simmons* prohibited the execution of defendants who committed a crime when they were minors. The effect of the Supreme Court decision on ratification of the Convention by the United States is uncertain.

The Convention also has two optional protocols adopted by the General Assembly in 2000 that apply to the states that have signed and ratified them. These are the optional protocol on involvement of children in armed conflict and the optional protocol on the sale of children, child prostitution, and child pornography. The Convention does not address child labor, which remains an international issue.

A study by the International Labour Organization in 1997 estimates that 250 million children worldwide are committed to full-time labor. The Social Accountability International organization places the estimate at more than 100 million. Child labor is concentrated in Asia, Africa, and South America. Rising public concern about child labor, sweatshops, and inhumane working conditions in general led to the creation of the Council on Economic Priorities Accreditation Agency in 1997. In 2000, the council established itself as a new entity, Social Accountability International (SAI). The role of SAI is to develop voluntary standards for social responsibility that would forestall the need for more legislation.

Membership in SAI allows retailers to demonstrate their commitments to standards for labor issues by agreeing to do business only with socially responsible suppliers. Certification by SAI requires manufacturers and suppliers to demonstrate compliance with standards governing labor and workplace conditions. SA 8000 is a code of practice that includes nine key areas, the first of which is child labor. Companies that apply for SA 8000 certification must ensure that none of their staffs or those working for suppliers uses or promotes child labor. The remaining eight key areas include forced (prison or slave) labor, health and safety, discrimination, disciplinary practices, working hours, compensation, management practices, and freedom to associate and bargain collectively.

—Eleanor G. Henry and Pamela Gershuny

See also Child Labor; Children, Marketing to; Consumer Product Safety Commission; Consumer Protection Legislation; Consumer Rights; Food and Drug Safety Legislation; Human Rights; Recalls, Voluntary; Work and Family

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Christian Ethics

Although there are diverse ways to understand Christian ethics, generally it is considered a body of systematic knowledge to guide good human behavior based on the teachings of Jesus of Nazareth (Christ) and the apostles contained in the Bible (Old and New Testaments), and for many, it also includes the living Christian tradition and some developments of Jesus's followers.

Christian ethics is a widespread ethical tradition, starting 2,000 years ago. Although there are different degrees of adherence to and interpretations of these ethics, the great number of Christians—about 2,100 million worldwide—gives an idea of the importance of the Christian ethics tradition. Moreover, Christian ethics has had a practical influence on philosophers and even on ordinary people in many historical periods, opening new horizons to them.

Christian Ethics and Moral Philosophy

The relationship between faith and reason, including ethics, is problematic. One of the problems is related with the *Euthyphro dilemma* presented by Plato

(*The Last Days of Socrates*). Socrates essentially asks whether something is good because God commands it or whether God commands something because it is good. Many Christians defend that a natural order understood through reason cannot be contradictory to God's will as expressed in the Revelation, since God is both the Creator and who explicitly reveals. This position is far from being an understanding of morality as an arbitrary will of God, but it is also far from being a vision in which morality is independent of God's will.

In contrast, a theologian called Ockham (14th century), who has had a great influence, presented morality as only based on an arbitrary will of God expressed in divine commandments. He not only abandoned reason to discover morality but also reduced Christian ethics to a set of obligations, with practically no room for virtue.

Now, some Christians, putting philosophy aside, only recognize biblical teaching freely interpreted by each individual or maybe with the support of churches or communities of believers. However, many other Christians consider that it is reasonable to think that Christian ethics includes both faith and reason.

Augustine of Hippo in the 5th century and Thomas Aquinas in the 13th century are two outstanding examples in joining faith and reason. Augustine employed neo-Platonic and Stoic thought to a great extent, while Aquinas extensively used Aristotle, although both authors did so in a new and creative way.

Currently, there is a well-developed body of moral theology, which accepts and examines divine Revelation and simultaneously responds to the demands of human reason. Moral theology includes philosophy for a sound vision of human nature and society, as well as of the general principles of ethical decision making and other proposals of moral philosophy.

Scrutinizing the Bible and the primitive Christian tradition, one can find that, apart from obligations (moral law, expressed in principles and rules), there are also values and virtues.

Principles are hierarchical issues, such as the priority of people over things, the subordination of economic goals to human dignity and rights, and the priority of seeking God's approval rather than man's. *Rules*, closely related to principles, are moral dictums for human action, for instance, respect for human life and other people's property and the prohibition of lying. *Values* are goals for life or moral goods, such as freedom, love, peace, and truthfulness. *Virtues* are permanent moral habits in the character and dispositions of the individual Christian by the Holy Spirit.

Moral Law: Three Levels of Knowledge

Many Christians understand that moral law has three levels of knowledge. First, the "Natural Law," which comes from God, the Creator, who established a moral order knowable through reason. Natural (moral) law is present in the heart of each human, at least in its more basic prescriptions. Natural law includes respect for the dignity of the person and determines the basis for fundamental human rights and duties.

Jesus presented himself as someone who had come not to abolish the law and prophets but to fulfill them. Thus, the second level of moral law is the moral precepts of the Old Testament, the "Old Law" or "Law of Moses." It is summed up in the "Ten Commandments," or "Decalogue," which forms a coherent whole. It expresses many truths also accessible to reason and, consequently, belonging to the natural law.

The Decalogue contains the obligations to worship God; not to make wrongful use of the name of the Lord; to observe the Sabbath day and keep it holy; to honor one's father and mother; to respect human life, other people's material goods, and the reputation of individuals; to avoid inappropriate sexual intercourse; and not to covet the neighbor's wife or desire anything that belongs to one's neighbor.

The third level is the "New Law," or the "Law of the Gospel," which includes the commandments and the other moral precepts of the Old Testament but goes beyond them. It requires following Christ and imitating him along the path of love and by the working of the Holy Spirit in the soul. It requires not only living in accordance with a set of norms but also reforming the heart, the root of human acts, trying to imitate Jesus. In the "Sermon on the Mount" (Chapter 5 of Matthew's Gospel), which is considered as the Magna Carta of Jesus's morals, are declared blessed those who are poor in spirit (detachment, humility), those who mourn, the meek, those who hunger and thirst for righteousness, the merciful, the pure of heart, the peacemakers, and those who are persecuted for righteousness' sake. These "Beatitudes" have been extensively explained and commented on throughout the centuries by Christian writers.

Christian Ethics in Business

The Bible encourages working and making honest profits but warns against greed, avarice, and envy. Riches should be seen as instrumental, not a supreme good. In practice, serving God rather than riches means putting people first when managing business and considering profits as a necessity and a measure of the results but not as the only end for the business. Profits are not acceptable if they have been gained without respecting people's rights and their well-being.

Christian tradition, for a long time, has been suspicious about capitalist economics and has emphasized wealth distribution rather than its creation. It was considered difficult to harmonize the continuous accumulation of wealth, extolled by capitalism, with the Bible and early Christian writers. The latter were influenced by the economic and cultural context at the beginnings of Christianity. At that time, the economic mechanisms and social benefits of wealth creation were not understood as they now are.

Max Weber held that some Puritan preachers of the 17th century, interpreting Calvinist doctrine regarding predestination, thought that wealth accumulation would be a sign of predestination to eternal salvation. Consequently, they encouraged the development of what has been called the Protestant work ethic, which includes virtues such as being hardworking, frugal, and industrious. According to Weber, these conceptions and habits were indispensable to the emergence of the new capitalist ethos. Now, many Christians and churches see wealth creation and business as a noble task and encourage human virtues, which make work prosperous because business and wealth creation contribute to the common good.

Regarding business ethics, a set of obligations for business can be derived from the Decalogue. Among others, dealing with people in a fair way; providing humane conditions in work; providing safe products; not committing fraud; being truthful in financial reports, product information, and in any corporate communication; not bearing false witness; avoiding calumny, rash judgment, and detraction; and so on. A labor weekly rest and a reasonable working day, which does not prevent duties toward God and family, can also be related with the Ten Commandments.

The Bible is also explicit regarding integrity in honoring promises, observing legitimate contracts, and repairing injustices, and people in power are strongly required to refrain from abuse of those in need. It condemns bribery and extortion, cheating, paying unjust wages, and forcing up prices by taking advantage of the ignorance or hardship of others.

In the Bible, there are two generic moral principles of conduct significant for business: the golden rule and the commandment to love one another. In the New Testament, Jesus is the model for this love.

The commandment of love entails much more than duties of justice. In dealing with others (coworkers, customers, etc.), Christian ethics requires not only being fair but also taking care of others by considering their needs. In this sense, St. Paul directed a Christian master to treat his Christian slave as a brother.

Furthermore, Christian ethics stand for respect and mercy for all human beings, even for those who are not known. Jesus's parable of the Good Samaritan, who took care of an enemy, is quite eloquent in this respect. All humans have been created in the image and likeness of God, and Christ is the Universal Redeemer; all of them are members of a whole family and all deserve an attitude of compassion and solidarity. However, in the Christian tradition it is also stressed that there is a hierarchy of duties in caring for others.

Christian Work Ethics

Christian ethics stresses the rational finding that work is a deliberate and free activity that comes from the person. It not only produces things but also changes the worker. This confers dignity to work. Work needs not only remuneration but also recognition as a personal contribution to society. By working, a person develops his or her capacities, interacts with other people, and finds the opportunity to serve others. The Christian faith gives new horizons to work. The divine commandment to subdue the earth in the beginning of Creation is carried out through work. Jesus himself worked as a craftsman giving labor a great dignity. Christians can work feeling themselves children of God and called to imitate and identify themselves with Jesus Christ. They cooperate in this purpose by working with professional competence, uprightly, and by offering their activity to God.

Work can also be considered in terms of vocation. In the New Testament terminology, *vocation* (κληστζ or *klésis* in Greek) means the calling from God in Jesus Christ addressed to an individual to become a Christian. This calling discloses to each one the deep meaning of his or her life and the mission associated with this calling. Thus, vocation is a sense of dialogue and response between God and each person. It is not a divine calling for a certain elite, as some understood. But neither is it equivalent to "profession," in the sense of professional work, leading to the current secular meaning, which completely sets aside God as the origin of the calling, as some others have interpreted. Christian vocation or calling refers to the whole life of each individual, including work, which certainly is an important part of human life.

Without ignoring the religious roots of this concept, Michael Novak considers that a calling can be entirely secular and has talked about business as a calling. In this way, he overcomes the current view of business, which reduces it to making money.

That labor rights are included in the context of human rights is an outstanding point of Christian ethics. Among other rights we should remember are a fair process of hiring and dismissal, working in healthy and safe conditions, receiving a fair wage, the right of worker association (unions), an appropriate participation in managing business, and harmonizing work and family duties as much as possible.

Social Issues in Christian Ethics

Since the end of the 19th century, Christian churches have presented teachings regarding social issues, starting with Pope Leo XIII and the document *Rerum novarum* (on the new things) on the social question, which dates from the Industrial Revolution. Successive contributions have become an updated doctrinal "corpus" called Catholic Social Teachings on social, economic, and business matters. The Church of England, The Orthodox Church, the Lutherans, the Methodists, and other Christian churches and the Evangelical movement have also developed streams of thought, documents, and actions based on Christian ethics and related to social, economic, and business issues. Generally, they all agree in recognizing the positive contribution of the market economy, but under certain ethical conditions—among others, considering humankind as a whole human family with links of solidarity; wealth creation with social justice; market strength regulated by the interests of the community; safeguard of the natural environment; the social inclusion of all people and groups in prosperity, social structures, and policies to foster the initiative of individual and local communities; and solidarity to eradicate poverty, to contribute to human development, and as a framework for globalization.

—Domènec Melé

See also Capitalism; Charity, Duty of; Divine Command Theory; Golden Rule, The; Jewish Ethics; Natural Law Ethical Theory; Weber, Max

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Churning

Churning is excessive trading in a client's account by a broker, who has control over the account, with the intent to generate fees or commissions rather than benefit the client. Brokers—who are typically employees of a brokerage or investment banking firm with responsibility for handling the investment portfolios of clients—often occupy a dual role as sellers of securities and trusted advisers. In the former role, brokers have only the obligations of sellers in a market, but in the latter capacity, they have both moral and legal obligations, a fiduciary duty, to act in the interests of a client. Because brokers are compensated by fees and commissions from the sale of securities, they have a conflict of interest when they also serve as an adviser or have control of an account due to the opportunity to enrich themselves at a client's expense. To engage in churning, then, is to violate a fiduciary duty to act in a client's interest as the result of a conflict of interest.

Churning can be legally prosecuted either under the common law doctrines of fiduciary duty and fraud or under various federal and state securities laws. A fiduciary duty may be created by an explicit pledge by a broker to serve as a trusted adviser. Absent such a pledge, a fiduciary duty may be inferred by the "shingle theory," which holds that by offering a professional service ("hanging out a shingle") a broker implies the he or she will deal with clients fairly and honestly. The common law elements of fraud are the willful misrepresentation of a material fact that causes harm to a person who reasonably relies on the misrepresentation. Thus, a broker who willfully misrepresents either his or her trustworthiness as an adviser or the reasons for recommending or executing a trade commits fraud.

Most actions for churning are brought under Rule 10b-5 of the 1934 Securities Exchange Act, which prohibits any manipulative, deceptive, or other fraudulent device or contrivance in connection with the purchase or sale of a security. In addition, the National Association of Securities Dealers (NASD), an industry organization, holds that churning is a violation of its suitability rule, which requires members to recommend only transactions that are suitable for a client. Although an action can be brought by the Securities and Exchange Commission (SEC), state regulators, or the NASD with the aim of imposing penalties, most cases of churning are private suits or arbitration claims brought by individuals seeking restitution.

Individuals who charge a broker with churning are required by the courts to prove three elements: (1) that the broker had control over the account, (2) that the broker engaged in excessive trading given the investment objectives of the client, and (3) that the broker acted with an intent to defraud or acted with a reckless disregard of the client's interests. Although each of these elements raises certain difficulties, the first two are especially problematic.

A broker who is authorized in writing by a client to make transactions without further approval has explicit or formal control. Ordinarily, a broker who is merely executing a trade for a client has no fiduciary duty to serve the client's interest. However, implicit or informal control and an attendant fiduciary duty may be established when an unsophisticated client always or usually follows a broker's advice. Both elements are necessary—a pattern of reliance and a lack of knowledge or experience. The reason for imputing control in the case of an unsophisticated, easily influenced client is that a broker may have the de facto power to control this person's account without being explicitly authorized.

When are a broker's trades for an account excessive? This question is problematic because any trading strategy depends on a client's investment objectives and tolerance for risk, and it may be difficult to distinguish between excessive trading and an aggressive but unsuccessful strategy. Courts have accepted two indicators of excessive trading—turnover ratios and cost-to-equity ratios.

The turnover ratio—which is a measure of the number of times the portfolio is turned over during a certain period of time, usually 1 year—is commonly calculated by dividing the total value of the trades during a year (or some other period) divided by the average value of the portfolio during that time (adjusted, if necessary, to produce an annualized number). Thus, the turnover ratio of a $1 million portfolio for which a broker makes $2 million in trades during a 12-month period is 2. The cost-to-equity ratio is calculated by dividing the total fees and commissions over a period of time by the average value of the portfolio, adjusted, if necessary, to produce an annualized number. Thus, a $1 million portfolio that generates $100,000 in annual revenue for the broker and the firm has a cost-to-equity ratio of 0.1 or 10%.

With both indicators, the courts must establish what number indicates excessive trading. The general rule of thumb for turnover is the 2–4–6 rule, according to which a ratio of 2 indicates possible churning, a ratio of 4 creates a presumptive case of churning, and a ratio of 6 is conclusive evidence of churning. A cost-to-equity ratio of 3% or 4% should raise concern. Such mechanical rules take no account of the soundness of the trading strategy being employed or the gain or loss to the client. Thus, trading that produces a sixfold turnover or has a cost-to-equity ratio of 8% might be the result of a sound strategy that produces little loss, whereas a broker, for no sound reason, might turn over a portfolio only once or trade enough to collect only 2% in fees and commissions.

A third method for determining excessive trading involves the use of modern portfolio theory and sophisticated statistical techniques to compare the expected return of any given broker-managed portfolio with a large number of mutual funds with similar objectives. The assumption of this method is that the turnover ratios and the cost-to-equity ratios of mutual funds, whose managers are compensated solely on the basis of performance, provide benchmarks against which to judge the trading strategies of brokers. Although brokers may have a higher turnover and higher expenses than comparable mutual funds, they should also have a higher expected return, and whether this is the case can be determined using modern portfolio theory and readily available data about comparable mutual funds.

The final issue in churning is the damages that should be awarded to a victim. Justice requires that the victim of a wrongful act be compensated in a manner that corrects the wrong. Courts have applied three standards for awarding damages: (1) the out-of-pocket loss to the client, (2) the gain to the broker from the excess trading, and (3) the difference between the loss to the client and the return that would have been achieved by a properly managed portfolio. The amounts produced by using the first two standards are relatively easy to determine; the third standard typically involves a comparison with mutual fund benchmarks.

—John R. Boatright

See also Compensatory Damages; Conflict of Interest; Fiduciary Duty; Finance, Ethics of; Fraud; National Association of Securities Dealers (NASD); Securities and Exchange Commission (SEC)

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Civil Rights

An adequate understanding of civil rights requires that they be set within the broader conceptual framework provided by rights theory. Civil rights are related both to natural rights and positive rights, which are typically characterized as distinct and incompatible accounts of rights. According to natural law theory, natural rights are those rights that are part of the natural, given, moral structure of the universe, not unlike those other natural laws that govern the physical universe (i.e., the law of gravity, the law of constant motion, etc.). As natural rights, civil rights are those that are justified by appeal to the moral structure of the universe rather than to any given political system. What makes civil rights important, on this view, is their relation to this higher moral order. A society is well-ordered when its members enjoy all the rights that inhere in this natural, moral order. Natural rights are also often referred to today as human rights—those rights that all humans are entitled to by virtue of our common human nature. In this sense, civil rights and human rights overlap considerably.

On the other hand, according to positive law theory, rights are granted by a given political system or regime and are justified only by reference to the values and principles espoused by that regime. In this sense, the sort of civil rights one has will depend on one's government. For example, civil rights, understood in this way, may include the right to park in your driveway or the right to vote for judicial officers in your district. However, living in a district that does not appoint justices by popular vote means that no such right exists in that district for those citizens. In this theoretical framework, civil rights may refer to rights as diverse as the natural human right against torture or to the positive right to drive a car in California.

A further important theoretical distinction, which relates to the discussion of civil rights, is the distinction between negative rights and positive rights. Here, the sense of positive rights is slightly different from that found in positive law theory. Here, positive and negative are defined in opposition to one another. A negative right is typically the sort of right that imposes duties of noninterference or nondiscrimination on others. An example of a negative right may be the right to vote, where the right prohibits interference with the exercise or enjoyment of the right. If someone bars a voter from the polling station, or uses their public power to remove an eligible voter from the polling lists, then this amounts to interference with the right to vote and would be considered a violation of that right.

A positive right, on the other hand, is the sort of right that imposes duties of provision on others. Such a duty may be placed on individuals in a position to provide what the right requires or it may be addressed collectively by vesting the duty to provide in government. For example, a child may have a right to be fed, which imposes a duty to provide suitable food for the child. Typically, this duty falls on the child's parent, but it may fall on the society as a whole or on some appropriate social or governmental institution when the parent is unable or unwilling to comply. Another example of a positive right is the right to a minimum level of education; where this exists, it typically imposes a duty on the society as a whole, through the government, to provide either the education directly (as in a system of publicly funded schools) or at least the means to acquire such education (as in a system of grants or loan guarantees to attend various private schools). Civil rights may be of both sorts—negative and positive.

Regulating Relationships

Civil rights play a central role in regulating the relationship among individuals, government, and various social institutions. The concept of civil rights has two distinct, yet interrelated, meanings: (i) rights of citizens to liberty, property, and well-being as members of a particular civil society; (ii) rights as specific legal protections against discrimination, typically on the basis of race or sex, which are legislative or judicial in origin and serve to correct past inequities both in the distribution of educational and employment opportunities and in access to various social or public goods.

For both senses of civil rights, the principal challenge rests in identifying the nature of the right at issue and in finding the proper remedy for its violation. For example, the U.S. Declaration of Independence of 1776 clearly identified the rights at issue—every citizen enjoys the right of political representation. The failure of the British government to respect this right, by levying taxes and denying voting rights to the American colonists, is remediable by wresting governmental authority from Britain and establishing an independent government.

Another example of how this challenge has been met is found in the Civil Rights Act of 1964, which clarified the rights to nondiscrimination and equal protection first articulated in the Thirteenth, Fourteenth, and Fifteenth Amendments to the U.S. Constitution. The Civil Rights Act of 1964 restated and affirmed that the worst impediment to racial equality is continued failure to act affirmatively against pervasive patterns of racial discrimination. The remedy, for the violation of the constitutional rights, is identified in the act as affirmative action that ensures equal opportunity and access to important social goods such as employment and education.

Civil Rights as Civil Liberties

In its broadest meaning, civil rights refers to those moral guarantees accorded to members of a civil society to ensure equality, liberty, and fairness. These values are, according to many political theorists, best achieved through constraints placed on governmental or state power.

Political theorists of the 17th and 18th centuries, most notably John Locke, proposed that the basis for governmental legitimacy is the consent of the people. The only rational basis for the people to consent to government, he argued, is to protect their natural interests in life, liberty, and property. Individuals' rational interest in securing their life, liberty, and property would serve as the legitimating basis for governmental authority and would justify civil rights—the rights that all individuals possess as members of a civil society. Civil society, then, is best when it retains all the positive attributes of the natural human condition, without any of its dangers, namely conflict and strife.

Civil rights, however, were never limited merely to the regulation of state power. Rather, they have always had a prominent place in the regulation of power between individuals. On this view, a legitimate government is one that can protect each individual in the enjoyment of her or his liberties, natural ability, and property from all those other individuals with whom she or he lives in society. This requirement for state action, however, empowers the government to act against individuals who would violate the civil rights of others. The challenge for government is to do so without itself becoming a threat to those very same rights to life, liberty, and property.

Civil rights, in this broad sense, may include rights of individuals to their property and other broadly economic rights, such as the right to contract, to apply for work, and to minimal subsistence, as through social security; rights to security of the person, to security and protection from violence and harms of various preventable sorts, which may include, in some contexts, the right to medical or health services; rights of political participation and representation, including voting for and holding public office; rights to secure various important liberties, such as liberty of conscience, religion, speech, assembly, petition, and privacy; and rights that ensure that these liberties are not arbitrarily alienated or abrogated.

While we may be most familiar with the civil rights encoded in the U.S. Bill of Rights, this should not be taken to mean that civil rights are not important in other historical, political, and legal contexts. In the language of human rights, civil (and political) rights are understood as first-generation human rights—those that flourished under the European Enlightenment and those that came to define the core of liberal democratic government, as ensuring against the abuse of the coercive powers of the state.

Indeed, by presenting such rights as the basis for legitimate government, civil rights serve as the standard by which governmental action may be understood as abusive, arbitrary, or oppressive. The degree to which a government ensures the civil rights of its subjects is the degree to which that government wields its authority, especially its coercive powers, legitimately. The degree to which it fails to do so is the degree to which its authority is illegitimate and, so, properly resisted. As such, many emerging democracies and developing nations are seeing substantial improvements in the recognition and protection of the civil rights of their own citizens and, thus, the civil rights of peoples around the globe.

This broadly moral sense of civil rights is found most clearly expressed in historic documents such as the U.S. Declaration of Independence, the French 1789 Declaration of the Rights of Man and Citizen, and the 1948 Universal Declaration of Human Rights.

Civil Rights as Legal Nondiscrimination and Equality Rights

In its more specific and narrow sense, civil rights refers to the various legal guarantees to equality before the law; due process; and nondiscrimination on the basis of race, sex, ability, age, national origin, religion, and, increasingly, sexual orientation. This sense of civil rights finds its legal roots in a variety of U.S. Civil War–era constitutional amendments and in several key post–World War II judicial and legislative actions.

While civil rights law varies from country to country, from historical period to historical period, and from domestic to international law, the development of civil rights norms and practices owes much to their manifestation in U.S. constitutional law. Examples of the influence of U.S. civil rights law in international law are found in the inclusion of strict due process and nondiscrimination rights in the Universal Declaration of Human Rights, the Convention on the Elimination of All Forms of Discrimination Against Women, and significant portions of the European Declaration of Human Rights. Hence, the remainder of this entry will take, as its primary focus, the development of civil rights law and policy in the U.S. context, with the understanding that this is not exhaustive of the variety and meaning civil rights may have in other national, international, and historical contexts.

History

The period from 1865 to 1875 saw the adoption of several substantive legal correctives to the United States' history of race-based slavery. Two Civil Rights Acts, the first in 1866, followed by the second in 1875, bracket three constitutional amendments whose legal legacy has shaped modern civil rights law. The Thirteenth Amendment of 1865 made slavery and involuntary servitude illegal, except as punishment. Later, this amendment would be interpreted to prohibit the legal continuation of any badges of slavery or markers of past slave status, such as the segregation of public facilities, the denial of economic opportunities or public services, or the enforced segregation of schools in the 1954 *Brown v. Board of Education*. The Fourteenth Amendment of 1868 undid the legal effects of the Dred Scott case, *Scott v. Sandford*, by affirming citizenship for everyone born or naturalized in the United States. It also forbade state governments from depriving any U.S. citizen of life, liberty, or property without the due process of law and guaranteed the equal protection of law to all citizens. These two guarantees—to due process and to equal protection—would find their greatest legal effect 90 years later under the Warren Court's emphasis on civil rights and liberties. The Fifteenth Amendment of 1870 affirmed the right to vote for all citizens and denied state governments the power to deprive this right on the basis of race, color, or previous condition of servitude.

Taken together, these three amendments to the Constitution served as a formal legal corrective to the legacy of slavery in the United States, especially to its legacy of racial discrimination in all aspects of social, economic, political, and personal life—in short, in all regards in which an individual may participate in civil society. These amendments are viewed by some legal scholars as having finally completed the U.S. Constitution's promise of the Enlightenment liberal ideal of equality, freedom, and individual autonomy. These amendments, it is argued, formally extended this ideal to African Americans. These Enlightenment ideals would be further extended to women in 1920, with the adoption of the Nineteenth Amendment's guarantee of women's voting rights, and to the poor in 1964, with the adoption of the Twenty-Fourth Amendment's prohibition on poll taxes and on denials of voting rights for failure to pay taxes. With the adoption of the Americans with Disabilities Act in 1990, these rights would finally be extended to prohibit discrimination against citizens with disabilities to access employment and educational opportunities, criminal justice, and health and human services.

This combination of amendments significantly shaped modern U.S. civil rights law and contemporary understandings of the rights of citizenship. Most significant is the linkage of the legal concepts of due process and equal protection to the elimination of racial discrimination. However, it is important to note that these amendments were no guarantee that equality between the races materialized or that the effects of discrimination were remedied in practice. Indeed, throughout the 19th century and early 20th century, the U.S. Supreme Court impeded various attempts by Congress to enact civil rights legislation (see, e.g., the 1883 *Civil Rights Cases*). These amendments also failed to discourage the Supreme Court from affirming the separate but equal doctrine that legalized and legitimized the policies and practices of Jim Crow segregation (see *Plessy v. Ferguson*). Nor did these amendments discourage the courts from affirming the federal government's policy of interning resident Japanese and Japanese Americans during World War II.

Contemporary U.S. Civil Rights Norms

Not until the mid-20th century, notably with the U.S. Supreme Court's reversal of its prior affirmation of the separate but equal doctrine in *Brown v. Board of Education*, did the era of civil rights—understood primarily through the lens of due process and equal protection—find its legal footing. The period from the 1950s onward would witness an era of legal advances in all aspects of civil rights, mainly through concerted efforts on the part of the courts and Congress. Congress passed Civil Rights Acts in 1964, 1966, 1968, and 1991, which elaborated and clarified important liberties such as equality of opportunity in education and employment, individual privacy, religious freedom, and general nondiscrimination. Guarantees were made, without regard to race, sex, poverty, or religious faith, to due process in the courts and to equal opportunity to access a wide variety of social goods, especially education and employment.

By specifying the necessity for remedial action against pervasive racial discrimination, the Civil Rights Act of 1964 brought into legal parlance the concept of "affirmative action." This act mandated that effective elimination of practices of race and sex discrimination required affirmative action. Affirmative action has at least two competing and, some have argued, incompatible meanings: (1) that positive steps be taken to ensure that decisions awarding employment or educational opportunities, or permitting the enjoyment of various social goods, shall be made without preference at all for any race or sex categories; (2) that positive steps shall be taken to ensure that, all things being equal, preference in decisions awarding employment or educational opportunities, or permitting the enjoyment of various social goods, shall be given to those persons who are members of a minority race or women.

The difference between these two meanings and their effect on contemporary civil rights law is considerable. The first sense of affirmative action is most often referred to as ensuring a formal equality between the races. Formal equality prohibits the use of explicitly or intentionally racist (or sexist) policies, procedures, and criteria in the allocation of social goods such as education and employment opportunities, access to criminal justice, housing, health care, and access to public facilities. In the case of formal equality, the legal emphasis is on prohibiting intentional, individual discriminatory practices and procedures. Formal equality ensures that the policies, procedures, and criteria used to allocate social goods must not themselves employ race-based criteria. For example, a hiring policy that specifies that employees must be white constitutes a violation of formal equality. Similarly, a policy of awarding higher scores to racial minorities on college entry applications violates formal equality requirements. However, where discrimination is unintentional, systemic, or institutionalized, reliance on formal equality may allow such discrimination to go unaddressed and uncorrected, since it fails to recognize this as discriminatory in the legally relevant sense.

The second sense of affirmative action shifts the legal focus from formal equality to substantive equality. Attention is drawn to the effects of policies, procedures, and criteria on the equal status of individuals. Substantive equality is concerned with the exclusionary and discriminatory effect of otherwise racially or sexually neutral procedures, policies, and criteria. Substantive equality draws attention to the effects of formally neutral policies and procedures as they function in a social context that carries the historical residue of race and sex inequality. Where the starting point for the existing distribution of important social goods is not itself equal between men and women or between the races, application of formally neutral policies and procedures risks exacerbating those inequalities. For example, a hiring requirement that police officers must be at least 6 feet tall would effectively exclude the majority of women from becoming police officers. Such policy, while not restricting applicants to males only, in its effect works in the same manner to ensure that police officers are largely, if not exclusively, men. Similarly, college recruitment policies, which are formally neutral between races but which rely heavily on alumni and provide only few and meager need-based scholarships, may effectively deny access to educational opportunities for students who are members of a minority race.

It is important to add that the distinction between formal and substantive equality is not limited to affirmative action. Rather, this distinction arises with regard to all areas of civil rights law: in criminal justice law and procedure, in voting rights law and policy, and with regard to almost every area of civil rights law as it has been developed thus far. The challenge in identifying appropriate remedies to civil rights violations lies in distinguishing between these two seemingly incompatible objectives—formal equality or substantive equality. How should the demands of equality, fairness, and liberty be understood? This is itself a moral question and demands that we consider not only what the law requires as it is currently formulated but also what alternatives are possible. Answering this question will shape much of the future of civil rights law.

Future of Civil Rights and Social Change

In the history of civil rights law, the meaning, definition, and effect of civil rights have depended on changes in social will. Sometimes the courts and legislatures have led social opinion with society following; sometimes social opinion and the desire for change have led legislative and judicial action. The law is never sufficient on its own to guarantee much to any individual. What is always necessary is social will. Perhaps more than other rights, the recognition and enforcement of civil rights have relied on social will because they are so intimately bound to personal, professional, and public relationships among individuals. These are the relationships that give normative shape to our everyday lives, whether at work, in school, or at leisure. Social will and how it changes remains central to the civil rights project.

Some legal scholars have noted that the success of the civil rights cases in the mid-1900s, as compared with those in the late 1800s and early 1900s, rests primarily with changing social opinion about the fairness of the separate but equal doctrine. This changing social opinion reflects a change in people's willingness to carry out legislative and judicial directives in their everyday lives and in the norms they adopt to regulate their behavior toward one another. While this phenomenon is not unique to civil rights law, it is most palpably felt when people apply for work, seek promotion, or apply for university education, as well as in more mundane activities such as making hotel reservations or dining at restaurants. Not long ago in the United States, it was common for African Americans to be denied a table at restaurants, for Chinese Americans to be denied promotion at a job, and for a woman only to be paid as a supplement to her assumed husband's salary. Today, these behaviors are unthinkable. When they do appear, they are not only now violations of federal and state law but they are also viewed as morally corrupt and as socially repugnant. The law and social opinion are intimately connected in the meaning and practice of civil rights.

Consider also the increasingly common practice of employers to adopt policies of nondiscrimination on the basis of sexual orientation (currently, 80% of Fortune 500 companies are reported to have such policies). While some states require that nondiscrimination policies cover sexual orientation, there currently is no federal legal requirement for employers to do this, since federal civil rights law does not extend this far. However, extending civil rights guarantees in this direction seems to make good business sense. Many employers note that employees are more reliable, dedicated, and committed to their jobs when their equality is respected in a nondiscriminatory workplace.

With regard to sexual orientation and equality, businesses are at the forefront, ahead of most of the courts and state and federal legislatures. They may even be leading the majority of the population who may not yet be committed to extending, and thereby guaranteeing, civil rights to gays and lesbians. However, at the very least, the quest for competitive advantage in hiring may mean that ever more employers will voluntarily extend their policies and practices of nondiscrimination to include sexual orientation. Guarantees of civil liberties and enforcement of civil rights are as much a matter of social recognition and affirmation as legal recognition and affirmation. The lead, which major corporations have taken on the voluntary extension of civil rights to gays and lesbians, may make it easier for legislatures and the judiciary to affirm the extension of civil rights law to include nondiscrimination on the basis of sexual orientation.

The future of civil rights, therefore, is not merely about what meaning we give to equality, fairness, and liberty but will also require that we revisit the question "Civil rights for whom?" as we attempt to achieve the Enlightenment ideal of civil rights for everyone.

—Christina M. Bellon

See also Affirmative Action; Americans with Disabilities Act of 1990 (ADA); Due Process; Equal Opportunity; Gay Rights; Gender Inequality and Discrimination; Human Rights; Legal Rights; Racial Discrimination; Religious Discrimination; Rights, Theories of

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Clarkson Principles for Business

The Clarkson principles for business are a set of standards intended to guide the decisions and actions of corporate executives and managers. Recognizing that business leaders exercise significant discretion in their roles as corporate agents, the principles seek to create an ethical context for the exercise of managerial authority. They do so by identifying a core set of moral obligations that are incumbent on managers at all levels of the enterprise. These duties address relations with stakeholders, that is, groups and individuals who are affected, positively or negatively, by corporate decisions and operations (e.g., customers, employees, investors, and communities). In brief, the core obligations include engaging proactively in dialogue with stakeholders; disclosing risks stemming from corporate activities; distributing fairly the benefits and burdens that result from business operations; preventing, minimizing, or redressing harm to stakeholders; avoiding activities that entail unacceptable risks; and addressing openly and appropriately conflicts between managers' self-interest and the interests of stakeholders.

The principles are named after the late Max B. E. Clarkson. Clarkson, a management theorist and former corporate executive, significantly influenced the principles' content, as well as the multiyear, multinational project that gave rise to them. Named Redefining the Corporation Project, this collaborative endeavor was undertaken between 1995 and 2001 by an international group of more than 100 scholars. It sought to improve the quality and quantity of managerial and scholarly attention devoted to the nature, purpose, and governance of the corporation, emphasizing a stakeholder view of the firm. Funded by the Alfred P. Sloan Foundation and hosted by the University of Toronto, the project produced five major publications. Clarkson, Lee E. Preston, Thomas Donaldson, and Leonard J. Brooks served as the effort's leaders and developed the principles for business from participants' comments and suggestions.

The text of the Clarkson principles is contained within a statement titled *Principles of Stakeholder Management*. The statement opens with a section devoted to introductory definitions and observations. These comments acknowledge the prominent role large, professionally managed corporations play in the contemporary global economy, as well as criticisms of these organizations. They introduce the stakeholder concept, noting that all stakeholders have something at risk because of corporate activities but that the nature of this risk varies from group to group. Shareholders, it is suggested, are distinguished by the fact that risk is *inherent* to their contractual relationship with the corporation: Whether their investment yields a profit or loss ultimately depends on what remains after all other stakeholder claims have been satisfied. The introductory comments also underscore the need for managers to act transparently and fairly in their dealings with all stakeholders.

The document's second section contains the principles proper. Each of the seven proposed norms is followed by a short explanation. Principle 1 emphasizes managers' responsibility to identify stakeholder groups, actively monitor their concerns, and incorporate these interests appropriately into organizational decisions. Principle 2 directs managers to listen to stakeholders and notify them of any risks that may arise from their association with the firm. Principle 3 urges managers to address stakeholder concerns in a manner that duly considers their differing capacities to understand and evaluate information. Principle 4 calls on managers to recognize stakeholder interdependence and to distribute burdens and rewards fairly among them, given the risks to which the various groups are subject. Principle 5 requires managers to minimize the risks and harms that result from corporate operations. It counsels that partnerships with private organizations and public agencies may be needed to prevent harm or to compensate negatively affected parties. Principle 6 underscores that some corporate activities may entail risks or consequences that are patently unacceptable, for example, loss of life or the impairment of human rights. Managers are called on to modify operations, whether planned or existent, to avoid such possibilities. If this goal cannot be achieved, the operation should be abandoned. Principle 7 requires managers to recognize that they themselves constitute a distinctive stakeholder group. Since their self-interest may conflict with the duties they owe to other stakeholders, managers should welcome and encourage monitoring and oversight. Assiduously implemented, such reporting and review processes help build and sustain managerial credibility.

Complying with these norms, the principles' authors imply, enables managers to address stakeholder interests *ethically* and not merely *strategically*, that is, with an eye only toward how these interests might impede or advance the firm's attainment of its financial or competitive goals. The authors suggest that compliance also leads to trust-based relationships and to enhanced collaboration with stakeholders, two factors that ultimately redound to organizational survival and success.

Like other general standards for corporate conduct, the Clarkson principles provide business leaders with a broad aspirational model—in this case, one that helps managers identify their responsibilities to groups that stand to gain or lose as a result of a firm's activities. The principles also encourage managers to place their professional duties within a broader social context, promoting greater awareness of the diverse constituencies they serve. Considered in their entirety, the principles steer managers toward stakeholder engagements that are responsive, transparent, and respectful. In a sense, then, the Clarkson principles call on managers to deal with stakeholders in light of a quite basic ethical standard, the golden rule, and suggest a set of concrete behaviors that can help them begin to put this standard into practice.

—T. Dean Maines

See also Codes of Conduct, Ethical and Professional; Fairness; Global Codes of Conduct; Stakeholder Engagement; Stakeholder Responsibility; Stakeholder Theory; Transparency; Trust

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Coalition for Environmentally Responsible Economies (CERES)

Formed in 1989, the Coalition for Environmentally Responsible Economies (CERES) brought together

15 major U.S. environmental groups and a wide array of socially responsible investors and public pension funds. A set of goals and principles for environmental performance was developed by this alliance between business, consumer groups, environmentalists, and other stakeholders. The coalition emerged after the *Exxon Valdez* oil spill, which was not the largest in history but proved to be one of the worst in terms of adverse media coverage, disruption to local business and industry, and long-term environmental damage. However, several positive changes occurred in corporate accountability, shipboard responsibility, environmental cleanup procedures, and environmental awareness and reporting. Among the most significant of these was the development of CERES and its core principles.

The 10 CERES principles include (1) protection of the biosphere, (2) sustainable use of natural resources, (3) reduction and disposal of wastes, (4) energy conservation, (5) risk reduction, (6) safe products and services, (7) environmental restoration, (8) informing the public, (9) management commitment, and (10) audits and reports. All organizations that choose to become members of CERES must adhere to these 10 principles. By adopting the principles, member organizations acknowledge that they have a responsibility to the environment and that they must not jeopardize future generations to sustain themselves in the short run.

Today, more than 80 organizations stand behind the CERES principles. These firms include labor unions, environmental groups, public interest organizations, and investors. The coalition of investors is critical, as these firms explicitly consider environmental criteria in investment decisions. In addition, CERES partners with more than 70 corporations that have a significant commitment to the principles.

Over the years, the coalition has promoted greater corporate responsibility toward the environment and taken a leadership role in standardizing environmental reporting by organizations. CERES was founded with the belief that businesses should take a proactive stance on environmental issues, because their influence over human decisions and behaviors often surpasses that of governments, schools, or religious organizations. To control and provide accountability for environmental performance, however, companies need effective measurement and communication tools. This need brought about initiatives to establish benchmarks for environmental performance and to provide an easier way to report information about environmental performance.

In 1997, CERES launched the Global Reporting Initiative (GRI), which was designed to stimulate change for the companies by allowing them to track their progress and performance among competitors and peers who also adhere to high standards. Although both regulatory and nonregulatory factors are driving enhanced environmental reporting, there is no universally accepted method for reporting and comparison. Each year, more companies voluntarily report information about their environmental performance to the public, but firms may employ different formats, rendering comparison among reports somewhat problematic. These discrepancies in and issues with environmental reporting have generated calls for standardizing and verifying reports. CERES provides such a standard, but there are many different stakeholders in the environmental reporting process. More than 700 companies use the GRI guidelines, which means it has become the de facto international standard for corporate reporting on economic, social, and environmental performance.

—Debbie M. Thorne

See also Environmental Assessment; Self-Regulation; Social Audits

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Coase, Ronald H. (1910–)

Ronald Henry Coase is a University of Chicago economist who was awarded the 1991 Nobel Prize in Economic Sciences. The prize recognizes Coase's path-breaking work examining the institutional arrangements that govern the process of market exchange. In the citation accompanying his Nobel Prize, the Royal Swedish Academy specifically noted two journal articles that exemplified Coase's Nobel Prize–winning work.

The 1937 article "The Nature of the Firm" addressed the question of why firms exist in a market economy. Coase likened a firm to a little planned society that relies on administrative decisions to internally coordinate production, as opposed to relying on the invisible hand of the external price system. Coase argued that firms exist to mitigate transaction costs, defined as the costs of managing market transactions such as negotiating and enforcing contracts. Coase argued that in a world with positive transaction costs, there would be an efficient mix of production coordinated through a market-driven price system and production coordinated administratively within firms. By explicitly introducing transaction costs into his analysis, Coase was able to explain not only the existence of firms but also the scope of activities coordinated within firms.

The 1960 article "The Problem of Social Cost" cited by the Royal Academy began as a critique of the traditional (i.e., Pigouvian) analysis of externalities defined as the divergence between private and social costs (and benefits). Traditional analysis suggests that government action (a tax or a subsidy) is necessary to induce economic agents to internalize the costs (or benefits) their actions impose on others. Coase exposed flaws in the traditional analysis by considering a regime of zero transaction costs. Under such a regime, Coase argued, market forces will efficiently allocate legal rights (e.g., the right to pollute vs. the right to breathe clean air) and, moreover, the efficient outcome will not depend on the initial assignment of legal rights. That is, even if legal rights are initially misallocated, this misallocation will be corrected by market forces. This argument became known as the "Coase theorem." Coase himself viewed the theorem as a stepping stone to his true interest, which was the analysis of a real-world economy with positive transaction costs. Under a regime of positive transaction costs, an initial misallocation of legal rights may persist, uncorrected by market forces. Coase's analysis suggests a government role in promoting the efficient allocation of legal rights through policies that help lower transaction costs and thereby help facilitate market exchange. These government actions include things such as writing clear laws and enforcing property rights. The insights from Coase's analysis became crucial in the development of the field of law and economics.

Coase was born and raised in England. He emigrated to the United States in 1951 to accept a position at the University of Buffalo. In 1958, he moved to the University of Virginia where he remained until moving to the University of Chicago in 1964, succeeding Aaron Director as editor of the *Journal of Law and Economics.*

—James A. Overdahl

See also Chicago School of Economics; Coase Theorem; Contracts; Free Riders; Market Failure; Pollution Externalities, Socially Efficient Regulation of; Property and Property Rights; Public Goods; Transaction Costs

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Coase Theorem

The "Coase theorem" is a proposition concerning the economic theory of externalities. The proposition states that under a regime of zero transaction costs, market forces will efficiently allocate legal rights (e.g., the right to pollute vs. the right to breathe clean air) and, moreover, the efficient outcome will not depend on the initial assignment of legal rights. That is, even if legal rights are initially misallocated, this misallocation will be corrected by market forces. The proposition, although not the theorem name itself, was introduced by Ronald H. Coase in his 1959 article "The Federal Communications Commission" and elaborated on in his 1960 article "The Problem of Social Cost." The proposition acquired theorem status when the label was applied by economist George Stigler to summarize the thesis of Coase's work on externalities.

To appreciate the power of the Coase theorem, one needs to understand its motivation. Coase's point was to challenge the traditional analysis of externalities, defined as the divergence between private and social costs (and benefits). Traditional analysis suggests that government action (e.g., a tax or a subsidy) is necessary to induce economic agents to internalize the costs (or benefits) their actions impose on others. The absence of such taxes or subsidies, it was argued, would result in a suboptimal allocation of resources as economic agents would overproduce goods causing external harm and underproduce goods producing an external benefit. Coase's analysis exposed flaws in the traditional approach.

Zero Transaction Costs

Coase argued that traditional analysis is directed at solving the wrong problem with respect to externalities. Under the traditional approach, if a factory billowing fumes imposes damages on neighboring homeowners, the analysis is directed at how best to restrain the factory's fumes. Coase argued that the analysis is misdirected because any action aimed at avoiding harm to homeowners necessarily inflicts harm on the owners of the factory. The correct question, in Coase's view, is how to avoid the more serious harm.

Underlying Coase's argument is the view that, in terms of the cold logic of economic analysis, the cause of an externality cannot be attributable to any single party. In almost all cases, the externality is a joint product of decisions made by economic agents. For example, a factory billowing smoke may be a nuisance to the homeowners living downwind. Coase argued that, in the economist's view of causality, the externality would not exist without both the factory producing smoke and the homeowners desiring to breathe clean air. Coase observed that the economic analysis of an externality stands apart from the legal analysis of determining, based on a notion of fairness, who is a victim and who is liable for causing damages.

Coase argued that the notion of economic efficiency under the traditional approach was incomplete because it took for granted the outcome of the legal process. Coase argued that, within the limits of the traditional approach, an efficient solution is produced only if the party assigned liability happens to be the one who can avoid the problem at the lower cost. The approach is incomplete, in Coase's view, because it fails to account for the fact that in a smoothly operating market (i.e., one without transaction costs), economic agents are free to buy and sell rights. If the law assigns the right initially to the wrong person, the person to whom the right is of the most value can still buy it. The Coase theorem states this thesis.

Coase's Example

To illustrate his argument, Coase used an example of straying cattle damaging the crops growing on an adjoining property. When analyzed in the traditional way, the cattle raiser would be required to pay for all damage caused. Failing to require the cattle raiser to pay for damages would mean that the damage to crops would continue because the cattle raiser would have no incentive to prevent the damage. Coase analyzed the problem by comparing the outcome of two liability regimes. In the first regime, the cattle raiser is not liable for the damage to the farmer's crops. In the second regime, the cattle raiser is liable for the damage caused by his straying cattle. Coase showed that in a smoothly operating pricing system, defined as one without transaction costs, the cattle raiser and the farmer would come to a mutually beneficial bargain that would result in the same number of cattle raised and crops damaged under either liability regime.

Using Coase's example, assume that the cattle raiser faces no liability for damaging the farmer's crops. Further assume that adding an additional steer to the herd will result in $3 additional damage to the farmer's crops. If the gain to the cattle raiser of the additional steer is $2, then it is possible for a bargain to be struck that will make both parties better-off. The farmer would be willing to pay the cattle raiser up to $3 to forgo adding the additional steer to his herd, and the cattle raiser would be willing to comply for any amount greater than the $2 he would receive by adding the steer.

Now consider the outcome under a liability regime where the cattle raiser must pay for crops damaged by his herd. Under this liability regime, the cattle raiser would be willing to pay the farmer up to $2 for the right to add a steer to his herd. But the farmer would require at least $3 to agree to the deal. Under these circumstances, the cattle raiser would refrain from adding an additional steer to the herd—the same outcome as when the cattle raiser was not liable for damaged crops.

Coase used this simple example to illustrate that, in a world without transaction costs, the initial delimitation of legal rights does not have an effect on the efficiency with which the economic system operates.

Although the initial delimitation of rights is an essential prelude to market transactions, the optimal allocation of resources will not depend on this delimitation. No matter how rights are initially delimited, both parties will take into account the harmful effect (i.e., the nuisance) when deciding on their course of action. In a smoothly operating price system, the rearrangement of legal rights will be undertaken when an increase in the joint value of production results.

Positive Transaction Costs

Coase himself viewed the theorem as a stepping stone to his true interest, which was the analysis of a real-world economy with positive transaction costs. Under a regime of positive transaction costs, an initial misallocation of legal rights may persist, uncorrected by market forces. One arrangement of rights may bring about a greater value of production than any other. But unless this is the arrangement of rights established by the legal system, the costs of reaching the same result through the market may be so great that this optimal arrangement of rights, and the greater value of production that it would bring, may never be achieved.

Coase also observed that the traditional analysis of externalities led to the conclusion that the government ought to intervene to fix the problem. Coase's analysis suggests a possible role for government, but he showed that, for some problems, there is no legal rule or no form of regulation that will generate a fully efficient solution. Coase argued that direct governmental regulations will not necessarily give better results than leaving the problem to be solved by the market. Coase argued that all solutions have costs and that, in his view, there is no reason to suppose that governmental regulation is called for simply because the problem is not well-handled by the market.

However, Coase noted that on occasion governmental regulation could lead to an improvement in economic efficiency. For example, Coase argued that government intervention may be required when a large number of people are involved, such as with air pollution, and when the costs of handling the problem through market transactions may be high.

Coase's analysis suggests a government role in promoting the efficient allocation of legal rights through policies that help lower transaction costs and thereby help facilitate market exchange. These government actions include things such as writing clear laws and enforcing property rights. Coase's analysis suggests that transaction costs can be reduced when courts, legislatures, and government regulators consider defining property rights in a way that is "vendible," that is, rights that are defined in a way that facilitates market exchange in case the initial allocation of rights is inefficient.

The insights flowing from the Coase theorem has led to a major federal policy initiative to create tradable emission allowances for various types of greenhouse gas pollutants. The federal government allocates emission allowances and firms are permitted to trade these allowances. Firms, such as the Chicago Climate Exchange, have evolved to lower the transaction costs associated with trading these allowances. The result of trading directs the allowances to their highest valued use. Polluting firms can decide whether to devote resources to reducing emissions or buying allowances. Firms choosing to buy allowances must compete with other firms and clean air advocates to obtain the allowances. Clean air advocacy organizations have emerged to buy up and retire emission allowances. The end result is that the allowances are directed by market forces to their highest valued use.

The insights from the Coase theorem have also proved useful in analyzing disputes involving externalities, apart from pollution and other nuisances. For example, the theorem has yielded valuable insights in evaluating disputes involving financial contracts such as when a corporate restructuring, which benefits shareholders, leads to bondholder harm.

The Coase theorem has also been applied to cases involving positive externalities. For example, fruit growers benefit, in terms of higher productivity, when the bees of honey producers are located on their property. Consistent with the Coase theorem, contracts between beekeepers and farmers have been common practice for many years. When the crops were producing nectar and did not need pollenization, beekeepers paid farmers for permission to put their hives in the farmers' fields. When the crops were producing little nectar but needed pollenization, farmers paid beekeepers.

Influence and Criticisms of the Coase Theorem

The insights contained in the Coase theorem greatly influenced the way economists think of externalities. These insights have also caused legal scholars to think more carefully about how legal rights are defined and enforced. Legal scholars have applied the Coase theorem to determine what legal rules lead to the best outcome from the standpoint of economic efficiency. Because the Coase theorem combines thinking about legal rights and economic efficiency, it has been an important spur to the development of the interdisciplinary field of "law and economics."

The circumstances under which the Coase theorem applies have been widely debated by economists and legal scholars. The Coase theorem has never been formally proved or disproved, although it has been subjected to numerous theoretical, empirical, and experimental challenges in the law and economics literature. Medema and Zerbe survey the controversy and discussion surrounding the Coase theorem in an article published in 2000. Although still controversial, the Coase theorem has caused economists and legal scholars to refine their thinking about externalities and the proper role of government in addressing them.

—James A. Overdahl

See also Chicago School of Economics; Coase, Ronald H.; Contracts; Free Riders; Market Failure; Pollution Externalities, Socially Efficient Regulation of; Property and Property Rights; Public Goods; Transaction Costs

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Codes of Conduct, Ethical and Professional

Codes of conduct are statements of values, beliefs, standards, legal compliance, or organizational policy and procedures that are articulated to inform those governed by the codes or hold those affected by the codes accountable to this type of ethical behavior. Every professional association has created and promulgated a code of conduct for its members. There are more than 1,000 codes of ethical conduct developed by business organizations. Recent surveys of Fortune 500 companies report that more than 97% of all large multinational businesses have codes of conduct. Codes are understood as the primary means of institutionalizing ethics into the culture, religion, profession, learned societies, or business organizations. A Touche Ross national survey revealed that their respondents believed that codes are the most effective measure for encouraging ethical behavior at work.

Historically, the *Code of Hammurabi* contained almost 200 paragraphs of rules governing business, moral, and social life reaching back to the third millennium BCE. Other early codes included the Codes of UrNammu (ca. 2060–2043 BCE), the Code of Lipit-Ishtar (ca. 1983–1733 BCE), and the Code of Eshnunnia (ca. 1950 BCE). These codes were compilations of customs, laws, and rules of ancient Mesopotamia, going back to Sumerian times. The United National Universal Declaration of Human Rights (1948) is a contemporary counterpart to these early codes of conduct.

Corporate or Business Codes of Conduct

Nearly every large business organization today has a corporate code of business conduct. Many of these codes were developed in response to some legislative action. For example, in the United States, a plethora of activity manifesting itself in the development or revision of corporate codes followed the passage of the Foreign Corrupt Practices Act in 1977, the creation of the 1991 United States Corporate Sentencing Guidelines (which exonerated businesses to clearly state expected ethical behavior for their employees), and the Sarbanes-Oxley Act of 2002. In other instances, companies or entire industries responded to an ethics scandal by developing or rewriting codes of ethics, such as in the 1980s when the U.S. defense industry and the financial community on Wall Street were rocked with numerous discoveries of unethical behavior. Many non-U.S. businesses have developed codes of conduct so that their employees are in compliance with U.S. law when the company conducts business in the United States.

Types of Corporate Codes

The titles given to ethics policy statements are quite varied. Some are called codes of business conduct or guidelines for ethical behavior. Some companies have unique names for their codes, such as Johnson & Johnson's "Credo" or Hewlett-Packard's "The HP Way." In the 1970s, when many codes were first being developed, they were called corporate directives or administrative practices until the more common terms of *code of ethics*, *code of business conduct*, or similar terminology was adopted.

Max Clarkson and Michael Deck, scholars at the University of Toronto's School of Business, separated ethics policy statements into three categories—codes of conduct, codes of practice, and codes of ethics. Codes of conduct are statements of rules, indicating for the employees what expected or prohibitive behavior is. Often included in codes of conduct are penalties for code infractions, along with a discussion of numerous ethics topics: conflicts of interest, political contributions, the acceptance or offering of gifts and bribes, and so on. These codes intend to ensure a commonality of behavior among the organizational employees or to protect the firm from the likelihood of costly unethical employee behavior.

Next are codes of practice. These codes are interpretations and illustrations of corporate values and principles. These codes typically intend to empower the employee as an ethical decision maker. Rather than provide strict rules for compliance or avoidance, as indicated in codes of conduct, codes of practice identify for the employee "how we do things around here." A code of practice seeks to shape the expression of the corporation's stated values through the practice of its employees, using rules of thumb such as act and disclose or seek advice.

Finally, codes of ethics are statements of values and principles that define the purpose of the company. The intent is to generally define for the organization's employees various responsibilities to stakeholders. These statements also have been identified as corporate mission or constituency obligation statements. The popular Credo from Johnson & Johnson, mentioned earlier, would be considered a code of ethics according to Clarkson and Deck's designations.

Corporate codes are developed to highlight company philosophy or policy; to define employee rights and obligations; and/or to specify certain responsibilities, such as regarding the treatment of employees, the environment, or other company stakeholders. Most codes speak to the purpose, administration, and authority of the code; the nature of the company; employee issues; legal requirements; and civic responsibilities.

Content of Corporate Codes

Many codes cover specific topics to delineate for employees or other stakeholders what is expected of them. There is a growing trend to develop a code of conduct for the company's customers or suppliers. In the case of the company suppliers, these stakeholders are required to comply with the company's expectations of ethical standards or risk losing the business relationship.

Some of the more common topics covered in corporate codes include

- conflicts of interest;
- use of confidential information;
- use of company assets or property;
- sexual harassment;
- employment hiring, promotion, or termination;
- health and safety issues;
- proper reporting of company-incurred expenses, gifts, bribes, and entertainment expenses (especially for global businesses);
- accurate accounting and reporting practices;
- antitrust or other legal compliance issues;
- government contract relationships;
- environmental responsibility;
- intellectual property; and
- political campaign participation or involvement in public office.

Compliance with corporate codes does not have the force of law behind it because compliance with these codes is technically voluntary. However, in most corporate codes, there are sanction provisions that state that if an employee does not follow the rules established in the company's policy the employees could face disciplinary sanctions. These sanctions could include verbal reprisal, suspension, probation, demotion, transfer, or, in the most serious of cases, termination.

Code Drafters

Various business personnel have been entrusted with drafting the company's code of ethics. At times, senior management or the chief executive officer is involved in writing or suggesting content for the corporate code. Involvement by the highest level of management in the organization often signifies for employees the importance of the document and of behaving ethically.

If the code's purpose is primarily to ensure that employees are legally compliant with the law, then the company's general counsel (chief attorney) or staff primarily will be given the responsibility to draft the code. Sometimes the code is burdened by the legalese that accompanies having the legal department write the document.

Finally, the drafting of the company code could be entrusted with the human resources department because many of the important issues are governed by employment law, such as sexual harassment or equal employment.

Communication of Corporate Codes

One of the most important elements for an effective code of conduct is the communication of the document to all employees or other stakeholders governed by the policy. Some companies are negligent in developing frequent means of communicating the code, thus the policy is often filed in a drawer and forgotten. If the document is not a "living document," then it has little effect on the employees or other stakeholders of the company. However, most companies have developed active and extensive communication procedures to ensure that the code is known and followed.

Most companies provide new employees with the company code at an orientation training session or distribute the code to all employees acquired through a merger. Periodic dissemination of the code occurs in some firms annually or after a breach of the code. Rarely is the code circulated more often than annually, but some companies supplement the distribution of the code with a requirement that employees, typically managers, sign-off on a document that attests that the manager has read the code and has reported any violations of the code to the proper company authority. Companies with global operations might translate the company's code into many different languages so that their employees, customers, or suppliers can read the code in their native language.

In nearly all cases, companies distribute their code to all their employees. There is a growing trend to make the code publicly available and to distribute the code to various company stakeholders, such as customers, suppliers, and investors. The posting of the code of ethics to the company's Web site also is increasing as a practice for communicating the ethical standards held by the company.

International Business Codes of Conduct

Attempts to develop international business codes of conduct have been undertaken by various international governmental bodies with minimal success, such as the

- International Chamber of Commerce (1972),
- Organisation for Economic Co-operation and Development (1976),
- International Labour Organization (1984),
- European Social Charter (1996),
- Code of Conduct for European Multinationals (1998), and
- United Nations Global Compact (2000).

Some specialized United Nations agencies have achieved success on industry-specific issues, such as the World Health Organization's code on pharmaceuticals and tobacco. The International Monetary Fund and the World Bank have codified specific industry practices between nations.

Despite these efforts, most international government or nonprofit organizations have had limited successes in developing codes of conduct. Conflicts in ideology—finding common values or practice—and special interests—protecting economic advantages or political influence—often plague these efforts. International efforts also are thwarted by the lack of an international governing body or the ability to prosecute violators of the code.

One organization, comprising Asian, European, and North America business organizations, has drafted an international code of ethics. The Caux Roundtable's code emphasizes two fundamental ethical principles—*kyosei*, working for the common good, and a respect for human rights. While a promising start, this organization, like their predecessors noted above, is finding it difficult to promulgate their code because there is no enforcement body to ensure that the code is being followed or to punish those that violate the international business standard.

Professional Codes of Conduct

As noted earlier, every professional organization has a code of conduct. By definition, a professional organization drafts and enforces expected ethical behavior of its members and typically will banish members from the professional association for gross violations of the association's code.

A professional code, like most corporate codes, provides standards of practice by describing what is expected or prohibited practice by association members. These stipulations do not apply to everyone, just those who are members or seek to be members of the association. For example, in a business organization not all employees are governed by the American Institute for Certified Public Accountants, just those employees who also are certified public accountants (CPAs) in good standing with the association. In some organizations, there may be multiple professional codes governing individuals' activities, such as at a health care facility where doctors and nurses have different professional codes of conduct.

Professionals, through their codes, set a "higher standard" for their members. Professions are more demanding in the conduct of their professional members. This establishes a clear distinction between what is professionally expected and legally compliant. Professionals are often asked to go beyond the law in their behavior and how they treat those they serve. Professional codes often entrust the individual association member to seek the higher purpose or act without compromise to certain ethical principles, such as honesty, integrity, and justice.

In instances where there is a conflict between professional ethical expectations and workplace practice, members of the profession know that the professional standard is the higher and expected rule. For example, in the accounting field, CPAs are often pressured to recommend additional and costly consulting services for their clients to bolster revenues for their companies. But this practice is contrary to their professional standards detailing a responsibility to their clients and acting on behalf of society and now is prohibited by the Sarbanes-Oxley Act.

What Constitutes a Profession?

The service provided by a profession must be of any morally permissible sort from which its practitioners can earn a living. Most professions are a collection of relatively well-educated occupations, such as physicians, nurses, engineers, educators, CPAs, and so on. Members of a profession believe that there is some benefit to belonging to the professional association and being in compliance with the profession's code of conduct. Sometimes, a profession provides collective bargaining strength to acquire better wages or working conditions, as seen with teachers or nurses. Professions might also organize around a sense of prestige or reputation, such as physicians, attorneys, or CPAs, who serve society in a special way through their work. Whatever the reason, the profession possesses a code of conduct to govern its members and to serve society in a special or highly ethical manner.

Examples of Professional Codes of Conduct

One of the more well-known professional codes is the physicians' Hippocratic Oath. This is an oath sworn by all medical doctors where they attest: I swear by Apollo Physician and Asclepius and Hygieia and Panaceia and all the gods and goddesses, making them my witnesses, that I will fulfill according to my ability and judgment this oath and this covenant.

Similarly, there are codes of conduct for lawyers, who belong to the American Bar Association (ABA). Until 1983, lawyers ascribed to the ABA Model Code of Professional Responsibility and since 1983 there is the Model Rules of Professional Conduct. In addition to the federal professional standards, each state has adopted its own—Pledge of Professionalism (Alabama), Ideals and Goals of Professionalism (Florida), Code of Civility (Maryland), and Working Rules for Professionalism (Pennsylvania), among others.

Engineers, as members of the National Society for Professional Engineers (NSPE), commit to the NSPE Code of Ethics for Engineers. The code's preamble states,

> Engineering is an important and learned profession. The members of the profession recognize that their work has a direct and vital impact on the quality of life for all people. Accordingly, the services provided by engineers require honesty, impartiality, fairness, and equity, and must be dedicated to the protection of the public health, safety, and welfare. In the practice of their profession, engineers must perform under a standard of professional behavior which requires adherence to the highest principles of ethical conduct on behalf of the public, clients, employers, and the profession.

Nurses take the Florence Nightingale Pledge and are guided by a number of professional associations and their codes of ethics. The American Nurses Association states that their Code of Ethics for Nurses has three purposes:

1. It is a succinct statement of the ethical obligations and duties of every individual who enters the nursing profession.
2. It is the profession's nonnegotiable ethical standard.
3. It is an expression of nursing's own understanding of its commitment to society.

University and college professors who belong to the Academy of Management have developed a code of ethical conduct to govern their professional activities. In the Academy of Management's code, five responsibilities are delineated to their students, to managerial knowledge, to the Academy of Management association, to practicing managers, and to all people they work with in the world community.

Codes exist for public sector employees, such as the U.S. Code for Federal Civil Servants, as well as codes for city managers, the International City Managers Association Code of Ethics with Guidelines, and public administration officials, the American Society for Public Administration Code of Ethics.

Within business, some function-area professions have developed their own code of conduct. The American Institute for Certified Public Accountants (AICPA) has a Code of Professional Conduct. The AICPA code consists of two sections—the Principles and the Rules. The Principles provide the framework for the Rules, which govern the performance of professional services by members. The Code of Professional Conduct was adopted by the membership to provide guidance and rules to all members—those in public practice, in industry, in government, and in education—in the performance of their professional responsibilities.

For managers practicing in finance, some belong to the Association for Investment Management and Research (AIMR) and are governed by the AIMR's Code of Ethics and Standards of Professional Conduct. The Code states that members of the profession will

- act with integrity, competence, dignity, and in an ethical manner when dealing with the public, clients, prospects, employers, employees, and fellow members;
- practice and encourage others to practice in a professional and ethical manner that will reflect credit on members and their profession;
- strive to maintain and improve their competence and the competence of others in the profession; and
- use reasonable care and exercise independent professional judgment.

In the marketing field, there is the American Marketing Association's Code of Ethics. In this professional code, the members pledge their commitment to ethical professional conduct. This conduct focuses on various responsibilities, the practice of honesty and fairness in their actions, respecting the rights and duties of parties whom they affect, and adherence to numerous organizational responsibilities.

In the ethically volatile information systems domain, the Association for Computing Machinery (ACM) has developed a Code of Ethics and Professional Conduct. This code consists of 24 imperatives formulated as statements of personal responsibility. It contains examples of many of the issues professionals in the field might likely encounter in their performance of their technical duties. The general expectations for ACM members include the following:

- Contribute to society and human well-being
- Avoid harm to others
- Be honest and trustworthy
- Be fair and take action not to discriminate
- Honor property rights, including copyrights and patents
- Give proper credit for intellectual property
- Respect the privacy of others
- Honor confidentiality

All professional associations and many business organizations have codes of conduct to guide their members or employees and to protect the organization from wrongdoing. In general, these statements are important guides to behavior, but their effectiveness depends on the professionals and employees being aware of and adhering to these codes.

—James Weber

See also Caux Principles; Certified Public Accountants (CPAs); Ethical Role of the Manager; Federal Sentencing Guidelines; Foreign Corrupt Practices Act of 1977 (FCPA); Human Rights; Professional Ethics; Sarbanes-Oxley Act of 2002; United Nations Global Compact; World Bank; World Health Organization (WHO)

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COERCION

To be coerced is to be forced to act against one's will. Coercers are unable to use rational persuasion to convince victims of coercion into performing a specified action and so resort to physical force and threats. Coercion is widely understood to undermine individual freedom, and because of this, its use requires justification. Coercion is relevant to the conduct of business in several ways. For example, coerced contractual agreements are typically regarded as invalid both in ethics and in law. But to determine whether or not coercion has taken place, one must first determine what constitutes coercion.

The Nature of Coercion

To know whether or not a person's freedom has been undermined by coercion, it is first necessary to understand the nature of coercion. Coercion may be usefully divided into two categories—physical coercion and psychological coercion. Physical coercion occurs when one's bodily movements are physically forced. In cases where one person physically coerces another person, the victim's body is used as an object or instrument for the purpose of fulfilling the coercer's desires. Physical coercion does occur in business. For example, a factory worker may be physically compelled to remain at work until a quota is met. Nazi Germany used physical coercion to force laborers to work in wartime factories. In Alabama, as recently as 1928, African American men were taken from city streets and brought to mines where they were physically coerced into mining coal for large mining companies. And in workplaces throughout the world, women employees continue to be physically coerced by coworkers, or managers, into complying with sexual demands.

Unlike cases of physical coercion, psychological coercion involves the threat of violence or of some other form of harm such as economic harm. But what, precisely, constitutes coercion? Is someone who must choose between a bad, poorly paid job and no job at all coerced? To answer this question, it is necessary to have a proper understanding of the nature of psychological coercion. Philosophers have produced a substantial literature that seeks to clarify this matter. Two principal views have emerged in the literature—the moralized view of psychological coercion and the empirical view of psychological coercion. The moralized view maintains that the truth conditions of coercion claims rest on prior moral claims. According to this view, we cannot determine whether one person has coerced another person into performing a specified action without first determining whether the alleged coercer has a right to make the supposedly coercive proposal and whether the recipient of the threat has an obligation to resist that proposal. The empirical view maintains that the truth conditions of coercion claims are empirical. According to this view, we cannot determine whether one person has coerced another person without first determining whether the alleged victim is under significant psychological duress, whether the alleged victim is capable of resisting the coercer, or some other fact pertaining to the situation.

The moralized view of coercion is flawed and should be rejected for at least two reasons. First, proponents of the moralized view acknowledge that appeals to rights and obligations assume prior moral judgments. However, such judgments are of little use for adjudicating claims between individuals who disagree over those judgments or the substantive moral claims that support them. What is needed is a morally neutral account of coercion. Second, the moralized view is unable to account for the prima facie wrongness of coercion. Coercion is prima facie harmful because it undermines individual freedom. This judgment is based on a strong moral presumption against the forced restriction of individual freedom. One centrally important task of any adequate theory of coercion is to explain how coercion undermines individual freedom. To analyze coercion primarily in terms of rights and obligations, or other moral considerations such as utility maximization, does not adequately highlight the fact that coercion constrains individual freedom and undermines individual autonomy. For these reasons, it is necessary to provide an empirical rather than a moralized account of coercion.

Denis Arnold provides one plausible account of coercion. According to Arnold, for coercion to take place three conditions must hold. First, the coercer must have a desire about the will of his or her victim. However, this is a desire of a particular kind because it can only be fulfilled through the will of another person. Second, the coercer must have an effective desire to compel his or her victim to act in a manner that makes efficacious the coercer's other-regarding desire. The distinction between an other-regarding desire and a coercive will is important because it provides a basis for delineating between cases of coercion and, for example, cases of rational persuasion. In both instances, a person may have an other-regarding desire, but in the case of coercion, that desire will be supplemented by an effective first-order desire that seeks to enforce that desire on the person, and in cases of rational persuasion, it will not. Third, the coercer must intentionally attempt to compel the victim of coercion to comply with the coercer's preferences. These are necessary, but not sufficient, conditions of coercion. For coercion to take place, the coercer must be successful in getting his or her victim to conform to his or her other-regarding desire. It should be noted that if coercion is morally objectionable, the *attempt* at coercion will be objectionable whether or not the attempt at coercion is successful.

Coercion and Employment

One of the most common circumstances in which coercion is alleged to occur is regarding employment. It is often argued that capitalists coerce workers into accepting wage proposals, especially when people work for low wages in difficult working conditions. In typical cases, people work for low wages because they believe that that is the best available option for them. When a person makes a choice that seems highly undesirable because there are no better alternatives available, is she coerced? On the account of coercion employed here, having to make a choice among undesirable options is not sufficient for coercion. Such a person is not coerced even though she has no better alternative than working for extremely low wages and in undesirable working conditions. This is because in such cases the employer lacks a coercive will.

Nonetheless, coercion does occur in employment. For example, coercion is sometimes used by supervisors to improve worker productivity. Workers throughout the world report that they are coerced into working long overtime hours. In such cases, the supervisors possess a coercive will and are successful at compelling employees to work long overtime hours, typically by threatening to fire the employee. Nearly all developing economies lack the social welfare programs that workers in North America and Europe take for granted. If workers lose their jobs, they may end up without any source of income. Thus, workers are understandably fearful of being fired for noncompliance with demands to work long overtime hours. When a worker is threatened with being fired by a supervisor unless she agrees to work overtime, and when the supervisor's intention in making the threat is to ensure compliance, then the supervisor's actions are properly understood as coercive. Similar threats are used to ensure that workers meet production quotas, even in the face of personal injury. The use of production quotas is not inherently coercive. Given a reasonable quota, employees can choose whether or not to work diligently to fill that quota. Employees who choose idleness over industriousness and are terminated as a result are not coerced. However, when a supervisor threatens workers who are ill or injured with termination unless they meet a production quota that either cannot physically be achieved by the employee or can only be achieved at the cost of further injury to the employee, the threat is properly understood as coercive. In such cases, the employee will inevitably feel compelled to meet the quota.

According to the analysis provided here, workers choose to work for low wages because the alternatives available to them are worse. However, once they are employed, coercion is sometimes used to ensure that they will work long overtime hours and meet production quotas. Respecting workers requires that they be free to decline overtime work without fear of being fired. It also requires that if they are injured or ill—especially as a result of work-related activities—they should be allowed to consult health care workers and be given work that does not exacerbate their illnesses or injuries. Using coercion as a means of getting employees to work overtime, or to meet production quotas despite injury, is incompatible with respect for employees because the coercers treat their victims as mere tools.

—Denis G. Arnold

See also Autonomy; Consent; Employment Contracts; Exploitation; Freedom and Liberty; Freedom of Contract; Free Will

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Cognitive Moral Development

The basic tenet of moral development, understood as a cognitive process thus also called cognitive moral development, is grounded in the belief that human nature is naturally good. As humans, we lean toward an awareness of the good and have a preference for it rather than for evil and injustice, although we do not always achieve this inclination in our behavior. Human nature is also self-realizing and self-perfecting in our moral understanding. Our morality, or cognitive moral development, grows along with our physical growth and social capabilities. Both individually and in social interaction the human species evolves mature moral conscience and character despite the many potential psychological and social impediments that could slow or derail the process for a time.

Supporting these beliefs are the discoveries made by developmental psychologists, who have found that an individual's cognitive moral development progresses, often correlated with age or education, to a broader and more morally preferable perspective. In the late 19th century, cognitive moral development was revived as a lively research field in social science. This revival was later fueled by the moral developmental approaches espoused by Jean Piaget, Lawrence Kohlberg, Carol Gilligan, James Rest, and Augusto Blasi. For these psychologists, cognitive moral development was not determined wholly by age but was heavily influenced by a natural development involving complex combinations of trial-and-error social interactions. Through these experiences, individuals altered their reasoning processes and typically their behavior to model after the new and morally advanced patterns of cognition. Humans are naturally prone toward moral progress and to strive for the moral ideal.

This entry focuses on the key cognitive moral development frameworks that have been applied to the study of ethical decision making and the field of business ethics. While there have been debates and criticisms regarding these key frameworks and reasoning assessments over the years, these models remain the primary tools for assessing moral reasoning in the business ethics field.

Jean Piaget

Piaget conducted research for more than 40 years into the origins and development of cognitive structures and moral judgments in the early years of life. Piaget rejected the traditional emphasis on linking development either to nature or to nurture by introducing a third factor: a cognitive schema or system that mediated the interplay of biopsychology and socialization—nature or nurture. Piaget asked children to describe their intentions and behavior, their goals and aspirations, and how they made sense of them.

He found that children coconstructed their moral realities and uncovered two cohesive systems of moral thought. The childhood *morality of constraint* or stage of heteronomy focuses on rules as external laws that are sacred because they have been laid down often by adults. This reasoning centers on conformity to approved social conventions by fulfilling them. The child reasons that there are a certain number of commands or rules that must be obeyed whatever the circumstances be. Right is what conforms to these commands, wrong does not.

The adult *morality of cooperation* or stage of autonomy shows greater concern with doing the right thing per se within the framework of mutual purposes. Rules are seen to be the outcome of a free decision and worthy of respect in the measure that they have enlisted mutual consent. The child gradually comes to realize that social rules can be used as instruments for coordinating social activity and that cooperative social arrangements can lead to mutually valued goals. Piaget's two moralities often are characterized as poles of development. They are now seen as rough descriptions of the beginning and the end points of the course of development rather than successive transformations in cognitive development.

Lawrence Kohlberg

Lawrence Kohlberg, a student of Piaget, expanded on the initial construction of two poles of morality into a theoretical model depicting three levels of cognitive moral development, with two stages within each level. Like Piaget, Kohlberg did not concentrate on moral behavior. He did not concern himself with individual actions; rather, he studied the reasons given for why certain actions are perceived as morally just or preferred. These reasons, for Kohlberg, were the indicators of the stages of moral maturity. As Kohlberg's research bears out, when one looks at the reasons people give for their moral judgments or moral actions, significant differences in their moral outlook over time become apparent. These differences are captured in Kohlberg's stages of moral development.

Kohlberg's commitment to a stage concept of cognitive moral development was based on three important traits. First, Kohlberg's analysis of underlying stage structures rests on people's responses to open-ended dilemmas. These stage structures are far more powerful and incisive than Piaget's two stages. Second, the results from Kohlberg's longitudinal study strongly supported the notion of a stage model. During the 20 years in which 58 males were provided moral dilemmas and their responses recorded, subjects seemed to proceed through developmental stages of moral reasoning in a specific sequence. No subject skipped a stage in the sequence or showed a significant downward stage trend. Third, Kohlberg stressed a preference for qualitative analysis over quantitative analysis. The cognitive developmental approach emphasizes ideal-typological constructs that emphasize qualitative organizations or patterns of cognition that lead to behavior rather than focusing on quantitative descriptions, such as frequency, intensity, and others.

Kohlberg's three levels of moral development correspond to three sociomoral perspectives: preconventional and the concrete individual perspective, conventional and the member of society perspective, and postconventional and the prior to society perspective. Within each of the three levels are two stages, with the second stage a more advanced and organized form of the general perspective of each level.

Kohlberg's Stages of Moral Development

At the preconventional level, an individual is responsive to cultural rules and labels of good and bad, right and wrong and understands morality in terms of the personal consequences involved, such as punishment, rewards, or an exchange of favors, or focuses on the imposition of physical power by authority. In Stage 1—the punishment and obedience orientation—the physical consequences associated with an action determine the goodness or badness of a decision regardless of the human meaning or value of these consequences. Avoidance of punishment and unquestioning deference to power are valued in their own right, though not in terms of respect for an underlying moral order supported by punishment and authority.

In Stage 2—the instrumental relativist orientation—right action consists of that which instrumentally satisfies one's own needs. Human relations are viewed in terms of a marketplace. Elements of fairness, reciprocity, and equal sharing are present, but they are always interpreted in a physical or pragmatic way. Reciprocity is a matter of "You scratch my back and I'll scratch yours," not of loyalty, gratitude, or justice.

Reasoning at the conventional level, encompassing Stages 3 and 4, emphasizes performing good or right roles, maintaining traditional or acceptable order as determined by a group or society, or meeting others' expectations. In Stage 3—the interpersonal concordance or good boy–nice girl orientation—good behavior is that which pleases or helps others and is approved by them. There is much conformity to stereotypical images of what is majority or natural behavior. Behavior is frequently judged by intention: He means well—becomes important for the first time. One earns approval by being nice. The individualistic perspective found in Stages 1 and 2 are coordinated into a third-person perspective at this stage. Mutually trusting relationships among people, embodied in a set of shared moral norms according to which people are expected to live, characterize this stage. The justice principle, present in some form in all of Kohlberg's stages, is represented in Stage 3 as the golden rule: Do unto others as you would have others do unto you.

In Stage 4—the law and order or social system orientation—the individual takes the perspective of a generalized member of society. This perspective is based on a conception of the social system as a consistent set of codes and procedures that apply impartially to all members in a society. The pursuit of individual interests is considered legitimate only when it is consistent with the maintenance of the sociomoral system as a whole. A society that includes formal institutions and social roles serves to mediate conflicting claims among its citizens and promote the common good. Thus, there is awareness that there can be conflicts even between socially good citizens, although these conflicts can be resolved due to the presence of a system of roles for the citizenry within the society. The perspective taken is generally that of a societal, legal, or religious system that has been codified into institutionalized laws and practices.

In the postconventional level, the individual defines moral values and principles apart from established moral authority and relies on self-chosen principles, from a set of universally acceptable principles, to guide reasoning. In Stage 5—the social contract legalistic orientation—there is a clear awareness of the relativism of personal values and opinions and a corresponding emphasis on procedural rules for reaching consensus. Apart from what is constitutionally and democratically agreed on, what is right is a matter of personal values and opinion. The result is an emphasis on the legal point of view, but with the possibility of changing law in terms of rational considerations of social utility rather than rigidly maintaining adherence to the law as seen in Stage 4.

In Stage 6—universal ethical principle orientation—right is defined by the decision of conscience in accord with self-chosen ethical principles appealing to logical comprehensiveness, universality, and consistency. These principles are abstract and ethical, such as the categorical imperative, and are not concrete moral rules, such as the Ten Commandments. There are universal principles of justice, of the reciprocity and equality of human rights, and of respect for the dignity of human beings as individual persons.

Traits of Kohlberg's Stage Development

Kohlberg's six stages of moral development manifest a number of traits essential to a full understanding of his cognitive moral development theory. Kohlberg argued that these characteristics were integral to his stage theory of moral development and carried valuable implications for moral education.

First, development is step by step, that is, the stages are invariant. Hence, a Stage 2 person does not leap to Stage 4. Rather, the person gradually moves from Stage 2 through Stage 3 on the way to Stage 4.

Second, development can terminate at any stage. Kohlberg, for example, found in his prison studies that many inmates reason from Stage 2 structures. The majority of adults probably terminate at Stage 4, some develop to Stage 5 in their cognitive capabilities, but rarely to Stage 6.

Third, an individual's reasoning is predominantly one stage. Occasionally Kohlberg found that the individual spills over into one stage above or one stage below the predominant reasoning stage.

Fourth, an individual can be attracted to reasoning one stage higher than the predominant stage. However, an individual is typically not attracted to the stage below the predominant stage.

Fifth, development is not governed by age. The rate of moral development, Kohlberg found, varies among individuals. Some young people achieve higher stages than older adults.

Sixth, cognitive development is a necessary, but insufficient, condition for moral development. Abstract reasoning ability is essential to entertain alternatives in moral reasoning and to order priorities in values. One reason why children under 12 years of age cannot be expected to attain higher stages of moral development is because those stages require more sophisticated cognitive abilities than young children possess, primarily the ability to reason abstractly.

Seventh, empathy is also a necessary, but insufficient, condition for moral development. It is through empathy that one develops an understanding of what a community is and begins to judge actions as right or wrong on the basis of mutual respect. These traits of stage development have been supported through the findings of Kohlberg and his associates.

Carol Gilligan

Kohlberg's theory and stage model of cognitive moral development has achieved substantial notoriety and usage among scholars but the theory and scoring method have not been without their critics. Some of the early and most specific critiques came from feminist scholars, emerging from the findings of Carol Gilligan, a former student and colleague of Kohlberg. Highlighting the all-male population that Kohlberg used for his 20-year longitudinal study, Gilligan argued that Kohlbergian research, like that of Rawls, Piaget, and Freud, reflected a male bias on morality and development. Her critique was particularly timely, as research in many fields was gradually seen to privilege the experience of white males as the norm, to the detriment of women and minorities, whose experience was treated as abnormal and less relevant for empirical analysis or theory building. Kohlberg's all-male research sample gave evidence of a moral orientation toward justice and rights, focusing on foundational moral concepts and universal laws, and in its higher stages, on abstract principles.

Gilligan's research, in contrast, focused on the reasoning of women and girls facing challenging moral issues in their lives. Whereas Kohlberg provided his research participants with hypothetical dilemmas to reason through, Gilligan asked research subjects to describe real-life dilemmas that they faced. In doing so, she argued that Kohlberg's hypothetical scenarios were biased by his own views of what constitutes a moral issue. She was interested in studying how women and men defined and experienced moral issues uniquely and whether their reasoning differed.

Ultimately, Gilligan argued that her research gives evidence of a predominant ethic of care among women, which she contrasted to the ethic of justice articulated by Kohlberg. While she insisted that this was not an absolute gender split, the essentialist association of men being most interested in justice and women being most interested in care was widely and popularly interpreted as the legacy of Gilligan's research on moral reasoning. Her findings gave impetus to a broad range of research on the ethics of care and the reasoning of women and girls.

The ethics of care focuses on moral responsibilities within relationships—on supporting, nurturing, and responding to others in ways that are most valued by them, not on demanding reciprocity or defending rules. Even the golden rule is seen in this contrast to be more reflective of an ethic of justice than an ethic of care. Mature caring shows great competence in attending to others, in listening and responding sensitively to others through dialogue aimed at consensus. As a goodness ethic, caring also emphasizes the sharing of aspirations, joys, and accomplishments of others.

Underlying Gilligan's theory of a caring morality are the research findings of Nancy Chodorow and Janet Lever. Chodorow asserted that the universal role of women as caregivers, for young children as well as other family members, deeply affects the personal and moral development of sons and daughters. Daughters see themselves as similar to their mothers and build their identity in relationship to their mothers, while boys understand early on that they are different from their mothers and must build their identity by separating from their closest caregiver. As a result, in any given society, the female personality comes to define itself in relation and connection to other people more than the male personality does. Chodorow suggested that girls and women are thus defined through attachment and identifying with others in contrast to boys and men who gain their sense of self through individuation. Gilligan drew the further observation and conclusion that more often women perceive the highest morality to be about caring selflessly about others, while men focus more on abstract principles of justice and fairness among equal individuals.

While subsequent research by Gilligan's students supported her findings, other researchers suggested that it is more likely that both women and men have the ability to reason from the perspectives of care and justice, and that if these are distinct moral orientations, they are perhaps on a continuum with most people somewhere in the middle. For example, Robbin Derry's research on moral reasoning in work-related settings proposed that people make choices about which kind of moral reasoning they use, depending on the values within the different environments of their lives.

Cognitive Moral Development as a Field of Managerial Research

From its infancy in the late 1800s to today, cognitive moral development is a research specialty of cognitive and developmental psychology. It has strong associations and implications for anthropology, cognitive science, social and political psychology, law, and education. It is only since the 1980s that cognitive moral development has been applied to business or become an area of concern for management scholars. The key underlying emphasis on morality makes it a natural field of inquiry for moral theorists, philosophers, organizational behavioralists, and business ethicists.

Most cognitive development theorists focus on children as their subjects, measuring the progression of moral reasoning over time. Management scholars, however, often focus on measuring the moral reasoning of adult populations, including managers, typically using the Defining Issues Test developed by James Rest, which builds on and extends Kohlberg's theory of moral development. This analysis specifically measures moral reasoning rather than development, since the subjects are morally mature as adults. Research by Brabeck, Treviño and Youngblood, and Weber and his colleagues has gone beyond simply identifying a manager's moral reasoning stage to characterize or predict how a manager might reason when confronted with an ethical or moral dilemma.

Scholars have found that, when using a managerial population, moral reasoning is heavily influenced by the context or situation confronted by the decision maker or the moral intensity of the dilemma. Frey provides a good summary of this work. Sometimes managers use lower stages of reasoning when resolving familiar situations or dilemmas involving minimal consequences, whereas higher stages of reasoning are evoked when hypothesizing what the decision maker might do or when the situation involves the risk of human life.

Various personal characteristics have been assessed regarding their relationship to an individual's moral reasoning. One study by Ruegger and King, for example, reported that older managers with more work experience actually used lower reasoning stages than young, less experienced managers. This may indicate that the influence exerted on a decision maker by the organization that employs the individual might be a significant influence on moral reasoning.

Research conducted by Brabeck, Treviño and Youngblood, and Green and Weber reports that there is a moderate relationship, when using managers as the sample, between moral reasoning and moral behavior. Managers using higher-order reasoning more often are inclined toward the morally preferred behavior. This finding gives rise to the call for greater attention toward improving managers' moral reasoning through organizational training using moral development schemas.

In exploring the question of how moral understanding and moral action are linked, Augusto Blasi has focused on the integration of morality in identity. The integration metaphor assumes that human personality strives for unity, and while the integration of morality may be driven by reason, it is a fragile process, often at odds with our most natural and instinctual impulses. One aspect of Blasi's research that is particularly relevant to the study of managers is moral self-deception. He proposes that moral self-deception can only occur in a person who understands morality and is genuinely motivated by moral concerns, that is, an individual who has achieved some degree of moral integration. But a corollary is that moral self-deception is less likely to occur when the morality is more strongly integrated with identity and the motivating power of morality is deeply felt. In Blasi's view, moral integration makes self-deception possible, while it also limits and provides a barrier to self-deception.

The investigation of moral development and reasoning is critical to ethics scholars and professors in managerial education, as they suggest that achieving moral understanding is only a partial explanation and determination of one's moral action. Nonetheless, the scholarly understanding of ethical behavior in the workplace is directly related to the field of cognitive moral development. The "why" people reason resulting on "how" they act is an important conundrum confronting moral development scholars.

—James Weber and Robbin Derry

See also Ethical Decision Making; Ethical Role of the Manager; Ethics of Care; Feminist Ethics; Justice, Theories of; Kohlberg, Lawrence; Moral Education; Moral Reasoning

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COGNITIVISM AND ETHICS

Cognitivism in ethics maintains that ethical convictions (regarding actions, states of affairs, or character traits) function the same way as other ordinary beliefs in that they are capable of being true or false. Cognitivism, therefore, holds that such convictions have *propositional* content and their correctness or incorrectness is determined by whether they are true or false, respectively. So, for instance, ethical claims such as "it would be unjust to terminate that employee" or "it is dishonorable for him to deceive her like that" are conveying states of mind regarding just and honorable behavior that can be determined to be true or false. In this regard, cognitivism is a metaethical thesis regarding the semantic status of ethical claims that has both ontological and epistemological implications regarding what is true and what we can know to be true.

Cognitivists disagree with noncognitivists who maintain that ethical convictions actually *express* attitudes, feelings, desires, or other affective states of mind and, as such, are not capable of being true or false. This disagreement has significant implications for the supposed objectivity of ethical claims; cognitivist views tend to defend the objectivity of ethical judgment because they ground the correctness of ethical evaluations in what is literally true and false—either about the world or as a matter of reason. Noncognitivists of various stripes are thought to advocate a kind of subjectivism whereby ethical convictions express nothing more than attitudes, feelings, desires, or preferences. One needs to exercise caution here, however, since subtle differences between various forms of cognitivism and noncognitivism may not easily map on to the distinction between objectivism and subjectivism in ethics. One plausible form of cognitivism, for instance, asserts that ethical claims function as *summary reports* of attitudes, desires, or preferences toward a certain kind of act. On this variant of cognitivism, to think that "it would be unjust to terminate that employee" is tantamount to thinking "I (or my group) disapprove of that employee's termination." We can evaluate the truth or falsity of this ethical conviction by simply consulting whether the relevant individual (or group) possesses the attitude, feeling, or desire implied by the claim. This is undoubtedly a cognitivist account of one's convictions, but it remains fundamentally subjectivist because it identifies what is ethically true with prevailing human attitudes, desires, or feelings. In short, there is a fundamental difference between *reporting facts about* what an individual or group prefers (a cognitive, truth-apt matter) and the *expression* of such preferences (a noncognitive, affective matter). Despite this kind of complexity, there is a clear tendency among cognitivist theorists to defend a notion of moral truth that is not reducible to desires, attitudes, and preferences, hence the generalization that cognitivism supports objectivism in ethics.

To the extent that cognitivists assert the truth aptness of ethical claims, an important question immediately arises for cognitivism, "What does ethical truth consist in?" The answer to this question is complicated and will occupy the remainder of this entry.

One avenue that theorists have taken to defend cognitivism in ethics is represented by so-called moral realists. Realists maintain that (1) ethical claims are genuine claims in the sense that they purport to *describe* intrinsic ethical facts found in the world and (2) such ethical facts actually exist. So, in the above examples, there are *facts* about whether certain actions are unjust or dishonorable, independent of our judgments about them. More important, the normative force of such predicates—that we have inescapable *obligations* to refrain from unjust and dishonorable behavior—is irreducibly part of the very nature of unjust and dishonorable actions. Realists assert that actions have an ethical character just as they have other factually identifiable properties.

In what some have taken to be one of the early formulations of realism, G. E. Moore famously wrote that moral "goodness" is a noneliminable, nonnatural property of human action. Moore and others, most notably W. D. Ross and H. A. Prichard, have extended this line of thought to an array of moral claims involving the properties of fairness and beneficence. These so-called intuitionists have been saddled with a particularly challenging epistemological problem: How do we come to *know* such properties given that they seem so radically different (in kind) from natural properties? To say that humans have a special faculty of intuition or direct awareness of these special moral properties seems called for by this form of realism; yet this solution remains very unsatisfying for some due to its seemingly ad hoc nature.

Naturalists have attempted to recast moral realism within a less metaphysically obscure framework. Instead of supposing that moral properties are nonnatural, naturalists believe that moral claims simply describe natural states of affairs. Moral concepts such as goodness can be reduced to other more basic sociological, psychological, or even scientific properties. States of human happiness, for instance, can, in principle, be identified and reported as facts about the mental states of human beings. This form of naturalism asserts that a moral property such as goodness can be reduced to assertions about what will promote the experience of human happiness, individually or collectively. Naturalists are immediately faced with a particularly challenging objection that served as Moore's original motivation for developing the kind of nonnaturalist intuitionism described above. The so-called naturalistic fallacy holds that it is impossible to derive a moral conclusion from nonmoral facts about the world. More common, one cannot derive an "ought" from an "is." This problem is underscored by Moore's famous "open question" argument, which was designed to show that for any naturalist account of moral claims, someone can always intelligibly ask *why* the identified natural property has the moral characteristic identified with it. So, in the above version, the naturalist would find the question "Is happiness good?" unintelligible because she or he has already reduced the meaning of goodness to states of happiness. But Moore believes that such a question is quite intelligible and, therefore, demonstrates how moral properties cannot be reduced to natural states of affairs.

Other cognitivist approaches to ethics rely more on the rationality of ethical claims as opposed to their supposed description of actual properties, whether natural or nonnatural. The historical figure most naturally associated with this way of grounding the cognitive nature of ethics is the Enlightenment German philosopher Immanuel Kant. Kant maintained that the truth of basic ethical claims could be uncovered because humans were rationally autonomous creatures. The basis for our ethical prescriptions rested, for Kant, on our distinctive capacity to seek good *reasons* to act in certain ways. Basic ethical principles, thus, are nothing more than prescriptions and prohibitions derived from the laws that humans set for themselves as rational creatures. This led Kant to construct his famous Categorical Imperative, the most general expression of the law of reason, which maintains that one ought to act only in ways that can be willed to be universally adopted by all others. From the Categorical Imperative, Kant was able to explore what kinds of actions could and could not be universally willed in this manner. The former are permissible, that is, can serve as an acceptable ground for an autonomous will, while the latter were impermissible.

In this way, Kant was able to salvage a universal basis for ethical claims while grounding their truth in the form of reason itself rather than a metaphysics of moral properties.

—*Jeffery Smith*

See also Kant, Immanuel; Kantian Ethics; Metaethics; Moral Realism; Naturalistic Fallacy; Noncognitivism

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Collective Choice

Collective choice refers to situations in which two or more individuals jointly pursue a common objective. As such, collective choice is fundamentally a problem of coordination. This is in contrast to instances in which individuals pursue similar or even identical objectives independently; in this case, coordination of individual actions is not expected.

Collective choice exists because humans have an inherent inclination to form and interact in groups. This is because there are many things that people can do collectively that cannot be achieved when acting individually or independently. Generally, collectives form voluntarily. Business firms, social clubs, religious organizations, social movements, caucuses, and governments are examples of collectives that form because individuals desire to achieve a common objective. However, sometimes collective choice arises in situations in which members are brought together involuntarily, as when people are called to jury duty or drafted in the army, or when children are added to families by birth or adoption.

Collective choice is necessary in the case of the public goods problem and the related tragedy of the commons. Public goods are goods or services that cannot be excluded from nonpayers and that do not diminish when consumed. Private firms are often reluctant to provide these goods; hence, their provision and distribution must be accomplished collectively. The tragedy of the commons refers to the tendency for people to overuse or exploit publicly available goods or common property. Sometimes the establishment and enforcement of private property rights can mitigate the exploitation of some common properties but, generally, these are ineffective in the case of goods that have characteristics of public goods. In these instances, collective choice regarding the use of common properties is almost always the most viable means of solving the tragedy of the commons.

Although there are advantages to collective choice, there are also problems that arise when people seek to make decisions and take actions collectively. For instance, members do not always agree on what the collective objective ought to be, and collectives do not always achieve their stated objective. The root cause of problems afflicting collective choice is that individuals interested in their own self-interest do not always behave in ways that support the collective. Two of the most important factors affecting the degree to which individual interests coincide with those of the collective are homogeneity of members and group size. Collectives with members having similar interests or characteristics are more likely to agree on and support collective objectives. Small groups are more likely to consist of members with similar interests when compared with large groups. Furthermore, in small groups individual members generally receive a greater fraction of total group benefits, and small groups also have lower organizational and coordination costs than large groups.

There are several problems that limit the effectiveness and desirability of collective choice. One problem is free riding on the joint efforts of others. Free riding means obtaining a benefit without expending an effort or paying a cost. Free riding is a problem if members join a group to obtain benefits of membership but have little or no intention of contributing to the group effort. For example, businesses using a team-based organizational structure often report difficulty in motivating all members of the team to contribute fairly. Simply, people might shirk if they believe it is difficult for superiors to assess precisely the individual effort of all team members. Another problem is members controlling or influencing the collective choice in their favor. One example of this is when employees spend time and effort currying favor with superiors at the expense of completing their assigned duties.

The coordination of the varied interests of group members is vital to the success of collective choice. Fundamentally, this requires the creation of a collective or social contract among members, in which members agree to participate and contribute to the collective good in exchange for explicit or implied group benefits. There are many mechanisms that can facilitate the process of social contracting, such as formal rules, group norms, stakeholder dialogue and engagement, selective incentives, coercion, monitoring, and the threat of expulsion. Ultimately, collective choice succeeds when members believe that the benefits of participation exceed the costs and when the interests and actions of group members are aligned with the collective's interests.

—Harvey S. James, Jr.

See also Commons, The; Externalities; Free Riders; Prisoner's Dilemma; Public Goods; Self-Interest; Social Contract Theory

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Collective Punishment and Responsibility

Collective Responsibility

Collective responsibility is to be contrasted with individual responsibility. Here, we shall be focusing on the debate concerning collective *moral* responsibility rather than any legal significance of the term because Western legal systems primarily regard individual humans as the proper subjects before the law. The philosophical debate surrounding the legitimate attribution of moral responsibility is premised on the notion that *individual* humans generally possess certain metaphysical characteristics in virtue of which they qualify as moral agents and may, thus, be legitimately attributed with moral responsibility. The debate concerning *collective* moral responsibility is then couched in terms of discussing whether or not a group of individuals can collectively possess the relevant characteristics of moral agency to be legitimately attributed with moral responsibility collectively.

It is generally accepted that there is an important difference between two types of collectives—an aggregate collective and a conglomerate collective. An aggregate collective (also called a random collective) consists of a group of individuals who together bring about a certain event through the aggregation of their individual efforts. For example, an angry mob of people may cause damage to a neighborhood through the aggregation of each individual's act of destruction. A conglomerate collective, on the other hand, is an organized group of people with an established decision procedure to make collective decisions. The members of a conglomerate collective work concertedly in the pursuit of a common goal. For example, the members of an orchestra each contribute their individual parts to the collective goal of playing a symphony in concert.

It is commonly accepted that there are three necessary conditions for moral agency: to have the ability to *intend* an action, the ability to *perform* an action, and to have the *autonomy* to choose an intentional action. With regard to the attribution of moral responsibility, it is generally acknowledged that an aggregate collective does not possess any of these characteristics as a collective unit, but being a mere aggregation of individual actions each member is distributed moral responsibility for the event in question. However, controversy surrounds whether or not a conglomerate collective can meet the conditions of moral agency. It has been argued (e.g., by Virginia Held) that the entire membership of a collective may be morally responsible as a unit. The idea is that the collective decision structure binds the members and obscures lines of responsibility to the individual members such that only a responsibility attribution to the collective whole is possible. It is the members collectively who are attributed responsibility, but because the structure obscures the lines of individual responsibility, the attribution of responsibility is not distributable to the individual members, but rather the members are held collectively responsible as a unit. The collective whole is considered to satisfy the conditions of moral agency in virtue of the actions of all the individual members (or vicariously by some of the members) who are moral agents, and thus, the collective is deemed to be the legitimate subject of moral responsibility attributions.

Another possibility that has been suggested (e.g., by Peter French) is that the organizational structure of a conglomerate collective might qualify as the principal, in a principal-agent relationship, where the collective's members act as agents on behalf of the organization. The idea is that the structure with its decision procedure and policies qualifies as the *intention* of the organization and then directs the members to act on its behalf. In this case, the moral responsibility attribution is meant to lodge with the collective's structure conceived as logically distinct from the members, and thus, the responsibility is not distributed to the members.

Theories of collective responsibility are of great importance to the debate over corporate moral agency because a corporation may often be represented as a conglomerate collective with decision procedures, lines of authority, and a corporate policy that directs the efforts of members in pursuit of a common goal. However, it should be mentioned that the legitimacy of attributing moral responsibility to conglomerate collectives is controversial. There are strong arguments against it on the basis that collectives do not possess the capacities for moral agency in any morally relevant sense because they do not per se have intentional mental states. For example, a conglomerate structure might causally *explain* a collective event but it does not literally "intend" the event.

Collective Punishment

Collective punishment involves the imposition of a penalty, such as corporal harm, social scorn, the deprivation of personal freedom, or a financial fine, on a collective of individuals. For example, a teacher might decide to collectively restrict the freedoms of an entire class on the basis of the act of one or more children. Collective responsibility bears on collective punishment in that the collective may be regarded as the proper subject of punishment. Theories regarding the justification of punishment are generally considered to be retributive or utilitarian. Being able to maintain that a group is collectively responsible is most important for proponents of retribution because the punishment is based on the subject *deserving* the penalty. Utilitarian justifications for collective punishment tend to be based on some instrumental dimension such as expediency. For example, it may be difficult to discern which member of a collective is responsible for an event, and thus, it is easier to simply punish the collective whole. Irrespective of one's view on whether or not attributions of collective responsibility are distributable to the individual members, it should be clear that collective punishment is always distributive because what affects the collective whole will inevitably affect its members. The attribution of moral responsibility is usually not itself considered a punishment, although such an attribution may often be difficult to separate from a social sanction of disapproval.

Western legal systems generally disapprove of collective punishment. The Geneva Convention (IV) of 1949, Part III, Section I, explicitly prohibits the use of collective punishment. However, legal sanctions imposed on corporations are not considered a form of collective punishment because the corporate legal person is regarded as an entirely separate legal entity from the corporate members.

—David Ronnegard

See also Corporate Moral Agency; Corporate Social Responsibility (CSR) and Corporate Social Performance (CSP); Moral Agency

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Collusion

Collusion is an agreement between two or more persons to deprive another person of his or her legal rights or to obtain a benefit forbidden by law. In addition to persons, collusion may involve companies, associations, or countries. Collusion implies the existence of fraud or the use of unlawful means to accomplish an unlawful objective. Collusion implies also secrecy and deception on the part of parties who have obtained a mutual benefit in the form of profit or control and, in the process, have intentionally violated established laws or rules.

Because collusion involves intent to deceive for an unlawful purpose, it differs from cooperation and collaboration. Cooperation and collaboration provide an assumed mutual benefit but they do not involve violation of law or rules. Society and governments desire that companies collaborate and cooperate if the purpose is to enhance products or services for the public good and does not restrain competition. However, given that a legal interpretation must be made as to when legitimate cooperation becomes illegal collusion, prosecution of collusion cases are often time-consuming and heavily reliant on circumstantial evidence.

Collusion is illegal in most countries of the world. In the United States, collusion for criminal misconduct is prosecuted by the Antitrust Division of the Department of Justice under the antitrust provisions of the U.S. Sherman Act of 1890. Civil lawsuits under the Sherman Act are the responsibility of civil trial lawyers, often referred to as "private attorneys general."

The remainder of this entry is organized in four parts. The first section describes the objective of federal antitrust enforcement with respect to collusion. The second section outlines and describes the major forms of collusion. The third section discusses important legal forms of collusion. Finally, the fourth section offers an overview of means and methods to prevent and detect collusion.

Federal Antitrust Enforcement

Collusion interferes with the free flow of trade and commerce in competitive markets, which are expected to provide the best goods and services at the lowest prices. When competitors collude, consumers pay inflated prices, supplier firms may experience depressed prices, and market participants may have fewer choices. The Sherman Act prohibits any agreement among competitors to fix prices, rig bids, or engage in anticompetitive activity. In recent years, the Department of Justice has prosecuted cases, at the regional, national, and international levels, involving construction, agricultural products, manufacturing, service industries, and consumer products. Most criminal antitrust cases involve price-fixing, bid rigging, or market division and allocation schemes.

Because of the nature of secrecy and deception, collusion is rarely overt. The most subtle form of collusion is referred to as tacit collusion. In tacit collusion, parties act for mutual benefit often without meeting or direct communication. The tacit colluders act discreetly at the expense of a third party or the market system in general. An example of tacit collusion that violates the Sherman Act is price signaling. Companies in an industry with few sellers may engage in price signaling in which one company publicly announces a price increase as a signal for other industry participants to mimic the action. In the case of signaling, companies are tacitly colluding to fix or set prices in restraint of trade and fair competition.

The Antitrust Division of the Department of Justice prosecutes collusion among competitors not only under the Sherman Act but also under the mail or wire fraud statute, the false statements statute, and other federal felony statutes. If they occurred at least in part within the last 5 years, collusion cases may be prosecuted as criminal offenses. Proving that a crime has been committed does not require the existence of an agreement to collude. Testimony and circumstantial evidence may be sufficient.

Forms of Collusion

Price-Fixing

Price-fixing is an agreement among competitors to raise, fix, or control the price at which their goods or services are sold. The purpose of price-fixing collusion is to limit supply to generate monopolistic prices and higher than competition-based returns to the colluders. For the collusion to be successful, the colluders must act like a monopoly or oligopoly, that is, have a limited number of providers, large number of purchasers, relatively constant demand, and ease of monitoring others' supply chains. Examples of collusion include Archer Daniels Midland (ADM) and F. Hoffmann-La Roche.

In the late 1990s, ADM and several other companies participated in an international cartel organized to restrict the output of lysine, a livestock and poultry feed additive. The cartel inflated the price of this amino acid product during the course of the conspiracy. ADM pleaded guilty and was fined $100 million. Other participating corporations were also prosecuted and assessed multimillion-dollar fines. In addition, three ADM executives were convicted for their personal roles in the cartel.

F. Hoffmann-La Roche Ltd., a Swiss pharmaceutical company, and a German firm, BASF Aktiengesellschaft, participated in a worldwide, 9-year conspiracy to fix prices and allocate market shares for vitamins. At trial, the firms pleaded guilty and were fined $500 million and $225 million, respectively.

Colluding can not only be very costly on conviction but also extremely embarrassing to high-profile defendants. In France, six of Paris's most prestigious five-star hotels were convicted of illegal price-fixing in 2005 after it was determined that hotel managements made regular exchanges of confidential information in a collusive effort to set floor or minimum prices for luxury rooms. The hotels were convicted and fined. In another embarrassing case in the state of New York, 27 Mercedes Benz dealers were convicted of colluding to fix prices.

Bid Rigging

When colluding to rig bids, competitors agree in advance as to who will win the competitive bid on a contract. Bid rigging may take the form of bid suppression, complementary bidding, bid rotation, or subcontracting. Bid suppression occurs when one or more competitors agree to refrain from bidding. Complementary bidding produces bids that are too high to be accepted or bids that contain unacceptable terms. They give the appearance of legitimate bids, and they have the effect of making otherwise unattractively high bids appear reasonable. Bid rotation involves collusive agreement to take turns at being the low bidder, thus passing the winning bid to a predetermined competitor. Subcontracting is a means of rewarding competitors who have agreed to submit losing bids in bid suppression or bid rotation schemes. All bid-rigging schemes have in common a plan that predetermines the bid winner and eliminates competition among the colluding contractors or vendors.

Small businesses as well as large multinational corporations are subject to prosecution for collusive activities. In 1997, the U.S. Justice Department, in concert with the U.S. Department of Agriculture, successfully prosecuted two cattle buyers in Nebraska for bid rigging and mail fraud in connection with the procurement of cattle for a meat packer. The defendants pleaded guilty and were fined and ordered to make restitution to the victims.

According to the U.S. government, a red flag is signaled when the following occur:

- Contracts are repeatedly awarded to bidders from the same company
- Contracts are repeatedly awarded to bidders from the same geographic area
- Alternating high and low bids are received from the same bidder
- Very low or no participation on certain contracts by bidders who normally bid for work in a given area
- Notable subcontracting between an unsuccessful (or nonbidder) and the award-winning bidder

Research economists have developed sophisticated models to assist in the prosecution of collusion. Researchers refer to an asymmetric model of bidding where bidders in a competitive environment expect other bidders to have relative cost structures, both as advantages and disadvantages, to complete the project under bid. Examples might include physical distance to project, available capacity, age of company, and size of company. For bids to be truly competitive, they must meet two conditions. First, the bids must be conditionally independent. This means that the bids are not positively correlated with one another after adjusting for the impact of all publicly available information. Second, the bids must have exchangeability. This means that companies with similar asset bases and cost structures will offer bids in a reasonably narrow range. Conversely, bids not meeting these conditions indicate the possibility of collusion. Stated another way, the researcher sets the research hypothesis—companies bid competitively—seeking to support the hypothesis. When this hypothesis is accepted, there is a high probability that the bids were entered competitively. When rejected, there is a high probability that the bids were entered collusively.

Market Division or Allocation Schemes

Market division or allocation schemes are collusive agreements in which competitors divide markets among themselves segmented by customer type, product type, or geographic region. Competitors agree in advance to restrict their sales, purchases, or bids on contracts to specific market segments. In 2001, the Antitrust Division prosecuted Akzo Nobel Chemicals BV, a Dutch chemical company, for participating in an international price-fixing and market allocation scheme involving chemicals used to produce herbicides in the United States. The company pleaded guilty, agreed to pay a $12 million criminal fine, and the company executive received a prison sentence and fines. In 2002, Elf Atochem S.A., a French chemical conglomerate, pleaded guilty to the same scheme. In 2003, Empire State News Corporation, Inc. of Buffalo, New York, pleaded guilty to allocating markets for the wholesale distribution of magazines, periodicals, and books in western New York and at the Pittsburg International Airport. A criminal fine of $200,000 was levied against the company. Empire's coconspirator, New York Periodical Distributors Inc. of Massena, New York, was fined $500,000 for its role in the market allocation scheme.

Bribery

Bribery is considered a crime against justice. Bribery involves the offering or giving and soliciting or receiving of any item, privilege, or advantage intended to alter the behavior of a public or legal official. The change in behavior is expected to work to the advantage of the briber. Commercial bribery involves soliciting or accepting a benefit in exchange for violating an oath of loyalty such as one owed by an employee, a partner, a trustee, or an attorney. Bribery may be used to induce a purchasing agent to deal with a specific supplier. Bribery can also influence an appraisal of goods or services.

Paying for the privilege to conduct business is as old as business itself. History shows that criminals, often in concert with government officials, use "shake downs" of legitimate businesses, that is, require a payment to allow normal commerce. A *Gallup* Survey of more than 40,000 people taken in 2003 found that corruption or paying of bribes was perceived to be most prevalent in Argentina, Bulgaria, and Bosnia and Herzegovina. The United States, Canada, and Pakistan were rated as the most vigilant in protecting their business systems from bribes.

Paying a bribe is a special type of collusion, given that in many cases there is an attempt to hide the true nature of the transfer of funds through words such as "commissions" or "fees." Making this form of collusion of greater significance is the fact that it is often the only way to do business in some countries. One of the most infamous scandals in the United States involved a Japanese company, Japanese government officials, and Lockheed Corporation, which paid $12.5 million to obtain a sales contract with the Japanese company. The scandal resulted in the famous Treadway Commission Report, which prompted Congress to pass the Foreign Corrupt Practices Act (FCPA) of 1977. The FCPA prohibits businesses in the United States from paying bribes and requires that sufficient internal controls be established such that if an illegal payment is made, it will be detected.

Collusion by Employees

Collusive actions by employees of the same company are the most common form of collusion. Two trends increase the probability of internal collusion: (1) the complexity of business systems and (2) vendor alliances. Increasing business complexity is irreversible and driven primarily by globalism and technology. Vendor alliances draw purchasers and suppliers into tight and often personal relationships where documentation may be limited and the audit trail intermittent. Productivity increases and cost savings may result from these arrangements, but the risk of collusive fraud increases. Estimates vary, but colluders may account for as much as 50% of all internal frauds.

Company control systems are the first line of defense against employee fraud, but these systems are geared toward individuals acting alone. Consequently, internal controls are not generally effective against colluders. Internal collusion occurs when strategically placed company personnel agree to circumvent or override controls to steal company assets. Although the colluders' actions are difficult to detect when authorizing, custodial, recording, and/or reconciling powers are merged, a strictly enforced rotation and vacation policy in conjunction with ongoing data analysis and keen observation by management should ferret out most internal collusive wrongdoing. External collusion occurs when the colluding parties agree to circumvent rules to defraud a third party, such as in bid rigging or price-fixing. Internal/external collusion occurs when a party or parties inside a company conspire with a party or parties outside the company to defraud the first company, such as in kickback schemes or bribes. Common activities include purchasing schemes and payments for the privilege to conduct business.

A variant of the term *collusion* involves cyber crime and is called "collusion attacks." Collusion attacks occur when multiple users conspire to electronically steal and distribute copyrighted or classified material, diluting or erasing the original digital ID, or fingerprinting, from the stolen multimedia content to avoid implication. Fortunately, an antidote, interdisciplinary digital fingerprinting technology, is available to catch these colluding cyberthieves. The method employed not only detects the crime and the culprits but does so without endangering the integrity of the target material or the medium on which it is stored.

Legal Forms of Collusion

Some forms of collusion are exempted or granted antitrust immunity under the U.S. Sherman Act. Some industries have a safe harbor for their activities. For example, the U.S. agricultural industry has an exception to the prohibition against collusive agreements in restrain of competition by way of the Capper-Volstead Act of 1922. This law allows producers of agricultural commodities to form processing and marketing cooperatives because agriculture is a protected industry. The effect of these associations is to allow members of the cooperative to engage in joint selling at a price agreed to by the producer members of the cooperative. Cooperatives are subject to certain limitations enforced by the U.S. Department of Agriculture.

A cartel is a group of formally independent producers who act cooperatively to gain monopoly benefits in fixing prices, restricting supply, and limiting competition. Although cartels are prohibited by antitrust laws in most countries, they continue to exist in national and international commerce because some can escape antitrust enforcement. When an agreement to control prices is sanctioned by a multilateral treaty or protected by a government, no antitrust actions may be taken.

Cartels represent the most overt type of collusion. Two well-known examples are the Organization of the Petroleum Exporting Countries (OPEC) and the De Beers diamond cartel. The DeBeers diamond cartel, once reputed to be the strongest cartel in the world, was forced to abandon its monopoly in the diamond industry in the early 2000s due to increases in the world supply of diamonds.

Prevention and Detection of Collusion

Two competing legal theories test the boundaries of U.S. antitrust provisions. The parallel conduct doctrine requires that evidence demonstrate, similar if not identical, pricing behaviors leading directly to restraint of trade through noncompetitive actions by companies in the same industry. Under this legal theory, the plaintiff does not have to present evidence of an actual conspiracy, that is, meetings, phone calls, expense reports, e-mails, and so on between and among the parties. The competing legal doctrine, referred to as the plus factor, requires evidence of the conspiracy or evidence that excludes the possibility that the colluders acted independently.

An effective method in preventing and detecting internal/external collusion at the individual company level is to monitor gross profit. Gross profit is the difference between the revenue from selling inventory and the cost of the inventory items sold. Significant fluctuations may signal collusion between sales staff and customers. A common technique of this collusion is to undercharge and/or to falsely issue refunds. Other useful methods to prevent and detect collusion include writing company policy regarding fraud;

requiring disclosure of personal and family relationships, both internally and externally; prohibiting acceptance of gifts from vendors; encouraging vendors and clients to notify management of any suspicious or inappropriate employee behavior; and making a tip hotline available.

In the final analysis, collusions are doomed to fail given the natural workings of the competitive market system and the failings of the human beings orchestrating the collusion. Specifically, the collusions are unable to maintain themselves due to falling demand, entrance of new suppliers, exposure to legal liability, and the inclination to cheat by overproducing. Ultimately, colluders become subject to what is called the Prisoner's dilemma; colluding to restrain trade is in the best interest of all members of the collusion but not in the interest of each individual member. Consequently, cheating and internal rivalries eventually cause even the most carefully planned collusive strategies to fail.

—Gary G. Johnson and Eleanor G. Henry

See also Antitrust Laws; Archer Daniels Midland; Auction Market; Cartels; Corruption; Developing Countries, Business Ethics in; Foreign Corrupt Practices Act of 1977 (FCPA); Fraud; Monopolies, Duopolies, and Oligopolies

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Colonialism

Colonialism is the expansion of one people or nation into the territory of another people or nation to establish a material, economic, political, and cultural presence. Archaeological evidence suggests and textual records confirm that human communities have been colonizing territories for millennia. Sometimes, the original intent has been simply to solve a problem of overcrowding or resource shortage through the peaceful establishment of new settlements with ties to the original community. At other times, the intent has been to establish commercial networks that foster the welfare of both the original and the colonial communities. Frequently, however, the colonial enterprise has been accompanied by military force with the primary purpose of extracting value from the colony to increase wealth, freedom, and power for the ruling class of the colonizers. From the ancient regimes of Mesopotamia, Egypt, China, and Rome to the more recent European colonization of Africa, the Asia Pacific, and the Americas, economic, political, and cultural domination has characterized the colonial experience. It is this form of colonialism, along with the beliefs used to legitimize its practice, that has come under intense moral scrutiny in recent years in a critical reexamination of the past 500 years of European/Western history.

Colonialism as a Social Issue

The seminal modern critical work in colonialism, published by Jean Paul Sartre in 1964, framed discursive parameters of colonialism, neocolonialism, postcolonialism, and postmodernism, generating a robust exploration of European colonialism, influencing Jean-François Lyotard, Frantz Fanon, Pierre Bourdieu, and Jacques Derrida. In his advocacy of violence as an instrument of political goals of freedom, Sartre's work was a touchstone not only for the dissolution of the French colonial empire but also for colonialism itself as a legitimate social concept. Theorists such as Homi

Bhabha, Mikhael Bakhtin, Anne McClintock, Edward Said, Ella Shohat, Gayatri Spivak, Sara Suleri, and others have examined the colonial and postcolonial experience from diverse critical perspectives, giving rise to an interdisciplinary field of colonial/postcolonial scholarship that casts new light on history as well as on the legacy of colonialism embedded in the contemporary global political economy of nation-states and multinational corporations perpetuating structural disparities of wealth, freedom, and power among the world's human communities. The legitimate exercise of power by wealthy, Western nations remains a moral challenge as long as the residual effects of colonialism are experienced by smaller, poorer nations whose interests are not as effectively positioned on the world stage.

Ancient Origins of Colonialism

The antecedents of European colonialism are evident in the classical cultures of the ancient Mediterranean. The linguistic roots of colonialism reflect centuries of practice among early peoples who established settlements, trading networks, and colonies along the Mediterranean coastal areas. The English term *colony*, drawn from the Latin *colonia,* refers to a town or settlement, landed estate, farm, or dwelling. The German city of Cologne bears permanent witness to its origins as a Roman colony established during Julius Caesar's campaign against the Gauls. The semantic field of *colonia* (colony), *colona* (country woman), and *colonus* (farmer) suggests a connection to the land and agriculture. The Romans built their empire by establishing colonies, following the earlier practice of Phoenicians and Greeks, who established colonies throughout the Mediterranean, Aegean, and Black Sea before the end of the second millennium BCE. Rome traces its own mythic history to descendants of the defeated Trojans, and much of the Italian peninsula was settled by Greek colonists in the early first millennium BCE. The Greek term for *colony*, αποικια, linked to the Greek word for household, οικος, suggests a strong original connection to the household and the family. Major ancient cities such as Tunis, Carthage, Syracuse, and Marseille were established as colonies. Greek colonies were typically established as independent city-states, although some of them, such as Syracuse, maintained active economic, cultural, and social ties with their parent cities.

It could be said that Europeans learned colonialism from the Romans. By the first century CE, Rome had colonized vast territories stretching from North Africa to Asia Minor and Britain where Roman styles in language, customs, education, and manners were quickly adopted. Colonial outposts at Trier, Paris, Cologne, London, and major European urban centers were incorporated into a provincial administrative system controlled directly from Rome through the appointment of governors and stationing of military troops. Roman territories paid taxes not only to fill the imperial coffers and support distant military campaigns but also to finance their own provincial governor and his troops. Romans welcomed provincials into the army, civil service, and upper echelons of society; by the second century CE, emperors with provincial origins were commonplace, and in 212, all free persons within Roman territories were granted the universal status of Roman citizenship. Many of the tribal kingdoms emerging after the fifth century CE continued structural foundations of Roman beliefs, customs, and administrative systems as well as the Latin language.

A dominant feature of ancient colonization was the belief systems supporting and legitimating domination of what were considered to be "inferior" peoples. The concept of "barbarian" as an uncivilized less than human creature, so evident in Herodotus, was a hallmark of ancient Mediterranean thought. The Romans appropriated Greek canons of philosophy, learning, arts, and sciences, imposing them onto colonized territories in monumental sculpture and architecture, institutions, literature, religious rituals, entertainment, and art, making cities the centers of Roman cultural norms. The trope of "country bumpkin" and the "city slicker" originated in Roman literature as a contrast between the less Romanized rural areas and the sophisticated urban centers. A millennium after the demise of the Roman Empire, the ancient Roman model of colonization was adopted by Europeans in their encounters with Asia, Africa, and the Americas.

Modern European Colonialism

Colonialism was the established vehicle of expansion used by powerful European regimes from the 15th-century Portuguese and Spanish imperial conquests to the 20th-century Cold War superpowers. During the early age of exploration (1410–1700), fiercely competitive European nation-states sought to enhance their positions in relation to each other through the exploration and acquisition of territories beyond Europe. When Pope Alexander VI mediated the dispute between

Spain and Portugal in 1494 by establishing a line of demarcation in the newly discovered American territories, European claims of ownership were not in question. By the time Ferdinand Magellan successfully circumnavigated the earth in 1522, Europeans had come to regard the entire planet as their own. Quickly realizing the potential value of Africa, Asia, the Pacific, and Americas, Europeans joined in the competitive search to capture the wealth of earth's natural resources through establishment of mercantile enterprises and control of trade routes (1700–1815). Established by Estates-General of the Netherlands in 1602 as the first national joint stock company for international mercantile enterprise, the Dutch East India Company was a dominant global commercial force for nearly two centuries until it was dissolved in 1798 after declaring bankruptcy. The formation of stockholding corporations of shared risk and reward revolutionized global commerce, generating unprecedented pools of capital to fund continuing cycles of enterprise. The British East India Company, Dutch and British West India Companies, the Hudson Bay Company, and other joint venture trading companies were formed to capitalize commercial colonization throughout the world.

By the early19th century, France, England, and Spain had lost possession of American colonial territories and popular sentiment in Europe was turning against slave trade. Spurred by new opportunities for investment, market development, and wealth creation, Europeans turned to Africa, Asia, and the Pacific. The success of global market development in creating wealth for European nations and private investors gave rise to a new form of economic imperialism (1870–1914) by which indigenous local economies were dismantled and replaced with local markets designed to meet the needs of colonial home economies.

The Berlin Conference (1884–1885) on the partitioning of Africa exemplifies the imperialistic worldview of European colonialism. At the time, European colonies were concentrated around coastal areas representing about 20% of the continent. The rest of Africa included more than 1,000 indigenous cultures with traditional languages, social and economic networks, and governing structures. In response to a request from Portugal, German chancellor Bismarck convened major Western powers (Austria-Hungary, Belgium, Denmark, France, Germany, Great Britain, Italy, the Netherlands, Portugal, Russia, Sweden-Norway, Turkey, and the United States) to negotiate control of Africa. France, Germany, Great Britain, and Portugal were the major powers in Africa and exerted the most control in the partition of Africa. The result was 50 gerrymandered nations constructed to serve the interests of colonial powers without regard for established indigenous ethnic, linguistic, or cultural affinities.

By the dawn of the 20th century, Eurocentrism was literally mapped onto the world and Europeans had colonized major portions of its land masses. Australia was totally colonized; more than 90% of territories in Polynesia, Africa, and Asia were 56% colonized; almost a third of the Americas was colonized. World markets built by Europeans with colonial labor and raw materials filled newly wealthy households and cities with everything from exotic luxury goods to daily staples of tea, coffee, and wicker baskets. Because colonies were appropriated, usually by force, they required the constant supervision and military presence of resident European authorities to assure cooperation and compliance. A divisive class structure emerged to reward Europeanized indigenous people with status and privileges unavailable to those who clung to traditional language, dress, and customs and alienating generations of people from their own cultural roots and identities.

The European colonial enterprise was almost entirely one of domination and exploitation. A few individual colonies, such as the United States, were successful in resisting colonial domination early on, but the value and legitimacy of colonialism remained firmly entrenched in the Western political lexicon well into the 20th century. The moral case for colonialism became increasingly difficult to defend, however, as social contract and human rights theories found their way into the political understanding of colonizing European nations. Even in the independent United States of America, however, the champions of independence were themselves transplanted Europeans who applied the values of human rights articulated in the Constitution and Bill of Rights to themselves but not to Native Americans or enslaved African Americans.

The Historical Defense of Colonialism

Advocates of colonialism have argued that colonial rule benefited the colonized by developing the economic and political infrastructure necessary for modernization and democracy, pointing to former colonies of the United States, Canada, Australia, New Zealand, Hong Kong, and Singapore as models of successful postcolonial sovereignty. Most colonies of the modern era were founded for the benefit of the colonizing power, although benefits were thought to accrue as well to the colonized peoples as they developed modern, Western ways. Jules Ferry's 1884 address to the French Chamber of Deputies represents the typical colonial viewpoint of his time, which was that French colonial policy was inspired by the need for safe harbors, defenses, and supply centers such as those found in Tunisia, Saigon, Indochina, and Madagascar. He stated that France would never leave these territories. Contemporary defenders of colonialism point to the benefits of modern technology that centuries of globalized enterprise and wealth generation have made possible: vaccines, air travel, air conditioning, synthetic fabrics, electronics, hybridized food production—a cornucopia of products and services that few citizens of former colonies would choose to live without.

The Critique of Colonialism

Sartre's critique of colonialism galvanized growing anticolonial public sentiment among Europeans following centuries of colonial domination. Dependency theorists, such as Andre, Gunder, and Frank, argue that colonialism actually leads to a net transfer of wealth from the colonized to the colonizer and inhibits successful economic development. Postcolonial critics Frantz and Fanon argue that colonialism does political, psychological, and moral damage to the colonizer as well. Indian writer and political activist Arundhati Roy observes that debating the pros and cons of colonialism/imperialism is comparable to debating the pros and cons of rape. Although many former colonies have become independent nations and some, such as India, have retained strong cultural traditions and built competitive market economies, colonialism continues as a topic of active debate in world affairs. For example, the current military actions in Afghanistan and Iraq are seen by some critics as the perpetuation of a colonial worldview in which some nations, such as the United States, assert their right to infringe on the sovereignty of other nations in the service of their own economic and political interests.

—Lindsay J. Thompson

See also Cultural Imperialism; Ethical Imperialism

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COMMENSURABILITY

Commensurability (or *commensurableness*) is an abstract noun, the adjectival form of which is *commensurable*, and apart from being easier to pronounce, it is easier to define. In defining a concept, the essence or the qualities of the concept are described, that is, saying what makes it what it is and not something else. To say that some things are commensurable is another way of saying that they are capable of being measured by the same standard of values or that they have a common measure.

The meaning of commensurability may be illustrated by showing how the word is used in everyday speech; for example, concepts such as equity and justice and matter and gravity are commensurable because they can be measured by the same set of values. Mind and space are incommensurable because they are not capable of being measured by a common standard. Justice and economic development are incommensurable because there is no common measure to evaluate them.

Commensurability has mathematical connotations, as shown in the following examples. (1) The numbers 12 and 9 are commensurable because they are divisible by 3. (2) A foot and a yard are commensurable because they are capable of being measured by the same unit; that is, they can be translated into inches—namely, 12 inches and 36 inches, respectively. (3) Hours and minutes are also commensurable because they too share a common measure.

With respect to recent research, Thomas Kuhn (1922–1996) and Paul Feyerabend (1924–1994) have both considered *commensurability* and *incommensurability.* Feyerabend (whose career included service in the German Wehrmacht as an officer and then being wounded on the Russian front) argued that the semantic principles of construction underpinning a theory could be replaced by another theory. As a result, theories could not always be compared with their context. Kuhn claimed that science developed in one particular paradigm or in a different era would be incommensurable with science produced in another; that is, there would be no equitable way of comparing them. He identified three kinds of incommensurability: (1) methodological incommensurability, (2) perceptual and observational incommensurability, and (3) semantic incommensurability.

To illustrate the meaning of *commensurability* within a business context, we could ask whether *the value of profits* was commensurable with *the value of distributive justice.* In the example, there seems to be little commensurability between the value of profits and justice (whether it be distributive, interactional, procedural, retributive, or social).

—*Michael W. Small*

See also Justice, Distributive; Justice, Theories of

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Commerce and the Arts

Today, the arts are a multibillion-dollar industry. Commerce plays a key role in producing or coordinating the physical and financial resources needed for the production of artistic works and for their dissemination to consumers. Nevertheless, the relationship between commerce and the arts can be tense, with the profit motive of commerce at times conflicting with the social, humanistic, and political motives of artists.

Definition: The Arts

Traditionally, the arts include the musical arts (e.g., piano music, symphonies), the literary arts (poetry, novels), the dramatic arts (plays), the musicodramatic arts (opera, ballet), and the visual arts (painting, sculpture, drawing), to which modern times have added, for example, cinema, still photography, and computer graphics. A characteristic of the 20th century was a conscious exploration of the distinction between "arts" and "nonarts," with a consequent blurring of the distinction. As such, it is virtually impossible to find a satisfactory definition of "the arts." Nor is the distinction between "high art" and "popular art" useful. Historically, the distinction was primarily economic but modern forms of reproduction are removing that distinction: the operas of Wagner are now available on DVD; the paintings of Titian are now available as framed prints. Key to the distinction between art and nonart is authorial intention: Did the creator intend the work to be a work of art?

The Purpose of the Arts

The arts have many purposes, of which four may be singled out; however, the reverse is not also true: Just because something fills one of these purposes does not mean that it is a work of art. First, at the most superficial level, the arts entertain and allow for shows of wealth and affluence: But soccer also does this, and like soccer, such arts tend to be commercially viable.

Second, the arts provide social cohesion. Especially in traditional societies, the arts play a key role in national or ethnic identity: They help distinguish Germans from Nigerians, Canadians from Brazilians, and so it is not surprising that government, where it has the funds to do so, usually plays a strong role in supporting such arts. But national costumes and customs also do this. The arts also play a role in other types of social cohesion, such as religion; for example, Martin Luther understood the importance of communal singing in congregational bonding, and so music played a central role in the development of the Reformation church. However, soccer also provides social cohesion in some societies.

Third, the arts give insight into our humanity by getting us to see the world in a different way; for example, a novel or movie from another culture may invite us to place ourselves in the shoes of the principal character.

Finally, the arts give a voice to the politically oppressed and the dispossessed and are a key vehicle for social change. In South Africa, black musicians played a key role in the battle against apartheid. The sexually explicit photographs of Robert Mapplethorpe challenged our views on the human body and the line between art and pornography. Mart Crowley's 1968 play *The Boys in the Band* or the 2005 movie *Brokeback Mountain* challenged entrenched attitudes about homosexuality. The dance group K-PAG Mix, a member of the Kenya Performing Arts Group, has some members who have physical disabilities and some who do not; their dance piece *Crossing* forces the audience to confront their attitudes about disability and people with disabilities. Each of these examples has, at its core, an ethical component: political oppression and racism, censorship, homophobia, and disability discrimination. By its very nature, some art that challenges will be regarded by the majority within a society as unethical if it conflicts with their norms and beliefs and values; but the examination of why the majority believes it to be unethical fulfills its role as art regardless of whether or not it actually leads to social or political change.

Art that challenges is often not commercially successful at the time that it was created. As time passes, however, it generally becomes more and more conventional and ceases to challenge. There were riots at the premiere of Igor Stravinsky's *The Rite of Spring*, and D. H. Lawrence's *Lady Chatterley's Lover* was banned as obscene; both are now regarded by the mainstream as classics and both are commercial successes.

Types of Commercial Involvement in the Arts

There has been a long history of commercial transactions between creative or performing artists and consumers of their product; for most of this time, the consumer has driven the commercial relationship, be it a painter painting a portrait or a musician writing a string quartet for a patron. The way that the relationship has changed, especially in the 20th century, has been the intermediation of business between the artist and the consumer as a third party. Commerce is generally involved in the arts in one of two ways: either directly, where a commercially viable artistic product or service is offered by the business as a product (such as a CD) or a service (such as an artist's agent), or indirectly, for noncommercially viable arts (such as art galleries or major opera companies), through sponsorship or philanthropy.

The types of corporate form used in the arts relate to the extent of the resources that need to be coordinated. Most creative artists, be they writers, musicians, or painters, are entrepreneurs running their own microbusinesses; apart from their talent and time, the resources required for the creation of works of art tend to be minimal, although there are notable exceptions such as the works of Christo. The role of larger organizations is usually not with the creation of art but with its distribution, which requires much larger resources: publishing and recording companies (although the Internet is reducing the capital necessary for undertaking such activities) or companies that arrange large-scale performances (such as major orchestral or operatic presentations or international tours of popular bands). In cinema, although the resources involved in creation are substantial, "art" movies generally require far fewer than "mass entertainment" movies.

Commerce is also involved in the manufacture of resources used by artists, such as musical instruments or artists' paints, and the building and hiring of venues such as playhouses. The price of resources has historically decreased, and in many cases, the quality of those resources has increased, owing to competition between commercial providers of those resources. A clear example of this is the piano. Piano manufacturers have, since the 18th century, made profound technical developments in design and construction, such as the introduction of iron frames, which allow for much greater string tension and, hence, power, and composers and performers responded by exploiting these innovations. The price decreases associated with mass production saw the piano become essential in Western middle-class homes by the end of the 19th century and so opened up the playing of the piano to an unprecedented number of people, which also benefited the music publishing industry and provided increased royalties to composers. The availability of appropriate commercial venues was essential for the rise of the public concert in the 19th century.

The Role of Commerce in the Arts: The Artist

All artists have basic economic needs: At the very minimum, they need housing, food, and the materials with which to create their art. Commerce allows them to benefit financially from their creations and for some brings financial independence. The diversity of contemporary commerce gives artists unprecedented opportunities to fund their work; this funding allows them greater freedom and so enables an ever richer and diverse body of artistic creation. Many artists are entrepreneurs, fulfilling market needs and growing businesses. Rembrandt ran a very successful workshop and, much like an owner-manager, drummed up business for his workshop, personally attending to the most important painting tasks and leaving the lesser tasks to others in his workshop. Commerce allows much wider distribution of artistic creation than was previously possible; recording companies may sell millions of copies of a work, providing significant royalty payments to the artists. Some artists, especially those driven by a desire for social change, are more interested in influence than profit; however, high levels of profit indicate that their message is being spread (but this does not necessarily mean accepted), and they may devote their earnings to pursuing social causes. Despite this, many artists remain among society's lowest income earners.

The Role of Commerce in the Arts: The Consumer

The ever-increasing market for the arts, resulting from economic development, benefits both artists and businesses. The consumer of art will ultimately determine whether or not the artistic product is commercially viable; this is unrelated to whether or not it is great art. Commerce doesn't just supply consumers with the artistic products that they want: It drives that demand through marketing, and so business determines which artistic works will be most widely available, most financially successful, and, importantly, in many cases, most influential. Businesses may distribute works that are clearly unethical, such as those of some rap artists that encourage violence and discrimination, while not distributing works that challenge racism and homophobia. Commerce sits more comfortably with the aims of the arts to entertain and to provide social cohesion, but less so with their humanistic and political aims: People generally are more likely to pay to be entertained than pay to be challenged (as is suggested by the relative box office receipts of *Jaws* and *Another Country*). Here, we see a fundamental clash in values between commerce, which seeks to maximize profit, and the arts, which generally have very different aims.

Protecting Commerce in the Arts: Copyright

Copyright plays an essential role in the relationship between commerce and the arts by securing economic benefits of artistic production. There are two principal international copyright conventions, the Berne Union for the Protection of Literary and Artistic Property and the Universal Copyright Convention; there are also copyright laws enacted by individual nations. Copyright allows its holders to reap *some* of the economic rewards from their labors: If you "create" a house, the economic benefits from that house remain yours to control indefinitely, but if you "create" a song, you have time-limited intellectual property rights. At the beginning of the 21st century, the most prominent ethical issue is piracy, that is, the theft of the intellectual property created by artists; it appears that the average person does not take this sort of theft as seriously as the theft of physical property (e.g., some people illegally download music but would never steal from a supermarket).

The Role of Government in the Arts

Government's role in the arts may be divided into two principal areas. First, government enacts legislation that provides the commercial framework within which the arts operate (such as corporations legislation and tax law); the minimum ethical criteria that all citizens, including artists, must abide by or risk legal sanction (such as legislation on public morality or defamation); and arts-specific legislation, such as that controlling specific arts organizations. Second, government subsidizes especially noncommercially viable arts as part of its social role, such as through the U.S. National Endowment for the Arts. Organizations such as national art galleries invariably require subsidy that, if not from the private sector, can only come from government.

Whether government should be involved in the arts, and especially in the funding of the arts, is an area of contention. Reasons for its interest may be divided into three main areas: sociocultural, political, and economic. First, the arts help define national identity and help provide social cohesion; these are of great interest to government because, among other things, they help provide political stability. New art provides an important impetus for challenging who we are and where we as a society should go, which enables social progress; historical works remind us of where we came from, which is essential given the path dependency of history (i.e., how we have arrived at where we are will constrain our options for going forward).

Second, that the arts are a powerful political tool is clear from the control that nondemocratic governments, such as Nazi Germany or Stalinist Russia, exercised over the arts. Government, for better or worse, is always interested in political tools. The arts can only fulfill their humanistic and political roles where government does not exert undue influence on the arts, such as by imprisoning artists whose work is politically activist. In democratic societies, political impartiality in funding of the arts—especially arts that have a social or political message—has become a major issue.

Third, the arts have a significant impact on the economy. The Australia Council has over many years commissioned numerous reports on the economic impact of the arts on the Australian economy; these reports have shown that government support for the arts has had a positive economic impact.

Despite all this, over the past decade, there has been internationally an increasing shift in arts funding from the government to the private sector, principally driven not only by government funding cuts but also by changes to law on tax deductibility of support for the arts as happened in France in 2003.

Criticisms of Commerce in the Arts

Artistic autonomy, which may be viewed much like academic freedom, is viewed by many as fundamental to the role of the arts and, in particular, the artist's ability to freely challenge established views. Commerce is often believed to undermine artistic autonomy. Professional artists need income to live and that income is often provided by commercial transactions involving sale of their output. Commerce seeks and rewards output that maximizes profit and generally does not support output that is not commercially viable; as such, artists may be pressured to survive, to produce not what they want but what commerce believes to be most profitable, regardless of whether or not the artist is interested in maximizing profit. Attempts to undermine artistic autonomy by treating the artist solely as a means, not an end, violate the second formulation of Kant's categorical imperative. Nevertheless, it is the artist's choice to become involved with commerce. Although commerce may encourage certain types of artistic production, it cannot *prevent* certain types of artistic production (excluding cases where autonomous individuals have bound themselves contractually). However, J. S. Bach's massive output was driven by commercial considerations: As Kantor at St. Thomas's, Leipzig, he had to produce cantatas for Sunday services and passions for Good Friday; could Bach, if it were not for his employment obligations, have produced a series of operas to match or even surpass those of Handel? Commerce may have given him the freedom to do so.

Many people look to the masterworks of the past, compare them with works from the present, conclude that there has been a decline in artistic quality, and blame this on the commercialization of the arts. However, history has effectively filtered out almost all past artistic creation, and only the very best works have survived. More than 10,000 18th-century symphonies survive (and many more may be assumed to have been written), but of these only a handful are known to modern audiences; a majority of Mozart's symphonies are little more than curiosities. The masterworks in this repertoire may be viewed as statistical outliers. Of the vast amount of artistic creation in the present, history has not had time to select the few canonical works.

The argument that financial motives are at variance with great art—that the artist cannot "produce on request" like a machine but is a genius inspired by the muse—is, at least in the West, a 19th-century one imbued with the spirit of romanticism; in music, it is first seen in the works of Beethoven and Schubert. Before that, artists generally saw themselves as artisans, paid to do a job, and that their talent was for God's glory, not their own fame—examples include Josquin, Palestrina, and Bach. Mozart's letters show a great interest in money. Apart from those holding university posts, most freelance composers today rely heavily on commissions for financial survival and have to produce the required work on time and on budget.

A serious criticism, however, relates to the corruption of cultural identity. For example, Australian aboriginal art has become commercially viable owing to international interest. Indeed, in many developing countries, the market for traditional art is driven by tourists who do not understand the significance of the art, but simply appreciate its beauty or "otherness." Commercial interest has led to significant stylistic issues: Consumers of aboriginal art prefer styles particular to certain tribes, and so other tribes whose traditional styles are not desired by consumers have taken to copying the more desired styles. This undermines the copier's sense of tribal heritage. The *didjeridu*, a musical instrument, is indigenous only to northern Australia, but owing to its successful commercialization has become the iconic aboriginal instrument and is now played by aboriginal musicians from all parts of Australia, sometimes replacing their traditional instruments.

Despite the criticisms leveled at commerce's involvement in the arts, it is clear that artists, consumers of artistic output, and the arts themselves have, overall, benefited from the involvement of commerce and that commerce has benefited from its involvement in the arts.

—Royston Gustavson

See also Corporate Social Responsibility (CSR) and Corporate Social Performance (CSP); Humanities and Business Ethics; Nonprofit Organizations; Property and Property Rights

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Commodification

Commodification is the social process of rendering something capable of being bought or sold in a market. While the term *commodification* became current only in the 1970s, the idea of commodification and the moral controversies surrounding that idea have a long history, centering on the question of what, if anything, should be commodified. Immanuel Kant, for example, in the *Foundations of the Metaphysics of Morals*, drew a sharp distinction between things that have a price and things that have a dignity. Since persons, being ends in themselves, have a dignity, it was Kant's view that they should not be commodified (i.e., enslaved), although Kant did not object to commodifying their labor. Karl Marx, in the *Communist Manifesto*, objected to any form of commodification, railing that the capitalist bourgeoisie has reduced personal worth and family relations into monetary value. It was Marx's view that the expansion of capitalism was commodifying an ever greater range of human relations that should not be commodified. Marx believed, in fact, that it was wrong to commodify even a person's labor, arguing that commodification produced alienation. Through commodification things are seen as separate from the self and come to be treated as if they have a value and life of their own, a process that Marx called commodity fetishism. Other 19th-century thinkers, such as Thomas Carlyle and John Ruskin, as well as 20th-century thinkers sympathetic to Marx, such as Jean-François Lyotard and Georg Lukacs, have continued to protest commodification. Marx's followers, in particular, have argued that capitalism has continued to expand commodification into ever-widening areas of human life and thought until virtually everything has a price tag.

A great deal of contemporary discussion has centered on whether particular types of things or relationships should be commodified, including children, human organs, blood, semen, ova, sexual services, genes, fetal parts, surrogate motherhood, and intellectual property such as basic scientific discoveries, essential drug formulas, and critical software. At one extreme lie libertarians such as the legal theorist Richard Posner, who see nothing wrong with commodifying virtually everything. At the other extreme lie those such as Karl Marx and many of his followers, who object to any kind of commodification, arguing that market relations should not replace any human relations. Somewhere in the middle lie those who object to the commodification of some things but not of others.

Those who argue in favor of leaving people free to commodify anything they choose generally do so on the grounds that people have a right to liberty and this right implies that people should be left free to engage in whatever market exchanges they choose; or it is argued that the opportunity to buy and sell anything in markets improves people's welfare since markets are not only liberating but can also harness society's resources with the utmost efficiency. Richard Posner, for example, argued in a 1978 article that people would be better-off if parents were allowed to exchange their children for money (i.e., by letting buyers adopt them). A standard criticism of such "universal commodification" is the claim that because many important human goods are incommensurable with each other, there can be no common measure or scale in terms of which every given good can be said to have more or less value than any other good (incommensurability is also a standard objection to utilitarianism, which assumes that there is such a scale and which often underpins the arguments of supporters of commodification). In particular, it is argued, monetary value does not provide a scale for measuring the value of, for example, human life, intense suffering, or the loss of a loved one.

Those who claim that only certain things should not be commodified generally argue on the grounds that commodifying those things in some way dehumanizes persons, treating them, as Kant would have said, as means and not as ends, or as things and not as persons. For Kant, and later for Hegel, the dividing line between what can be commodified and what should not be commodified is the line between what is part of the person and what is external by nature to the person. Thus, Hegel approved of the commodification of labor because labor was external to the person, but he condemned slavery on the grounds that slavery commodified the person. More recently, others have argued against commodifying certain things—such as body parts or sexual services—on the grounds that the desperately poor would be forced into selling such things to their detriment. Finally, those who argue that nothing should be commodified—not even labor—have generally taken a Marxist line, claiming that commodification of any sort is alienating.

It is important to distinguish between what Margaret Radin has termed rhetorical commodification and real commodification. In rhetorical commodification, something is rendered capable of being bought or sold in a market but is so rendered only in thought or in discourse; in real commodification, it is so rendered in reality. When one speaks of sexual interactions in marriage, for example, as "exchanges" in which one party "sells" a sexual "service" in exchange for "financial support" from another, we have an example of rhetorical commodification. However, when a prostitute actually sells her sexual services to a client in exchange for money, we have a case of real commodification. Among economists, Gary Becker and his followers have long argued that virtually all human interactions fruitfully can be understood as "trades" or "sales" of goods that have a "price." While it may seem to many that rhetorical commodification is harmless, others, such as Margaret Radin, have argued that rhetorical commodification can change the way we think of those things that are rhetorically commodified and such changes may be injurious. For example, if persons are rhetorically commodified this can undermine the Kantian conception of the person, by leading us to think of ourselves and others as means or things, and not as ends or persons, and this, she claims, would be deleterious.

A second important distinction, also drawn by Margaret Radin, is the distinction between full and partial commodification, on the one hand, and complete and incomplete commodification on the other. The distinction between full and partial commodification of a thing is the distinction between a situation in which some, but not all, exchanges of a thing are commodified, and a situation in which all or virtually all exchanges of that thing are commodified. For example, while some blood is given freely by donors in noncommodified exchanges, others sell their blood for money and such exchanges are commodified. Blood is, thus, only partially and not fully commodified. On the other hand, because virtually all automobiles are exchanged for money they are fully commodified. Critics of commodification have argued that partial commodification is an unstable situation because partial commodification of a thing tends to devolve along a slippery slope into its full commodification and such full commodification can be bad. Richard Titmuss, for example, argued in *The Gift Relationship* that once blood was partially commodified, it would eventually become fully commodified, and this was bad because it would render communities less altruistic and less unified. Several Marxists have likewise argued or assumed that partial commodification always gives way to full commodification.

The distinction between complete and incomplete commodification of a thing is the distinction between a situation in which that thing can be bought and sold in markets without restriction and a situation in which the thing can be bought and sold but only under certain restricting regulations. For example, tables and chairs are virtually completely commodified since they can be bought and sold with no restrictions on their sale. Labor, however, is incompletely commodified because it is subject to numerous legal restrictions including age laws, minimum wage laws, antidiscrimination laws, and a multiplicity of other labor laws. Margaret Radin has suggested that instead of trying to decide whether to choose between fully commodifying a thing and not commodifying it at all, it is more useful to think in terms of choosing between complete and incomplete commodification. That is, when discussing the desirability of commodifying contested goods such as sexual services, surrogate motherhood, babies, human organs, and so on, it is more useful to think about the regulatory restrictions we would want to impose on the commodification of these goods than to debate the choice between full commodification or full noncommodification of these goods.

—Manuel Velasquez

See also Commensurability; Compensatory Damages; Cost-Benefit Analysis; Marx, Karl

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Commodity Futures Trading Commission

The Commodity Futures Trading Commission (CFTC) is an agency of the federal government charged with regulating commodity and financial futures and options contracts and markets. The CFTC serves three key functions. Its first mission is to protect market users and the public from fraud, manipulation, and abusive practices related to the sale of these instruments. Second, the CFTC regulates financial practices in the market to ensure that the entire market remains financially sound and that the markets continue to function with financial integrity. Third, the CFTC uses its regulatory powers to help the markets fulfill their key social functions of providing a means for price discovery and the hedging of price risk.

Organized commodity futures markets arose in the United States about 1850 with the establishment of the Chicago Board of Trade and the Chicago Mercantile Exchange, still two of the largest futures exchanges in the world. At their outset, these markets traded futures based exclusively on agricultural commodities such as corn and wheat. These markets first came under federal regulation in the 1920s, and Congress charged the CFTC with the regulation of these markets in 1974.

Since the 1970s, futures and options markets have expanded in size and scope, with trading of futures and options on many nonagricultural commodities. These now include oil, gold, and financial instruments, such as foreign currencies, stock indexes, and Treasury debt instruments. The markets regulated by the CFTC are of huge financial size and importance, with many billions of dollars being traded in these markets annually. The instruments traded in these markets are complex, as are the markets themselves. In addition, the markets are important to the financial system and the economy in general.

Futures and options markets serve two main social functions. First, the markets aid in the process of price discovery, the discernment and communication of information about the future direction of prices for commodities and other goods. The markets serve this function because futures prices prove to be among the best predictors of actual future cash prices for the underlying goods, such as oil, grains, interest rates, and foreign currency values. Thus, transactions in these markets generate observable prices, and the prices reported have a valuable social role because of the information they provide. Second, through a process known as hedging, futures and options prove to be extremely powerful instruments for managing and reducing commercial risks that arise in the ordinary conduct of business. In the classic example of a hedge, a farmer reduces uncertainty about the price to be received for a future harvest by trading in the futures market to establish a certain future sale price for the crop. The same kind of risk-reducing strategy works for financial futures and options to reduce financial risk and uncertainty.

—*Robert W. Kolb*

See also Finance, Ethics of; Financial Derivatives; Manipulation, Financial

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Common Law

The common law is the body of legal rules created over time by judges as they issue written opinions resolving individual lawsuits. The opinions serve as precedents to guide the resolution of future similar cases. The common law is to be contrasted with positive law, which consists of statutes passed by legislatures.

The principal subject areas of the common law are contracts, property, and torts. Common law originated as customary rules of social conduct that came to be enforced in the English courts. It also applied in the British colonies and was adopted by the fledgling United States, whose courts adapted it as necessary to suit the American experience.

The common law has three distinctive features that define it and set it apart from positive law. First, it is not a written code. There is no single source, such as a statute book, that codifies the principles that apply to a given case.

Second, common law develops through the resolution of actual legal controversies, primarily at the appellate level. The judge's opinion typically sets forth the facts and the applicable legal principles and resolves the case by applying the principles to the facts.

Third, the common law develops through the accumulation of these opinions, or precedents, as they are applied to similar cases in the future. The doctrine of precedent is based on the principle of *stare decisis* (to stand by a decision), which binds courts to follow prior judicial decisions unless circumstances (e.g., a change in societal norms) compel a reexamination or overturning of a prior case. The doctrine is intended to ensure that the same legal principles apply to all similarly situated parties. It also establishes the rule of law: Basing decisions on precedent ensures that society is governed by established rules rather than the personal views of each judge.

Contracts

A contract is an agreement between two or more parties. Contracts usually consist of an exchange of promises of future performance; for example, one party promises to paint the other party's house, while the other party promises to pay a certain sum on completion.

The essence of contract is free exchange—each party freely decides what to promise and what to demand in return. Freedom of contract promotes mutually beneficial exchanges by willing parties. In interpreting ambiguous contract terms, courts attempt to determine the intent of the parties to carry out their will.

The question at the heart of contract law is, "Why does society enforce promises?" According to libertarians, the key is free choice: The purpose of the state is to secure individual liberty, and contracts embody the free choice of the parties. Others answer that contract is a form of economic exchange in a free market. Because contracts are free exchanges, each party to a contract believes it has benefited by the exchange—has gotten more than it has given—and, therefore, contracts increase the sum of society's wealth. Indeed, because the enforcement of contracts makes free exchange and, hence, business transactions possible, it is one of the law's most important functions.

Still others believe that society enforces contracts not to promote exchanges but to compensate the injured party in the event of breach. Because a promise induces reliance, a party must be made whole when he or she relies on a promise to his or her detriment. This rationale shifts the focus of contract law from the will of the parties to a notion more like that of tort: The focus is on fairness to the injured party rather than enforcement of a free exchange.

In an influential work, Charles Fried argued that the promise principle is the moral basis of contract law. A person makes a promise to induce the promisee to rely on it, thereby invoking the societal convention under which promises are binding. The utilitarian argues that the ability to rely on promises increases social utility by increasing free exchange. Fried, however, takes a Kantian approach; he asserts that respect for the other party to the contract demands that we fulfill the expectations our promise has created.

Property

Property law defines people's rights to society's wealth. Property rights recognized and enforced by the common law include, among others, the right to possession of property and to its use and income, the right to alienate (transfer), and the right to prevent interference by others. Historically, this last purpose was the essence of property rights, as the law barred almost all interference with enjoyment of property. Thus, for example, the common law disallows trespass to property and developed the concept of "ancient lights," under which one property owner could prevent another from erecting a building that blocked the first owner's view. Some consider property rights the foundation of the common-law system: Property law concerns the ownership of property, contract law the transfer of property, and tort law harm to property (as well as person).

Many believe that private property rights are the basis of a free society. Others champion the instrumental value of private property: Utilitarians believe the law must protect the use and enjoyment of property because social peace and stability depend on security in one's possessions. Still others argue that private property is essential to economic growth; as the common law developed, property rights expanded to include not only the right to use and enjoy property free from interference but also the right to develop it. Property came to be viewed as a productive asset, and in some cases, the law even allowed a property owner to inflict harm, such as by polluting, if the societal benefits of the productive use outweighed the social costs.

Torts

A tort is a civil wrong, other than breach of contract, for which the law will award damages. The law of torts protects a wide variety of interests, including interests in person, property, and reputation. For example, it provides redress for battery (touching or striking another person without the person's consent) and intentional infliction of emotional distress, which protect the person; trespass and conversion (theft), which protect interests in property; libel and slander, which protect reputation; and wrongful interference with business relations (such as inducing another to breach a contract with a business), which protects business interests.

The three bases of liability under tort are intent, negligence, and strict liability. One is guilty of an intentional tort if he or she intentionally inflicts injury on another. One is liable for negligence if he or she fails to act as a reasonable person would in the circumstances and unintentionally injures another. Strict liability imposes liability without fault. Originally, strict liability applied only when a party engaged in an unreasonably dangerous activity, such as blasting. Today, it applies primarily in cases of product liability, when a consumer is harmed by a defective product.

The question at the heart of tort law is why to impose liability on one individual for harm done to another. Reasons for imposing liability have been the subject of much debate. Some argue that the purpose of tort law is retribution: A wrongdoer must be made to pay for his or her actions. This purpose is most clearly reflected in the law of intentional torts, which punishes morally wrong conduct.

However, neither strict liability nor negligence is premised on moral wrongdoing. Because negligence liability is based on the reasonable person standard, a party may be held liable for negligence even if he or she was personally incapable of avoiding the harm. Therefore, some assert that the purpose of tort law is compensation. These observers also note that a theory of retribution does not explain why tort damages are paid to the injured party rather than to a third party such as a state fund.

Still others suggest that the purpose of tort law is deterrence: Punishing conduct of which society disapproves discourages others from engaging in it. It is unclear, however, how a theory of deterrence justifies liability for negligence, in which harm is unintentional.

Though not based on moral wrong, negligence at least retains the concept of fault: One party's carelessness has harmed another. Strict liability dispenses with the notion of fault altogether. Manufacturers and distributors of goods are held strictly liable for harm caused by defective products even if they exercised all due care in manufacturing and inspecting their products. Here, tort law imposes liability on the party better able to bear the loss. Manufacturers can spread the costs of injury among all users of their products by including the costs in the price. Liability also may encourage them to develop new manufacturing techniques or designs that can prevent future injuries. Similar justifications support the doctrine of vicarious liability, under which an employer is liable for torts committed by his or her employees during the course of the employer's business.

Finally, law and economics theorists abandon entirely the traditional focus on the individual tortfeasor and victim in favor of a societal view. They assert that a person should be liable for harm caused by another only if the cost of taking measures to avoid the harm would have been less than the damage caused. According to these theorists, this principle will maximize society's wealth, since people will spend money to avoid injury only when the benefits of avoiding injury outweigh the costs. They also argue that the reasonable person standard implicitly embodies this principle and, therefore, that common-law courts have always applied it, even if not explicitly.

Common Law as Science and Policy

Does the theory of the common law hold: Does the doctrine of precedent result in the consistent application of neutral legal principles to decide like cases? Early commentators on the English common law believed that common-law principles were based on natural law. The great English commentator William Blackstone held that natural law was dictated by God, was therefore superior to all earthly law, and that judges applied preexisting natural law rules to decide cases. According to this theory, judges discovered rather than made law; decided cases were not the law itself but merely evidence of the law. If a judge overturned a precedent, he or she was not changing the law but correcting it. Legal principles were universal and unchanging.

Thus, common-law decision making was both divinely sanctioned and scientific. It was an objective process in which the identity of the judge was irrelevant. This theory prevailed until the early 20th century, when the legal realists turned it on its head. They asserted not only that judges made law but also that the law consisted solely of decided cases. If, for example, a court held a defendant liable for an invasion of property rights, that holding did not mean that the trespasser had violated preexisting property rights. Instead, the judge had created the property right by virtue of his holding. Legal realists believed that precedents were indeterminate: A judge could find a precedent to justify any decision he or she wanted to reach in any case. Therefore, rather than discovering legal principles and applying them to cases, judges decided cases by applying their own moral conceptions and then found precedents to support their decisions.

The realists conceived of the common law as an instrument of social policy in which judges balanced competing interests, just as legislatures did. Many found the realist position troubling because it meant that unelected judges made law: Realism rendered the common law undemocratic. It also challenged the basic claim of the system of precedent, its assurance that similar cases were treated similarly.

According to legal realists, however, judicial decisions were not intended simply to resolve individual controversies. Instead, judges must look beyond the case at hand to determine the best social policy. Legal realism reflected a new view of the common law as an instrument of social progress. This view was reflected, for example, in the changing law of torts, under which courts began to socialize the costs of accidents by imposing strict liability on manufacturers and, in negligence actions, to limit the cases in which the plaintiff's negligence barred recovery (by abandoning the doctrine of contributory negligence, under which any negligence by the plaintiff, no matter how slight, defeated recovery, in favor of comparative negligence, under which the plaintiff's recovery was reduced proportionally by the degree to which his or her negligence contributed to the injury).

In the 1970s, the critical legal studies movement took legal realism a step further, asserting that the law not only reflected the judges' moral and social views but was overtly political. According to this view, advanced by David Kairys among others, judges imposed the elite's policy views on society. Today, many view the common law as a mixture of enduring legal principles, individual and societal moral judgments, and adaptations to social change.

—Barry Bennett

See also Business Law; Contracts; Legal Rights; Natural Law Ethical Theory; Negligence; Product Liability; Property and Property Rights; Torts

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Commons, The

The commons refers to an open-access resource, usually land, which is available for community use. In urban areas, it is often public property, such as Boston Commons or New York's Central Park, where access is unrestricted even for noncitizens. In rural areas, the eligible commoners are generally well-defined. In particular, its agricultural manifestation refers to uncultivated or harvested land with open access for grazing; the gathering of wood, leaves, and bracken; and the digging of peat, leading to the notion of common pool resource (CPR).

The precise difference between these two notions of the commons can be seen with the aid of Figure 1, which gives the standard economic taxonomy of goods according to the properties of excludability and rivalry. A good is excludable if it is feasible for the owner to restrict access. A good is rival if its use or consumption effectively removes the possibility of the same by others. Private goods are both excludable and rival; purchasing a box of breakfast cereal gives the owner the right to determines who eats it (excludability), and on consumption, another consumer cannot enjoy its benefits (rivalry). Public goods such as Boston Commons or Central Park are neither excludable nor rival. The establishment of these areas created access for all passersby, and the use of the area by an individual does not preclude its use by others. If substantial numbers of users are required before crowding effects set in, then rivalry is not an issue of concern. Furthermore, publicness in no way implies that the provider of the good is a government authority. Examples of privately provided public goods include pollution abatement; finding a cure for a disease; and the all-volunteer fire department in Santiago, Chile. In contrast, CPRs are characterized by open access, but individual use (often seriously) deteriorates continued use or availability for use by others. Examples of global CPRs include ocean fisheries, air and water pollution, spamming in cyberspace, and geostationary orbits for satellites.

In his seminal 1968 *Science* article, "The Tragedy of the Commons," Garrett Hardin likened the inevitable ruin of the commons to a situation in which livestock herdsmen have access to a common pasture for grazing. The benefit an individual herdsman receives for adding another animal to the pasture is almost entirely private. In contrast, the cost of the additional

	Excludable	**Nonexcludable [Open Access]**
Rival	Private	Common pool resource (CPR)
Nonrival	Impure public good Partially rival ⇒ Club good Anticommons	Public

Figure 1 Types of Goods

overgrazing created by one animal is public in that it is shared by all herdsmen. So long as the individual benefit exceeds the public cost, an individual will rationally increase his herd without limit—even though the common pasture itself is limited. Individual freedom in the commons, therefore, leads to its ruin. In a reverse way, consider the pollution of a common water source. A rational man finds that his share of the cost of the wastes he discharges into the commons is less than of purifying his waters before releasing them.

For Hardin, the Tragedy of the Commons stands in stark contrast to Adam Smith's invisible hand, in that rational individual action no longer promotes the public interest but, instead, befouls it. Furthermore, many forms of the commons have no technical solution that would demand little in the way of changing human values or ideas of morality. Instead, the commons requires relativist ethical behavior in which the morality of individual action within the commons is a function of its current state.

Finally, the tragedy of the anticommons refers to the underutilization of a common resource. It occurs when multiple individuals have the right of exclusion. This, accompanied by a lack of hierarchy, allows the owners to effectively stand in each other's way. An example is "patent trolling," whereby companies with few actual products of their own acquire obscure patents that are essential to basic research and development and use their rights to extract licensing fees. Another is concern over commercialization of genetic patents that are essential for basic human functioning.

Public Goods

The creation of an area with open access and little or no crowding effects falls under the rubric of public goods. Public goods are important for the functioning of any society. They include national defense, highways, lighthouses, union-negotiated contracts, radio transmissions, and law and order. Public goods exhibit jointness of supply; if one individual receives them, then so do others. For this reason, public goods are also called collective goods.

The properties of nonrivalry and nonexcludability generally imply that public goods are subject to market failure. This is because the public benefit associated with a public good rarely exceeds the individual cost of provision; hence, self-interest results in public goods going unprovided or underprovided. More generally, this phenomenon is known as Olson's free rider problem because individuals have an incentive to enjoy the benefits associated with a public good and let others bear the cost of provision. For many types of public goods the incidence of free riding increases with the size of the population receiving public benefits. Group size often increases the divergence between the level of voluntary provision of a public good and its Pareto efficient (socially optimal) production. Furthermore, the (Nash equilibrium) outcome resulting from voluntary provision is invariant to income transfers among group members. This phenomenon is known as Warr neutrality.

Even when a group is privileged, so that some or all the members receive a benefit that exceeds the individual cost of provision, efficient provision is not guaranteed. If the cost of contribution is associated with individual benefits, then self-interested individuals will not truthfully reveal their true preferences for the public good. Underprovision again results. For this reason, private groups often use selective incentives to overcome both the free rider and the preference revelation problems. Selective incentives are private benefit inducements that accompany contributions to a public good. For example, contributors to the American Association of Retired Persons not only fund lobbying efforts that benefit all retirees but also receive membership discounts on meals, hotels, and insurance. Selective incentives not only include material incentives but also psychological incentives such as the warm glow associated with altruistic behavior and moral incentives for adhering to an ethical norm.

Government intervention is popularly viewed as an effective way to overcome the market failure associated with voluntary provision. As indicated above, however, Warr neutrality implies that the government cannot simply tax contributors to finance further expenditure on the public good. Existing contributors will react by reducing their own expenditure by the amount of the tax, thereby implying that government expenditure financed in this way crowds out private contributions on a dollar-per-dollar basis. Instead, provision will increase if noncontributors are taxed. Such a scheme can be problematic for several reasons. First, if those taxed do not receive the benefits from the public good or do not prefer it, then the tax and finance regime does not necessarily result in an improvement in social welfare. Second, government intervention can come with its own set of restrictions on access and behavior, thereby changing the character of the public good. Third, public goods can be financed by the public sector but produced through private actions (e.g., defense contractors). If more than one government agency is involved, and their knowledge of the private contractor's actions is imperfect, then a common agency problem can arise owing to conflicting aims of the agencies.

The Tragedy of the Commons

Hardin's original article on the Tragedy of the Commons is actually concerned with overpopulation. In his Malthusian metaphor, grazing stands for procreation and the commons for nonrenewable resources to support population growth. In many respects, however, the metaphor itself has become a model for the dire consequences of overutilization of CPRs, particularly the environment. For example, it has been found that water pollution increases in areas closer to the U.S.-Mexican border as compared with areas further from the border in either country. Similarly, the deforestation of Easter Island is an example of resource exhaustion.

Resource exhaustion is not an inevitability, however, and this has turned the analysis of CPRs to the conceptual difference between *res nullius* (open access with no property rights or ownership) versus *res communes* (access rights held by a group of coowners). When a collective with access has the right to exclude nonowners, effective management can result in sustainability. It is important to note that sustainability refers to the ability to continue to put the resource to its most effective use, and not necessarily to restore it to its original unfettered state. Under *res communes*, it is possible for coowners to successfully set voluntary grazing limitations through stinting (setting a maximum amount of livestock each household could graze) or overwintering (free access to as many animals as commoners could sustain with their own resources during the winter). In an alternative context, competing oil companies that hold drilling rights over a common pool of crude can legally form consortia so that their rate of extraction does not exceed the efficient one. In contrast, they cannot legally form cartels to fix gasoline prices. The difference is that efficient extraction from the common oil pool benefits both producers and consumers, whereas price-fixing is welfare reducing for consumers.

The dissolution of the commons through the establishment of private property rights can also lead to efficient and sustainable usage. This principle is known as the Coase theorem, although the distribution of welfare is not independent of the assignment of private property rights. Indeed, a historical debate exists regarding whether enclosure and privatization of commons led to the removal of a social safety net for peasants during adverse agricultural conditions. Marxians assert that dissolution of the commons by this means reduced the independence of subsistence-level poor from the labor market, further contributing to peasants' proletarianization and poverty.

When a commons is truly *res nullius*, it is not possible to assign property rights or establish external governmental control. In such situations, the individuals involved may be able to self-organize and overcome the tragedy. Ostrom provides an example of local fishermen who randomly assign initial fishing sites at an inland lake on a yearly basis, with an agreed-on system of rotation for the remainder of the season. In general, she finds that appropriators are willing to commit themselves to voluntary systems that clearly define the boundaries of the CPR; recognize the current state of the resource; are independent from external authorities, both for monitoring use and resolving conflicts; allow for the alteration of rules via consensus; and involve graduated sanctions for violators.

The Prisoner's Dilemma: A Unifying Model?

Traditionally, both the tragedy of the commons and the voluntary provision of public goods are considered examples of the Prisoner's Dilemma, a metaphor and theoretical model in the social sciences that illustrates the dichotomy between individual self-interest and collective action. Yet this common theoretical construct hides significant differences between the two problems, as can be seen by examining Figure 2.

(a) Voluntary Contribution

↓Row player / Column player→	Contribute	Not
Contribute	1, 1	–1, 2
Not	2, –1	0, 0

(b) Tragedy of the Commons

↓Row player / Column player→	Not	Graze
Not	0, 0	–2, 1
Graze	1, –2	–1, –1

Figure 2 Prisoner's Dilemmas

Figure 2a represents the decision to voluntarily contribute to a public good as a Prisoner's Dilemma. If neither player contributes, then the southeast cell of Figure 2a illustrates a payoff of 0 for each of the players. Suppose that a contribution creates a public benefit of 2 at a private cost of 3. If the row Player 1 contributes and the column does not, then Row 1 receives a payoff of −1 (= 2 − 3), whereas column free rides and receives the public benefit of 2. These payoffs are illustrated in the northeast cell of Figure 2a. The reverse situation—where row free rides and column contributes—is given in the southwest cell. Finally, if both contribute a public benefit of 4 (= 2 + 2) is created. Each player pays a private cost of 3, meaning each receives a net payoff of 1 (= 4 − 3). This outcome is given in the northwest cell. If column contributes, then row is better-off by not contributing (a payoff of 2) as compared with contributing (payoff = 1). If column does not contribute, row is again better-off by not contributing, which earns 0 versus a payoff of −1 for contributing. By similar reasoning, column is always better-off by not contributing, regardless of row's strategy. Acting in individual self-interest results in each player receiving the payoff of 0 in the southeast cell. If they instead act in the interest of the group, they receive a payoff of 1 each in the northwest cell. Individual rationality is, therefore, at odds with group rationality.

In the commons game in Figure 2b, grazing yields an individual benefit of 3 at a public cost of 2. If neither player uses the commons for grazing, each receives the payoff of 0 in the northwest cell. When one player grazes and the other does not, the grazer receives a net payoff of 1 (= 3 − 2), while the inactive player faces only the public cost, resulting in a payoff of −2. These outcomes are given in the southwest and northeast cells of Figure 2b. Finally, if both graze, a total public cost of 4 (= 2 + 2) is created, and each receives a payoff of −1 (= 3 − 4), represented by the southeast cell. Grazing is always in an individual's self-interest. When the other player does not graze, grazing yields a payoff of 1 versus 0. Furthermore, when the other player grazes, a grazer earns −1 versus −2. Individual self-interest results in the southeast cell, whereas acting in a group interest is preferred (the northwest cell).

This dichotomy between individual and group rationality is what has made the Prisoner's Dilemma an important model in the social sciences. Furthermore, the ubiquity of the Prisoner's Dilemma is illustrated by its applicability to both the issue of free riding and the Tragedy of the Commons, which themselves represent a broad spectrum of social interactions. Important differences exist between the two manifestations of the Prisoner's Dilemma, however. For example, in the voluntary contribution game, action is desired over inaction. In contrast, in the commons, inaction is desired over action. Regardless of whether the commons occurs under *res nullius* or *res communes*, its resolution requires participants to relinquish a privilege. This implies a profound difference in policies to remedy situations that are akin to the commons, because studies have shown that incentives must be much stronger to induce individuals to give up their rights to an action versus inducing them to take an action, even when the impact of each is equivalent. The implication of these framing effects is that selective incentives work to encourage voluntary contributions but selective disincentives (punishments) are part of policy prescriptions for the commons. For example, the Montreal Protocol was framed in terms of preserving the stratospheric ozone layer—a public good—whereas the Kyoto Protocol is framed in terms of reducing greenhouse gas emissions—a commons. The Montreal Protocol, therefore, provides for funding to induce developing countries to reduce their use of chlorofluorocarbons, whereas the Kyoto protocol contains a punishment phase of increased abatement of greenhouse gases for any violating country.

Further differences include the ability of underprivileged members to rely on larger privileged members to contribute greater amounts toward the provision of a public good (the exploitation of the large by the small), whereas larger members further degrade the commons as compared with smaller users (the exploitation of the small by the large). In a public goods agreement, the effect of the exit of a member can be made up with additional contributions by remaining members. In contrast, an exiting appropriator may complete offset management efforts in the commons. Furthermore, resolution of the free rider problem via reciprocal altruism often makes perfect sense. Each provides conditional on the other providing. Yet if reciprocal altruism does not work in the commons, the resource is further degraded and sustainability may not be recoverable. Such a dynamic possibility, which is not present in the Prisoner's Dilemma, must be included when modeling potential resolutions to the Tragedy of the Commons. Last, the outcomes of public goods (or "give some") experiments are vastly different from commons ("take some" or "nuts game") experiments, with group-desirable behavior being much more prevalent in the former.

While these considerations indicate that the commons may be a more difficult problem to resolve than public goods provision, other studies focus on self-limits to the exploitation of the commons. The end result of *res nullius* is not ruin, but a level of overutilization that is bounded by the market price of the resource. The public costs of an activity are indeed borne by each appropriator, and these must be compared with the market price when deciding on the individually rational level of appropriation. In contrast, a different type of constraint exists for the misallocation of resources due to free riding; the aggregate-benefit-generated public good is never fully captured by the market price, due to nonrivalry. As a result, there is no guarantee that provision will occur.

No Technical Solution

Hardin's paper has been criticized due to his lack of historical understanding of the management of common land, but in any unmanaged commons his appeal to ethical behavior remains valid. His solution—mutual coercion, mutually agreed on—is meant to denote the limited ability for government intervention or the establishment of property rights to resolve the problem. It advocates the promotion of the common interest in a rational manner rather than the rational promotion of self-interest. In this way, during the 1980s and 1990s, environmentalists rallied around the ethic of sustainability, as presented in the UN-sponsored Brundtland report, *Our Common Future.* Sustainability has a Lockean foundation, advocating that every person should remove resources from the state of nature by mixing his or her labor with them and making them his or her property as long as there is enough, and good enough left in common for others. The idea that these "others" include future generations yet unborn has caused the emphasis on sustainability to give way to stewardship and the precautionary principle, which recognize that there is no single truth about the state of the environment. Instead, one should proceed cautiously to minimize the effects of one's action. Yet difficulties remain in operationalizing these concepts due to differences between competing stakeholder paradigms for valuating the state of nature.

—Daniel Arce

See also Coase Theorem; Nash Equilibrium; Pareto Efficiency; Prisoner's Dilemma; Public Goods; Tragedy of the Commons

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Commonsense Morality

Philosophically, the term *commonsense morality* is used most often to refer to the philosophy of commonsense, sometimes known as the Scottish philosophy after its primary exponents, Thomas Reid and his successors. It should be noted, however, that not all Scottish philosophers followed the philosophy of commonsense, and not all commonsense philosophers were Scottish. Also, other philosophers have used, in their normative ethical theories, notions of commonsense morality; in doing so, they typically are referring to our shared ideas of morality and moral judgment.

Commonsense philosophy as espoused by Reid, in its essence, was a reaction to the idealism espoused by George Berkeley and to David Hume's skepticism. In response, Reid argued that even if the existence of concepts such as real external objects or space are not strictly provable in a logical sense or cannot be learned from experience, their existence remains self-evident to all humans (the doctrine of natural realism). He further held that such principles and concepts are inviolable, since denying them does not rid oneself of them (denying the reality of external objects does not make them disappear).

Reid's realism in such questions carried over to his thoughts on ethics. Morality has principles, Reid argued, and the first principles of morality were as self-evident to people with moral education as were the principles mentioned above. These principles were of several types. One type, referred to as *general*, deals with matters such as whether a person can be blamed for an action over which the person had no control. The second type, referred to as *particular*, contains the more recognizable normative moral principles concerning duties to self, others, and God. For example, Reid gives a version of the Golden Rule as one of the self-evident duties to others; the other duty is that people should act to benefit the society of which they are a part. The latter sounds consequentialist, but Reid is typically considered a deontologist, and commonsense morality, in general, can be considered deontological in that moral rules are fundamental to ethics.

Ordinary commonsense is seen by Reid as containing the self-evident moral principles he discusses. If commonsense and theory are in conflict, then theory must be in error and should be altered to fit commonsense. However, instead of people agreeing to obligations out of self-interest and then recognizing their moral nature, Reid argues people know concepts in similar ways and understand their moral nature before agreeing on rules upholding such concept.

Reid quite rightly notes that the particular principles can conflict with one another. In this he agrees with moral pluralists. His solution is unlike that of pluralists such as W. D. Ross, however, because Reid says we also can see self-evident priorities among the moral principles. If the priorities are self-evident, they are always in a certain order, so context means little, unlike in Ross's pluralism. For example, Reid mentions that between the virtues of (unmerited) generosity, gratitude (generosity in response to another's action), and justice, justice is self-evidently the most important, gratitude the second, and generosity the third. On the other hand, Reid sees greater worth in generosity than in justice. Thus, justice must be instituted, but when one is unencumbered by other considerations, generosity should always appeal to the actor.

The self-evident moral principles noted by Reid are to be directly and immediately perceived by all humans through what he calls a conscience. In part, this is an intellectual power allowing us to perceive self-evident principles and, in part, an active power that might motivate us to act on our perceived duty. All humans have this conscience and so are able to act in morally correct ways. However, conscience needs to be developed over time. Some form of moral education is thus necessary, but Reid seems to indicate that all humans go through the process somewhat naturally—and can be aided or harmed by education.

Contrary to what he believes is Hume's view of morality, Reid argues that morality involves judgment and reason and is not merely a matter of sentiment and passion. Sentiment and judgment are related, but for Reid sentiment changes as judgments are made. Reid acknowledges passion as a motive for action, but he insists that other motives arise from rational principles such as our overall good and our duty (which is superior in authority to interest).

Although Reid's overall philosophy of commonsense was altered over time by his followers to the point that some have argued it became closer to skepticism than to Reid's original thought, his moral philosophy was relatively unchanged. Followers such as Dugald Stewart and James Beattie agreed with Reid's ideas concerning morality, which formed one response to Hume. Kant formed another and different response. Kant's response has been much more influential, although in Great Britain, France, and the United States Reid's followers had influence for much of the 19th century. C. S. Peirce and G. E. Moore developed their ideas in part based on commonsense philosophy.

Other philosophers have invoked commonsense in one way or another in explaining their normative ethical theories. For example, Aristotle uses commonsense (in the sense of common beliefs about the good) as a beginning point for his arguments and as a test of whether his theory passes muster. Kant notes some common ideas concerning morality and seeks to explain philosophically the conditions that must underlie our ordinary ideas of morality, if these ideas are true. Proponents of natural law, such as Saint Thomas Aquinas, believe that the most basic moral principles are self-evident and thus available to all humans. Finally, John Rawls's notion of reflective equilibrium relies on considered judgments that may need to be accepted by all competent judges (in one version this is true; in another version it is not). This notion also speaks to commonsense.

Commonsense morality is an interesting if underexplored approach to business ethics. Several questions might arise in such exploration. For example, how does commonsense morality relate to the decisions businesspeople make on a daily basis? Can commonsense be relied on to guide those decisions, and what is the effect of business school education on commonsense? To what degree are codes of conduct based on commonsense and how is that related to their effectiveness? To what degree do commonsense notions of treating well those with whom one comes in contact (such as colleagues, employees, customers, and suppliers) coincide or conflict with managerial or stakeholder capitalism? Exploration of these questions could prove fruitful for those interested in business ethics.

—Brian K. Burton

See also Aristotle; Deontological Ethical Systems; Friedman, Milton; Hume, David; Intuitionism; Kant, Immanuel;

Moral Luck; Moral Realism; Moral Sentimentalism; Natural Law Ethical Theory; Pluralism; Rawls's Theory of Justice

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Communications Decency Act

The Communications Decency Act (CDA) was enacted by the U.S. Congress in 1996 in response to concerns about minors' access to pornography via the Internet. The CDA was Title V of the Telecommunications Act of 1996, but in two separate cases, *Reno v. Shea* of 1997 and *Nitke v. Gonzalez* of 2005, federal judges found that the indecency provisions were found to abridge "the freedom of speech" protected by the First Amendment to the U.S. Constitution. Both decisions were affirmed by the U.S. Supreme Court without comment.

The CDA has become a powerful example of federal regulation in place of an industry's self-regulatory activities. The CDA was enacted on February 1, 1996, as representatives and senators prepared for reelection campaigns the following fall. The CDA was intended to show voters that Congress understood the risks of a rapidly growing emerging technology.

The CDA created a criminal cause of action against those who knowingly transmit "obscene" or "indecent" messages to a recipient under the age of 18 years. It also prohibited knowingly sending or displaying a "patently offensive" message containing sexual or excretory activities or organs to a minor. The CDA did, however, provide a defense to senders or displayers of online "indecent" materials—if they took reasonable good faith efforts to exclude children.

This legislation had numerous problems that affected both Internet service providers (ISPs) and businesses. First, there was no way for senders or displayers to know if they were within the exception. At that time, it was difficult and cumbersome for a sender to screen out minors. The displayers could ask for a credit card number as validation, but it would not allow them to conduct business with those who did not have a credit card and were over the age of 18 years. In addition, the terms *indecent* and *patently offensive* were too ambiguous, and the CDA as a whole placed an undue burden on free speech.

These portions, especially those regarding the phraseology of the CDA, were quickly fought by civil rights groups and free speech advocates and were challenged in a court of law by numerous plaintiffs. The case was ultimately brought to the Supreme Court in *Reno v. ACLU*, which was argued on March 16, 1997, and decided on June 26, 1997. The provisions in Sections 223 of Title 17 U.S. Code Annotated regarding *indecent* and *patently offensive* materials were found to abridge "the freedom of speech" protected by the First Amendment to the U.S. Constitution.

Although the portions of the CDA regarding indecent conduct were overturned, there are provisions within the CDA that remain intact. The portions of Section 223 regarding obscene content were challenged in *Nitke v. Ashcroft*, but Nitke was unable to meet the burden of proof necessary to support her claim. On July 26, 2005, an appeals court ruled that obscene content is not protected by the First Amendment, but that Nitke's challenge was to the reliance on community standards to determine whether her online content was obscene. The U.S. Supreme Court upheld this decision in 2006.

Another distinctly different portion of the CDA can be found at 47 U.S. Code Annotated Section 230. This section had previously been introduced by Representatives Chris Cox and Ron Wyden as the Internet Freedom and Family Empowerment Act and had already passed the House. The text of this bill was added to the CDA during a conference to reconcile differences between the Senate and the House versions of the bill. Section 230 creates a federal immunity to any cause of action that would make service providers liable for information originating with a third-party user of the service. Although this does protect online forums and ISPs from most federal causes of action, it does not exempt providers from criminal, communications privacy, or intellectual property claims, nor does it exempt them from applicable state laws.

In practice, ISPs' immunity from prosecution has itself created problems. While ISPs are protected by the "Good Samaritan" portions of this section, there have been individuals and groups who have sued Internet users and ISPs over libelous Web pages. Some parties maintain that users should be able to sue ISPs in cases where it is appropriate, including situations where an anonymous poster of questionable content in an online forum cannot be identified.

Also, the courts have not clearly defined the line at which a blogger, who may be viewed as an information publisher and a user, becomes an information content provider. Editing a Web page, or posting a comment, so as to create a new, defamatory meaning for the existing content, may cause that user to lose protection under Section 230. Section 230 does not provide immunity from federal criminal law, intellectual property law, and electronic communications privacy law.

—William A. Sodeman

See also Electronic Surveillance; Internet and Computing Legislation; Privacy; USA PATRIOT Act; Workplace Privacy

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Communications Workers of America

The Communications Workers of America (CWA) is America's largest communications and media union. The CWA represents employees in telecommunications, broadcasting, cable TV, journalism, publishing, electronics, and general manufacturing. It also represents employees in airline customer service, public safety, government service, health care, and education.

The CWA is headquartered in Washington, D.C. It is affiliated with the AFL-CIO, the Canadian Labour Congress, Communications Workers Union and the Society of Telecom Executives in the United Kingdom, and the worldwide Union Network International.

As of 2005, the CWA represents more than 700,000 men and women in both private and public sectors who are party to 2,000 collective bargaining agreements on wages, benefits, working conditions, and employment security provisions for its members. Among the major employers of CWA members are AT&T, GTE, the Regional Bell telephone companies, Lucent Technologies/Bell Labs, General Electric, NBC and ABC television networks, the Canadian Broadcasting Corp., *New York Times*, *Wall Street Journal*, *Washington Post*, US Airways, the University of California System, and the state of New Jersey.

Attempts in the early 1900s to unionize the communications industry by groups such as the International Brotherhood of Electrical Workers and the Women's Trade Union League were largely unsuccessful because of the monopolistic powers of the Bell Telephone Company and the nature of the industry, for example, geographically dispersed and transitory workers, and changing technology, that is, the introduction of dial telephones. The ability to unionize grew stronger with the passage of the National Labor Relations Act (commonly known as the Wagner Act) signed by Franklin Delano Roosevelt in 1935. The Wagner Act had three provisions: It prohibited the employer from engaging in certain activities that were defined as unfair labor practices; it protected union and collective activity, protected workers who took part in grievances, on-the-job protests, picketing, and strikes; and it established an agency, the National Labor Relations Board, to enforce the provisions.

The CWA arose from the collapse of The National Federation of Telephone Workers (NFTW). This loosely federated group benefited from stagnant wages and deteriorating working conditions during World War II, which stimulated telephone worker solidarity and union amalgamation, and held a successful strike in 1946, which led to the first national agreement with AT&T. The NFTW could not repeat its success in subsequent years and disbanded. In 1948, the CWA was born. Throughout its history, the CWA has focused on unionizing workers in the telecommunications industry, fighting for wage increases, comparable pay and benefits, fair working hours, and the right to strike. In the 1980s, the CWA began to expand beyond telecommunications. It created a Public Employees Department, which successfully organized 34,000 New Jersey state workers. It merged with or absorbed other unions, including the International Typographical Workers Union, the National Association of Broadcast Employees, and the Newspaper Guild.

At the turn of the 21st century, the CWA enters a critical period. Union membership, particularly in the private sector, has declined in recent decades. Since 1970, the percentage of the U.S. workforce that is organized has dropped from 30% to 12%. The decline in membership comes at a time when managements argue for lower wages and benefits and eliminate job security in the name of efficiency and flexibility and there are threats to jobs from deregulation and global competition. The current issues that the CWA is concerned about include the health risks of working with lasers, for example, in fiber-optic communications systems, telecommunications reform, and consolidation of media ownership.

—Donna M. Schaeffer

See also Labor Unions

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Communism

Communism is a social philosophy based on the common possession of property and the elimination of private ownership. The moral basis of communism is founded on the belief that private property represents an obstacle to the creation of a genuine human community. By creating inequality and encouraging competition for the possession of scarce resources, private ownership undermines cooperation and creates artificial social hierarchies that benefit the powerful and cause suffering to the poor. By replacing private ownership with the common possession of the productive resources of society, communism aims to overcome social injustice and create a new society based on human cooperation.

History

Among the earliest discussion of communism as a moral concept is Plato's *Republic*, which is an extended meditation on the question of justice. The just society, according to Plato, is one in which those with wisdom rule over the others. Wisdom is embodied in the ruling class of guardians and, ultimately, in a philosophical elite. These "philosopher-kings" would rule justly and disinterestedly, living communally and without private property. Merchants and craftsmen would be permitted some private property but would be barred from governing. In addition to abandoning private property among the ruling class, a just society, according to Plato, would also abolish traditional familial relationships and recruit the ruling class from among the children of all members of society. Plato, thus, proposes a system that is simultaneously egalitarian and elitist, insofar as any child may potentially be drafted to serve as a member of the guardians, but only those deemed to be the "best" among the members of society are permitted to share in its governance.

Unlike many later versions of communism, only the elite abandon private property. Ordinary citizens, incapable of abandoning and transcending their desires to contemplate the good, true, and beautiful, are not expected to live communistically. The rulers, on the other hand, knowing the nature of the good, don't desire material goods and, according to Plato, are not susceptible to the corruption that other, baser political and economic arrangements engender.

Some early Christian communities seem to have subscribed to a communist social arrangement. According to the New Testament account in the Acts of the Apostles, "the whole group of those who believed were of one heart and soul, and no one claimed private ownership of any possessions, but everything they owned was held in common" (Acts 4:32). However, it is not clear how this common possession was administered. The author of Acts relates the story of Ananias and Saphira, a couple who sells a plot of land but keeps some of the proceeds for themselves. Peter admonishes Ananias, "While it remained unsold, did it not remain your own? And after it was sold, were not the proceeds at your disposal?" This would seem to imply that the community of goods was at least somewhat voluntary. Even so, it is noteworthy that the author of Acts discusses these events in the past tense. However, it was that the early Church held property in common; within only a few decades, it appears to have abandoned the practice.

The practice of holding all things in common remained alive in the Church primarily through the discipline of monastic life. The model for monastic communal life is the Rule of St. Benedict. Chapters 33 and 34 of the Rule state that individual monks are not permitted to hold any private possessions without the abbot's permission and prescribe the criteria for the just distribution of goods among the monks.

Thomas More's *Utopia* (a word that means "no place") purports to be the account of the adventures of a sailor named Hythloday in a newly discovered country, the residents of which share all their goods in common and have no distinctions of rank. Each household in Utopia is identical and even the clothing worn by the utopian citizens is identical. Communal ownership of property is taken to such a degree that the citizens rotate among the houses on a regular basis.

Prior to the publication of *The Communist Manifesto* in 1848, *communism* as a political movement had been developing for several decades. The term may have come into official political currency through the work of Emile Babeuf, the French utopian thinker, but it was quickly adopted among the revolutionaries of the period. One can also find criticisms of private property in the works of Jean-Jacques Rousseau, among others.

The term *communism* as it is used today is based on the theoretical groundwork laid by Karl Marx and Friedrich Engels, who together developed communism from a utopian theory of communal life into a political program that proved to be intellectually attractive as well as politically successful through much of the 20th century. What distinguished Marx's communism from its earlier cousins was Marx's determination to understand communism primarily as a scientific, political, and economic program rather than as a moral ideal. This program was rooted in an "historical materialist" description of social conditions. According to this theory, there are no cultural, moral, or political values that exist independently of one's class status. The way to change the values of society was, therefore, to change the economic conditions as they existed by overthrowing the existing ruling class and elevating the proletariat to the ruling class, thereby creating a society whose values were rooted in universal social conditions.

Vladimir Ilyich Lenin, who combined Marx's economic and political theories with a particularly brutal revolutionary strategy, was able to bring the Bolshevik party successfully to power in Russia during the October 1917 revolution. Afterward, the identification of communism with the philosophical and political agenda of what came to be known as "Marxism/Leninism" became a matter of course. This had several effects, not least of which was elimination of any discussion of other, putatively more "utopian," approaches to communism. In addition, moral evaluation of communism became identical with moral evaluation of the totalitarian political and economic system of the Soviet Union. Finally, it established the Leninist interpretation of Marxism as normative for purposes of evaluating its social, political, and moral implications. Nevertheless, there remained an undercurrent of non-Leninist interpretation of the Marxist philosophy that existed throughout the Soviet era and that still exists.

Communist Ethics

While earlier approaches to communism were emphatically moral, even moralistic, in their arguments for the abolition of private property and the establishment of a society rooted in communal values, the communism of Marx, Engels, and Lenin was disdainful of moralistic appeals. By arguing for the "scientific" status of communism, they sought to take the argument out of the field of morality altogether in the name of an ultimately deterministic metaphysical system (Marx's "historical materialism," later modified to "dialectical materialism" by Engels).

Nevertheless, Marx's own writing frequently betrayed an injured tone that decried unjust social conditions as dehumanizing and immoral. In *Das Kapital*, he describes the "vampire like" effects of the capitalist system, which drained workers of their very lifeblood through exploitation. By the same token, he argues that capitalism, through its creation of an alien and alienating system of commodities, dissolves the traditional bonds of civil society, including even the family. The very foundational mechanisms of capital, as Marx understands them, are rooted in the extraction of "surplus value" from workers, essentially robbing them of value that they had rightfully earned.

All this is not to say that Marx was seeking to make a primarily moral argument about the nature of capitalism. However, although Marx's arguments were seldom explicitly moral in their content, they were rooted, as Cornel West has argued, in a moral critique of the social conditions under which he observed workers living.

In "The Tasks of the Youth Leagues," Lenin argued in favor of the idea of communist ethics. According to Lenin, communist morality, contrary to bourgeois morality, is rooted not in the command of God but in the concrete interests of the proletariat. This means, in the first instance, that communist morality is dedicated to overcoming the oppression of the working class through the destruction of capitalist society. In doing so, communism would overcome class divisions in the name of human unity. Morality, determined as it is by class interests, also exists in the service of the interests of that class. The only criterion, thus, becomes whether a particular course of action promotes or hinders the revolutionary ascendancy of the working class.

There is, however, also a positive dimension to Lenin's interpretation of communist ethics. In destroying the bourgeois culture of exploitation, communism seeks to put in its place a system based on cooperation and mutual aid. However, no morality, according to Lenin, rises above the particular historical circumstances in which it exists.

Leon Trotsky strikes similar notes in his 1936 essay "Their Morals and Ours." Like Lenin, he argues that morality is a function of social circumstances and serves class interests. He argues contemptuously against various versions of what he terms "bourgeois" morality, but, in addition, he seeks to distinguish his own approach to morality from Stalinism. As opposed to the class-based morality advocated by Lenin, argues Trotsky, Stalinism is a reactionary reinforcement of the old order. Trotsky distinguishes his interpretation of communist ethics from the idea that the end justifies the means, a view he associates with Stalin, on the grounds that this perspective reflects a reactionary rather than a revolutionary agenda.

With variations, most Marxist-Leninist discussions of morality follow this general outline. Many noncommunist versions of socialism, including those informed by Marx's philosophy, explicitly reject this approach to morality, arguing that a genuinely Marxist ethic may be rooted in larger moral principles while at the same time being conscious of its historical contingency. The lineage that runs from Leninism through Stalinism, Trotskyism, and Maoism, however, affirms the class contingency of all morality and rejects any moral claims that are not rooted directly in the proletarian struggle for supremacy.

Ethical Criticisms of Communism

A number of criticisms can be made against communist ethics in general and the Marxist-Leninist variety in particular. First, communist ethics, in general, may be criticized as unrealistic and utopian, grounding its moral claims not in real human possibilities but in an ideal that human beings are incapable of achieving. This very argument, indeed, was used by Marx and Engels against the so-called utopian socialists with whom they struggled over the socialist agenda in the 19th century. By appealing to a malleable human conscience rather than concrete human possibilities, this objection runs, communist ethics evades genuine responsibility for the world it purports to seek to change.

A second objection is based on the human right to private property. Although Marx's analysis of capitalism was deeply indebted to the work of John Locke and Adam Smith, Marx, unlike them, did not regard property as something over which people had any form of natural right. For Locke and Smith, however, as well as for their many descendants, private property is at the foundation of a just society, insofar as it permits people a realm of personal autonomy that constrains efforts at control by the state or other social institutions.

A third critique of communism is that its social strategy runs contrary to its stated objective, the creation of a classless society. Lenin's justification of Bolshevist activism in the name of the "dictatorship of the proletariat" merely substitutes an ideological and ultimately corrupt bureaucratic elite for a capitalist oligarchy. Communism, as practiced, has proven to be far less economically productive than capitalism and has thus produced a far smaller degree of aggregate social welfare. Communism has been more effective as a critique of capitalism than as a constructive political or economic theory in its own right. By focusing on the maldistribution of wealth under capitalism, without a corresponding understanding of the nature of economic growth, communism never developed effective techniques for sustained economic expansion.

A fourth objection, relevant particularly to the Leninist stream of communist ethics, is that by basing its ethics solely in the concrete interests of the working class, communist ethics becomes hopelessly relativistic, allowing any form of cruelty or barbarity in the name of promoting revolutionary change. Both Lenin and Trotsky sought to address this criticism but neither ever offered a strong rebuttal to the accusation. Indeed, their most developed elaborations of communist ethics seem to support this objection in spite of their best efforts.

In the final analysis, communism as an economic system failed to deliver on its most central promises—the creation of a classless society and the creation of a productive and nonexploitative economic and political system. Whatever its inadequacies, however, communism may still possess some enduring value as a critique of capitalism, particularly in light of the inequities of globalization. While it may provide no prescription for the solution of these problems, it embodies the protest that an economy in which all people participate should, insofar as possible, be an economy from which all benefit.

—Scott R. Paeth

See also Christian Ethics; Engels, Friedrich; Locke, John; Marx, Karl; Marxism; Property and Property Rights; Relativism, Moral; Rousseau, Jean-Jacques; Smith, Adam; Socialism

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COMMUNITARIANISM

Communitarianism designates a political theory that reminds us that persons live within a complex web of groups and associations by which they define themselves and take up responsibilities that form the bonds uniting them in common efforts. The modern world is dominated by the great institutions of the state and the market. Communitarians emphasize that in addition to those two great centers of power, there are numerous other communities and associations that people form so as to carve out together meaningful and effective lives together. Indeed, through these associations members can gain the power to influence the state and the market. Communitarianism is, in part, a sustained response to contemporary liberalism's tendency to emphasize the freedom of individuals at the expense of neglecting the role of communities. Communitarianism is best understood, then, as a critique of liberalism, especially of its excessive individualism, largely done as a corrective within—not against—liberalism itself.

Liberalism asserts two universal principles concerning human beings, *autonomy* and the *respect* due to persons because of their autonomy. Communitarians argue that contemporary liberalism holds society to be composed of individuals each of whom seeks his or her good through a political order protective of individual rights and private pursuits. Many liberals champion individuality to the neglect of the complex forms of cooperation that nurture and support all persons' lives; discount the interdependence essential for gaining knowledge and power; and forget the development of self-identity through reciprocally revealing interchanges with, and commitments to, others. Communitarians assert the interdependence of the self with others in numerous associations through which persons become unique individuals with perspectives, talents, and identities of their own with which to pursue the good as they conceive it together. Communitarians acknowledge and encourage the formation of associations, both large and small, in *civil society*, a space for civic action lying between the state and the market, where people discover themselves and their world through accepting the responsibility to act effectively and morally in solidarity with their fellows.

Alasdair MacIntyre emphasizes that communities endure through time because members hand down their beliefs and practices as traditions for newcomers to learn and perform with excellence. A practice, such as medicine, is widely respected because its practitioners are recognized as part of a tradition of education and performance of a widely recognized good upheld by the policing of the practitioners themselves. MacIntyre's emphasis on tradition and continuity through practices led him to turn away from liberalism and toward Aristotle and Thomas Aquinas, philosophers who discussed excellence through traditional practices within authoritative institutions, the *polis* and the Church, respectively.

Liberalism asserts persons' equality due to their freedom of choice. Liberalism is aptly named for it is a doctrine of autonomy, the view that persons have the freedom to *choose* to participate in society's institutions and to determine the goods whose pursuit is at the core of their own lives. *Autonomy* here means freedom as self-assertion and efficacy ranging from individual or private interests to the system of public deliberation, agency, and law. Autonomy includes persons' ability to accept moral obligations they decide they *ought* to perform due to a problematic situation they face. When people decide together the rules they agree to obey for their mutual benefit, they are expressing their freedom, not limiting it. When a person decides that a certain action is an objective moral obligation to which she or he holds herself or himself, she or he is exercising her or his moral freedom. Acting on a decision is an expression of power—the ability to realize in deed one's considered intention rather than to submit to extraneous forces. Due to their autonomy, persons deserve respect from one another, because in their freedom they reveal themselves as one another's equals before the law, engaged in articulating through their words and realizing through their deeds their vision of a common world. Respect requires that persons not use one another as mere instruments, but that they seek to form a common bond with others that opens the way to accord and solidarity in common purposes.

If all are free and equal, their polity should reflect and respect this fact about persons. As a result, numerous liberal theorists have sought through thought experiments to discern those organizational principles that will best enable free and equal persons to construct a fitting civil order for themselves. These experiments can be traced from Thomas Hobbes's and John Locke's "states of nature" and "social contracts" to John Rawls's "original position." These thought experiments all argue for rights due to all members of the imagined order as well as limitations on members' actions for the sake of the security and well-being of all. In return for the limitations on persons' actions, they are free to advance their self-interest in the market rendered secure by the state's oversight.

Liberal theorists, generally, have sought to construct political orders that provide, on the one hand, the equal opportunity to participate in the public realm of politics through the protection of civil rights and, on the other, security in the private realm needed for the pursuit of economic and other personal goods. Liberal theories retain the tradition's two realms: (1) a public realm in which discourse and decisions concerning politics, ethics, and law direct a government dispensing justice and (2) a private realm in which people attend to their own affairs, whether among intimates within the household or among others earning a living in the market. The protections provided to members of society are *rights* that can be claimed against anyone who would violate them while members pursue the *good* as they understand it.

People display *plurality* in their uniqueness, for no one is exactly like any other, and their different views on the good life arise from their singular experiences. Liberalism respects plurality among persons and, so, permits flexibility in choices made for a good life. That is, the polity should be neutral toward goods unless some good's pursuit leads to an injustice. Communitarians spy a problem here, for despite the specificity of persons evident in the goods they seek, the rights specified for them in a liberal state cannot honor that specificity, for justice demands universality—the application of the same rules and procedures to all independently of their uniqueness as persons. Justice in its liberal formulations necessarily treats persons as abstract individuals indistinguishable one from another. Communitarians complain that this liberal ideal provides only for universal justice as obedience to the laws. The good is left to private discernment while the state remains neutral toward citizens' decisions about private goods. Universality of justice and neutrality toward the good, however, is all that can be expected in a polity formed by the strangers in liberal thought experiments who draw up social contracts.

The liberal dedication to public justice and neutrality toward private goods is problematic because liberals do not agree among themselves concerning what are matters of justice and of good. John Rawls, for example, takes poverty to be a question of justice presenting an obligation that social and economic inequalities should be to everyone's advantage, especially the worst off. Rawls's position is an example of egalitarian liberalism. Robert Nozick, in contrast, argues that a just state ought only to protect persons in the security of their property and its legitimate transfer. Beneficence toward the less advantaged is a supererogatory good; that is, persons *may* address poverty on their own initiative but it ought not be required of some for the benefit of others. A requirement of beneficence is nothing short of confiscation of some persons' goods for their redistribution to others. Nozick's position is termed *libertarianism,* which holds the minimum government possible to be the best because it interferes least with the liberty of citizens to accumulate and transfer goods as they choose.

Charles Taylor proposes a communitarian response to Nozick's view that justice concerns only protection of one's property and its transactions alone, rendering assistance to others supererogatory. If we claim that persons have rights, we must presume persons or institutions also have the capacity to acknowledge those rights and act on them. That is, if we claim rights, we presume the capacity in someone or some institution to accept the responsibility to realize those rights. Furthermore, if we claim rights as something worthwhile, we must also affirm the worth of those capacities that enable us to enjoy our rights. We cannot look to ourselves for the source of the knowledge and use of our capacities; the source must initially reside in others. By ourselves we would be helpless to develop our own potential. Even libertarians have need for membership in those groups that enable growth in knowledge and practice. If libertarians take these human capacities as worthwhile, moreover, they have obligations to make them available to others. Standing idly by and allowing these goods to pass away through inaction would indicate that libertarians do not care about them enough to ensure their continuation in the world. Society is richer and fuller if we engage in all the institutions that enable us to become active and effective agents on behalf of our common human world.

The political core of liberalism is the establishment of a state that protects citizens' rights, establishes a rule of law, and enables citizens to enter into agreements with one another for the sake of whatever goods they choose. The public realm in a liberal polity is not the center of citizens' lives, however. Citizens enjoy their private lives while public officials administer the state so that it provides justice and security for all within its borders. Citizens expect their rights to be protected by the government, but there are few responsibilities expected of them in return. The scarcity of public duties enables citizens to concentrate on their private concerns alone. Attentive to public affairs primarily in terms of their own interests, citizens have little encouragement to take up the perspectives of other citizens. Intent on their own interests alone, citizens can mistake their needs for rights; sensitive to any infringement of their rights by injurious actions by others, citizens can become wary and litigious. Liberalism, despite its respect for the rights of all, offers too little encouragement for citizens to move beyond their concentration on their own interests toward the public attitude of citizens intent on comprehending the perspectives of their fellow citizens and participating in resolving political disputes in a way that fosters solidarity and support even for painful but reasonable resolutions of hard problems. Liberal polities are in danger of becoming soft tyrannies, using Alexis de Tocqueville's phrase, of benevolent administrators who oversee persons who have lost control of their government by forgetting how to think and act as citizens. The liberal state unites people as citizens concerned with rights but disperses them again as individuals seeking private goods.

Communitarians criticize liberalism's sharp division between "right" and "good" as artificial. Justice, after all, is itself a good and concerns goods. How can citizens determine what decisions are just until they discuss the goods that they will protect? How can citizens determine a just distribution of goods until they learn what human beings need for a decent life? It is only through the experience of living together that people can determine what is just and, so, good for human beings living within the context of their way of life. One of liberalism's achievements is the assertion and protection of plurality, but this good is best learned through forging familiarity and solidarity with various groups, not through separating oneself off from them. For liberal theory, the enumeration of rights enables people to reflect on what they consider essential components of justice in abstraction from any specific social context. But persons never live abstractly, *unencumbered*, using Michael J. Sandel's term, by particular social roles and expectations binding them together. Concepts of both the good and the right arise within the context of specific persons living together within a personal and group history that clarifies and justifies shared responsibilities and expectations.

To be sure, liberalism has advanced politics through its protection of minorities from oppression under a tyranny of the majority as well as of the majority from well-organized minorities. Living with pluralism and respecting those who disagree with oneself are virtues discovered and nurtured under liberalism in a way never achieved in earlier regimes. Public life in liberal democracies is diminished and precarious nonetheless. Communitarians fear that lack of public engagement presages a loss of democratic temperament that could endanger people's liberal commitment to plurality; liberal citizens are at risk of becoming isolated and self-absorbed even when surrounded by others.

Communitarians attempt to resolve liberalism's problem of citizens preoccupied with their private affairs by recognizing and building on the fact that we are all—always—members of numerous communities. Communitarians join other social theorists in referring to the many associations, whether in service to government and the market or not, that constitute civil society. These associations arise due to a public-minded interest in furthering certain ends, taking a stand with like-minded citizens, enjoying the company of others, and doing something of significance for the larger society. Members of civil society engage in professional work in universities, courtrooms, and hospitals; in civic work, in charities, or other nonprofits supporting the arts, health, and education; or in principled engagement in both domestic and international organizations dedicated to solving political and economic problems concerning human rights violations, famine, and disease. For protection against forces of the market, workers have formed unions, customers have organized boycotts, and environmentalists have presented educational programs and groups to build up political pressure. All these associations constitute and condition who their members become through their interactions within them, just as members participate in fashioning what these groups become through their membership.

Individuals in liberal society face danger because they too often stand alone—or think that they do—before vast political and economic institutions, unable to influence or confront the elites directing these institutions. Due to their isolation, citizens become estranged from a world within which they have no ties other than the abstract, thin ones of a voter or an employee; they come to consider all human interaction to be egoistic, market-like transactions driven by self-interest. Communitarians rely on organizations of civil society to resolve the problem of isolation liberalism produces along with autonomy and respect for plurality. *In so doing, communitarians resolve a liberal problem with a liberal solution.* It is the liberal character of the people that makes them adept at forming civil associations. Civil society organizations enable citizens to take direct action with one another for purposes they recognize as good. In civic action, citizens both learn political skills and put them into practice. One purpose of civic action, then, is to help persons grow as engaged citizens.

Civil society gives its members an alternative to government and the market for achieving social goods. Some purposes are not reducible to the private transactional interests of individuals or to legislated policy holding universally. Some goods, rather, are achieved best by persons acting together for a good held in common. Civic organizations need to require that their members think and act in a democratic way. Democracy requires the exchange of opinion, drawing citizens to consider problems in ways that take them beyond their own perspectives to those of others discovered through deliberation and disclosure. Citizens' commitment to action comes from agreement reached on possibilities none of which could have been reached alone. Liberalism provides the foundation for this communal achievement by instilling in citizens a realization of their right to participate equally with others and respectfully to consider others' points of view. Expositions of liberalism too often fail to clarify the democratic capacity at its heart, however, emphasizing instead individual autonomy. Communitarianism focuses on the vital core of liberal democracy—the community of citizens challenging one another to move beyond private interests for the sake of goods that can be sought together and held in common.

Members of civil organizations do not forsake their independence through participation; they learn to be critical of themselves, of their organizations, and of society and its institutions generally so as to prepare themselves to realize more fully their political freedom. Due to multiple group membership and conversation with their fellows, citizens assess society from many points of view—their interest and their capacity to understand their whole society grow apace. Civil society that makes possible civic engagement in the pursuit of common goods would be undermined were it to create reticent, incurious citizens confined within the horizons of their own groups. The activities essential to effective membership—attention, discussion, disagreement, and compromise—are crucial for good citizenship and are learned only by engaging citizens with different interests and views.

Public action is complicated, sometimes past all compromise. Communitarians seek to remind liberals that social exchange requires patience, experience, forbearance, and care. At times, at an impasse, only their respect for one another holds people together as fellow citizens. Unless citizens are awake to the commitments of community as well as stirred by the promise of rights and autonomy, they will not have the fortitude to be responsible and, as such, truly free.

—William W. Clohesy

See also Hobbes, Thomas; Individualism; Liberalism; Libertarianism; Locke, John; MacIntyre, Alasdair; Nonprofit Organizations; Nozick, Robert; Nozick's Theory of Justice; Pluralism; Political Theory; Rawls, John; Rawls's Theory of Justice; Social Contract Theory

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Community Reinvestment Act of 1977 (CRA)

In 1977, the U.S. Congress enacted the Community Reinvestment Act (CRA) to encourage banks and thrifts to help meet the credit needs of all segments of their communities, including low- and moderate-income neighborhoods, in ways consistent with safe and sound lending practices. The act, which applies to federally insured depository institutions, national banks, thrifts, and state-chartered commercial and savings banks, essentially extends and clarifies the long-standing expectation that banks must serve the convenience and needs of their local communities.

Prior to the passage of the CRA, many bankers were accused of *redlining*, a practice of systematically excluding low-income neighborhoods and people of color from their lending products, investments, and financial services. The term was coined by community activists when they found that the lack of bank loans in some low-income neighborhoods was so geographically distinct it was easy to draw red lines on maps to delineate the practice. Using the Fair Housing Act of 1968, which prohibited discriminatory practices in the housing market, and data on lending patterns made available through the 1975 Home Mortgage Disclosure Act, activists across the country began to create strong pressure on banks to improve their performance in equitable lending to everyone in their communities.

In passing the CRA, the Congress found that (1) regulated financial institutions are required by law to demonstrate that their deposit facilities serve the convenience and needs of the communities in which they are chartered to do business, (2) the convenience and needs of communities include the need for credit services as well as deposit services, and (3) regulated financial institutions have a continuing and affirmative obligation to help meet the credit needs of the local communities in which they are chartered. The act requires the federal financial institution regulators—the Office of the Comptroller of the Currency (for national banks), Board of Governors of the Federal Reserve System (for state-chartered banks that are members of the Federal Reserve System and bank holding companies), Federal Deposit Insurance Corporation (for state-chartered banks that are not part of the Federal Reserve System), and Office of Thrift Supervision (for savings associations and savings and loan holding companies)—to assess the record of each bank and thrift in fulfilling these obligations. The Federal Financial Institutions Examination Council (FFIEC), a formal interagency body empowered to prescribe uniform CRA principles and standards, periodically publishes *Interagency Questions and Answers* and *Interagency Interpretive Letters* in an effort to promote consistency in CRA implementation across these agencies and financial institutions.

The regulators have three basic responsibilities: (1) to *encourage* banks to meet the credit needs of their entire communities, (2) to *assess* the CRA performance of these lenders in meeting community credit needs, and (3) to *consider* this performance when evaluating a bank's application for expansion. As a result, every financial institution covered by the CRA is examined and given a rating, as part of its normal regulatory review, every 2 to 5 years that reflects its record in this area. The ratings range from "outstanding," "satisfactory," and "needs to improve" to "substantial noncompliance." A written performance evaluation of a bank's CRA activities, including its CRA rating, is prepared at the end of each CRA examination and made available to the general public (e.g., the FFIEC publishes the latest CRA ratings of financial institutions on its Web site). Community and civic organizations, local government, and other members of the public are encouraged to express their views about a bank's CRA performance to the bank and the appropriate regulatory agency.

The regulators are required to consider this record in evaluating applications for bank charters, bank mergers and acquisitions, and branch openings and relocations. The CRA provided citizens with standing to intervene in the regulatory process, and a poor CRA record could serve as grounds for denial of an expansion request. Local community groups, nonprofit development organizations, small business associations, and public agencies have used the CRA to air complaints about the lending performance of individual institutions and to seek redress for their grievances.

Over time, the CRA has come to play an increasingly important role in improving access to credit in both urban and rural communities across the country. Yet, although the CRA challenge is a popular grievance procedure for grassroots organizations, it has rarely worked as originally intended. In fact, by the early 2000s only a handful of the estimated 250 or more CRA challenges have resulted in application denials. Generally, the effectiveness of the challenge process rests with the ability of community groups to win commitments directly from the financial institutions themselves, usually in the form of negotiated settlements to the dispute. These agreements are often quite detailed and spell out the specific steps and action plans the banks agree to take to improve their lending record in the low- and moderate-income neighborhoods in question.

Under the impetus of the CRA, many banks and thrifts opened new branches, provided expanded services, and made substantial commitments to increase lending to all segments of their communities. Despite these successes, the CRA examination system has been criticized by both financial institutions and community groups. Financial institutions argued that policy guidance from the regulatory agencies was unclear, examination standards were applied inconsistently, and that the examination process generated excessive paperwork. Community, consumer, and other stakeholders have generally agreed with the industry that there were inconsistencies in CRA evaluations and that examinations placed greater emphasis on process rather than performance (e.g., actual lending). Community and consumer groups have also criticized the agencies for failing to aggressively penalize banks and thrifts for poor CRA performance.

Amendments to the CRA

While there were a number of modifications to the act over the years, in 1996 a new system of CRA regulations was phased in that was developed in response to these criticisms. The final rule sought to emphasize performance (outcomes) rather than process, to promote consistency in evaluations, and to eliminate unnecessary reporting burdens. The new regulations reduced recordkeeping and reporting requirements, especially for small banks, and made other modifications and clarifications. Under the new regulations, for example, separate evaluation systems were developed for small banks (those with assets less than $250 million), large banks (assets more than $250 million), wholesale and limited-purpose banks (generally those that either do not take deposits or do not have branch operations), and banks that choose to develop their own strategic plan. Large banks would be examined on three distinct tests: lending, bank services (especially those targeted to low- and moderate-income individuals), and investment in their surrounding community (e.g., supporting affordable housing, equity investment in small businesses). Large banks were also publicly required to disclose information about their community development lending, mortgage lending in nonmetro areas, and small business lending. Small banks would be tested mostly on lending and have looser reporting requirements. Banks that chose to develop their own strategic plan were expected to detail how they proposed to meet their CRA obligations. By seeking input from community stakeholders, this approach was intended to allow banks to tailor their plans to more effectively meet the specific needs of their local communities.

Under the rule, community development was also expanded to include activities outside of low- and moderate-income areas if (1) the activities provide affordable housing for, or community services targeted to, low- or moderate-income individuals or (2) if they promote economic development by financing small businesses and farms. As part of the final rule, to be considered a community development loan or service, the activity must have community development as its primary purpose. Activities that are not specifically designed for the express purpose of revitalizing or stabilizing a low- or moderate-income area, providing affordable housing for and/or community services targeted to low- or moderate-income persons, or promoting economic development by financing small businesses and farms are not eligible. The fact that an activity provides indirect or short-term benefits to low- or moderate-income persons does not make the activity community development. As an example, a loan for upper-income housing in a distressed area would not qualify on the basis that the activity provided indirect benefits to low- or moderate-income persons from construction jobs or an increase in the local tax base that supports enhanced services to low- and moderate-income area residents.

Future Prospects

When the CRA was first created, banking was predominantly a local business, largely due to restrictions on interstate banking and branching activities, and banks and thrifts were responsible for the vast majority of mortgages. Thus, the CRA's definition of a bank's community—which was essentially where it has branches and takes in deposits—made sense. Over the three decades since the act was passed, however, the mortgage and financial services industries have undergone significant restructuring. Internet banks and mortgage firms literally offer credit everywhere, industry consolidation has spawned banks with customers (but not necessarily branches) across the country, and nonbanks (e.g., credit unions, mortgage companies), which are not subject to the CRA, vie with banks to offer loans.

Given these changes, bank regulators published an Advanced Notice of Proposed Rulemaking, which noted that while CRA regulations are sound, the act must continually be updated to keep pace with the changes in the financial services industry. Questions, for example, have been raised about the necessity of two key provisions of the CRA: (1) the community reinvestment obligation, which stated that banks and thrifts have a specific affirmative obligation to help meet the credit needs of their communities; and (2) the enforcement provision, which dictates penalties against banks and thrifts with substantial noncompliance ratings. In March 2005, the federal banking agencies published a joint notice of proposed rule making in the *Federal Register* intended to further reduce the regulatory burden on community banks while attempting to make the CRA more effective in encouraging banks to meet community needs. Some of the changes being examined include raising the threshold defining large banks from $250m to $1 billion and creating a middle tier of banks with assets between these limits. These mid-tier banks, like the smaller institutions, would face streamlined examination and would be exempt from many reporting requirements as well as exemption from the rigid three-part test in lending, services, and investments that large banks must follow. While regulators would still scrutinize the investment and services activities of these institutions, they would give the banks more flexibility to decide whether or not these activities made any sense in their specific performance context.

Today, most bankers claim they would do the bulk of what the act requires—providing mortgages and small-business lending—without the CRA because it is profitable business. Yet, despite these changes and challenges, the CRA has had an importance influence on the expansion of access to mortgage credit and banking services to low- and moderate-income individuals. Clearly, while the growth of large and diverse lending organizations will continue to pose significant regulatory challenges for the CRA, the act continues to provide significant incentives for regulated financial institutions to expand the provision of credit to lower income and/or minority communities where they maintain deposit-taking operations.

—Anthony F. Buono

See also Federal Deposit Insurance Corporation (FDIC); Federal Reserve System; Racial Discrimination; Regulation and Regulatory Agencies

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Commutative Theory of Justice

Commutative justice deals centrally with fairness in the exchange of goods and fair participation for buyers and sellers in the system of exchanging goods for payment. Theories of commutative justice articulate the content, processes, social relationships, antecedents, consequences, and boundaries of systems that provide buyers and sellers with fair participation in the exchanges of goods for payment.

Justice is the attribute of being fair to what is properly merited by facts, reasons, and principles. Commutation describes systems of exchange; the economy is a commutative system in which goods are exchanged for payment in a marketplace of buyers and sellers. There is much debate, however, about the content of commutative systems that deserve to be labeled as just. Sellers with significant market power over buyers, for example, may set prices at a level that creates substantial profit but locks out some deserving buyers. One such case is in some segments of the pharmaceuticals industry, where sellers still retain the power to set drug prices but may set them at a level that poor people cannot afford the therapies they need. The counterargument in this debate notes that high prices attract additional sellers and reinvestment so that over time more buyers will be able to participate. In this view, the marketplace adjusts in a dynamic process that is as fair and just as possible.

Some argue that the justice of the buyer-seller exchange can be determined only by the subjective judgment of each participating individual. In this view, free markets based on voluntary exchange are the most just because there is no coercive interference with the individual's subjective perception of what is fair and properly merited by facts, reasons, and principles. This perspective is most notable in the theories of Austrian economics. Seminal thinkers in this tradition include Carl Menger, Ludwig von Mises, and Friedrich Hayek.

Free markets of individuals sometimes are criticized for failing to adequately supply critical social resources such as education, transportation, communication and computing services, nutrition, health care, child care, and clothing. Importantly, each person's ability to access these social resources is likely to enable or hinder their capability to participate as a buyer or seller in the marketplace. Access to these social resources, therefore, is likely to be a significant antecedent of commutative justice, and commutative justice is likely to decrease as the distribution of such resources becomes increasingly narrow. This view emphasizes the sociological and public policy processes that are likely to influence commutative justice. Egalitarianism, utilitarianism, and socialism are normative philosophies often applied by social scientists in this tradition of commutative justice.

It is difficult to develop a positivist science of normative commutative justice consisting of lawful theoretical relationships that can be reliably observed and empirically falsified. This is because justice is an intangible principle of philosophy that is difficult to measure; and each observer's subjectivity and individual normative preferences regarding the definition of justice make reliable and standard measurement very difficult if not impossible. These obstacles to our theoretical understanding may be overcome, in part, by a descriptive approach to commutative justice that focuses on tangible measures of market participation.

—Greg Young

See also Austrian School of Economics; Egalitarianism; Hayek, Friedrich A.; Justice, Theories of; Normative Theory Versus Positive Theory; Socialism; Utilitarianism

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COMPARABLE WORTH

Comparable worth is the theory that states that wages for particular occupations, most notably those traditionally filled by women, should be set by an assessment of the meaningfulness of the work in relation to jobs of similar worth rather than through a market-determined process that often results in lower wages for women in certain jobs. Factors such as education, skills, effort, responsibility, experience, and other relevant factors are all part of a formula to determine the relative worth of a job and the employee is paid consistent with that determination. This avoids the issue of paying employees different wages for jobs based on whether the jobs are male or female dominated and would avoid the limitations of the law only permitting comparison of pay among employees with the same jobs.

In the United States, as virtually everywhere in the world, wages earned by men and women for the same or comparable work are not equal. U.S. figures show that women make 77 cents for every dollar men make. A 2003 report by the U.S. Census Bureau found that the average male working full-time, year-round earned $54,803, while the figure for females was $37,123, or 32% less. A June 2, 2004, Bureau of Labor Statistics (BLS) report concluded that women earn less than men with the same education, at all levels. A 2004 study by Stephen J. Rose and Heidi I. Hartmann found that the 77% figure is actually closer to 44% because the BLS statistics consider only full-time, year-round employees, which accounts for only about 25% of female employees. Roughly 75% of female employees work only part time or go in and out of the labor force to bear or care for children and/or elderly parents.

The wage gap is present in every profession. For instance, on average female doctors earn 58% less than male doctors. According to the AFL-CIO, the average 25-year-old woman who works full-time, year-round until she retires at age 65 will earn $523,000 less than the average working man, and if things continue at the rate that they are presently progressing, women's wages will not be equal to men's wages until the year 2050.

There are many reasons for the wage gap, some of which have nothing to do with intentional discrimination, but according to BLS and other researchers, gender discrimination accounts for a portion of it. Even when males and females have comparable education, experience, time on the job, and other relevant factors, women's pay still lags behind. The 1991 Civil Rights Act called for establishment of a Glass Ceiling Commission to investigate this phenomenon. In 1995, the Commission reported that while women had gained entry into the workforce in substantial numbers, once there, they faced a glass ceiling that prevented them from progressing upward in the workplace and glass walls that channeled them into jobs that had little chance of leading to upward mobility.

The Equal Pay Act of 1963 prohibits employers from paying different wages to male and female employees based on gender. The law requires equal pay for jobs of equal skill, effort, and responsibility performed under similar circumstances. The basis for wage differentials can be quantity or quality of work, merit, seniority, or any factor other than gender, but cannot be solely gender. Title VII of the Civil Rights Act of 1964 also prohibits wage discrimination on the basis of, among other things, gender. However, as Title VII did not contain the differentials of Equal Pay Act's exceptions for wages based on quantity or quality of work, merit, seniority, and so on, the Bennett Amendment was passed to incorporate them into Title VII so that the two laws would be consistent.

However, claims under the Equal Pay Act and Title VII do not address the more persistent problem of entire employment categories being systematically undervalued and thus underpaid because they are predominantly female, that is, secretaries, elementary school teachers, nurses, and clerks (traditionally known as "pink collar jobs"). For instance, in many school districts, the predominantly female positions of secretaries and teaching assistants earn less than the predominantly male category of school janitors. In West Islip, New York, pay for the predominantly male category of groundskeeper begins at $29,000, while pay for the predominantly female category of school nurse starts at $27,000. Similarly, in Denver, nurses make less than gardeners. The Equal Pay Act only allows claims for pay discrepancies in the same jobs; therefore, if the jobs are different, there is not a basis for a claim. Comparable worth gained prominence in 1983 when the district court in the state of Washington found for employees who sued the state on the basis of workplace surveys conducted by the state in 1974, which found wage discrimination in that male-dominated jobs of equal skill, effort, and responsibility conducted in similar working conditions paid an average of 20% more than female-dominated jobs.

Under comparable worth, wages are based on the objective criteria of how much the job is worth to the employer rather than what it is worth based on the predominant gender of those holding the jobs. Factors such as education, skills, effort, responsibility, experience, and other relevant factors are all part of a formula to determine the relative worth of a job and the employee is paid consistent with that determination. This avoids the issue of paying employees different wages for jobs based on whether the jobs are male or female dominated and would avoid the limitations of the law only permitting comparison of pay among employees with the same jobs.

In the Washington case, *AFSCME, AFL-CIO v. Washington*, 770 F.2d 1401 (9th Cir. 1985), Washington State conducted studies of prevailing market rates for jobs and wages for state jobs. It found that female-dominated jobs paid lower than male-dominated jobs. It then compared the jobs for comparable worth and after finding the female jobs paid about 20% less than male jobs, legislated it would begin basing its wages on comparable worth rather than the market rate, over a 10-year period. Employees in female-dominated jobs sued the state for gender discrimination under Title VII to have the comparable worth plan begin immediately. Since the jobs compared were not the same, the case could not be brought under the Equal Pay Act. As mentioned above, the lower court found for the employees and ruled that the state's pay scales discriminated on the basis of gender. The appellate court, however, ruled against the employees, finding, among other things, that since the state did not create the competitive market system used to pay employees there was no illegal gender-based consideration that violated Title VII.

After this case, comparable worth virtually lapsed into disuse because of its failure to create the pay equity envisioned. Determining comparability of jobs is complex, time-consuming, and expensive. It is even more expensive to implement once the wage gaps are found. Since the law does not require such an approach, employers found the theory to be of little value. Under the circumstances, many employees saw little use in pushing the issue, though advocacy groups still try to keep it alive.

—Dawn D. Bennett-Alexander

See also Civil Rights; Diversity in the Workplace; Equal Employment Opportunity; Equality; Equal Opportunity; Equal Pay Act of 1963; Gender Inequality and Discrimination; Glass Ceiling; Just Wage; Racial Discrimination; Women in the Workplace; Women's Movement

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Comparative Advantage

The theory of comparative advantage in economics states that trade between two countries can benefit both countries if each country exports the goods in which it has a relative comparative advantage. David Ricardo coined the term. The principle explains the benefits of free trade.

The example on which the principle was based is very simple. Let us assume that, given the endowment of factors of production (labor, land, climate, capital, etc.), a worker in a foreign land is able to produce one unit of cloth or one unit of wine per day, whereas in the homeland a worker is able to produce four units of cloth or two units of wine per day. On the face of it, the foreign land seems likely to be excluded from trade, as the homeland has an absolute comparative advantage in both products.

However, the inhabitants of both countries will be better-off if the workers of the homeland specialize in producing the cloth and export a part of their output to the foreign land, while the workers of the foreign land concentrate on producing wine and sell a part to the homeland. In the foreign land, the opportunity cost of wine in terms of cloth is 1 (to produce one unit of wine the foreign land has to forgo one unit of cloth, which is what one worker produces in 1 day), whereas in the homeland the opportunity cost is 2 (four units of cloth for two units of wine). It is more profitable for the homeland workers to produce only cloth, in which they are relatively more productive, even though they are also more productive than the foreign land workers in producing wine.

Trade between two countries benefits both if each specializes in the products in which it has a "relative comparative advantage"—the ones it can produce with a relatively lower cost. This argument can be generalized to many countries, factors, and products; the main conclusion remains the same, though the details get more complicated. For example, the existence of more than one factor of production reduces the tendency toward specialization; and transportation costs may interfere with the direction of trade and with specialization.

A good deal of the theory of international trade derives from the theory of comparative advantage. Examples include the following three. The Heckscher-Ohlin theorem establishes that, under certain conditions, an economy will tend to be relatively effective at producing goods that are intensive in the factors with which the country is relatively well-endowed. The Stolper-Samuelson effect says that trade benefits the scarcest factor. The Lerner-Samuelson factor price equalization theorem establishes that, under fairly restrictive conditions, trade leads to the equalization of factor prices internationally, even if factors are not mobile.

Implications for Labor

The theory of comparative advantage leads to some important conclusions for the welfare of nations. Comparative advantage affects specialization of production, volume and direction of trade, prices nations pay for imports and receive for exports, and the income generated for nation's factors of production. Comparative advantage thus affects the standard of living and its growth and the distribution of wealth among a nation's citizens. The income and wealth effects have economic, social, and ethical consequences.

The theory of comparative advantage is a positive economics theory: It seeks to explain the direction of trade (what products each country exports and imports) and the relative prices of goods and production factors. However, it may also become a normative theory: Countries "must" specialize in the products in which they have relative comparative advantage, provided the recommendation is intended to maximize the value of the goods and services produced and consumed. Comparative advantage is, therefore, an argument in favor of free trade. In the example given earlier, both countries will be able to consume more wine and cloth than if they tried to satisfy their demand for both products exclusively with domestic production. The establishment of trade barriers (tariffs, quotas, taxes, etc.) is, therefore, undesirable.

In practice, what is at issue is not the theory of comparative advantage, but its normative implications—the defense of free trade. Discussions of these issues must be based on a proper understanding of the theory and its consequences. In what follows, we briefly present some of those issues.

The theory has important consequences for wage levels, because the competitive advantage of an industry depends not only on its productivity relative to the foreign country but also on the domestic wage relative to the foreign wage rate. In our example, the foreign land has lower productivity than the homeland and must pay lower wages to make its wine production competitive.

Is it fair that workers in the foreign land should earn lower wages than workers in the homeland? The theory of comparative advantage does not address issues of justice. It merely notes that if a foreign land pays its workers higher wages, its products will lose competitiveness. The homeland may even find it worthwhile to invest in wine production and stop buying it from the foreign land.

It is often said that trade makes a country worse off if its workers receive lower wages than workers in other nations—the exploitation argument. Obviously, there may be social and ethical reasons for that argument. But from the point of view of the theory of comparative advantage, the relevant question is whether the workers and their countries are worse off exporting goods based on low wages than they would be if they refused to enter into such trade, because their wages would be even lower.

Of course, it is legitimate to discuss issues of justice regarding relative wages between countries. In any event, the theory of comparative advantage suggests that we should take into account the consequences of any decisions made regarding relative wages. The foreign land government cannot ignore the consequences of a wage increase in its country. And if the homeland government imposes any kind of labor standard on its imports, it will have to consider the effects that this measure will have on the employment of the less productive foreign land workers. And, of course, there is room here for ethical arguments, such as that it is morally unacceptable to take advantage of child labor in underdeveloped countries.

Let us now look at the problem from the viewpoint of the country with higher productivity: Is the competition from the lower-wage country unfair? This is the pauper labor argument, which tends to be used by unions in the industries hardest hit by competition from cheap labor countries. Yet the theory does not support that argument. In fact, in our example, the homeland is more productive than the foreign land in both industries and, although the foreign land's lower cost in wine production is due to its having lower wages, that wage is irrelevant to the question of whether the homeland gains from the exchange. For the homeland, the relevant fact is that it is cheaper, in terms of its own labor, to produce cloth and trade it for wine than to produce wine itself.

This discussion highlights yet another dimension of the theory of comparative advantage—its impact on the redistribution of wealth. Let us assume that the two countries in our example have been autarkic (i.e., self-sufficient and closed to trade with other countries) and now decide to open up their economy to free trade. The homeland's higher productivity in cloth production means that the cloth industry in the foreign land will disappear, while wine production in the homeland will cease to be profitable. (In practice, specialization will not be absolute. There will be some production of wine in the homeland and some production of cloth in the foreign land, according to their endowments of resources, relative productivities, and demands.)

Both countries will end up better-off under free trade, which means that their aggregate income will be higher, although in each country there will be an industry that suffers and will be opposed to free trade. From the economic point of view, the argument put forward by that industry—its loss of income—will be unsustainable in light of the benefits of free trade for the country as a whole. But we must not forget the social and ethical reasons, partly because the productive resources devoted to wine making in the homeland and to cloth making in the foreign land will not be readily redeployable to other industries. In other words, each industry has "specific" factors. In that case, trade benefits the factor that is specific to the export sector but hurts the factor specific to the import-competing sectors. Effects on mobile factors are ambiguous. Again, the theory of comparative advantage must shed light on the discussion, as well as on whatever economic policy measures are adopted.

Other Implications of the Theory

The theory of comparative advantage has sometimes been presented as an obstacle to economic development. If countries "must" specialize in the products in which they have a comparative advantage, and if it is irrational to try to break away from the pattern of trade dictated by the theory, does that not imply a form of economic determinism?

The answer is no: A country's comparative advantages at any given time are determined by its factor endowment (land, climate, natural resources) and its history (labor, physical and human capital, technology). But they may change as a result of decisions concerning saving and investment in physical and human capital, population growth, openness to foreign capital, and so on. Typically, a poor country starts by specializing in whatever it has in greatest abundance—for example, natural resources and cheap, unskilled labor. Low wages attract investments, which generate employment and income. As a result, domestic saving starts to grow. If the financial system develops properly, that saving will be channeled toward the most productive industries, prompting a process of diversification of production. The growth of the stock of capital will increase labor productivity and wages, worker training and education will intensify, and the new investments will be more capital and technology intensive. Thus, as labor costs rise, the initial comparative advantages will gradually be forfeited, while new advantages will be acquired.

This process is neither linear nor simple, but it is the process that many countries have undergone. Naturally, there are winners and losers, and there is sure to be political pressure to try to halt or divert the growth process to the benefit of the status quo. And the ethical arguments will have to be taken into account, too—for example, arguments about the justice of the situations and the changes that take place, about human rights and the freedom of the agents, about environmental protection and the rights of future generations, the creation of new opportunities, and so on.

What years ago was known as the "new" theory of international trade raised the possibility of using active policies to create "acquired" or "artificial" comparative advantages. For example, a tariff on imports may foster the growth of a domestic industry until it is able to exploit economies of scale, generate spillovers into other industries, and acquire a sustainable comparative advantage. Essentially, this is a variant of the infant industry argument (the need to protect new industries from competition in their early growth phases), the economic rationality of which is seriously questioned.

Last, ethics may help rectify misinterpretations of the theory. For example, it has sometimes been argued that developing countries have a "comparative advantage" in their ability to absorb pollution, due to the nature of their environment, the lack of environmental awareness among their population, and the rigidity of their demand for environmental goods. Ethical arguments, however, may help put in its rightful place what is basically a shortcoming of the economic model of humans.

—Antonio Argandoña

See also Child Labor; Developing Countries, Business Ethics in; Development Economics; Free Trade, Free Trade Agreements, Free Trade Zones; Globalization; Income Distribution; International Trade; Most Favoured Nation Status; Natural Resources; Opportunity Cost; Positive Economics; Sweatshops; Tariffs and Quotas; Trade Balance; World Trade Organization (WTO)

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Compensatory Damages

Compensatory damages are those damages (i.e., a financial judgment) awarded by a court that are intended to reimburse an injured party for the harm caused by the actions of another. These damages are awarded in a wide variety of legal actions (e.g., torts, breach of contract, wrongful termination) and include harm caused to a person's property, personal well-being, and/or financial interests. For example, if a plaintiff is injured in an automobile accident caused by the reckless driving of the defendant, then the defendant may be required to pay an amount intended to place the plaintiff in the same position he or she would have been in had the accident never occurred. That is, the defendant may be required to pay the plaintiff's medical bills, lost wages (from missing work due to the accident), and an amount to cover the plaintiff's intangible pain and suffering. Compensatory damages do not include "punitive damages," which are monetary damages intended to punish the defendant for intentional or grossly negligent actions.

In a breach of contract case, on the other hand, the party breaching the contract (the defendant) must pay damages to the nonbreaching party (the plaintiff) such that the plaintiff is in the same position he or she would have been in had the defendant not breached the contract (also known as giving the plaintiff the "benefit of the bargain"). In some cases, these damages include "consequential damages," which are damages that are indirectly related to the breach of contract but are a foreseeable result of breaching the contract. This is demonstrated by the classic 1854 case of *Hadley v. Baxendale*. In that case, the plaintiff hired the defendant to take a broken crankshaft from his mill into town for repair. The defendant promised to return the crankshaft the following day, but the delivery was delayed for several days. During this time, the plaintiff was unable to operate his mill. The plaintiff filed a lawsuit seeking compensatory damages that would put him in the same position he would have been had the contract not been breached, which included the consequential damages of lost profit due to the mill being shut down for those additional days. In this particular case, however, the defendant was not required to pay the additional, consequential damages because it was not reasonably foreseeable that the entire mill would have to be shut down during his delay (i.e., the defendant may assume that there were other problems with the mill or that the plaintiff had an additional crankshaft). Had the shutdown of the mill been foreseeable, however, then the compensatory damages would include the lost profits.

Compensatory damages play a vital role in ensuring that actors invest in preventative measures efficiently. From a law and economics perspective, the goal of our tort system, for example, is to minimize the total costs of accidents (i.e., harm suffered) and actions to prevent accidents. Society is better-off if the costs of prevention are less than the costs of an accident occurring, but society is worse off if the preventative measures are greater than the benefits they provide. By requiring the defendant to compensate injured parties for the harm caused by their actions, the legal system provides incentives for actors to efficiently invest in preventative measures. Likewise, in contract law, requiring the defendant (the breaching party) to pay compensatory damages to the nonbreaching party allows for so-called efficient breach. Under the idea of efficient breach, if the defendant can benefit more from breaching the contract but also paying the plaintiff his or her expected "benefit of the bargain," then we have reached a Pareto superior result. The concept of efficient breach is not without criticism, however. For example, it may often be the case that the plaintiff is not indifferent between a compensatory damages award and performance of the contract and, therefore, is made worse off by the defendant's breach.

—David Hess

See also Economic Incentives; Negligence; Punitive Damages; Torts

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COMPETITION

Competition is a process in which individuals strive to achieve mutually exclusive positions, such as the attainment of a single reward. Competitive processes may be among individuals within a single business, or it may be among businesses. Decision making in a competitive context tends to emphasize the efficient accomplishment of self-interested goals. Governments often intervene in competitive processes with laws and regulations to influence competitive processes and outcomes.

This entry discusses issues of efficiency, justice, human rights, and public policy associated with competition. The trade-offs and debates surrounding these issues are likely to intensify as the global economy becomes increasingly competitive and rival businesses seek to outdo each other by harnessing genomics and nanotechnology for their own advantage.

Competitive Allocation of Resources

A key outcome of competition is the allocation of resources in a marketplace where supplies are limited or scarce. A business conducts its activities in an environment of scarcity—scarce supplies, scarce skills, and scarce channels to the customer—and it may confront other organizations dependent on access to the same scarce inputs. In this context, competition allocates scarce resources among businesses based on the relative advantages of each to create value for potential suppliers and customers.

Businesses that are lucky, skillful, or endowed with advantages in the competitive process expend less capital, time, and effort to operate their value-creating activities. Conversely, competitors with relative disadvantages in an environment of scarcity are not able to operate with comparable scale, scope, efficiency, and quality. In this way, competition between businesses is the conduct of interdependent organizations striving for mutually exclusive positions of advantage to create value so that the success of one comes at the expense of another.

One consequence of competition is that rivals may bid up the prices for valuable and scarce inputs they demand for their activities. In an economy that equilibrates supply and demand, more supply of these inputs is offered as their prices are bid up, and competitors are provided with more inputs to produce a greater quantity of valuable goods and services. The process seemed to Adam Smith as if an invisible hand guided productive resources for social progress.

Another consequence is that competitors strive for relative advantage in forming valuable relationships. For example, competition may cause a rival to invest in product innovation, extend warranty programs, develop new channels for convenient shopping and delivery, customize service, and enhance the postsales customer experience. In competition, a successful seller must remain alert to opportunities for strengthening the unique value it brings to a potential customer relationship.

Business competitors, each motivated by self-interest to capture profit, also strive to outdo each other to form and protect attractive relationships with suppliers. For example, a rival might offer to share proprietary technology with its suppliers, train suppliers' personnel at no cost, enter long-term contracts, or provide suppliers with development funds.

In these ways, competition appears as an intendedly efficient process of struggle for advantageous position to reduce scarcity and strengthen the creation and distribution of value in society. Business competitors, motivated by self-interest to capture profit, constantly strive to outdo rivals by forming and protecting increasingly attractive relationships with customers and suppliers.

Public Policy Issues

At some times in some places unregulated competition may lead to unserved needs and unintended consequences. One function of government is to regulate the actions of business so that their competitive pursuit of advantage is not at the expense of the public good. Typical government regulatory controls on competitive action target the effects on the environment, safety, health, and property. For example, antitrust regulations limit consolidation within industries to encourage the social benefits of competition, commerce regulations govern the actions of competitors within industries to ensure fair trade, and some regulations may be used to raise or lower barriers against the entry of new competitors. In the United States, for example, broadband communications is subject to regulations restricting competitors in the cable industry from either consolidating or realizing exclusive advantage from their own investments in cable assets.

Barriers can be a factor in an industry's competitive structure. In this vein, licensing regulations are an example of a regulatory barrier to competition. In the United States, for example, there are more than 500 occupations that require licensing. Licensing may facilitate honest and fair exchange by monitoring and controlling quality and standards. Conversely, licensing may be a barrier that limits competition, economic opportunity, and wealth creation. For example, occupational licensing has sometimes limited the supply of hairstyling salons for minorities in some areas of the United States because the local certification requirements excluded the hair needs of the minority groups. This is an example of a regulatory limit on competition that affects the fair distribution of goods and services to all segments of the community.

Some businesses may seek to participate in the public-policy-making process to influence the scope and magnitude of the regulatory constraints on their competitive conduct. Mechanisms for their participation include organizing in trade associations and supporting autonomous advocacy groups for research, information dissemination, lobbying, and political donations. Though competitors in business, they may cooperate through these mechanisms to persuade legislators and regulators to pass laws and regulations that are favorable, and to defeat those that are unfavorable, to the special interests of the participating businesses.

Business participation in the public-policy-making process, motivated by the competitive struggle for advantage, may have both good and bad consequences. For example, participation that increases the use of reliable information in the process is likely to enable better policy decisions than could be expected from a relatively uninformed process. Conversely, the pursuit of self-interested advantage may motivate some competitors to corruptly "capture" governments by coercing or compelling the public policy decision makers to align with their special business interests against the interests of other public policy participants and citizens.

Problems of Global Competition

The dynamics of global competition compel business activities to locate in geographic areas where scarce supplies can be acquired and deployed most advantageously. As comparative advantages among geographic areas change and businesses relocate their activities, the changes in the quality of life in local communities may lead to calls for social protection. These dynamics highlight the temporal dimension of social welfare in those areas where competitors are engaged and the need for competitors to demonstrate responsibility in both the short and long terms as the process unfolds across multiple geographic areas.

When competing on a global scale, a significant challenge for managers is to effectively and fairly balance the interests of stakeholders in both the home and host societies. This situation has potential conflicts of interest, created when one individual has an explicit responsibility to one party and simultaneously has an incentive to serve inconsistent interests of another. The efficacy of competition as a process to create value and increase social welfare in this situation is put at risk. Calls for government regulation on business may become more frequent if competition disrupts traditional lifestyles and sustainability of communities.

Other Social Concerns

Competitive conduct arises from the decision making of competitors responding to their perceptions of opportunities to create value. Decision making that is misinformed, grounded in uncertainties, or unable to efficiently adjust to the information of the marketplace may lead to surpluses and shortages. Factors influencing these outcomes include the magnitude of profit that satisfies their motive for competitive conduct and their responsiveness to trade-offs between profit and commonly accepted definitions of basic human rights. The paragraphs below consider issues of just distribution, human rights, and social efforts to lessen the potential harms from competitive failures.

Competition and Distributional Justice

Cognitive constraints on competitive decision makers may, even without unjust intent, produce unjust distributions. For example, self-interested competitors may pursue a "cherry-picking" strategy in which they first rank-order potential customers based on their value and then serve the most valuable in the order until the capacity of the seller is exhausted. This strategy leads to underserving the least attractive segments of need.

Absent any regulatory constraints, for example, private health care providers in a community may compete, but still may leave unsatisfied a portion of the community's need for care (e.g., care for the uninsured) even while abundantly serving another portion (e.g., care for the insured). This situation, common in the United States, focuses attention on the strength of profit and the weakness of distributive justice as motivators of competition in free markets. Furthermore, this example illustrates that the principle of appropriable value embedded in unregulated competition may not consider all social costs in its accounting.

Article 25 of the United Nations' Universal Declaration of Human Rights lists access to health care as a basic human right. In this view, the inability of competition to produce a sufficient supply of health care to satisfy the entire need, including the need of those unable to pay a market price, points out a fundamental deficiency of competition. Related basic human rights include (but are not necessarily limited to) food, housing, clothing, education, information, and transportation. Those who view competition as conduct that does not fairly distribute the basic necessities of human rights often call for constraints on self-interested autonomy in business decision making. Socialism is an alternative system intended to introduce such constraints. There are many forms of socialism, ranging from fully centralized planning of production to more mixed economies, which attempt to blend the benefits of competition with public welfare interests.

Subsidies for Competition

Subsidies, financial assistance given by one person or government to another to serve some private or public purposes, can be one mechanism of a mixed economy to ensure broad participation in competitive processes likely to have beneficial social consequences. For example, a national government may subsidize private sector research and development to ensure the home country's ability to compete in high-technology global markets; or it may subsidize its domestic farm community so that it can compete in world food markets.

The recipient of a subsidy could apply it to reduce its internal cost of business or pass it along to its buyers in the form of lower prices. In markets that are not perfectly competitive, however, either approach may lead to a distortion of the competitive process for determining prices. This calls attention to the ethical issues related to fair bargaining and determining a just price in a marketplace that mixes competition with subsidies.

The justice with which costs and benefits are distributed is a consideration when evaluating government-subsidized competition. For example, a subsidy recipient may externalize environmental and public health impacts and fail to consider the fairness or justice associated with burdening third parties with these costs. Similarly, subsidies may go to businesses with large existing endowments and leave out small poorly endowed businesses that have no other means to enter the competitive arena; or a business may organize strictly to benefit itself by the amount of the subsidy rather than to establish the value-creating competitive activities that were the intended economic purpose of the subsidy.

Competition as Action: The Precautionary Principle

In the 21st century, business competition often takes the form of a race to commercialize innovative technology. Examples of these competitive races include the pursuit of opportunities created by rapid advances in sciences of genetics and nanotechnology to resolve great problems of scarcity in access to food, organ transplants, and pharmaceuticals. Many individuals and organizational stakeholders are concerned, however, that the pace of innovation in these areas exceeds our capabilities to determine the consequences prior to commercialization. There are risks to be first to commercialize innovations. Not only are there potential technical and market failures but also potential costs to litigate and resolve harms to health, safety, or the environment.

These concerns have led some to urge business to voluntarily restrain the pace of competitive action in their strategies for genetic commerce. This "better safe than sorry" approach to competition, called the precautionary principle, lets others try to prove novel approaches, and then quickly copies the ones proven safe, effective, and valuable. The principle, however, is highly contested by some business stakeholders. It has been called antiscientific, forcing business to offer proof against every allegation of harm. Many competitors argue that uncertainties will never be completely resolved, and it is the job of independent scientists to monitor human health and the environment for signs of harm. In competition, businesses strive for positions of advantage. One approach to capture advantage is to act before rivals—to be the innovator—and then to protect the position with patents and long-term contracts.

Advocates on both sides, however, recognize that the precautionary principle's key test will be in the regulatory context and economic incentives of competition. The rapid pace of scientific discovery makes the balance between commercializing innovations and the precautionary principle an increasingly important dimension of business competition.

Intra-Organizational Competition and Legal Compliance

Compliance with law and regulation is important in countries with developed and enforced legal systems governing competition. Competition within organizations also may be governed. For example, the integrity of internal competition for job promotions may need to demonstrate compliance with legal requirements such as equal opportunity rules in the United States. To ensure integrity of competition within a business, formal processes must address the honest reporting of information, fair and diligent analysis according to standard practice, and visibility for independent monitoring. When the intensity of competition within an organization may cause some to violate, or witness violations of, informal standards for integrity, then the desirable traits of trustworthiness and virtue become increasingly important values. Neutral ombudsmen, hotlines, recruiting, training, and codes of ethics are examples of mechanisms that organizations may use to increase alertness, monitoring, and appropriate resolution of threats to competitive integrity.

Competition, Cooperation, and Individual Decision Making

Attention to the competitive context, or "rules of the game," is useful to understand the ethics of strategic decision making in competition. Game theory, an approach for gaining insights into strategies of decision making constrained by rules, offers a widely known model of the context of competition—the prisoner's dilemma. The prisoner's dilemma illustrates that the outcomes of competition may depend on the instrumental ethics embedded in the rules of the competitive processes. These include trade-offs between social accounting and private interests in the governance of competition and competitors' reputations for honesty, integrity, fairness, and virtue.

In this competitive game, two prisoners not yet convicted are held by a judicial system in separate prison cells. They are not allowed to communicate with each other. The prosecutor wants convictions with minimal expense, and she of he offers a reduced sentence for the prisoner who confesses and testifies against the other. At the same time, the prosecutor promises an extremely long sentence for the prisoner who does not confess. If both confess, however, the testimony is not needed and will not be rewarded. The prisoners are given the sentences for each possible decision. The prisoners cannot change their decision once made and they cannot confer with each other.

The prisoners each see that the total time they will spend in prison is the least if they both do not confess (4 years for the first and 4 years for the second equals 8 years total). Prisoner 1 sees a risk of receiving a 15-year sentence if Prisoner 2 decides to confess. Without the benefit of additional communication, Prisoner 1 will receive a lower sentence by confessing no matter what Prisoner 2 decides (10 instead of 15 years for Prisoner 1 if Prisoner 2 confesses; 1 instead of 4 years if Prisoner 2 does not confess). Thus, Prisoner 1, competing for the lowest sentence, confesses.

Prisoner 2 sees the same logic from her or his cell. No matter what Prisoner 1 decides, Prisoner 2 gets a lighter sentence by confessing. Not so regrettably, perhaps, the logic of competition in this game leads both prisoners to confess. From the prosecutor's perspective, the cause of social justice could not have been better served—the criminals will be in prison for the longest combined sentences possible given the alternatives.

In addition to its suggestion of an interesting prosecutorial technique, the game offers two major insights into the ethical principles of self-interested decision making in a competitive context. These principles address the interest of society relative to that of the competitors and the value of reputations for reliable trustworthiness and, surprisingly, for vengeance. The first insight is that more social welfare is created (the longer combined sentences when they both confess) when competitors cannot communicate with one another. If they are permitted to communicate before they make their choice, they may arrange to collude with each other by agreeing "not to confess." Collusion earns the best outcome for the competitors under the circumstances, though it is to society's detriment.

The second insight is that competitors' (i.e., prisoners') mutual interests are best served when they may be trusted to forbear and trade fairly. One may be exploited, however, by a self-interested competitor willing to defect from the position of mutual forbearance. It follows, then, that there are advantages to be gained from cooperation when competitors have known reputations for reliability and trustworthiness.

Conclusion

Competition as a process to allocate scarce resources has been praised for its efficiency and criticized for its amoral focus on short-term self-interest. Some people believe social progress is best served when the smooth functioning and integrity of competition is supported by government institutions and regulation. Others prefer to use public policy and nongovernmental organizations to create alternatives to competition that they believe will better serve the needs of a fair and just society. This debate is likely to intensify as the global economy continues to affect the lives of more of the earth's people.

—Greg Young

See also Barriers to Entry and Exit; Conflict of Interest; Corporate Social Responsibility (CSR) and Corporate Social Performance (CSP); Game Theory; Global Business Citizenship; Human Rights; Invisible Hand; Justice, Distributive; Mixed Economy; Prisoner's Dilemma; Rawls's Theory of Justice; Regulation and Regulatory Agencies; Socialism; Subsidies

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Comptroller of the Currency

The Office of the Comptroller of the Currency (OCC) is the federal government agency responsible for chartering, regulating, and supervising national banks in the United States. The primary mission of the OCC is to ensure the safety and soundness of the national banking system. The OCC achieves this mission by employing a nationwide staff of examiners who conduct onsite reviews of national banks and continually supervise bank operations. The agency issues rules and legal interpretations concerning bank management, bank investments, bank lending activities, and other aspects of bank operations.

The OCC was established in 1863 under the National Currency Act. This act created a system of nationally chartered banks to issue standardized national bank notes. The OCC was established to administer the new banking system. The law was superseded by the National Bank Act, which authorized the Comptroller of the Currency to hire a staff of national bank examiners to supervise and examine national banks. The act also gave the OCC authority to regulate lending and investment activities of national banks.

The OCC is an agency of the U.S. Department of the Treasury based in Washington, D.C. The OCC is headed by the Comptroller of the Currency, who is appointed by the president, with the advice and consent of the Senate, for a 5-year term. The Comptroller also serves as a director of the Federal Deposit Insurance Corporation (FDIC) and as a director of the Neighborhood Reinvestment Corporation.

The OCC regulates and supervises more than 2,200 national banks and 56 federal branches of foreign banks in the United States. The OCC regulates and supervises only banks with a national charter. Banks chartered by individual states are regulated and supervised by state banking authorities or the FDIC. The Federal Reserve Board regulates and supervises bank holding companies and foreign-based affiliates.

OCC bank examiners review the activities of national banks and assess the safety and soundness of banks. In conducting their safety and soundness reviews, OCC bank examiners assess the bank's exposure to various risks including market risk, credit risk, liquidity risk, and legal risk. OCC examiners review bank lending procedures and bank investment portfolios to ensure that the risks associated with these activities are identified, measured, and managed properly. OCC examiners also review bank funding operations, the level and quality of bank capital, bank underwriting standards, the quality of bank earnings, and compliance with consumer banking laws. OCC examiners also review the bank's internal risk management controls and the bank's performance of fiduciary duties.

In addition to conducting safety and soundness bank exams, the OCC has other regulatory duties. These duties include reviewing applications for new bank charters and branches. The OCC also has the authority to take enforcement actions against banks that do not comply with banking laws and regulations. The OCC has the authority to remove bank officers and directors and can promulgate rules and regulations under the authority of the National Bank Act governing investments, lending, and other practices of national banks. The OCC also provides written guidance to the industry in the form of banking circulars, bulletins, and interpretive releases.

—*James A. Overdahl*

See also Federal Deposit Insurance Corporation (FDIC); Federal Reserve System; Regulation and Regulatory Agencies

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Computing, Ethical Issues in

Computer ethics deals with new ethical issues that distinctly arise out of the use of computer technology. This focus excludes, for instance, the ethical assessment of embezzlement even if carried out with the aid of a computer, since the discussion of computer-based embezzlement hardly differs from traditional discussions of theft. In contrast, an assessment of computer hacking raises some distinctive issues. Although hacking initially resembles a traditional act of misappropriation, it also raises special issues in computer ethics dealing with how one assesses the level of responsibility that lies with the supposed victims that permitted some amount of open access to their computers. That is to say that the open environment for Web-based file sharing has created a context where is it not clear when and to what extent a hacker may assume that a resource may be viewed as open to public use. Hacking draws our attention to distinctive issues in computer ethics concerning the separation of personal and public resources in cyberspace.

Issues in computer ethics typically affect choices in the design of computer technology, in the management of computer systems, or in the formulation of public policy that responds to computer technology. An example of a design issue is the decision by major providers of operating systems to accommodate Web sites that place “cookies” to record personal information on a user’s hard drive, which is then accessed when the user revisits the site. The ubiquitous presence of cookies has a significant impact on the notion of personal privacy in computer use. An example of a management decision would be the establishment of a standard for password access (including length of password and frequency of password revisions) for access to sensitive data, with consequences for the assessment of responsibility when data are compromised. An example of a public policy issue is whether and how online purchases may be subject to local or state sales, with consequences for a wide range of economic practices with socially sensitive consequences. Most issues (for instance, issues of privacy) are also the subject of ethical inquiry on their own.

The issues that are debated under the rubric of computer ethics have evolved in step with the history of the computer industry. The ongoing disputes over the ethical significance of intellectual property claims provide a simple example. As the software industry grew in the1970s, there were doubts about the appropriateness of various forms of property protections. Those debates contributed to the public policy standards that were more or less established in the 1980s as copyrights become the most common form of protection, while patents were accepted under certain conditions and specially customized forms of protection (so-called sui generus protections) were seen as unappetizing. Even though some ethicists still have qualms about the social values inherent in those standards, the debate over the alternatives seemed resolved by statutory law. At the same time as those policy issues were being settled, a rising emphasis on home, desktop computing focused attention on a new set of property issues, including the validity of shrink wrap contracts and the availability of protections for the look of popular user interfaces. In time, policy guidelines again set these issues as well. Not surprisingly, however, new shifts in computer technology continue to raise new sets of property issues. At the present moment, the widespread use of the Web-based file sharing has, for instance, raised the question of secondary responsibility of file sharing facilitators for copyright infringements carried out by their clients. In each instance, ethicists have entered into the public policy debates with concerns for the social values inherent in how policy decisions will structure the new industries. There is every reason to expect that the innovations of this rapidly changing technology will continue to be mirrored in unexpected ethical dilemmas.

The present overview of computer ethics sets out a fairly standard categorization of areas of ethical debate and identifies issues within those categories. It is entirely reasonable to expect that technological developments and changing public policy decisions will alter the boundaries of these categories and shift the focus of “hot topics.”

Access to Resources

The buzzwords *digital divide* and *digital society* draw attention to a potential for ethically sensitive, social inequities in access to computer resources. Computer use is presently essential to all commercial enterprises in industrialized countries, and it is rapidly becoming more of a social necessity than simply a convenience for personal use. In this environment, the inability to use or lack of access to a computer at a reasonably level is a major social handicap. The divide is alternatively based on economic, geographic, and educational resources, raising serious ethical concerns in all areas.

In 2005, in the United States, a home computer with rapid Web access is economically beyond the means of over half of the population. Given that everything from job searches to bill payment is becoming computer based, that portion of the population is seriously cut off from economic opportunities. This digital divide thus aggravates the social inequities that are already present in an industrial culture. A serious ethical argument can thus be made for a personal right to basic computer resources on the same level as a right to a basic education. The divide is further aggravated by geographic constraints. There are, for instance, fewer computer resources available in remote geographic areas or in unindustrialized countries. The divide thus aggravates the disadvantages of the unindustrialized countries.

The ethical dilemmas are highlighted by recent debates over the introduction of wireless Web access in both commercial and public spaces. At present, a number of public advocacy groups have urged communities to provide free wireless access as a way to bridge the divide. This solution, however, is a shift from a commercial service to a public service that both interferes with commercial opportunities valued by private providers and frightens public officials worried about a new category of potentially expensive social entitlements. The argument furthermore depends on a distinction between basic computer services (perhaps deserved as a social entitlement) and premier services (perhaps a commercial product) that is as hard to define for computer uses as it is in the continuing debates over the quality of state-supported education.

The divide also raises ethical issues for those who propose broadening socially sensitive computer uses to include options such as e-voting in public elections. Obviously, that process will be more comfortable and more acceptable to those with computer experience, raising concerns over the effects of e-voting on the makeup of the active electorate. This same issue will be reflected in computer-based publication of public documents, and it is aggravated by concerns for the accuracy of computerized translations of those documents.

Privacy and Surveillance

In the early years of computer use, there was considerable discussion of a potential loss of individual privacy inherent in the maintenance of large computer databases. The fear was that databases of automobile licenses, of educational loans, of tax payments, and so on would be cross-referenced, with the potential for the construction of detailed profiles of individuals. A number of institutions proposed guidelines on access to databases that were intended to prevent the appearance of a data mining "big brother." For instance, the United Kingdom Data Protection Act of 1984 demands that data files be classified by their specified purposes and that those files only be accessed for those specified purposes. Although those issues continue to attract attention, many of the protective guidelines are now routinely ignored without significant public protest, especially when sophisticated data mining has led to the identification of tax evaders, fraudulent charities, and so on.

Recently, the debate over privacy has turned more to issues relating to several varieties of "tracking" software, including highly sophisticated "spyware" programs. The most obvious examples involve the creation of individual profiles from records of credit card or Web use. A leading commentator tells a true story of how a nonpurchase visit to an online cigar vendor led to a challenge from a medical insurance company to an individual's claim to be a nonsmoker. The issues become more sensitive as the Web-based activities become more commonplace. When pornography, for instance, was published in hardcopy magazines and purchased with anonymous cash, it was very hard for censors to identify individual customers. If the Web becomes the primary means for the distribution of pornography, then sophisticated tracking programs make it possible to identify those users. By expansion, there is a real possibility for high-level overview of individual reading preferences.

The issues are complicated by a notable difficulty in drawing a line between public and private life and in identifying the levels of privacy expected in these ill-defined realms. If, as a presently popular argument suggests, privacy is valued as a basic for intimacy that is central in human life, then it becomes much more important to preserve the expectation of privacy in electronic communication between individuals (private life with an expectation of intimacy) than in commercial transactions (public life). The distinction is hard to maintain in practice. Two examples will make this clear. Consider a divorce court asking the operators of a standard Web search engine to release information on a plaintiff's request for maps and driving instructions. It is unclear whether such information is part of private or public life, whether it is owned by the user or by those who offer the map services, or whether an individual's expectation of privacy deserves special recognition. Second, consider the routine corporate practice of reviewing network-based social correspondences between employees. Although there is an intuitive feeling that social correspondence is not the concern of corporate system operators, the practice is justified by the fact that trade secrets can be compromised through uncontrolled social correspondence. These ethical examples show not merely that the issues of surveillance and privacy are especially sensitive in computer contexts but that they raise immediate concerns for the professionals who maintain or manage the computer systems. The issues are even more complex when data files are held in cross-national locations with differing legal codes and ethical traditions.

The issues affect decisions on the production of computer technology, which can be produced to permit or preclude external investigation of individual use at several levels. The new emphasis on wireless Web access promises to raise a new set of issues concerning the expectation of privacy.

Software Property

Although there is a popular prejudice for the recognition of a "natural right" of software producers to their creative efforts, modern analyses of intellectual property policy eschew claims for natural rights and treat software property as public policy designed to encourage a variety of social goods. Whether gaming programs deserve copyright or patent protections is, on the standard analysis, not a question of whether the producer has a natural right to own his or her production, but a question of whether those protections create a legal context that is for the good of society. In the broadest possible terms, the social goods at question typically include an interest in a vibrant economy with a strong commitment to software research and development. Within this broad outline, however, there is obviously a great deal of room for alternative ethical ideals.

As a simple example, we may consider the term of protection under copyright and patent protection in the context of a claim for ownership over a digitized file. With many exceptions and qualifications, copyrights generally provide a lengthy 75-year term of protection while patents provide a mere 17-year term of protection. The historical basis for this difference is that patents cover items of industrial value while copyrights cover items of literary value. The common wisdom is that the economic consequence of long-term protections of industrial items is likely to harm the expansion of industry, while there is little to fear economically from long-term protection for literary items. This tradition suggests that form of protection for a file depends on whether that file has a literary or applied use. But the distinction is impossible to maintain in computer environments. It would create a legal morass of incredible complexity to ask of each interactive program whether it is a pass-time game or a piece of an industrial process. The choice between copyright and patent protection had to be addressed in broad and general terms for the software industry in the 1970s, not for each individual piece of the software. Even though the long-term effect of copyright protection is problematic for software that generally has a short shelf life, other issues, particularly the bureaucratic ones of copyrights application, made copyrights seem the better alternative for the software industry.

The example draws attention to how ethical and social issues underlie the debates over property issues in the computer industry. The example draws attention to the underlying value of industrial progress, with a hidden assumption that progress is encouraged when industrial items enter the public domain fairly rapidly. Taking this argument for short-term protections to the extreme, it has been argued that even 1 year of software ownership restriction has the potential for interfering with software development and that, therefore, all software should be open and free to all users. Taking the argument in the opposite direction, it has been argued that long-term restrictions that enrich successful software developers encourage continuing software development by placing economic resources in the hands of those whose past successes show the potential for further software development. The argument is both an economic dispute over the distribution of wealth and a dispute over free access to inventive science, both issues of long-standing concern to ethicists.

Present debates over the levels of property protection continue to be grounded in economic assessment. But when music, movies, industrial processes, commercial data, and machine designs are all recorded in digital format, it becomes increasingly difficult to design property policies based on distinctions between the level of economic protections that is needed to encourage research, creation, or development. Intuitively, it would seem that a movie industry that invests huge sums in the production of individual works deserves a higher level of protection than the music industry. Intuitively, it would seem that customer lists produced from ordinary business records are protected differently than inventive designs that lead to new industrial products. But when the issue in all cases is access to a digital file, those differences are hard to maintain. The consequence is that public policies cannot appeal to distinctions that seemed intuitively important to past ethicists. For the moment, intellectual property policy is undergoing a deep social and ethical reassessment at many levels.

The issues pertain directly to ongoing technological research and policy studies, creating serious dilemmas for system developers and operators. Under the general rubric of "digital rights management," new techniques are under development for the control of access to digitized information. The developers confront a difficult ethical-technological problem of developing systems that both prevent overzealous infringement of property rights while still permitting the "fair use" rights of the public to appropriately open uses.

Professional Responsibility

Questions of personal and group responsibility for acts are tied to the debates over the definition of the "computer professions" and to proposals for "codes of conduct" for those purported professions. The basic point can be made in a comparison of a computer profession to an established profession such as medicine. In a case of improper medical care, a licensed medical doctor is held to a high standard of malpractice, while a layman is held to a lower standard of negligence, with some intermediate standards applying at intermediate levels of expertise. If computer personnel establish themselves as professionals, presumably they establish a high standard of malpractice against which to judge their failures. The malpractice standard in medicine is justified not merely by the level of technical education that is assumed of medical doctors but moreover by the level of ethical education in matters such as patient expectations, social expectations, and knowledge expectations that are set out in a number of significant medical codes of conduct. If computer programmers are to rise to that standard, it will be, in part, through the formal establishment of a code of conduct for programmers.

Given that it is hard to identify even the various fields of expertise that comprise the still youthful computer industry, it is obviously difficult to sort out who might be seen as a professional in what professional specialization. Are "data analysis" and "knowledge management" distinct professions deserving distinct codes of conduct or are they subsumed under "information technology" with a single code of conduct? Is "Web maintenance" professional practice or nonprofessional labor? Placed in the context of professional responsibility, these questions of categorization have significant ethical content. Insofar as we lack a sense of how to approach these questions, we have a hard time treating computer technology as a profession and a hard time assessing the appropriate level of responsibility to which we hold various computer practitioners. All the same, professionalization must begin somewhere. Several computer societies, including the popular Association for Computer Machinery, explicitly recognize that the formulation of a distinctive code of conduct is a central piece of a claim to be a professional organization.

Most of the large "professional" societies that focus on computer-related practice (notably the Association for Computer Machinery, the British Computer Society, the Institute of Electrical and Electronic Engineers, and the Institute for the Management of Information Systems) have either a "code of ethics" or a "code of conduct." The choice of terminology reflects an ongoing debate over the ethical significance of codes. Although the distinction is often ignored in practice, some ethicists suggest that a code of conduct is akin to a legal system enforced within a jurisdiction, while a code of ethics reflects an assumed personal moral commitment by the organizations members. The specific content of the codes reflects a number of ethical debates. To a certain extent, there is consistency in content across codes. All the codes, for instance, demand recognition of social welfare and forbid acts that cause social harms. This consistency, however, does not diminish the ethical debates inherent in that content. There is serious ethical disagreement over whether a professional status entails a positive duty to provide for social good, or more simply a negative duty to refrain from social harms. A close reading of the codes shows somewhat different attitudes on these duties, reflecting serious debate among the membership involved in authoring or authorizing the codes.

Politeness

There are a range of issues concerning everyday use of computer resources that do not fit neatly into the above categorization, either because they touch on several sorts of issues or because there is disagreement over how they should be viewed. These issues are generally viewed as a matter of computer politeness rather than as deep social problems. It is impossible to give a comprehensive overview of these matters. Two examples can suffice to show the complexity of these matters.

There is debate concerning interference with computer use, from the serious threat of destructive viruses to the nuisance of unwanted computer-based advertising. It is easy enough to condemn the pernicious spread of viruses. It is harder to ethically assess the nuisance of unwanted e-mails. To some extent these issues can be subsumed under the "privacy" rubric. A complaint from a homeowner about a noisy, barking dog or late-night door-to-door salesmen would traditionally be seen as a complaint about an invasion of privacy. Although aggressive pop-up advertising may similarly be seen as an invasion of privacy, it has generally been viewed as an impolite nuisance of secondary importance to more basic privacy issues. This does not mean that "spam" and "pop-ups" are ignored by ethicists. There is need for a sense of the social and ethical limits to such behavior. These issues are most deeply felt by network designers who can either block or permit a certain level of intrusion, and who feel the need to do this at an appropriate, although as-yet-undefined level. A closely related issue concerns the appropriate level of use of computer resources. It is not clear, for instance, if it is appropriate to make use of any unguarded wireless access to Web resources that may happen to be available for whatever reason.

There has been considerable discussion in recent years of censorship or free access to lewd stories, violent or hate speech, and culturally unaccepted levels of nudity. As so many ethical issues, they become aggravated in a Web context that opens speech across national boundaries with very different mores. The most ordinary sort of advertising image from one culture may be shockingly offensive in its nudity when viewed from in another culture. Hate speech that is protected in one country may be banned in another. One special problem for computer ethics is whether cross-cultural availability should be considered when addressing local matters.

—John W. Snapper

See also Codes of Conduct, Ethical and Professional; Digital Divide; Electronic Commerce; Electronic Surveillance; Intellectual Property; Internet and Computing Legislation; Privacy

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Conference Board, The

The Conference Board is a global business membership and research organization that provides its members the opportunity to access pragmatic research and exchange ideas on global business trends, issues, standards, and best practices. Its mission is to create and disseminate knowledge about management and the marketplace to help businesses strengthen their performance and better serve society. It is the Conference Board's commitment to service and to shaping values that is of particular interest to those concerned with business conduct and corporate responsibility.

The Board's current membership, which includes many Fortune 1000 companies, is made up of nearly 2,000 in 61 countries (as of 2005), including the United States, Canada, Latin America, Europe, Asia-Pacific (including China and India), the Middle East, and Africa. The annual subscription fee, which provides members access to global networks of other corporate leaders and research by economic and management experts in business, government, and academia, is based on the size of the company.

History

The Conference Board was founded by business leaders as a nonprofit entity in 1916 in response to the public's lack of confidence in business and rising labor unrest. During the next several decades, the Board established the first Conference Board Council of Human Resources Executives; conducted research on various labor issues in the United States, such as working women and safety in the workplace; and began to track trends in the cost of living across America, directors' compensation, and corporate contributions. From the 1950s through the 1970s, it launched research on the impact of the federal budget on the United States and world economies and engaged in consumer research. From the 1980s to date, the Board has emphasized the study of corporate governance and the economy. Since the 1990s, its perspective has become increasingly global, as reflected in its design of business cycle indicators for eight nations (previously published only for the United States) and the establishment of the Asia Business Initiative and the Conference Board China Center for Business and Economics.

Areas of Focus

The Conference Board lists its areas of focus as follows: corporate citizenship, corporate governance, economics, human resources, marketing/communications, and strategy/planning. Corporate citizenship, which the Board defines as the interaction of corporations with their communities, is closely linked to the concept of social responsibility. The Conference Board includes under this category the environment, health and safety, community relations, corporate contributions, and sustainability. Examples of the Board's corporate citizenship initiatives are the annual Corporate Contributions Report, an analysis of the giving patterns of major corporations, and the Ron Brown Award for Corporate Leadership, an award established by President Clinton in honor of the late U.S. Secretary of Commerce Ron Brown for a company's outstanding achievements in employee and community relations.

Corporate governance, the Conference Board's second area of focus, might be defined as the manner in which a company is directed or controlled; the Board explains the term as encompassing the role of the board of directors and the performance of top management. Key corporate governance initiatives of the Board in recent years include the formation of (1) the Global Corporate Governance Research Center, which is designed to facilitate communication between business leaders and major institutional investors; (2) the Director's Institute, which provides practical governance education for directors; and (3) the Commission on Public Trust and Private Enterprise, which published a highly respected and influential report in 2002 and 2003 on executive compensation, corporate governance, codes of conduct, shareholder relations, and accounting and audit practices.

In its report, the Commission on Public Trust and Private Enterprise concludes that executive compensation has become too disconnected from long-term performance goals, primarily due to use of fixed-price stock options (whose value has related more to short-term stock price gains than to long-term performance goals), skewed relationships between consultants and compensation committees, and lax oversight by boards and compensation committees. Its recommendations include increased independence of the compensation committee, performance-based compensation tied to long-term strategic goals, full disclosure of all executive compensation arrangements in filings with the Securities and Exchange Commission, and expensing of fixed-price stock options.

With regard to corporate governance, the Commission's primary concern is that strong CEOs have exerted a dominant influence over boards, preventing them from carrying out their central oversight role through independent and objective decision making. Recommendations in its report include selection of a board structure designed to assure a balance of power between the CEO and the independent directors, a substantial majority of independent directors, a three-tier director evaluation mechanism (of individual board members, committees, and the board as a whole), board responsibility for oversight of corporate ethics, and development of procedures to receive and consider shareholder nominations for board members and regarding serious business issues.

Finally, the Commission report addresses the audit process and its oversight by noting that audited financial statements must provide an accurate picture of a company's finances to ensure the confidence that the capital markets require. It recommends, for example, vigorous compliance with the Sarbanes-Oxley Act and stock exchange listing standards, an orientation program and continuing education for each member of a company's audit committee, and establishment of an internal audit function that reports to the audit committee. The report also includes recommendations regarding accounting principles, including the Financial Accounting Standards Board and the International Accounting Standards Board, that continue to consider a "principles"-based rather than a "rules"-based approach to audit opinions.

The Conference Board is perhaps most well known for its economic analysis and forecasting and its consumer survey data. Its periodic reports include the Leading Economic Indicators (for the United States, Australia, France, Germany, Japan, Korea, Mexico, Spain, and the United Kingdom), the Help-Wanted Advertising Index, the Consumer Confidence Index, the Consumer Internet Barometer, and the CEO Confidence Survey.

The Conference Board's study of human resources includes compensation, benefits, diversity, leadership, organizational structure, productivity, performance measurement, recruitment, retention, training, development, and work-life. Topical research reports have addressed subjects such as development of global talent, the benefits of and obstacles to using overseas labor, and managing the mature workforce.

As part of its focus on marketing and communications, the Conference Board provides its members information on marketing, sales, corporate communication, image, branding, and customer management. Examples of its publications include a report on improving communications between companies and investors, the Hispanic market in 2010, and employee communication during mergers.

Finally, in the area of strategy and planning, the Board offers assistance to business leaders on management of costs, knowledge, supply chain, mergers, quality, security, outsourcing, finance, taxation, and legal affairs. Examples of resources for members in this area include an enterprise security Web forum and a conference on supplier relationship management.

For each area of focus, the Conference Board produces research reports and other publications, sponsors conferences in various parts of the world, and invites its members to participate on councils and research working groups. More than 100 councils, each consisting of 30 to 35 cross-industry senior executives, meet up to three times a year in the United States, Europe, and Asia. Examples of these councils are the Council of Chief Legal Officers, the Middle East Council, and the Council on Executive Compensation. Research working groups are small networks of executives who come together for a year, working with Board research experts, to share information and collect data on a specific topic, such as off-shoring, best practices in implementing the Sarbanes-Oxley Act of 2002, and strategic workforce planning.

Conclusion

The post-Enron era of corporate scandals, with its resulting loss of public confidence in American capital markets, is reminiscent of the crisis in industry that led to the founding of the Conference Board nearly a century ago. Now, as then, the public (and the regulators) expect business leaders to ensure integrity and transparency in their organizations. Many observers have also sounded the call for business to assume a broader leadership role in society. The Board, through its Commission on Public Trust and Private Enterprise, has expressed its sharing in the public's anger over recent corporate misconduct. Given its membership of prominent corporate leaders, its influence on business policy and the financial markets, and its focus on corporate responsibility, as well as enhancing the bottom line, the Conference Board is well situated to lead the business community in repairing the breakdown of public trust and restoring confidence in corporate America.

—Francy Stewart Milner

See also Business Ethics Research Centers; Corporate Accountability; Corporate Citizenship; Corporate Governance; Corporate Social Responsibility (CSR) and Corporate Social Performance (CSP); Economics and Ethics; Global Business Citizenship; Leadership; Multinational Corporations (MNCs); Power, Business; Shareholder Model of Corporate Governance; Stakeholder Theory

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Confidentiality Agreements

Confidentiality agreements are contractual arrangements between two parties to keep something private, without external disclosure. For example, if a lawsuit is filed and later settled, a confidentiality agreement might be entered into preventing either party from disclosing to anyone else information about the lawsuit or the settlement. Confidentiality agreements in business can involve various organizational stakeholders. Sometimes confidentiality agreements are necessary for the conduct of business. But sometimes confidentiality agreements work against broader social interests. The main ethical issues with regard to confidentiality in business focus on the intent of maintaining confidentiality and are context specific.

What Is the Intent of Confidentiality?

Often, confidentiality is necessary for a business transaction such as a merger that is being negotiated or for a new business idea that is being developed. A confidentiality agreement in such cases ensures that nonpublic information that would be harmful to that legitimate business activity is not disclosed. At some point, however, confidential information must be often disclosed—the merger is announced or the business idea is patented or introduced. When the intent of a confidentiality agreement is to protect a legitimate business activity until it is ripe for appropriate public scrutiny, then it is likely to be ethical and legitimate.

Sometimes, however, confidentiality agreements constrain legitimate activities or protect illicit behavior. There is no moral obligation for an employee or another organizational stakeholder to maintain confidentiality for unethical behavior. Also, to the extent that confidentiality agreements make it unreasonably difficult for an employee to leave one employer to work for another or for information about an unsafe product to be made public, they may similarly be ethically suspect.

In short, the intent behind confidentiality agreements matters. Confidentiality can support legitimate business activities that would be harmed by premature public disclosure. But confidentiality can also shield businesses from legitimate scrutiny or keep employees from pursuing other job opportunities.

Confidentiality and Duties of Loyalty

Behind legitimate confidentiality agreements are usually duties of loyalty. The employee who is negotiating a merger or working on a new project owes a duty of loyalty to her or his employer. The confidentiality agreement puts this duty of loyalty in writing, but the duty of loyalty precedes the agreement and stands whether or not such an agreement exists.

There are also duties of loyalty owed to shareholders. Mergers and the development of new products have financial implications. When employees, for example, possess nonpublic information, there is a danger that they will engage in inside trading. Such activities violate duties of loyalty owed to their corporations and shareholders in those corporations. Confidentiality agreements are legitimately used to prevent such sorts of opportunistic behavior.

Confidentiality Agreements in Context

Confidentiality agreements are used in a variety of business situations. When there is business value in maintaining confidentiality, then such agreements are useful and legitimate. There will be, however, some situations in which the use of confidentiality agreements leads to ethically problematic outcomes.

Mergers and Acquisitions

When two companies are negotiating a merger or an acquisition, there is generally a desire to keep the negotiations secret. Premature disclosure of such information may lead to a merger being called off, or to a bidding war. When a merger agreement is announced publicly, then there are opportunities for counter bids. But while the agreement is being negotiated, a confidentiality agreement can allow the parties involved an opportunity to examine the financial and business records of each firm—and this information should be held confidential in any case whether or not the agreement come to fruition.

People involved in a merger or acquisition negotiation also have ethical and legal obligations not to use that information to engage in inside trading. Part of the duty of loyalty owed to shareholders includes not using nonpublic information for personal enrichment.

Suppliers and Business Partners

Sometimes suppliers and business partners (such as members of a strategic alliance) will need to share confidential information, such as information about how a product is made or some other trade secret. This information should generally be held in confidence, but a confidentiality agreement in such cases would be ethically and legally binding. While trust can substitute for formal means of governance in such situations, written confidentiality agreements are generally advisable.

New Product Development

Individuals or companies (if there is an alliance) developing new products have similar ethical duties to maintain confidentiality. New products and trade secrets can be sold. Individuals wanting to engage in inside trading might use information about new products for personal gain or might seek to move to a competitor and take information about the product with them. Confidentiality agreements in such cases would serve legitimate business purposes.

Employees

Many of the examples previously discussed involve employee behavior and help delineate when confidentiality agreements reduce to writing existing ethical obligations employees owe employers. An employee working for a company might over time acquire firm-specific knowledge about the company that would be valuable to a competitor. In such cases, a company might ask the employee to sign an agreement agreeing to hold such information confidential, which would include a noncompete clause preventing the employee from working for a competitor for some period of time.

Courts will generally look at the reasonableness for such clauses when deciding whether or not they are legally enforceable. A noncompete clause preventing an employee from ever taking a job with a competitor would likely be unenforceable. Employees who work for one firm and then switch employers still owe duties not to use confidential information (say about business plans) for the benefit of their new employers. A noncompete agreement that includes a confidentiality agreement can be drafted in a way that balances the interests of the employers and the employee.

Finally, confidentiality agreements cannot be used to prevent employees from sharing information about illegal and unethical behavior with the public or with regulators. An employee's duty of loyalty does not extend so far as to include withholding such information. The use of confidentiality agreements to shield such business behavior would be contrary to ethical expectations and public policy.

Product Safety

An example of an ethically problematic confidentiality agreement would involve product safety. When a dangerous product causes harm and leads to a lawsuit that is settled, the settlement agreement might include a confidentiality agreement that prevents information about the agreement—including perhaps information about the defect itself—from being made public.

It is understandable why companies would not want information about product defects to be made public. But companies have prior ethical duties to provide safe products for their consumers. Confidentiality agreement may provide incentives for companies to settle lawsuits. But such agreements can work contrary to public interests by preventing information about unsafe products from reaching the public and business regulators. There may be a role for public policy in preventing the use of confidentiality agreements in such cases.

Confidentiality and Public Policy

There is also a need for public policy to outline when confidentiality agreements are legitimate and when they are not. Common law in the United States has delineated when an employee's confidentiality agreement is fair to that employee and when it is unduly restrictive. In many cases, confidentiality agreements are both ethical and legally enforceable. But sometimes confidentiality and secrecy runs counter to fairness or to broader public goals such as product safety.

In such cases, public policy will need to intervene to delineate when a confidentiality agreement serves a legitimate business purpose and when it would be contrary to social welfare or to values such as fairness. Balancing the interests of business and society is an important role for government, and especially so when businesses want to keep information secret.

Conclusion

Confidentiality and secrecy in business is not always bad. When confidentiality agreements support legitimate business goals, then they are generally ethical and legally enforceable. When such agreements protect illicit behavior or unduly prevent employees from pursuing job opportunities, confidential agreements are ethically and legally suspect. The intent and content of any particular confidentiality agreement therefore matters in making judgments about it.

—Harry J. Van Buren III

See also Fiduciary Duty; Finance, Ethics of; Insider Trading; Loyalty; Mergers, Acquisitions, and Takeovers; Piracy of Intellectual Property; Product Liability; Trust

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Conflict of Interest

A conflict of interest is a situation in which a person has an interest that interferes with that person's ability to act in the interest of another when that person has an obligation to act in that other person's interest. This definition contains several crucial elements.

First, there must be an obligation to act in the interest of another. This kind of obligation is characteristic of fiduciaries, agents, and professionals (who are commonly agents and sometimes fiduciaries), all of whom are in positions of trust. A physician or an attorney, for example, like a trustee of a fund or a real estate agent, agrees, usually for a fee, to exercise specialized knowledge and skills for the benefit of another. As a result, there is an obligation, either explicit or implicit, to serve that other person's interest.

Second, there must be an interest that interferes, actually or potentially, with the ability of a person with such an obligation to act in another person's interest or, in other words, to exercise specialized knowledge and skill solely for the benefit of that person. The interest that interferes is usually some prospective financial gain, but it can be anything that a person values, such as family well-being or public recognition. A situation in which an interest actually leads a person to fail in an obligation to serve another's interest is usually called an *actual* conflict of interest, whereas the mere presence of a conflicting personal interest but no failure to fulfill an obligation is called a *potential* conflict of interest.

Third, interference means that the person fails or is likely to fail to serve the interest of another in a manner that meets some expected or required standard. A person with a conflict of interest may fulfill the obligation in question, either in full or in part. A conflict of interest may still be present, though, as long as the ability of the person to serve the interest of another is compromised to a significant extent.

Examples of conflict of interest include a physician who orders a test from a lab in which he or she is an investor; a judge hears a case in which a family member is a party; an executive owns stock in a supplier of her or his company; an accountant audits a company in which he or she holds stock; the administrator of a trust invests funds in a company that she or he owns; and an insurance broker is paid commissions by the insurer he or she recommends to a client. In each case, the person's objectivity or independence is compromised. The ability of that person to fulfill an obligation to serve others is reduced by a countervailing, personal interest.

The inability to fulfill an obligation in a conflict of interest is different from merely having a bias or a conflict of obligations. Thus, a judge who is biased against criminal defendants may fail to render justice, but the interference in this case comes from an attitude rather than some personal interest. The judge's judgment is biased but not influenced. Furthermore, an executive who has an obligation to choose the best supplier and also to favor a minority supplier has a conflict, but the conflict, if there is one, is between obligations that cannot both be fulfilled.

Not only persons but also organizations can be in conflict of interest situations. Law firms, advertising agencies, and investment banks, for example, serve many clients, and an interest in one client may interfere in the organization's ability to exercise unbiased judgment or unstinting diligence on behalf of another. For accounting firms to provide audit and consulting services to the same clients is often cited as a conflict of interest because they have an incentive to perform lenient audits to retain the more lucrative consulting services.

History of the Concept of Conflict of Interest

Although conflict of interest has become a ubiquitous and increasingly important moral concept, it did not come into recognized use until about 1950. No popular English dictionary included the term until 1971, and it first appeared in a law dictionary in 1979. In both cases, the definitions are confined to the public officials in the performance of their duties. Conflict of interest in professional practice started attracting attention in the early 1970s, especially in legal ethics, and the concept began to be included in company codes around the same time. Why the concept came into use when it did and why it has become so prominent are questions that invite speculation. One possible answer is that in the second half of the 20th century, society became much more dependent on fiduciaries and agents, especially those in the professions, while, at the same time, market forces have come to play a larger role in their activities. When the professions—most notably, medicine, law, accounting—began to be practiced more and more in a market economy based on financial incentives, both the benefits and the harms of this development were recognized. To enjoy the benefits, it was necessary to develop a concept that identified the source of the potential harms and to devise means for reducing the harmful consequences.

What Is Wrong With Conflict of Interest?

The moral wrong in conflict of interest is simple: A person in a conflict of interest—a fiduciary, agent, or professional—has failed to fulfill an obligation, one for which he or she has accepted an engagement and, usually, compensation. If such a person acts contrary to the other person's interest or fails to perform up to the expected or required standard because of a conflicting personal interest, then the service that has been contracted and paid for is not being provided. Thus, if a physician orders an unnecessary test to increase his return from the lab he or she owns, then he of she is failing in his or her duty to the patient; he of she is not delivering the service for which he or she is being paid.

Even if the service is up to an acceptable standard, a person in a conflict of interest has failed to deliver a service with the confidence that is expected and, in some cases, demanded of persons in positions of trust. A judge in a case involving a family member might render impartial justice, and an auditor might perform a thorough audit of a company in which he or she owns stock. In each case, though, the confidence that we have a right to expect is eroded. Not only is this confidence part of the service that a person in a conflict of interest has agreed to provide, but when this confidence is compromised, the service itself is diminished. A decision by a judge with a conflict of interest, for example, cannot produce the desired effect of ensuring that justice has been done. Similarly, an audit by a compromised accountant is less effective as an attestation of the company's financial statements.

A further wrong is committed when, as is usually the case, the people who rely on the services of fiduciaries, agents, and professionals are unaware of the conflict of interest. They are deceived with respect to the quality of the service or the confidence they can place in it. The beneficiary of a trust, for example, may be wronged twice if the trustee invests in a company he or she owns. The person is wronged once if the investment is not the best that could be made, and yet again by being deceived about the reliability of the trustee.

Managing Conflict of Interest

Conflict of interest is an ever present feature of professional and organizational life and cannot be easily eliminated. It is not only unreasonable to expect that people in positions of trust would have no conflicting interests, but in some cases, it would be undesirable to avoid such conflicts entirely. For example, medical research, which produces great benefits for everyone, would be severely hampered if practicing physicians were not involved, even though the financial incentives they receive create conflicts of interest. Similarly, auditing and consulting by accounting firms arguably benefits everyone despite the conflicts involved.

Nevertheless, it is important for professions and organizations to manage conflicts of interest to ensure that the harms are minimized and offset by any benefits. Fortunately, there are many means for managing conflict of interest.

Avoidance

The most direct means of managing conflict of interest is to avoid acquiring any interests that would bias one's judgment or otherwise interfere with fulfilling any obligations to serve the interest of others. Federal law prohibits public accountants from holding stock in companies they audit, and company policies often have similar prohibitions on employees' ownership of stock in suppliers or competitors. However, complete avoidance might impose an undue burden on some individuals. It is unreasonable to prevent the manager of a pension or mutual fund from trading for a personal portfolio, for example, since doing so would deprive that person of the ability to accumulate wealth. Complete avoidance is also impossible because the conflicting interests cannot always be identified or anticipated. For example, law firms generally screen new clients for any conflicts they might bring, but undiscoverable conflicts might arise in the course of representing a client. For investment banks, whose business involves large numbers of clients, some conflicts of interest are inevitable.

Alignment

When conflicting interests cannot be avoided for whatever reason, they can be countered by incentives that align the person's interest with the interests of those to be served. High executive compensation is often justified as aligning the executive's interest with that of shareholders. Although lower pay is usually sufficient to induce executives to act generally in the shareholders' interest, they still have personal interests in perquisites such as power and prestige that might lead them to make some trade-offs with profitability. Higher pay linked to performance, especially in the form of stock grants and options, thus creates a strong personal interest in profitability so that their interests are aligned more closely with those of shareholders.

Objectivity

A commitment to be objective serves to avoid being influenced by a conflicting interest. Virtually all professional codes require objectivity as well as independence (which is generally understood as avoidance of or freedom from any undue influence). Thus, a physician with an investment in a lab might still be able to make the patients' interest paramount, as prescribed by the Hippocratic Oath. To be effective, however, objectivity requires both a strong character that resists the temptation to earn more and a reputation for such a character.

Disclosure

Disclosing a conflict of interest to those who would be affected is a common means of managing conflict of interest. Government officials are generally required to disclose all financial investments on appointment and to make annual reports. Managers of pension and mutual funds have similar disclosure requirements. In legal ethics, a conflict of interest is acceptable if an attorney discloses the conflicting interest and affirms that he or she can be objective, and if the client, being fully informed, consents. The rationale behind disclosure is that whoever is potentially harmed by a conflict of interest has the opportunity to disengage or at least to be on guard against any harm from the conflict. In short, forewarned is forearmed. However, research has demonstrated that disclosure can have perverse effects that make conflicts of interest more harmful. Advisers who inform clients of conflicts sometimes feel licensed to pursue personal interests more aggressively, and the clients who receive advice from conflicted advisers often do not discount the advice enough.

Independent Judgment

A commonly employed remedy when one's judgment is impaired by a conflict is to seek the judgment of an independent third party. The standard response of a judge in a case involving a family member is to recuse, that is, to step aside and turn the case over to another judge with no conflicting interest. An executive who is selling personal assets—a piece of land, for example—to the company that employs her or him might seek an independent appraisal of the value of those assets. Such third-party appraisal assures that the price paid is fair and not inflated due to the executive's potentially biased judgment.

Competition

Strong competition provides a powerful incentive to avoid conflicts of interest, both actual and potential.

Insofar as conflicts of interest make organizations less efficient, they pay a price in the market that they may not be able to afford. For example, at one time commercial banks gave their brokerage business to firms that were already bank customers. This practice, know as reciprocation or "recip," has virtually disappeared because of the need for returns on trust accounts to compare favorably with alternative investments. Competition thus dictates that the allocation of brokerage commissions be based on the "best execution" of trades and not on satisfying brokers who are also bank customers. Of course, no firm would use increased competition as a means for managing conflict of interest, but industry regulators should recognize that the power of competition to reduce conflict of interest is another reason to encourage competition.

Rules and Policies

Most professions and organizations have various rules and policies concerning conflict of interest. Many of the restrictions imposed employ other means, such as avoidance and disclosure. Most company codes either prohibit stock ownership in suppliers and competitors (avoidance) or else mandate disclosure. Rules and policies can also operate, however, by prohibiting the kind of conduct that would be an actual conflict of interest. For example, pension and mutual funds impose "blackout periods" during which managers are prohibited from personal trading in stocks that have been bought or sold by the funds they manage. Controls on the flow of information can also limit conflict of interest. Thus, if fund managers have no knowledge of the trading done by other funds in a firm, they have fewer opportunities for acting in a conflict of interest. Priority rules are another means for managing conflict of interest. For example, an investment bank that advises outside funds faces a conflict of interest in deciding which investment opportunities to bring to each fund and which ones to keep for the bank. This kind of case is generally managed by establishing priority rules so that each client knows in advance the order of favor. Thus informed, no client can complain of unfair treatment in the allocation of investment opportunities.

Structural Changes

Because conflicts of interest result from providing many different services to different customers or clients, they can be reduced by compartmentalizing these services. Advertising agencies, for example, form separate creative teams for each account, and commercial banks split trust management from the retail side of the business. Within multifunction institutions, conflicts can be reduced by strengthening the independence and integrity of each unit. For example, instead of treating their investment research divisions as arms of their brokerage units, investment banks are being urged to upgrade their status and insulate them from pressure. Some structural features of American business are dictated by law. Because of the potential conflicts of interest, Congress mandated in 1933 in the Glass-Steagall Act that commercial banks could not also sell stocks or insurance, thereby making investment banking and insurance separate businesses. The repeal of the Glass-Steagall Act in 1999 has permitted the rise of larger banks, which, in turn, not only creates greater potential for conflict of interest but also, arguably, better service. Some have proposed that accounting firms be required to divide into separate auditing and consulting organizations, although the accounting industry has vigorously opposed this measure. Addressing the problem of conflict of interest by structural changes should be done carefully because of the many advantages of combining different services in one firm.

—John R. Boatright

See also Accounting, Ethics of; Agency, Theory of; Disclosure; Fiduciary Duty; Fiduciary Norm; Legal Ethics; Professional Ethics; Trusts

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CONFUCIANISM

Confucianism is an ethical system practiced in China and other East Asian countries such as Japan and Korea. Confucian ethics arose in the turbulent "axial age" in ancient China (ca. 600–200 BCE), when warring states violently fought for dominance, creating a climate for Confucius and other scholars to seek answers to questions about human nature, morality, and social harmony. In seeking to build a harmonious society, Confucius found his answer in *Ren*, humaneness, the highest level of virtue encompassing a variety of lesser virtues, such as reverence, tolerance, trustworthiness, keenness, and kindness. Attaining *Ren*, thus, involves achieving other virtues, such as courage, prudence, cautiousness in talking, and propriety. In short, *Ren* is a lofty ideal for people to aspire to. Confucius himself admitted that he had not entirely achieved *Ren.*

Confucianism can be categorized as virtue ethics, a teleological ethical system that inquires about the goal or end of the human person. Western virtue ethics mostly takes its inspiration from Aristotle, the ancient Greek philosopher. Aristotelian virtue ethics, embodied in Aristotle's *Nicomachean Ethics*, aims at achieving personal *eudaimonia*, meaning "flourishing" or "success," through the cultivation of moral traits such as prudence, justice, fortitude, and temperance. Confucianism, however, differs from Aristotelian virtue ethics in significant ways. Instead of *eudaimonia*, Confucianism strives for interpersonal harmony in a hierarchical society. Confucian *Ren*, to a large extent, entails vertical virtues: *Ren* is not expected to be cultivated to an equal extent across social hierarchies. For instance, an emperor is expected to achieve a higher form of *Ren* than his subject does. *Ren* is, therefore, specific to one's social station in the society. Aristotelian virtue ethics, in contrast, having evolved in a democratic society, placed largely equal expectations on the citizens in the city-states in terms of cultivation of virtue ethics, although the citizens with full voting rights did not include women, slaves, foreigners, children, and senior citizens.

What exactly then is *Ren*? Simply put, *Ren*, humaneness (also translated as benevolence), is love. This concept is illustrated in *Lunyu*, one of the four books comprising Confucius's teachings, but *Ren* allows for different interpretations in different contexts.

There exists a convergence between Confucian ethics and Western ethics. A cornerstone of major Western ethical theories is impartiality—one's own interest is placed on a par with the interests of others. Egoism is discouraged and generally denounced. Like Western ethics, Confucian ethics is also built on curbing egoistic impulses. Confucian ethics, thus, is connected to Western ethics through its assertion of overcoming one's self.

Parallel to overcoming one's self is the return to propriety that enables one to achieve *Ren.* Propriety, *Li*, another central value of Confucian ethics, is the code of behavior prescribed to men and women based on their role, social station, and gender. In essence, it is respect for other members of the society and varies in form from one social station to another, and from gender to gender. Though it is also a vertical virtue like *Ren*, *Li* is in many ways similar to Donaldson and Dunfee's hypernorm of respect for human dignity. In fact, it is this form of respect or propriety that helped to build a cohesive and civilized ancient Chinese society.

In sum, the central values of Confucian ethics are *Ren*, humaneness, and *Li*, propriety, with *Ren* being the dominant value. *Ren* and *Li* govern human relationships and underline a civil and harmonious Chinese society.

Over the past 2,000 years, Confucian ideals have gone through modifications and sometimes have even met with resistance. In the Maoist era, for example, attempts were made to purge them, together with petty bourgeois values, and to replace them with revolutionary ideals. In today's largely market economy, the Chinese society itself is experiencing values in tension, with traditional and Western values coexisting and competing against each other. Thus, on the one hand, it is hardly accurate to claim that the Chinese society is governed by purely Confucian ideals. On the other hand, having been dominant values and beliefs in the Chinese society for about 2,000 years, Confucian ideals are indeed deeply ingrained in the Chinese culture.

Confucian Ethics in Business Stakeholder Relationships

In recent years, China has emerged as a major economic player on the world stage, attracting investors and manufacturers from around the world. Accompanying this economic emergence has been an increase in the attention paid to business ethics and corporate social responsibility in China both for Chinese firms and for multinational firms. It is thus of interest to consider the implications of Confucianism to business ethics and corporate social responsibility. Since Confucian ethics is mostly concerned about how to promote harmonious relationships, in this part, we examine Confucian ethics in terms of major stakeholder relationships.

Stakeholder analysis has become the most important tool for modern business entities to approach corporate social responsibility. It recognizes the mutual influences between a business and its stakeholders: A business entity is not an all-powerful entity, free to pursue its profits without regard for its stakeholders. Stakeholder analysis has been justified in the management literature by its descriptive accuracy, instrumental power, and normative validity. Yet stakeholder theory originated in the West, the United States, in particular, and has a Western ethical orientation. Explaining Confucian ethics in the context of stakeholder relations sheds light on how business is conducted (or more precisely how it *should be* conducted) in China. This also provides guidance to multinational firms in terms of how to manage their business relations in China. In the following sections, Confucian ethics is applied to the relationships between a firm and the following primary stakeholders: employees, customers, suppliers, stockholders, partners, the community, and governments.

Employees

Confucian ethics demands that those in power particularly embody *Ren*, humaneness, for subordinates. *Ren* on the part of superiors often takes the form of kindness and protection. A superior with the *Ren* attitude assumes a paternalistic role and takes care of them as if they were his or her children. There is little wonder then that employees in Maoist China needed to obtain permission from their employers for marriage certificates. Employees, on the other hand, in their role, have the responsibility to carry out the duty entrusted to them with reverence and assiduousness—a strong sense of duty and a sense of loyalty are expected of them. Unequal though the roles are, both superiors and subordinates, nevertheless, exercise *Ren* and *Li* in their own ways.

In comparison with the largely rights-based Western stakeholder analysis, Confucian ethics as exemplified in this stakeholder relationship takes on a family tone. Rights and justice are, to some extent, embodied in and replaced by *Ren* and *Li*, in the form of kindness and protection (employers) and loyalty and duty (employees). Yet *Ren* and *Li* do not guarantee rights and justice—power can be a source of abuse. Employees' dependence on an employer for their *Ren*, therefore, rests on precarious grounds. Nevertheless, *Ren* is the ideal to pursue in Confucianism.

Customers

The relationship between a firm and its customers is largely horizontal. The enormous power that a firm may possess, however, can place customers in a disadvantaged position. This unequal power requires a different form of *Ren* for both the firm and its customers. The *Ren* on the part of a firm in this relationship is the Confucian golden rule: One should not do to others what one would not want done to oneself.

This context-independent principle prescribes one's relationship with other members of the society. On the part of the firm, it constrains them from involving themselves in fraudulent and deceptive practices that could place customers at various risks. The golden rule principle also applies to a firm's relationship with arm's-length transaction partners such as suppliers.

Regarding customers, the form that *Ren* takes in this relationship is best represented by *Zhi*, judiciousness. Confucian ethics emphasizes mental keenness and independent decision making. A customer who can judge a corporation's actions accurately and take appropriate actions has, no doubt, achieved *Zhi.* The same can be said of less powerful suppliers, for whom *Zhi* is the proper form of *Ren* to deal with powerful buyers.

Stockholders

The relationship between a business entity and its stockholders is fiduciary: Stockholders entrust the business with the management of their money. A business, in turn, to various degrees, depends on the financial resources from stockholders for its operations. To be able to obtain the financial resources from stockholders, a business needs to establish itself as trustworthy and put the money to good and effective use. In this case, *Xin* (trustworthiness) is the virtue expected of a business. Similarly, a business is like a carriage. It cannot move forward smoothly without the trust of its stockholders, the yoke bars.

Partners

Again, the relationship between a firm and its partners is largely horizontal. Since the success of cooperative relationships depends, to a large extent, on trust building, establishing oneself as trustworthy is necessary. *Xin* (trustworthiness) is again the form of *Ren* in this relationship.

Confucius distinguished between *Junzi,* gentlemen, those morally cultivated and dependable, and *Xiaoren*, small men, those morally dubious and unreliable. Gentlemen pursue *Ren* for its own reward and *Xiaoren* may use *Ren* for self-interest. In the relationship between a business and its partners, therefore, both parties are expected to act as trustworthy gentlemen and not engage in opportunistic behavior to ensure smooth relations and future collaboration. With the distinction between *Junzi* and *Xiaoren*, business entities in Confucian societies have generally preferred long-term cooperative relationships to arm's-length transactions, once they have built trusting relationships.

The Community

Though Confucian ethics does not specifically inform a person on his or her role in the community, in today's world, we can infer the Confucian attitude toward the community from his writings. Given the power a firm has and the wealth it accumulates, Confucians would be in favor of some form of corporate contribution to the community. In this way, the less privileged in the community would benefit from the help of a business, which already benefits from the local community in terms of talent and other resources. The relationship between a business and the community, therefore, is one of mutual advancement.

Governments

Finally, the relationship between a business and the governments is again vertical, like the one between a firm and its employees, though a firm would find itself in an inferior position in this relationship. In today's fiercely competitive market economy, *Ren* for different levels of government entails legal protection of businesses. Businesses, on the other hand, need to comply with the laws created by the governments. *Ren*, for a business firm then, is compliance oriented. Given that China has long been ruled by emperors rather than laws, the governments seem to have a long way to go with regard to establishing adequate laws to protect the corporations. In other words, a sustained effort is needed on the part of the governments for them to achieve *Ren* in today's world.

In summary, the examination of Confucian ethics in the context of stakeholder analysis reveals that the relationships between a business and its various stakeholders in light of Confucian ethics are subtly different from largely rights-based Western stakeholder relationships. Specifically, stakeholder relationships characterized by egalitarian horizontal relationships in the West often turn into vertical relationships in a Confucian society. Such an understanding can especially assist international business entities to place their home values and norms in perspective while doing business in China so that they can make contextually appropriate ethical decisions. In this way, they can fulfill their social contract and demonstrate their global citizenship with more effectiveness.

—Jiyun Wu and Richard E. Wokutch

See also Aristotle; Confucius; Stakeholder Theory; Virtue Ethics

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Confucius (551–479 BCE)

Confucius is regarded as the most influential philosopher and educator in Chinese history. He largely shaped

Chinese civilization and molded its moral beliefs. Confucius is best known for founding the Ru (Confucian) school of Chinese thought, which grew into one of the traditional religions, competing and coexisting with Taoism and Buddhism in Chinese civilization.

He was born into a declining noble family in the state of Lu, in modern Shandong province. His family name was Kong and first name Qiu. He has been traditionally honored as Grand Master Kong (Kong Fuzi in Mandarin Chinese), which has been Latinized as Confucius.

Confucius was about 3 years old when his father died. His mother was determined to provide him with a first-class education; as a result, he was well trained in the classics of Chinese literature, history, poetry, and music. As a young boy, fishing, chariot driving, and archery were among his favorite amusements. At the age of 15, Confucius aspired to be a scholar and teacher. He fulfilled this vocational dream in education at the age of 22. Using his own house as a school, he started to teach history, poetry, government, morality, and music to a few students. He often engaged his students in sustained Socratic exchanges. Passionate and inspiring, he soon attracted some 2,000 gentlemen-scholars around him, many of whom followed him religiously. It was from then on that a Chinese literati class was developed.

Believing in the cultivating effect of education on an individual, Confucius emphasized character development, instead of vocational preparation, in his teaching. Although he upheld the innate goodness of humanity, Confucius also recognized corrupt social influences. In light of this, Confucius distinguished between two types of individuals: gentlemen whose conduct is governed by moral principles and small men whose character is driven by profit. Education, based on sound moral principles, Confucius maintained, can restore and strengthen the virtuousness in us.

Confucius ultimately promoted a society of harmony and order built on virtues. He asserted that the moral basis of social bonds derived from an individual's social station. He delineated five relations of mutual moral responsibility: ruler and minister, father and son, elder brother and younger brother, husband and wife, and one friend and another. For instance, in an emperor-minister relationship, he deemed it proper for an emperor to treat the minister with benevolence, while the minister deferred to the emperor with noble reverence and loyalty. Among the many virtues he advocated, filial piety and brotherly respect remain the two fundamental moral traits that one should possess.

In addition to teaching, Confucius also pursued politics. One legend has it that Confucius was once appointed Minister of Public Works and later Minister of Crime in the state of Lu. He governed by good example rather than coercion. As a result, during his reign, the crime rate substantially dropped and society was peaceful. However, he was later forced out of his position by his enemies. Although he took some minor government posts later, he never again held a significant position.

In terms of his works, Confucius is said to have edited books such as *The Book of Songs* and *Spring and Autumn Annals.* Although there are controversies about which books he wrote or edited, *Analects* is generally considered the most authentic source of his teachings.

—Jiyun Wu

See also Confucianism

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Conscience

Bishop Joseph Butler (1692–1752), in his famous *Sermons*, said of conscience that it was a principle in man by which he approves or disapproves his attitudes and actions. He added that this faculty tends to restrain us from doing mischief and incline us toward doing good.

The history of the concept of conscience is instructive as one seeks to understand its contemporary meaning. Originally, according to the *Oxford English Dictionary*, *conscience* was understood as a common quality in which individuals *shared*: A man or a people had more or less conscience, as persons or groups had more or less science, knowledge, intelligence, prudence, and so on. The word came gradually to be used as an individual faculty or attribute, so that *my conscience* and *your conscience* were understood no longer as our respective shares or amounts of the common quality *conscience*, but as two distinct individual consciences, mine and yours.

This individualization of the meaning of *conscience* is significant not only etymologically but also philosophically. It signals a polarity at the core of our moral awareness: On the one hand, conscience is our subjective touchstone for ethical decision making; on the other hand, an appeal to conscience in moral argument (or dialogue) usually lays claim to *common* ground, a warrant for our ethical convictions that reaches *beyond* the merely subjective. Insofar as conscience must respond in actual decision-making situations, it has a certain private authority, both in relation to nonmoral decision guides and in relation to the consciences of others. We can refer to this as the *autonomy dimension* of conscience. But because conscience can be "undeveloped," "neglected," or "out of touch," philosophers have looked to it for a broader kind of authority, less private and more rooted in human nature or reason. We can refer to this as the *discernment dimension* of conscience.

In either of its dimensions, conscience can be effective or not in actually guiding action, a fact that no doubt led Bishop Butler to exclaim that if it had strength, as it has right, and if it had power, as it has authority, it would govern the world. At its strongest, conscience prevents wrongdoing. Accounts of "guilty consciences," "weakness of will" (*akrasia*), and relief at being caught on the part of some criminals also testifies to the influence of conscience subsequent to wrongdoing.

The Autonomy Dimension: Freedom and Dignity

Commentators on conscience often emphasize its role in providing a zone of freedom and dignity around each human person. It is the capacity and the need to decide about right and wrong, good and bad, virtue and vice. But this capacity also calls for respect from others, even if they disagree. The right to "freedom of conscience" is frequently cited as among the most basic of human rights. Most of us believe that a person ought to follow his or her conscience, but just as surely, we believe that a person ought to be *allowed* to follow his or her conscience—at least up to the boundary of respecting the rights and freedoms of others. For example, some societies allow *conscientious objection* to military service (offering alternative forms of service), a practice that indicates the seriousness with which freedom of conscience is taken. And throughout the ages, *civil disobedience* has been practiced to affirm the autonomy and sovereignty of conscience in the face of injustice (e.g., Socrates, Gandhi, Martin Luther King Jr.).

Philosopher Richard M. Hare, in the title of his classic, *Freedom and Reason*, emphasized the centrality of autonomy or freedom in normative ethics. At the same time, however, his title suggested a second central aspect of moral thinking (*reason*), to which we now turn.

The Discernment Dimension: Reason and Wisdom

The polarity or dual dimensionality of conscience springs from the fact that as a human faculty it is as much opposed to *arbitrariness* as to *subordination.* The source and content of conscience has usually been thought to be reason, a shared moral sense with access to a natural law that is independent of both personal wants and civil statutes.

Butler spoke of this dimension of conscience as a superior principle of reflection in every person that reaches beyond the internal promptings of the heart and pronounces some actions to be in themselves just, right, and good, and others to be in themselves evil, wrong, and unjust. Immanuel Kant referred to the deliverances of conscience as categorical (vs. hypothetical) imperatives that were legitimated by their universal nature.

A century later, but in a similar spirit, Philosopher Josiah Royce suggested that conscience discerns through the moral insight, the full realization of one's neighbor and the resulting resolution to treat one's neighbor unselfishly. And while, for Royce, the moral insight was subject to a kind of waxing and waning, it nevertheless provided a solid foundation for conscientious thought and action.

The Reverend Martin Luther King Jr., in his famous "Letter from Birmingham City Jail," appealed to conscience as moral leverage against unjust laws. He believed that an individual who breaks a law that his or her conscience judges to be unjust, willingly accepting the penalty of imprisonment to awaken the conscience of the community, is in reality expressing the very highest respect for the law. King went on to insist against the relativist that the content of conscience was not arbitrary. He believed that just laws are those in accordance with moral law or the law of God—unjust laws do not. He added that any law uplifting human personality is just, while any law degrading human personality is unjust.

King's perspective helps us to see the significance for conscience of what the Declaration of Independence called the laws of nature and nature's God. Without some kind of anchor in human nature, appeals to conscience can lose their traction. If conscience is interpreted as—at best—a personal emotion that may have evolutionary survival value, it is unlikely that it will sustain the principles to which human beings have appealed over the centuries—principles such as caring for the weak, social justice, natural rights, fiduciary duty, and the pursuit of the common good. If conscience is rooted in an awareness of a *natural* law, however, it can function as a source of moral reasoning with some hope of moral progress—and ultimate moral consensus. The authority of conscience, in this way of thinking, lies in an order not *decided on* by each person (the discernment dimension), even if it is ultimately *interpreted by* each person (the autonomy dimension).

The "postmodern" fear may be that in adding *reason* to the private emotional aspects of conscience, we run the risk of having to sacrifice freedom or autonomy. But on this point, we might do well to consider philosopher Richard Norman's observation that the sacrificing of one's own interests need not be thought of as a sacrifice to something *external.* Commitments to our friends or our children, or to causes in which we believe, may be a part of our deepest being, so that the experience of devoting ourselves to them is less like *sacrifice* and more like *fulfillment.*

Norman suggests that the deepest being in each of us reaches for the same moral insight—and ultimately the same basis for conscience. Ethical inquiry, at any rate, is rooted in the presumption of a *shared moral consciousness*, which we can approach in a disciplined way rather than fleeing it as if it were fragile and fragmentary.

Developmentalism: Responsibilities *Of* and *For* Conscience

One of the most famous writers on the development of conscience in the 20th century was Swiss psychologist Jean Piaget. His observations of children were clinically rich and led to contemporary schools of "cognitive developmentalism" in psychology. Piaget spoke of an initial stage of *egocentrism* in which the child guides its decisions primarily out of a concern to satisfy its own desires and interests. This stage was followed, he believed, by a second stage called "moral realism" (*heteronomy*). At this second stage, external factors in the child's environment (e.g., game rules, peer pressure, parental norms) are given full sway as restraints on self-interest. Only in the third stage (*autonomy*) did Piaget see the emergence of genuine conscience. In his view, for actions to be characterized as moral, there had to be something more than compliance with commonly accepted rules. It was necessary that some inward principle (conscience) be capable of appreciating the value of such rules.

The third stage required, according to Piaget, inner direction born not of egocentrism, but of mutual respect, and cooperativeness born not of submission, but of a sense of reciprocity. At the third stage, the individual sees others as deserving of consideration in their own right, whatever the rules may be.

The developmental approach to conscience helps in identifying a distinction between the responsibilities *of* conscience and responsibilities *for* conscience. Responsibilities *of* conscience are the dictates about which Bishop Butler wrote so eloquently in his *Sermons.* But responsibilities *for* conscience, since it is capable of examination and development, signal the need for both moral education (by parents and schools) and personal character cultivation. Without responsibilities *for* conscience, it would be difficult to criticize the decision making of criminals of conviction such as Hitler and Stalin. Cardinal Joseph Ratzinger, who became Pope Benedict XVI in April 2005, has emphasized this point. While it is never wrong to follow one's convictions, he pointed out, it can very well be wrong to have come to certain convictions in the first place by stifling the protests of conscience. The guilt in such cases lies not in the present judgment of conscience, but in the neglect of my obligation to cultivate a healthy conscience, attuned to the internal promptings of truth.

Personal and Corporate Conscience

As Plato observed centuries ago, organizations are in many ways macro versions ("projections") of ourselves as individuals—human beings writ large. Because of this, we can sometimes see more clearly in organizations certain features that we want to understand better in ourselves. And the reverse is often true as well. Sometimes, the management of organizations can profit from what we understand about ourselves as individuals.

The dynamics of goal-directed behavior and conscience are present in both individuals and groups and offer us fruitful comparisons. The basis for exploring organizational conscience in this way comes from the following (occasionally disputed) principle:

> *Moral Projection Principle.* It is appropriate not only to describe organizations and their characteristics by analogy with individuals, it is also appropriate normatively to look for and to foster moral attributes in organizations by analogy with those we look for and foster in individuals.

The implications of applying Piaget's account of conscience to organizations are similar to those of applying it to individual persons: (1) growth consists in a fuller acknowledgment of the reality and dignity of others and (2) external or environmental constraints, while they may be necessary guides, are not morally sufficient. Indeed, just as Piaget saw the moral development of the child as a kind of liberation, so we might suggest that the moral development of the corporation is a kind of liberation.

Concern for stakeholders can evolve from purely instrumental status (e.g., public relations) through the status of an environmental constraint (e.g., legal or regulatory requirements) to being a direct management concern. Such an evolution represents a maturation process analogous to the development of conscience in individuals. Philip Selznick saw this point decades ago when he wrote about the process of "character formation" as an important area of exploration for those who would understand the decision making of organizations. Leadership, according to Selznick, was about institutionalizing values.

Leaders who seek to orient, institutionalize, and sustain ethical values in their organizations—to foster a corporate conscience—often employ mission statements, codes of conduct, ethics officers, executive development seminars, recruitment and promotion practices, and various other forms of communication. As in the case of individuals, organizational character formation (conscience) can lead to a fundamental revision of an organization's understanding of *success.*

—Kenneth E. Goodpaster

See also Authenticity; Autonomy; Free Will; Human Nature; Moral Leadership; Relativism, Cultural; Relativism, Moral; Teleopathy

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Consent

Consensual exchanges and contracts are the foundations of a free market; consent makes a free market free and is essential to any moral justification of the free market.

For an act of consent to have ethical merit, it necessarily has certain characteristics: (a) both parties must be fully informed—they must know and understand what they are consenting to; (b) there must be no coercion of either party; and (c) there must be a clearly performed action that constitutes consent. Actions that signify consent are culturally defined; consent, for example, can be signified by a handshake or other gesture, by signatures, or by simple verbal agreement. There is no ethical significance to these cultural variations.

Ethical concerns about consent to business transactions can arise in any of three ways: (1) apparent consent can fail to be actual consent, (2) the ethical value of consent can be undermined when a person has no or few alternatives, and (3) consent to a transaction within a socioeconomic system may be invalidated ethically because of failure to consent to the system.

Failed Consent

Some agreements in business that appear to be consensual may not be; apparent consent can fail in many ways. For example, suppose a drug company in its advertisements lists the benefits of a drug but does not list the side effects that have shown up in drug trials that only the company has access to. People who buy this drug based on the advertisements may appear to consent to the purchase, but since they do not really know what they have consented to, consent in the moral sense has failed.

Besides raising ethical issues, failures of consent often invite government regulation of business. Indeed, a great many laws, especially labor laws and consumer protection legislation, deal with failures of consent. Such laws should not be viewed as external interference in free markets or as attempts to determine the outcome of market exchanges. Such laws are attempts to ensure that the market is a free market based on consensual exchanges. Some sources of consent failures and regulations meant to deal with them include (1) coercion, regulated by laws against unfair and predatory trading practices; (2) asymmetrical or false information, regulated by transparency and full disclosure laws, consumer product labeling requirements, and antifraud laws that prohibit giving false information; (3) emotional pressure or distraction, regulated by rules such as cooling-off periods; (4) mental incompetence, regulated by laws that prohibit children from making contracts and certain purchases and laws that protect people with mental disabilities, including some elderly people, who cannot make informed decisions; and (5) externalities, regulated by laws that prevent externalities, or force compensation for them.

Lack of Alternatives

If people have no or few alternatives to a transaction, then their consent to it may not be morally significant. People, for example, who consent to a wage below the poverty line may be doing so because they have no other choices. Having alternatives is usually a matter of degree; there may always be some alternatives, but they may be very expensive, excessively time-consuming, or difficult for the person. There is no specific answer to the question of how constrained by the lack of alternatives people must be for us to say their consent was not freely given. The conclusion that follows is that the ethical value of consent is sometimes a matter of degree, not just an either/or situation. Some philosophers, such as Robert Nozick, dispute the claim that alternatives are relevant to the moral worth of consent and argue that only coercion can limit the value of consent.

Those who worry about viable alternatives are often especially concerned with the consent people give to employment because poor people frequently lack alternatives to taking whatever job is offered, sometimes at very low wages. Some people argue that the only way we can be sure consent to employment is always genuine is to make sure everyone has some guaranteed source of income. Defenders of a "universal basic income" (whereby the government pays all citizens enough to live on) frequently use this argument.

Consent to the Economic System

Besides problems with failure of consent to specific transactions, consent can also fail ethically if a person consents to the transaction, but does not consent to the socioeconomic system in which the transaction takes place. This problem can be seen most clearly in extreme situations. For example, if a slave "owner" says "Tow that barge; lift that bail" and the slave says "yes," the slave's "consent" to the specific action is made morally illegitimate by his failure to consent to the system of slavery, and to being a slave within it. The issue of slavery seldom arises for businesses in most developed countries, but it can arise even today when multinational corporations (MNCs) use suppliers in parts of Asia, Africa, and South America, or if an MNC's suppliers use prison labor. However, even if slavery is not involved, the same question of consent to the socioeconomic system arises when MNCs do business in many different societies.

Some thinkers, for example, Robert Nozick, think consent to the social system is irrelevant to the moral value of consent. Those who are concerned with this issue generally take one of three sorts of approaches to the problem: tacit approval, actual democratic consent, and hypothetical consent.

First, John Locke, in his defense of private property, argued that people gave tacit (or implied) consent to social systems whenever they took part in those systems. People give tacit consent to the system of private property whenever they claim anything, especially money, as their property. The problem with this argument is that people cannot avoid the current social system in which they live even if they object to it. For many people in some countries in which MNCs do business, objecting to the social system is unwise, refusing to go along with it can be fatal, and leaving is not possible. Even in free countries, objectors have to live within the current system while they try to change it. Tacit consent does not seem morally adequate.

Second, in free and democratic counties, people have a chance to approve or disapprove of capitalism through the voting process. Some people may complain that they have always voted against capitalism and been outvoted, but this objection is not valid because democratic decision-making processes are the morally appropriate way to make decisions about social and economic systems. More serious objections to democracy conveying moral legitimacy on corporate capitalism are that economic special interests may have disrupted democratic processes; that many aspects of corporate capitalism (including corporate personhood) have been decided by courts or treaty negotiations not elected legislatures; that minorities are not always protected in democracies; and, most important, that many societies are not democratic. But in countries where freedom and democracy have been long established, actual democratic consent lends significant moral legitimacy to capitalism.

Third, hypothetical consent is used by social contract justifications of socioeconomic systems. Its most important use in business ethics is by Donaldson and Dunfee in their integrated social contract theory. Donaldson and Dunfee use hypothetical consent to deal with the invalidity of apparent consent to transactions and norms when people do not consent to the system. Social contract theorists ask the hypothetical question, "Would rational people consent if they were free to do so?" often adding Rawlsian constraints on the question, such as supposing people do not know which positions in society they will occupy. Donaldson and Dunfee use this approach to develop the concept of hypernorms; even if a social or economic system appears to have people's consent, the norm is not legitimate if it fails to have hypothetical consent, in other words, if no reasonable person would agree if given a free choice. Many people believe that hypernorms are a powerful ethical guide when doing business in nondemocratic societies.

Conclusion

Four conclusions can be drawn from this discussion of consent in the business context. First, consent is what makes free markets free, and it is thus essential to the moral justification of free markets. Second, apparent consent to a transaction can fail to be ethically legitimate for a number of reasons. The many laws and regulations that deal with these failures should be seen as supporting the creation and maintenance of free markets. Third, consent can be seen as a matter of degree depending on the alternatives a person has. Fourth, failure to consent to a socioeconomic system may sometimes render ethically void consent to a specific transaction within a system.

—John Douglas Bishop

See also Capitalism; Coercion; Externalities; Freedom and Liberty; Free Market; Informed Consent; Integrative Social Contract Theory (ISCT); Nozick's Theory of Justice; Rawls's Theory of Justice

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Consequentialist Ethical Systems

Consequentialist ethical systems are ethical theories that take the moral status of all actions to depend somehow on the value of their consequences. For example, if a particular action of keeping one's promise is morally obligatory, it is made obligatory by its good consequences, or by the hypothetical good consequences of people accepting a rule that requires it (such as a rule requiring promise keeping). It is *not* made obligatory by God's having commanded us to keep promises, by a self-evident right-making factor that simply inheres in promise keeping, by the fact that we could not consistently will promise breaking to be universalized, or by the fact that a person of good moral character would characteristically keep the promise. Most philosophers count a theory as consequentialist only if it holds that the rightness of actions depends on the *impartially reckoned* overall goodness of their consequences. An example of a business decision that is influenced by consequentialist thinking would be the decision to control a plant's hazardous emissions for the purpose of preserving people's health and quality of life, not just to get good publicity or to be safe from lawsuits.

Some philosophers use the terms *consequentialism* and *utilitarianism* interchangeably, while others define utilitarianism as that species of consequentialism that takes good consequences to be limited to happiness or welfare. (Complicating this terminological choice is the fact that the influential early 20th-century utilitarian G. E. Moore explicitly contends that knowledge, among other things, has value over and above its value as a means to happiness or welfare.) Consequentialist theories are widely agreed to constitute one of the three most influential branches of normative ethics, the other two being deontological theories and virtue ethics.

Contemporary consequentialist theories are mainly divided between act-consequentialism and rule-consequentialism. According to act-consequentialism, each person is morally required on every occasion to act in such a way as to make the greatest possible net contribution to the overall good. The rightness or wrongness of actions is determined not by moral rules, but instead by the net values of the consequences of the actions themselves. In contrast, rule-consequentialism holds that rules are indispensable as determinants of the moral status of actions, for the very function of morality requires that it provide a public system of rules. Moral right and wrong are determined by the most beneficial rules—either by the most beneficial individual rules (according to some forms of rule-consequentialism) or by the most beneficial code of rules (according to others). For example, the most beneficial rules may require every business to control its pollution even if that pollution, considered in itself, is negligible. For the cumulative effects of businesses' controlling their individually negligible pollution could be a great public benefit. A code of rules can be considered to be the most beneficial if the expected overall net value that would result from the general internalization of that code exceeds the expected overall net value that would result from the general internalization of any rival code of rules. It is sometimes further specified that an assessment of the overall value of the consequences should give some priority to the well-being of the worst off.

One aspect of everyday moral views that is rejected by act-consequentialism is moral permission for people to favor their own goals to some extent. Such a permission is sometimes known as an agent-centered option or an agent-centered prerogative. For example, on everyday moral views, rare book lovers are morally permitted to spend money on rare books for themselves despite the fact that they could obviously produce much more overall good by donating the money instead to a worthy charity. Furthermore, it is generally thought that when people do sacrifice their own interests to maximize their contribution to the general good—for example, in the case of saints, heroes, or even self-denying, charitable rare book lovers—these people are going *beyond* what is morally required of them. According to act-consequentialism, however, all such people are just doing what is morally required of them. On this account, Merck and Company was doing no more than fulfilling its moral obligations when, without any hope of making a profit thereby, it decided to research, develop, and manufacture a drug to cure and prevent river blindness to prevent an enormous amount of suffering by poor people living along tropical rivers.

Another way that act-consequentialism departs from everyday moral views is by denying the existence of constraints. A constraint is a prohibition against performing a certain type of action. For example, a constraint against deception would prohibit people from committing a deception, even for the purpose of preventing other people from committing more and bigger deceptions. According to act-consequentialism, however, it may be right to perform any action (such as deception or even murder) to prevent others from causing greater harm (such as bigger deceptions or more murders).

Unlike act-consequentialism, rule-consequentialism does permit people to favor their own goals to some extent. For any rules that did not permit this would require so much sacrifice that they would be costly (in effort and resources) to maintain as internalized rules—and this cost would militate against those rules being the most beneficial. Thus, the most beneficial rules, which determine right and wrong, permit people to favor themselves. Again, unlike act-consequentialism, rule-consequentialism endorses constraints. Since a moral code of rules is by definition public, and since widespread consternation would be caused by public knowledge that moral rules lacked constraints, the most beneficial code of rules will contain constraints. Still, rule-consequentialism's acceptance of permissions and constraints may well fail to satisfy defenders of everyday moral intuitions. For they, unlike rule-consequentialists, attribute to permissions and constraints a status that is not derived from the most beneficial rules. For example, they may see constraints as directly reflecting the basic principle that individuals must not, without their consent, be sacrificed or used to produce good.

Although act-consequentialists take the maximization of good results as the criterion of an action's moral rightness, they do not thereby advise us to aim consciously to maximize good results in our ordinary conduct. They point out that it may be counterproductive always to try to determine which action would produce the most overall good. Since we can produce the most overall good by *not* always trying to figure out which action will produce that good, we ought not always to try to figure it out. For example, an act-consequentialist may think that we normally ought to decide what to do by reference to rules of thumb that are framed in terms of commonly accepted nonconsequentialist moral expectations, such as honesty and loyalty. (Of course, if we are in circumstances where we know that doing what is disloyal and dishonest will produce the best overall consequences, all things considered, then we ought to do what is disloyal and dishonest.) In contrast to act-consequentialism, rule-consequentialism does not posit an important gap between the criterion of rightness and the appropriate procedure of deliberation. According to rule-consequentialism, the rules that determine rightness are the very rules that it is best that we internalize and use in deliberation. Thus, rule-consequentialism need not deal with the charge of "moral schizophrenia" that is sometimes leveled against act-consequentialism.

Objections Against Act- and Rule-Consequentialism

The most common objections against act-consequentialism arise from its departure from confidently held everyday moral views. Two of these departures have already been noted—the rejection of self-favoring permissions and of constraints. To these objections, a common act-consequentialist reply is that the departure from everyday moral views is greatly reduced once the distinction is properly noted between a criterion of moral rightness and a morally appropriate method of deliberation. Except in unusual circumstances—where perhaps our everyday moral intuitions are in fact less trustworthy than usual—act-consequentialism approves of individuals deliberating on the basis of rules of thumb that do contain permissions and constraints. A different act-consequentialist defense of the denial of constraints is to argue that constraints are paradoxical. A constraint against deception, for example, assumes that deception is bad. But if deception is bad, then it stands to reason that less deception is morally preferable to more deception. It would be paradoxical to morally prohibit a person or business from bringing about that morally preferable result. But that is what constraints do. For example, if the only way to prevent one's competitor from deceiving the public very badly were by committing a much milder deception of oneself, one's mild deception would still be prohibited by a constraint against deception.

Another objection against act-consequentialism is that it is inconsistent with human well-being. Human nature being what it is, human well-being requires commitment to particular projects and also loyalty to particular people and groups. Yet, the objection continues, such particular commitments are incompatible with an overriding commitment to impartiality; and an overriding commitment to impartiality is required to accept an act-consequentialist criterion of moral rightness. Act-consequentialists respond that they do and should have real particular commitments and loyalties that are hard to override. A commitment may be real and hard to override, they say, without itself overriding every other commitment. So they may, for example, maintain real loyalty to their spouses and act on many occasions expressly for the good of their spouses. But they are able, in good conscience, to maintain a special loyalty to their spouses because they see that such loyalty is compatible with the greatest impartial good.

An important challenge to rule-consequentialism arises from the fact that there may be partial rather than universal compliance with the most beneficial rules. Obedience to the most beneficial rules may have very bad consequences in some of these cases. To take a simplified example, suppose that a "no first military strike" rule is among the most beneficial rules. Still, obedience to that rule can have disastrous consequences when one's enemies do not accept the rule. So it is counterproductive for rule-consequentialism to require obedience to the most beneficial rules. A rule-consequentialist response to this objection is to posit that the most beneficial code of rules includes a particularly strong requirement not to bring about great harm. Since great harm would be brought about by allowing an evil enemy to strike first, the "no first strike" rule would be overridden in such a case.

An objection against both act-consequentialism and rule-consequentialism challenges consequentialism's assumption that the value of states of affairs is independent of moral considerations. Consequentialism must make this assumption, because it takes the moral status of actions or rules to be determined by the value of the resulting states of affairs. A supposedly uncontroversial example of a valuable state of affairs is someone's being happy. If, however, the value of someone's being happy were itself to be dependent on moral considerations, then it could not function as the "independent variable" that consequentialism takes it to be. Immanual Kant famously held that nothing is always good except the will to do right. The value of a particular person's being happy, for example, cannot be assessed independently of moral considerations. A person's happiness could be rendered morally inappropriate by that person's wickedness and, in such a case, the person's being happy would not be good. So consequentialists are misguided to suppose that the value of states of affairs can function as independent variables in determining the rightness of actions. In response to this objection, consequentialists must maintain that, contrary to Kant, there is always positive value in people being happy. In the case of wicked people, this positive value may be outweighed by further bad effects, but the value of states of affairs can nevertheless be assessed independently of moral considerations.

—B. C. Postow

See also Deontological Ethical Systems; Divine Command Theory; Ethics, Theories of; Expected Utility; Kantian Ethics; Moral Rules; Normative Ethics; Satisficing; Supererogation; Utilitarianism; Utility, Principle of; Virtue Ethics; Well-Being

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Conspicuous Consumption

Thorstein Veblen coined the term *conspicuous consumption* around the turn of the 20th century. If you have ever wondered why someone drives a Cadillac when a Hyundai will get you where you want to go, then you understand the basic concept of conspicuous consumption. Any make of car may get you to your destination, but driving a Cadillac will get you noticed by others. Economists postulate that consumers derive "utility" from the consumption of goods. Veblen would say that this utility comes from two distinct characteristics of goods. The first is what he called the serviceability of the good. This basically means that the good gets the job done. Both the Cadillac and the Hyundai will get you from New York to Boston. The other characteristic of a good is what Veblen called its honorific aspect. Driving a Cadillac provides evidence that you can afford to drive a car that others will admire not primarily because it gets the job done, but rather because it provides visible evidence you have enough wealth to own a Cadillac. The Cadillac is thus an outward display of your status in society. Barbarian societies might display gold captured from enemies as evidence of prowess in warfare. In modern society, people drive Cadillacs.

A corollary of these dual characteristics of goods is that such conspicuous consumption is waste. In using this term, Veblen is not making a judgment that the good is unneeded by society, but rather uses *waste* as a technical term indicating that the production of a Cadillac requires more resources than the production of an Hyundai. A Cadillac may have leather seats; a Hyundai has vinyl seats. The difference Veblen would label *waste*, but this does not mean that Cadillacs should not be produced.

The core of Veblen's analysis of modern society was the fact that, on the one hand, there is enormous technological potential to produce goods. On the other hand, business enterprise constrains the amount produced to that which can be profitably sold. One way to think of this is that if all one needed to do is get from New York to Boston, then that could be satisfied by Hyundais. To sell more cars, wants must be continually expanded. In Veblen's view, the function of advertising was to ensure that people want a Cadillac. The gulf between the wants of consumers and the technological potential is reduced through advertising. It is for this reason that Veblen viewed advertising as waste, but one that is intrinsic to a modern economy based on the principles of profit-making business enterprises.

An important point in Veblen's analysis is the recognition that all goods have elements of serviceability and waste. The typical textbook example of conspicuous consumption cites fur coats, diamonds, or expensive cars. These are examples everyone would recognize. However, the dichotomy that Veblen draws between the "honorific" aspects of a good and those that further the "life process" implies that all goods possess these dual characteristics. This means that both the Hyundai and the Cadillac have both serviceable and honorific elements. The fact that one drives a car implies that you are wealthy enough that you do not have to take public transportation, but the Cadillac conveys still higher status in society because you do not have to take public transportation or drive a Hyundai.

—Ronnie J. Phillips

See also Advertising, Subliminal; Conspicuous Consumption; Deceptive Advertising; Deceptive Practices; Economics and Ethics; Entrepreneurship, Ethics of; Evolutionary Psychology; Executive Compensation; Fraud; Free Market; Great Depression; Hedonism, Ethical; Hedonism, Psychological; Veblen, Thorstein

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Consumer Activism

Consumer activism is a term that describes a variety of disparate movements that seek to influence the behavior of companies through activities ranging from providing information to boycotts, pickets, and litigation, with the aim of forcing companies to act in a way that benefits the perceived interests of consumers. Underlying the unifying idea of consumer activism is the belief that consumers can and should exercise their market power to improve not only the quality of products but also the conditions under which they are made, distributed, advertised, and sold. Consumer activism takes Adam Smith's dictate that the consumer is king to mean not only that the market responds to consumer demand for products but also that consumers can translate that demand into power for the sake of social transformation.

Consumer activism has played a role in debates on many important issues in the past several decades, from environmental activism and workers rights to antiglobalization and fair trade movements. In mobilizing consumer power on behalf of these issues, activists have occasionally been able to effect changes more quickly and more effectively than they would have by going through governmental or regulatory institutions (although these institutions have also been affected by consumer activist movements).

Early consumer activism movements included the work of the National Consumer's league, which worked in the first half of the 20th century to improve the labor conditions of workers through the promotion of "ethical consumption." In using consumer power to create pressure for social change, this organization had some success in the 1930s in bringing about better labor standards for American workers.

The contemporary period in consumer activism may be said to have begun with the publication of Ralph Nader's *Unsafe at Any Speed* in 1965. As an exposé of the American automobile industry, this book revealed a number of the hazardous practices that were common among car manufacturers. He subsequently founded the group Public Citizen, through which he continued to work on consumer issues.

In the 1990s and into the 21st century, consumer activism has become much more closely involved in movements critical of the phenomenon of globalization and the concentration of corporate power. Activists such as David Korten have written critiques of the global economy, not on anticapitalist grounds, but on the ground that an unregulated global economy creates the conditions for an unhindered expansion of corporate power, the degradation of democracy, and the inability of consumers to control key aspects of their lives as both citizens and as participants in the market. Such critiques are also often tied to environmental concerns about the effects of particular patterns of production and consumption that become more difficult to control in a global economy.

Moral Foundations of Consumer Activism

The moral basis of consumer activism is rooted in the morality of the act of consumption itself. Capitalism rests on the premise that in a free market consumers are free to make choices with regard to what they consume and how. The market itself cannot be an arbiter of the morality of any particular transaction. Demand can produce a supply, whether the demand be for solar energy or illicit drugs. The moral character of the market is ultimately determined by the morality of the consumers who inhabit it. As such, it is the responsibility of the consumer to demand those products that most fully conform to his or her core moral convictions.

In addition, consumers may take responsibility not only for the particular products they consume but also for the manner in which those products are manufactured and supplied. Consumers as well as manufacturers are responsible for products that are produced in ways that are harmful to workers or to the environment or use unethical or illegal production methods.

The reverse side of this is the responsibility of the producer to the consumer. The producer is obliged to provide the consumer a safe and reliable product that is produced using morally acceptable methods. *Caveat Emptor* ("let the buyer beware!") does not absolve the producer or seller of a product from the need for scrupulousness in ensuring that products meet minimal standards of quality and morality.

This view rejects the idea that buyer and seller exist as isolated individuals engaged in a decontextualized commercial transaction. Rather, it recognizes both the consumer and the producer as part of a capitalist economic and social system. The consumer and producer are morally bound together as members of this system and bear moral responsibility for the results that they jointly bring about—the producer through his methods of production and the consumer through his demand for the product.

However, this moral analysis assumes that the consumer has knowledge of all the morally relevant aspects of production. Without such knowledge, the consumer cannot be held responsible. Thus, a key issue in consumer activism is that of transparency, the idea that consumers must have adequate information to make informed choices with regard to the products they purchase. In the absence of informed consent or the threat of exposure, it is argued, companies have no incentive to make safe products. Consumer activists seek to create conditions of transparency either by exposing unsafe or unethical business practices or by advocating for regulations that would either require that companies meet particular standards or inform consumers of information relevant to their purchasing decisions.

Types of Consumer Activism

Many consumer activists are primarily concerned with protecting consumers from unethical or fraudulent business practices. Through use of legislation and litigation, as well as through raising public awareness, they attempt to identify and target particular companies or particular practices that they view as being unethical. Often, their work is aided through cooperation with state or local consumers affairs departments or with the Better Business Bureau, an organization of businesspeople that aims at holding businesses to high ethical standards.

This brand of consumer activism operates by providing a forum through which consumers can make one another aware of those businesses they should patronize and those they should avoid. By providing such forums, consumers thus cooperate in enforcing high ethical standards among competing businesses. Consumers given a choice between two companies offering the same product can be expected to prefer a company with a better reputation for good customer service and ethical behavior to one with a number of negative reports.

The moral presupposition of this brand of consumer activism is that it is in a company's self-interest to act ethically when it is held publicly accountable for its actions. Absent such public accountability, companies may lack sufficient incentive to moral behavior.

Another approach to consumer activism seeks to evaluate companies' claims about their products, comparing them to similar products on the market. This approach is typified by the magazine *Consumer Reports*, which evaluates and rates products to enable consumers to make informed choices among competing brands. This approach to consumer activism does not seek to make any direct moral claims but rather seeks simply to inform consumers of their available options.

Other approaches to consumer activism concern themselves with how companies treat their employees. These approaches seek to publicize companies that either violate labor laws or take advantages of gaps in the law that allow them to treat their workers in ways that are viewed by activists as failing to uphold an adequate moral standard. One case of consumer activism of this kind was the attempt made by consumer activists in the United States to raise awareness of the treatment by the manufacturer of Nike athletic shoes of many of its workers in Vietnam and Indonesia, where people were being paid low wages and were working in poor conditions. By raising this issue in a way that garnered a great deal of publicity, these activists succeeded in forcing Nike to address the issue of their treatment of workers and, in some cases, to improve working conditions.

Another, though similar approach, is one in which a company is targeted due to the treatment of workers by its subcontractors. This strategy is frequently used in the apparel industry, where well-known companies will often farm out much of their work to low-wage, and sometimes illegal, "sweatshops." Because of the difficulty of targeting these sweatshops individually, activists will often seek to exert pressure on their contract partners, who have more at stake in preserving a good reputation.

It is not clear how effective these strategies are. In the case of Nike, although the company launched a public relations campaign to restore its image, it is unclear that they made any substantial changes to their business practices in either of the countries in question. In addition, although activists tried to enlist the support of Nike's chief spokesperson, Michael Jordan, they failed to do so. In the end the campaign may have succeeded in raising the consciousness of U.S. consumers about the issue of low-wage foreign workers, but it is not clear that it did much to resolve the underlying issue. Similarly, although pressure on companies that employ sweatshop labor may have some limited effect, it does not appear to have done much to change the overall practices of the apparel industry.

Another approach to consumer activism relies on giving consumers a choice between products that meet certain ethical standards and those that do not. The "fair trade" movement, particularly in the coffee industry, has had some success in providing consumers alternatives to coffee that is grown on large plantations under exploitative conditions. Through certification and inspection programs, some brands of coffee have been recognized as "fair trade" coffees. Consumers can purchase these brands for the sake of supporting better conditions for workers in the coffee industry.

A variation on this theme involves the labeling of products to allow for informed consumer choices, for example, labeling genetically modified foods on the one hand, or labeling television programming content on the other. In each case, by allowing the consumer to know in advance what they are consuming allows them to make an informed decision as to whether or not to consume.

Yet another form of consumer activism can be seen in movements for socially responsible investing and shareholder activism. Both these strategies rely on the role of the stockholder as a form of consumer as well as an owner. Socially responsible investing involves choosing stocks on the basis of criteria of moral acceptability. For example, an investor might choose, either individually or through a mutual fund, to avoid investing in military contractors or tobacco companies. Alternatively, they might choose to invest in companies that promote particular social goods, for example, companies that promote sustainable agriculture or renewable energy. Either or both of these strategies may be used by a given investor, though the particular social screens might vary from investor to investor, or from mutual fund to mutual fund.

Shareholder activism could be thought of as the opposite strategy. Instead of avoiding investment in morally problematic companies, consumer activists might try to change a company's behavior from within, either by buying a relatively small number of shares to have the right to speak at shareholder meetings or by seeking to influence the attitudes of other shareholders with the objective of altering a company's policies.

By operating from within a company's structure, these approaches have the advantage of being perceived as coming from those having a vested interest in the financial good of the company. However, it is once again not clear whether this has been a particularly effective strategy in altering corporate policies.

Consumer activism, as the Nike example above may indicate, also has global implications. As markets become more flexible, and both labor and materials are increasingly able to transcend national boundaries, and thus the legal and regulatory oversight of particular nations, it becomes more difficult for consumers to know the conditions under which products are made, or to control those conditions. If national governments are unable or unwilling to institute or enforce labor or product safety laws, it becomes more and more necessary for activists to appeal directly to the companies themselves, either via moral suasion or via the use of bad publicity. If these appeals have the effect of eroding a company's consumer base, then the company becomes more likely to institute desired change. In the absence of a strong set of legal protections within a global economy, consumer activism becomes a more viable strategy to achieve desired aims.

Tactics of Consumer Activism

The various approaches to consumer activism discussed above each represent a strategic choice as to how they affect change in the behavior of companies. In addition, there are various tactics that can be brought to bear in consumer activist movements. Some of these tactics are relatively nonconfrontational, while others are more so.

Consciousness-raising is a large part of the work of consumer activism. Through raising the public's awareness of particular issues, activists have a greater likelihood of success at mobilizing consumer sentiment in a way that will affect company policies. Such consciousness-raising can take place on many different levels. Books, such as Nader's *Unsafe at Any Speed* or Rachel Carson's *Silent Spring*, can have a galvanizing effect on both movements and governments, but smaller efforts can include picketing, letter-writing campaigns, newspaper editorials, or exposés. These tactics can be particularly effective when companies are unable to mount a successful campaign to counter the bad publicity.

Beyond consciousness-raising, however, is the active effort to change corporate policy. A variety of tactics may be used with relatively open and cooperative companies to seek to create changes. For example, activists may seek to secure a meeting with corporate leaders to air their grievances and seek policy changes for the sake of consumers. This tactic tends to be very effective in those circumstances where activists can demonstrate that they represent a relatively broad constituency and where the issue in question is one that affects the consumer directly. In the case of many product safety and labeling issues, this tactic may prove to be quite effective, since companies are unlikely to take actions that risk alienating a significant portion of their customer base.

Activists can also turn to the courts in those cases where informal attempts at mediation fail. Class action suits can sometimes be an effective tool in addressing consumer grievances, particularly where it can be shown that a company or industry acted in a corrupt way. As a tactic to achieve change, such lawsuits can be effective, though as a means of compensating victims they may often produce limited results.

Legislation is another tactic that can be an effective tool for consumer activism. By convincing lawmakers of the need for some form of regulation or remedy, consumer activists can succeed in affecting corporate behavior precisely by making such behavior illegal or by regulating the behavior in question.

From a product safety perspective, regulation is an important tool of consumer activism. By creating legislation that created agencies such as the Food and Drug Administration, the Consumer Product Safety Administration, the Environmental Protection Agency, and the Occupational Health and Safety Administration, the U.S. Congress created a web of institutions the task of which was to ensure that consumers were provided information necessary to make informed decisions. The Securities and Exchange Commission can also be considered a consumer protection agency, insofar as its mandate is to ensure that stock transactions take place in a maximally fair and open manner.

A tactic associated, in particular, with shareholder activism involves the use of shareholder resolutions to affect company policies. Activists may seek to bring issues of concern to a company's shareholders, in an effort to mobilize them to vote in favor of changes in corporate policies. Although not frequently successful, this tactic does have the benefit of raising consciousness if done well.

Another very common technique in consumer activism is the boycott. Boycotts have been used in numerous situations, with mixed success, to affect the policies of particular companies or entire industries. The California grape boycott in the 1970s aided the worker of the United Farmworkers Union to secure the right to organize California's produce workers, while a boycott of Nestlé products had the effect of changing corporate policies regarding the marketing of baby formula in underdeveloped countries.

Boycotts are not always so successful however. When, in the 1990s, the Southern Baptist Convention urged Christians to avoid Disney World because of Disney's perceived toleration of homosexuality, the boycott fell flat, as have some other boycotts of supposedly gay friendly companies. The practice of boycotting itself has recently become less prevalent as well, in part perhaps because it sometimes seems to have the effect of harming workers while not noticeably altering corporate policies.

These tactics are among the most common, but the particular tactics used will depend on the circumstances in question, the goals sought by activists, and the receptivity of the company. If activists are perceived to represent a large movement, then these tactics may prove to be quite effective, while activists who are perceived to have an insignificant constituency may not be effective no matter what tactics they attempt. However, a movement is not always necessary for successful consumer activism. The advantage of litigation and legislation is that they do not necessarily rely on popular movements if it can be demonstrated that they are responses to violations of existing laws or deeply held moral or civic ideals. In any consumer activism campaign, however, it will be the abilities of the activists to effectively mobilize their constituency and properly choose tactics that will do much to determine the outcome of the campaign.

Conclusion

Although not all activism is consumer activism, consumer activism plays at least some part in a wide variety of movements that involve the interaction of social questions with market forces. As part of an overall strategy for social change, consumer activism has the potential to be an effective tool. By attempting to affect companies at the level of the individual purchase, consumer activism can succeed in ways that litigation or appeals to government may not. It is effective because it relies on the freedom of the consumer in a capitalist economy to buy or not buy that which he or she desires and on the ability of social movements to affect the moral sensibilities of consumers in such a way that they choose to refrain from consumption rather than lend support to an institution they deem to be acting immorally.

—Scott R. Paeth

See also Better Business Bureau (BBB); Boycotts; Coercion; Consumerism; Consumer Product Safety Commission; Consumer Protection Legislation; Consumer Rights; Consumer Sovereignty; Corporate Accountability; Corporate Moral Agency; Corporate Social Responsibility (CSR) and Corporate Social Performance (CSP); Corporate Social Responsiveness; Disclosure; Federal Trade Commission (FTC); Food and Drug Safety Legislation; Globalization; Litigation, Civil; Market Power; Regulation and Regulatory Agencies; Shareholder Activism; Shareholder Resolutions; Smith, Adam; Social Accountability (SA); Social Investment Forum; Socially Responsible Investing (SRI); Transparency

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Consumer Federation of America

The Consumer Federation of America (CFA), based in Washington, D.C., is the nation's largest consumer advocacy group. It is an umbrella of organizations and includes labor unions; state and local consumer organizations; and senior citizen, low-income, labor, farm, public power, and cooperative organizations. The initiative for founding the CFA in late 1967 came from a small group of consumer activists primarily from the labor unions, the President's Consumer Advisory Council, and the Consumers Union. At the time of its founding, it reported having 140 affiliates. By 2005 that number had climbed to 300. The CFA claims to indirectly have some 50 million members, a number that permits it to be a "voice for virtually all consumers."

The CFA was originally intended to be an information clearinghouse for its members. Lobbying was to be left to individual members. However, while CFA still has a substantial fact-finding role, it has evolved into a major lobbying force on Capitol Hill. Its staff members frequently testify before Congress on consumer-related matters. Today, its mission explicitly includes representing consumer interests before Congress and federal agencies as well as assisting its state and local members in their activities in their local jurisdictions. Other activities include commissioning surveys on consumer attitudes and product safety. The CFA also analyzes the voting records of members of Congress and produces voter guides at election time.

According to economic analysis, a genuine mass-based consumer organization cannot exist. That is because the benefits it provides are public goods. Since, by definition, public goods are available to all members of the group (here consumers) irrespective of whether they contribute to providing them, it is in the rational self-interest of all consumers to free ride. But if all members of the group free ride, then the public goods won't be supplied at all. This is the problem of collective action identified by Mancur Olson: Unless the number of individuals in a group is quite small, or unless there is coercion or some other special device to make individuals act in their common interest, rational, self-interested individuals will not act to achieve their common or group interests. It is not simply a question of organizing for political activity. Individual consumers remain rationally ignorant of the policies and programs that exploit them because it is not in the self-interest of any consumer to expend the resources to obtain such information.

Thus, the CFA provides a natural experiment for testing Olson's theory of collective action. How has the CFA overcome Olson's free rider problem? First, the CFA does not organize dispersed consumers. Its membership doesn't consist of 300 million consumers but consists of some 300-odd organizations. Second, the CFA is a service organization that provides selective incentives to its members in the form of lobbying and technical expertise.

For these reasons, the free rider problem is greatly reduced—but at a potential cost. The interests of CFA's membership may diverge from the interests of consumers. In case of conflicts, where do CFA's loyalties lie? These potential or actual conflicts of interest have provoked conservative criticisms that public interest groups such as the CFA are in reality lobbies for economic and ideological special interests.

There is evidence that the CFA can go toe to toe with other powerful Washington lobbies on behalf of consumers. This is illustrated by some of CFA's recent interests, which include consumer credit scores, USDA meat testing, credit life policies, hidden finance charges, homeowners' insurance, beanbag-type infant pillows, children's playgrounds, heating costs, home phone bills, cable TV charges, gasoline price, privacy protection, and much more. These are fairly classic consumer protection issues. The CFA is particularly alert to scams and rip-offs and hazardous products. It has been very successful at using surveys and exposes to generate free media.

On the other hand, there have also been cases where the CFA has taken stands that apparently conflict with consumer interests. Thus, the CFA has been noticeably reticent about removing trade barriers, despite the benefits for consumers of doing so, presumably out of deference to organized labor. In 1981, President Reagan fired more than 11,000 striking air traffic controllers who defied his order to return to work under the terms of the Taft-Hartley Act. The CFA supported the rehiring of the fired air traffic controllers despite its questionable link to consumer interests.

Another potential conflict of interest is ideological. The CFA has been a reliable member of the liberal coalition in Washington. It has supported the assault weapon ban and opposed the line item veto. It has also lined up in opposition to tort reform, medical malpractice reform, and class action reform. CFA's voting ratings of members of Congress have consistently favored Democrats, and its scores are highly correlated with the ratings of other liberal groups such as ADA and COPE. These positions reflect the philosophy of CFA's constituent organizations rather than that of consumers who, of course, split their votes pretty evenly between the two major parties.

Substantively, the CFA has shared liberals' traditional suspicion of market forces. Its policy positions have tended to follow a predictable pattern—prices are invariably too high. High prices, in turn, are always caused by scams, profiteering, price-gouging, windfall profits, monopoly, cartels, market power, and other predatory and anticompetitive practices. Consumers are unsophisticated and no match for powerful businesses. Therefore, government's thumb (or visible hand) is necessary to tip the scales in favor of consumers. As a result, the CFA has tended to call for more regulation, price controls, product recalls, and tougher enforcement of consumer protection laws.

CFA's critics (particularly economists) have charged it with trying to protect consumers from the scourge of lower prices. The CFA has allegedly ignored the costs to consumers of increased government regulation. Another charge is that the CFA takes away from consumers the right to determine how much safety to buy. According to the pro–free enterprise Competitive Enterprise Institute, consumer groups think they know better than consumers what consumers want. Another criticism is that the CFA hypes dangers associated with products.

Over time CFA's views have evolved. Today, the CFA is readier than it was to accept market forces as part of the solution. This pragmatism is evident in its positions on energy markets. In the 1970s and 1980s, the CFA was adamantly opposed to the deregulation of the prices of oil and gas. The CFA denounced President Carter's plan to gradually decontrol oil prices. Today, the CFA still maintains that energy markets are being manipulated and that oil companies purposely minimize their inventories to create artificial shortages and higher prices. However, while the CFA still endorses a windfall profit tax, it soft-pedals the tax and (rhetorically at least) embraces increased competition. In recent congressional testimony, the CFA has said, "Our preferred approach is to find ways to introduce more competition. . . ." "No amount of consumer protection . . . can make up for a market that suffers from fundamental competitive flaws." The CFA now sees regulation as a second-best solution. But the CFA is still quick to conclude that market forces have failed consumers.

—Ian Maitland

See also Asymmetric Information; Consumer Product Safety Commission; Consumer Protection Legislation; Free Riders; Interest Groups; Public Goods; Public Interest

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Consumer Fraud

Fraud is a purposeful, unlawful act to deceive, manipulate, or provide false statements to damage others. In general, fraud is viewed as false communication that conceals or contains a scheme to create a materially false statement or representation. Often, fraud is associated with documents that are transmitted by mail, wire, or through any type of electronic signal to a receiver. Statements that a court determines as false or fictitious or that have the intent to deceive constitute a crime and are subject to a fine or imprisonment or both. In 2005, fraud cost U.S. organizations more than $600 billion annually, and consumers lose more than $30 billion annually from fraud. The U.S. Department of Justice has identified major categories of consumer fraud including identity theft and fraud, solicitation of donations for victims of terrorist attacks, Internet fraud, telemarketing fraud, bank fraud, and mortgage scams. Mail and wire fraud is a broad category that captures many consumer and business fraudulent activities.

Types of Fraud

The *mail fraud* statute, first enacted in 1872, enabled the government to prosecute undesirable activity (e.g., securities fraud, real estate scams, etc.) years before such behavior was specifically outlawed by other laws. In 1994, Congress amended the mail fraud statute by adding the words "any private or commercial interstate carrier" to the mail fraud statute. As a result, delivering communications or merchandise via carriers such as FedEx and UPS as part of their fraudulent scheme will now violate the law.

The *wire fraud* statute was patterned after the mail fraud statute, and judicial analysis of one applies with equal force to both. When combined with wording in the mail fraud statute that prohibits fraudulent schemes involving interstate transmission of "wire, radio, or television communication . . . writings, signs, signals, pictures, or sounds," these provisions give the federal government virtually unlimited jurisdiction to regulate direct marketing activity through mail and wire fraud legislation.

Telemarketing fraud is a term that refers generally to any scheme in which the persons carrying out the scheme use false statements carried over the telephone. Most typically, fraudulent telemarketers will include current business trends or widely publicized news events as references in their attempts to solicit victims. Types of telemarketing schemes include charity schemes, credit cards, investment schemes, lottery schemes, office supply schemes, prize promotion schemes, and so on. The Federal Trade Commission (FTC) indicates that sweepstakes and lottery fraud were among the top 10 complaints filed in 2004. An AARP study, based on a survey, indicates that lottery victims are likely to be older, with an average age of 74.5 years, and more likely to be women living alone.

Internet fraud refers to any type of scheme involving the Internet, such as chat rooms, e-mail, message boards, or Web sites, to present fraudulent solicitations to perspective victims, to conduct fraudulent transactions, or to transmit proceeds of fraud to financial institutions or to others connected with the scheme. Consumers are increasingly worried about becoming victims of online fraud. Among the complaints and accusations is "shell bidding" in online auctions, which involves sellers bidding on their own items to heighten interest and competitive bidding. Another problem is sellers not delivering promised items after receiving the buyers' funds. *Phishing* is a general term for criminals' creation and use of e-mails and Web sites that are designed to look legitimate but deceive Internet users into providing personal data.

Identity theft and *identity fraud* are crimes in which someone obtains and uses another person's personal information in some way that involves fraud or deception, typically for economic gain. In 2005, more than 40 million credit card holders were susceptible to the loss of personal information and identity theft when their Visa, MasterCard, and other credit card data were compromised. In 2006, the number of identity theft complaints increased 5% over the previous year; however, the annual losses increased much more rapidly reaching $680 million. Credit card fraud loss has been slowed by corporate investment in antifraud technologies and risk management systems. Visa USA reports its fraud losses at 6 cents out of every $100 processed, down from 12 cents a decade ago. Child identity theft also increased steadily.

A growing area of identity theft is the theft of employee records. In 2006, the personal information of more than 26.5 million U.S. veterans was stolen. As the top consumer fraud complaint filed with the FTC, identity theft is becoming an increasingly important risk area for companies to manage. Often, personnel identity theft occurs as an "inside job." A disgruntled, departing, or opportunistic employee sees the revenue potential from selling personal data of employees. Companies and employees are working to control notebooks and hard drives that contain sensitive employee data. Employers who exhibit negligence in this area can be susceptible to civil lawsuits from employees who have been affected.

In response to the September 11, 2001, terrorist attacks on the United States, *terrorist attack fraud schemes* have become a major concern. Consumer groups and members of the public have reported receiving unsolicited e-mail messages that urge people to donate money to the Red Cross or to funds for victims of the attacks and their families. Some of these e-mails are sincere and reputable; others try to encourage donors to leave valuable personal and financial data, such as credit card numbers at Internet Web sites not affiliated with legitimate charitable organizations. Fraudulent telemarketers have been involved in suggesting that a portion of magazine subscriptions will be used to provide disaster recovery and relief.

Mortgage scams use taglines such as "trouble making your home mortgage," "are you facing foreclosure," and so on. Fraudulent assistance with mortgages and false mortgage rates with fees are a growing category of consumer fraud.

The FTC enters Internet, telemarketing, identify theft, and other fraud-related complaints into *Consumer Sentinel*, an online database made available to civil and criminal law enforcement agencies worldwide. In 2005, the most prevalent form of fraud, based on complaints, was identity theft (37%); Internet auctions (12%); foreign money offers (8%); shop-at-home and catalog sales (8%); prizes, sweepstakes, and lotteries (7%); Internet services and computer complaints (5%); business opportunities and work-at-home plans (2%); advance loan and credit protection (2%); and others (17%). The total consumer fraud complaints in 2005 totaled 686,683, up slightly from the previous year.

Fraud Perpetrated by Consumers

Consumer fraud involves intentional deception to derive an unfair economic advantage by an individual or group over an organization. Examples of fraudulent activities include shoplifting, collusion or duplicity, and guile. Collusion typically involves an employee who assists the consumer in fraud. For example, a cashier may not ring up all merchandise or may give an unwarranted discount. Duplicity may involve a consumer staging an accident in a grocery store and then seeking damages against the store for its lack of attention to safety. A consumer may purchase, wear, and then return an item of clothing for a full refund. In other situations, the consumer may ask for a refund by claiming a defect. Although some of these acts warrant legal prosecution, they can be very difficult to prove, and many companies are reluctant to accuse patrons of a crime when there is no way to verify it. Businesses that operate with the "customer is always right" philosophy have found that some consumers will take advantage of this promise and have, therefore, modified return policies to curb unfair use.

Fraud Perpetrated by Organizations

If a consumer believes that a product is not worth the price paid for one reason or another or perhaps because he or she believes the product's benefits have been exaggerated by the seller, there may be reason to investigate the possibility of fraud. For example, although some marketers claim that their creams, pills, special massages, and other techniques can reduce or even eliminate cellulite, most medical experts and dermatologists believe that only exercise and weight loss can reduce the appearance of this undesirable condition. If consumers believe that a firm has not fulfilled its basic economic responsibilities, they may ask for a refund, tell others about their bad experience, discontinue their patronage, contact a consumer agency, and even seek legal redress. Many consumer and government agencies keep track of consumer complaints.

To protect consumers and provide businesses with guidance, a number of laws and regulations have been enacted to ensure that economic responsibility is met in accordance with institutionalized standards. The FTC works to stem unfair and deceptive trade practices through both law enforcement and consumer education. The FTC tries to alert as many consumers as possible to telltale signs of fraud. Working with a variety of partners (e.g., other federal agencies, state and local consumer protection agencies, trade associations, professional organizations, volunteer groups, corporations, the Better Business Bureau, the military, and extension agencies), the FTC's goal is to disseminate information to consumers and businesses to prevent fraud.

—O. C. Ferrell and Linda Ferrell

See also Accountability; Better Business Bureau (BBB); Business Ethics; Consumer Protection Legislation; Consumer's Bill of Rights; Ethical Culture and Climate

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Consumer Goods

Consumer goods is a generalized term for any product or service purchased primarily for personal, family, or household uses. Consumer goods such as clothing, foodstuffs, or toys are intended to satisfy human wants and needs through their direct consumption or use. Capital goods, in contrast to consumer goods, are purchased by individuals or organizations to produce other products and services that are sold to or provided for other individuals or organizations. According to their usage, many goods (e.g., cars, telephones, or personal computers) can be categorized either as consumer goods or as capital goods.

The term *consumer* traditionally refers to the ultimate user of products, ideas, and services. Beyond that, the term is also used to characterize the buyer or decision maker. A mother buying semolina pudding for consumption by a small child is often called the consumer although she is not the ultimate user.

Categories of Consumer Goods

Consumer goods can be classified in different ways. Depending on the *frequency and duration of their usage,* the following categories can be distinguished:

- *Durable goods* can be used repeatedly or continuously for an extended period of time. This category comprises, for example, furniture, bicycles, and major household appliances.
- *Semidurable goods* can be used on multiple occasions and have an expected lifetime of about 1 year, such as clothing and footwear.
- *Nondurable goods* are normally consumed in one or a few uses. Groceries, gasoline, and tobacco products belong to this category. In practice, nondurable goods also include a few goods of little value that are used more than once, such as household supplies.

Marketers usually classify consumer goods on the basis of the *type of the buying decision process*. Varying marketing strategies and instruments are used to market products and services belonging to the different classes of goods:

- *Convenience goods* are those that the consumer usually purchases frequently, often on impulse, with little time and effort spent on the buying process. Examples include toothpaste, newspapers, and candy bars. Convenience products usually are low-priced, and marketers place them in many locations to make them readily available for customers.
- *Shopping goods* are less frequently bought consumer products and services that the consumer, in the process of selection and purchase, usually compares carefully on bases such as suitability, quality, price, and style. Examples include furniture, a used car, a better dress, or hair treatment for which the consumer is willing to spend considerable time and effort in gathering information on relevant product attributes. Several retail outlets are customarily visited. Marketers usually distribute their products through fewer outlets but provide deeper sales support to help customers in their comparison efforts.
- *Specialty goods* are high-risk, expensive, and very infrequently bought consumer products and services. They have unique attributes or other characteristics that make them singularly important to the buyer and require an extensive problem-solving decision process. Consumers make a special purchasing effort to buy products such as specific brands and types of cars, designer clothes, and the services of legal specialists. The products in this category need very specialist retailing that will provide a high level of augmented product services, both before and after sale.
- *Unsought goods* are consumer products and services that the consumer either does not know about or knows about but does not normally think of buying. Most major product innovations are unsought until the consumer becomes aware of them through advertising. Examples of unsought goods are life insurance, gravestones, and encyclopedias. To sell these goods, marketers make a lot of advertising, personal selling, and other marketing efforts.

Consumers' Perceptions of Products and Services

Consumers have different *types of product knowledge* that they can use to make purchase decisions. When developing marketing strategies, marketers analyze and focus on different levels of consumers' product knowledge. Consumers can think about *products as bundles of attributes.* Even the simplest products have several attributes (e.g., pencils have varying lead densities, softness of erasers, shapes, and colors). More complex products such as cars and DVD players have many attributes. When deciding which products to buy, consumers usually consider only a few selected product attributes. Consumers often think about *products as bundles of benefits.* Benefits are the desirable consequences consumers seek when buying and using products and brands (e.g., Consumer A wants a toothpaste that whitens the teeth; Consumer B wants a toothpaste that prevents tooth decay). Consumers also assess the personal, symbolic *values* that goods help them to satisfy or achieve.

Consumers can also be aware of a variety of *negative consequences* that might occur when they buy and use products. Several consumers worry about negative ecological consequences such as air pollution of a sporty car with fast acceleration. More and more consumers also are aware of negative social and ethical issues that are related to the production and consumption of many consumer goods such as textiles, footwear, or toys. They have heard, for example, about child labor or other insufficient or even dangerous working conditions in textile factories in the Far East or in Central and South America. Because consumers hesitate to purchase products they associate with negative social performance, firms try to behave in an ethical manner and communicate their ethical conduct to their stakeholders to positively affect product sales and the image of the company. This is one of the reasons for the rise of marketing ethics and the corporate social responsibility or "corporate citizenship" movement. However, although a number of surveys show that consumers care about the ethical performance of a company, only a few consumers actually place ethics at the top of their list in making purchasing decisions. At present, price, quality, and value outweigh ethical criteria in shaping consumer purchase behavior.

—Sonja Grabner-Kräuter

See also Consumer Preferences; Corporate Citizenship; Corporate Social Responsibility (CSR) and Corporate Social Performance (CSP); Green Marketing; Marketing, Ethics of

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CONSUMERISM

The term *consumerism* may be understood using four distinct interpretations. These interpretations are as follows: (1) the movement within society and government to protect consumers from defective or otherwise unsafe products; (2) the demand-side economic theory (usually associated with Keynesian economics), which states that increasing consumption of consumer goods drives economic growth as opposed to encouraging higher rates of saving as a national economic policy; (3) a societal state in which happiness or success is somehow equated with increased consumption and a concomitant creation of limitless demand; and (4) a combination of the second and third meanings in which an emphasis of advertising and marketing is concentrated on the creation of consumers within a culture that embody limitless demand. Each of these meanings of consumerism has specific and important application in the understanding of business and society and, ultimately, in our collective ability to pursue sustainability.

The first meaning of consumerism can be traced to the Latin maxim *caveat emptor* (buyer beware). In the United States, government and societal actions to protect consumers predate the creation of a consumer protection agency within the Department of Agriculture in 1862. As more citizens became dependent on others for food and essential materials for daily life, consumers of these products began to demand standards of quality and a mechanism for the assurance of the safety and wholesomeness of these products. It was not until 1906 that legislation was passed to create the first version of the Food and Drug Administration (FDA). This government agency has grown in importance and purview as the variety of products and dependence on commercial sources for these products has increased. However, the FDA covers a bounded spectrum of consumer goods; in 1914, the Federal Trade Commission was created to regulate other types of goods and services. Still, for many, the true start of modern consumerism dates to the 1960s when consumer activists such as Ralph Nader began to influence public perception, culminating in legislation of, for example, the Consumer Products Safety Act of 1972 and the earlier Motor Safety Act of 1966. Since that time, there have been many other actions to protect consumer interests; for example, producers and service providers have lobbied Congress to reduce restrictions and liability standards on the grounds that it reduces competition and it restricts consumer choice.

The second way that the word consumerism is used is to express the idea that increasing consumer demand can be the engine that drives a healthy national economy. While this is an oversimplification of one element of Keynesian economic theory, it is sufficient for our purpose of understanding this usage of consumerism. The important contrast of this usage of the term *consumerism* with the first usage is that there is a shift away *from* saving money in banks as a national priority, which is an important element of capital formation in early capitalism, *to* an emphasis on consumer spending as a means of economic stimulus and continued economic growth. This manifestation of consumerism as put into national policy is exemplified by the exhortation of President George W. Bush for consumers/citizens to spend the tax surplus that he rebated and/or cut for some taxpayers. The idea was to spend our way out of an economic slowdown after the revaluation of stocks and resultant portfolio deflation of 2000 and in the wake of national trauma in 2001.

The third way that the word consumerism is used expresses the idea that increasing material consumption increases personal and societal well-being. As with the first meaning, this definition reframes an age-old debate stretching back to early Buddhism and Christianity. In both these traditions, material wealth is presented as an obstacle to true happiness and contentedness. In contemporary society, we are confronted with a confluence of issues as we are encouraged to tie happiness and status to ownership of material goods thus creating the pressure for cheap consumer goods. As a result, contemporary societies can experience internal conflict, as, for example, when premium priced goods are marketed to populations that often exist below or at the poverty line. Societies that experience this conflict are then forced to consider the consequences of the demand for cheap and abundant consumer goods in terms of the need for sustainable practices and fair hourly wage rates. The consumer society in the United States of America is confronted with declining employment in the manufacturing sector, including substantial losses of market share in entire industries, such as textiles and consumer electronics, and huge workforce reductions by major companies in the automotive sector (once a bellwether for the health of the entire U.S. economy). In addition, there is a growing national trade imbalance with foreign trading partners, most notably China. Finally, in terms of national and global *sustainability,* some would argue that any practice that advocates unexamined consumption of goods and services renders the concept of sustainability unattainable.

The fourth way that the word consumerism is used embodies the combined mechanism to achieve both the economic goal of fueling growth by ever-increasing demand as well as the cultural state of equating self-worth and happiness with consumption. For some believers of this type of consumerism, sometimes presented as an implied state of grace, goodness is tied to limitless consumption and the ability to practice this behavior. Advertising and marketing executives are assigned the task of quantifying and qualifying the desires of target markets and packaging consumer goods in ways that fit those needs. However, after generations of improved marketing and advertising techniques, some scholars would argue that demand is being created for consumer goods and not actually serving real needs. In this fourth understanding of consumerism, it has been suggested that creating unlimited and diverse demand through media campaigns has made *the act of consumption* the product, instead of providing knowledge about items people need.

—David H. Saiia

See also Capitalism; Consumer Activism; Consumer Federation of America; Consumer Fraud; Consumer Preferences; Consumer Protection Legislation; Consumer Rights; Consumer Sovereignty; Corporate Citizenship; Corporate Ecology; Deceptive Advertising; Free Market; Just Price; Just Wage; Living Wage; Pricing, Ethical Issues in; Product Liability; Sustainability

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Consumer Preferences

Consumer preferences represent the building block for assessing the value of any good or service relative to another. Once determined, a consumer may or may not wish to reveal a willingness to pay for an item given the asking price. Of course, assessing value is not always straightforward for the consumer. It can be an amalgamation of economic, aesthetic, and moral characteristics that are uniquely determined and weighted by each individual consumer. Of course, there may be a tension among those characteristics. As a result, a consumer's preferences could be highly flexible given changes in both his or her and society's outlooks. For example, the thought of purchasing a large sport utility vehicle may satisfy a personal preference for a powerful and spacious vehicle; but, at the same time, it may have to be reconciled with a social preference for reduced petroleum dependency and carbon dioxide emissions.

By reconciling the inherent tension, the consumer could assign a level of satisfaction (technically called marginal utility, *MU*) derived from owning a unit of the item in question. The way these marginal utilities change over different units of an item, as well as across units of other items, establishes the profile of the consumer's preferences. When an item is preferred over others, it is useful to consider this in terms of a range of purchasable items constrained by their prices (*P*) and the purchasing power of the consumer. After all, possessing a preference for an item that is not affordable does not say much about a consumer's actual purchasing patterns.

To understand and model consumer preferences, certain assumptions must be made. An important one is to assume that consumers behave rationally. For example, the assumption of consistency means that if one unit of Item A is preferred to one of B, then the opposite cannot be true at the same point in time. The assumption of transitivity means that if one unit of B is preferred to one unit of C, then the latter could not have been preferred to one unit of A. It is also useful to assume that marginal utility diminishes and the consumer can become satiated as more units of a particular item are purchased. In that case, one cannot say that Item A is *always* preferred to B because it depends on how many units of each the consumer possesses or has consumed. For example, consider a thirsty consumer on a hot day. Given a choice, he or she will likely use a vending machine dispensing sodas before one dispensing candy bars. Being thirsty the consumer will pay for any successive sodas he or she can afford up to and until the thirst is quenched. In effect, the consumer is trading off candy bars for sodas, but this trade-off is becoming less and less pronounced because of diminishing marginal utility for sodas. The first soda to a parched consumer is the one giving the greatest satisfaction and, therefore, worthy of foregoing the greatest amount of candy bars. But as the consumer's thirst is quenched a candy bar will become worthy of foregoing sodas. Of course, preferences for something habitual or compulsive may take a lot of purchases before satiation is reached. This helps explain the behavior of compulsive gamblers, alcoholics, and consumers with large credit card debts.

Since prices are assigned to goods and services, consumers face limits on their purchasing power. Thus, another useful assumption is that consumers wish to spend their disposable income so as to maximize their total satisfaction (technically called total utility) over the range of purchasable items they desire. In this context, it is the marginal utility per dollar spent on the item (i.e., MU/P) that is important because it shows the cost of achieving a level of satisfaction. A consumer will have maximized his or her total utility when the following occurs: $MU_A/P_A = MU_B/P_B = MU_C/P_C = \ldots = MU_n/P_n$. If this were not true, the consumer could reallocate \$1 from one item to another and increase the total utility. In reality, consumers cannot always satisfy the above equation because indivisible units of A, B, C, and so on cannot be broken down into fractions of a unit. However, it should be noticed that by satisfying the equation the consumer is in equilibrium whereby the relative cost of acquiring an extra level of satisfaction for any of the items is equal. For example, consider a consumer at a baseball game who can simultaneously purchase sodas, candy bars, and bags of peanuts over the duration of the game. He or she would first purchase the item providing the highest marginal utility per dollar, then the next, and so on. Because of diminishing marginal utility, the ratio for each item falls as more of it is purchased; and the ratios begin to align according to the equation.

Note that prices indicate a cost for consumption. So if the price of an item were high enough a consumer's preference is constrained. But in terms of the habitual and compulsive items noted above, could price be irrelevant to the decision process? Possibly so, to the extent that disposable income is being spent (or debt is accumulated) to satisfy a preference at the expense of items that would add to one's physical health, family stability, and so on. This raises the question as to when the government ought to intervene and attempt to constrain one's freedom of choice. Certainly, illicit drugs are a case in point.

Since consumer preferences are individualized and subjective, it is controversial to compare levels of satisfaction across consumers. A unit of satisfaction to one consumer cannot readily be compared with that of another. Of course, such comparisons are often made in the political arena; for example, taxing one group to redistribute wealth to another. Does the gain in satisfaction by the subsidized group outweigh the loss in satisfaction by the taxed group? It is hard to say.

Also in the realm of government action and consumer preferences is the concept of a pure public good. In terms of consumption such goods are nonrival and nonexcludible. This means that one person's use in no way affects another's; and it is very costly to try to exclude someone else from enjoying the good if it is already provided to another. The classic example is national defense since all citizens can feel equally protected by the armed forces while it makes no sense to exclude a citizen from protection if thousands around him want the protection. Of course, pure public goods cannot be provided in the marketplace because of the incentive the consumer has to free ride. A free rider could choose not to reveal a true preference for the good knowing that the others will and, in effect, pay for the joint consumption of the public good. Of course, if enough consumers decide to free ride the good may not be provided at all. To overcome this problem, the government simply provides the good to all and taxes all consumers using some politically agreed-to tax formula.

Do consumers compare their levels of satisfaction to others? Such interpersonal utility comparisons do take place in the real world but they are difficult to model. For example, Consumer 1 may feel better-off with a $10 prize; but he may feel less so (possibly worse off) if those close to him won prizes of, say, $100. Consumer 1's preferences are dependent in some way on others whose are, in turn, dependent on his. An example of such interdependence is the phenomenon that Thorstein Veblen called conspicuous consumption. The consumer's preference for an item is determined not just in its personal use but in how its ownership is perceived by others.

Also difficult is an attempt to aggregate preferences in some way so as to derive a representation of the collective preferences of all consumers. The result, if achieved, is called a social welfare function. Such a construct would be useful in political decision making (but its existence is tenuous). In fact, Kenneth Arrow developed a theorem showing the impossibility of constructing a social welfare function short of all consumers being identical or having them acquiesce their preferences to an authority figure who would make their decisions for them.

Aggregating preferences assumes that levels of satisfaction can be examined in a cardinal sense; that is, a unit of satisfaction for Consumer 1 always equals a certain number of units for Consumer 2. But even ordinal problems can arise. For example, rational voters each having transitivity across their preference ordering can, under real circumstances, exhibit collective intransitivity that leads to uncertain collective choices. This so-called voters' paradox, as noted by Arrow, makes for an unstable environment for politicians when they try to assess the needs of consumers in their jurisdiction.

Consumer preferences represent an attitude while actually making a choice involves an action. Preferences may be honed over time while, often times, choices have to be made quickly. As such, seemingly irrational decision making may simply reflect the constraints the consumer faces. Preferences, in that context, are taken as intrinsic but they are subject to further learning and evolution.

—Darren Prokop

See also Consumer Sovereignty; Marginal Utility; Revealed Preference

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Consumer Product Safety Commission

The Consumer Product Safety Commission (CPSC) was created by the Consumer Product Safety Act of 1972 to protect the public against unreasonable risks of injury associated with a wide range of consumer products. The rationale for this act came from a national commission study on product safety, which found that 20 million Americans were injured severely enough each year because of product-related accidents to require medical treatment. Some 110,000 of these people were permanently disabled and 30,000 were killed at a cost to the country of more than $5.5 billion annually. Thus, a crisis situation was believed to exist that demanded government attention, and the solution was direct regulation.

From an ethical point of view, it was believed that market forces alone did not assure that the public was protected adequately from unsafe and dangerous products. Under competitive pressures, business was likely to slight safety concerns and lessen its adherence to the principle of "do no harm" with regard to the products it put on the market. As products grew more sophisticated, consumers were less likely to know about the risks these products might pose to their health and welfare. Private organizations, such as Consumer Reports, which tested products, were not able to provide enough protection, and thus, it is was believed necessary to create a government agency with the expertise to fulfill this function.

The CPSC is a five-member commission headquartered in Washington, D.C., with several field offices and testing laboratories around the country. The commission has jurisdiction over some 15,000 types of consumer products ranging from automatic-drip coffee makers to toys to lawn mowers. The only consumer products not covered by the act are foods, drugs, cosmetics, automobiles, firearms, tobacco, boats, pesticides, and aircraft, all of which are regulated by other agencies. The CPSC was also given responsibility for enforcing specific consumer legislation including the Flammable Fabrics Act, the Refrigerator Safety Act, the Hazardous Substances Act, and the Poison Prevention Packaging Act.

The CPSC has the authority and responsibility to (1) develop and enforce uniform safety standards governing the design, construction, contents, performance, and labeling of consumer products under its jurisdiction; (2) develop voluntary standards with industry cooperation; (3) ban products if no feasible standard would adequately protect the public; (4) initiate the recall of products deemed to be hazardous or arranging for their repair; (5) conduct research on potential product hazards; and (6) inform and educate consumers through the media, state and local governments, and private organizations and by responding to consumer inquiries.

Regarding its enforcement powers, the commission can order a manufacturer, wholesaler, distributor, or retailer to recall, repair, or replace any product that it determines to be unreasonably risky in the course of its research. Where the action is deemed to be justified because of the hazard involved, the commission can simply ban the product from the market. In addition, the act also requires manufacturers, wholesalers, distributors, or retailers to report the existence of any substantial hazard that is known within 24 hours of discovery. The commission can then demand corrective action including refunds, recalls, public hearings, and reimbursement of buyers for expenses they incur in the process.

The Consumer Product Safety Amendments of 1981 changed the rule-making procedures of the commission by placing more emphasis on voluntary standards. An advanced notice of proposed rule making has to invite the development of a voluntary standard. The commission must then assist industry in developing a voluntary standard, and if it appears likely that this standard will eliminate or adequately reduce the risk of injury, and it is likely that there will be substantial compliance with the standard, the CPSC must terminate its mandatory rule-making effort and defer to the voluntary standard. This provision, along with other provisions in the amendments, severely restricted the agency's rule-making authority.

In creating the agency, Congress emphasized the importance of information sharing; thus, the agency maintains a National Injury Information Clearinghouse that provides injury data from electronic data sources and disseminates statistics and information related to the prevention of death and injury associated with consumer products. The Clearinghouse responds to 6,000 requests for information of this nature from the American public each year, and information specialists search agency databases to tailor responses to each customer's needs.

The CPSC gathers data about product-related injuries through a National Electronic Injury Surveillance System (NEISS). This system consists of a sample of hospitals that are statistically representative of hospital emergency rooms nationwide. Data are collected on a broad range of injury-related issues, covering hundreds of product categories. From these data, estimates can be made of the numbers of injuries associated with consumer products, and national estimates of the number and severity of product-related injuries can be provided. In 1966, the CPSC introduced a publication called the *Consumer Product Safety Review,* which includes national injury data from NEISS hospitals, studies of emerging and continuing hazards, and important recall and correction action activities.

During his first term of office, President George W. Bush asked all federal agencies to give a high priority to their communications with the public and improve the ability of agencies to share information with each other to enhance public security. To comply with this request and provide better service in alerting the American people to unsafe, hazardous, or defective products, six federal agencies with vastly different jurisdictions joined together to create www.recalls.gov, a Web site that provides links to all federal agencies with statutory authority to issue recalls. This includes the CPSC, the Food and Drug Administration, the Environmental Protection Agency, the U.S. Coast Guard, the National Highway Traffic Safety Administration, and the U.S. Department of Agriculture.

In 2005, the CPSC announced an agreement with the Canadian government aimed at further improving consumer safety in both U.S. and Canadian marketplaces. The agreement calls for both countries to share inspection and laboratory results when it is appropriate and for increased harmonization of both existing and prospective safety standards and the exchange of more information related to safety research and other findings. When a product violates a Canadian safety standard or poses a danger to Canadian consumers, Health Canada agreed to provide advance notification to the CPSC if the product is intended for export to the United States. Canadian officials will inform the CPSC of the content of the shipment and intended importer so the agency can take appropriate steps to ensure protection of American consumers.

—Rogene A. Buchholz

See also Regulation and Regulatory Agencies

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Consumer Protection Legislation

Consumer protection regulation refers to government involvement in the marketplace to protect consumers in commercial transactions from potential harm caused by businesses. The potential harm may arise from the use of unreliable or unsafe products, deceptive advertising, asymmetry of knowledge of products and services, and privacy intrusion in the Internet age. In the United States, the federal and state governments took important steps in consumer protection, especially in the late 1960s and 1970s. Before this, the ancient rule of *caveat emptor*, or "let the buyer beware," generally guided consumer transactions. Although consumer protection regulation did exist (e.g., the 1906 Food and Drug Act, the creation of Federal Trade Commission [FTC] in 1914), it was limited and weakly enforced.

The surge of government protection regulation in the 1960s and 1970s derives from a strong consumer movement and the general politics of the time. The 1980s, however, saw a decrease in support for consumer protection regulation. The Reagan administration cut budgets and staffing sharply and was later forced to restore much of the cuts in support for consumer protection regulation due to regulatory failures. Although the Clinton administration was more aggressively involved in consumer regulation in the 1990s, there have been very sharp cuts during the Bush years in the 2000s. The current consumer protection regulation has addressed issues related to the digital age as well, such as consumer privacy.

Both the federal and state governments are responsible for consumer protection regulation. The key federal agencies involved in consumer regulation include cross-industry regulatory agencies, such as the FTC and the Consumer Product Safety Commission (CPSC), and industry-specific agencies, such as the Food and Drug Administration (FDA), the National Highway Traffic Safety Administration (NHTSA), and the U.S. Department of Agriculture (USDA). At the state level, regulatory responsibilities reside with the state attorney general and a number of state agencies that promulgate regulations. However, for reasons such as politics of the state and budget constraints, all states are not equally forceful in consumer regulation. In some states, the attorney general actively defends consumer interests; in others, she of he protects local industries, often accepting political contributions from them. In other words, state laws place different burdens on the state attorney general to act as a defender of consumer interests, investigating and bringing cases against firms under state consumer protection statues. In states that lack effective state enforcement of consumer laws, consumers often act as "a private attorney general" by resorting to tort laws and suing businesses for incurring harms or injuries. Although state regulation remains crucial, the focus here is on consumer protection regulation at the federal level. The following part discusses the two aspects of consumer protection regulation: the need for consumer protection and the areas of consumer protection.

The Need for Consumer Protection

The Argument Against Government Regulation

Though consumer protection regulation is widely regarded as necessary for the well-being of consumers, some scholars take a different stance. Milton Friedman, for example, argues that government legislation on consumer protection is, in general, an intervention in the free market system and that an efficient market system without fraud, deceit, or coercion will take care of consumer interests. He maintains that government regulation on consumer protection disrupts the free market system in various ways: suppressing innovation, limiting consumer choices, and raising product prices. Such intervention, according to Friedman, can only result in market inefficiency. For example, the FDA, a government regulatory agency, Friedman maintains, does more harm than good. Friedman asserts that the FDA can make two types of errors: (1) approves a drug that has harmful effects on patients and (2) refuses or delays approving a drug that can save the lives of millions of people. While the first error, according to Friedman, is traceable and can be documented, the second worries him the most. Friedman warns that the nature of the bureaucracy is such that even the best-intentioned and most benevolent individuals are led to reject a drug that has the slightest possibility of harmful side effects.

The Argument for Government Regulation

Friedman's arguments against government regulation derive from his faith in an efficient market system. With the tremendous power that corporations hold today, critics challenge the efficiency of the marketplace. Stone, for instance, argues that although the market generally allocates resources efficiently, it does not solve all the problems in the system. Very often, the consumer does not have perfect information to determine whether she of he may be injured by a product. Elbing and Elbing, for another example, also point out that the marketplace is dominated by business; consequently, consumer power is weak, compared with the power of business. The following demonstrates some of the issues in the marketplace that call for consumer protection.

Unsafe Products

The issue of product safety involves a wide range of industries. For example, Ralph Nader's exposure of the unsafe features of the Corvair in 1965 illustrates the need for government to regulate the automobile industry for safety reasons. In addition, the extensive use of food additives and preservatives has created potential public health hazards. The risk of pesticide residues is another source of concern. Recently, biotechnological companies, such as Monsanto, have introduced genetically modified foods to developing countries before thorough knowledge of their side effects has been established. In short, the hazards that a wide range of consumer products pose to human safety and health compel government regulation.

Deceptive Advertising

A deceptive advertisement is one that includes a distortion or omission about a product or service that misleads a consumer. Deceptive advertising causes consumers to make purchasing decisions based on false beliefs about the nature of the products. It hinders the flow of information in the marketplace. For example, in the 1940s, R. J. Reynolds, a tobacco company, with the knowledge of harmful effects of smoking on health, declared to consumers that "More Doctors Smoke Camels." In the 1950s, Lorillard Tobacco Company claimed that the micronite filter in Kent Cigarettes was so safe and effective that it had been selected to help filter the air in hospital operating rooms. The deceptive advertising misled people to consume a hazardous product that often resulted in diseases and deaths.

Asymmetry of Information

In light of modern technology, many products are becoming highly complex. Some products, such as Intel processing chips, are hidden inside already complex products such as computers so that consumers cannot even see them. Consumers, no matter how technologically savvy they are, have difficulty judging the merit of some products in today's high-tech society. In other words, the complexity of products also obscures adequate information in the marketplace. This asymmetry of information can play into the hands of opportunistic sellers. In addition, the specialization of services also hinders consumers from being clearly informed about the services they receive. The specialized knowledge of professions, such as attorneys, dentists, and financial and insurance brokers, can baffle a consumer seeking services in these areas.

Privacy Intrusion

In the Internet age, consumer privacy has become more vulnerable. Whenever one uses a credit card online or surfs or shops on the Internet, one risks revealing unique personal information—credit card numbers, birth date, hobbies, and purchasing characteristics and preferences. New technology allows businesses to gather personal data about their customers; however, people, in general, are not comfortable with this information collection, especially when they do not know who is collecting the information and what they are going to do with it.

Areas of Consumer Protection

Consumer protection regulation seeks to fulfill several goals. Owing to the potential existence of unsafe products, one area of consumer protection is *hazard avoidance.* The major method of regulating potential hazardous products has been the issuance of standards, which are typically used to provide necessary information to consumers. The CPSC plays a key role in protecting consumers from harms caused by unsafe products. It regulates the manufacture and sale of more than 15,000 types of products, including toys, swimming pools, and consumer electronic products. Furthermore, individual industry agencies are also responsible for setting industry-specific safety standards. For example, the NHTSA sets motor vehicle standards; the FDA sets safety standards for food, drugs, food additives, cosmetics, and medical devices; and the USDA sets guidelines regarding the labeling of genetically modified foods.

To redress harms that have been caused, consumers most often resort to product-liability torts for cases involving personal injury or death from product use. Product liability refers to burden of responsibility on the supplier side for damage caused through consumers' use of a product. Damage is attributed to any or all parties throughout the manufacturing and the distribution chain. Strict liability is sometimes at work when it comes to product liability: The manufacturer or supplier is held solely responsible for harm done to a consumer through the use of a product, even if the consumer was negligent in using the product. For example, McDonald's huge settlement with an elderly New Mexico woman in 1994, who spilled McDonald's hot coffee in her lap and was severely burned, exemplifies the extent of strict liability. In the late 1990s, about 20% of noncriminal cases in the United States were product liability cases. The average settlement in these cases was $141,000.

The second area of government regulation is *information disclosure*, addressing problems raised by deceptive advertising and information asymmetry, as mentioned in the previous section. Business can lure consumers using false advertising, bait-and-switch tactics, and breaches of warranty claims. The FTC was created, in part, to halt such practices. The Truth in Lending Act of 1968, for example, specifies conditions for advertising credit plans. In addition to creating laws against deceptive advertising, the FTC seeks remedies against violators through measures such as cease-and-desist orders, temporary restraining orders, or civil action suits, depending on how public interest is best served.

Furthermore, industry-specific agencies also set standards for information disclosure for products within a particular industry. For example, the FDA requires that food and beverage labels show more complete information. In 2003, the FDA required that all food items list the amount of trans fat, a potential contributor to heart disease. Also, manufacturers of tobacco products and alcoholic beverages are required to display health-warning labels. Automobiles are required to display a breakdown of price, and potentially hazardous home appliances and toys are required to carry a warning label. Although consumers today in some areas are far from having access to perfect information, government intervention in information disclosure has, in general, enabled consumers to make more informed purchasing decisions.

The third area of government regulation is *consumer privacy protection*. Privacy is a constitutional right protected by the Fourteenth Amendment. The FTC plays the role of enforcing privacy laws in the marketplace. Privacy laws include the Privacy Act of 1974, the Gramm-Leach-Bliley Act of 1999, the Fair Credit Reporting Act of 1970, and the Children's Online Privacy Protection Act of 1998.

The Privacy Act of 1974 prevents personal information held by the federal government from unauthorized disclosure. The Gramm-Leach-Bliley Act of 1999 (also known as Financial Modernization Act of 1999) protects consumers' personal financial information from misuse by financial institutions. The Fair Credit Reporting Act of 1970 limits access of personal financial information collected by consumer reporting agencies. A recent amendment in 2003 to the Federal Fair Credit Reporting Act has provided consumers access to a free copy of a credit report from each of the nationwide consumer reporting companies once every 12 months. Finally, The Children's Online Privacy Protection Act of 1998 places limits on information collection of children under 13 years of age. Although laws exist that protects children's privacy, online consumer privacy is generally inadequately protected. Consumer information, such as age, name, demographics, e-mail address, and financial information, can easily be collected through computer cookies.

Other privacy regulations include the national "do-not-call" registry and the Can-Spam Act of 2003. The FTC's do-not-call registry, established in 2003, was designed to put a stop to the bombardment of unsolicited telemarketing calls to households. The Can-Spam Act of 2003 (Controlling the Assault of Non-Solicited Pornography and Marketing Act) addressed the issue of unsolicited bulk e-mails. The act specified certain accountability on commercial senders. For example, it requires that the header information and the subject line cannot be misleading and that the subject line must match the content of the message. The Can-Spam Act also prescribed opt-out methods for receivers. Violators of the provisions can be fined up to $11,000 per violation. The FTC and the Department of Justice are the federal agencies that enforce this law.

In sum, consumer protection regulation is generally grounded in issues related to hazard avoidance, information disclosure, and privacy protection. Consumer protection regulation is an ongoing process and evolves over time; it adapts to the economic, technological, political, and social forces.

—Jiyun Wu

See also Advertising Ethics; Bait-and-Switch Practices; Consumer Activism; Consumerism; Consumer Product Safety Commission; Consumer Rights; Consumer's Bill of Rights; Federal Trade Commission (FTC); Food and Drug Safety Legislation; Friedman, Milton; National Highway Traffic Safety Administration (NHTSA); U.S. Food and Drug Administration (FDA)

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Consumer Rights

The subject of consumer rights historically covers two related areas: issues related to the actual products and services that a company sells to consumers and corporate business practices that directly affect consumers. As part of the evolution of consumer rights and concerns, a third area, spawned in large part by the growth in information processing industries and integrated computing networks, has emerged. This area concerns the use of information *about* the consumer, including privacy and security of that information. While there is little legislation establishing actual rights of consumers, there is a large body of law dealing with a range of consumer issues, which taken together are often referred to as "consumer protection."

At its core, a discussion of consumer rights implies that the interactions between consumers and corporations will naturally tend to be to the advantage of the corporation (due not only to size but also due to political, economic, and social influence) and so legal and political means should be used to equalize any imbalance of power. (More bluntly, many laws passed to protect consumers assume that the consumer is either unable or incapable of protecting himself or herself, due to the complex nature of business or products, and must be protected in the most basic sense of the word.) The key assumption of most consumer rights initiatives is that, absent any restraining influences, corporations will make decisions that ignore the welfare of consumers and maximize the assumed advantages of the supplier. A secondary assumption is that the consumer will (1) usually have less information than a business and (2) will be more easily confused by business complexities and, therefore, must be protected from businesses that will take advantage of these informational or experiential asymmetries. (Note that the advent of the Internet has greatly reduced the information disparity between consumers and suppliers, as well as offering a significant increase in resources that consumers can use to defend their rights. Consumer rights advocates believe information is power and that information transparency is critical to producing informed consumers.)

Most of the societal and legislative initiatives over the years either prohibit what is considered to be anticonsumer behavior or provide tools to consumers by which they may force companies to address individual (or sometimes group) grievances related to products or business practices. Anticonsumer behavior has historically included clear-cut examples such as price-fixing and price-gouging, deceptive marketing and sales practices, production and distribution of dangerous products (including pharmaceuticals and medical devices), and failure to deliver promised products or services. Less obvious but no less critical to the consumer are more recent developments in the consumer-business relationship, such as information privacy (especially in health care matters), unsolicited sales and marketing, and refusal to provide services or nondiscriminatory prices to a particular class of consumer.

While there is a case to be made that the Hippocratic Oath (the traditional oath that physicians take that binds them to keep the best interests of the patient uppermost in their considerations) embodied the first consumer protection principles in history, arguably the first U.S. legislation intended to protect the consumer was the Sherman Antitrust Act, signed by President Benjamin Harrison in 1890. The act declared that "Every contract, combination in the form of trust or otherwise, or conspiracy, in restraint of trade or commerce among the several States, or with foreign nations, is declared to be illegal." Often assumed to restrict monopolies, the act was targeted not at the size or form of corporations or trusts but at "restraint of trade," which would ultimately lead to artificially high prices for the consumer. Free markets were deemed better for the consumer; anything that prevented free markets was, therefore, bad and should be outlawed.

Following the enactment of the Sherman Antitrust Act, just what was allowed and forbidden by the law remained open to interpretation, as the U.S. economy evolved and the size of corporations allowed greater market control by a few companies or individuals. Such questions were debated and refined over the ensuing 24 years, particularly during President Theodore Roosevelt's administration. Roosevelt believed the solution lay in a commission that would regulate business practices and established the Bureau of Corporations in 1903. In 1914, Woodrow Wilson signed the Federal Trade Commission and Clayton acts. These acts established the Federal Trade Commission (FTC) as an investigative and enforcement body, creating the first government agency with the power to protect consumers, and explicitly outlawed monopolies, respectively. Since 1914, Congress has continued to expand the reach and powers of the FTC, allowing the FTC to address consumer issues as diverse as defining deceptive or unfair practices, establishing rules for granting credit, and regulating telemarketing practices.

The modern era of consumer rights traces to March 15, 1962, when President John F. Kennedy sent a special message to Congress containing his statement of the four basic consumer rights that the government should work to protect and promote:

1. *The right to safety:* protection against hazardous goods
2. *The right to be informed:* the right to access information the consumer needs to make an informed choice and protection against fraud and deceit
3. *The right to choose:* access to a variety of products and fair prices and protection against business practices that reduce competition
4. *The right to be heard:* the guarantee that consumer concerns will be heard and fully considered by the government

Since Kennedy's message, these rights have been added to by various groups worldwide, most notably the United Nations, to include the following:

- *The right to consumer education:* early and lifelong education about the consumer marketplace and the laws supporting consumer rights

- *The right to consumer redress:* the right to be compensated for misrepresented or unacceptable goods and services and the responsibility to actively pursue such redress
- *The right to a healthy and sustainable environment:* the right to live and work in a safe and healthy environment that supports a life of dignity
- *The right to basic needs:* access to goods and services necessary for survival throughout societies
- *The right to access:* fair and equitable distribution of goods and services throughout society

Kennedy's main point was clear and has been echoed by many others: From an ethical perspective, consumers have certain rights that exist outside of government policy and law, and it is the government's job to ensure these rights are not infringed on in the marketplace. In the ensuing years, the federal government and state legislatures worked to implement laws and policies that institutionalized those rights.

Inherent in Kennedy's message is a more subtle requirement that the consumer, and the public as a whole, have a responsibility to *proactively* use consumer information, education, and rights to not only make informed decisions but also to actively work to be sure that government and industry act in the consumer's interest. The classic example of citizen responsibility in this regard is Ralph Nader and his group of young activists known as Nader's Raiders. Arguably the beginning of the modern consumer rights movement, Nader began in 1965 by taking on the auto industry over the alleged safety problems of GM's Corvair automobile. His activities soon expanded to include waste in government, including monitoring and exposing government agencies who were failing to effectively perform their duties to protect consumers.

While there are many laws at the federal and state levels aimed at protecting consumers by legislating against harmful business practices, a few are worthy of special note as examples of the philosophy of the government's role in protecting consumers. The Truth in Lending Act was originally enacted in 1968 and revised in 1980. It requires complete disclosure to consumers of all costs involved during the life of a credit transaction, including loans and leases, and demands explicit and clear statement of the conditions under which credit is granted. In addition, the law provides legal recourse for consumers against lenders who violate the terms of the act. The act was in response to predatory lending and leasing arrangements, deceptive credit marketing, and discriminatory practices in granting credit based on nonfinancial factors.

The Fair Credit Reporting Act (FCRA) passed in 1970 regulates the way that consumer credit information is collected, distributed, and reported. Prior to the passage of this law, major credit bureaus operated largely independently of oversight or even cursory review as regards to accuracy, privacy, security, use, and dissemination of consumer's credit information. Consumers for their part had no recourse against incorrect information provided by credit unions or the resulting burdens on their financial dealings. In the most egregious cases, consumers could be denied credit based on credit reports to which they had no access and were not even aware were the basis for the denial. In response to growing evidence of incorrect credit reporting, information and privacy abuses, and pressure from consumer advocates, Congress passed the FCRA to provide tools to consumers for dealing with credit reporting issues and to legislate how credit bureaus would conduct their businesses relative to consumers. The FCRA requires credit bureaus to provide consumers with the information in their files and to take all reasonable steps to be sure the information is complete and accurate. It also requires that credit bureaus undertake "reasonable investigations" of any information disputed by a consumer and inform the consumer of the disposition of that dispute.

In 2003, the FCRA was updated through the Fair and Accurate Credit Transaction Act (FACTA). As part of the FACTA, consumers are entitled to a free credit report every 12 months, from each of the three major credit reporting agencies (Equifax, Experian, and Transunion), available through an FTC Web site established for that purpose. In addition, consumers are entitled to notification when credit is denied based on negative information in a credit report and at that point are also entitled to a free credit report. FACTA also required the FTC create a "Summary of Rights for Consumers," which would be supplied with any credit report provided to a consumer, detailing the specific consumer rights and credit bureau responsibilities provided by FACTA.

Combined with the FCRA, the Fair Debt Collection Practices Act (FDCPA) provides the major portion of consumer credit rights. Passed in 1978, the FDCPA was in response to serious abuses by the debt collection industry that included home and workplace harassment by phone, misrepresentation, threats of arrest or legal action that are outside the scope of debt collection and therefore not credible, and reporting false information to credit bureaus. The FDCPA regulates the means by which third-party debt collectors may do business, details the rights of consumers when dealing with such agencies, and provides legal recourse for consumers against abusive or non-FDCPA-compliant debt collectors.

The Telephone Consumer Protection Act of 1991 was passed to limit the number of unsolicited phone calls consumers receive at their homes. Congress recognized that as well as being a nuisance to consumers, such calls were often the vehicle by which unscrupulous business operators and fraudsters preyed on the public. The act limits the entities that may call a consumer's house to those with which the consumer has an existing business relationship (although "existing" is loosely defined) and also prohibits calls from entities with an existing business relationship whom the consumer has specifically asked to cease calling. The act also required the FTC and the Federal Communications Commission to establish a National Do-Not-Call registry, containing the numbers of all consumers who do not wish to be subject to uninvited telephone solicitations. The registry requires consumers to proactively register phone numbers and is one of the laws that provides the tools for consumers to use to protect themselves.

The Health Insurance Portability and Accountability Act of 1996 (HIPAA) is intended to do for a consumer's health information what other laws have done for financial information.

HIPAA specifies a set of "patient rights" regarding access and dissemination of medical and health information and, in many ways, parallels the protections of financial data provided by the FCRA and the FACTA. As with the other laws, it also provides for consumer redress in cases where the law is violated.

HIPAA also signaled a fundamental shift in how personal data of all kinds, not just financial data, is to be considered by businesses. HIPAA established the rights of people to control access to information about themselves and placed the burden of information security and protecting confidentiality of personal information clearly on those who store and access it. Personal information is now a "thing," associated with a person, to be protected rather than information to be collected and used for the benefit of the business.

All these laws serve to protect consumers by leveling the playing field in complementary ways. It is clearly the intent of the government to force businesses to become more transparent in their dealings with consumers, as well as allowing consumers to dictate how they will interact with businesses. In addition, the government has chosen to specify what kinds of information must be given to the consumer, how it is to be presented, and how information about the consumer may or may not be disseminated. Perhaps most critically, these laws provide specific redress for the consumer when businesses violate the laws. Again, the assumption is that information is power, if put in the hands of the consumer, and short of being forced to act in a fair manner, businesses will withhold, misuse, or misrepresent information. The new assumption in these laws, though, is that given the proper tools, consumers can protect themselves, as well as other consumers, through penalties and processes specified by these laws.

While the aforementioned laws deal with protecting consumers from harmful business practices, there is also a "right" or expectation that businesses will not sell *products* that are harmful to consumers. Toward this end, Congress established the Consumer Product Safety Commission (CPSC) by passing the Consumer Product Safety Act of 1972. Again, Congress posited a fundamental inability of the consumer to understand the implications of using a product, finding that "complexities of consumer products and the diverse nature and abilities of consumers using them frequently result in an inability of users to anticipate risks and to safeguard themselves adequately." In the language of the act, the CPSC exists

1. to protect the public against unreasonable risks of injury associated with consumer products;
2. to assist consumers in evaluating the comparative safety of consumer products;
3. to develop uniform safety standards for consumer products and to minimize conflicting state and local regulations; and
4. to promote research and investigation into the causes and prevention of product-related deaths, illnesses, and injuries.

The other laws mentioned previously are somewhat passive in their protections, establishing guidelines for businesses and providing tools for consumers. The CPSC, however, was established as an active agency, charged with "protecting the public," "assisting consumers," and "investigating causes and prevention of injuries." When commerce and business practices are concerned, the consumer is given assistance in protecting his or her "rights." When injury and death are possible, the government is expected to not only assist but also to proactively work to protect the consumer.

—Tom Bugnitz

See also Advertising Ethics; Asymmetric Information; Bait-and-Switch Practices; Consumer Activism; Consumer Federation of America; Consumer Fraud; Consumer Product Safety Commission; Consumer Protection Legislation; Consumer's Bill of Rights; Deceptive Advertising; Deceptive Practices; Federal Trade Commission (FTC); Health Insurance Portability and Accountability Act; Lemon Laws; Privacy; Product Liability; Restraint of Trade; Tylenol Tampering; U.S. Food and Drug Administration (FDA)

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Consumer's Bill of Rights

The idea of a Consumer Bill of Rights grew out of the consumer movement that began in the 1960s as a protest movement of consumers and their advocates against what they saw as unfair, discriminatory, and arbitrary treatment by business organizations. This movement involved a number of activities that were designed to protect consumers from a wide range of practices that infringed on the rights that consumers were believed to possess in the marketplace. The time was ripe for a new consumer movement that was concerned with a range of issues that grew out of a highly affluent population, a technologically sophisticated marketplace, and a society that in general had high expectations and aspirations for the fulfillment of human needs.

This modern consumer movement had no particular focus as did previous movements of this kind, but was concerned about a variety of issues related to the marketplace including product safety, quality of products, reliability and product obsolescence, truth in advertising and packaging, uses of credit, completeness of information, product warranties, product liability, and other issues.

Eight Consumer Rights

Former President John F. Kennedy was the first president to enunciate four rights of consumers that he believed needed protection in the marketplace: the right to safety, the right to a choice, the right to know, and the right to be heard. These rights were supported by other presidents. To these four several other rights of later vintage were added by consumer advocates to make a complete consumer bill of rights.

- *The right to safety:* The consumer has a right to be protected from dangerous products that might cause injury of illness as well as from the thoughtless actions of other consumers.
- *The right to a choice:* The consumer has the right to be able to select products from a range of alternatives offered by competing firms.
- *The right to know:* The consumer must have access to readily available, relevant, and accurate information to use in making purchase decisions.
- *The right to be heard:* The consumer must be able to find someone who will respond to legitimate complaints about abuses taking place in the market and products that do not meet expectations.
- *The right to recourse and redress:* The consumer has a right to full compensation for injuries or damages suffered as a result of unsafe products or abuses in the marketplace.
- *The right to full value:* The consumer has a right to expect a product to perform as advertised and meet the expectations that were created so that the consumer is getting full value for the money spent.
- *The right to education:* Consumers must have access to educational programs that help them understand and use the information available in the marketplace to make rational purchase decisions.
- *The right to representation and participation:* Consumer interests must be represented on policy-making bodies that deal with issues related to the marketplace.

These rights were believed to need government legislation and regulation to be protected adequately as the marketplace itself did not provide enough incentives for business to respect these rights in all their actions related to consumers. Congress responded with a host of legislation in the 1960s and 1970s that was directed at one or more of these rights of consumers. New regulatory agencies such as the Consumer Products Commission were created and new powers given to existing agencies such as the Food and Drug Administration and the Federal Trade Commission. These rights have been of continuing concern in government as new issues related to secondhand smoke and safety issues about drugs and other products surfaced.

Expanding the Idea of Consumer Rights

The idea of a consumer bill of rights caught on in other areas over the years as many organizations formulated such a set of rights in relation to specific areas of concern. For example, in 1997, then President Bill Clinton appointed an Advisory Commission on Consumer Protection and Quality in the Health Care Industry that as part of its work drafted a consumer bill of rights to protect consumers and workers in the health care system. This bill of rights covered eight areas of consumer rights and responsibilities including information disclosure, choice of providers and plans, access to emergency services, participation in treatment decisions, respect and nondiscrimination, confidentiality of health information, complaints and appeals, and consumer responsibilities.

In 1999, the Federal Communication Commission launched a campaign for a Cable Consumer Bill of Rights to let consumers know that even though the agency's direct role in regulating cable rates was ending consumers still had a number of rights regarding their cable service. This campaign was designed to educate consumers about their options after direct regulation ended. The proposal covered what consumers should expect from their cable company, local government, and the Federal Communications Commission itself, along with additional expectations. This Bill of Rights was expected to help consumers protect their rights in a deregulated environment.

An organization called Digital Consumer proposed a Consumer Technology Bill of Rights to what they believed was an erosion of the rights of consumers to use digital content that was becoming more and more available. The California Department of Consumer Affairs proposed a Bill of Rights for consumers of certain types of telephone services within the state. Finally, in January 2000, Fannie Mae announced a "Mortgage Consumer Bill of Rights" to help advance consumer protections for more home buyers in America. This bill of rights was touted as the cornerstone of the agency's American Dream Commitment, which was meant to increase homeownership rates by lowering costs, removing barriers to homeownership, and serving families that are overcharged, underserved, and overlooked by mainstream housing finance. Thus, the idea of a consumer bill of rights thus seems to be alive and well in American society.

—Rogene A. Buchholz

See also Advertising Ethics; Antitrust Laws; Consumer Activism; Consumerism; Consumer Protection Legislation; Patients' Bill of Rights; Regulation and Regulatory Agencies; Rights, Theories of

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Consumer Sovereignty

Consumer sovereignty is an economic concept with roots in classical economics that argues that consumers are the primary force for determining the scale and scope for the production of goods and the provision of services in the economy, through their power to choose whether or not to consume goods and services.

Theoretical Background

Consumer sovereignty is a classical economic concept that appears at least as early as Adam Smith's *An Inquiry Into the Nature and Causes of the Wealth of Nations.* It imputes to consumers the primary, if not sole, discretion for assessing the marginal costs and benefits of their prospective consumption of goods and services. This decision-making role determines the scale and scope of the production and provision of these goods and services, respectively. The concept continues in the neoclassical economic tradition, with both descriptive and prescriptive dimensions. In its descriptive dimension, consumer sovereignty refers to the capacity for consumers to discern and to maximize their own preferences without interference and to drive the resulting production and provision of goods and services in the economy. It joins with the following propositions to form a theoretical matrix in support of the free market:

- Producers are profit maximizers.
- There are no barriers to entry and exit from the market.
- There is perfect information, that is, true information about market conditions is available without limitation to direct and indirect market participants.
- Economic agents act atomistically, that is, as individuals and not in coordination with one another.

In its prescriptive dimension, the concept of consumer sovereignty is the economic analog to the political principle of noninterference, which John Stuart Mill defends in *On Liberty.* Because in the eyes of some supporters of the free market the concept of consumer sovereignty descriptively is foundational for the logic and operational viability of markets, it has been an accessible and attractive concept for prescriptive arguments in favor of market allocations that involve consumers and consumer choice.

Criticisms of the Concept of Consumer Sovereignty

However, the concept has faced challenges in the recent evolution of economic theory and policy, even from successors to the classical and neoclassical traditions out of which it arose. One criticism is that the conflation of the political concept of sovereignty into an economic concept is logically defective, in that it supports the problematic position that consumers can or should impose preferences in a market that ostensibly is free of coercion. The concept of consumer sovereignty as a principle for socioeconomic policy lacks a satisfactory account of why other market actors—or other stakeholders in general—would or should be less sovereign than consumers.

A second criticism has to do with the ethical vindication of the concept in its ostensible prescriptive dimension, that is, whether it is capable of sustaining a valid moral claim—or policy argument—on its own. To the extent that one invokes the concept of consumer sovereignty normatively, that is, to justify an ethical claim, it functions as a minor premise that furnishes factual or technical content. For consumer sovereignty to be normatively intelligible and viable as a principle for action requires that one underwrite it with a substantive and distinct *moral* principle as a major premise, for example, the principle of utility or an articulable account of a moral right. Otherwise, the argument dissipates into a purely descriptive (economic) construct and falls short of an authentic ethical justification.

The economic concept of consumer sovereignty bears a superficial similarity to the normative concept of moral autonomy, though it remains logically distinct from it. Without an independent ethical justification for consumer sovereignty, the normative claims for the concept would rest merely on appeals to the *preferences* of consumers themselves and, by extension, of producers and providers of goods and services. This would leave open the question of whether these preferences otherwise would be consistent with *moral* principles that most members of society share, including justice, rights, respect for persons, and autonomy itself. The absence of such normative grounding would call into question the justifiability and intelligibility of ethical guidelines and policies that ostensibly safeguard consumer interests, for example, product safety, truth in advertising, and product warranty and support.

A third criticism of the concept of consumer sovereignty emerges when one considers the effects of market failure or preemption. For example, consumers simply may not have accurate or sufficient information to form their preferences, or they might be liable to form different preferences with additional information. These failures may be due to breakdowns in communication of information through market processes ("signaling problems"). Such market dysfunctions may reflect (1) limitations in the ability of consumers to perceive, absorb, and analyze information ("bounded rationality"); (2) constraints on consumers' responses to changing market conditions due to their relatively fixed investments in skills, relationships, and infrastructure ("asset specificity"); and/or (3) deceptive, manipulative behavior by other market participants ("opportunism").

Even when consumers possess sufficient information to form preferences, and face few proximate barriers to acting on them, public policies may preempt their capacity to express these preferences in their consumption behavior. Such preemptive conditions are characteristic of a merit good, a concept that Richard A. Musgrave elaborated in 1957, and that inherently involves *interference* with the choice of consumers and, in a derivative sense, producers. A merit good is one for which society determines the levels of production and consumption as a matter of public policy rather than through market allocations. An example of a merit good is education, which many jurisdictions require every capable person to consume through a certain age. Examples of "demerit" goods include highly addictive nonmedicinal drugs and child pornography, which are forbidden, regardless of the willingness of consumers and producers to trade in them. In these examples, the determination of levels of production and consumption does not rest with economic agents *qua* economic agents (including prospective consumers).

Although there is no consensus regarding the wisdom of constraining consumer choice through such policies, these limits are abiding features of all economically advanced societies. To the extent that such interference with consumer choice rests on moral appeals, there arises a salient challenge to the normative claims of the concept of consumer sovereignty and to the sovereignty of economic agents in general. Moreover, modern mainstream economic theories and policies recognize the relevant influences of multiple factors in addition to consumer demand when it comes to the scale and scope for economic performance, for example, productive capacity; markets for labor, capital, commodities, and organizational leadership; the regulatory environment; and the infrastructural apparatus, including telecommunications, roads, education, venues for dispute resolution, and an enduring ethical climate conducive to trust and transparency.

—Lester A. Myers

See also Austrian School of Economics; Chicago School of Economics; Consumer Preferences; Economic Efficiency; Economic Growth; Economic Incentives; Economic Rationality; Economics and Ethics; Efficient Markets, Theory of; Fact-Value Distinction; Is-Ought Problem; Political Economy; Political Theory; Regulation and Regulatory Agencies; Signaling; Smith, Adam; Utility, Principle of

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Consumption Taxes

Consumption tax is also known as an expenditures tax, a consumed-income tax, or a cash flow tax. It is a tax on the monies spent as opposed to the income tax, which is a tax on the amount of money earned. Consumption tax applies only to income spent and can be broadly explained as an income tax with unlimited deductions for savings and taxes on savings withdrawn and spent. If there is no savings or capital income, a consumption tax is equal to an income tax, assuming equivalent tax rates. Although it can be applied to firms, the consumption tax is usually discussed in terms of taxation of individuals.

Current, but not pure, examples are the European value-added tax (VAT) and the Australian goods and services tax (GST). Certain goods and services are exempt from the VAT and GST. The United States is the only Organisation for Economic Co-operation and Development (OECD) country that does not have a VAT on consumer expenditures, although sales taxes in some state and local communities in the United States are akin to a consumption tax.

The rate of taxation can be flat (i.e., equal for everyone) or progressive, with higher rates for more affluent taxpayers in an effort to achieve "distributive justice." It even can be modified to have different rates for different products to achieve social objectives, somewhat akin to the "sin tax" on alcohol and tobacco or the "gas guzzler" tax on some large cars in the United States. Arguments for and against the use of consumption taxes appeal to economic, social, environmental, and political objectives in terms of what consumer behavior is encouraged or discouraged, the differential impact based on wealth and spending/saving patterns, and the potential impact on international trade.

Arguments for a Consumption Tax

Supporters argue that the consumption tax encourages savings as it discourages spending and consumerism. With decreased spending and consumerism, there would be less waste of resources, less material produced, and an overall improvement in the natural environment as fewer demands are placed on it. In this way, the consumption tax would promote efficient use of resources and protects the environment. However, for the same reason it is also seen as a hindrance to the growth of the consumption or consumer-based economy. Business interests are placed at the opposite end of environmental protection. Proponents of the consumption tax also argue that an income tax encourages spending and consumption while penalizing savings, investments, and innovation, thereby damaging the economy in the long term. Finally, proponents of the consumption tax argue that the income tax taxes what people contribute to society in terms of work, while a consumption tax taxes what people take from or what resources people use in a society. Therefore, a consumption tax is just in that it distributes or places the burden (tax) on those that benefit (use the resources).

Arguments Against a Consumption Tax

Opponents argue that a consumption tax would require a higher tax rate to raise the same amount of revenue and so there may be an adverse impact on the balance of work and leisure. Opponents also argue that a nominally flat consumption tax can be regressive, shifting the greater burden on the working class, because returns to savings and investments would not be taxed, which constitutes a greater percentage of wealthier people's incomes. Another objection to the consumption tax used to be that it is difficult to monitor how much people save. However, in practical terms, a consumption tax would essentially be the equivalent to unlimited access to tax-deferred individual retirement accounts, with no penalty for early withdrawal except for payment of taxes on the withdrawn savings.

While consumption in the environmental community usually refers to the use of resources (such as the global commons of air and water or scarce natural resources such as fossil fuels, virgin forest, and biodiversity), consumption in the case of consumption taxes refers to goods and services used, regardless of their impact on natural resources. Because there is no distinction between resources used and what is taxed, there is no clear environmental benefit of the consumption tax. However, a consumption tax can also be used differentially as a means of influencing consumer behavior. Variations of a consumption tax include taxation of goods made from scarce natural resources or energy-intensive items. One example is a proposed "carbon" tax in Japan on energy resources, with the tax rate proportional to the amount of carbon released on utilization.

Globalization and changes in international trade continue to challenge governments to adapt tax systems that are perceived as both socially fair and economically efficient. This requires balancing demands for distributive justice with the need to minimize the cost of compliance for business, and distortion of market forces in a competitive environment, so as to provide a level playing field for business operations.

—Virginia W. Gerde

See also Economics, Behavioral; Flat Tax; Justice, Distributive; Tax Ethics; Value-Added Tax (VAT)

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Contingent Valuation

Contingent valuation is a survey-based method of determining the economic value of a nonmarket resource. It is used to estimate the value of resources and goods not typically traded in the economic markets. It is most commonly related to natural and environmental resources.

Contingent valuation is employed to assess environmental resources, goods, and services. Government agencies apply the technique to estimate use and nonuse values of environmental resources that it oversees and manages, and to make decisions regarding environmental policy and lawsuits, and to assess damages. For example, the government employed this methodology to estimate the environmental damage of the *Exxon Valdez* oil spill in 1989. Businesses use this technique to estimate cost-benefit values on environmental projects.

Contingent Valuation Survey Methods

Contingent valuation surveys are administered using a variety of methods to select respondents and to develop survey questionnaires. Respondent selection is at the discretion of the survey administrator. Respondents are always individuals and the survey samplings may range in size. In addition, they may be chosen randomly or selected using other approaches such as geographic specifications or database segmentation.

Survey questions are based on hypothetical scenarios. Respondents are asked to estimate what they would be willing to pay to sustain, improve, maintain, prevent loss, or repair natural and environmental resources. For example, the government may want to ascertain the cost-benefit value of a future project of the Bureau of Reclamation to repair water storage facilities. It may use contingent valuation to answer the question, "What would be the environmental cost of this project if it affected the water supply of nearby cities and farms and also disrupted the ecosystem of an endangered species?" Survey recipients may be asked to comment on their willingness to pay $10, $20, or $30 more in utilities per year to improve water storage and pay environmental conservation costs.

Views on Contingent Valuation

Contingent valuation is a disputed method of estimating natural and environmental impact. Opponents argue that the technique is not empirical enough to accurately estimate financial data and to encompass the complexities of natural resources management. Unlike other methods of economical valuation, survey responses are not based on an individual's behavioral choice, nor are they based on a person's actual conduct. Therefore, survey responses are subjective and uninformed, creating a high likelihood of "hypothetical bias." There have been many attempts to improve survey controls, but opponents argue that these improvements are not sufficient to minimize the inaccuracies. Contingent valuation is also criticized for being expensive and time-consuming.

Proponents of the methodology claim that it is the most flexible option and is, therefore, suitable to environmental concerns. The technique also accounts for costs that more traditional methods do not, and it adds a critical consumer perspective. Proponents also state that the technique is reliable, as it has been refined and improved over a long period of time—it was first proposed as a theory in 1947.

Conclusion

As global environmental issues gain increased attention and concern, there is and will be more focus on the accuracy of estimating nonmarket values for natural and environmental resources. Environmental issues are extraordinarily complex and require sophisticated methods of analysis. Contingent valuation is the most widely used method for estimating nonmarket values, yet it is unclear as to whether it is an appropriate and reliable method. Contingent valuation methods present an ethical challenge to those who use them to make significant decisions about the future of the environment.

—Pamela C. Jones

See also Bureau of Reclamation; Environmental Assessment; Environmental Ethics; *Exxon Valdez*; Natural Resources; Pricing, Ethical Issues in

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Contracts

A contract is one of the basic social and legal institutions in modern society. A contract frames and coordinates human interactions. It is an agreement that creates, assigns, delegates, and transfers rights and obligations, tangible and intangible goods, services, and entitlements between the contracting parties, relying on their voluntary, rational, and deliberate consent. Today, contractual relationships among persons, communities, organizations, and states emerge as an alternative or at least as an amendatory legal instrument of market coordination and state regulation. A contract binds person to person, person to organization, organization to organization, person to society, person to state, and state to state in private, social, economic, and political affairs.

Since contracts embrace almost all aspects of human affairs from business to marriage, it is difficult to develop a general theory of contract that could provide a normative framework for all human interactions based on various macro- and micro-level, formal and informal, and written and unwritten agreements. Since the theoretical diversities of the notion of contract are rooted in different legal and philosophical traditions, they offer different accounts of its philosophical origin, moral motivations, and practical justification for its prevalence in modern society. Conflicting assessments cause theoretical, doctrinal, and practical tensions and incoherencies in contract law, adjudication, and contractual settlement. Therefore, despite the long and rich intellectual history of philosophical, moral, legal, economic, and political reflections on contract, many contemporary scholars hold that contracts still lack any clear and consistent theoretical foundation. The critical remarks about differing assumptions and interpretations apply equally in civil law countries, where contracts are often justified on moral grounds and given a certain kind of redemptive power in the implementation of a just and well-ordered society, and in common-law countries, where the economic analysis of contracts seems to be too narrow in its philosophical and moral foundation.

This entry presents an overview of the basic theoretical concepts of contract from contractarian rights-based to consequentialist perspectives (explained hereafter). Instead of making a futile attempt to outline a general theory of contract, this entry will focus instead on how competing approaches and theories endeavor to conceive and explain the basic philosophical ideas underlying contract.

Rights-Based Contract Theory

Contemporary social contract theorists emphasize that the myriads of contracts performed by individual and institutional contractors should be considered as the everyday manifestations of a social contract that binds people together in a politically constituted society on the basis of a fair and impartial distribution of rights and obligations. This social contract has priority over common contracts in which individual rights and obligations are specified in various forms of private agreements, trade and exchange of tangible and intangible goods, services, and entitlements among members of society.

Because classical social contract theorists derived the social contract from a prepolitical state of nature and presocial forms of human behavior, opponents of a contractarian view traditionally have questioned using a social contract of specious origins as the philosophical justification for the basic institutions of a fair society. Some contemporary contractarians draw the normative principles of social interactions from a hypothetical social contract that avoids the question of historical origins and presocial forms of human behavior. Other contemporary contractarians think that binding contracts cannot be traced to a hypothetical social contract and individual rights originating from philosophical ideas; they believe that a social contract originates in a rational agreement by members of society. In other words, the normative principles of interpersonal relationships conceptually emerge from the practical procedures of political dialogues that assign individual rights and obligations to promote individual cooperative interactions and set legal and moral constraints on the pursuit of personal interests. Rights-based contract theorists emphasize that the most important principles of the formation of contractual arrangements among individual and institutional contractors are freedom and equity, moral autonomy, fairness, individual well-being, and social utility. They believe that rights should entail these moral and legal constraints on the pursuit of each individual's economic and social interests to motivate and frame all the contractual relationships among members of society. These normative principles are implicitly present in our public morality, legal and political culture providing the legal justification for contract formation, contract law, and adjudication. Should contracts and contract law fail to meet these principles, their justification could be suspect from moral and legal points of view. The rights-based contract theorists generally emphasize that among the principles of contract and contract law, freedom and autonomy have priorities over other concerns, especially efficiency, utility, or general welfare maximization. This contractarian view represents a rights-based theoretical approach to contract and contract law and regards contracts as creating and transferring rights and entitlements in correlation to self-imposed and legally enforceable obligations. The second-order rights arising from the particular contractual relationships are corollaries of individual inherent rights of freedom and autonomy. Preexisting individual rights justify the legal protection of a party's legitimate expectations and the enforcement of obligations in case of legal dispute, breach, or infringement of contract. The sole basis for adjudication and legal enforcement of a contract is the preexisting and correlative rights and obligations of the parties at the time of contract formation. Therefore, rights-based contract theorists consider that in the case of a contractual dispute a court is required to discover the rights of the contracting parties exchanged at the time of contract formation and to resolve ambiguities through the interpretation of their intentions. Since there is a right answer for all contractual disputes, a court must invent new rules of prospective reason to fill gaps in contracts to point to future efficient behavior or to grant disputed rights and entitlements in the interest of efficient outcome of contracts. The retrospective and prospective views of adjudication are the main sources of conceptual and methodological disagreement between rights-based contract theorists and law and economics scholars. While rights-based contract theorists think that a court has to take the retrospective view of adjudication in every contract case, law and economics scholars emphasize the prospective view of adjudication, especially, if a contractual gap exists. Of course, rights-based contract theorists do not refute the importance of the efficiency criterion in contractual arrangements and contract law, but they think that the enforcement of the obligations of the parties should be based not on welfare maximization but on their rights, the respect of their freedom, and individual autonomy. They think that the voluntary, rational, and deliberate consent of free and autonomous parties in contractual arrangements logically advances social welfare and produces the best economic outcomes. They believe that if a court prospectively defines the welfare-enhancing preferences for the parties to settle contractual disputes and to steer them toward efficient outcome, judicial paternalism is likely to occur.

Economic Analysis of Contract

In the late 20th century, the economic analysis of contracts has gained ascendancy in American academic and judicial discourse. Its impact as a normative theory of contract law, adjudication, and contractual settlement on the European legal systems is quite moderate because the role of the European judges is primarily limited to the interpretation and enforcement of contract in the context of the civil and business code provisions enacted by the legislature. In continental Europe, the judges are bound to apply and enforce the law and have less room to exercise judicial discretion by referring to external economic criteria, uncodified commercial norms, or private orderings. The success of economic analysis of contract in the United States attests not only to the country's common-law tradition but also to the pervasiveness of legal pragmatism in jurisprudence.

In a perfect world, where transaction costs are zero; unforeseen contingencies never happen; opportunistic behavior, asymmetric information, and bargaining power disparities are unknown phenomena;

and the parties voluntarily and deliberately perform their contractual obligations for the benefit of mutual welfare, legal intervention may be unnecessary. Nevertheless, in our less perfect world all these phenomena and anomalies quite frequently occur when the parties enter into contracts. Economic analysis attempts to provide an alternative theoretical approach to contracts. Law and economics scholars apply economic concepts and theories to the analysis of contracts to settle contractual disputes resulting from incompleteness, nonperformance, impossibility to comply, contract breach, and other damages. Besides offering practical guidance about the economic analysis of contracts in contract formation, contractual settlements, and adjudication, economic analysis also endeavors to provide a solid normative foundation for contract law. The system of contract law—the set of optional and mandatory rules—is tested in accordance with external economic criteria as well. As indicated frequently, the use of external economic criteria in legal arguments and adjudication contradicts the concept of justice and makes the legal system inconsistent and nontransparent, especially when infringements of rights, legal entitlements, and deliberate breaches of contract are at issue. The use of economic criteria in adjudication is external to law. If a judicial decision is based not on the examination and upholding of preexisting contractual rights and obligations but on the measurement of the prospective welfare effects of the enforcement of contract, adjudication becomes uncertain. Law and economics scholars contest this objection, alleging that economic analysis of law does not intend to change the principles of the legal system but rather to explain legal rules and to shed light on efficient outcomes.

Since law and economics scholars assume that rights-based theories of contract cannot give a reasonable explanation of why promises and contract terms are binding, they seek to justify contract and contract law by reference to economic outcomes. In analyzing contract disputes, law and economics scholars, in contrast to rights-based contract theorists, tend to emphasize consequences rather than intentions. The economic elements of this legal doctrine mainly come from mainstream economic theories and concepts such as cost-benefit analysis, the Pareto and Kaldor-Hicks concepts on efficiency, the Coase theorem, the theory of transaction costs, the problem of market externalities, rational choice theory, and so forth. In theorizing about contracts in accordance with these economic theories and concepts, law and economics scholars place particular emphasis on efficiency and welfare maximization. The concept of human rationality in law and economics also recalls the great narrative of the liberal tradition on *Homo economicus,* which considers human beings as free, rational, and self-interested agents whose main goal is welfare maximization defined in terms of individual preference satisfaction. Law and economics scholars presume that the application of these simple normative economic criteria liberates us from endless moral debates on the keeping or breaching of contracts and about most of the hard philosophical questions related to freedom and equity, fairness, and justice in cases of contractual arrangements. Thus, law and economics can be characterized as representing an instrumentalist view in jurisprudence, namely, that contracts and contract law should create incentives for the contracting parties to maximize individual and/or social welfare measured in terms of individual preference satisfaction. Law and economics definitely takes a consequentialist stand on the economic analysis of contract and the definition of legal rules even if it also appeals for moral theory to provide philosophical justification and a constitutional foundation for the freedom of contract. Law and economics is firmly rooted in the utilitarian tradition of moral philosophy despite superficial reconciliation of the deontological moral claim of freedom and autonomy and the prospective view of efficiency of contract. It follows that efficiency and welfare maximization criteria may override some original claims and rights that the parties initially brought to the bargaining table. These two rival moral theories of justification of contract can hardly be brought together unless we give priority to some basic rights—such as freedom, autonomy, equity, fairness, justice, and so on—over efficiency and welfare maximization. Law and economics scholars seem to eschew the acceptance of such reconciliation. A quite recent opposing argument in law and economics literature is that because fairness diminishes welfare, the pursuit of fairness makes individuals worse off. From the consequentialist point of view, the trade-off between the efficiency and moral autonomy considerations of contracts is fully justified by the efficiency advantages if they outweigh the consequences of the insistence of the parties on their original claims, rights, and entitlements. Consequentialists do not rule out the possibility that welfare maximization may result in the denial of some rights, while deontologists do not allow any concession about individual rights and legal entitlements on behalf of efficiency advantages. To sum up, law and economics represents an efficiency-based approach to contract and contract law and draws on utilitarian moral philosophy.

For law and economics scholars, the Pareto principle of efficiency serves as a normative criterion for the moral justification of contracts. Nevertheless, when contracts equally increase the welfare of symmetrically situated and empowered, informed and rational parties in comparison to their original positions, the argument is weak, merely reflecting the commonsense wisdom that contracts based on voluntary, informed, and deliberate consent are likely to improve the overall welfare of all involved parties. In such a case, contract law facilitates contracting and creates additional incentives for the parties to complete their contractual obligations efficiently. If contracts improve at least one party's welfare and do not make any other parties worse off in comparison to their original positions, the transaction is Pareto superior. Though this strong version of the Pareto principle provides a more adequate tool for the prospective analysis of the efficiency of voluntary exchange, it is thought to be too strong to be applied to real-world situations where the outcomes of contracts and the costs and benefits of the parties are rarely distributed according to the Pareto superior state. In spite of the transparent intentions and benevolence of the contracting parties at the time of contract formation, transactions sometimes have losers and gainers. But the Pareto criterion of efficiency does not allow trade-offs between one party's gains and another party's losses; it permits aggregation only in a narrow sense. As it is also frequently stressed, further problems of Pareto efficiency arise from the fact that contracts between two parties usually entail externalities for a third party, which are either marginalized or not noted at all. Third-party externalities are frequently considered as trifles, nonmeasurable, or insignificant so that the legal protection of third-party interests leads to marginal social utility. Nevertheless, third-party externalities sometimes provide a rationale for the judicial overriding of contracts. Since the Pareto principle of efficiency focuses on the model of a two-party sitatuation—one party and the rest of the world—it is difficult to apply the principle to sophisticated and typical multiparty problems such as the preservation of natural environment, the interests of future generations, and the assignment of property rights in case of public domain and intangible commons. Without calculating the impact of a contract imposed on the welfare of a third party, it is hard to judge whether that contract brings about a Pareto inferior, optimal, or superior state of the contracting parties and other constituencies. As critics contend, the Pareto criterion of efficiency is indeterminate in serving as a solid foundation for measuring efficiency and welfare due to its limited focus, competing conceptions of individual preferences and welfare, the problems of externalities, imperfect information, and limited rationality. In the last resort, the prospective view of efficiency of contracts weakens its very foundation, namely, the expressed intentions of the parties laid down in legally binding contractual terms that constituted a contract at the time of contract formation.

Most law and economics scholars prefer to use the Kaldor-Hicks principle of efficiency—sometimes called "potential Pareto improvements"—which is less controversial and more realistic at least from the point of view of welfare economics. According to this principle, contracts meet the Kaldor-Hicks efficiency principle if the aggregate gain exceeds the aggregate loss including externalities. The Kaldor-Hicks principle does not require the gainers either to compensate the losers or to internalize the externalities of the third-party losers. However, law and economics attributes intrinsic moral significance to individual welfare maximization and uses individual preference satisfaction as the metric of welfare. Therefore, sometimes it is hard to accept the economic outcomes of the Kaldor-Hicks principle of efficiency, which is indifferent to some individuals' actual welfare losses. The so-called efficient breach theory of contract and the prospective view of breach in adjudication are cases in point. Law and economics scholars do not regard contracts and contract law as appropriate legal institutions to bring about the redistributive aims in society. Any kind of compensation to mitigate the distributional inequalities caused by the economic outcomes of contracts would evidently contradict the Kaldor-Hicks efficiency norm. As its advocates allege, if contract and contract law require redistributive rules and terms, the better-off parties will never be interested in entering into contractual relationships. At least, the better-off parties will attempt to contract out of the rules, which they assume to be inefficient. Law and economics theorists neglect other welfare theories that—beyond efficiency norms—take rights-based compensation, distributional inequalities, or distributive justice into account because it regards them to be creating disincentives for contracting and efficient behavior.

—László Fekete

See also Consent; Consequentialist Ethical Systems; Cost-Benefit Analysis; Economic Efficiency; Ethics, Theories of; Fairness; Freedom of Contract; Natural Law Ethical Theory; Normative Ethics; Pareto Efficiency; Promises; Rationality; Rawls's Theory of Justice; Rights, Theories of; Social Contract Theory; Utilitarianism

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Copyrights

A copyright is a set of exclusive, time-limited rights granted by a government to regulate the use of a particular form, way, or manner in which an idea or information is expressed. Copyright may be claimed for a wide range of creative or artistic works. These include literary works; motion pictures; music, audio, and video recordings; paintings; photographs; software; and industrial designs.

Copyrights are a type of intellectual property. Copyright law only addresses the rendering, manner, or form in which creative thought, ideas, or other information has been depicted, implemented, or manifested. These laws are not designed or intended to cover the actual facts or concepts included in the work, nor the styles or techniques that are used or represented by the copyrighted work.

The term *exclusive right* means that the copyright holder is the only party that may exercise the attendant rights and privileges of registration. Anyone else who wishes to use the copyrighted work must gain the consent of the copyright holder. This consent may be tacit or explicit, depending on the relevant legal interpretation, the medium, and the terms of the copyright.

Copyright is often called a "negative right," as it serves to restrict the users or viewers of a work from taking certain actions rather than permitting creators or owners to take specific actions beyond the registration, performance, and distribution of a creative work.

The Value of Copyright

The doctrine of copyright protects the reputation of the creator or rights holder in several ways. *Reputation* is a key attribute of any creative endeavor, as it can directly influence the financial value of a work. Copyright may be used to protect a work even when the author wishes to remain anonymous or uses a pen name.

Copyright also strengthens the *archiving* and *integrity* of content, so that the owner and the works have legal protections against unintended changes, uses, or alterations of a copyrighted work. Publishers provide *surety* through the persistence, preservation, and distribution of creative works.

Copyright is also of great utility in the growing use of the Internet and computer technology to deliver personalized selections of media to users. This is a powerful example of how a networked economy can use existing social practices and laws to develop robust new business models. Applications such as Web portals, blogging, RSS feeds, and digital media distribution rely on the power of copyright to support the reputation, financial value, archiving, integrity, and surety.

Relevant Legislation

The U.S. Constitution does not specifically mention copyright. However, Article 1, Section 8 specifically gives the U.S. Congress the authority "[t]o promote the Progress of Science and useful Arts, by securing for limited Times to Authors and Inventors the exclusive Right to their respective Writings and Discoveries."

Congress has passed and amended various laws pertaining to copyright. With each change, the duration of copyright was increased and additional rights were awarded to copyright owners. The United States became a signatory to the Berne Convention for the Protection of Literary and Artistic Works in 1988. This international agreement was first promulgated in 1886 and allows national copyrights to be claimed and enforced among all member nations. The convention also specifies the minimum term of copyright protection, which is 50 years after the creator's death, except for photographs (25 years minimum) and cinematographic works (50 years after the first showing or the creation of the work). The convention does not extend the term beyond that provided by the country of record for a specific copyright claim, even when other nations provide longer terms of protection.

Even so, the United States does not recognize certain moral rights of creators. For example, a creator who does not wish to attach his name to a work may use a pseudonym, but she will abandon her moral rights to the work in the process. If the work is unfinished, and copyrighted without the creator's true name, it is assumed that the copyright owner has the right to complete the work.

U.S. courts have been reluctant to enforce this level of moral rights, even though Section 6bis of the Berne Convention gives authors the right to claim ownership of their works and publicly object to the distortion, mutilation, or any other derogatory action taken on the work that might be detrimental to the author's reputation. In the case *Gilliam v. ABC*, Terry Gilliam successfully sued a U.S. television network that had edited episodes of a British television show, *Monty Python's Flying Circus*, for standards and content prior to their transmission on late-night U.S. television. Gilliam is a member of the *Python* troupe, which wrote and performed its own works. The group had never been asked nor had granted permission to the network to modify the content.

Technological Issues

In 1998, the Congress amended the existing copyright laws by enacting the Digital Millennium Copyright Act (DMCA). The legislation was, in part, required by the United States' ongoing participation in the World Intellectual Property Organization (WIPO). The DMCA enacts elements of two different treaties that the United States signed in 1996: the WIPO Copyright Treaty and the WIPO Performances and Phonograms Treaty.

During the negotiations that led to the 1996 WIPO treaties, Bruce Lehman, the U.S. patent commissioner, advocated the principle that "any licensable act should be licensed." As old and new content is distributed in digital formats, digital rights management (DRM) should support the power of publishers to license content to users. Opponents noted that a market-based approach, in which the government refrained from banning technologies, might be prudent during the development of digital copyright law. By allowing the development of technology and societal norms, it would be possible for markets, including publishers and consumers, to adapt.

Professional organizations have objected to the DMCA on the grounds that the act is too broad. The DMCA includes anticircumvention provisions that prohibit the users of a technology to defeat or work around the rights management tools included in that technology. This restriction prevents security specialists and forensic scientists from reverse engineering the security measures contained in DRM implementations and from reporting the results of their efforts. The DMCA, in effect, prevents skilled professionals from performing the kinds of research necessary to test and improve DRM policies. The responsible improvement and progress of knowledge are key parts of the scientific method. Thus, the Association for Computing Machinery (ACM), the Institute for Electrical and Electronics Engineers (IEEE), and other groups have suggested that the anticircumvention restrictions be reinterpreted so that they apply only to cases involving copyright infringement.

Alternatives

Alternatives to copyright law have been proposed throughout the history of copyright law. The copyleft and Creative Commons movements are both responses to current implementations of digital copyright law. These doctrines use existing national and international copyright law to present a variety of licensing schemes that allow users to modify and distribute a creative work, but only in a manner that the original creator permits. The original creator can also allow commercial and noncommercial derivations of their work and choose to retain their payment or credit rights for any user-modified works.

The Creative Commons framework, developed by Lawrence Lessig and others, extends copyleft by allowing creators to tag or electronically mark their works with a standard, machine-readable license agreement that is freely available on the World Wide Web in several file formats. This system allows creators to claim ownership for their works in an efficient manner that acknowledges the rapid nature of electronic publishing and distribution. Creative Commons licenses are based on U.S. interpretations of international copyright law. However, the distributed nature of the movement has allowed professionals to harmonize the license so that it may be applicable and useful in their own countries.

The Creative Commons system also supports the assignment of works to the public domain and to open source licenses. An open source license allows other users to view and modify the text, images, underlying source code, or programming instructions of a creative work as long as their modifications are also released to the public. Various forms of open source licensing have been used to develop computer operating systems such as GNU/Linux that may be distributed free of charge. It is possible to commercially distribute open source works but the modifications must be made available to the public, usually through the World Wide Web or another electronic medium.

Customers and Copyright Holders

Over the last decade, copyright has come under attack as users have attempted to circumvent the doctrine's rules. One common example is the distribution of music over the Internet, through the use of peer-to-peer networking services. These services, such as BitTorrent, the original version of Napster, and others allow computer users to connect with each other and share specific files and folders. The MP3 file format allows digital music to be downsampled and converted to a much smaller format than that provided on a compact disc, with an acceptable loss in signal quality. There are widely accepted Internet conventions for scanning and sharing books, movies, and other works in compressed digital formats.

The creators of these file-sharing systems usually did not consider the restrictions of copyright or the moral rights of creators. The implementation of these systems is more focused on their speed and accuracy than on intellectual property law. In the United States, various industry groups, including the Recording Industry Association of America and the Motion Picture Association of America, have identified and sued Internet users who allegedly used their home or corporate Internet service to exchange copyrighted music and videos.

Recently, there has been a rise in the use of Web-based video sharing sites to post and distribute videos. In some cases, the creator of the video posted the work themselves. However, it has become easier to use a computer to capture or record a television broadcast or the playback from a DVD. Thus, television networks, movie and video production firms, and copyright holders have sued these sites or licensed their copyrighted works for limited distribution. In some cases, television networks have posted their own content on their own sites in an effort to control the digital distribution of these works.

User Rights and Electronic Distribution

Consumer/users often assume that they "own" the recorded and printed works that they have purchased. Copyright, however, provides users with a limited license to use these works. This license does allow users to sell their copy to another user, as long as the original user does not retain a copy of the work. Because it is easier than ever to copy and store digitized works, users are tempted to "have their cake and eat it too." Users often justify or rationalize their actions by citing the high price they paid for their license to use a creative work.

Authors, creators, and copyright holders have countered this trend by citing the significant costs and risks they face in developing and distributing creative works. The musical group Metallica stated publicly that file-sharing services harmed their livelihood, for example. Musicians do need to universally agree on the harm or value of electronic distribution, however. The growing use of electronic audio players such as Apple Computer's iPod, together with the popularity of online music stores that allow users to purchase and download licensed digital copies of recorded works, has fundamentally changed the economics of retail distribution.

Some users have responded by developing their own original creative works. In some cases, these works are a melding or "mashup" of two or more existing properties. This format was previous used in collages of printed media and the "sampling" of brief sections of recorded songs for inclusion in another performance. Again, computer technology allows users to combine two seemingly different songs into a new song that may strongly or vaguely resemble the original sources. It is also possible to edit the existing video so that actors are placed in different environments or a different audio is heard.

The popularity of Web logs or "blogs" also relies on the electronic distribution of original works. A text-based blog may be nothing more than a user's diary, posted to the Internet. Some bloggers link to newspaper and magazine articles, as well as other blog postings, and provide their own comments or interpretation of events. Many blogs allow users to read these postings and upload their own comments, thus creating a multitude of narrowly defined creative communities that work at a much faster pace than the traditional media.

—William A. Sodeman

See also Communications Decency Act; Intellectual Property; Internet and Computing Legislation; Patents; Property and Property Rights; Public Domain; Trademarks

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Corporate Accountability

Corporate accountability is a foundation of corporate social responsibility. Corporate social responsibilities, at the most general level, include economic duties, legal and regulatory compliance, responsiveness to ethical norms, and discretionary social welfare contributions. In addition, one of the most basic of all corporate social responsibilities is corporate accountability. It is defined as the continuous, systematic, and public communication of information and reasons designed to justify an organization's decisions, actions, and outputs to various stakeholders. According to this definition, corporate accountability is primarily a form of ethical communication directed toward those parties who are affected by corporate activities and effects.

Corporate accountability represents a corporation's social responsibility to explain its actions (past, present, and future) in an accessible, reasonable, and meaningful way to the society in which it operates. In a democratic society dependent on informed political discourse and deliberations, corporate accountability is a necessary foundation for the system of free enterprise. The appropriate level of corporate accountability underpins the legitimacy of corporate autonomy and decision making in a system of democratic capitalism. In such a system, business enterprises enjoy a high degree of economic freedom of choice and are expected to engage in activities that promote the interests of the business. This economic freedom, however, is contingent on the existence of strong accountability mechanisms.

There are various traditional institutional mechanisms, both external and internal to the corporation, designed to enhance and strengthen accountability to stakeholders. These well-known mechanisms include the annual report to shareholders, corporate governance, government regulations, corporate codes and credos, and various forms of corporate communications.

The Annual Report to Shareholders

The single most important component of corporate accountability is the annual report to shareholders. It includes three important financial statements: the balance sheet, the income statement, and the statement of cash flows.

The balance sheet provides a detailed list of corporate resources (assets) and claims to those resources (liabilities and equity). It can be compared with a photograph that summarizes the financial condition of a business entity at a *fixed point in time.* The income statement provides detailed information about revenues, expenses, gains, and losses. It is like a movie in that it explains what happened *over a period of time.*

The statement of cash flows provides information about the sources and uses of cash. It consists of three categories: operating, investing, and financing. The financial statements gain credibility because they are audited by certified public accountants. According to the Financial Accounting Standards Board, the three main objectives of financial accounting are to provide information that is useful to those making investment and credit decisions; helpful to present and potential investors and creditors in assessing the amounts, timing, and uncertainty of future cash flows; and about economic resources, the claims to those resources, and the changes in them.

Corporate Governance

Corporate governance is essential to corporate accountability and without which no corporation can exist. State laws demand that corporations are to be managed and directed by a board of directors. This board acts as a surrogate for the shareholders of the corporation and its primary role is to oversee management's performance in terms of increasing profits and meeting social responsibilities. As such, corporate governance is a fundamental component to corporate accountability as defined above because it provides a strong institutional forum for communication between managers and shareholders' representatives.

Corporate Regulations

In 2002, the U.S. Congress overwhelmingly passed one of the most significant pieces of securities legislation in U.S. history, the Sarbanes-Oxley Act. One of the main purposes of passing the Sarbanes-Oxley legislation was to reestablish the credibility of the financial markets by strengthening corporate accountability. This purpose is in line with the goals of previous federal and state legislation in the United States and across the world.

Sarbanes-Oxley contains several important features relevant to corporate accountability. It established the Public Company Accounting Oversight Board to oversee the accounting profession, thus radically limiting the profession's traditional autonomy. It requires chief executive officers and chief financial officers to certify all financial statements and assigns criminal responsibility to those executives who knowingly make a false certification while demanding enhanced corporate disclosures concerning off-balance-sheet financing. Sarbanes-Oxley contains several provisions to enhance auditor independence. It also requires corporate boards to establish independent audit boards.

Corporate Credos and Codes of Conduct

Credos and codes can potentially serve an important role in strengthening corporate accountability. By carefully defining its own ethical aspirations, a corporation can helpfully communicate the criteria by which it wants to be held and judged. While critics are quick to note the self-serving nature of many corporate credos and ethical codes, these kinds of documents often provide both outsiders and insiders specific and clear statements to use in evaluating the credibility of corporate management. Johnson & Johnson's corporate credo, for example, establishes customers as the primary stakeholder of the corporation. This credo is often cited as an exemplar.

Increasing Demand for Corporate Accountability

In recent years, the demand for corporate accountability has increased dramatically. This demand has been spurred by the sheer growth of corporate power and by corporate environmental disasters such as the *Exxon Valdez* oil spill of 1989 and the Union Carbide and the Bhopal, India, tragedy. Corporate ethics and audit failures such as those at Enron, WorldCom, and many other U.S. and global corporations have also contributed to the increased demand for more and better accountability. Globalization, the Internet, the greenhouse effect, the increased interconnection of the world economy, and the rising power of institutional investors have also contributed to this change. Finally, changes in ethical values, especially an expanded conception of corporate social responsibility, have altered expectations surrounding the need for a broadened conception of corporate accountability.

Limitations of the Financial Statements as an Accountability Mechanism

At the same time that the demand for accountability has increased, the usefulness of traditional financial statements is being questioned. While financial statements remain as an important source of reliable and relevant information about corporate activities, they have come under intense scrutiny in recent years. There are several limitations associated the traditional financial statements.

First, many items are omitted from the balance sheet. These include intangible assets, the value of human resources, and many liabilities such as pension and health care obligations. Second, investors and other interested parties question the use of historical cost as the predominant method of valuing assets. Third, there is a lack of forward-looking information in the annual report such as management's forecast of earnings per share. Fourth, the traditional annual report focuses exclusively on the financial performance of corporations and excludes information about environmental and social performance. Finally, annual reports, especially income statements, are subject to questionable accounting manipulations such as earnings management, a process whereby managers alter the timing of revenues and expenses to change investors' perceptions.

There is now convincing statistical evidence that earnings management is a frequent management technique used to make a company look better than it otherwise would have. These manipulations occur despite the requirement that all financial statements are audited by certified public accountants. Each of these limitations diminishes the usefulness of the financial statements as an accountability mechanism.

Corporate governance has also come under intense scrutiny in recent years. This criticism of corporate governance reached a climax in the wake of ethics failures, including earnings management, at Enron and Andersen.

The Broadening Scope of Corporate Accountability

In response to the increasing demand for corporate accountability and the limited ability of traditional solutions to the meet this need, the scope of corporate accountability has broadened considerably in at least four distinct ways.

Backward-Looking Information Versus Forward-Looking Information

At the heart of the traditional accounting model was the historical cost principle, which states that the original cost of an asset is the most reliable valuation basis. It has long been argued that the best way to measure assets, liabilities, equities, revenues, and expenses is through the use of historical cost. The primary justification for this has been reliability. Simply put, historical cost can be documented and verified by auditors with a high degree of confidence and certainty.

Although historical cost accounting scores high in terms of reliability, it scores much lower in terms of relevance. Investors and creditors trying to predict future performance are more interested in forward-looking information such as managers' forecast of future earnings per share than backward-looking information (such as last year's earning per share).

In the United States, the Securities and Exchange Commission has taken a major step forward in this area by requiring publicly traded companies to publish a management discussion and analysis section in their annual reports. These reports, as has been documented, contain valuable information not only about past decisions but also about future events and trends. In short, corporations are being asked by regulators and other stakeholders not only to reasonably justify *past* actions, but they must now also disclose and explain anticipated *future* actions.

Hard Versus Soft Data

The second change in broadening the scope of corporate accountability is related to the first. There is an ever-increasing flow of financial data carefully audited by outside accountants. This is the hard data. But, at the same time, there is an increasing demand for soft data, that is, information that cannot necessarily be quantified in a precise and exact way but nonetheless is important for decision making. Soft data include descriptions of new products, emerging markets, anticipated layoffs, planned capital expenditures, joint ventures, research and development projects, advertising campaigns, and many other items.

Consider the recent controversy over the disclosure of stock options as just one important example. Many companies argued with some justification that there is simply no known and noncontroversial way to value these options in a reasonable manner. These companies argued that assigning a dollar value to stock options would provide misleading and unreliable information to shareholders and creditors. Despite these arguments, however, the demand for additional disclosure concerning stock options is unabated.

Although at one time it was possible for companies to legitimately meet the obligation of corporate accountability by publishing a set of numbers with almost no description accompanying the financial statements, today this is no longer the case. Justification now requires accurate verbal disclosures and descriptions as well.

The Bottom Line Versus Multiple Bottom Lines

Third, can corporate performance be measured with a single number? Is it conceivable that all of a corporation's thousands of decisions, actions, and outcomes can be summarized and evaluated through net income? Although some companies and many short-term investors continue to act as if the answer to both these questions is yes, other companies have now learned through experience that even if it was once true, it is certainly no longer the case.

Perhaps the most important of the changes that we have documented so far is the increasing recognition that corporate accountability now requires managers to justify not only purely financial outcomes but also environmental and social outcomes. Connected to this change, the list of legitimate stakeholders has also expanded to include employees, customers, local and global communities, and others. This means there is no longer such a thing as the bottom line. Today, there are multiple bottom lines. In a sense, there are as many bottom lines as there are stakeholders.

While just a few years ago the phrase multiple bottom line was more metaphor than reality, today it is more reality than metaphor. The Global Reporting Initiative (GRI) was established in 1997 as a joint venture between the Coalition for Environmentally Responsible Economies and the United Nations Environment Program. In June 2000, GRI published a set of guidelines to help companies improve on their environmental and social reporting. These guidelines were revised in 2002. One thousand global companies now use some form of triple-bottom-line accounting in line with GRI guidelines—reporting on economic, environmental, and social behaviors and outcomes. Among these companies are 3M, AT&T, General Motors, Ford, Shell, McDonald's, Dupont, Dow Chemical, Nike, Canon, Electrolux, Ericsson, France Telecom, and some other smaller companies as well.

Monologue Versus Dialogue

Finally, careful examination of a set of recently issued sustainability reports demonstrates the most radical change of all. To legitimately justify an organization's decisions and actions, corporate accountability is now viewed and described by many as a dialogue between the corporation and its stakeholders and not as a monologue on the part of management. For example, see especially AccountAbility 1000's AA1000—Principles and Measurement Standards and a U.K. company law reform proposal that would require the dialogue between corporations and their shareholders to be published online. This means that corporate accountability requires listening to a company's diverse stakeholders as well as responding to them. It also means that many companies now openly recognize that corporate accountability is an evolving and contested concept.

There is a growing awareness of dialogue as a formal component of corporate accountability. Dialogue is emerging as one of its central and most innovative aspects. Dialogue does not imply that organizations are abdicating their responsibility for decision making. But it does imply a recognition that organizations are embedded in society and rely on it for legitimacy.

Conclusion

Those managers committed to the capitalistic system realize that it is in their own self-interest to enhance corporate accountability. In a world of instant communication, those corporations that can justify their actions in a clear and sensible way may possess a strong competitive advantage over rivals who maintain a policy of secrecy. It makes good business sense to enhance corporate transparency.

Corporate accountability, however, should not be conceived of as a kind of game. Rather, it is a form of ethical communication among human beings on which the future growth and legitimacy of business depends. As globalization spreads, corporate accountability is becoming the linchpin of the worldwide economic system. As the notion of corporate social responsibility gains credence across the globe, corporate accountability is increasingly viewed as a crucial task for boards of directors, corporate management, business consultants, and accountants. Corporate accountability has always played an important role in the financial markets, but as the concept of corporate accountability broadens, its role in society will gain in importance.

—Moses L. Pava

See also Accountability; Accounting, Ethics of; Corporate Citizenship; Corporate Social Responsibility (CSR) and Corporate Social Performance (CSP); *Exxon Valdez*; Honesty; Securities and Exchange Commission (SEC)

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Corporate Average Fuel Economy (CAFE) Standards

In 1975, in response to an energy crisis in the United States, Congress enacted the Energy Policy and Conservation Act, which included the Corporate Average Fuel Economy (CAFE) Standards. Initially, CAFE standards were part of an effort to reduce U.S. dependence on foreign oil. Today, these standards are part of the debate surrounding global climate change, as vehicles are one of the major emitters of greenhouse gases.

CAFE standards require automobile manufacturers to meet certain miles per gallon (mpg) standards for their fleet of vehicles. In 1974, the average U.S. passenger car had an mpg of less than 13, which was less than the average mpg of just a few years earlier. The CAFE standards required all new automobiles to have an average mpg of 27.5 by 1985. Although there have been numerous proposals to raise mpg requirements, as of 2005, the 27.5-mpg standard remains unchanged for passenger cars (although it was temporarily lowered from 1987 to 1989). Light trucks and SUVs, however, are held to a lower standard. Those vehicles must meet a standard of 22.2 mpg by 2007.

A manufacturer's CAFE is the average fuel economy of the manufacturer's fleet of vehicles for that model year weighted by the production volume of each model of car. Passenger cars and light trucks/SUVs are calculated separately. In addition, a manufacturer's fleet of passenger cars is divided into domestics and imports, as determined by the percentage of components manufactured outside the United States and Canada. The manufacturer must meet CAFE standards for both its domestic and import fleets separately. Failure to meet the standard results in a penalty of $5.50 for each one-tenth mpg the manufacturer is below the standard multiplied by the number of vehicles in manufacturer's fleet for that model year. If a manufacturer exceeds the CAFE standard in any year, the manufacturer is granted excess credits that may be used against past or future shortfalls (up to 3 years in either direction). Manufacturers may also receive credits through the use of alternative fuels (e.g., natural gas, ethanol) under the Alternative Motor Fuels Act of 1988. The National Highway Traffic Safety Administration, which is the agency with responsibility for CAFE standards, reports that manufacturers have paid more than $500 million in fines since 1983.

Opponents of raising CAFE standards claim that requiring automobile manufacturers to increase the mpg of their vehicles causes greater harm to society than benefits. The primary concern of opponents is that manufacturers meet mpg standards by reducing the size and weight of their vehicles, which leads directly to more deaths from automobile accidents. Others, however, claim that new lightweight materials can allow manufacturers to build higher fuel economy vehicles without a negative impact on safety. Opponents also argue that a higher fuel economy will lead to higher prices for consumers and to more traffic congestion and automobile accidents due to an increase in driving (assuming that individuals will drive more as the costs of driving a mile will be reduced with a higher automobile mpg). Finally, opponents claim that CAFE standards are unnecessary as technology development, and not regulation, drives improvements in fuel economy. Proponents of CAFE standards argue that those technologies already exist and manufacturers simply need the financial incentive to make the use of those technologies cost-effective.

—David Hess

See also Economic Incentives; Environmentalism; Environmental Protection Legislation and Regulation; Greenhouse Effect; National Highway Traffic Safety Administration (NHTSA); National Transportation Safety Board (NTSB); Regulation and Regulatory Agencies

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Corporate Citizenship

Corporate citizenship, sometimes called corporate responsibility, can be defined as the ways in which a company's strategies and operating practices affect its stakeholders, the natural environment, and the societies where the business operates. In this definition, corporate citizenship encompasses the concept of corporate social responsibility (CSR), which involves companies' explicit and mainly discretionary efforts to improve society in some way, but is also directly linked to the company's business model in that it requires companies to pay attention to all their impacts on stakeholders, nature, and society. Corporate citizenship is, in this definition, integrally linked to the social, ecological, political, and economic impacts that derive from the company's business model; how the company actually does business in the societies where it operates; and how it handles its responsibilities to stakeholders and the natural environment. Corporate citizenship is also associated with the rights and responsibilities granted to a company or organization by governments where the enterprise operates; just as individual citizenship carries rights and responsibilities, however, companies have considerably more resources and power than do most individuals and do not have the right to vote.

While CSR has historically referred to a company's economic, legal, ethical, and discretionary responsibilities, corporate citizenship emphasizes the integral responsibilities attendant to a company's strategies and practices. There are other definitions of corporate citizenship, but they are generally consistent with the theme of integrating social, ecological, and stakeholder responsibilities into the companies' business strategies and practices. For example, the United Nations' definition states that corporate citizenship is the integration of social and environmental concerns into business policies and operations. The U.S. association Business for Social Responsibility defines it as operating a business in a manner that meets or exceeds the legal, ethical, commercial, and public expectations that society has of business. The definition of the Center for Corporate Citizenship at Boston College requires that a good corporate citizen integrate basic social values with everyday business practices, operations, and policies so that these values influence daily decision making across all aspects of the business and takes into account its impact on all stakeholders, including employees, customers, communities, suppliers, and the natural environment.

The definition of the Corporate Citizenship Unit at Great Britain's University of Warwick Business School indicates that corporate citizenship involves the study of a broad range of issues, including community investment, human rights, corporate governance, environmental policy and practice, social and environmental reporting, social auditing, stakeholder consultation, and responsible supply chain management. Australia's Deakin University's Corporate Citizenship Research claims that corporate citizenship recognizes business's social, cultural, and environmental responsibilities to the community in which the business seeks a license to operate and recognizes economic and financial obligations to shareholders and stakeholders.

Background

The term *corporate citizenship* as applied to companies' core business practices, strategies, and impacts became popular particularly in the European Union in the mid-1990s but has been in use at least since the 1950s. The terminology evolved from earlier conceptions of business in society, particularly from the concept of CSR, which connotes doing explicit good for society mainly through philanthropy and is considered voluntary on the part of companies. Although some scholars and practicing managers do define corporate citizenship more narrowly than the definitions above, believing that discretionary activities on the part of companies to deliberately improve societies constitute corporate citizenship initiatives, most of the business associations and centers in academic environments have developed the more broad-based conception accepted here.

Typical manifestations of CSR occur through philanthropic programs, volunteer activities, in-kind giving, and community relations. In contrast, the dominant conception of corporate citizenship applies to the ways a company operates, that is, its fundamental business model, and the stakeholder, societal, and nature-related impacts that derive from the way the company does business. Although some definitions of corporate citizenship do focus more narrowly on social good activities of companies, the more business-model-based definition related to overall corporate responsibilities is widely accepted, as the definitions given above indicate.

In the 1960s, U.S. legal scholar Dow Votaw noted that companies needed to be understood not just as economic actors in society but also as political actors. Votaw focused on specific issues related to a company's corporate citizenship that retain currency today, particularly in light of the vast size and economic clout of many large multinational corporations. The issues that concerned Votaw included companies' influence and power, which are derived from a company's size and control of economic and other resources; questions about the legitimacy of firms in society and how they are to be made accountable to broader societal interests; and how companies could be sanctioned when wrongdoing occurs. Thus, deeply embedded in the notion of corporate citizenship is the idea that companies gain legitimacy through a form of social contract granted by societies typically in the form of incorporation papers. With legitimacy comes a set of rights and also responsibilities. Corporate citizenship highlights the specific arenas in which those responsibilities apply, encompassing relationships with stakeholders and impacts on the natural environment and societies.

The reach, scope, and size of many large companies have created significant pressures from different groups in society for better corporate citizenship and greater attention to the ethical values that underpin it. These pressures are highlighted by the fact that, by 2002, 51 of the world's largest economies were said not to be countries but companies. In part, it is this spectacular size and attendant power that have created much of the attention to corporate citizenship, fueled further by concerns about globalization's impacts; management practices of outsourcing key functions to developing nations to reduce costs; ethical and accounting scandals; and corporate influence on governments, communities, and whole societies.

Corporate leaders began paying significant attention to issues of corporate citizenship during the late 1990s and early 2000s, following waves of antiglobalization protests; critiques of corporate outsourcing practices; fears about climate change and other serious environmental problems said to be at least partially created by businesses; and the rise of anticorporate activism sometimes directed at specific companies and sometimes at policies of powerful global institutions such as the World Trade Organization, the World Bank, and the International Monetary Fund. Advanced communication technologies fueled the ability of activists and other critics to question corporate activities and create increasing demands for responsibility, transparency, and accountability by companies.

On the business side, numerous new activities and organizations designed to highlight good corporate citizenship emerged during the 1990s and early 2000s. At least partially in response to vocal activism about supply chain practices, many multinational corporations developed and implemented internal codes of conduct during the 1990s. Some of these companies also asked their supply chain partners to implement the codes in their operations as well. In addition to internal codes, a number of codes and sets of principles, frequently generated by multisector coalitions that included companies, governmental representatives, activists, and nongovernmental organizations (NGOs), also emerged. These codes represent what their developers consider to be a baseline or floor of ethical conduct that serves as the foundation of corporate citizenship. Prominent business ethicists Thomas Donaldson and Thomas Dunfee have labeled such foundational values hypernorms. Although still somewhat controversial as to whether they exist, hypernorms identified by Donaldson and Dunfee include basics such as respect for human dignity, basic rights, good citizenship, and, similarly, fundamental values. Such hypernorms serve as a foundation for all human values and also as a basis for good corporate citizenship. They are built on three principles, including the respect for core human values that determine a floor of practice and behavior below which it is ethically problematic, respect for local traditions, and respect for the context in which decisions are made.

During the 1990s and into the 2000s, there was a great deal of activism against certain corporate practices such as outsourcing, which frequently involved contracting with manufacturers in developing nations whose workers were subjected to abusive conditions, ecological deterioration, and poor labor standards, as well as the impact of globalization. This activism generated a flurry of development of codes of conduct that attempted to codify how such basic principles could be put into practice in companies. As the codes developed, many companies, particularly large multinational firms with brand names to protect, began demanding that their suppliers live up to the standards articulated in the codes.

Many companies developed their own codes of conduct; in addition, a number of codes emerged that were developed by multisector coalitions working from internationally agreed documents or core ethical standards. Among the most prominent, although not without its critics, was the United Nations' Global Compact's set of 10 (originally nine) principles, which were drawn from internationally agreed declarations and treaties. The Global Compact, which had nearly 2,000 members by 2005, was established in 1999 by UN Secretary-General Kofi Annan to "initiate a global compact of shared values and principles, which will give a human face to the global market." In signing onto the Global Compact, companies agree to uphold 10 fundamental principles on human rights, labor rights, environment, and anticorruption.

The Global Compact's 10 principles focus on core or foundational principles and are drawn from major UN declarations and documents that have been signed by most of the countries of the world. Documents from which the principles are drawn include the Universal Declaration of Human Rights, the International Labour Organization's Declaration on Fundamental Principles and Rights at Work, the Rio Declaration on Environment and Development, and the United Nations Convention Against Corruption. The two human rights principles require companies to support and respect the protection of internationally proclaimed human rights and make sure that they are not complicit in any human rights abuses. The four labor standards require companies to uphold the freedom of association and the effective recognition of the right to collective bargaining, eliminate all forms of forced and compulsory labor, effectively abolish child labor, and eliminate discrimination in employment. The three environmental principles require companies to support a precautionary approach to environmental challenges, undertake initiatives to promote greater environmental responsibility, and encourage the development and diffusion of environmentally friendly technologies. The corruption principle, added in 2004, requires companies to work against all forms of corruption, including bribery and extortion.

There are other important codes and principles aimed at putting corporate citizenship efforts into operating practices and strategies. These codes include the Guidelines for Multinational Enterprises of the Organisation for Economic Co-operation and Development, the Global Sullivan Principles of Corporate Social Responsibility, the Marine Stewardship Council's Principles and Guidelines for Sustainable Fishing, the Natural Step's Sustainability Principles, the UN's Norms on the Responsibilities of Transnational Corporations and Other Enterprises with regard to Human Rights, the Equator Principles (for the financial services industry), the Sustainable Forestry Principles, the Caux Principles, the Business Principles for Countering Bribery, the CERES (Coalition for Environmentally Responsible Economies) Principles, the Clean Clothes Campaign model code, the Workplace Code of Conduct of the Fair Labor Association, the Keidanren Charter for Good Corporate Behavior and the Keidanren Environment Charter, the Canadian Business for Social Responsibility Guidelines, the World Federation of the Sporting Goods Industry Model Code, and numerous others.

One observer at the International Labour Organization, a division of the United Nations, counted more than 400 such principles and codes including individual company codes. Many, although certainly not all, of the core issues embedded in these codes are similar, despite differences in wording and specific focus.

These codes and principles evolved, in part, because of societal concerns about corporate practices and impacts. For example, the practice of outsourcing operations including manufacturing and production of many goods and services to low-wage developing nations became very popular among large companies starting in the 1990s and continuing to the present. This practice drew attention to the companies' corporate citizenship because many of the facilities in the developing nations were exposed in media reports as having sweatshop working conditions, abusing the human rights of workers, having poor safety standards, or employing weak environmental management. The practice of outsourcing continued into the 2000s and expanded to call and support centers, programming, and other technologically sophisticated services, which shifted from the developed nations to the developing nations. Concerns about domestic job loss for communities where the outsourcing company had facilities combined with low wages and poor conditions in some developing nations created a public focus on the implications of this type of practice for different groups of stakeholders.

Other factors fueling attention to corporate citizenship include the array of ethical scandals, accounting misrepresentations, and frauds that were uncovered in the United States in the early 2000s, as well as in Europe and elsewhere. Accompanied by accusations of corruption and undue influence in the political affairs of nations, and participation by companies in abusive regimes in certain countries, these scandals drew attention to corporate citizenship or what some believed to be lack thereof. Chief executive compensation, estimated to be on the order of 450 times that of the average worker in the early 2000s, and a wave of consolidations through mergers and acquisitions that created huge oligopolies and even near monopolies in many industries, further fanned the desire for better corporate citizenship and also fanned the flames of attention to corporate citizenship.

Pressures for ever-increasing short-term financial performance from financial markets beginning in the 1980s and continuing to the present have focused many corporate leaders' attention on short-term share prices. The attention to share price caused some observers and critics to believe that companies were failing to pay sufficient attention to other stakeholders, that is, those affected by and able to affect the company's activities. Corporate citizenship thus evolved during the 1990s and 2000s in part as a voluntary effort by many large, and therefore highly visible, transnational corporations as well as numerous smaller ones, to demonstrate their goodwill in the face of concerns about their size, short-term decision-making orientation, their power accrued through control of financial and other resources, and not always positive impacts on stakeholders, societies, and the natural environment.

Criticisms of Corporate Citizenship and Responses

Criticism of a company's corporate citizenship can come from many sources, including activists, the media, local communities affected by company activities, customers, and sometimes nations. Some activists set up Web sites that attempt to foster action against a company, such as a boycott. Wal-Mart, for example, has faced significant problems in some communities because of the company's impact on local shopping districts, low wages, and discrimination against women. Some investors are also concerned about corporate responsibility or citizenship and choose their investments at least in part on the basis of how they perceive the company's corporate citizenship through what is called socially responsible investing. The Social Investment Forum in the United States estimated in 2003 that some $2.16 trillion or more than one of every nine equity investment dollars in the United States was invested in assets that employed at least one of the three main responsible investment strategies—screening investments, shareholder advocacy, and community investment. Screening investments means paying attention to particular negative practices, including poor supply chain management practices such as child labor or abusive working conditions, poor environmental practices, or harmful products such as cigarettes, which some investors wish to avoid. Some investors look for positive practices that they wish to encourage. Returns for investments in screened funds as compared with traditional funds are roughly comparable.

Shareholder advocates focus on changing corporate practices by submitting shareholder resolutions.

Shareholder resolutions are aimed at changing matters of concern to activist investors and are directed to the board of directors through the annual meeting process. Shareholder resolutions can focus on a wide range of issues of concern, including environmental policies and practices, labor standards, wages, harmful products, and excessive executive compensation, to name a few areas of criticism. Some chief executives engage in dialogue with the shareholder activists and promise changes, resulting in the resolutions being withdrawn, while others come to a vote during the annual meeting process. Community investors sometimes put their money into projects that are aimed specifically at helping to improve communities, such as housing developments, retail establishments, and similar projects. They may carry a somewhat lower rate of return than traditional investments, but social investors are willing to make that trade-off when necessary.

Defining corporate citizenship as the contributions of businesses to society through the combination of core business activities, social investment and philanthropy, and participation in the public policy process, the World Economic Forum created a framework for action signed by 40 multinational companies' CEOs in 2002. This framework for action focuses on three key elements that help flesh out what corporate citizenship means in practice: the companies' commitment to being global corporate citizens as part of the way that they operate their businesses; the relationships that companies have with key stakeholders, which are fundamental to the company's success internally and externally; and the need for leadership on issues of corporate citizenship by the CEOs and boards of directors of those companies. This statement also points out the array of terminology used to signify corporate citizenship activities: triple bottom line or sustainable development, ethics, corporate responsibility, and corporate social responsibility. The statement also emphasizes key elements of managing responsibility: leadership that defines what corporate citizenship means to a company, integration into corporate strategies and practices, implementation, and transparency.

Evidence of growing interest on the part of companies in corporate citizenship can be found not only in their joining organizations such as the UN Global Compact, the World Business Council for Sustainable Development (WBCSD), and similar organizations but also in a growing acceptance of the need to manage their responsibilities explicitly. The WBCSD focuses on three pillars of corporate citizenship that have come to be called the triple bottom line—economic growth, ecological balance, and social progress through the lens of sustainable development. For example, many transnational firms with long supply chains have been exposed to criticisms by activists that practices in supply chain companies, which may not actually belong to the multinational company, are problematic, with poor labor standards, working conditions, and environmental standards.

Some companies have actively begun to manage their supply chain relationships by asking suppliers to live up to the multinational's own code of conduct and standards of practice, as well as ensuring that conditions in their own operations are managed responsibly. Such responsibility management approaches are aimed at helping companies protect their reputations for good citizenship by establishing global standards throughout their supply chain. They are supplemented by an emerging institutional framework aimed at assuring that stated and implicit corporate responsibilities are actually met.

Stakeholders and Corporate Citizenship

The definition of corporate citizenship as having to do with the impacts of corporate practices and strategies on stakeholders, nature, and the natural environment links corporate citizenship integrally to the relationships that companies develop with their stakeholders. In the classic definition offered by R. Edward Freeman, stakeholders are said to be those who are affected by or who can affect a company. Stakeholders can be classified into two categories—primary and secondary. Primary stakeholders are those groups and individuals without whom the company cannot exist and typically are said to include owners or shareholders, employees, customers, and suppliers, particularly in companies with extended supply chain. Secondary stakeholders are those affected by or can affect the company's practices and strategies, but who are not essential to its existence. Secondary stakeholders typically include governments, communities where the company has facilities and operations, and activists interested in the company's activities, among numerous others. Sometimes governments or communities can be considered primary stakeholders, as when a company is in a regulated industry or when its business directly serves a given community. The environment is not a person but because all companies and indeed all of human civilization depend on its resources, it is frequently treated as if it were a stakeholder; hence, environmental management and related issues of ecological sustainability are tightly linked to concepts of corporate citizenship.

Each stakeholder group either takes some sort of risk with respect to the company, makes an investment of some sort in it, or is tied through some sort of emotional, reputational, or other means into the company's performance. Shareholders or owners, for example, invest their money in the company's shares and rightfully expect a fair return on that investment. Employees invest their knowledge, physical strength and abilities, skills, intellectual resources, and frequently also some of their emotions in the firm, and the firm invests in training and developing employees. Employees are repaid through their salaries and wages. A significant body of research exists that suggests that when employees are treated well by a company through progressive employee practices that are representative of good corporate citizenship, their productivity will be better and the company will benefit financially and in other ways. Customers trust that the products or services that they purchase will serve the purposes for which they are designed and add appropriate value. Good corporate citizenship with respect to customers, therefore, involves the creation of value-adding products and services. Problems with suppliers can result in numerous issues for companies relating to product quality, delivery, and customer service, not to mention the fact that if the supplier itself uses problematic practices, such as sweatshops or poor labor standards, the company purchasing its products will suffer from a degraded reputation. Hence, it is important for companies to manage their relationships with suppliers and distributors well, particularly because many external observers fail to differentiate between the corporate citizenship of the main company and its supply and distribution chain.

Communities are important to companies because they create local infrastructure, such as sewers, communications connections, roadways, building permits, and the like that companies need. Many companies that view themselves as good corporate citizens have extensive corporate community relations programs, including philanthropic programs, volunteer initiatives, and community-based events intended to enhance their local reputation as a neighbor of choice and sustain what is called their license to operate. Governments are important stakeholders, too, and most large companies have developed significant public affairs functions to deal with governmental relations. They also participate in the political processes of countries where they are located to the extent permissible locally, including contributing to campaigns and working through lobbyists to influence legislation.

Environmental management and sustainability have become important elements of good corporate citizenship as worries about the long-term sustainability of human civilization in nature have become more common. Many large companies have implemented environmental management programs in which they attempt to monitor and control the ways in which environmental resources are used so that they are not wasted through programs that encompass resource reduction, reuse, and recycling. A few progressive firms have begun to focus on issues of long-term ecological sustainability as well.

Responsibility Management and Assurance

Most large corporations today have developed specific functions to deal with these different stakeholder groups in what are called boundary-spanning functions. Because the quality of the relationship between a company and its stakeholders is an important manifestation of the company's corporate citizenship, these boundary-spanning functions, which include position titles such as employee relations, community relations, public affairs, shareholder relations, supplier relations, customer relations, are increasingly important.

In most large companies today there is still no one particular job title or function in which all the corporate citizenship activities reside, though some corporate community relations officers have assumed a great many of these responsibilities. A few companies have appointed individuals to positions with titles such as corporate social responsibility officer, vice president of corporate responsibility, or director of corporate citizenship. These jobs, however, are still far from common as of 2005.

In response to criticisms about their negative impacts on society, stakeholders, and nature, and questions about the credibility of their corporate citizenship, many large companies have developed corporate citizenship statements and strategies; some have even appointed managers to positions with titles such as corporate citizenship, corporate social responsibility, or corporate responsibility officer. By the early 2000s, many large corporations voluntarily began to issue social, ecological, or so-called triple-bottom-line reports, which encompass all three elements of corporate citizenship, aimed at economic, social, and ecological impacts.

Responsibility Management

Responsibility management and reporting in the early 2000s consisted of voluntary efforts on the part of companies to be more transparent about some of their practices and impacts. Because companies were able to report how, when, and what they wanted to, however, many critics still found problems with their corporate citizenship. In response, what can be called a responsibility assurance system, consisting of principles and codes of conduct, credible monitoring, verification, and certification systems to ensure that those principles were being met, and consistent reporting mechanisms began to evolve in the early 2000s.

A given company's corporate citizenship is guided by the company's vision and underpinned by its values. Responsibility management approaches begin with vision and values and are reinforced by stakeholder engagement, which helps companies to determine the concerns and interests of both internal and external stakeholders and make appropriate changes. Unlike CSR, which focuses on discretionary activities, corporate citizenship in its broadest sense represents a more integrated approach to the broad responsibilities of companies that is increasingly being accepted by leaders of global enterprises. When a company adopts a responsibility management approach as part of its corporate citizenship agenda, it also focuses on integrating the vision and values into the operating practices and strategies of the firm, typically by focusing on human resource practices and the array of management systems, corporate culture, and strategic decisions that constitute the firm. Another important aspect of responsibility management, which can be compared in its major elements to quality management, is developing an appropriate measurement and feedback system so that improvements can be made as necessary. A final element is that of transparency, as many companies managing corporate citizenship explicitly publish some sort of report that focuses on their social, ecological, and economic performance. Such reports have come to be called triple-bottom-line reports.

Responsibility Assurance

Skeptical stakeholders need reassurance that companies actually manage their stakeholder, societal, and ecological responsibilities well and were unsatisfied with voluntary internal responsibility management approaches, particularly since such approaches were still mostly in use by large branded companies concerned about their reputation, leaving most business-to-business companies and small and medium-sized enterprises to their own devices. Such critics need reassurance that stated standards are actually being met and that statements about corporate citizenship made by companies are accurate. As a result, in addition to internal and voluntary responsibility management approaches, during the early 2000s some large multinational companies began participating in an emerging and still voluntary responsibility assurance system. Responsibility assurance attempted to provide some external credibility to what companies were doing internally to manage their corporate citizenship. Responsibility assurance involves three major elements: principles and foundational values; credible monitoring, verification, and certification systems that help ensure that a company is living up to its stated values; and globally accepted standards for transparently reporting on corporate citizenship and responsibility activities.

Principles and Foundation Values

Principles and foundation values can be found in documents such as the UN Global Compact, OECD Guidelines for Multinational Corporations, and similar codes of conduct as discussed above. They provide guidance to companies about a floor of practice below which it is morally problematic to go and typically rest on core ethical principles or, as noted above, internationally agreed documents and treaties.

Credible Monitoring, Certification, and Verification Approaches

The second aspect of responsibility assurance encompasses credible monitoring, certification, and verification approaches. Because there is a great deal of skepticism about companies' actual corporate citizenship practice, many critics are unwilling to believe companies when they state that they are ensuring that their codes of conduct are actually being implemented. This skepticism increases in long global supply chains, where companies outsource manufacturing, assembly, and related low-skill work to facilities in developing nations; the outsourced work is granted to suppliers who are not actually owned by the customer or sourcing company. Although the supplier facilities are not actually part of the sourcing company, some multinationals' reputations have nonetheless been tainted when activists have uncovered problems in the suppliers' operations related to human and labor rights, environment, safety, working conditions, abuses that involve poor pay even by local standards or failure to pay overtime, and related problems. Child labor is another serious concern for some activists. It turned out that the media, activists, and ultimately the general public did not make a distinction between the supplying company manufacturing in developing nations and the customer company that was purchasing those goods—both were blamed for the use of child labor, but the multinationals were the nearer and more familiar target, so they bore the brunt of the blame. Even when the multinationals implemented their codes of conduct and asked their suppliers to live up to those codes, problems persisted.

As a result, some footwear, clothing, toy, and sports equipment multinationals and some large retailers, who were among the first companies targeted by activists for poor sourcing practices, not only asked their suppliers to implement a code of conduct but began hiring external verifiers to go into those companies and ensure that standards were actually being met. These verifiers are mostly independent agents; they include both NGOs and sometimes accounting firms attempting to develop an expertise in social, labor, and ecological monitoring. The verifiers perform three main functions in supplying companies, wherever they are found: verification that the standards of the sourcing firm are being met; monitoring of working conditions, pay, labor standards, and health, safety, and environmental standards; and certification to the external world that conditions are what the company says they are. Major companies such as Nike, Reebok, Levi Strauss, The Gap, Disney, and Mattel, and numerous others who have been spotlighted in the past, now employ external verifiers in addition to having their own codes of conduct and internal management systems.

Among the many organizations involved in the verification or social audit process are the Fair Labor Association; SAI International, which offers a set of standards called SA 8000; and the British firm AccountAbility, which offers a set of standards called AA 1000. Others include the Clean Clothes Campaign, the Worldwide Responsible Apparel Production program, the Ethical Trading Initiative, Verité, the Fairwear Foundation of the Netherlands, and the Worker Rights Consortium. Many of these independent monitoring and verification organizations are NGOs, while some social auditors are for-profit enterprises. In addition, some represent women's rights groups, some are focused on labor and human rights, and others are backed by religious groups. Some are local in scope and use local parties to actually conduct the monitoring, while the larger ones are international in scope. Concerns about this type of monitoring or responsibility audit, according to the U.S. association Business for Social Responsibility (BSR), range from issues about the effectiveness of monitors in actually uncovering abuses; lack of resolution of issues uncovered in reports by corporate headquarters; and opinions that other means of reducing poverty, corruption, and related systemic problems will be more effective than verification processes. BSR also suggests several positive reasons why companies wish to employ social auditors and verifiers, including cost reduction by using local monitors rather than in-house monitors especially when facilities are globally distributed, benefits to corporate reputation, better compliance both with the code and legal requirements, enhanced productivity and quality brought about by better working conditions, and greater transparency and related credibility with the public.

Globally Accepted Reporting Standards

The third important element of responsibility assurance is having globally accepted reporting standards that ensure that real transparency exists about corporate practices and impacts. Here, the analogy needs to be made to financial auditing and reporting. The auditing and accounting industry, at least within each nation, has long established standard practices, formats, and criteria for reporting corporate financial performance. Such standardization is important so that investors can compare one company's performance against others in the same industry or across different industries. Currently, the same cannot be said for corporate reporting about social and ecological matters, yet there are increasing demands on companies for greater transparency about their practices and impacts.

Although many companies issue triple- or multiple-bottom-line reports that focus not only on economic and financial matters but also on social and environmental ones, there is still no fully accepted reporting procedure that details what, how, and when different aspects of performance are to be reported. As a result, comparing the social or ecological performance of one company with that of others even within the same industry can be problematic. Restoring public trust in corporate citizenship ultimately will require standardization of social reports and even potentially some legal requirements that all companies issue such reports.

There are a number of initiatives aimed at developing globally accepted reporting standards that ensure social and ecological transparency, including a major initiative by the European Union to standardize CSR reporting. Indeed, the ISO organization, which sets quality and environmental standards, began to develop a set of corporate responsibility standards in 2004, which will be voluntary for companies once completed. A company called One Report helps multinationals and other companies gather and report on issues related to sustainability, which include both social and ecological elements, in a standardized format. Perhaps the most prominent of the initiatives around standardized triple-bottom-line reporting, sometimes called sustainability, reporting is that of the Global Reporting Initiative or GRI.

The GRI began in 1997 as an initiative of the CERES and became independent in 2002. Its mission is to develop globally standardized guidelines for sustainability reporting. Formed by a multistakeholder coalition, the GRI regularly gets input from businesses, accounting firms, and investment, environmental, research, human rights, and labor organizations to ensure that its standards are comprehensive, correct, and appropriate to the situation of different businesses. Linked cooperatively with the UN Global Compact, the GRI has developed specific reporting guidelines, principles for determining what to report and how, and content indicators that guide organizations in developing their own reports. In addition, because industries differ dramatically in the characteristics of what needs to be reported, the GRI also has begun developing industry-specific standards.

The GRI attempts to help companies integrate a number of complex attributes related to their corporate citizenship. These include their code of conduct, international conventions and performance standards, management systems standards, accounting for intangibles, assurance standards, and specific standards related to the company's industry. Sometimes criticized for its complexity, the GRI represents the most recognized approach to date of standardized triple-bottom-line or sustainability reporting.

Criticisms of Corporate Citizenship

Some observers believe that corporate citizenship merely represents an effort on the part of companies to create a positive public image rather than substantive change within the corporation. Particularly when corporate citizenship is treated as discretionary or voluntary activities designed to improve aspects of society, critics believe that it does not go deep enough. Others point out that while the United Nations estimates that there are approximately 70,000 multinational corporations in the world with hundreds of thousands of subsidiaries, only a few highly visible, mostly brand-name companies are actively engaged in explicitly forwarding themselves as good corporate citizens. For example, as of 2005, about 2,000 companies had joined the UN Global Compact, while about 350, many of which had joined the Global Compact, had completed triple-bottom-line audits following the procedures of the GRI.

Another criticism of the concept of corporate citizenship focuses on the fact that citizenship is an individual responsibility involving a corresponding set of rights that relate to membership in a political entity, typically a nation-state, that involve civil, social, and political rights and responsibilities, while companies are not people. Companies, however, do bear responsibilities for their societal and ecological impacts, because they command significantly more resources than do most individuals, because they can influence the public policy process in many nations, and because when they participate in civil society or the political process, they carry more weight than do most individual citizens.

—Sandra Waddock

See also Accountability; Codes of Conduct, Ethical and Professional; Corporate Philanthropy; Corporate Social Responsibility (CSR) and Corporate Social Performance (CSP); Disclosure; Global Reporting Initiative; Integrity; Strategic Transparency; Triple Bottom Line; United Nations Global Compact

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Corporate Democracy Act

The Corporate Democracy Act of 1980 was a bill introduced on April 2 to the 96th Congress by Representative Benjamin S. Rosenthal. The bill had eight cosponsors and was promoted by an alliance of consumer, labor, religious, and environment groups, most prominently, Ralph Nader, a lawyer and consumer advocate. It would have established additional federal standards for the internal governance and conduct of large nonfinancial corporations with more than 5,000 employees or $250 million in total assets. Although the bill was never passed, its introduction had lingering effects.

The sponsors of the bill and its advocates wanted to promote ethical business practices through broader public participation in and greater transparency of corporate activities, as well as increased rights for employees and penalties for corporate leaders who violated the new rules. Most significantly, the bill sought to democratize corporate governance by requiring that the majority of board members be independent from management and directors or officers serve no more than two corporations. The bill also mandated corporate disclosure of particulars, such as employee diversity, compliance with environmental regulations, and political activities. Furthermore, through community impact studies and corporate and federal assistance to employees and local governments, it sought to minimize the incident and impact of corporate relocations and closings. Last, it would have prevented corporations from dismissing or otherwise punishing employees for refusing to submit to a search or a polygraph test or for exercising legal rights in the workplace.

The debates that ensued over the bill centered on the question of whether management-dominated profit-seeking behavior was at odds with or in favor of the public interest. Proponents of the Corporate Democracy Act argued that corporations had become too powerful and secretive and that concentrated leadership led to business practices detrimental to the well-being of employees, communities, and the environment. Opponents of the bill countered that profit-maximizing behavior, regardless of who makes the decisions, benefits shareholders, through increased share prices, and the public, through the assurance of low prices and responsiveness to consumer demands. Sharing corporate decision making with countervailing groups, such as labor unions, environmental organizations, and consumer advocates, opponents claimed, would politicize board members and reduce efficiency, thereby harming shareholders and the public.

The bill did not succeed, but the political goals continue to be pursued by Nader and others. The original bill was referred to the House Committees of Interstate and Foreign Commerce, Energy and Commerce, Judiciary, and, last, to the House Committee of Education and Labor, where no further action was taken. However, components of the act have emerged as principles of U.S. political parties, such as the Green Party and the New Party, and a retitled version of the Corporate Democracy Act, called the Corporate Decency Act, continues to be promoted by Nader through the Center for Study of Responsive Law as a "Model Law."

In the Model Law version of the Corporate Decency Act, some changes have been made to the original act, including greater emphases on penalties for corporate crimes. However, it preserves the general intent of the Corporate Democracy Act—the protection of the public and employees through proposed changes to the corporate governance. Some key aspects of the Corporate Decency Act are as follows:

- The majority of the board will be comprised of independent directors.
- Unlawful corporate behavior will result in more stringent penalties.
- Notification and, in some circumstances, compensation to local governments and former employees for large industrial plant closings or relocations will be required.
- Employees' rights of speech, especially employee "whistleblower" rights, will be protected.
- Information, such as that related to the largest shareholders, company performance, political action committee contributions, health and safety, and criminal convictions will be disclosed.

—Julie Whitaker

See also Corporate Governance; Power, Business; Public Interest

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Corporate Ecology

Corporate ecology is a term used to describe the process through which resources are collected and transformed by corporate entities for use by citizens in modern, free market societies. Influenced by systems theory, corporate ecology seeks to achieve a deeper understanding and appreciation of the dynamic processes through which resources are concentrated and redistributed throughout interlinked elements including living organisms, naturally occurring physical cycles, and corporate activities. More specifically, as corporations act in pursuit of their missions, they have direct and indirect impacts on a variety of people, communities, governments, and natural environmental systems (e.g., air, water, soil, and biodiversity). From this perspective, scholars have found it important to reenvision business as a system nested within, and therefore dependent on, other larger systems, including the social, economic, and natural environments. Since corporate ecology conveys the nature of these systems' interdependencies, it does not imply that corporate activity is good or bad per se. Rather, the idea is that corporate activity has interconnected and multilayered influences and, therefore, must be studied in a multidimensional manner to more completely understand its importance in society.

This understanding has become more significant as members of modern society have become more dependent on corporate production for essential resources required to sustain life. While this may seem like a statement of the obvious, the near total dependence on corporate products to sustain human life is a relatively new development. A mere century ago, for example, nearly 90% of the U.S. population was able to get some proportion of their sustenance from noncorporate sources or self-production. The concomitant changes in resource acquisition and distribution have required new language to allow for proper discussion and analysis of the ecological dimensions of business. Such new language was first introduced to corporate social performance (CSP) modeling by David Saiia when he added corporate ecology to the economic, legal, and ethical responsibilities of Archie Carroll's CSP model to more fully explore these responsibilities as multidimensional, multilayered, and interdependent. Corporate ecology suggests that in some cases activities once deemed acceptable are actually in violation of some aspect of corporate social responsibility or corporate citizenship. For instance, Hooker Chemical exceeded the letter of the law in the disposal of highly toxic waste at Love Canal, but internal documents indicate that some members of the organization voiced doubts about the safety of chemical waste disposal practices at Hooker Chemical. These doubts foreshadowed the terrible consequences that occurred at Love Canal and inspired the Superfund legislation. Love Canal also captures the need and possibility of understanding corporate actions as ecological events. As a first step, William Frederick provided an overarching definition of ecologizing as the ability of business to forge cooperative, collaborative linkages with society that function adaptively to sustain life, which he contrasts to economizing as a process that efficiently converts inputs to outputs through competitive behaviors. Diane Swanson made further contributions to ecologizing by cautioning against reducing business activity to simple categories without reintegrating concepts back into a representation of the whole, including assessing the complementary relationships and dynamic tensions that can exist between ecologizing and economizing.

Along these lines, economizing and ecologizing might be complementary, as when business collaborates with consumers and government regulators to design products that are both safe and profitable. In contrast, trade-offs between ecologizing and economizing can pose social problems, especially since many corporate leaders have been trained to externalize all organizational costs that society will allow and then disregard what has been successfully put outside the boundaries of the corporation. For instance, in an attempt to economize or reduce costs, a firm may pollute the environment instead of internalizing the cleanup costs. However, as in any ecological system, checks and balances may eventually emerge to address such problems, as when a concern for pollution gave rise to the federal Environmental Protection Agency in the 1970s as well as state agencies that help regulate waste and its disposal. Some business firms, in turn, have responded by finding cheaper solutions to waste disposal, thus mitigating the tension between ecologizing and economizing. Since corporate ecology involves processes that are typically beyond organizational mission statements, it necessitates a larger, systematic grasp of organizational activities and reactions to their impacts. Advocates claim that this type of revisioning of corporate organizations and their activities is essential if executives, policy makers, management scholars, and students are to address adequately holistic concepts such as environmental sustainability, which argue for corporations to build more fuel-efficient cars or for power plants to adopt technologies that drastically reduce greenhouse gas emissions.

Despite calls for such reenvisioning, corporate ecology is still far from the mainstream view of business. Jerry Taylor of the Cato Institute dismisses concern about sustainability as corrosive to the global economy at worst and misguided at best. He argues that the sum total of the societal good corporations have done in raising the quality of the human condition far outweighs any environmental damage done incidentally through their activities. He rightly points out that dire poverty is often the proximate cause of environmental degradation in less economically developed countries. Moreover, Julian Simon famously challenged Paul Ehrlich's neo-Malthusian hypothesis that population growth would overshoot the world's resource supply by postulating that since the ultimate resource-creating capacity is human ingenuity, that people would actually be able to add more to the wealth of future generations than they would extract from it. Finally, some neoclassical economists, including Milton Friedman, have argued that corporate social responsibility or the idea of mandating that business organizations account for more than wealth creation for shareholders is inefficient and uneconomical. A closer reading of Friedman, however, reveals an important caveat—he expressly states that wealth creation is bounded by the legal and ethical standards of society. It logically follows that if corporate activity leads to environmental damage that adversely affects the social well-being, then that activity, while it might be economical, is not ethical. Indeed, there is mounting evidence that some corporate activity can have measurable negative impacts on societal well-being and ecological systems.

For instance, perfluorooctane sulfonate, the primary precursor to the popular Scotchguard product, has been found in tissue samples of animals in remote wilderness areas, including penguins in Antarctica, as well as in people worldwide. While there is some evidence that this chemical may be a carcinogen, another disturbing question is, "How does an industrial chemical used in relatively small amounts make its way to the most remote corners of our planet when no direct vectors are present?" As another example, high levels of dioxin, an unintended by-product of plastic incineration and other industrial chemical processes, have been found in whale and fish fat providing evidence of industrial ocean pollution. And global warming is at least partially a product of industrial power generation; and one indication of its impact is that the Arctic ice cover has been decreasing at a rate of 9% per decade since the 1970s. These issues are but a few among numerous scientific findings of detrimental social and environmental harms stemming from industrial activities. Some corporations have taken steps to adopt more ecologically friendly practices by issuing sustainability reports. And a number of management tools and approaches have been suggested for helping business organizations improve their ecological performance, including triple-bottom-line accounting, balanced scorecard, the natural step, the Zero Emissions Research Initiative, ecological footprint, and eco-effectiveness, all of which represent an opportunity for management and governments to recognize that ecologizing and economizing are not necessarily in conflict.

As important as these environmental initiatives are, it is important to remember that there are also distinctly human costs associated with corporate activity, such as low wages and bad work conditions that raise the specter of employee exploitation and alienation. More generally, the pressures and demands of modern employment often leave little time for family and parental duties, which can also cause alienation of employees from employers, the things being made, and the society that consumes them. That these outcomes are seen as direct and indirect consequences of corporate activity is an insight rooted in the late 1800s when society began to recognize the resource, product, and social alienation problems stemming from "industrial man" in isolation from the natural and social environment. Hence, corporate ecology encompasses intergenerational issues of justice, such as the rights of employees and consumers to a certain quality of life as well as the intergenerational rights of species to share a habitable planet.

Historically, management thinking and scholarship has preferred a compartmentalized vision of business in society. As an alternative, corporate ecology offers a way of understanding business as part of larger interactions and interdependencies, the goal being to sustain and enhance the benefits of business activity while reducing or eliminating their negative consequences.

—David H. Saiia

See also Biodiversity; Consumerism; Corporate Citizenship; Corporate Social Responsibility (CSR) and Corporate Social Performance (CSP); Deep Ecology; Invisible Hand; Natural Assets (Nonuse Values); Productive Efficiency; Recycling; Resource Allocation; Social Efficiency; Sustainability; Transparency, Market

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Corporate Ethics and Compliance Programs

Corporate ethics and legal compliance programs are formal programs aimed at managing the ethical and legal conduct of a company's employees. Although companies such as J.C. Penney have had codes of conduct since the early 1900s, the history of more complex ethics and legal compliance programs can be traced to the 1980s and the Defense Industry Initiative on Business Conduct and Ethics (DII). The DII is a consortium of U.S.-based defense industry contractors that subscribes to shared principles and standards of business ethics and conduct (see www.dii.org). The DII developed out of the U.S. president's Blue Ribbon Commission on Defense Management that was convened following a number of defense-industry scandals in the early 1980s. The Commission was asked to develop proposals to guide future defense contractor behavior. A number of companies voluntarily joined together to promote ethical business conduct. As of July 2004, 60 companies were DII members, including a number of smaller companies and companies that supply the defense industry. Members agree to live according to the following obligations:

- Adopt a written code of conduct.
- Conduct employees' orientation and training with respect to the code.

- Provide employees a mechanism to express concerns about corporate compliance with procurement laws and regulations.
- Adopt procedures for voluntary disclosure of violations of federal procurement laws.
- Participate in Best Practices Forums.
- Publish information that shows each signatory's commitment to the above.

The organization hosts a 2-day Best Practices Forum each year, with participation from member organizations and the Department of Defense. It also conducts workshops on specific topics, including yearly 1-day training for ethics/legal compliance professionals, and publishes an annual report to the public and government summarizing DII activities. Information about all these activities can be found on the DII Web site referenced above.

The DII obligations listed above contributed to the development of corporate ethics and compliance programs in these firms because they mandate a number of formal organizational programs, structures, and actions that member companies must undertake to avoid problems such as conflicts of interest and fraudulent time reporting in defense contracting work. For example, companies must have a written code of conduct, they must conduct orientation and training sessions, and they must provide a system for employees to report misconduct or express concerns. Organizations are also required to participate in best practices forums, meaning that they must have personnel who are responsible for managing ethics and legal conduct within the firm.

Shortly after the DII was established, in 1991, the U.S. Sentencing Commission guidelines for organizations were adopted to assess culpability and guide the sentencing of all organizations found guilty of corporate crimes (see www.ussc.gov). Since then, many companies have attended to these guidelines in an attempt to avoid serious sanctions that might be brought against the organization in any future legal proceeding. The guidelines were developed based, in part, on the DII principles and the assumption that the organization should not necessarily be held responsible for a single employee's illegal conduct if the court determined that the organization had made a good faith effort to avoid such misconduct on the part of its employees. In the case of conviction and sentencing, sanctions meted out to the organization by the court would be less severe if it found evidence of such good faith efforts to avoid illegal behavior. To provide organizations with some guidance regarding what the court would be looking for, the U.S. Sentencing Commission offered seven guidelines organizations should follow to be dealt with more leniently. These guidelines included features such as assigning responsibility for legal compliance at high organizational levels, development and distribution of conduct standards (e.g., a code of conduct), training on those standards, discipline for misconduct when it occurs, and an advice and reporting system that would catch problem behavior early and deal with it effectively. As a result, many organizations implemented formal ethics or compliance "programs" that included these elements and they assigned high-level personnel (often the legal counsel or someone in that office) to lead the effort.

With the establishment of this new formal role and structure in many organizations, the Ethics & Compliance Officers Association (www.theecoa.org) was formed, and as of 2006, it had grown to include more than 1,000 members from all kinds of organizations in 160 countries. Members serve as ethics or compliance officers (part-time or full-time) for their organizations and they meet regularly to share best practices regarding areas such as code development, training, hotline use, and conducting investigations. All these activities suggest that formal corporate ethics and compliance programs have become institutionalized, at least in larger U.S. firms. These formal programs generally include the following key elements: written standards of conduct that are communicated and disseminated to all employees; ethics training; and systems for anonymous reporting of misconduct, sometimes combined with telephone or Web-based advice lines. Since the Sarbanes-Oxley law was passed in 2002, organizations have paid even more attention to establishing anonymous reporting systems because these are now required by law.

In 2004, the U.S. Sentencing Commission revised its guidelines for sentencing organizational defendants after receiving input from companies, consultants, academics, and other interested parties. Among other changes, these revised guidelines call for more attention to "ethics" as well as legal compliance and attention to the ethical "culture" of the organization. These changes were thought to be necessary because observers had noted that a large number of organizations were engaging in a kind of "check-off" approach to the guidelines. These organizations conformed to the letter of the guidelines by assigning responsibility for the program to a high-level executive, and they developed codes of conduct, training programs, and reporting systems. But many of these formal programs were either unknown to employees or they were decoupled from everyday organizational activities. In other words, the organization might have a code of conduct, conduct perfunctory training on it, and post a free telephone number that employees could call to report problems. But, if the code was not widely distributed or used in daily decision making, training was ridiculed, or the telephone line was not trusted, organization members would see the formal program as inconsistent with the broader organizational culture, resulting in employee cynicism and program ineffectiveness. More and more, the commission recognized that formal programs must be consistent with the organizational culture to be effective.

It is important to note that a January 2005 U.S. Supreme Court decision (referred to as the Booker/Fanfan decision) has raised questions about the future role of all sentencing guidelines in the United States (organizational and individual). Although the guidelines are now considered advisory, they and the Commission remain in place and studies suggest that the large majority of sentences continue to conform to the guidelines. Therefore, companies that are engaged in these activities largely because of the U.S. Sentencing Guidelines will likely continue to pursue corporate ethics and compliance programs.

The ethics and compliance infrastructure in an organization generally includes some kind of office devoted to these issues. But how these offices and their activities are organized varies widely. Some organizations have large professional ethics and/or compliance staffs while others manage with just a few people at corporate headquarters and then delegate much of the work to line managers. Some structures are highly centralized while others are more decentralized, with business units having their own ethics/compliance officers. In public companies, oversight is generally provided by a committee of the board, such as the audit committee, that receives reports from executives who are responsible for these activities. Given their increased accountability, boards of directors have become more interested in the activities of ethics and compliance offices. However, little, if any, research has been conducted to investigate the effectiveness of different infrastructures.

Organizations communicate their policies to employees in a variety of ways, but most large organizations now have codes of conduct that are distributed to employees and taught about in training programs. Beyond that, organizations use mission statements, newsletters, Web sites, and other communication vehicles to remind employees of their obligations and commitments.

Training programs also vary widely from organization to organization. For some, training is designed by external consultants. Other organizations have in-house staffs that design and deliver their own training. Training is also delivered in a wide variety of formats from Web-based training to small group exercises and case discussions that may be led by ethics office staff, line managers, or consultants. Finally, training is offered at different times to different groups. Most organizations provide some training to new employees and annual training thereafter. Others also offer more specialized training for employees with particular needs. Sometimes, this training is voluntary. Again, we know little about the effectiveness of these various approaches to ethics and compliance training or the circumstances under which some approaches are more effective than others.

Organizations have also established telephone call-in lines. As suggested earlier, at a minimum, most organizations have such a line for the purpose of reporting observed illegal conduct. These are sometimes run by outside vendors who can answer the phone at all times of day and in different languages (for multinational firms with employees in different countries). Others are answered in the organization's ethics or compliance office and some encourage employees to call with questions and concerns, not just to report misconduct. Many organizations scrutinize these calls as part of their evaluation of program success. For example, an increase in calls that ask for guidance before taking action is generally considered to be a good sign that employees are using the hotline for its intended purpose. However, most organizations find that employees are reluctant to use the hotline to report misconduct because of concerns about confidentiality and associated fears of retaliation or because of feelings of futility (that nothing will be done).

Research does suggest that formal ethics and legal compliance programs are somewhat effective in reducing misconduct such as employee theft and increasing other types of behaviors such as reporting. The National Business Ethics Survey (NBES) of the U.S. population, conducted in 2003 by the Ethics Resource Center (www.ethics.org), reported that employees who work in organizations that have all four program elements (standards, training, advice lines, and reporting systems) observe less misconduct and are more likely to report such observed misconduct to management.

However, certain kinds of formal programs appear to be more effective than others. Researchers have characterized differences in the control orientations of such programs. For example, some programs are more "compliance" oriented, meaning that they are focused on adherence to rules, monitoring employee behavior, and discipline for misconduct. Compliance-oriented programs are designed to work by teaching employees about rules and policies and then holding them accountable for departures from the rules. They are likely to work largely by influencing employees' calculus about the likelihood of getting caught and the severity of penalties for misconduct. Other programs are more "values" oriented, meaning that they focus more on creating and appealing to shared aspirations, ideals, and values. As such, they tap into employees' ethical identity and create expectations for the kind of behavior that is appropriate within the organization. These two types of programs are not mutually exclusive and employees may perceive different emphases within a single organization's program. For example, a values-based program can create shared aspirations, but be backed up with accountability mechanisms and discipline for misconduct. Although both types of programs have been associated with positive effects, such as reduced misconduct, employees do respond more positively to values-based programs.

Furthermore, formal programs can be ineffective if employees see them as "window dressing" only (such as with Enron's famous ethics code). For example, the NBES reports that when employees perceive that executives and supervisors emphasize ethics, keep promises, and model ethical conduct, observed misconduct is significantly lower than when employees do not hold such perceptions. Similarly, another study found that informal cultural characteristics such as messages from leaders, daily discussion of ethics and legal compliance issues, and perceived ethics program follow-through (detecting misconduct, following up on concerns raised by employees, behaving consistently with policies) were found to be more important than the existence of a formal program for outcomes such as observed misconduct and willingness to report misconduct. These findings are consistent with the notion that formal programs work best when they are consistent with the broader ethical climate and culture of the firm. However, additional research will be required if we are to answer the many remaining questions about ethics and compliance program effectiveness.

—Linda K. Treviño

See also Ethical Culture and Climate; Federal Sentencing Guidelines; Sarbanes-Oxley Act of 2002

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Corporate Governance

In its essence, corporate governance refers to the organization of the relationships between shareholders, board of directors, management, and other stakeholders in a corporation. According to the Cadbury Committee, corporate governance is concerned with the processes by which corporations are directed and controlled. Corporate governance especially deals with exercise of authority over the directions of the company, the supervision of actions of top management, the acceptance of accountability, and the compliance with legal and regulatory frameworks in which the company operates. The term *corporate governance* is not easy to define, as it can be used differently in different contexts. Several academic disciplines that study corporate governance bring their own distinctive meaning of the term. For example, economic theory emphasizes the mechanisms used by financial suppliers of corporations to assure themselves of getting returns on their investment. The study of law examines the power and duties of various corporate governance actors and discusses the legal instruments by which property rights are organized. The authors from the management and business administration focus on internal governance mechanisms that enhance decision making and improve performance.

Definitions of corporate governance have also changed over time to reflect the shift of the purpose and roles of corporations in modern society. In the 1960s, the main purpose of corporate governance was control of business power and authority. Therefore, corporate governance was dominated by investor predisposed definitions supported by agency theory. The corporate discussion was primarily about the control of managerial self-interest and a board of directors' monitoring role. More recent definitions adopt a much broader view, contemplating the whole complexity of corporate life. Margaret M. Blair offers one such definition, according to which corporate governance refers to the whole set of legal, cultural, and institutional arrangements that determine what publicly traded corporations can do, who controls them, how that control is exercised, and how the risks and returns from the activities they undertake are located.

National Governance Systems

Although the conceptualization of national differences in corporate governance is often debated, most comparisons categorize countries into three groups: Anglo-American, continental European, and Japanese–East Asian models. The Anglo-American model is characterized in terms of dispersed ownership and corporate financing through equity or short-term debt markets and active markets for corporate control. It is shareholder oriented and perceives the firm as the private property of its owners. This model is prevalent in the United States and the United Kingdom. The continental European model is stylized by concentrated ownership (usually by large blockholders, such as banks and families), long-term debt finance, and underdeveloped market for corporate control. Although it primarily emphasizes the interests of shareholders, it also takes into account the interests of employees. This model is widely adopted in Germany and to a smaller extent in Continental Europe. Japan and East Asian countries follow a model that emphasizes development of long-term relationships among various stakeholders—the main bank, major suppliers, distributors, owners, and employees. In this pluralist framework, employees' interests take priority. Such an inward-oriented and employee-centered environment of strong and long-term internal relationships, which dominates the firm's governance structure, also diminishes most chances for hostile takeover.

Differences in national patterns of corporate governance are shaped by a plethora of historical, political, institutional, economic, and social influences and determinants. A large number of studies have shown how historical conditions and political institutions influence certain features of property rights and financial markets and, consequently, ownership concentration and company's access to external finance in different countries. Furthermore, some authors argue that one of the main political and social factors relevant to understanding corporate governance is the conflict between owners, managers, and workers. For example, where owners and managers have more power, corporate governance institutions tend to favor shareholders over stakeholders. Property rights, financial systems, and network structures are among the major factors accounting for these national differences.

Property rights define mechanisms through which different groups of shareholders exercise their control and how this control corresponds to managerial discretion. Shareholders rights vary internationally. The outcomes of such a divergence are complex legal and economic arrangements that shape the different mechanisms of corporate control. The Anglo-American system incorporates a liberal market approach. Here, market-oriented mechanisms of control are used to reinforce shareholder rights. Liberal property rights, which postulate relatively high disclosure of company information and establish a one-share–one-vote norm, provide strong protection of minority shareholders. Therefore, this system discourages disproportional control through blocks and favors different dominant interests within corporate governance. The continental European system exemplifies a constitutional model of shareholder control. In this model, shareholders delegate substantial control rights from the general shareholder meeting to a supervisory board. This approach tends to contribute to disproportionate power effects by large blockholders (families, banks, or other corporations). Given the ability of blockholders to secure greater control, they are able to pursue their strategic interests within corporate governance. Empirical research has supported the idea that concentrated ownership increases the external influence over management, whereas in the case of dispersed ownership the shareholders are largely separated from the firm. The Japanese system conforms to a shareholder authority model in which large shareholders hold broad powers. Cross-corporate shareholdings and weak information disclosure predominately protect property rights of majority shareholders and disable minority shareholders from having any influence over the firm.

The second major determinant of governance patterns is the type of financial system on the supply side of the capital market. Financial systems are usually divided into market-based and bank-based systems. The former has greater importance in the United States and the United Kingdom (Anglo-American model). This system promotes equity finance through active capital markets, where suppliers of capital (individuals or institutions) directly or indirectly invest in equity (shares) that is publicly issued by companies. Individual shareholders have little direct influence on management. If dissatisfied with management decision, shareholders have the ability to sell their equity holdings in the firm. In the United States and the United Kingdom, banks typically do not hold company equity and their representatives do not sit as bank representatives on the board, although bank directors as individuals are represented. The bank-based financial system is found to be a dominant investment pattern in Continental Europe and Japan. Banks are the key financial institutions and are closely involved in ownership of the corporate sector. Banks hold shares either in their own right or collect deposits and invest them into companies for others. Their double role as lenders and important shareholders has often been stressed. It has been a historical tradition for this financial system to mobilize capital to the industry. In doing so, it has contributed to the growth of strong relationships between banks, industrial corporations, and other business partners. Dominance of debt finance, through the bank-based financial system, has caused in Germany, for example, the equity market to be relatively undeveloped when compared with equity markets within the Anglo-American system. The German banks have a mechanism for evaluating companies that is not practiced in the banks of the Anglo-American system. In Japan, the same function is covered by large and powerful planning departments of the *keiretsu's* main bank and trading company. The differences between these two financial systems are evident in several measures—share market capitalization, the distribution of financial assets, and firm debt/equity ratios. Even though a large number of countries occupy a position between the two opposing models, financial systems have significant impact on corporate governance. This grip is based on their ability to provide different sources of finance and via their capacity to influence relationships between different shareholders.

Variations in governance systems are also a consequence of interorganizational arrangements or network structures. A network structure refers to the quality and quantity of direct and indirect relationships between companies. Research on social networks has shown that the company's position within the network determines its access to critical resources, diffusion of practices across the companies, and overall power of the company within the network. Interorganizational arrangements of firms that belong to the Anglo-American system of corporate governance are characterized by loosely coupled connections. Their network structure is usually not based on ownership arrangements. Such weak ownership ties, fostered by financial interests of companies, facilitate market-like behavior in their mutual relations. Corporate networks in countries of the continental European system of corporate governance often involve vertical ownership arrangements with various suppliers and the board, thereby interlocking directorates among critical shareholders and creditors. These interorganizational networks are characterized by a high degree of intercorporate cooperation, which strategically promotes long-term relationships between various stakeholders. Codetermination policies in the German model of corporate governance, for example, see large companies as informal partnerships between labor and capital. At the center of the Japanese corporate grouping is a powerful bank or a financially strong company that can provide the other members of the group with capital at low cost. Reciprocal cross-shareholding in the Japanese system strengthens the commitments of organizations within the corporate network/group and weakens the influence of outside entities. This is why hostile takeovers in Japan are virtually unknown. Companies are acquired by other companies only through mutual consent.

The Shareholder Wealth Maximization Model of Corporate Governance

Given an assumed separation of ownership and control in the modern corporation, the shareholder wealth maximization model regards the firm as a nexus of contracts through which various participants arrange their transactions. This theoretical perspective received the strongest support from the "Chicago School" of law and economics. Relationships between shareholders and managers are seen as classical principal-agent relationships with all the difficulties of enforcement associated with such contractual arrangements. The primary responsibility of management is to maximize the value of shareholders' investment via dividends and market prices of the company's shares. Thus, according to this model, the major concern of good corporate governance is how to control the behavior of top management and get them to run the company in the interest of shareholders.

There are at least four mechanisms by which shareholders can induce management to adopt an orientation toward shareholder value: (1) a relatively large ownership position, (2) compensation linked to shareholder return performance, (3) threat of takeover by another company, and (4) competitive labor markets for corporate executives. It is expected that a management share ownership option will motivate managers to identify more closely with the shareholders' economic interest. Though many top executives own a relatively large percentage of shares in their companies, their perspective on risk may differ from that of shareholders. It can be expected that managers have a lower acceptance of risk than shareholders. Where a company makes risky investments, shareholders can always balance this risk against other risks in their portfolio. Managers, however, can only balance an investment failure against the other activities of the company and are, therefore, more affected by investment risk.

The second mechanism that aligns managers' with shareholders' interests refers to compensation tied to shareholder return performance. This is the most direct means of influencing management behavior. Here, a variable portion of managers' compensation is linked to the shareholders' realized market returns. However, this mechanism is not without limitations. For example, an increase in the price of market share may be the consequence of factors beyond management control, regardless of whether they have worked hard or made good decisions.

The third mechanism is the threat of takeover by another company. Any extensive exploitation of shareholders' or maximization of managers' self-interest should be reflected in low share prices. A lower share price provides a takeover opportunity for another company or investors. The new owners will usually replace existing management. Where such a circumstance is plausible, an active market for corporate control proves to be both an external and ultimate mechanism that has the ability to create a convergence of interests between managers and shareholders.

The fourth and last mechanism of aligning managers' self-interest with those of shareholders is the competitive labor market for corporate executives. Managers compete for positions within and outside the company. Within this market they are evaluated on corporate performance, both in terms of accounting-based and share market–based measures. As a result, executives leading poorly performing companies will be offered fewer top executive positions within and outside the company.

The shareholder value perspective was dominant both in U.S. and U.K. companies in the 1970s and 1980s. An emphasis on sustaining share price and dividend payments at all costs encouraged the use of mergers and takeovers as mechanisms of corporate control to punish managers who were unsuccessful in improving shareholder value. Such an approach created economic instability and insecurity and was widely criticized by various economic and strategic analysts.

Throughout the years proponents of the shareholder value perspective have become more tolerant toward the interests of other stakeholders. Nevertheless, the main principles, which claim the supremacy of the ultimate owner, have remained the same. Consequently, the focus on shareholder value and stakeholder interests has become a foundation of good corporate governance.

The Stakeholder Value Perspective on Corporate Governance

The stakeholder view of corporate governance argues that all groups and/or individuals with legitimate interests in the company have the right to participate in the company's activities and gain a share of its economic success. There is no distinct priority of one set of interests and benefits over another. Therefore, a company should be seen as an organizational coalition between numerous and heterogeneous groups who provide their resources (i.e., capital, labor, management, loans, expertise, material, and service) to accomplish multiple, and not always congruent, goals through the company's activities.

Primary stakeholders are considered to be those with a legitimate claim to participate in the company's affairs, that is, those who directly participate in the economic-value-creation process and who are directly affected by the company's policies (e.g., employees, specific customer segments, key suppliers, certain financial institutions, and key governmental agencies). Other interest groups such as local communities, trade associations, and consumer groups, which are indirectly affected by the company's actions, are regarded as the secondary stakeholders.

According to the stakeholder perspective, the major concern of corporate governance is how to balance the interests of different stakeholders. Shareholders' legitimate emphasis on share prices and dividends must be balanced against the legitimate demands of other groups. However, these demands are not only financial. Different groups have different values. For example, employees might highly regard education and training support, suppliers of materials might prefer secure demand, and the local community might appreciate minimal air pollution. The balancing of these interests requires constant negotiation and compromise between inside and outside stakeholders and between directors and managers.

The trend toward the stakeholder perspective of the corporate governance is reflected in existing and emerging regulations of many developed countries. The codetermination laws in Germany, which require employee representation on the supervisory board; harmonization of the rules relating to company law and corporate governance in the European Union, which will take into account interests of employees, creditors, and customers; the Japanese well-known legal and customary model of corporations with its interrelated stakeholders including customers, suppliers, financial institutions, and other business partners; and the campaign toward stakeholder law in the United States all demonstrate demand for formal instruments to democratize the governance of corporations.

Board of Directors

The board of directors is a governing body elected by shareholders to direct and supervise the management of the company. The board establishes the strategic direction and objectives of the company and sets the policy framework within which the company operates.

Different countries have different governance practices in terms of the board composition and its functioning. However, in general, members of the board of directors can be grouped into two main categories: (1) executive directors, who also have a management function in the company; and (2) nonexecutive (outside) directors, who have no managerial responsibilities. Nevertheless, they can have executive functions in other companies. Nonexecutive directors are selected to ensure that a broad range of skills and experience is available. In addition, a nonexecutive director can be formally classified as "independent." An "independent director" has no direct or indirect, current or previous, professional or personal interest or relationship in the company. It is believed that independent directors will empower the board with their ability to exercise independent judgment and effectively monitor management. Increasingly, the corporate governance practice of some countries has required or encouraged representation of formally independent directors on the board.

Within the tradition of the companies that originate in the Anglo-American system of corporate governance, boards can delegate some of their functions to various committees of the board. The purpose of a committee is to address certain issues in a more detailed manner than is possible at board meetings. The board as a whole, however, retains full responsibility. It is a standard practice for nonexecutive directors to establish the audit committee and remuneration committee. The audit committee oversees compliance with statutory responsibilities, thus ensuring that adequate internal controls are in place, advises the board regarding accounting policies and practices, and reviews the scope and outcome of the external audit. The remuneration committee deals with remuneration packages of the executive and nonexecutive directors and other groups of key executive managers. It may also consider succession issues.

Roles of the Board

Board roles can be generally categorized into three groups—control, service, and resource provision roles. The control roles involve the directors' fiduciary duties of monitoring management on behalf of shareholders. Directors' responsibilities in this role include appointing and dismissing the chief executive officer (CEO)/president and other top executives, deciding executive remuneration, and monitoring managers to ensure that shareholders' interests are protected. The services roles consider directors' advisory functions in formulating strategy and providing guidance to the CEO and top managers in other managerial and administrative issues. The resource roles refer to directors' assistance in the acquisition of critical resources for the company.

From a legal perspective, the control role is the primary purpose of the board of directors. Directors owe fiduciary responsibility to the corporation and shareholders. Fiduciary duties include the duty of care and duty of loyalty. Essentially, fiduciary duties call on directors to make every attempt to be well-informed before they make decisions, to act in good faith and the best interest of the shareholders, and to be independent in their decisions. From a financial perspective, directors' control role is primarily grounded in agency theory. That is, directors' source of power is derived from shareholders. Board members are selected by principals (shareholders) to monitor managerial behavior (agents). By actively monitoring management actions and firm performance, the board can reduce agency costs and maximize shareholder value.

One of the most prevalent roles of the board is its service role, that is, provision of advice and support to the CEO. It is argued that this role is most visible in organizations that experience external monitoring mechanisms, such as product and managerial labor markets. The service role is also stressed in the companies with major institutional shareholders, which decrease the need for active board control. Directors' involvement in the determination of corporate strategy is an important aspect of their advisory role. A number of studies have shown that directors engage in various stages of the strategic planning process, from the review of strategic initiatives to active involvement in strategy formulation.

The board is often seen as a key organizational body that could provide critical resources for the company, protect the company from environmental uncertainties, and reduce transaction costs in managing external relationships. Nonexecutive, outside directors, in particular, play an important role in providing (1) specific resources otherwise unavailable to management (e.g., financial funds, information), (2) access to external institutions and influential organizations (e.g., regulatory bodies, consulting firms, and international organizations), and (3) legitimacy. Resource scarcity prompts corporate boards to engage in interorganizational relationships in an attempt to moderate influences of external pressures on their companies. As capital is one of the key resources, companies often use interlocking directorates with financial institutions as a tool to facilitate access to cash. Contextual factors may moderate the importance of the resource role of the board. For example, small and entrepreneurial companies in which access to critical resources is problematic will benefit from the appointment of a reputable and influential director on their board.

Different Board Structures

In the Anglo-American system, boards of directors are usually unified bodies dominated by management. In a great number of large corporations in the United States and the United Kingdom, the CEO is also the chairperson of the board of directors. CEO duality is often criticized as an undesirable feature of this system, as it may limit the board's independent decision making. A typical board has between 9 and 15 members, most of whom are nonexecutive, outside directors. All directors are elected by shareholders in a general annual meeting. It is common for many individual shareholders not to attend these meetings. Most shareholders will vote on the election of directors and important policy proposals by "proxy," that is, by mailing election forms. There is no legal requirement for any specific stakeholder or interest group to be represented on the board. To achieve a greater accountability of directors to shareholders, an attempt is made to restructure the traditional board composition and introduce a majority of nonexecutive directors (i.e., directors not employed by the firm).

The continental European system of corporate governance functions on a two-tier board structure. This model is practiced in Germany, Austria, Holland, France, and Finland. The functions of the board are performed and split between a supervisory board or council and a management or executive board. The supervisory board has three core roles. First, it approves and evaluates the company's strategy and policies proposed by the management board. Second, it monitors the company's performance and accounts. Third, it appoints and dismisses members of the management board and monitors and evaluates the performance of the board itself. All members of the supervisory board are nonexecutives and no common membership is allowed between the boards. The supervisory board is headed by a chairperson, whereas the management board is headed by the CEO. The members of the supervisory council are elected at the general shareholders meeting. The management board is responsible for the day-to-day operations and running of the company. A two-tier board structure may work better where shareholdings are not as diversified as in the Anglo-American system and where there is a strong stakeholder concept, as in Germany.

In the German model, which is the most distinctive in this system, the supervisory council (*Aufsichtsrat*) consists of both employee representatives, appointed through trade unions, and capital representatives, appointed by shareholders. Members of the management board (*Vorstand*) are professional managers. Although all directors in the supervisory council are nonexecutives, they are seldom truly independent of the company. In enterprises with more than 500 employees, employees are represented in the supervisory council. In such cases, the council can have up to one third of employee representatives.

In the Japanese system, the formal corporate structure is that of a unitary board. Japanese boards are usually very large, with sometimes more than 30 members. Some researchers consider the *keiretsu* of cross-shareholdings as an informal governing body. It is a common practice that corporate governance takes place behind the scenes, between the corporate executives and representatives of major institutional shareholders. In general, the board of directors does not have external representatives of shareholders (outside directors). The only external person on the board may be a representative of the main bank. The board is composed of the corporation's own executives and former executives. The majority of directors within Japanese corporations are promoted from within the company and the rest are appointed from parent or affiliated companies. This internal promotion practice is an important component of the lifetime employment policies in Japanese corporations. The advancement to board membership is awarded to employees at the end of their working career for excellent performance during their professional employment. In this way, the boards of Japanese corporations represent the collective interests of the company and its employees rather than its shareholders.

Relations Between the Board and Management

The quality of board-management relationships is an ongoing issue for every board, regardless of the national setting. Both management and the board are responsible for the well-being of a corporation. The main question is how do the board and corporate management strike a balance for sharing these responsibilities?

The CEO is responsible for the day-to-day company operations and is expected to be the best-informed individual and most committed to the company. The directors are usually not involved in the operational affairs of the company and rely on the information provided by the CEO. In general, the directors should give an overall direction to the company, approve strategic decisions, and propose structural changes. It is believed that the separation of the role of the CEO from that of the chairperson enables a greater balance in board functioning, by way of limiting the power of the CEO to dominate the board.

However, many scholars and corporate governance experts also believe that effective functioning of the board depends on the quality of individuals and their ability to interact among themselves, and with the CEO and other managers, rather than only on the structural composition of the board. The fact that shareholders, management, and other stakeholders have changing expectations about the directors' knowledge and contribution to and involvement in the company's strategic affairs have led boards around the world to redesign themselves and their relationships within and outside corporations. Boards are expected to be more proactive in seeking information, in challenging the CEO in a constructive manner, in working together as a team, and in getting a deeper understanding of the company's business.

Some proponents of board redesign emphasize the importance of the dynamic balance between control and collaboration approaches in the board-management relationship. According to this view, a control approach protects a corporation from self-serving behavior and reduces goal conflict, whereas a collaborative approach encourages cooperation between the board and management and fosters trust and goal alignment. Acceptance, understanding, and management of control-collaboration tensions promote learning and improve governance. Other authors stress the role of the CEO and called to attention the evolution of the CEO-board relationship. Following the evolutionary perspective, these authors argue how the advisory role of board has a relatively higher significance in the early period of CEO tenure while the control-focused approach is emphasized more in the later CEO tenure.

The Changing World of Corporate Governance

The emerging research on corporate governance has extensively considered new developments in national corporate governance systems, the increase of institutional shareholders activism, and the changing role of boards in knowledge-based organizations.

Changes in National Governance Systems

The Asian financial crises in the late 1990s and the U.S. corporate scandals at the beginning of this century have fuelled debate concerning the current models of corporate governance. Market failures and corporate collapses have urged the need for radical reforms in corporate governance and regulation. In the last decade, corporate governance transformation has become a major concern of national governments, stock exchanges, international organizations, and corporations themselves. More than 40 countries published corporate governance codes; the OECD has issued the principles and World Bank and IMF released the guidelines. In the United Kingdom, Sir Adrian Cadbury's final report on "The Financial Aspects of Corporate Governance" in 1992 and the final Hampel Report in 1998 were influential in setting in motion corporate governance reforms in the United States and in the United Kingdom. The Cadbury Code became a framework for international standards of governance. The main recommendations related to (1) the clear separation of responsibility at the corporate level, (2) involvement of nonexecutive directors, (3) the role of committees formed by nonexecutive directors, and (4) the formation and functions of audit and remuneration committees.

The most current major initiative to radically improve the corporate governance system in the United States came in the form of the Sarbanes-Oxley Act of 2002. The act was formed in response to a series of corporate collapses, including the Enron, WorldCom, and Tyco International financial scandals. It is designed to protect shareholder value and the general public from corporate wrongdoing. The Sarbanes-Oxley Act dealt with four major issues in corporate governance of public corporations. First, the act created an oversight board to set and enforce auditing standards and discipline public company auditors. Second, the act intended to foster auditor independence. For example, the corporate members with a financial reporting supervision role should not be employed by the external auditor. Third, the act increased corporate responsibility, by requiring that CEOs and CFOs certify all periodic reports containing the company's financial results. Having knowledge of the certification of false statements is subject to criminal liability. Finally, the act enhanced financial disclosure with regard to the off-balance-sheet transactions and obligations with consolidated entities and individuals. These key provisions of the Sarbanes-Oxley Act have significantly strengthened the role of the board of directors and have made managements more accountable.

The cooperative, inward-oriented and employee-centered model of the Japanese corporate governance system was usually portrayed as a source of competitive strength for the Japanese economy. However, since the beginning of the Japanese recession in the 1990s, many studies have shown that some of the reasons for the economic downturn in large Japanese companies originated due to a lack of effective monitoring of managers by shareholders and weak accurate disclosure of companies' financial conditions and business performance. To improve the state of the economy, Japan has embarked on the modernization of the corporate governance system emphasizing better protection of shareholders rights, increased responsibilities of directors, and regular disclosure of information. In 2003, the Corporate Governance Forum in Japan established guidelines and defined best-practice corporate governance principles. The forum proposed the adoption of specific elements of the Anglo-American system. These included appointment of nonexecutive directors on the board, introduction of an executive officer system, and enforcement of auditor power.

The German model of corporate governance has also been pressured to undertake reformative changes. The publication of the official "German Corporate Governance Code" in early 2002 marked a milestone in the development of good governance in Germany. The code addresses all major criticisms, especially from international investors, that point against German corporate governance—namely, inadequate focus on shareholder interests, insufficient independence of supervisory boards, the two-tier board structure, the limited independence of financial statement auditors, and inadequate transparency of the German corporate governance system. The main purpose of the code is to make Germany's corporate governance rules transparent for both national and international investors.

In Europe, the EU Commission's role in corporate governance has increased in recent years but is limited due to major differences in national and company laws. In May 2003, the EU Action Plan was set up to define minimum governance standards for European companies. The idea of the EU Action Plan is not to legislate for all EU member states but to achieve convergence of the many different governance regimes within a well-defined timeframe.

The Rise of Power of Institutional Shareholders

In the 1970s, individual shareholders held almost 80% of the equity in the United States. By the end of the 1990s, however, their holdings had decreased below 45% while institutional shareholding had increased to 53%. In 2002, individual ownership declined further to just over 37% while institutional ownership reached over 55%. Corporate governance is highly affected by changes in power of different categories of shareholders. Controlling shareholders, such as families, individuals, or other corporations, can have significant influence over corporate strategic behavior. Small individual shareholders, on the other hand, do not exercise governance rights as they usually do not have knowledge, power, and incentive to control corporations. However, they are concerned about fair treatment from majority shareholders and management. Institutional shareholders have emerged as a distinctive and demanding voice in corporate governance within the Anglo-American system. Institutional investors, such as large pension and mutual funds, have the power to directly influence managerial decisions in many corporations. Their activism has led to a greater emphasis on shareholder value and directed management to place greater priority on their interests rather than those of stakeholders. The board of directors meets regularly with representatives of institutional and large investor groups to actively communicate corporate developmental strategies. It is expected that such groups have higher knowledge and long-term interest in the company. In this situation, management interests are more likely to be aligned with those of shareholders. Some observers of institutional investor activism assume that this development is bringing the Anglo-American model of corporate governance closer to those of the continental European and Japanese models.

Corporate Governance in Knowledge-Intensive Firms

The context of increasing technological intensity creates additional challenges for corporate governance. A boards' legal and moral authority has always been derived from their representation of shareholders of the firm. This authority, legally translated into accountability for the key strategic assets of the firm, guides deployment of these assets toward the most productive and shareholder-approved uses. However, the nature of strategic assets that needs to be accounted for in a knowledge- or technology-intensive company is significantly different. It is not only that these assets are intangible but also there is difficulty in agreement over who owns them and who is responsible for them. Specific assets, such as human capital, producer's tacit learning, or complex networks of interorganizational interactions, create a governance problem that standard models of control in corporations do not explicitly address. Due to lack of knowledge and inability to evaluate information, a traditional board of directors, for example, may be an ineffective governance mechanism.

The competitive advantage of knowledge-intensive firms comes mainly from nonphysical and nonfinancial assets, which can include employee know-what and know-how, training and development processes, and intellectual property. These companies offer different organizational cultures that thrive on ambiguity and offer an antithesis to control approaches that are more amenable to traditional industries. Such cultures reflect changes in power relations between financial and human capital. In these organizational environments, greater attention is paid to human resource issues because of an increased importance of technical and scientific personnel. As some authors suggest, human capital—the assets that each day go home and which are readily moveable—should be treated with care. Therefore, corporate governors should more explicitly affirm the rights of nonshareholders by allowing them formal involvement in governance processes. This formalization may be initiated through special compensation schemes or other arrangements that align the employees' interests with those of shareholders. Thus, if knowledge is the immanent resource and a critical asset of new companies, are individual employees becoming residual claimants in the changing world of corporate governance?

Conclusion

The topic of corporate governance has attracted a lot of attention and has become a subject of enormous debates in the recent years. Corporate scandals and collapses taking place in most countries have prompted regulatory reforms in all national governance systems. The issues of corporate governance are complex and deeply embedded in specific historical conditions and economic and political circumstances. Corporate governance researchers and professionals all agree that there is no one best way to design a governance system. In the modern world, an emerging perspective on corporate governance goes beyond the conventional emphasis on financial aspects of corporate control and takes into account interests, constraints, actions, resources, and influences of all constituencies in the corporate governance system. This entry has attempted to present some of the key building blocks, major perspectives, and the most recent developments and challenges of corporate governance.

—Ljiljana Erakovic

See also Agency, Theory of; Chicago School of Economics; Chief Executive Officer (CEO); Fiduciary Duty; *Keiretsu*; Minority Shareholders; Property and Property Rights; Sarbanes-Oxley Act of 2002; Shareholder Model of Corporate Governance; Shareholders; Shareholder Wealth Maximization; Stakeholder Theory

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Corporate Issues Management

Corporate issues management is the internal process by which a firm attempts to assess potential and future threats from unfolding events, situations, and interactions that either arise from organizational actions and past history or are externally driven. Issues that arise externally can be a result of nongovernmental organizations' activities; from events outside the organization's control, as a result of legislation and regulation; and as a consequence of changing societal mores. Issues management is the long-range planning tool of the corporation (and its public affairs department) to assess potential areas of concern and prepare the organization to lead the issue development or to respond in a reactive manner to the issue that is led by others.

What Is an Issue?

Some have defined an issue as any major environmental trend and possible events that might have a significant impact on the firm. There are other definitions that use "impact" as a way to define issues. But this is insufficient to define an issue in a manner that any organization can act on it. Others tie in the notion of impact with the timing of the issues likely to emerge as shown in Figure 1 (the comments in parentheses are examples of types of issues that could appear or have appeared in the quadrant). The argument is that issues with a high impact on the organization and with a high likelihood of actually occurring are dangerous and should be attended to with great care. Issues of medium impact and moderate likelihood should be monitored for developments, and issues of low impact and low likelihood, while not ignored, should be watched for future developments. This is the most simplistic view of issues but has appeal, as it is a visual way of capturing the complex interactions that occur. Issues are not simple—consider genetically modified organisms. What is the issue here? Is it a trade issue and as such should be resolved by the rules of international trade? Or is it a public health issue and therefore resolvable in regulatory and legislative hearings? Or is it an issue of prevention of starvation of large segments of society?

A crisis is not an issue, but it can be a trigger for an issue to emerge after the crisis is resolved in some manner. Consider the explosion of a Union Carbide plant in Bhopal, India; the sudden collapse of Enron; or the enormous oil spill of the *Exxon Valdez* in Valdez Alaska. All these events occurred with blinding speed; engaged and affected large segments of society; and

	Likelihood of Issue Emerging/Occurring		
Impact	**High**	**Medium**	**Low**
High	Dangerous (terrorism)	Concern	Closely monitor (increasing trade barriers)
Medium	Potentially dangerous (energy shortages, data security)	Monitor (immigration reform)	Occasional monitoring
Low	Monitor (rising energy costs)	Occasional monitoring	Infrequent monitoring

Figure 1 Severity and Likelihood of Occurrence of Various Corporate Issues

demanded immediate responses to limit further damage to the environment, human life, and investors. Issues do not always emerge with such speed and/or breadth of impact. But as noted, the explosion in Bhopal led to interest in legislative measures in plant safety worldwide—and that was an issue for the chemical industry to deal with as a whole. In a similar fashion, the collapse of Enron led to new legislation for the regulation of accounting and reporting and continued interest in corporate governance that goes far beyond the accounting industry. Finally, the oil spill in Alaska led to increased interest in tanker safety and in how organizations respond to such crises.

It should become readily apparent that an "issue" is not what it always appears to be and that part of understanding issues is to be aware of the complexities and dynamics involved in defining what the issue is and how other players (stakeholders) will attempt to define an issue and place it on a specific agenda for resolution.

Another way of looking at issues is to consider them as a disagreement between one or more parties over facts (what is), values (what is or ought to be), and/or policies (how shall we deal with the problems raised by the issue). Note that policies can be developed even if there is no agreement on facts and/or on values. Further building on this theme, one can argue that an issue can be seen as a conflict between one or more actors over procedure (how will decisions to pursue a solution and its implementation be undertaken) or substantive matters relating to the distribution of positions or resources. The controversy approach implies contestability among key stakeholders of the organization as a key dimension of change that underlies an organization (or corporate) issue.

A final approach to defining an issue is to consider an issue as an expectational gap between society's (or a key stakeholder's) expectation of social conditions or what the organization should be doing and the actual behavior of the organization. If we put these three approaches together, we get a complicated but useful definition of an issue. A *corporate issue* is a controversial inconsistency based on one or more expectational gaps involving management perceptions of changing legitimacy and other stakeholder perceptions of changing cost/benefit positions that occur within or between views of what is and/or what ought to be corporate performance or stakeholder perceptions of corporate performance and imply an actual or anticipated resolution that creates significant, identifiable present or future impact on the organization. This is a long definition, but it captures the dynamics and complexities of unfolding corporate issues.

Techniques for Dealing With Issues

Issues seek an arena for resolution—that is, when an issue arises the organization and the stakeholders involved seek to have the issue "resolved" in a specific arena. The legislature, the judiciary, and the regulatory agency are examples of specific arenas. Please note that organizations (and stakeholders) seek to choose an arena in which they have an advantage over other actors. However, the first approach to dealing with an issue is to prevent it from achieving visibility and building momentum. If an issue can be blocked, diverted, and postponed such that it does not require action, then the organization does not have to expend resources and attention on the issue. One technique for doing this is to refuse to recognize that an issue exists. This has been used by many in arguing against global warming. The argument is simple—this is not a problem and it does not deserve our attention. Another approach is to argue that the issue or problem is an isolated event and not worth the effort to develop policy to deal with it. Initial arguments on AIDS indicated that it was isolated to a limited few and not worth further effort (and clearly this was wrong). Finally, an organization can refuse to recognize the groups or stakeholders attempting to advance the issue or problem for resolution. This is a favorite tactic of governments, to deny groups (e.g., civil rights groups, environmental groups) access and ignore them. Note how these techniques are linked—they involve nonconfrontation with those advancing the issue. The media plays an enormously important role in raising the visibility of an issue. If an issue has villains, visuals, and victims, it stands a very good chance of being picked up by the media and becoming more visible.

No matter how good an organization is, it cannot prevent an issue from arising and gaining attention and adherents. This process occurs via what some have called naming, blaming, and claiming. An issue gains visibility when it is named and causes separation between actors in the process of resolution. For example, is world trade an economic issue of global trade or is it an issue of imperialism and discrimination against Third World countries? Note that how an issue is named has powerful consequences on how the issue unfolds and "who" is for or against the issue.

Once an issue is named, then blaming can occur—whose fault is this? Blaming is about assigning responsibility for the consequences/effects of the issue. Blaming also provides strong suggestions about where (arena) the issue will be resolved. Is mad cow disease a problem of governmental oversight of the beef industry or the result of unscrupulous farmers? If it is a problem of government oversight, the arena for resolution might be a legislature or a regulatory hearing. If it is unscrupulous farmers, then lawsuits might be the preferred arena choice. After blaming, claiming occurs. This is where specific claims are made on the organization responsible for the issue/problem.

If an organization fails to contain an issue, it emerges and gains visibility. The approach here would be to select an arena where the organization might have an advantage. This would require the organization to frame the issue (name and blame) in such a manner that the issue would go, say, to a legislative solution instead of a legal battle.

If others dictate the arena in which an issue might be resolved then the organization can pursue other techniques. At this point, the organization needs to decide if it wants to attack the group advocating the issue or attack the issue itself. Actions here involve questioning the legitimacy of opposing groups (attack their credibility, their skills, their knowledge, their history, etc.) or attacking the issue directly—for example, this is an issue, but it is too complex for resolution and understanding by nonexperts (global warming is an example here as is nuclear power). A final approach is to raise the fears of the general public and divert attention to other issues away from the specific issues being addressed (e.g., raise issues of terrorism, homeland security).

If these approaches and techniques fail, then the organization can recognize the existence of the problem and undertake actions that can be seen as coping with the issue. Arguments center around mutual interests, cost-benefits (costs exceed benefits), setting up committees, co-opting the leadership of opposing parties by bringing them inside the focal organization (e.g., appointing them to committees), postponing action (would like to but can't for a variety of reasons), and pointing out the past accomplishments/successes of the organization.

A careful reading of the techniques discussed thus far would demonstrate that they increase in cost and effort to the organization. Clearly, if an issue can be denied access and does not arise, the amount of time, effort, and resources involved can be minimal. Once an issue achieves a threshold of visibility, the cost and effort dynamics change. As the issue continues to grow, building adherents and opponents and entering a specific arena, even more costs and effort is involved in dealing with the issue.

Issues Linked to Stakeholders

Issues management is about identifying issues of import to the organization and prioritizing them. Once the issues are prioritized, then policy development occurs. Policy development is where the organization decides what exactly its position is on a given issue (and what arena an issue should be placed in). Only after policy development can an organization (normally its public affairs department) engage in public advocacy on the issue. Organizations are very adept at identifying and prioritizing issues but lose precious time and advantage in delays associated with policy development. Organizations frequently find themselves in a reactive mode because an issue that was identified and properly prioritized emerges faster than planned and led by others. Why? Because the organization is unable to develop its own internal position on the issue in a reasonable timeframe.

Issues are, as noted, a long-range planning tool and process for organizations, but issues do not exist in isolation. Organizations do not "manage issues," they plan for issues, much like a coach plans for an athletic contest. But nothing happens without the other players—generally termed stakeholders. Superlative corporate issues management not only identifies and prioritizes issues but also clearly identifies likely stakeholders, their positions on the issue, and their likely level of involvement and then suggests courses of action the organization can take.

Once an issue achieves some threshold of visibility, actors (stakeholders) take positions on issues. These positions may represent interests that they have in the issue and its resolution. Other stakeholders may have no interest whatsoever in the issue and its resolution—they are kibitzers or commentators. Their "stake" in the issue is one of being asked to comment on the issue, to offer suggestions for the issue, to assess proposed solutions, and the like. Simply put, these stakeholders are not substantive ones but on the fringes of the issue. There are also zealots that surround issues—zealots are those individuals and groups that have the *one and only* *solution to the issue.* They are quite willing to destroy the organization in the process of seeking a resolution and will not compromise. Finally, there are stakeholders who get involved in an issue because of prior commitments. These stakeholders may "owe" other stakeholders involved with the issue and get involved to pay a debt or a commitment made, but their degree of commitment to a resolution is modest at best.

The challenge for any organization is to clearly identify the substantive stakeholders from the kibitzers, the zealots, and those stakeholders who are involved because of prior commitments. Stakeholders form alliances and a first-rate organization recognizes the potential patterns in those alliances and moves to prevent the most threatening ones from ever forming around the issue of interest. In short, not all stakeholders are equal nor are they all interested in the resolution of the issue. This is where the techniques for dealing with issues come into clear relief. The process of issue identification, specific tactics, arena selection all can impact on stakeholders and their continued involvement in the issue. Issues management well executed can (1) prevent an issue from emerging, (2) place the issue in an arena of the organization's choosing, (3) prevent or discourage selected stakeholders from engaging on the issue, and/or (4) prevent threatening stakeholder alliances on a given issue from ever forming.

Issues management is a sophisticated, ever-evolving organizational skill to deal with complex problems and can be used by private organizations, nongovernmental organizations, and governments.

—John F. Mahon

See also Corporate Citizenship; Corporate Political Advocacy; Corporate Public Affairs; Corporate Social Responsibility (CSR) and Corporate Social Performance (CSP)

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CORPORATE MORAL AGENCY

Insofar as they are capable of exhibiting intentional action, corporations may be regarded as moral agents. Agents reflectively endorse specific ends and shape the world by imposing those ends on the world. Because agents have this sort of intentional capacity, they are properly characterized as responsible for the actions they impose on the world. Persons are prototypical examples of agents and the class of persons is properly understood as subset of the class of moral agents. In U.S. law, the class "persons" includes entities other than human beings such as corporations. The courts attribute personhood to corporations on pragmatic grounds, finding this a useful convention for the purposes of corporate law. The question of whether or not there are grounds for thinking that, from a metaphysical standpoint, corporations are properly understood as moral agents is a separate matter.

French's View

A quarter-century ago, Peter French published an influential essay on the metaphysical status of the corporation. He has subsequently defended the core of that view in a series of books and essays. Despite its many critics, French's theory of corporate personhood remains the single most influential account of the metaphysical status of corporations. Corporations, as French noted, are of particular interest in comparison to other sorts of collectives or organizations because of their distinct rules of governance and hierarchical structure. In his early work on the metaphysical status of corporations, French reached three main conclusions. First, corporations exhibit intentionality. Second, corporations are capable of exhibiting rationality regarding their intentions. Third, corporations are capable of altering their intentions and patterns of behavior. As a result, he concluded that corporations are full-fledged moral persons and have the privileges, rights, and duties that are, in the normal course of affairs, accorded to moral persons. This claim received sustained criticism over the years. In particular, critics have argued that French's position is illegitimately anthropomorphic. For example, Richard De George has argued that, unlike human beings, corporations are not ends in themselves. Other critics have argued that it is absurd to suggest that corporate persons have the same emotional status as human persons. Still others have argued that corporations cannot be persons, since all persons have a soul and no corporation has a soul.

Intentionality

In his early defense of corporate personhood, French grounded his arguments in the belief-desire theory of intentionality. He argued that when the corporate act is consistent with an instantiation of established corporate policy, then it is proper to describe it as having been done by a corporate desire coupled with a corporate belief and so as a corporate intention. Critics seized on French's use of the belief-desire theory, arguing that, since he wrongly attributed distinctly human intentionality to corporations, his defense or corporate intentionality failed. For example, Manuel Velasquez argues that all attributions of intentions to corporations must be understood as metaphorical since they are not literal mental states. He denies the possibility of such an argument because he stipulates that intentions must be understood as mental states identical to those present in individual human minds. However, this is not the only way of understanding intentionality. One alternative way of understanding intentions is as commitments to future action. Such a characterization of intentions leaves open the possibility that entities other than conscious biological beings may be properly understood as intentional.

Central to the claim that corporations are moral agents is the claim that corporations have intentions. Prosecutors and judges routinely attribute intentionality to corporations. Nonetheless, the attribution of intentions to corporations has been rejected by many theorists as an untenable hypothesis. Partly in response to such criticism, French has modified his view of the metaphysical status of the corporation in two significant ways. First, French has abandoned the idea of corporate "persons" in favor of a defense of corporate "actors" or agents. This move allows French to avoid the criticism that his view is illegitimately anthropomorphic. Second, French now rejects the belief-desire theory of intentionality that he had previously embraced in favor of Michael Bratman's planning theory of intentionality. This allows him to avoid criticisms associated with the belief-desire theory of intentions.

Corporate Intentions

Bratman's account of intentions emphasizes their future-directed nature. On his account, intentions are typically elements of plans. Bratman argues that as rational agents with complex goals most of our intentional actions will stem from deliberation and reflection prior to the time of action, that is, from planning. The plans characteristic of human agents have two essential features. First, plans are typically partial or incomplete. They need to be filled in over time. Second, plans typically have a hierarchical structure. Bratman has extended his analysis of the intentions of individuals to shared intentions of a certain type—namely, the intentions shared by two individuals who plan to engage in a joint activity. Consider two individuals who plan to take a trip together. What roles do their shared intention to take a trip together play? First, their shared intention allows for the coordination of planning. Second, their shared intentions structure relevant bargaining. Third, their shared intentions allow for the coordination of activities. On this account, shared intention is a state of affairs that consists of a web of attitudes of the individual participants. Shared intentions are not, then, mere mental states.

French has suggested that Bratman's account of intentionality will provide an adequate basis for a theory of corporate intentionality, yet French has not developed a sustained argument for that conclusion. However, Bratman's analysis of shared intentions has recently been extended to corporations by Denis Arnold. He argues that the state of affairs characteristic of shared intentions is also characteristic of corporations. Typically, corporate decisions are made in accordance with the structure previously characterized by French as a corporate internal decision (CID) structure. This well-known and essential feature of French's account of corporate moral agency includes hierarchical lines of organizational responsibility, rules of procedure, and corporate policies. A CID structure performs a normative function, that is, it tells members of the corporation how they ought to behave. When employees act in a manner consistent with the CID structure they instantiate corporate intentions. Corporate intentions are states of affairs consisting of both the intersecting attitudes of the class of agents comprising the corporation and the internal decision structure of the organization. The CID structure serves as the frame on which the attitudes of board members, executives, managers, and employees are interwoven to form corporate intentions.

Praiseworthy corporate intentions include value creation, the development of innovative technology, and respectful regard for stakeholders. Blameworthy corporate intentions include deceptive marketing, systematic dumping of toxic chemicals into pristine natural environments, and theft from shareholders.

Arnold argues that since corporations are properly understood to have intentions, there is a basis for thinking that corporations are properly understood as agents. However, he points out that for corporations to be properly regarded as moral agents, a further condition must also be satisfied. Corporations must be capable of reflectively endorsing corporate intentions. Corporations that are capable of evaluating past decisions and existing plans, of determining whether those intentions ought to remain in place, or whether they should be modified or eliminated in favor of alternative intentions are capable of the requisite reflective endorsement and are properly understood as moral agents.

Conclusion

The idea that corporations are properly understood as moral agents remains unpersuasive to many theorists. First, some critics maintain that all agents must be understood as having souls. Since it is implausible to attribute a soul to a corporation, some theorists conclude that corporations cannot be understood as agents. Second, the idea that corporations are capable of reflectively endorsing intentions strikes some theorists as implausible. They argue that reflective endorsement is a quality of human persons and one that cannot reasonably be attributed to organizations.

Defenders of the view that corporations are properly understood as moral agents point out that this view has important implications regarding moral responsibility. For example, if a corporation is properly understood as a moral agent, then it is possible to praise or blame corporations and not just the directors, executives, managers, and workers of a corporation at a particular time. Punishment of the corporation, and not just corporate personnel, is thereby justified when corporate intentions are morally objectionable. In cases where corporation actions are especially pernicious as a result of corporate intentions, corporate capital punishment in the form of the dissolution of the corporation may be justified. So too, corporations that exhibit consistently praiseworthy behavior as a result of corporate intentions are justifiably rewarded independently of corporate personnel.

—Denis G. Arnold

See also Autonomy; Free Will; Moral Agency; Moral Standing

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Corporate Philanthropy

Corporate philanthropy is the practice by companies of giving charitable donations to a wide range of societal institutions, especially nonprofit or nongovernmental organizations (NGOs), including social service agencies, environmental groups, housing and poverty agencies, schools and universities, hospitals, and other organizations, whose goals are to benefit society in some way. Sometimes termed *corporate social investment*, *corporate philanthropy* can be considered part of companies' overall approach to corporate community relations and to the somewhat broader concept of corporate social responsibility (CSR). CSR is defined as the direct attempt by companies to contribute to the betterment of society. CSR with its elements of philanthropy is part of the larger picture of companies' corporate citizenship, which is defined as the ways in which a company's strategies and practices, that is, the business model, affect its stakeholders, society, and the natural environment.

Corporate philanthropy takes a number of forms including direct monetary donations and grants to not-for-profit organizations; in-kind donations, such as product and service donations; employee volunteer programs; technical support; and the deployment of skilled managers into social enterprises on a volunteer or advisory basis, including sometimes as members of boards of directors of nonprofit organizations. In the most progressive firms, managers and sometimes employees are evaluated partially on their contribution to the community, which is seen as an important element of a company's philanthropic endeavors. In addition, multisector or public-private collaborations are frequently considered to be part of a company's philanthropic program or CSR. These types of contribution will be discussed in more detail below.

Companies in the United States are estimated by associations such as the Conference Board and the American Association of Fundraising Counsel to give between 0.7% and 1.3% of pretax profits in philanthropic contributions, according to Business for Social Responsibility. The American Association of Fundraising Counsel estimates that about 5% or about $13.5 billion of the total amount of charitable gifts of nearly $251 billion in the United States in 2000 was donated by corporations. The use of corporate philanthropy is most prevalent in the United States, where the practice began, though multinational corporations from other nations are increasingly developing giving programs as well. Some NGOs are skeptical of strategic philanthropy programs because they believe that there should be an intrinsic value to philanthropy that is diminished when the company benefits and because only those interests that benefit the corporation will receive philanthropy; however, there is also evidence that strategic philanthropy approaches are becoming increasingly popular.

Rationales for Corporate Philanthropy

There are numerous reasons why companies engage in philanthropy. Some of them have to do with improving their relationships with important stakeholders such as employees and customers. In surveys, many employees claim that they will make decisions about employment partially on the basis of a company's reputation for CSR. Similarly, some customers claim that, assuming quality and price are comparable, they will take a company's reputation for corporate responsibility, of which philanthropy and community relations is an important aspect, into account in their purchasing decision.

A survey by the Center for Corporate Citizenship at Boston College and the Points of Light Foundation found in 2003 that 52% of companies incorporate a commitment to their local communities into their mission statements. Thus, in some respects corporate philanthropy serves as a public relations vehicle for improving a company's image and, more important, its reputation with important stakeholders, though other uses are more strategic. Companies, of course, also hope that their philanthropy will engender greater loyalty from stakeholders, leading to reduced employee turnover and greater retention and repeat purchases on the part of customers.

In the early days of corporate philanthropy, much of the giving centered on societal issues and organizations that drew the attention and interest of the chief executive officer. By the early 2000s, most large companies had moved beyond giving donations simply on the basis of the chief executive's and other top managers' interests toward more structured programs of giving, some of which can be characterized as strategic philanthropy, in which donations are directly linked to business goals. Of course, one important reason for corporate philanthropy's existence is that of altruism, a desire on the part of company executives to do explicit good for society, which can be characterized as a normative or ethics-based rationale. The second major rationale for philanthropy is called enlightened self-interest and argues that there is a business case to be made for companies giving away money in ways intended to do social good. While there is a trend toward more strategic giving, which will be discussed below in more detail, usually both motives are embedded in philanthropy programs.

Companies that attempt to use philanthropy simply as a public relations activity rather than actually improving on their actual stakeholder-related practices subject themselves to criticism. Such companies are attempting to create a good public image for the firm just by giving corporate donations. The criticism focuses on the fact that philanthropy alone cannot make up for bad practices elsewhere in the firm. Still others, particularly people coming from the perspective of neoclassical economics, criticize corporate philanthropy as giving away shareholders money and suggest that only individuals should be allowed to give money away. The courts, however, have agreed with the philanthropists that companies can engage in corporate philanthropy as part of their practice of good corporate citizenship.

Methods of Corporate Philanthropy

Companies direct their giving efforts in a number of ways. These methods include direct grants, gifts, and donations; cause-related marketing; in-kind donations; community investment and economic development activities; and volunteerism, which are discussed in the sections below.

Grants, Gifts, and Donations

Many companies have direct giving programs to which charitable organizations or NGO can apply directly for grants, which can range from very small to quite substantial amounts of money. Most of these grants go to the nearly 800,000 nonprofit organizations estimated to be in the United States, as well as to other socially beneficial programs around the world. The U.S.-based Foundation Center estimates that corporate foundation giving decreased by about 2% in 2003, following a significant gain in 2002, which was partially attributable to giving related to the terrorist attack on New York's World Trade Centers in 2001. Some of the decline is attributable to declines in the stock market. The overall amount of corporate cash donations is generally relatively stable though was decreasing somewhat during the early 2000s, with other kinds of corporate philanthropy assuming a bigger proportion of giving. Processes for nongovernmental or nonprofit organizations receiving grants from companies or their foundations range from quite informal, for example, the submission of a letter explaining the purposes to which the grant will be put, to formalized application processes with extensive internal review and monitoring of outcomes and results.

Cause-Related Marketing

Cause-related marketing, which falls between philanthropy and marketing, occurs when a company links the level of sales or use of its products or services to donations to specific charities, often those whose interests are aligned with those of the company. Pioneered by American Express in the 1980s, when use of the company's credit card was tied to charitable donations, cause-related or cause marketing has become quite common. Types of cause marketing include corporate sponsorships of events, partnerships with NGOs for specific fundraising purposes for the NGO, and campaigns aimed at developing new business for the company while the NGO receives funding.

In-Kind Donations

Many companies provide in-kind donations, that is, donations of their particular products or services, to NGOs as part of their philanthropy programs. Such donations are termed *noncash* donations by the U.S.-based Conference Board and can include products manufactured by the firm; the donation of services for which customers usually pay; technical support that can be offered as a result of a company's expertise; and sometimes recycling and reuse of outdated equipment, which is given to NGOs. Loaned executives or other employees who use their skills to help NGOs by working for them part of the time—for instance, helping with strategic planning or day-to-day operations; making organizational changes; or improving operations, marketing, accounting, finance, or other functions—can also be considered as performing a type of in-kind giving. In-kind donations are estimated by the Conference Board to be on the order of 25% of total contributions, as measured through tax valuation or fair market value. Because companies draw resources from society, many people in society expect that the company will be involved in helping communities and society more generally to thrive, hence the growth in in-kind and charitable contributions.

Community Investment and Economic Development Activities

Some companies' managers believe that it is important to help the communities in which they have operations to thrive for a number of important reasons and do so through their community relations programs using community investment strategies. One reason is to build local communities that are healthy, have good amenities such as arts and culture, and good educational programs so that employees will want to live in those communities. Many companies donate to local schools and youth organizations because they recognize that having a well-educated workforce in the future will be critical to their long-term success. In addition, local communities provide much of the infrastructure, including telecommunications, sewers, roads, and public services of all sorts, on which companies' facilities rely, and establishing good relationships with local community officials, often done through the charitable donations to local service agencies and NGOs, helps ensure their success. Corporate philanthropy is directed at a number of types of causes, including local arts and cultural organizations, schools and universities, community development and housing programs, mentoring and job training programs for youth, children's organizations, environmental organizations, sports leagues and events, local economic development including both inner city and rural.

Community investment is an important form of philanthropy for many companies, although it can generate free rider problems when one company contributes and others simply benefit from the community improvements derived from those contributions. Typically run through the community relations program, community investment focuses on assuring the sustainability of local communities where a company has operations and is frequently most focused on the locale where the company is headquartered. A number of the donation strategies listed above are used to implement community investment locally. In addition, when some company leaders become actively involved in local civic and political life, the community relations program can invest in local businesses or create local investment opportunities and source at least some supplies locally to support the community. Sometimes corporate facilities are used for local events. Managers and other employees can sometimes get release time—paid time away from work—to volunteer in community-based organizations, participate in civic events and policy dialogues, and otherwise engage in activities that support a thriving community.

Volunteerism

Another aspect of corporate philanthropy is company support of employee volunteerism. Again, as with other forms of philanthropy, volunteering is more popular in the United States than in the other parts of the world, though it is increasing globally. Some companies encourage their employees to volunteer and some even provide paid leave for volunteer activities in the recognition that local communities will benefit directly from employee volunteer time and the company itself may well benefit indirectly. Some companies recognize employees who volunteer on their own time through awards ceremonies and publicity about their activities; others provide matching grants for volunteer services.

Some companies' leaders believe that there are direct and indirect benefits to the firm when employees volunteer. For example, when employee volunteers work in teams at a nonprofit organization, they can gain useful team-based skills that translate back to their work situations. In addition, employee volunteers make local connections with community and civic organizations and their leaders, providing better links between the company and its community-based stakeholders. Occasionally, companies find that good business data, new contacts, and even new markets can evolve from information and new insights brought back by employees from volunteer experiences. Thus, some of the benefits to the company and employees from volunteering can be enhanced skills, leadership opportunities that might not happen within the work setting, and better teamwork, particularly when teams of employees volunteer together. Business for Social Responsibility suggests that other benefits may also inspire volunteer programs, for example, the ability to develop a local labor pool, improve the company's reputation with the community, create connections that help communities when there is a crisis or problem, and leverage other philanthropic resources better. Companies that have volunteer programs, in turn, may find it easier to recruit employees because they find the company to be a better employer, easier to create satisfying relationships with local officials in the community, and easier to work with public officials when the company needs new infrastructure or community support for a new facility.

Multisector Collaboration/ Social Partnerships

In addition to giving away money, products and services, and employee time, some companies find that their corporate philanthropy involves establishing ongoing partnerships or collaborations with NGOs, including schools, local social service and health agencies, and sometimes governmental organizations. Partnerships and collaborations can involve monetary donations, but they are more interactive, in that they also require ongoing involvement in whatever the focal activity of the partnership is. For example, many companies become involved in partnerships to improve local schools in communities where they have facilities because they recognize the importance, on a long-term basis, of a well-educated and highly skilled workforce. Other companies become involved in collaborative efforts to improve the community through community development activities that can include improved housing, better community policing and safety standards, and the creation of economic opportunity through improving access to local jobs and higher education for all.

Strategic Philanthropy

Companies increasingly view their philanthropy activities through a strategic lens, in what has come to be called strategic philanthropy, although some observers are skeptical about how strategic much philanthropy actually is. In strategic philanthropy, the company attempts to link its own mission, or particular products and services, with the charitable activities it funds, so that the society, through the social mission of the NGO, and the business benefit simultaneously.

In developing a strategic philanthropy program, a company takes into account its own strategic objectives, the interests of its stakeholders, the issue area in which it wants to make contributions, and what the company and the NGO with whom it will link do best—that is, what are both organizations' core competences. When there is alignment between the missions of the two organizations, then philanthropic activities can be considered strategic in nature. For example, a sports equipment or gear manufacturer might associate some of its philanthropy with sporting events, perhaps aimed at youth, the disadvantaged, or people with disabilities, so that the company generates goodwill with a specific target market potentially interested in the use of its products. These events carry the company's name and have the potential to enhance its image and reputation with a group of actual or potential customers.

Harvard Business School economist Michael Porter suggests that corporate philanthropy can actually be strategic when it is somehow used to improve the competitive context—that is, the quality of the business environment where businesses operate. By improving local education, providing individuals with training in skills that the company needs, or improving the community in significant ways, the company can actually reap long-term benefits. Porter identifies four elements of the competitive context that can be enhanced by strategic philanthropy. One element is the availability of high-quality, specialized inputs, such as human and capital resources, physical and administrative infrastructure, scientific and technological infrastructure, and natural resources. A second aspect of the competitive context is the status of local policies and incentives that either help or hinder businesses and vigorous local competition. A third element is the presence of sophisticated and demanding customers, who create specialized local demand that also reaches far beyond the community. The fourth aspect is strong local suppliers and related companies clustered within a given region or community. Porter advises investment in strengthening these aspects of the environment through strategic donations to key organizations within the community that can help strengthen these elements.

Corporate Philanthropy Programs

Philanthropy programs in companies can take three general forms, although numerous variations of these are possible. The least formalized programs simply allocate some money for donations, often based on the charitable interests of the chief executive officer. Most large U.S. companies today, however, have gone beyond such informal programs and established formally structured giving programs. Within the corporation, these programs are typically housed within the corporate community relations department, the public affairs unit, or in a similar function within the company. Alternatively, they are sometimes set up as separate corporate foundations, which receive money from the corporation or its founder but are managed independently of the firm.

Corporate philanthropy is more prevalent in the United States than in other parts of the world, because there is a long history of individual philanthropy in the United States that has translated to corporations. Most large corporations have some sort of giving program established; however, the tendency seems to be to allocate most of the giving domestically with smaller proportions going to international divisions. Among the major targets of overall philanthropy at about $251 billion in 2003, according to the Giving USA Foundation, are educational organizations (about 13% of total giving); religious institutions (about 36%); foundations (about 9%); international affairs (about 2%); environment and animals (about 3%); public-society benefits (about 5%); arts, culture, and humanities (about 5%); human services (about 8%); and health (about 9%), with the rest unallocated.

In 2003, *BusinessWeek* published its first annual ranking of the most philanthropic companies in the United States, citing retail giant Wal-Mart stores as the most philanthropic company in its study for donating $156 million in cash, although the company did not make the top 10 in terms of contributions compared with total sales. The company topping the list in terms of both cash and in-kind gifts compared with total sales was Freeport-McMorRan Copper & Gold at 0.879% of sales, followed by Corning at 0.787%, and Computer Associates at 0.640% of sales. Critics sometimes charge that companies give away money to burnish their images through what is called greenwashing, that is, trying to look environmentally or socially friendly when they actually are not. Others, however, believe that there are both sound business reasons and altruism for companies working directly to improve society. Despite the conflicts, what is clear is that many companies do give substantial amounts of money, products and services, employee time, management assistance through collaborations of various sorts, and other forms of giving.

—Sandra Waddock

See also Corporate Citizenship; Corporate Social Responsibility (CSR) and Corporate Social Performance (CSP); Strategic Corporate Social Responsibility; Strategic Planning; Trust

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Corporate Political Advocacy

Corporate political advocacy addresses a firm's participation in the formulation of public policy at various levels of government. As the regulatory environment has become more intense and complex and as other changes have taken place in society, firms have had little choice but to become more politically active. Attempts by firms to influence government are a major and accepted part of the public policy process in the United States. The U.S. political system is driven by the fervent participation of interest groups striving to achieve their own objectives. The business sector is, therefore, behaving in a normal and expected fashion when it assumes an advocacy role for its interests. As decisions about the current and future shape of society and the role of the private sector shift from the marketplace to the political arena, firms, like all interest groups, find it imperative to increase their level of political advocacy.

Historically, firms engaged in vigorous debates in Washington, D.C., only on an issue-by-issue basis and with no overall sense of a purpose, goal, or strategy. Also, firms tended to be reactive; that is, they dealt with issues only after the issues had become threats. Today, success in Washington is just as important as success in the marketplace. Just as business has learned that it must develop competitive strategies if it is to succeed, it has learned that political strategies are essential as well. The firm engages in this activity by using techniques such as having a political strategy, lobbying, political action committees, and coalition building through organizations to influence rules, regulations, and laws enacted by government that affects its environment. One of the things that the firm has to manage in its environment is the government's actions and its effect on the market. The U.S. government abides by a stringent privatization model for the business market. The government frowns on owning and operating businesses in the United States. Instead, it monitors the firm's activities in the market to ensure that on balance efficiency and fairness are practiced throughout. The government, through its complex rule-making process, attempts to ensure that the market is fair, a firm does not have an unfair advantage, and the resources in the environment are not abused. At any point in time, the government can veer the market's direction by using controls that impact the business and consumers. Over the past 100 years, firms have been very successful in acquiring a coveted status in the market similar to that of a person. Today, firms are beheld as a legal "fictitious person" and are afforded the same rights, privileges, and protections as individuals. Thus, firms are able to use constitutional safeguards identical to what individuals exercise when their rights are abridged. More specifically, numerous clauses in the constitution including the First, Fourth, Fifth, and Fourteenth Amendments grant enormous rights to firms against government actions. With the advent of these new rights, firms have taken the liberty of using its influence to affect the actions implemented by government.

Under Articles 1, 2, and 3, the government may delegate some of its duties for rule making, enforcing rules, and interpreting the laws to the legislative, executive, and judicial branches. Accordingly, the legislative branch has established federal agencies to monitor the activities taking place in the market. Some of these agencies report directly to the executive branch while others are independent from both the legislative and executive branches. Some examples of executive branch agencies are the Department of Commerce, the Department of Agriculture, and the Department of Transportation. These agencies report directly to the president of the United States. Conversely, independent administrative agencies operate on an autonomous basis from the president. Examples of these agencies include the Federal Trade Commission, the Federal Communications Commission, and the Securities and Exchange Commission. Executive branch agencies function under a concerted policy orchestrated by the president of the United States. These branches venture to provide a certain type of structured environment for firms to operate in. Each branch has a specific role in the process of establishing policy for the government.

The legislative and executive branches of government are easier for firms to influence. There are specific parts of the rule-making process that afford firms the ability to intercede and influence the policy before it is developed. Conversely, it is more arduous for the firm to influence the judicial process because most federal judges are appointed for life, although some federal judges, who are appointed by the president, serve for a limited term in office. Federal judges who are appointed to preside on the tax court, bankruptcy court, or international trade commission serve for limited terms. However, they can be subsequently reappointed to successive terms. So the vast majority of a firm's resources are headed for the political advocacy arena and used to influence the legislative and executive rule-making process.

Special interest politics have become a way in which most legislation is passed in the United States. Subsequently, most firms have come to recognize that to endure it one must be an active and effective player in the process. One telling example of not being involved in the process demonstrates what can happen to firms that take an isolationist policy toward the rule-making process. Microsoft used a superficial presence in Washington, D.C., prior to the Justice Department bringing an antitrust case against it for monopolistic competition. Before the suit was brought, Microsoft used one lobbyist and its office was in the Microsoft federal sales office. The lobbyist had no secretary and no relevant lobbying experience in Washington. Microsoft had no real savvy in understanding how the lobbying system worked in Washington. Microsoft transposed its isolationist strategy for political advocacy as a result of being sued by the Justice Department. Microsoft began to increase its level of political giving to both parties. It retained an impressive cadre of well-connected lobbyists and public relations officials to adduce its case to legislators and the public. The in-house staff swelled from one person to 14, and it used a multitude of high-powered help on retainer.

Microsoft contributed millions to both political parties in the 2000 presidential election, hired both Bush and Gore advisers as lobbyists, and became the ninth largest "soft money" corporate donor in the United States. Microsoft ran a national ad campaign featuring a "warm and fuzzy" Bill Gates, while simultaneously touting the multimillion-dollar charity campaign contributions it made to various organizations. Think tanks that supported Microsoft interests received major donations; those that espoused views contrary to it were abdicated. Microsoft even hired almost entirely all the law firms in Washington, D.C., so that nearly all the lawyers in town would be unable to work for its competition. In 2004, after years of struggling with antitrust cases, both domestic and abroad, Microsoft situated one of its best lawyers to chair the American Bar Association's antitrust section, a group that has significant influence over the expatiation of antitrust policy and law.

Political Strategy

As illustrated from the example concerned with Microsoft, it is fatuous for a firm to engage in the political activism process without a sound strategy. The firm should have a goal of what it wants to accomplish and specific objectives for how it is going to get there. Befittingly, the impetus for developing a comprehensive strategy for engaging in the political process is to alter legislation. As firms devise and execute political strategies, it is useful to see their initiatives as factors in their development of stakeholder management capabilities. Unlike actual persons, corporations antithetic to actual persons cannot be imprisoned or suffer "capital punishment" by being forced out of business by the judicial system.

The firm has a multitude of objectives that it wants to pursue in developing a political strategy. First, it will attempt to limit the issue from taking a prominent position on the policy stage. Second, if the firm can't limit the initiative from moving into the limelight, it will attempt to define the public issue. Third, if the firm can't shape the issue, it will find a coalition to limit the impact on the industry. So the firm has to proceed in a manner that will yield the greatest results. The firm has to develop an approach to this process that allows it to engage the decision makers in a manner that focuses on outcomes. So the firm must determine how best to advocate its concern either for or against a proposed rule. The firm can influence the process at different stages and affect the ultimate policy that is created. Given the extreme nature of our competitive environment today, most firms find themselves working with other firms to develop a national agenda with a focus on a more progressive role in the public policy process. With so much pressure coming from foreign markets, firms are forced to band together to find workable solutions that benefit its industries. This mode does not require a recusant departure from traditional goals and strategies but is more biddable and adaptive to a changing political environment and structure.

Lobbying

The business community engages in lobbying at several different organizational levels. At the broadest level are umbrella organizations, which represent the collective business interests of the United States. The best examples of umbrella organizations are the Chamber of Commerce of the United States, the National Association of Manufacturers, State Chambers of Commerce, and City Chambers of Commerce. Out of these groups have grown organizations that represent some subset of business in general, such as the Business Roundtable, which was organized to represent the largest firms in America, and the National Federation of Independent Businesses, which represents smaller firms.

At the next level are trade associations, which are composed of many firms in a given industry or line of business. Examples include the National Automobile Dealers Association, the National Association of Home Builders, the National Association of Realtors, and the National Association of Medical Equipment Suppliers. Firms that are actively involved with an association do so by preference. They usually pay some type of member fee to be affiliated with the association. Also, they are in league with other firms that they compete directly against on a day-to-day basis.

Another tier of coalitions constructed to confront political issues are international associations. Examples of these organizations include the World Trade Organization, the International Chamber of Commerce, the International Fair Trade Association, and the United States Council on International Business (this is a U.S. group dealing with international business). These organizations work to provide a basis for firms to influence the foreign government's policy-making process.

Finally, there are the individual company's lobbying efforts. Here, firms such as IBM, BellSouth, Time Warner, Viacom, and Chase Manhattan Bank lobby on their own behalf. Typically, companies use their own personnel, establish lobbying offices for the sole purpose of lobbying, or hire professional lobbying firms or consultants located in Washington or a state capital. The business lobbyist plays a significant role in assisting firms in achieving their political strategy. The business lobbyist engages in the following activities for its clients including getting access to key legislators, monitoring legislation, establishing communication channels with regulatory bodies, protecting firms against surprise legislation, drafting legislation, communicating sentiments of association or company on key issues, influencing the outcome of legislation, assisting companies in coalition building around issues that various groups may have in common, helping members of Congress get reelected, and organizing grassroots efforts. Lobbyists also play the important role of showing busy legislators the virtues and pitfalls of complex legislation.

Political Action Committees

Political action committees (PACs) have been around for years, but their influence has been most profoundly felt in the past two decades. This is perhaps because the bottom line in politics, as well as in business, is often measured in terms of money—who has it, how much they have, and how much power they are able to bring to bear as a result. Business PACs appeared on the scene in the early 1970s as a direct result of the 1974 amendments to the Federal Election Campaign Act. Under this law, organizations of like-minded individuals formed together and created a PAC for the purpose of raising money and donating it to candidates for public office. Under the law, PACs may contribute $5,000 per candidate per election including primary, runoff, general, or special. There are no aggregate limits on how much a PAC may contribute to numerous candidates. The $5,000 limit is less restricting than that placed on individuals, who are limited to donating $2,000 per federal candidate per election.

At the start of 2004, 3,868 PACs were officially registered with the Federal Election Commission. This represents a decline from more than 4,000 PACs that were registered in 2001. Corporate PACs were the largest subgroup with 1,538 committees. In the 2000 elections, PAC contributions to the House and Senate totaled $200 million, with another $200 million going to national parties as well as candidates for local and state offices.

In addition, firms have used a loophole in the PAC legislation to donate what is called soft money directly to political parties instead of political candidates. The Bipartisan Campaign Reform Act (BCRA) of 2002 attempted to limit the use of soft money and curtail the use of certain political ads. BCRA bans national parties from raising and spending soft money. In addition, BCRA prohibits federal officeholders and candidates from raising soft money for political parties at the federal, state, and local levels and, likewise, from soliciting or raising soft money in connection with federal or nonfederal elections. Shortly after passage, certain special interest groups challenged the law's constitutionality in court. In May 2003, a federal court held the soft money ban to be unconstitutional and allowed political parties to raise soft money again while setting restrictions on the airing of issue ads. This was immediately appealed to the U.S. Supreme Court. On September 8, 2003, the Supreme Court upheld the soft money and issue ad restriction of the BCRA in a five to four ruling. This legislation did not stop firms from finding other mechanisms to pour soft money into political campaigns. Despite all efforts to limit the amount of soft money contributions, other strategies are being deployed to continue raising significant sums of capital for political campaigns. For instance, nonprofit organizations know as 527s are allowed to raise and spend soft money on campaigns. Some are concerned that these groups will be less accountable than the political parties were prior to the law's inception. In the 2004 elections, Democrats made particularly strong use of 527s to create a shadow Democratic Party that could circumvent campaign financing restrictions.

Yet another means by which firms are able to get around campaign financing reform is the act of bundling. Bundling is the collection of individual donations, with a limit of $2,000, that are then delivered in bulk to the candidate. Typically, a senior executive will host a fund-raising event and invite high-level employees to attend and donate up to the $2,000 threshold. Clearly, one unintended consequence of campaign financing reform has been to shift the burden for political contributions from firms to their employees. Furthermore, firms can abuse this legislation by discretely pressuring employees to support one particular political party or candidate and not another. These tactics undermine the integrity of the legislation and work to deteriorate the objective nature of the political process.

Coalition Building

Another technique that seems to be growing in popularity is the use of coalitions to influence the government process. A coalition is formed when distinct groups or parties realize they have something in common that might warrant joining forces to combat a specific issue. More often than not, an issue that various groups share similar views about something creates the opportunity for a coalition. In recent years, coalition formation has become a common practice for firms interested in achieving political goals or influencing public policy. The isolationist approach to confronting the political system is not as effective in today's business climate. If a firm or an association wants to pass or defeat specific legislation, it needs to mobilize the support of any firm that shares the same position on the issue. The greatest benefit to the firm in using coalitions is that they diversify the exposure and impact on the firm. Clearly, the petition resonates louder if many firms object or applaud the virtues of the legislation. Coalitions allow firms to spread limited resources in a more efficient manner. Firms can avoid overextending resources while trying to represent their interest. This allows them to fight or support the legislation on many different fronts. Coalitions allow the firms to be zealous about representing their interest while taking a lesser lead position in the process. Coalitions provide a very effective way for firms to gather support for their issues and protect the interest of the market at the same time. Coalitions allow firms to be involved without necessarily having their name attached to the issue. One high-profile example of coalition building around a specific issue is the Coalition for Economic Growth and American Jobs. Backers of this coalition included the U.S. Chamber of Commerce, the Business Roundtable, the American Bankers Association, the National Association of Manufacturers, and scores of other trade groups and individual companies. Recognizing that the issue of business outsourcing was evolving into a hot button for the 2004 election, they joined to fight the growing number of state and federal initiatives aimed at keeping jobs at home and restraining globalization.

Conclusion

Corporate political advocacy is an essential part of our system in the United States. Thus, lobbying, corporate political contributions, and coalition building will likely remain a permanent part of the political landscape in the United States. Unlike what firms considered involvement to be in the past, for the most part they are required to take an active role in the political process today. So firms should have a good idea of what their interests are and how certain activities occurring in the environment will affect those interests. As new regulations evolve and the environment changes, firms must be poised to modify their strategies for implementing new innovative programs that offer meaningful benefits to the firm. Ultimately, firms negotiate with political officials for the best arrangement that in some way promotes their interests. Similarly, firms have to advocate their positions and pursue a structured strategy to achieve that end through the political process. Firms can develop a proactive approach to managing this process without appearing to be hostile toward the government. In most instances, firms that have developed constructive relationships with government institutions are better suited to be in a position to address proposed changes that potentially could affect the environment. In this regard, it is necessary for firms to have a flexible plan of action in place that anticipates the actions of governmental institutions.

—Sylvester E. Williams, IV

See also AFL-CIO; American Medical Association (AMA); Chamber of Commerce of the United States; Corporate Public Affairs; Corporate Rights and Personhood; Interest Groups; Political Action Committees (PACs); Political Theory; Public Relations; Strategic Philanthropy

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Corporate Public Affairs

Corporate public affairs is that arm of the organization that deals with interactions of the organization in the nonmarketplace arena of action. The external environment in which organizations operate today is becoming increasingly intrusive and active in attempts to influence and shape organizational actions and decisions. Public affairs is the center of the organization's actions to anticipate, plan, and respond in a thoughtful and articulated manner to issues, problems, and situations.

These problems/situations can arise as a result of corporate and industry action or inaction, regulatory proposals, legislative actions, media and special interest actions, and so on. This can involve then dealing with regulatory agencies at all levels, with governmental bodies of all kinds and types, with the media, with the general public, and with nongovernmental entities either individually or simultaneously. This nonmarketplace arena is often referred to as the marketplace of ideas (as opposed to the marketplace for goods and services). Both for-profit and not-for-profit organizations have public affairs departments. The existence of these departments recognizes the critical role the marketplace of ideas plays in setting the rules and regulations under which competition is conducted and the costs that actions in this arena can impose on organizations. In addition, organizations have now recognized that their legitimacy as a societal actor is related to how they are perceived by society and government.

The Development of Public Affairs

Modern-day public affairs activities and organization can trace its roots back to three streams of development starting in the 1920s. These three areas—corporate philanthropy, urban and community affairs, and public relations—each contained elements of what was to emerge as today's public affairs department. Corporate philanthropy (financial contributions to not-for-profit and other socially oriented organizations) arose out of stormy relationships between and among businesses, governments, and society. In many ways the interest in philanthropy arose out of prior corporate excesses and this was the response to those poor behaviors. Although this was meant to demonstrate "corporate" charity, it too has become embroiled in controversy (most notably in charges by shareholders that this is not what they want done with their monies and by external groups who today see this as a skeptical and cynical approach to influence external actors to the corporation).

As urbanization occurred worldwide, with ever more numerous cities of ever larger size, unique problems arose (racial strife and tensions, slums, education, etc.), and the focus of organizations shifted to what was termed urban affairs. Although this could also be considered philanthropy, it was not focused solely on giving of funds for broad general purposes but the giving of funds, talents, and organizing skills to improve urban life. It should be noted that both corporate philanthropy and urban affairs activities were often pursued for self-interest motives by the organizations involved.

The final "root" of public affairs lies in public relations as corporate philanthropy and urban affairs were not sufficiently broad enough in focus for the organization and the increasingly complex environment it found itself embedded in. Originally, public relations were focused on struggles the organization had with regulatory agencies, politicians, and leaders of organized labor. Although this was a more thoughtful advance on the organization's relationship with the larger environment, it was limited in its role and impact. Many viewed public relations as the organization's attempt to spin an issue or problem after the fact. That is, public relations was *not* about preparedness and foresight but instead was focused on damage control once an issue, problem, or situation achieved visibility. It was recognized that public relations, corporate philanthropy, and urban affairs were simply not enough for the modern-day organization in dealing with a growing variety and sophistication of external actors all demanding that the organization respond to them and their issues and concerns.

But how do organizations respond to such concerns? They responded with the development of public affairs departments to deal with the breadth and depth of external issues and actors. Despite the documented growth in public affairs, corporations still use different names for this function. The most popular names are governmental affairs/relations, public affairs, corporate relations/affairs, corporate communications, and external affairs/relations. The key point is that whatever the name of the department, its focus has to be broad, on the interpretation and monitoring of the marketplace of ideas and on the prioritization of those external concerns, developing policy to reply to those concerns, and then advocacy for the corporation's position with external actors and agencies. Finally, the activities and focus of public affairs should be carefully aligned with the strategy and strategic plan of the corporation as a whole.

Tools and Techniques of Public Affairs

To be effective and to aid the organization in pursuit of its objectives, public affairs have developed a set of activities, tools, and techniques for dealing with these external groups and pressures. A modern-day public affairs department can encapsulate the following types of activities: lobbying (at all levels), political action committees, issues management, stakeholder management, trade association involvement, coalition building (both within the industry and with diverse external groups), grassroots activities, philanthropy, community relations, crisis management, regulatory affairs, media relations, environmental affairs, institutional investor relations, stockholder relations, educational relations, corporate social responsibility, employee communications, and nongovernmental organization relationships.

This is an impressive list, but what fundamentally defines a public affairs department is not the list of activities it engages in but the orientation to serving as a window into the organization for non-market-based challenges and organizations (e.g., nongovernmental organizations) and as a window out for the organization to those external players. The core of activities in public affairs are oriented to assessing the future risks to the organization of issues (in any forum—legislative, judicial, regulatory, general public), trends, situations, and stakeholders that challenge or limit the legitimacy of the organization or its ability to operate in a discretionary fashion.

Although the activities noted above are lengthy, they can be organized into larger categories of tools and techniques. One useful organizing tool is to consider short- and long-term time frames. In the area of strategy one thinks of a strategic plan as the organization's long-term response to its environment and tactics as the plan to achieve the short time frame operational choices to achieve the long-term goals. In a similar fashion, we can look at issues management and stakeholder management as reflective of long- and short-term considerations.

Issues Management

Organizations looking toward the future attempt to assess which issues (differences in facts, values, or policies) are likely to gain traction in the marketplace of ideas and which issues have an impact on the organization and therefore require planning and action. This action can range from attempts to block the emergence of an issue in a given arena (e.g., prevent global warming becoming a legislative or regulatory issue) to altering the definition of an issue after it has appeared and is being actively discussed (e.g., a discussion of immigration could be in the context of opening a country's borders to the oppressed or it could be couched in terms of blocking terrorism). Such definitional manipulation can impact on how stakeholders become energized to act or not and also impact on the arena where the issue might be resolved (e.g., in a regulatory hearing as opposed to legislative action). Issues management, therefore, is the tool of public affairs that allows the organization to think about the longer-term horizon of issues, problems, and/or situation that might arise; have an impact on the organization; and demand some sort of planned response.

Tools and techniques within issues management can include media relations, lobbying, grassroots campaigns, coalition building (within an industry, with other industries, and with outside actors), political action committees (organized fund-raising for politicians and their election efforts), Web activism, employee communications, and community relations. The goals are straightforward, to prevent the issue from arising and if that fails to amend, alter, and shape the issue in ways favorable to the organization and/or to place the issue in a specific area of resolution (legislative, judicial, regulatory) where the organization believes it has an advantage over other stakeholders on this issue.

Stakeholder Management

Issues management is simply not specific enough for an organization to act on in any meaningful manner. Although issues management can focus the organization's attention on a specific topic—global warming as an example—the next logical question is what do we do with this issue. This requires an exploration of who the likely "stakeholders" are with regard to this issue. Stakeholders, as might be easily surmised, are those individuals, groups, and organizations who have a "stake" in an issue and how it is resolved. Usually, this stake or level of interest and involvement is significant; otherwise, the organization will see no reason to become engaged in the issue. In global warming, for example, oil and energy companies have a stake in how that issue is discussed, debated, and ultimately resolved. The resolution of this issue might impose additional costs, threaten the legitimacy and survival of the firm, and/or limit the ability of the organization to make discretionary choices. Other stakeholders in this issue can include environmental and regulatory organizations, alternative fuel manufactures (e.g., nuclear power), and other related industries and individuals. The specific constellation of stakeholders will have major impacts on how an issue is resolved and *where* it is resolved.

It should be very clear that lobbying; coalition building; community, regulatory, and external affairs; and other techniques and tools noted above can be brought to focus when dealing with stakeholders. To be very clear, public affairs is about positioning the organization in such a way that it can deal with external pressures, groups, and situations in a thoughtful manner that meets organizational objectives. Although not widely considered, public affairs is also about advising the organization on issues and situations where it cannot "win" and that fighting the specific issue or situation at hand is unlikely to yield positive responses and is more likely to cost the organization (both in terms of finances and image/reputation/credibility/legitimacy).

International Public Affairs

The growth of the Internet and other forms of communications, along with global trade, poses new problems for corporate public affairs. In years past, geographical distances, cultural differences, and language meant that issues, problems, and situations would not easily migrate across geographic borders. This meant that a problem in China might not become a concern in Europe until years after it arose in China. This afforded organizations the "luxury" of following these new problems and how they arose and were treated. The organization could learn from this problem and be better prepared to treat it when it arose in a different area. It also allowed the organization to experiment with approaches to the problem, with the crafting of specific messages in predetermined arenas, and in interactions with stakeholders.

The luxury of time and geographical space no longer exists; an issue or problem (such as global warming) can arise simultaneously in multiple areas of the world, with different stakeholders involved, who define and conceptualize the problem or issue differently. Further, these problems can be defined and conceptualized differently, with the problems having highly different impacts on various societies, and might be addressed in different forums (e.g., legislative, judicial, regulatory).

In essence, the organization is compelled to fight a "multifront" situation, with all the attendant complexities such a multifront battle entails. One aspect that should not be underestimated is the impact of different cultural milieus on the identification, shaping, evaluation, and response of external national groups to an organization's actions.

Now an organization's response to a situation can become known worldwide in moments to a much larger audience and the response can be analyzed by external actors in different locales that can then shape their subsequent actions. As a result, there has been, over the last decade, an increase in outsourcing of public affairs activities. Clearly, the outsourcing of activities in international venues makes great practical and strategic sense.

Assessment of Public Affairs

No discussion of public affairs would be complete without addressing assessment. As in any area of organizational activity, the age-old question of value received in relationship to resources expended can and must be asked with regard to public affairs. In asking any such question, however, it must be remembered that using traditional corporate measures (profitability, costs, return on investments, etc.) may have little relevance to public affairs.

Consider the marketplace of ideas in which public affairs operates—a highly fluid and dynamic environment where losing a specific battle may be the best strategic and tactical choice available to the firm. The suggestion here is that the measurement and assessment of public affairs is difficult and is clearly both quantitative and qualitative in nature. Adding to the complexity of measurement is that a public affairs campaign on a specific issue with multiple stakeholders in different geographical locales might take years before a resolution is achieved—yet the time delay in the resolution of the problem might in itself provide advantages to the organization.

In addition, the public affairs department is constrained in being too public (either internally or externally) about its successes. A frequent "success" story for public affairs is that it successfully manages an issue in the legislative or regulatory arena that prevents the imposition of additional costs on the firm or preserves discretion for the firm to act. It might be unwise for the department or for the firm to tout its successes here.

However, there are broad areas in which public affairs can be assessed. Such areas would deal with the following: (1) Do public affairs actions preserve markets for the organization? (2) Do public affairs actions control and/or reduce risk for the organization? (3) Do public affairs actions afford the organization access to key decision makers on issues of import to the firm? (4) Do public affairs successfully prioritize and inform key organizational leadership of changes and issues arising in the marketplace of ideas with sufficient time to take action? (5) Do public affairs actions advance the organization's image and reputation with key stakeholders? (6) Do public affairs activities reduce the instances of crises for the organization and/or help the organization manage a crisis successfully?

The Foundation for Public Affairs in Washington, D.C., recently surveyed corporations on their assessment of public affairs. They found that performance assessment of public affairs was improving—with more than 50% of their respondents noting that they had a highly developed performance measurement capacity (only 42% answered this way in the previous survey). Fifty-six percent of the firms have a formalized process for measuring and evaluating public affairs performance. It is clear that measurement of public affairs performance is becoming increasingly sophisticated and formalized. In their survey, the tools and techniques for the assessment of performance fell into two major areas—outcomes and processes. In the category of outcomes, they found that corporations use three tools/techniques most often—objectives achieved, legislative wins/losses, and costs reduced/avoided. In the category of processes, the most used measure was internal customer satisfaction, followed by external customer perception/attitude. Notice the balance here between external-focused activities and internal-focused activities (the window in, window out phenomena) and the use of both quantitative and qualitative assessments.

No matter what the approach, there is agreement that measurement and assessment of public affairs leads to improved public affairs performance. Since a key aspect of the public affairs department is to maintain relationships outside the boundaries of the corporation, a key assessment approach to use is focus groups with external entities. In this manner the organization can set up a baseline comparator to use in unfolding assessments. Although objectives achieved is a primary measurement tool, one must be careful in its application.

Although organizational objectives can be easily specified, the marketplace of ideas in which the organization operates must be assessed. Reasoned objectives might be unachievable in a given ideas marketplace. The reasons for being unachievable might range from the timing of an issue (the marketplace is not ready to deal with this issue at this time) to the organization's poor reputation on this issue that precludes them from achieving success on the issue. Simply put, the tools of assessment for public affairs departments must be constructed not only with normal corporate procedures and objectives but also in light of the larger external marketplace of ideas.

The external environment in which organizations operate today continues to grow in complexity. Time in no longer an ally for an organization in decision making. Corporations are facing an increasing number of well-financed and organized nongovernmental organizations around the world. Public affairs management is and will continue to be a major organizational capability to represent the firm in the marketplace of ideas.

—John F. Mahon

See also Corporate Citizenship; Corporate Issues Management; Corporate Political Advocacy; Corporate Social Responsibility (CSR) and Corporate Social Performance (CSP); Corporate Social Responsiveness

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Corporate Rights and Personhood

Discussions of the rights of corporations can be divided into two overlapping topics—discussion of the current legal rights of corporations and discussion of what rights corporations ought to have. The latter is an ethical debate, the former legal and constitutional. After brief comments on the current legal situation, this entry will concentrate on ethical issues. Theoretical defenses of corporate moral rights will be outlined and comments made on current discussions of several possible corporate rights. However, the application of the theoretical defenses to possible rights is far too large a topic to be properly discussed here. Furthermore, it is an area that currently requires much more research and discussion.

Personhood and the Legal Rights of Corporations

The legal rights of corporations are whatever the law says they are. This varies from country to country, but the central principle in countries influenced by the Anglo-American legal tradition is that corporations are persons for legal purposes. This legal fiction derives originally from common law, but has received constitutional recognition in numerous countries. The framers of the American Constitution intentionally avoided giving the federal government the right to charter corporations, but later court decisions have extended constitutional protections to corporations. The most important and most cited case is the Supreme Court decision in 1886 in *Santa Clara County v. Southern Pacific Railroad Company.* This ruling had the effect of recognizing corporations as persons and of extending constitutional protection to them. In many subsequent cases, lawyers have successfully argued that as persons corporations should receive equal protection under the Fourteenth Amendment. However, critics of corporate personhood have pointed out that recognition of corporations as persons was not actually an explicit ruling of the Supreme Court in the *Santa Clara County* case; reference to personhood appears only in the preamble. The decision itself concerned taxing fences along railroads.

If corporations are persons, then what rights they have is fairly clear; they have the same rights that people have. This is not entirely true, especially for political rights, such as the right to vote or run for office, but U.S. courts have upheld the same-rights-as-people principle in many other instances. Stoll has collected a list of court-recognized legal rights of corporations that includes due process, the right to a jury trial, the right to avoid double jeopardy, and several others. The right of corporations to freedom of speech is debatable, as will be discussed later.

The Moral Rights of Corporations

Ethical debate about the rights of corporations centers on whether corporations have any rights that the law and the rest of society ought to recognize. Such rights are variously known as corporate moral rights, inherent rights, or prelegal rights. The language of corporate moral rights resembles that of human rights; if the law contradicts human rights or corporate moral rights, we do not say the rights do not exist, we say they have been violated. Corporate moral rights and human rights tend to be dissimilar in most other respects but there is some overlap in their justifications.

Justifications for Corporate Moral Rights

There are at least five types of arguments for corporate moral rights. Which rights corporations ought to have varies by the justification used and, in fact, is not always clear. However, none of these justifications should be taken as justifying the same-rights-as-people principle that is the basis of current law. The transfer argument might be interpreted as justifying something like that principle; the other arguments appear not to justify it. The status of various rights is discussed in the next section.

The first argument for corporate moral rights is the property rights argument that was used by lawyers in *Santa Clara County v. Southern Pacific Railroad.* This claims that violations of a corporation's rights are ethically equivalent to violating the rights of the corporation's owners. The problem with this argument is that it is severely limited. Since it relies on the concept of ownership, it seems to establish only that corporations have property rights that ought not to be violated. The argument seems to say nothing about any other rights corporations often claim, such as the rights to secrecy, to freedom of speech, to bear arms, and so on. The argument can also be criticized for lack of coherence. Why does the fact that a person owns something create any rights for that thing? What rights does one's lawnmower have? The argument also involves legal contradictions; if corporations are the property of their shareholders, and corporations are persons, then the shareholders own a person, which is prohibited by laws against slavery. The property right of the owners of corporations seems a confusing way of determining the rights that their property ought to have and certainly does not establish corporate personhood.

The second argument is the transfer argument. The creators of a corporation are thought to transfer to the corporation their own rights. If they transfer all their rights, this might justify the same-rights-as-people principle. This argument also can be criticized for lack of coherence. Is the transfer an actual action or a legal fiction? Do the corporation's owners keep their rights after they have been transferred? What right do people have to transfer their rights and why should anyone else recognize that right? The transfer argument seems to beg the question.

Utilitarianism underlies the third sort of argument. Utilitarian arguments for the rights of corporations are very powerful and have been developed at great length by the law and economics movement. The gist of these arguments is that recognizing the rights of corporations encourages investment, innovation, efficiency of production, and capital accumulation and concentration. The result will be a dynamic, thriving, growing economy from which everyone can benefit. These utilitarian arguments may not establish exactly the same-rights-as-people principle, but they tend to defend a large suite of rights for corporations. Critical concerns about the utilitarian approach include fears that it privileges people's economic goods over other goods such as social, family, public, and political goods and even over justice. Utilitarian theory should require that economic growth be balanced with other sources of human happiness. Second, economic theory ignores desires for economic processes as it includes only economic outcomes. And it ignores the issue of metadesires. Third, not all corporate investments tend toward the good of people. Investments in lobbying, market dominance, secrecy of harmful information, and some sorts of lawsuits (such as lawsuits that have the sole purpose of intimidating and bankrupting critics of corporations) may cause more harm than good. Perhaps corporations ought not to have the right to invest in these sorts of things even if recognizing such rights promotes economic growth.

Fourth, the idea of a social contract is sometimes used to establish the moral rights of corporations. When social contract arguments are mentioned in this context, most people think of a contract between society and corporations in which corporations are granted rights in exchange for promoting society's interests. There are two problems with this idea. First, although historically corporations had social obligations as part of their charters, the law has long recognized that corporations can be established to serve only private goals such as making a profit. To return to chartering corporations only if they pursue social goals would be such a radical departure from current practice that very few people defend it. Second, this social contract approach cannot establish the moral rights of corporations because any negotiations with corporations presuppose their rights to exist, to pursue their own interests, and to negotiate with society. These sorts of rights are precisely what the debate over corporate moral rights is trying to consider.

Another social contract approach is to advocate that people negotiate a social contract with each other that recognizes the rights of corporations but without corporations being party to the contract. This approach could advocate an actual social contract discussed in legislatures. The problem with this is that historically most corporate rights, including personhood, were not democratically discussed but decided by courts. Trying to start such a discussion now would encounter the political power of corporations to become involved in the debate, which undermines its social contract justification.

Instead of an actual social contract debate, one could argue for a hypothetical Rawlsian-style social contract. What rights this would imply for corporations is not clear, and this is an idea that requires further research.

Fifth, a deontological argument for the rights of corporations has also been advanced. This argues that corporations are, in fact, existing agents that have interests and autonomy that the law ought to recognize and protect. The problem with this is that the interests and autonomy of corporations may not be of the sort that makes them moral agents with rights.

The Right to Exist

The right of corporations to exist covers two issues—charter versus registration and forced dissolution. Governments originally chartered corporations for specific purposes. Charters were only granted after consideration of the social good that would result. Often, there were time limits on the corporation's existence. Now corporations are registered; anyone can create a corporation by registering it, and most corporations serve only private purposes. Morally, should society have the right to issue conditional charters, or should people have the right to create corporations for any legal purpose? Also, should the life of corporations be indefinite or have a time limit on them? In defense of registration, it has been pointed out that giving governments the right to accept or deny charters has generally led to government corruption.

The right to exist also raises the question of whether courts should be able to forcibly dissolve corporations, especially for criminal actions. Some people have argued that dissolution should be automatic if a corporation has a third criminal conviction; this they view as equivalent to life imprisonment for people with three convictions (or as close to equivalent as possible since corporations cannot be imprisoned). Others view dissolution as equivalent to capital punishment and think it should only be used for the worst sorts of corporate crimes. There are also people, including many American prosecutors, who hold that corporations should not be charged with crimes at all on the grounds that conviction would require criminal intent, and corporations cannot have intentions in the relevant sense. This view seems to undermine the whole concept of corporate personhood.

The Right to Own Property

All the theoretical justifications of corporate moral rights justify the rights of corporations to own property, to sign contracts, and to sue and be sued. These rights are basic to corporations being able to conduct business. Guaranteeing these rights is the origin, in common law, of the doctrine that corporations are persons. However, the right of corporations to own other corporations or their shares was a later development, and it is a right that some people question. They argue that not allowing cascading acquisitions and ownership of corporations by corporations would force businesses to compete on customer service rather than trying to gain market dominance or control by acquisitions. In the United States, the Sherman Act of 1890 prohibited pursuit of monopolies by acquisition, but this does not constitute a complete prohibition on corporations owning other corporations or their shares, and the enforcement of such antitrust legislation depends on the political will to do so.

The Right to Bear Arms

If corporations are persons, then the American Constitution may extend to them the right to bear arms. This would include the right to hire armed security guards to protect their property and to supply armed security services to other companies. Most people admit the need for corporations to protect their property, including cash, securities, chemicals, and explosives from criminals and terrorists, but in jurisdictions without the constitutional right to bear arms some people suggest that the police should have a monopoly on guns and that corporations should hire the police when they need security services. A more modest suggestion is that armed corporate security personnel should be trained, licensed, and monitored.

The size, wealth, and organization of corporations can raise issues not usual with individuals carrying guns. Large corporations can afford and can organize what amounts to private armies equipped with armored vehicles, helicopters, and heavy weapons. Some multinationals have done so, usually to protect assets and employees in countries where they cannot rely on the government for such protection. Multinational oil corporations operating in parts of Africa have done this directly or by contracts with suppliers. Ethical objections to this include the principle that armed forces should be a government monopoly; that corporate armies have been used to support government corruption and oppression; that corporate armies have taken on political and offensive roles beyond securing corporate property; and that there is a potential for corporate armies to overthrow governments, especially ones that might nationalize corporate property or rights to natural resources. In defense of corporate armies is the fact that the only alternative in some countries is to withdraw from the country. Also, most accusations of corporate support for oppressive governments involve financial support for corrupt government armies or paramilitary groups, not the use of the corporation's own security forces.

Recently, there has also been discussion of the ethics of private security firms offering protection services in active combat zones, especially Iraq. Such corporations have been actively involved in armed combat. Ethical concerns include lack of monitoring and accountability, lack of international law similar to the laws that apply to armies, fears that innocent bystanders may be harmed, and the possibility that these corporations may be run by or hire psychologically disturbed people. Although these companies claim they supply only security services, there is concern that security companies might be used as a cover for mercenaries (which would violate international law as well as ethics). The right to bear arms is a good example of a rights issue in which the personhood of corporations can distort discussion of the ethical issues that arise when individuals and corporations have the same rights.

The Right to Freedom of Speech

Should corporations enjoy the right to freedom of speech and expression? The U.S. Supreme Court in *Kaski v. Nike* has recently looked at this issue, but ruled on a technicality leaving the issue of free speech unresolved. Nike was claiming that it had the right to issue false press releases on the grounds that press releases are a form of political speech protected by the right to freedom of speech. Kaski's lawyers argued that since Nike was a for-profit corporation, all of its public pronouncements had a commercial intent and, therefore, should be covered by laws that prohibit false advertising. If corporations are viewed as entirely commercial entities, this would severely limit their political rights, including the right to free speech and other rights such as the right to lobby governments. Corporations do not have the right to vote or run for office, but their other political rights, especially the right to donate money to political parties and candidates, is greatly debated and litigated. Corporate political donations are banned in some countries; for example, donations by corporations to candidates for public office are banned in the United States.

The Right to Secrecy

As a final example of a debated corporate right, consider the claim of corporations that they are entitled to keep all their affairs secret. This right is voluntarily suspended for financial data when a corporation lists its shares on a stock exchange, but otherwise the right is jealously guarded. The argument that corporations have a right to secrecy simply because they are private should be rejected because it is based on the equivocation of two meanings of the word *private*—private as opposed to government and private as in the right to privacy. Under the doctrine of corporate personhood, corporations have argued, sometimes successfully in court, that protection against unreasonable search and seizure prohibits laws mandating government safety and environmental inspection of their industrial plants. The law and economics movement argues that the right to secrecy is justified because it encourages or is vital to investment in corporate enterprises. Critics argue that corporations ought to be transparent because industrial plants are not private in the sense that a family's living room or bedrooms are. Critics also argue that public safety requires transparency, that people have a right to know how society's resources are being used, and that consumer choice and the fee market depend on the availability of information. Suggestions for transparency include freedom of information statutes that cover corporations; making all contracts, or at least contracts between corporations, public; making all out-of-court settlements of litigation public; and requiring the publication of all safety-related research and information.

Contesting Corporate Personhood

Corporate personhood and the rights of corporations are currently being contested in three arenas. Corporations are defending and trying to expand their rights through litigation, often arguing for constitutional protections as far as the Supreme Court. Academics are discussing the moral issues surrounding rights and personhood, mostly in legal journals, but there is also some discussion in philosophy and business ethics journals. This is an area that needs a great deal more research. Finally, there is a movement in the United States to legally remove personhood from corporations. This movement has had some symbolic success passing local ordinances abolishing corporate personhood, but it is a long way from the constitutional amendment that is required to make any real difference.

The personhood of corporations has two significant effects on business ethics. First, it determines much of the legal environment of corporations and, thus, provides a framework in which the ethics of corporate actions and policies must be discussed. Second, it provides a frame for seeing corporations in a certain way, which leads many ethicists to argue that corporations have moral responsibilities similar to those that people have. For example, if corporations are persons, then we can talk about corporate social responsibilities or about corporate citizenship. Other people argue that the legal fiction of personhood should determine neither the moral rights nor the responsibilities of corporations.

—John Douglas Bishop

See also Agency, Theory of; Arms Trade; Autonomy; Business Law; Campaign Finance Laws; Collective Punishment and Responsibility; Confidentiality Agreements; Consumer Rights; Consumer Sovereignty; Corporate Accountability; Corporate Moral Agency; Corporate Political Advocacy; Disclosure; Economic Incentives; Freedom of Contract; Freedom of Information Act of 1966 (FOIA); Free Speech in the Workplace; Human Rights; Legal Rights; Moral Agency; Nike, Inc.; Privacy; Property and Property Rights; Rawls's Theory of Justice; Rights, Theories of; Utilitarianism

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Corporate Social Financial Performance

The relationship between corporate social performance and corporate financial performance is a topic that "business and society" scholars have been debating for several decades. This entry will focus on the empirical evidence that point to complementarities and, thus, a positive correlation between corporate social and financial performance. However, different scholars have also portrayed social and financial performance as two contradictory or independent concepts. Before the arguments for each position are summarized, the definition and consequences of "social responsibility" and "social performance" must be specified a bit more clearly.

Corporate social performance can be defined as an organization's configuration of principles of social responsibility, processes of social responsiveness, and observable outcomes as they relate to the organization's societal relationships. In other words, a socially responsible organization evaluates its impact on society comprehensively and acts on certain principles to protect and improve its social and natural environments. Consequently, such a responsible firm will develop internal structures and processes to respond constructively to concerns ranging from product safety to pollution prevention to employee work-life balance. As such, high corporate social performance is the outcome of a relationship-building process between the organization and all its internal and external stakeholders. Organizational stakeholders include, among others, employees, customers, suppliers, partners, social and environmental activists, governments, local communities, and other groups. It is important to keep these specific, technical definitions of "social responsibility" and "social performance" in mind throughout this entry. (Contrary to this usage of the term in this entry, some economists redefine "business social responsibility" as "profit maximization.")

A Complementary Relationship?

According to instrumental stakeholder theory, an organization will be more likely to achieve its economic goals if it tries to satisfy its various stakeholders' needs in a balanced way. Through social performance, an organization may enhance its economic effectiveness because it may have developed a favorable reputation for fair business dealings, which may attract more customers (increase sales revenues) or better and more committed employees (increase labor productivity). Simultaneously, balanced stakeholder management can either reflect organizational learning or build up managerial skills, which can translate into higher financial performance. In turn, higher financial performance may allow organizations to spend more money on social or environmental causes. Such complementarities may result in self-reinforcing cycles of social and financial performance in which both variables are positively correlated.

A Contradictory Relationship?

Some economists and ethicists regard the complementary vision of social and financial performance as utopian and idealistic. For example, economists such as Nobel Prize winner Milton Friedman argue that, by definition, corporate social performance is an altruistic, sacrificial strategy that expends financial and other organizational resources at the expense of the organization's owners. A social responsibility strategy, according to this view, is particularly harmful to a firm's market performance because stakeholder management is performed by executives that have not been elected by the public and generally do not possess the skills (especially compared with the government) to make informed decisions about stakeholders in social and environmental arenas. Overall, advocates of this perspective argue that social performance is a waste of shareholder funds and, thus, hinders rather than enhances an organization's economic performance, which explains and predicts a negative relationship between the two variables.

Are These Two Concepts Independent, and Thus the Relationship Null?

A third strand of theorizing postulates a null relationship between social and financial performance. More recently, economists have argued that corporate social responsibility was a normal good whose provision would be determined by the forces of supply and demand. Overall, market forces will cause the overall relationship to be zero, or null, although a number of contingencies (e.g., firm size or innovation) may also cause it to be positive or negative. Furthermore, some business and society scholars postulate that the principles driving instrumental market activities and duty-bound ethical activities are, in fact, very different. These normative incompatibilities may explain why many studies have indicated a null correlation between social and financial performance.

Overarching Empirical Evidence to Date

The Meta-Analytic Technique

Meta-analysis is the way most quantitative sciences (e.g., medicine, physics, psychology) take stock and reach overall conclusions about a research area. It represents an empirical quantitative integration of the findings of previous research and corrects for certain study artifacts that affect any primary study (e.g., sampling error, measurement error, and a few other possible study artifacts). Thus, for reaching conclusions about an entire research program spanning several decades, meta-analysis is a more valid research tool than narrative reviews, which in this research area have typically concluded that there does not appear to be any relationship between the two variables. However, four meta-analyses in this area have shown that overall social performance and financial performance are most likely complementary.

Interpretation of Results

Overall, the award-winning meta-analysis by Orlitzky, Schmidt, and Rynes supports the hypothesis of a positive relationship between social and financial performance. A lot of the variability in findings across studies seems to be due to statistical study artifacts and different research strategies. According to this meta-analysis, sampling and measurement errors accounted, on average, for 24% of the variance across studies; reputation measures of social performance were better predictors of financial performance than social-audit disclosures; and the economic impact of social performance was stronger on accounting measures than market measures of economic return. Orlitzky and his colleagues also addressed concerns regarding availability bias—the possibility that studies that fail to show a relationship between social and financial performance are unlikely to be published. File drawer analysis is a technique useful for assessing this concern. The file drawer analysis indicated that more than 1,000 such unpublished studies excluded from the meta-analysis would be needed to change their overall conclusions.

In addition, according to evidence provided by meta-analysis, corporate social performance and financial performance tend to be mutually reinforcing organizational activities. Through the use of time lags, Orlitzky and his colleagues found that financial performance is a positive predictor of future social performance and that social performance also predicts financial performance. In other words, the meta-analytic findings suggest that a business can develop mutually beneficial relations with stakeholder groups, which can actually pay off surprisingly quickly for the socially responsible firm.

Social performance and financial performance are most likely positively correlated because social performance helps improve managerial competencies and enhance corporate reputations. Through a company's positively constructive (rather than adversarial) relations with stakeholders, its stakeholders may perceive that company favorably. For example, internal stakeholders, such as employees, may become more committed, or external stakeholders, such as customers, may become more willing to buy the company's products or pay a premium for the goods from socially responsible firms. Although the meta-analysis suggested that competency building was a less important factor in the economic-performance-enhancing effects of social responsibility than corporate reputation, corporate social performance might also help organizations develop internal organizational learning mechanisms to deal with the uncertainties presented by its stakeholders.

Social performance may also reduce business risk. Again, these effects are most likely mediated by organizational reputation, as the meta-analytic findings by Orlitzky and Benjamin suggest. By balancing a multitude of stakeholder interests, a firm may increase various stakeholder groups' confidence that the firm will be understanding and nonadversarial in resolving future stakeholder conflicts. In turn, this may reduce the variability of accounting rates of return and share prices because the investment community will not respond to temporary company setbacks by panic selling of its shares, for example.

Organization size does not appear to confound the relationship between social and financial performance. That is, large and—quite unexpectedly—even small companies can reap economic rewards from balanced stakeholder analysis and management. The logic could be illustrated as follows: Small companies that are high in social performance may infuse greater trust into their relationships with allies and reach economically beneficial supply agreements because the company is seen as a more trustworthy and honest partner.

Predating but also narrower in scope than these meta-analyses by Orlitzky and his colleagues, Frooman had shown, in a meta-analysis of event studies only, that irresponsible and illicit corporate actions generally reduced shareholder wealth. This earlier meta-analysis by Frooman is another piece of evidence that suggests that building constructive stakeholder relations serves the enlightened self-interest of companies, their managers, and owners.

Implications for Management

The empirical research accumulated and meta-analytically integrated to date supports the view that, conceptually, corporate social and financial performance are not only compatible with each other in many cases but may also manifest, in tandem, the elusive construct of overall organizational effectiveness. This research program also supports the convictions of some practitioners that a business can maximize its performance when its executives are aware of the multitude of business opportunities that exist in its daily interactions with *all* its stakeholders. A narrow corporate orientation centered *only* on shareholder wealth maximization may miss these societal and environmental opportunities and cause the organization to be out of touch with developments in broader society. Ultimately, such an isolation from trends that are broader than market forces and from stakeholder concerns more generally may harm the corporation economically because it may lead to a reactive, rather than proactive, strategic stance.

The promotion of social performance can reflect enlightened self-interest because it may preempt costly defensive actions in lawsuits. By being socially responsible, an organization could be attuned to stakeholder concerns long before they become legal problems. More positively, quantitative literature reviews of this long stream of research on social and financial performance suggest that corporate social performance can be an investment in the long-term economic sustainability of the organization.

The finding that social performance is likely to be a lever of financial performance is not only reassuring, though. It also raises the important point of the effective and efficient *implementation* of this more value- and stakeholder-based management style. For example, there is a dearth of research in human resource management on the type of organizational staffing, pay, or performance-appraisal practices that are most suitable for maximizing social performance while enhancing financial performance. It is important to stress that the economic pay-offs from high social performance are not automatic. Therefore, business managers and researchers must understand in much greater depth how this potential synergy between social and financial performance can be cultivated in practice. This cultivation may be affected by, and indeed depend on, executives' value orientations and decision making, for example.

The meta-analyses by Orlitzky and colleagues also pointed to a number of challenges in this research area. First, both social performance and financial performance need to be measured with greater reliability. Second, more contingency factors must be considered because, overall, the meta-analysis showed that about 76% of the variability in past findings is *not* explained by the two statistical artifacts of sampling error and measurement error. With respect to several subdimensions of social and financial performance, the relationships were weak, partly due to stakeholder mismatching in prior studies. Stakeholder mismatching occurs when individual studies correlate specific social and financial performance measures that should, in fact, not be correlated (e.g., because researchers provide no theoretical rationale). In addition to these primary-study problems, theoretical contingencies may apply as well. For instance, in empirical research conducted between the late 1960s and the late 1990s, environmental performance was only a weak positive predictor of economic performance, and 60% of its cross-study variance remained unexplained. This finding points to moderators, or contingencies, that future research could explore.

—Marc Orlitzky

See also Corporate Social Responsibility (CSR) and Corporate Social Performance (CSP); Corporate Social Responsiveness; Stakeholder Engagement; Stakeholder Theory; Strategic Corporate Social Responsibility

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Corporate Social Responsibility (CSR) and Corporate Social Performance (CSP)

The concept of corporate social responsibility (CSR) refers to the general belief held by many that modern businesses have a responsibility to society that extends beyond the stockholders or investors in the firm. That responsibility, of course, is to make money or profits for the owners. These other societal stakeholders typically include consumers, employees, the community at large, government, and the natural environment. The CSR concept applies to organizations of all sizes, but discussions tend to focus on large organizations because they tend to be more visible and have more power. And, as many have observed, with power comes responsibility.

A related concept is that of corporate social performance (CSP). For the most part, CSP is an extension of the concept of CSR that focuses on actual results achieved rather than the general notion of businesses' accountability or responsibility to society. Thus, CSP is a natural consequence or follow-on to CSR. In fact, it could well be argued that if CSR does not lead to CSP then it is vacuous or powerless. Interestingly, many advocates of CSR naturally assume that an assumption of responsibility will lead to results or outcomes. Thus, the distinction between the two is often a matter of semantics that is of more interest to academics than to practitioners. Most of our discussion will be focused on CSR with the general assumption that CSP is a vital and logical consequence.

Development of the CSR Concept

The concept of CSR has a long and varied history. It is possible to trace evidences of the business community's concern for society for centuries. Formal writings on CSR, or social responsibility (SR), however, are largely a product of the 20th century, especially the past 50 years. In addition, though it is possible to see footprints of CSR thought and practice throughout the world, mostly in developed countries, formal writings have been most evident in the United States, where a sizable body of literature has accumulated. In recent years, the continent of Europe has been captivated with CSR and has been strongly supporting the idea.

A significant challenge is to decide how far back in time we should go to begin discussing the concept of CSR. A good case could be made for about 50 years because so much has occurred during that time that has shaped theory, research, and practice. Using this as a general guideline, it should be noted that references to a concern for SR appeared earlier than this, and especially during the 1930s and 1940s. References from this earlier period worth noting included Chester Barnard's 1938 publication, *The Functions of the Executive,* J. M. Clark's *Social Control of Business* from 1939, and Theodore Kreps's *Measurement of the Social Performance of Business* from 1940, just to mention a few. From a more practical point of view, it should be noted that as far back as 1946 business executives (the literature called them businessmen in those days) were polled by *Fortune* magazine asking them about their social responsibilities.

In the early writings on CSR, the concept was referred to more often as just SR rather than CSR. This may have been because the age of the modern corporation's prominence and dominance in the business sector had not yet occurred or been noted. The 1953 publication by Howard R. Bowen of his landmark book *Social Responsibilities of the Businessman* is argued by many to mark the beginnings of the modern period of CSR. As the title of Bowen's book suggests, there apparently were no *businesswomen* during this period, or at least they were not acknowledged in formal writings.

Bowen's work proceeded from the belief that the several hundred largest businesses at that time were vital centers of power and decision making and that the actions of these firms touched the lives of citizens at many points. Among the many questions raised by Bowen, one is of special note here. Bowen asked, what responsibilities to society may businessmen reasonably be expected to assume? This question drove much subsequent thought and is still relevant today. Bowen's answer to the question was that businesspeople should assume the responsibility that is desirable in terms of the objectives and values of society. In other words, he was arguing that it is society's expectations that drive the idea of SR.

Bowen went on to argue that CSR or the "social consciousness" of managers implied that businesspeople were responsible for the consequences of their actions in a sphere somewhat wider than that covered by their profit-and-loss statements. It is fascinating to note that when Bowen referenced the *Fortune* article cited earlier, it reported that 93.5% of the businessmen agreed with this idea of a wider SR. Because of his early and seminal work, Bowen might be called the "father of corporate social responsibility."

If there was scant evidence of CSR definitions in the literature in the 1950s and before, the decade of the 1960s marked a significant growth in attempts to formalize or more accurately state what CSR means. One of the first and most prominent writers in this period to define CSR was Keith Davis, then a professor at Arizona State University, who later extensively wrote about the topic in his business and society textbook, later revisions, and articles. Davis argued that SR refers to the decisions and actions that businesspeople take for reasons that are at least partially beyond the direct economic or technical interest of the firm.

Davis argued that SR is a nebulous idea that needs to be seen in a managerial context. Furthermore, he asserted that some socially responsible business decisions can be justified by a long, complicated process of reasoning as having a good chance of bringing long-run economic gain to the firm, thus paying it back for its socially responsible outlook. This has often been referred to as the enlightened self-interest justification for CSR. This view became commonly accepted in the late 1970s and 1980s.

Davis became well known for his views on the relationship between SR and business power. He set forth his now-famous *Iron Law of Responsibility,* which held that the social responsibilities of businesspeople needed to be commensurate with their social power. Davis's contributions to early definitions of CSR were so significant that he could well be argued to be the runner-up to Bowen for the "father of CSR" designation.

The CSR concept became a favorite topic in management discussions during the 1970s. One reason for this is because the respected economist Milton Friedman came out against the concept. In a 1970 article for the *New York Times Magazine*, Friedman summarized his position well with its title—"The Social Responsibility of Business Is to Increase Its Profits." For many years since and continuing today, Friedman has maintained his position. In spite of Friedman's classic opposition, the CSR concept has continued to be accepted and has continued to grow.

A landmark contribution to the concept of CSR came from the Committee for Economic Development (CED) in its 1971 publication *Social Responsibilities of Business Corporations.* The CED got into this topic by observing that business functions by public consent, and its basic purpose is to serve constructively the needs of society to the satisfaction of society. The CED noted that the social contract between business and society was changing in substantial and important ways. It noted that business is being asked to assume broader responsibilities to society than ever before. Furthermore, the CED noted that business assumes a role in contributing to the quality of life and that this role is more than just providing goods and services. Noting that business, as an institution, exists to serve society, the future of business will be a direct result of how effectively managements of businesses respond to the expectations of the public, which are always changing. Public opinion polls taken during this early period by Opinion Research Corporation found that about two thirds of the respondents thought business had a moral obligation with respect to achieving social progress in society, even at the possible expense of profitability.

The CED went on to articulate a three-concentric-circles definition of SR that included an inner, an intermediate, and an outer circle. The *inner circle* focused on the basic responsibility business had for its economic function—that is, providing products, services, jobs, and economic growth. The *intermediate circle* focused on responsibilities business had to exercise its economic activities in a sensitive way by always being alert to society's changing social values and priorities. Some early arenas in which this sensitivity were to be expressed included environmental conservation; relationships with employees; and meeting the expectations of consumers for information, fair treatment, and protection from harm. The CED's *outer circle* referred to newly emerging and still ambiguous responsibilities that business should be involved in to help address problems in society, such as urban blight and poverty.

What made the CED's views on CSR especially noteworthy was that the CED was composed of businesspeople and educators and, thus, reflected an important practitioner view of the changing social contract between business and society and businesses' newly emerging social responsibilities. It is helpful to note that the CED may have been responding to the times in that the late 1960s and early 1970s was a period during which social movements with respect to the environment, worker safety, consumers, and employees were poised to transition from special interest status to government regulation. In the early 1970s, we saw the creation of the Environmental Protection Agency, the Consumer Product Safety Commission, and the Equal Employment Opportunity Commission. Thus, it can be seen that the major initiatives of government social regulation grew out of the changing climate with respect to CSR.

Another significant contributor to the development of CSR in the 1970s was George Steiner, then a professor at UCLA. In 1971, in the first edition of his textbook, *Business and Society,* Steiner wrote extensively on the subject. Steiner continued to emphasize that business is fundamentally an economic institution in society but that it does have responsibilities to help society achieve its basic goals. Thus, SR goes beyond just profit making. Steiner also noted that as companies became larger their social responsibilities grew as well. Steiner thought the assumption of social responsibilities was more of an attitude, of the way a manager approaches his or her decision-making task, than a great shift in the economics of decision making. He held that CSR was a philosophy that looks at the social interest and the enlightened self-interest of business over the long-run rather than just the old narrow, unrestrained short-run self-interest of the past.

Though Richard Eells and Clarence Walton addressed the CSR concept in the first edition of their book *Conceptual Foundations of Business* (1961), they elaborated on the concept at length in their third edition, which was published in 1974. In this book they dedicated a whole chapter to recent trends in corporate social responsibilities. Like Steiner, they did not focus on definitions, per se, but rather took a broader perspective on what CSR meant and how it evolved. Eels and Walton continued to argue that CSR is more concerned with the needs and goals of society and that these extend beyond the economic interest of the business firm. They believed that CSR was a concept that permits business to survive and function effectively in a free society and that the CSR movement is concerned with business's role in supporting and improving the social order.

In the 1970s, we initially found mention increasingly being made to CSP as well as CSR. One major writer to make this distinction was S. Prakash Sethi. In a classic 1975 article, Sethi identified what he called dimensions of CSP and, in the process, distinguished between corporate behavior that might be called social obligation, SR, or social responsiveness. In Sethi's schema, social obligation was corporate behavior in response to market forces or legal constraints. The criteria here were economic and legal only. SR, in contrast, went beyond social obligation. He argued that SR implied bringing corporate behavior up to a level where it is congruent with the prevailing social norms, values, and expectations of society. Sethi went on to say that while social obligation is proscriptive in nature, SR is prescriptive in nature. The third stage in Sethi's model was social responsiveness. He regarded this as the *adaptation* of corporate behavior to social needs. Thus, anticipatory and preventive action is implied.

Some of the earliest empirical research on CSR was published in the mid-1970s. First, in 1975, Bowman and Haire conducted a survey striving to understand CSR and to ascertain the extent to which companies were engaging in CSR. Though they never really defined CSR in the sense we have been discussing, the researchers chose to measure CSR by counting the proportion of lines devoted to SR in the annual reports of the companies they studied. While not providing a formal definition of CSR, they illustrated the kinds of topics that represented CSR as opposed to those that were strictly business in nature. The topics they used were usually subheads to sections in the annual report. Some of these subheads were as follows: corporate responsibility, SR, social action, public service, corporate citizenship, public responsibility, and social responsiveness. A review of their topical approach indicates that they had a good idea of what CSR generally meant, given the kinds of definitions we saw developing in the 1970s.

Another research study in the mid-1970s was conducted by Sandra Holmes in which she sought to determine executive perceptions of CSR. Like Bowman and Haire, Holmes had no clear definition of CSR. Rather, she chose to present executives with a set of statements about CSR, seeking to find out how many of them agreed or disagreed with the statements. Like the Bowman and Haire list of "topics," Holmes's statements addressed the issues that were generally believed to be what CSR was all about during this time period. For example, she sought executive opinions on businesses' responsibilities for making a profit, abiding by regulations, helping to solve social problems, and the short-run and long-run impacts on profits of such activities. Holmes further added to the body of knowledge about CSR by identifying the outcomes that executives expected from their firms' social involvement and the factors executives used in selecting areas of social involvement.

In 1979, Archie B. Carroll proposed a four-part definition of CSR, which was embedded in a conceptual model of CSP. Like Sethi's earlier article, Carroll sought to differentiate between CSR and CSP. His basic argument was that for managers or firms to engage in CSP they needed to have (1) a basic *definition* of CSR, (2) an understanding/enumeration of the *issues* for which a SR existed (or, in modern terms, stakeholders to whom the firm had a responsibility, relationship, or dependency), and (3) a specification of the *philosophy or pattern of responsiveness* to the issues.

At that time, Carroll noted that previous definitions had alluded to businesses' responsibility to make a profit, obey the law, and to go beyond these activities. Also, he observed that, to be complete, the concept of CSR had to embrace a full range of responsibilities of business to society. In addition, some clarification was needed regarding that component of CSR that extended beyond making a profit and obeying the law. Therefore, Carroll proposed that the SR of business encompassed the economic, legal, ethical, and discretionary expectations that society had of organizations at a given point in time.

A brief elaboration of this definition is useful. First, and foremost, Carroll argued that business has a responsibility that is *economic* in nature or kind. Before anything else, the business institution is the basic economic unit in society. As such it has a responsibility to produce goods and services that society wants and to sell them at a profit. All other business roles are predicated on this fundamental assumption. The economic component of the definition suggests that society *expects* business to produce goods and services and sell them at a profit. This is how the capitalistic economic system is designed and functions.

He also noted that just as society expects business to make a profit (as an incentive and reward) for its efficiency and effectiveness, society expects business to obey the law. The law, in its most rudimentary form, represents the basic rules of the game by which business is expected to function. Society expects business to fulfill its economic mission within the framework of legal requirements set forth by the society's legal system. Thus, the *legal* responsibility is the second part of Carroll's definition.

The next two responsibilities represented Carroll's attempt to specify the nature or character of the responsibilities that extended beyond obedience to the law. The *ethical* responsibility was claimed to represent the kinds of behaviors and ethical norms that society expected business to follow. These ethical responsibilities extended to actions, decisions, and practices that are beyond what is required by the law. Though they seem to be always expanding, they nevertheless exist as expectations over and beyond legal requirements.

Finally, he argued there are *discretionary* responsibilities. These represent voluntary roles and practices that business assumes but for which society does not provide as clear cut an expectation as in the ethical responsibility. These are left to individual managers' and corporations' judgment and choice; therefore, they were referred to as discretionary. Regardless of their voluntary nature, the expectation that business perform these was still held by society. This expectation was driven by social norms. The specific activities were guided by businesses' desire to engage in social roles not mandated, not required by law, and not expected of businesses in an ethical sense, but which were becoming increasingly strategic. Examples of these voluntary activities, during the time in which it was written, included making philanthropic contributions, conducting in-house programs for drug abusers, training the hard-core unemployed, or providing day care centers for working mothers. These discretionary activities were analogous to the CED's third circle (helping society). Later, Carroll began calling this fourth category *philanthropic*, because the best examples of it were charitable, humanistic activities business undertook to help society along with its own interests.

Though Carroll's 1979 definition included an economic responsibility, many today still think of the economic component as what the business firm *does for itself* and the legal, ethical, and discretionary (or philanthropic) components as what business *does for others.* While this distinction represents the more commonly held view of CSR, Carroll continued to argue that economic performance is something business does for society as well, though society seldom looks at it in this way.

Corporate Social Performance

As suggested earlier, the concept of CSP is an extension of the CSR concept that places more of an emphasis on *results achieved.* The development of the CSP concept has occurred somewhat in parallel with the CSR concept, but with a slightly different emphasis. The *performance* focus in CSP is intended to suggest that what really matters is what companies are able to accomplish, that is, the results or outcomes of their CSR initiatives and the adoption of a responsiveness strategy or posture. Many of the writers on CSR would argue that results were implied in their concepts and discussions of CSR, but the literature added a branch in the 1970s when writers began emphasizing the "performance" aspect rather than the "responsibility" aspect. Obviously, the two go hand in hand.

Actually, many of the earlier discussions of CSR transitioned to an emphasis on corporate social *responsiveness* before the performance focus became common. Brief mention should be made of this in the discussion on CSP. William Frederick is often credited with best describing the difference between responsibility and responsiveness when he dubbed them CSR_1 and CSR_2. With CSR_1, he was referring to the concept of CSR that we discussed in the previous section. The emphasis there is on accountability. CSR_2, in contrast, was intended to reflect the emphasis on responsiveness, or action. In the responsiveness focus, attention turned to the mechanisms, procedures, arrangements, and patterns by which business actually responds to social expectations and pressures in society. The responsiveness focus, therefore, turned the attention from responsibility (business taking on accountability) to responsiveness (business actually responding to social expectations).

In many respects, the emphasis on performance in CSP continues to carry this line of thought forward. That is, the term implies the field has transitioned from *accountability* to *responding* to *results* achieved.

The concept of CSP began appearing in the literature in the mid-1970s. Writers such as Lee Preston, S. Prakash Sethi, and Archie Carroll were among the early authors to speak of the importance of CSP. As mentioned earlier, Carroll presented a conceptual "model" of CSP that motivated a series of improvements and refinements to the concept. Steven Wartick and Philip Cochran took Carroll's three dimensions and broadened them into more encompassing concepts. Wartick and Cochran proposed that the social issues dimension had matured into a new management field known as social issues in management. They extended the model further by proposing that the three dimensions be viewed as depicting *principles* (corporate social responsibilities, reflecting a *philosophical* orientation), *processes* (corporate social responsiveness, reflecting an *institutional* orientation), and *policies* (social issues management, reflecting an *organizational* dimension). In short, Wartick and Cochran updated and extended the three dimensions of the model.

The CSP model was further developed by Donna Wood in her reformulation of the model. Wood expanded and elaborated Carroll's model and Wartick and Cochran's extensions and set forth a reformulated model that went into further detail emphasizing the *outcomes* aspect of the model. Wood argued that CSP was a business organization's configuration of principles of SR; processes of social responsiveness; and policies, programs, and other observable outcomes related to the firm's relationship with society. More than previous conceptualizations, she emphasized the importance of the *outcomes* of corporate efforts.

Diane Swanson extended Wood's model by elaborating on the *dynamic nature* of the principles, processes, and outcomes reformulated by Wood. Relying on research from corporate culture, Swanson's reoriented model linked CSP to the personally held values and ethics of executive managers and other employees. She proposed that the executive's sense of morality highly influences such policies and programs of environmental assessment, stakeholder management, and issues management carried out by employees. One of Swanson's major contributions, therefore, was to integrate business ethics into the implementation of the CSP focus.

Other concepts have developed in recent years that have embraced a concern for CSR and CSP. They are mentioned here but not developed because they get somewhat outside the traditional boundaries of these concepts. *Corporate citizenship* is a concept that must be mentioned because in the minds of many it is synonymous with CSR/CSP. The entire *business ethics movement* of the past 20 years has significantly overlapped these topics. The *stakeholder concept* has fully embraced and expanded on these concepts. The concept of the "triple bottom line," a concern for economic, social, and environmental performance, has embraced the CSR/CSP literature. The concept of "sustainability" has also embraced CSR/CSP thinking. Corporate sustainability is the goal of the triple-bottom-line and CSR/CSP initiatives—to create long-term shareholder value by taking advantage of opportunities and managing risks related to economic, social, and environmental developments.

Business's Interest in CSR and CSP

To this point, we have been discussing primarily the contributions of academics to the development of the concepts of CSR and CSR. To be sure, the business community has had a parallel development of its interest in the concepts as well. The business community, however, has been less interested in academic refinements of the concept and more interested in what all this means for them, in practice. Prominent business organizations have developed specialized awards for firms' social performance. One example of this would be *Fortune* magazine's "most admired" and "least admired" categories of performance. Among *Fortune*'s eight attributes of reputation, one will find the category of performance titled "social responsibility." The Conference Board is another organization that has developed an award for corporate leadership in the CSR realm. The Conference Board annually gives an award titled the "Ron Brown Award for Corporate Leadership" that recognizes companies for outstanding achievements in community and employee relations. Among the core principles for this award are that the company be committed to corporate citizenship, express corporate citizenship as a shared value visible at all levels, and it must be integrated into the company's corporate strategy.

For several years now, *Business Ethics* magazine has published its list of Annual Business Ethics and Corporate Citizenship Awards. In these awards, the magazine has highlighted companies that have made stellar achievements in CSR/CSP. One of the important criterion used by the magazine in making this award is that the company have programs or initiatives in SR that demonstrate sincerity and ongoing vibrancy that reaches deep into the company. The award criteria also stipulate that the company honored must be a standout in at least one area of SR, though the recipients need not be exemplary in all areas.

Though one will always find individual businesspeople who might reject or fight the idea of CSR/CSP, for the most part today, large companies have accepted the idea and internalized it. One of the best examples of this acceptance was the creation in 1992 of the association titled Business for Social Responsibility (BSR). BSR is a national business association that helps companies seeking to implement policies and practices that contribute to the companies' sustainability and responsible success. In its statement of purpose, BSR claims to be a global organization that helps its member companies achieve success in ways that respect ethical values, people, communities, and the environment. A goal of BSR is to make CSR an integral part of business operations and strategies. An illustrative list of BSR's more than 1,000 members includes such well-known companies as ABB Inc., AstraZeneca Plc., Coca-Cola, Johnson & Johnson, Nike Inc., Office Max, GE, GM, UPS, Procter & Gamble, Sony, Staples Inc., and Wal-Mart.

The Business Case for CSR and CSP

After considering the pros and cons of CSR/CSP, most businesses today embrace the idea. In recent years, the "business case" for CSR/CSP has been unfolding. Before buying in to the idea of CSR, many business executives have wanted the "business case" for it further developed. The business case is simply the arguments or rationales as to why businesspeople believe these concepts bring distinct benefits or advantages to companies, specifically, and the business community, generally. Even the astute business guru Michael Porter, who for a long time has extolled the virtues of competitive advantage, has embraced the concept that corporate and social initiatives are intertwined. Porter has argued that companies today ought to invest in CSR as part of their business strategy to become more competitive. Of course, prior to Porter, many CSR academics had been presenting this same argument.

Simon Zadek, a European, has presented four different business rationales for being a civil corporation. These reasons form a composite justification for businesses adopting a CSR/CSP strategy. The first is the defensive approach. This approach is designed to alleviate pain. That is, companies should pursue CSR to avoid the pressures that create costs for them. The second is the cost-benefit approach. This traditional approach holds that firms will undertake those activities that yield a greater benefit than cost. The third is the strategic approach. In this approach, firms will recognize the changing environment and engage in CSR as a part of a deliberate corporate strategy. Finally, the innovation and learning approach is suggested. Here, an active engagement with CSR provides new opportunities to understand the marketplace and enhance organizational learning, which leads to competitive advantage. Most of these rationales have been around for years, but Zadek has presented them as an excellent set of business reasons for pursuing CSR.

Putting forth the business case for CSR requires a careful and comprehensive elucidation of the reasons why companies are seeing that CSR is in their best interests to pursue. Two particular studies have contributed toward building this case. One study by PricewaterhouseCoopers, presented in their 2002 Sustainability Survey Report, identifies the following top 10 reasons why companies are deciding to be more socially responsible:

1. Enhanced reputation
2. Competitive advantage
3. Cost savings
4. Industry trends
5. CEO/board commitment
6. Customer demand
7. SRI demand
8. Top-line growth
9. Shareholder demand
10. Access to capital

A survey conducted by the Aspen Institute, in their Business and Society Program, queried MBA student about attitudes regarding the question of how companies will benefit from fulfilling their social responsibilities. Their responses, in sequence of importance, included the following:

- A better public image/reputation
- Greater customer loyalty
- A more satisfied/productive workforce
- Fewer regulatory or legal problems
- Long-term viability in the marketplace
- A stronger/healthier community
- Increased revenues
- Lower cost of capital
- Easier access to foreign markets

Between these two lists, a comprehensive case for business interest in CSR/CSP is documented. It can be seen how CSR/CSP not only benefits society and stakeholders but also how it provides specific, business-related benefits for business.

Examples of CSR in Practice

There are many ways in which companies may manifest their CSR in their communities and abroad. Most of these initiatives would fall in the category of discretionary, or philanthropic, activities, but some border on improving some ethical situation for the stakeholders with whom they come into contact. Common types of CSR initiatives include corporate contributions (or philanthropy), employee volunteerism, community relations, becoming an outstanding employer for specific employee groups (such as women, older workers, or minorities), making environmental improvements that exceed what is required by law, and so on.

Among the 100 Best Corporate Citizens identified in 2005 by *Business Ethics* magazine, a number of illuminating examples of CSR in practice are provided. Cummins, Inc., of Columbus, Indiana, has reduced diesel engine emissions by 90% and expects that within 10 years the company will be at zero or close to zero emissions. In addition, the engine maker underwrites the development of schools in China, is purchasing biodiverse forest land in Mexico, and funds great architecture in its local community. Cummins also publishes a sustainability report that is available to the public.

Xerox Corporation, Stamford, Connecticut, is a multinational corporation that places high value on its communities. One of its most well-known community development traditions has been its Social Service Leave Program. Employees selected for the program may take a year off with full pay and work for a community nonprofit organization of their choice. The program was begun in 1971, and by 2005, more than 460 employees had been granted leave, translating into about half a million volunteer service hours for the program.

Green Mountain Coffee Roasters, Waterbury, Vermont, was a pioneer in an innovative program designed to help struggling coffee growers by paying them “fair trade” prices, which exceed regular market prices. The company has also been recognized for offering microloans to coffee-growing families and underwriting business ventures that diversify agricultural economies.

Another example of CSR in practice is the Chick-fil-A restaurant chain based in Atlanta, Georgia.

Founder and CEO Truett Cathy has earned an outstanding reputation as a businessman deeply concerned with his employees and communities. Through the WinShape Centre Foundation, funded by Chick-fil-A, the company operates foster homes for more than 120 children, sponsors a summer camp, and has hosted more than 21,000 children since 1985. Chick-fil-A has also sponsored major charity golf tournaments.

In the immediate aftermath of Hurricane Katrina in 2005, judged to be the worst and most expensive ever in terms of destruction, hundreds of companies made significant contributions to the victims and to the cities of New Orleans, Biloxi, Gulfport, and the entire Gulf Coast. These CSR efforts have been noted as one of the important ways by which business can help people and communities in need.

As seen in the examples presented, there are a multitude of ways that companies have manifested their corporate social responsibilities with respect to communities, employees, consumers, competitors, and the natural environment.

CSR in the New Millennium

As we think about the importance of CSR/CSP in the new millennium, it is useful to review the results of the millennium poll on CSR that was sponsored by Environics, International, the Prince of Wales Business Leaders Forum, and the Conference Board. This poll included 1,000 persons in 23 countries on six continents. The results of the poll revealed how important citizens of the world now thought CSR really was. The poll found that in the 21st century, companies would be expected to do all the following: demonstrate their commitment to society's values on social, environmental, and economic goals through their actions; fully insulate society from the negative impacts of company actions; share the benefits of company activities with key stakeholders, as well as shareholders, and demonstrate that the company can be more profitable by doing the right thing. This "doing well by doing good" approach will reassure stakeholders that new behaviors will outlast good intentions. Finally, it was made clear that CSR/CSP is now a global expectation that now requires a comprehensive, strategic response.

—Archie B. Carroll

See also Business for Social Responsibility (BSR); Corporate Accountability; Corporate Citizenship; Corporate Philanthropy; Corporate Social Responsiveness; Social Accountability (SA); Stakeholder Theory; Strategic Corporate Social Responsibility; Triple Bottom Line

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CORPORATE SOCIAL RESPONSIVENESS

Corporate social responsiveness refers to how business organizations and their agents actively interact with and manage their environments. In contrast, corporate social responsibility accentuates the moral obligations that business has to society. Responsiveness and responsibility can be viewed on a means-end continuum in that responsiveness can be shaped or triggered by public expectations of business responsibilities. Generally speaking, these responsibilities are implied by the terms of the social contract, which legitimizes business as an institution with the expectation that it serve the greater good by generating commerce while adhering to society's laws and ethical norms. From this perspective, corporations are in a dynamic relationship with society of which responsiveness is key.

Corporations actively interact with and manage their environments through various programs, policies, and procedures, which are formulated by top managers and carried out by other employees. Ideally, these processes of responsiveness are informed by long-term strategic planning, which starts with an assessment of the firm's external environment from which information about its constituents or stakeholders can be gleaned. To illustrate, this kind of assessment might reveal a trend that society has increased expectations that firms will enhance the quality of life in communities. A more fine-tuned analysis would identify the stakeholders who hold this expectation and the issues of importance to them. This information might prompt a bank to make a commitment to invest in community development projects aligned with the goals of local residents and aimed at generating goodwill befitting public expectations of corporate citizenship. In terms of strategic management, these projects would necessarily reflect the bank's formal policy toward community development carried out by employees in departmental programs guided by specific procedures, such as the criteria for approving loan applications. In this way, an awareness of environmental factors can prompt concrete changes in corporate responsiveness or the ways firms interact with and manage their social relationships.

While responsiveness ideally results from long-term strategic planning, it can also take the form of a more immediate reaction to a crisis. Whether a crisis results from an oil spill, product tampering, or another unexpected event, the conventional wisdom is that corporations should develop the capacity to anticipate emergencies and respond swiftly to the needs of adversely affected stakeholders. The case of Johnson & Johnson Tylenol poisonings has become a classic study of swift crisis responsiveness. In 1982, seven people died after cyanide was added to Tylenol capsules while they were on store shelves, prompting Johnson & Johnson, the maker of the product, to incur hefty expenses by voluntarily recalling and destroying remaining capsules. During this process, James Burke, the chief executive officer, made aggressive use of the media to apprise consumers of the steps that were being taken to address the crises. Shortly thereafter, Johnson & Johnson introduced tamper-resistant packaging as a preventative measure, demonstrating that crisis management involves not only swift responses and effective communication with stakeholders but also organizational learning.

Corporate social responsiveness is defined not only by a firm's policies, programs, and procedures but also by a firm's overall stance toward the environment. A constructive attitude is evident when corporate agents try proactively to anticipate stakeholder concerns and accommodate them whenever possible. That is, corporate managers can direct their firms to learn about the environment in which they operate and be attuned to it. In contrast, firms may exhibit a reactive or defensive posture toward stakeholders or may even neglect social issues altogether. Such attitude is apt to invite unwelcome criticism, unfavorable media coverage, stakeholder pressure tactics such as protests and consumer boycotts, and government intervention and oversight. In the first case, firms seeking to be attuned to stakeholder interests are fulfilling the spirit of the contract between business and society. In the second case of corporate neglect, this implicit contract is violated.

It can be seen that corporate responsiveness is not value neutral, especially since corporate actions impact society in beneficial and harmful ways. For example, benefits to society can accrue when corporations respond to the need for innovative products with research and development that leads to an enhanced quality of life for consumers. On the other hand, harmful impacts can result when corporations neglect their responsibilities, as when they fail to clean up the pollution traceable to their production facilities. The extent to which society encourages benefits and tolerates harms is reflected in the standards embodied in the law, public policy, and government regulation. In this context, business managers and public policy makers can assess or audit the impacts of corporate activity and attempt to direct firms to respond affirmatively to public expectations of responsibility. A cautionary note is that businesses are increasingly exerting influence on the government by political advocacy, which includes lobbying policy makers and contributing financially to their election campaigns. As a result, the link between responsiveness and responsibility is compromised to the extent that this influence results in legislation that favors business interests at the expense of the greater good. Under the terms of the social contract, corporate social responsiveness does not equate to corporations responding to their own rules.

Corporate social responsiveness, corporate social responsibility, and corporate social impacts are encapsulated in the phrase *corporate social performance*. Of these three concepts, responsiveness is the most forward looking, action-oriented, and malleable, since it is based on the precept that corporations have the capacity to anticipate and adapt to environmental factors. The potential is that corporate managers can learn to prevent or minimize the kind of unwelcome surprises that necessitate crisis management and government intervention while responding proactively to public expectations of how business can serve the greater good.

—Diane L. Swanson

See also Business Law; Corporate Accountability; Corporate Citizenship; Corporate Issues Management; Corporate Political Advocacy; Corporate Public Affairs; Corporate Social Responsibility (CSR) and Corporate Social Performance (CSP); Crisis Management; Public Interest; Regulation and Regulatory Agencies; Social Audits; Social Contract Theory; Social Costs; Stakeholder Theory; Tylenol Tampering

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CORRUPTION

Corruption is dishonesty or deliberate dereliction of duty for personal gain by a government official or a private entity official. Corruption broadly includes fraud, bribery, or deliberate misreporting. In a corrupt act, a binding duty is violated by someone who receives an unwarranted personal benefit. To define corruption concretely involves specifying the duty and the personal benefit and why and how the personal benefit is a violation of the duty.

In the case of a government official, corruption is violation of a sworn duty to uphold the public interest. In the case of a private entity official, corruption is violation of a contractual duty to uphold the lawful interests of the entity or its owners. In either circumstance, corruption involves specifically an agent's violation of some duty toward a principal in exchange for private benefits (commonly but not necessarily money). Corruption is typically illegal misconduct. Such dishonesty or dereliction of duty is in any case immoral and socially illegitimate, since it involves an indefensible breach of oath or contract. Citizens and shareowners rightfully expect honest, trustworthy, and loyal agents.

Toke Aidt identifies the essential conditions for corruption as discretionary power, economic rents, and weak institutions or controls. Corruption flourishes in business or government when an actor or group of actors has some degree of monopoly power (often asymmetric information or decision discretion) due to official position to which economic rents can accrue and over which external controls are relatively weak. Asymmetric information suggests secrecy or concealment: Disclosure and transparency is the natural enemy of corruption.

In August 2005, Jack Abramoff, a leading Washington, D.C., lobbyist, and a business partner were indicted on charges of wire fraud and conspiracy in connection with allegedly fraudulent purchase of a fleet of Florida gambling boats. The seller, a Miami businessman, was later killed in a gangland-style hit. Abramoff was also under investigation in connection with political lobbying on behalf of Indian casino interests. In November 2005, Conrad Black, the Canadian former head of the Hollinger International media empire was indicted in the United States with other former officers for allegedly stealing $51.8 million from the company. There has been a lengthy investigation into corruption in the UN oil-for-food program operated as part of the international sanctions against Saddam Hussein's regime in Iraq. The policy goal was to permit Iraq to sell oil for food to be distributed to the population of the embargoed country. An apparent scheme of bribery, allegedly including some UN officials and a large number of non-Iraqi companies, facilitated diversion of funds to Hussein's regime. In November 2005, the U.S. government charged a controller/financial officer for the U.S. occupation authority in Iraq with accepting kickbacks, bribes, and gratuities of at least $200,000 a month. The indicted American, who had served felony fraud prison time, directed construction contracts to another American's three companies. That individual was indicted on various charges.

The Nature of Corruption

Corruption is an ancient and widespread problem—for example, *mordita* ("bite") in Mexico or *baksheesh* ("present") in the Middle East. Baksheesh may cover alms giving, tipping, or gift as well as bribery. Tipping is a widespread commercial practice in the United States (taxi drivers and waiters work partly for tips), but regulated in other situations (i.e., minor gifts to business or government officials). A system of bribery/extortion can be distinguished from customary gift giving well-established in some societies. Traditional business transactions and relationships sometimes involve small gifts and gratuities given or exchanged before or after business. There is, however, a thin line between reward or thanks and bribe or extortion. Each case or situation must be examined on its own merits. A $20 gift of thanks to a helpful official is one thing, a $10 "fee" extorted by a police officer is another thing, and a $1 million bribe or kickback to an individual in connection with a $50 million government contract is quite another thing.

Recent research focuses on the causes and consequences of corruption to evaluate the effectiveness of reform proposals. One can analyze corruption in terms of "supply" and "demand" in a "marketplace." A corrupt payment requires a giver and a recipient. An improper payment may originate as a bribe (offer) on the supply side of benefit (which is the demand side for favors) or as extortion (requirement) on the demand side of benefit (which is the supply side for favors).

One can find in the literature a case for minor corruption as a form of auction for scarce resources (say telephone service or irrigation water) where queuing is unsatisfactory. Corruption can be perhaps a second-best solution for real problems including low wages for officials. Such practices may well lead on to systemic corruption schemes: Officials find an opportunity for corruption rather than a solution to resource allocation and wages.

In the XYZ affair of 1797–1798, French foreign minister Talleyrand refused to receive officially a three-man commission from the United States. Relationships between France and the United States had been strained by the French Revolution and its aftermath. A friend of Talleyrand made indirect suggestions of loans and bribes as a prerequisite for negotiations; discussions were conducted by three intermediaries ("XYZ"). In 1798–1800, for a variety of reasons including the affair, there was an undeclared naval war waged between France and the United States.

Coercive monopoly is suspect in economic theorizing and is ripe for misconduct. Adam Smith's criticism of the British East India Company, in the 1776 publication *Wealth of Nations*, is a description of corruption in a company exploiting quasi-governmental powers in a distant land. Henry (Lord) Acton's 1887 theorem states that power tends to corrupt and absolute power (i.e., monopoly) absolutely. In the present context, "power" might be interpreted broadly as corresponding to the conditions for corruption. Acton focused on executive leadership (kings and popes), but the conditions facilitating corruption may be widespread. Smith commented concerning the British East India Company personnel that his criticism was not personal—virtually anyone else in the same situation likely would have been as opportunistic.

The main anticorruption focus today is on official corruption in government, but corruption occurs in business and households as well. Corruption shades into the grey or underground economy, money laundering, and tax evasion. These forms of misconduct are socially illegitimate deviations from legal or moral obligation.

Business Corruption

One can broadly characterize officer and employee misconduct for personal gain and business-to-business collusions as corruption. There is some evidence suggestive of widespread employee misconduct and also lack of confidence in top management's impartiality. The difficulties of business corruption may be deeply embedded in corporate culture and the relentless drive to make targeted and temporally rising earnings estimates. The drive to lie in business is widespread. The corporate budgetary process arguably turns all participants unavoidably into liars: Everyone learns to game and scheme the system for more compensation. In the first years of the 21st century, following the dot.com bubble bust, there was a sad litany of corporate frauds and scandals—including Nortel (Canada), Parmalat (Italy), and Royal Ahold (the Netherlands). Recent U.S. business scandals (e.g., Enron, Tyco, and WorldCom) are hardly new phenomena.

A corruption perspective on the Enron scandal suggests the following analysis. The top executives of the company were corrupt in the sense of publicly stating high ethical standards while privately lining their own pockets in various ways. This corruption became corporate fraud when the books were cooked. The effect of the scandal—in combination with scandals at other companies—was passage of a new law, the Sarbanes-Oxley Act of 2002. The surprise in the Enron story was the systematic and complete failure of all the conventional corporate watchdogs: analysts, attorneys, auditors, bankers, directors, legislators, and regulators. This situation suggests a kind of corruption machine or process, whether deliberately or inadvertently evolved, in which the watchdogs were suborned in various ways—the private watchdogs by management pressure and dependence on revenues from Enron and the public watchdogs by donations and influence peddling.

The current situation resembles the sudden collapse in 1931–1932 of Samuel Insull's electric utility holding company empire, a collapse destroying the wealth of more than 1 million investors. The debacle helped enact much of the New Deal legislation regulating securities and utilities: the 1933 and 1934 securities acts, the Public Utility Holding Company Act of 1935, and the Federal Power Act of 1935. There are similarities to Enron in the sense of a financial bubble associated with rapid growth in a network industry combined with regulatory laxness.

Developing and Transition Economies

In June 2004, the UN Global Compact added a 10th principle dealing with corruption stating that businesses should work against bribery and extortion. UN General Assembly resolution 55/61 of December 4, 2000, approved the United Nations Convention Against Corruption. UN Secretary-General Kofi Annan commenting on the adoption made the essential case against corruption. It undermines governmental performance, democracy, and citizen morale.

Empirical evidence suggests that corruption in developing and transition countries has strongly negative effects on, respectively, economic growth and foreign direct investment. The great difficulty is, "How to change the course of history?" Corruption is often well-established and conducted by strongly entrenched subsystems or networks. When corruption is widespread in a society or community, individuals do not have sufficient incentives to oppose corruption even if everybody would benefit from the suppression of corruption. This explanation is an illustration of the collective action or free rider problem in the theory of public goods. Clean transactions generate a public good; widespread corruption generates significant negative (costly) externalities.

Transparency International (TI), headquartered in Berlin, Germany, reports annually information on corruption levels by country. The TI corruption information assembles a number of opinion (perception) surveys of knowledgeable individuals from which TI generates its own summary computations. While there may be methodological objections to the TI approach, it gives a rough picture of the corruption situation worldwide. The TI report does not cover all countries: Some Middle East states in particular are generally missing. The "Corruption Perception Index" (CPI) attempts to measure "demand" for corrupt payments: the CPI scale runs from 1.0 = *dirty* to 10.0 = *clean*. There is a rough confidence range around each point-estimate. In general, developing and transition countries fair the worst. Among the 146 countries included in the 2004 CPI report, the following rated below 2.0 beginning with the worst reported and working toward 2.0: Haiti, Bangladesh, Nigeria, Myanmar, Chad, Paraguay, and Azerbaijan. Ukraine rated 2.2 and Russia 2.8 among transition economies. The report states that corruption is rampant in 60 countries (all developing or transition) and that most oil-producing countries are corrupt. There are periodic country and region reports, and in 2003, there was a "Global Corruption Barometer" survey of citizens.

Advanced Economies

There is considerable variability in corruption levels among the advanced economies holding membership in the Organisation for Economic Co-operation and Development (OECD). None reach the low levels of the worst developing and transition economies. However, Italy at 4.8 tied with Hungary and ranked below Taiwan at the 5.6 level. The cleanest countries (8.9 or above) are typically New Zealand, Singapore, Switzerland, and the Scandinavian nations. Germany at 8.2 and Hong Kong at 8.0 both ranked above the United States at 7.5, about the level of Chile. France fell lower at 7.1 and Japan at the 6.9 level.

Criticism in developing and transition economies of the CPI—as stigmatizing those countries, when bribes are paid by multinational corporations—resulted in the "Bribe Payers Index" (BPI). BPI attempts to measure the "supply" of corrupt payments. BPI addresses the propensity of companies from leading exporting countries to pay bribes to senior public officials in surveyed emerging market countries.

In Japan, *dango* is a long institutionalized post–World War II scheme of bid rigging by private companies "competing" for public works contracts and excluding foreign companies from bidding. During 2005, Tokyo prosecutors, on the initiative of the Fair Trade Commission (FTC), raided various companies suspected of collusion in a bid-rigging ring concerning bids for government steel bridge construction orders—worth an estimated $3.2 billion per annum—in violation of the antimonopoly law. More than 40 companies may be involved in a scheme alleged to have operated for over four decades. The construction industry is a strong supporter of the ruling Liberal Democratic Party (LDP). In 2004, the FTC searched offices of firms in steel and heavy machinery industries. Effective 2006, a revision of the law will increase fines and grant immunity to the first firm reporting a bid-rigging scheme. The FTC does not have the support of business or the LDP in the recent crackdown drive.

Commercial and political corruption is an old story in the United States—home of the urban political machine of the late 19th and early 20th centuries. A classic instance was the Tweed Ring in New York City. William Marcy Tweed (1823–1878) became boss of Tammany Hall, the Democratic Party for the city. In the late 1860s, Tweed marshaled city officials, party workers, and contractors into a corruption network. A new city charter (1870) gave the city control of its budget and police. Large debts for contract work marched with kickbacks to Tweed and associates who gained control of city finances. Tweed, for example, received all city printing contracts through his own company. A lavish courthouse project caught public attention. The *New York Times* conducted an investigative campaign, cartoonist Thomas Nast targeted Tweed, and good government reformers ("goos-goos") stood for city offices. Samuel J. Tilden (Democratic candidate for U.S. president in 1876) obtained the conviction of Tweed on a misdemeanor of failing to audit contractor bills for the courthouse, but Tweed actually served only 1 year. The state of New York sued Tweed for more than $6 million. Tweed escaped from jail in 1875 and fled to Cuba and then to Spain, where he was arrested. He died in jail in New York City before the state suit could be tried.

International Collaboration to Combat Corruption

There was widespread corruption in many countries in the early 1970s, despite nearly universal legal prohibition. Some 14 European countries permitted, until recently, corporate tax deductibility of bribes paid abroad. In the wake of the Watergate scandal, when President Richard M. Nixon resigned to avoid impeachment and received a pardon from his successor, there was revelation in the United States of a widespread domestic and foreign pattern of questionable payments. During the 1974 presidential campaign, Nixon campaign operatives broke into the Watergate offices of the Democratic Party in Washington, D.C., and were arrested. Nixon orchestrated an illegal cover-up effort from the White House that included use of cash traced back to U.S. corporations. The investigation discovered that hundreds of American companies had made questionable payments abroad to officials of various countries—including Belgium, Japan, and the Netherlands. The Watergate scandal brought down the administration, resulted in conviction of various individuals including the U.S. attorney general, and resulted in the passage of the Foreign Corrupt Practices Act (FCPA) of 1977. Only Sweden followed the lead of the United States with the 1978 adoption of an antibribery provision.

The 1988 FPCA amendments emphasized international cooperation. The U.S. effort coincided with anticorruption efforts of the International Chamber of Commerce (ICC) and TI. TI, founded by Peter Eigen, formerly of the World Bank, is a coalition of country chapters attempting, sometimes at personal risk, to combat government corruption. A multipronged, sustained campaign by multiple institutions and actors will be necessary, but progress suggests that global norms against bribery/extortion can emerge despite mixed motives and diverse values. There are vital roles for corporate codes of conduct; nongovernmental organizations such ICC and TI; international institutions such as the International Monetary Fund, World Bank, and World Trade Organization; and multilateral anticorruption accords such as those adopted by the Organization for American States (1996), OECD (1997), European Union (1997) (expanding to include transition countries in Central and Eastern Europe, where corruption is rampant), and the Council of Europe (1999). The World Bank pioneered a new approach to controlling corruption through design of the money handling for the Chad-Cameroon Development and Pipeline Project. Chad is one of the most corrupt countries in the TI estimates. The International Anticorruption and Good Governance Act of 2000 concerns U.S. development assistance. A periodic International Anti-Corruption Conference brings together anticorruption government agencies.

—Duane Windsor

See also Agency, Theory of; Alien Tort Claims Act; Disclosure; Enron Corporation; Ethical Imperialism; Externalities; Extortion; Foreign Corrupt Practices Act of 1977 (FCPA); Fraud; International Business Ethics;

International Trade; Organisation for Economic Co-operation and Development (OECD); Public Goods; Sarbanes-Oxley Act of 2002; Side Payments; Transparency International

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COST-BENEFIT ANALYSIS

Cost-benefit analysis (CBA) is a rational choice framework for identifying the best or most profitable option a decision maker can undertake. The decision maker may be a principal (i.e., an individual) or an agent (i.e., management or government) acting for others. The basic logic of CBA is that, for any specific course of action to be adopted, the total expected benefits should exceed the total expected costs to the principal or principals. If expected costs exceed expected benefits, the decision maker should not undertake the proposed action. If expected benefits and expected costs are equal, the principal or principals should be indifferent between the proposed action and the status quo. CBA is in the tradition of consequentialism and teleology. The logic of CBA, applicable with or without money values or other numbers, is to identify and evaluate all the consequences, positive (i.e., for) and negative (i.e., against), of a proposed course of action. The largest net positive change is superior to any alternative, consistently evaluated (qualitatively or quantitatively).

CBA justifies a specific decision computation methodology. In economic theory, reasonably competitive markets ought to lead to these superior outcomes. And these outcomes would be consistent with Pareto efficiency. CBA is a qualitative or quantitative substitute for market exchanges. CBA is, thus, used in circumstances in which markets are less than reasonably competitive, due typically to market failures or intangible considerations. An individual or management might need to weigh effects on reputation of some course of action. CBA is applicable to public goods (such as government investment projects) and setting of governmental regulatory standards. In the Flood Control Act of 1936, the U.S. Congress required for the first time the identification and quantification in dollars of *all* flood control project benefits and costs. Government CBA should maximize gross national product through the most efficient allocation of scarce resources. Government CBA is not, however, a theory of public finance. It is narrowly a public expenditure evaluation approach undertaken without considering the financing alternatives. Some business decisions such as investments in information systems or R&D and many nonprofit entity decisions are not necessarily resolved by discounted cash flow (DCF) estimates.

In a narrowly "economic" CBA, the proposed course of action is the allocation of scarce resources to one competing use rather than to the next best alternative use. The statement "there is no free lunch" expresses this underlying opportunity cost notion. The decision computation methodology estimates a money value equivalent for all the positives and negatives, which can then be summed to a net money gain or loss. This single decision criterion requires a consistent cardinal measurement of all consequences.

A broader "social" CBA decision context reflects incompleteness of cardinal measures (whether money or numbers) and also typically multiple decision criteria. Social CBA compares "apples" and "oranges" (i.e., "incommensurables"). In real decision situations, some benefits and costs may be tangible and measurable in money, while others may be intangible and not measurable in any system of cardinal units. The intangible considerations could arguably outweigh the tangible considerations. These intangible considerations might be ecological sustainability or values grounded in nonconsequentialist ethical perspectives. Social CBA is effectively multiple criteria assessment (MCA). If all relevant criteria concur, then the incommensurable decision problem is solved. Otherwise, the competing criteria must be weighted or prioritized against one another in some manner. The "triple bottom line" and corporate social performance (CSP) measurement are instances of MCA.

The Basic Arithmetic of Cost-Benefit Analysis

The fundamental rule of CBA is to select the alternative (or set of alternatives) that produces the greatest net total benefit (NTB or NB), defined as the positive difference between all benefits and all costs. The basic arithmetic is to sum together computed total benefits (TB or B) and computed total costs (TC or C). If the balance is positive (TB > TC), then the project (i.e., decision or choice) should be undertaken. Maximization of (TB − TC) occurs when marginal benefit equals marginal cost: MB = MC. If the balance is negative (TC > TB), one should stick with the prevailing status quo. If TB = TC, then one is indifferent between change and status quo. This condition is sufficient for making the change. The required condition for undertaking the project is positive net benefits computed as shown:

$$NB = TB - TC > 0 \text{ or } NB = B - C > 0.$$

It has been common practice to use an alternative criterion called the benefit-cost ratio: TB divided by TC. The required condition for undertaking the project is then that the ratio should exceed 1:

$$TB/TC > 1 \text{ or } B/C > 1.$$

In many circumstances, the net benefit criterion and the benefit-cost ratio will yield the same decision outcome and the same relative ranking of multiple projects. However, the two measures are not strictly the same. If any difference arises, then the net benefit computation is automatically correct and the benefit-cost ratio logically must be wrong. More care must be taken with a benefit-cost ratio analysis. A benefit always has a positive sign; a cost always has a negative sign. In the NB computation, one simply sums together positive and negative sign elements. An NB computation is straightforward, because signs are known and any order of considerations is irrelevant to the summation result. With respect to the B/C computation, circumstances might arise in which the sign is not a definitive guide as to whether a consideration belongs in the numerator or the denominator, and the placement of considerations in the numerator or the denominator is fundamental to the division outcome. For example, where corrective action reduces some but not all environmental damage, should one think of the remaining damage as a reduction from benefit (in the numerator) or an addition to cost (in the denominator)?

Ethical Limitations and Criticisms of CBA

Economic CBA reflects a strictly utilitarian orientation to consequentialism. Utilitarianism is the ethical doctrine of the greatest good (i.e., net benefit) for the greatest number of people. Moral objections to CBA can be aimed at consequentialism, utilitarianism, or misconduct in CBA estimations. Pareto efficiency requires that net gain to at least one person impose no uncompensated harm on any other person, as in eminent domain acquisition of private property at fair market value. The weaker Kaldor-Hicks criterion often invoked in CBA substitutes "hypothetical compensation": Net gain to one party outweighing net loss to another party is justified on the basis that the winner(s) could potentially compensate the loser(s). Economic CBA is just one approach to decision making that is narrowly suitable for tangible, objectively quantifiable parameters occurring within reasonable probability ranges.

Intangible considerations, such as risk to environment or human life, can cause significant debates. A difficult aspect of CBA is valuation of human life and limb. In the early 1970s, Ford Motor subjected its Pinto subcompact auto to a monetary CBA conducted in accord with federally approved methodology. The

CBA found that it was not socially worthwhile to fix a known design defect (costing perhaps no more than $11 a vehicle), which permitted the gas tank to explode when struck from behind. The cost of fixing the entire production run of 12.5 million vehicles would be about $137 million. Valuing a life at $200,000 (for 180 lives), each serious burn injury at $67,000 (for 180 serious injuries), and property loss in vehicles at $700 each (for 2,100 cars), the benefits to society of fixing the Pinto model weighed in at $49.53 million—less than half the cost of the fix. The defective assumption in the CBA was the low value assigned to a human life. A jury trial determined that burn injuries, under these conditions, should be valued at $6.6 million. The Pinto example reveals technical flaws in CBA (undervaluation of life and limb), underestimation of legal reaction (the jury's findings), and arguably ethical myopia.

Pankaj Ghemawat argues that a rule or principle necessarily replaces rather than supplements CBA. A CBA involves trade-offs of pro and con value considerations, whether computed quantitatively or judged qualitatively. Ghemawat argues that strategic choices (i.e., resource-intensive commitments) must always reflect CBA (i.e., consequentialism) in some form. Steven Kelman argues that, in areas such as environment or safety and health regulation, a decision may be right even if benefits do not exceed costs; and further that it is not always appropriate to place dollar values on nonmarketed benefits and costs. A rule or principle must sometimes supersede CBA calculations.

The U.S. Environmental Protection Agency has proposed a standard for permissible level of arsenic in drinking water. Cass Sunstein points out that science can presently provide only wide benefit ranges for this standard. He suggests a range of 0 to 112 lives saved, equivalent to a range of $0 to $560 million in monetized benefits. One ethical position is that a life saved cannot be subjected to money valuation. Another ethical position is that, as a hypothetical estimate for illustration, several billion dollars in costs to save 112 lives worth $560 million would be unjustifiable—even admitting the possibility of significant undervaluation of the benefits.

Ethical difficulties in CBA can arise through the decision maker taking an inappropriately narrow or self-interested focus. For example, the decision maker ignores broader considerations or shifts costs to some other party as in the "tragedy of the commons." Decision makers may manipulate various aspects of the CBA computation methodology to inflate benefits or deflate costs. Ethical issues of equity, fairness, and honesty arise in such instances. Where the decision maker is not the owner of rights to benefits and costs, moral hazards of agency can arise.

Estimation and Distribution of Consequences

A typical use of CBA addresses government budgeting for "public goods" that will not be supplied optimally by the market economy. A public good is an extreme case of externalities (i.e., noninternalized side effects), combining nonrival consumption and nonexclusion by price. The government must undertake to estimate consumers' willingness to pay and the true opportunity cost of public good provision. The rationale for CBA is economic efficiency—society should seek optimal resource allocation to maximize society's economic welfare.

The CBA rationale draws on the theory of welfare economics under perfect competition: ideal welfare pricing is P = MC = AC, or price = marginal cost = average cost, for zero economic profit (defined as any profit in excess of ordinary or competitive profit). The government should price outputs and inputs at competitive conditions and ignore monopoly pricing distortions. It also should assume full employment of resources and price all externalities and repercussions of a course of action.

CBA must properly include all social benefits and all social costs, including nonpecuniary (i.e., real) externalities translated into dollar values but excluding pecuniary externalities already occurring as dollar values. A project or decision has both direct effects—the benefits and costs—and what one can classify as indirect effects or repercussions. An externality—positive or negative—is an effect on another party. In CBA, nonpecuniary externalities must, in principle, be incorporated. For example, if a dam is constructed to provide water supply for irrigation farming, one can compute the benefits and costs of the dam. Suppose that in addition the dam endangers a unique species of fish. The dollar value of the loss of that species must be accounted for in computing the worth of the project: the loss is a negative externality that must be internalized in the decision, reducing the net worth of the project. In principle, positive externalities—such as an increase in an endangered tree species now assisted by irrigation water—must be added to the net benefit side. All nonpecuniary externalities must be identified and quantified, in principle.

A pecuniary externality—positive or negative—is a change in the nominal price of an existing asset or resource. For example, land along the lake created by the dam may rise in value; land downstream of the dam may fall in value. These price changes are not benefits or costs of the project.

Income to the farmers is not a benefit of the project. The test for social benefits is consumers' willingness to pay (i.e., demand) for the outputs of the project. Willingness to pay, in economics, is the sum of the actual price consumers must bear and what is called consumers' surplus, which is what a monopolist practicing perfect price discrimination would be able to obtain. Technically, the net benefit of a project is the consumers' surplus, in the sense that willingness to pay is the sum of benefits and actual price is the sum of costs. A cost saving can be a form of benefit—a cost reduction is the same as a benefit increase.

Distribution of wealth is a different consideration. Transfer payments merely redistribute existing output. CBA deals with generation of additional output. Output value is computed before taxes, which are simply a form of transfer payment, unless taxes are levied by an external entity, such as another country; in that instance, taxes become a reduction of net national wealth. One can address distribution issues by attachment of judgmental weights (labeled w_i below), which must be derived by political processes or by ethical judgments:

$$\mathrm{NTB} = w_1\mathrm{NB}_1 + \ldots + w_n\mathrm{NB}_n.$$

Time Stream Evaluation

The arithmetic above has proceeded as if the benefits and costs of a proposed course of action occurred within a single time period. Time stream evaluation refers to the circumstance when consequences occur over two or more time periods. Benefits and costs must be discounted to present values. The logic of CBA becomes that, over some appropriate time horizon, the sum of all relevant present value benefits should exceed or at least equal the sum of all relevant present value opportunity costs. The basics of this net present value (NPV) determination are covered in the entry on "Discounting the Future." A vital concern in discounting, covered fully in that entry, is the conservation of nonrenewable resources for future generations, to whom present generations arguably owe definable moral duties. Intergenerational equity is an important issue in time stream evaluation.

NB, B, and C can represent simple one-period estimates. Benefits and costs may have been recomputed to present values, meaning that multiple time periods have been reduced to a single time period (the present time period) through discounting. With time stream evaluation, NB becomes NPV. The mathematics for time stream evaluation takes the following general form for computation:

$$\mathrm{NPV} = -K_0 + \sum_{t=1}^{n} \frac{\mathrm{B}_t - \mathrm{C}_t}{(1+r)^t} > 0.$$

In this particular formula, NPV is the net present value; K is an initial (capital) investment (i.e., a fixed cost) occurring at the beginning of the project (time period 0 indicated by subscript), t is each specific time period, n is the number of time periods, B is the stream of benefits occurring over time, C is the stream of costs occurring over time (after the initial investment), and r is the discount (or interest) rate applied (uniformly in this example) to each time period. The formula has the effect of increasingly reducing the nominal value of B and C over time.

One can compute the internal rate of return (IRR) of a project, defined as the discount or interest rate at which the present value of benefits is precisely equal to the present value of costs: $[\mathrm{B}(r) = \mathrm{C}(r)]$. The IRR reveals the breakeven point of the project. In the case of time stream evaluation, the IRR can yield what mathematicians call multiple solutions (i.e., roots to a quadratic equation), so that it is difficult to compare competing projects.

NPV is highly sensitive to discount rate. A low rate approves more projects; a high rate approves fewer projects. There are several schools of thought on the appropriate discount rate for government projects: (1) government long-term bond rate reflecting low risk, (2) a social rate of time preference lower than social opportunity cost, (3) a social opportunity cost equal to the private sector rate of return on investment, or (4) some weighted average of the social rate of time preference and the social opportunity cost. Theoretical choice of discount rate tends to reflect liberal (low) versus conservative (high) preferences concerning size of government (large for liberals, small for conservatives).

Relationship of CBA to DCF

The NPV formula looks superficially to be the same formula as used in a DCF analysis. The general mathematical form is the same: both NPV and DCF deal with time stream evaluation problems and the mathematical formula is logically the same treatment.

CBA is a balance sheet rather than a cash flow or profit-loss framework. CBA maximizes net benefits (i.e., gain) on the balance sheet of an individual, group, or entity. Benefits are new assets. Opportunity costs are existing assets (or resources) diverted (i.e., given up) to "production" of the new assets. If the net worth of the balance sheet would increase, that diversion should occur. A cash flow analysis might reflect monopoly restrictions and/or unemployment conditions. Businesses typically use DCF because maximizing free (i.e., net positive) cash flows in markets automatically provides the balance sheet solution.

A Multiple Criteria Assessment Example

Due to rising energy demand and prices (which in fact tend to fluctuate considerably), there have been unsuccessful efforts to build a natural gas pipeline from Alaska's North Slope to the continental United States. The Alaska Natural Gas Transportation Act of 1976 established a special decision-making process involving the president and the Congress as well as the Federal Power Commission in selection of the system and routing. The act required consideration of multiple environmental, safety, diplomatic, national security, financing, competition, economic, and energy dimensions. A proposal for an LNG system (liquefying gas at Valdez, Alaska, and deliquefying gas in southern California at an earthquake-prone site) was eliminated on qualitative environmental, security, and diplomatic considerations. Two overland projects were subjected to quantitative CBA at both commercial (10%) and government (6%) discount rates. One proposal showed somewhat higher net national economic benefit on both discounting procedures. It would finish earlier, use existing utility corridors, and risk less environment damage; it would not tap another gas field in Canada. The project was never built, because private investment is highly sensitive to the projected price of gas, which declined, and to the problem of government guarantees for the risk of the investment. A presently pending proposal is another LNG system originating at Valdez.

—Duane Windsor

See also Consequentialist Ethical Systems; Discounting the Future; Ford Pinto; Gross National Product (GNP); Moral Hazard; Net Present Value; Opportunity Cost; Pareto Efficiency; Public Goods; Rational Choice Theory; Regulation and Regulatory Agencies; Surplus, Consumer and Producer; Tragedy of the Commons; Triple Bottom Line; Utilitarianism; Welfare Economics

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Council of Economic Advisers

The Council of Economic Advisers (CEA) is a body within the executive branch of the United States government comprising three professional members appointed by the president with the consent of the Senate and whose duties and functions are (1) to assist and advise in the preparation of the annual Economic Report of the President; (2) to gather and analyze information concerning economic developments and economic trends and to compile and submit studies relating to these developments and trends; (3) to appraise the programs and policies of the federal government; (4) to develop and recommend national economic policies to foster and promote free market, competitive enterprise, to avoid economic fluctuations or to diminish the effects thereof, and to maintain employment, production, and purchasing power; and (5) to make and furnish such studies, reports, and recommendations with respect to matters of federal economic policy and legislation as the president may request.

The Council and its duties were created by the Employment Act of 1946, signed into law on February 20, 1946, by President Harry S. Truman, who had great hopes for the act and thought its value would be long-standing and significant. This act also created the Joint Economic Committee of the Congress. The legislation was stimulated by two major considerations. The first, a holdover from the Depression era of the 1930s, was the practical concern that a peacetime economy may not reach full employment, and the second, the influence of John Maynard Keynes's development of macroeconomic theory, which purports to show that as a matter of theory free market economies may settle at below full-employment equilibria and therefore his policy prescription that government stimulus is necessary to push the economy toward full employment.

This legislation created the CEA as a formal institution to advise the president. Prior to this time economic advice was given by different agencies, for example, the Treasury, the Department of Agriculture, and/or the Federal Reserve or individuals brought into the president's circle on an ad hoc basis.

This type of "employment" legislation, which, in earlier versions in the United States at least, contained specific targets and goals for macroeconomic variables such as the unemployment rate, was a feature of post-War Western economies, being preceded by several similar Keynesian-inspired recommendations in the United Kingdom, including the Beveridge Report (1943) advocating heavy government influence in the economy and the British government's White Paper on Employment Policy (1944), which committed the government to organize its post–World War II budget policies with a focus on Keynesian full-employment objectives.

Other Western governments brought forth similar papers, with Australia releasing its "Full Employment White Paper of 1944" and Canada its "White Paper on Employment and Income of 1945," outlining the government's intention to adopt Keynesian economic policies to maintaining a high level of employment and income.

In its early years, the CEA was staffed by economists sympathetic to the Keynesian view, such as Edwin Nourse, Leon Keyserling, and Gerhard Colm. By the 1960s and the Kennedy administration, the CEA was composed of prominent Keynesians with Walter Heller, Kermit Gordon, and James Tobin in the CEA seats and Paul Samuelson, John Kenneth Galbraith, Arthur Okun, and Seymour Harris in the background.

By design the CEA is a neutral agency without ties to a particular constituency and most often headed and staffed by economists on leave from other professional positions (usually academic). This provides an opportunity for new theoretical and applied research to be brought to bear on policy questions. The relatively short-term nature of the appointments, for example, there were four different chairs during the eight-year Clinton presidency, dissuades any particular person from empire building and becoming entrenched in an insulating bureaucracy. It is hoped that this allows the Council to impartially give the best advice of the day. However, this neutrality has not prevented controversy, for example, early on Chairman Nourse and Council member Keyserling clashed repeatedly over their view of the Council's public and private roles.

More recently, the Council has been criticized for writing on matters that may not pertain strictly to the economic. For example, in 2005, the National Security Council reportedly excised a chapter on Iraq's financial system from that year's Economic Report of the President. The CEA has also served as a seeming "testing ground" for further governmental service with, among others, Arthur Burns, Allan Greenspan, and Ben Bernanke all serving stints as chair of the CEA prior to becoming (not necessarily under the same president) chair of the board of governors of the Federal Reserve Board, a more influential and longer-term position.

—David L. Hammes

See also Advisory Panels and Committees; Free Market; Impartiality

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Council on Foreign Relations

While a nonpartisan and independent membership organization, the Council on Foreign Relations (CFR) is one of the United States' most influential policy groups. CFR leaders have strong ties to government, business, media, military, think tanks, foundations, academia, and other key entities. Membership is invited (more than 3,000), and those active in the Council are also commonly found in other such organizations (Bildeberg Group, Bohemian Club, Trilateral Commission, Project for the New American Century, etc.).

Such interlocking membership invariably has created a powerful and intricate web of influence, cutting across both liberal and neoconservative ideologies. Generally speaking, the Council has supported international initiatives and favored globalist collaboration, as compared with noninterventionist policies and independent national sovereignty. Both supporters and critics agree that since its founding in 1921 through support of J. P. Morgan & Co., CFR members have held a succession of high-level positions in every presidential administration, irrespective of party. Founding members included Morgan, Colonel Edward M. House (adviser to President Wilson), John D. Rockefeller, Paul Warburg, Otto Kahn, Jacob Schiff, and other internationalists who had earlier worked to establish the Federal Reserve System as America's national bank. The organization grew so much in stature that dating from the Franklin D. Roosevelt era up to the present, practically every secretary of state, secretary of defense, and secretary of the treasury has been recruited from the CFR. In the 2004 election, for example, whether Bush or Kerry won did not matter in one key aspect—there would still be around 400 members of the CFR in either administration. Not surprisingly, ideas promulgated in *Foreign Affairs*, the CFR's quarterly journal of global politics, as well in its numerous reports and books often become U.S. government policy.

The CFR is headquartered in New York with an office in Washington, D.C. Throughout the year, the Council hosts a number of meetings where world leaders, government officials, scholars, journalists, and other foreign policy specialists discuss and debate the major foreign policy issues of our time. Some sessions are off-the-record, while transcripts of on-the-record events are posted on the Council's Web site.

Because of its focus and influence, the Council has been controversial. Proponents argue that through Council forums, policies that reflect public good and the public interest evolve. Opponents present a difference case—that CFR's efforts are internationalist to the point that members would prefer world government to national sovereignty. Irrespective of impact, there is no doubt that Council members do help set as well as implement the foreign policy agenda of the United States. They do not simply analyze and interpret foreign issues, they help determine what is discussed and decided.

A major ethical issue involves whether or not holding "confidential" gatherings by power wielders under the aegis of a private organization is consistent with proper conduct in a free country. Democratic accountability is not an easy process. Nevertheless, openness and transparency are generally more desirable than covert closed-door decision making from the point of view of those influenced.

—Richard Alan Nelson

See also Bilderberg Group; Trilateral Commission

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Cowboy Capitalism

Cowboy capitalism is a term used, primarily by its critics, to describe the free market elements of the American (and, less often, the "Anglo-Saxon") economy. It has been contrasted both with socialism and with modern European "comfy" capitalism. An ongoing debate persists in business ethics circles concerning whether such a free market is morally good or morally bankrupt.

Cowboy capitalism has been likened to shareholder capitalism, where firms experience constant pressure from investors to maximize profits and focus on financial results. A theoretical foundation of this view is the efficient markets hypothesis, which holds that free markets are the ultimate, efficient arbiters of the economic goods in a society. This economic system is often characterized by numerous entrepreneurial startups and bankruptcies, as well as by frequent mergers, acquisitions, and leveraged buyouts. Individuals are encouraged to strive and to pursue their own self-interest, which some argue constitutes satisfying their own greed without restraint.

A hallmark of cowboy capitalism is the laissez-faire relationship between business and government. It is characterized by economic freedom and lower taxes for both businesses and individuals. The government associated with this economic system tends to remain small and noninterventionist, even in the cases of business trusts and mergers and acquisitions. However, some argue that political corruption is endemic in such systems, as businesses may bribe government officials to keep potential regulation at bay.

The long-term consequences of cowboy capitalism have proven to be very high standards of living, very low levels of unemployment, and unprecedented levels of productivity and per capita gross national product. These consequences are often claimed to be products of Adam Smith's invisible hand, which he argued enables the pursuit of individual interests to lead to the greatest macroeconomic output. Advocates argue that these gains have been made despite governmental regulation and interference. Critics, however, claim that it is precisely these regulations and social programs that have stimulated economies by putting money into consumers' pockets. They also focus on the variable distribution of wealth in such an economy, claiming that the system is morally indifferent to its less able or less fortunate members. In addition, firms have no guarantee of survival, nor workers of ongoing employment.

Opinions vary concerning the origins of the term. Some argue that it characterizes a cowboy's tendency to shoot first and think later, while others believe it symbolizes participants' thirst to win the competitive struggle presented by business. Still others go to the extreme of claiming that it means "doing in" rivals so that they can no longer compete.

Icons of cowboy capitalism differ among supporters and critics. Supporters would point to Ronald Reagan (on a horse) and to Reaganomics, as well as to the city that has been called the capital of cowboy capitalism—Houston, Texas, particularly during the 1980s' oil boom. Critics, in contrast, would focus on scandal-riddled Enron, modern Russia, and Eastern European markets after the breakup of the Soviet Union and before the rule of law. Even supporters acknowledge that the concept has sometimes been taken to extremes. Marianne Jennings has likened the Yeehaw culture of Enron and other scandal-ridden firms to distortions of cowboy capitalism.

—Lori Verstegen Ryan

See also Cato Institute; Freedom and Liberty; Free Market; Friedman, Milton; Hayek, Friedrich A.; Individualism; Libertarianism; Mergers, Acquisitions, and Takeovers; Nozick, Robert; Rand, Ayn; Self-Interest; Smith, Adam; Wealth Creation

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Crisis Management

The field of crisis management (CM) attempts to mitigate the losses incurred when a crisis occurs and to prevent crises that could occur in the future. An organizational crisis is defined as a low-probability but high-impact event that threatens an organization's existence by disrupting its normal operations and its social legitimacy. An organizational crisis can be distinguished from a natural disaster in that it implies human responsibility; furthermore, it is a highly complex event, both in terms of its genesis and its consequences.

First developed in the field of political science, the theory and practice of CM is today shaped by scholars from many disciplines, as diverse as administrative sciences, systems theory, risk management, positive psychology, and ethics. Gerald Mars and David Weir have rendered a great service to CM theory with their two compilations of papers by some of the most important authors in the field. CM is traditionally divided into two schools. The first, called *high reliability theory,* argues for the feasibility of designing systems that protect against crises and ensure organizational safety through the use of mechanisms such as centralization of decision making, redundancies, and downsizing of scales. The second school of thought, called *normal accident theory,* argues that while prevention can be achieved in relatively simple environments, crises cannot be adequately prevented and controlled in other more tightly coupled and complex environments, such as in the nuclear energy industry. Thus, this theory calls for such uncontrollable activities to be banned altogether.

The Crisis Management Model

Many scholars and practitioners consider the management of the Tylenol crisis by Johnson & Johnson (J&J) to be the prototypical example of efficient and ethical CM. In 1982 and 1986, the capsules of extra-strength Tylenol had been tampered with cyanide, leading to the death of six people in the first case and one in the second case. Even though J&J was exonerated of any wrongdoings, since the products were tampered with in the market place and not in the company's facilities or its distribution network, J&J reacted quickly and responsively and recalled 31 million Tylenol bottles—a retail value of more than $100 million. This case has been extremely influential on both CM practice and theory and has led to a checklist of what to do in the case of a crisis. Many observers have praised (1) J&J's quick response and actions; (2) the company's lack of defensiveness and acknowledgment of its responsibility to protect the public; (3) its recall of enormous quantities of product at great cost; (4) its extensive public relations campaign; (5) its redesign of the product, including the tamper-resistant triple-seal now standard in the industry; and (6) its effective defence of its brand name, corporate reputation, market shares, and stock price. J&J's response certainly stands out when compared with less successful CM interventions, such as Union Carbide's Bhopal disaster, the *Exxon-Valdez* oil spill, the Perrier water contamination incident, or the Three Mile Island nuclear accident. In addition to the points mentioned above, experts often attribute J&J's effective response to the company's mission statement, which stresses its ethical responsibility toward all its stakeholders, and the efficient and caring leadership of James E. Burke, then chairman of the board of McLean, which produces Tylenol.

But while J&J's response was clearly efficient, the Tylenol case is not as positive from an ethical point of view. Inquiries have revealed, for example, that drugs similar to Tylenol, such as aspirin, had already been tampered with on several occasions using deadly substances, such as cyanide or arsenic, many decades *before* the Tylenol crises. In one case in Switzerland, a mentally disturbed nurse added poison to the drugs used at her hospital. When these past incidents are taken into account, the question is no longer whether or not J&J reacted in a responsible manner: It did. The deeper ethical question becomes, why didn't J&J better protect its Tylenol products *before* these crises?

Two frequent objections are often raised when this question is asked. The first is that these tampering incidents had been rare in the past. But this is the essential point of CM: A crisis is, by definition, a low-probability but high-impact event that necessitates action by an organization if it is to be financially and ethically responsible toward its stakeholders. The second objection is that J&J was not aware of previous tampering and thus could not have imagined such a tragic situation. As we will see later, an ethically based CM approach requires a different kind of *moral maturity*, as well as a different kind of *ethical inquiry*. There is no doubt that J&J and its affiliated companies, which together control about 32% of the market, have dedicated significant resources to the R&D of the drug, including its potential side effects, and to its promotion and distribution. However, a more ethical strategy would have included a thorough evaluation of the potential crises that could arise and the implementation of various preventive actions.

This relatively low level of moral maturity and ethical inquiry is not unique to the J&J case. The tragedy of Nestlé's commercialization of its powdered milk product in Africa, which has tarnished the company's reputation to this day, is another example. During the 1970s and 1980s, thousands of African women, charmed by this new Western product, purchased the powdered milk and mixed it with the water they had available. Unfortunately, this water was often contaminated and the product led to the deaths of several thousand infants. Nestlé claimed for years that its product was perfectly safe and not to blame; the company further insisted that it was not doing anything illegal and that its packaging indicated that potentially unsafe water should be boiled prior to use. It ultimately took an order of the World Health Organization, after much lobbying by different activist groups, for the company to withdraw its product. In this case, Nestlé lacked moral maturity: It could not understand that its *good* product could become *lethal* when used by people with little to no education or reading ability in an environment such as in Africa where clean drinking water is not universally available. Furthermore, Nestlé failed to adopt an ethical approach, that is, really empathizing with the thousands of dying children and recognizing the tragedies experienced by their families; instead, the company was blinded by other issues, including technical, financial, and legal considerations. The Nestlé case is clearly more tragic that the J&J one.

While both companies lacked moral maturity and ethical inquiry, at least J&J didn't wait for an order from an external body before modifying its strategies. In comparison with the Nestlé example, the Tylenol incident is a good example of efficient and responsible *reactive* CM. However, both companies were not able to integrate the "four families of crises," as suggested in the CM literature. If they addressed the issues of (1) economic attacks and (2) informational attacks, they were less successful at addressing the issue of (3) product breakdown (J&J had even to wait for its second 1986 crisis before abandoning the production of its capsules, which were more vulnerable to tampering than tablets) and (4) psychosocial crises, including harm to stakeholders. In a similar vein, both companies did relatively well in two of the families of CM actions, that is, (1) technical audit and (2) structural design, but did poorly in the two others, that is, (3) internal emotional preparation and (4) external communications, while J&J did better than Nestlé in this last area.

Moral Maturity and Ethical Inquiry in Crisis Management

Many ethical frameworks, theories, or traditions are ill-suited for dealing with the complexity of crises. For example, the utilitarian framework, which is widely used in organizations and favors the well-being of the greatest number of people, could have lead to the decision to keep Nestlé's powdered milk in Africa if it could have been demonstrated that more people benefited from this product than suffered from it. Likewise, the use of legal frameworks could excuse both Nestlé and J&J in these two cases, as neither company broke the law.

Recognizing the complexity of real-life situations, several philosophers and theologians have proposed that an ethical framework should reflect at least three considerations: (1) it should address the reality of a problem, conflict, or crisis, and not just follow abstract principles; (2) it should be grounded in dialogue, open to conflicting ideas and paradoxes, which requires moral maturity to look beyond conventional norms and values on the part of both individuals and communities; and (3) it should proceed by deliberate ethical inquiry, testing the decisions made and the actions taken, considering them as working hypotheses rather than firm policies.

Two ethical frameworks that adopt this type of moral maturity and spirit are the *pragmatic democracy*, developed by the philosopher John Dewey, and the *systematic theology*, developed by the theologian Paul Tillich. Dewey emphasizes the notions of democracy, constant experimentation, and testing. He wishes to bring about a "collective intelligence" through the personal development of individuals and the encouragement of moral thinking in education. Central to Dewey's ethical system is the sympathetic regard for the intelligence and personality of others, even if their views are different, as well as the testing of ideas through scientific inquiry. Dewey is particularly against the use of prejudice, partisanship, checklists, or even traditionally accepted views and practices in ethics, striving instead for what can be called a "postconventional outlook," which is always in emergence.

In similar fashion, Tillich emphasizes that a moral life requires the existential courage to profoundly come to terms with one's own self, as well as with others. For him, one must have the courage to "accept acceptance," that is, the acceptance of one's mortality, of the ambiguous nature of one's work—leading potentially to success or crises—and of the recognition of one's very small place in the cosmos. For Tillich, it is essential to realize that all the genuine religions and spiritual traditions of the world had integrated both the positive and negative sides of life, calling the latter by different names: the devil, Hecate, Kali, the false, the bad, the ugly, Satan, Rakshasa, Thanatos, the *via negativa*, and so on.

It is very probable that if Nestlé and J&J had adopted one of these two ethical frameworks (among the many others that exist as well), the handling of their crises would have been different. In the case of Nestlé, the acceptance of the fact that its product could also have negative impacts might have helped the company to overcome its defensiveness and seek some creative solutions with the local populations. In the case of J&J, this sort of acceptance could have triggered a deliberate investigation into the potential dangers of its Tylenol product *prior* to the crises, leading to the implementation of preventive strategies. Furthermore, the use of such ethical frameworks would have probably widened the range of issues and increased the number of people considered to be important in both cases. For Nestlé, the Western-oriented financial and legal approach could have been complemented with a more African-oriented social and ecological view of the problem. For J&J, the possible impact of potential saboteurs, terrorists, and psychopaths could have been better integrated into the organization's CM strategy.

Increased levels of moral maturity and ethical inquiry could also enrich the two dominant theories in CM. *High reliability theory* could gain from not only pursuing safety but also considering more profoundly the moral grounds of an organization's operations. After all, the Mafia could be made "highly reliable" but this will not increase its level of morality. Also, while the *normal accident theory* leads to the conclusion that some activities are too complex to be carried out safely, it would gain from the addition of existential considerations to the administrative, sociological, and technological factors that it traditionally takes into account. This would help employees, executives, and policy makers to adopt a "postconventional view" and to better "accept acceptance," thus adopting a more proactive and preventive approach to their activities.

Some scholars have already adopted this more dialectical and ethical view of CM by exploring two related issues: (1) the developmental nature of a crisis itself for individuals and organizations, viewing a crisis as a potential "crucible" event, triggering learning and change; and (2) the exploration of ways to develop a more mature level of morality and inquiry in organizations by means other than the experience of a major crisis. We may be witnessing today the birth of a third major theoretical foundation in the field of CM, one that is grounded in moral development, both for individuals and organizations.

—Thierry C. Pauchant,
Caroline Coulombe, and Joé T. Martineau

See also Legal Ethics; Pragmatism; Utilitarianism

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Cross-Cultural Consumer Marketing

Marketing activities that originate in Western countries span the globe and reach many cultures. Questions of cross-cultural ethics arise when marketing practices that are acceptable in one country are inappropriate in another.

Consumer marketing, which is impersonal and directed at a mass audience, may be distinguished from relationship marketing, which is based on personal contacts. This is an important distinction because many of the cross-cultural problems surrounding consumer marketing arise precisely because much of the world has traditionally relied on relationship marketing.

World cultures tend to be either rule based or relationship based. Rule-based Western cultures rely on a legal or regulatory system to enforce what are seen as universal rules of fairness. Non-Western norms tend to place human relationships at the center of things. While relationship marketing developed in both kinds of cultures, consumer marketing is very much a product of the West and is an inherently foreign practice in relationship-oriented cultures. Even relationship marketing is done differently in the two kinds of cultures. These differences can present ethical challenges.

Consumer Marketing in Relationship-Oriented Societies

Impersonal consumer marketing requires consumers to trust products and believe advertisements created by strangers, which is unnatural for people who traditionally place their trust in friends and family rather than on an economic or legal system. As a result, consumers may have neither the skills necessary to identify safe and effective products nor a functional legal system that regulates them. Global firms may find it legal and possible to sell dangerous pesticides, high-tar cigarettes, unwholesome baby food, or unsafe equipment that would be unmarketable in some Western countries.

Mass marketing can also inject culturally inappropriate products, prices, and promotion into local cultures. "Morning after" pills may become available in strongly Roman Catholic countries, or the market prices of life-saving drugs may be far beyond the means of most people in economically less developed countries. Advertisements may contain sexual material or portray disrespect for parental authority that is frowned on locally. Conversely, local custom can draw multinational enterprises into supporting practices contrary to their own values. Ultrasound machines may be used locally to identify unborn female babies for abortion and donated organs may be reserved for high-status individuals.

Relationship Marketing

Even relationship marketing differs in rule-oriented and relationship-oriented cultures. Non-Western business cultures typically value loyalty to one's associates, boss, or company. Suppose, for example, that a Western purchasing agent has been interacting with Asian suppliers but changes jobs. The Asian partners may view the agent as immoral for failing to follow through on personal commitments, even though his or her departure from the company may be perfectly normal from a Western point of view.

Western business culture, on the other hand, typically values playing by the rules more highly than personal loyalty. Asian businesspeople, for example, may respect intellectual property obtained from Westerner business partners with whom they have a long-term personal relationship, but they may feel free to use it for their own purposes when there is no such relationship. To the Western mind, relationships are irrelevant when it comes to law.

Addressing Cultural Difference

One approach to accommodating cultural difference is to try to design a single product or promotion that is compatible with a wide range of markets. A growing trend, however, is to do the opposite. Although global communication and distribution technologies are often viewed as a force for homogenization, they actually reinforce regional differences. Multiple cable and satellite channels enable regionally specific programming, and direct advertising through the Internet reaches highly refined market segments. Sophisticated manufacturing plants and supply chains fill highly customized orders on a global scale. It is rapidly becoming possible for marketers to respect local cultural norms wherever they do business.

—John Hooker

See also *Guanxi*; Marketing, Ethics of; Multiculturalism; Side Payments

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Cross-Subsidization

Cross-subsidization is the organizational practice that uses a portion of revenue from some customers and applies it toward costs undertaken in activities for other customers. With cross-subsidies, a business may charge some customers more than the amount it requires to serve them so that its other customers can pay less. Managers who can subsidize across customer groups are able to achieve an overall business profitability that remains constant even while undertaking less profitable activities for some customer groups. Holding companies and diversified corporations are organizational forms that enable cross-subsidization as a path to competitive advantage.

Corporate Social Responsibility View

Government may subsidize the costs of some activities or segments in society. This often takes the form of taxation and redistribution of social wealth and resources to support public or political policies whose beneficiaries do not pay their full share of costs. Some advocates of corporate social responsibility may view cross-subsidization similarly as a means for business to finance socially desirable activities that otherwise may not be sufficiently profitable to undertake.

Cross-Subsidization Examples

A home builder may construct two types of houses—a large, finely crafted home for wealthy families and a small, basic home for low-income families—and use some of the premium price from the luxury homes toward the costs of constructing the low-end houses. This sort of cross-subsidization allows the builder to meet an overall profitability objective while simultaneously reducing the price of homes for low-income buyers.

Cross-subsidization, however, may not be the most socially effective means to respond to the housing needs of low-income families. The obstacle to effectiveness arises from the impact on the price information used for decision making. First, if people in the market for a luxury home are given a choice, then, rather than be altruistic, they may purchase from a builder who does not add a subsidy premium to their price. With buyer choice, the total amount available for a subsidy may not result in a significant reduction in housing prices for low-income families.

Second, builders who cross-subsidize may be less alert to innovative low-income housing solutions because they subsidize the status quo. Furthermore, competing builders who do not benefit from cross-subsidization are not able to introduce their own innovative solutions for low-income families unless they can beat the subsidized price. While well-off buyers may not be economically harmed to any substantial extent, the right of all people in society to have adequate housing is not effectively advanced.

Buyers who do not have choice are likely to perceive cross-subsidization as unfair. For example, customers of regulated utilities and public transportation usually do not have the ability to purchase from alternative suppliers. "Captive" consumers may think it unfair to be compelled to pay not just for their own usage but also for the usage of subsidized consumers.

Similarly, captive business customers may object if their efforts to lower internal costs are hampered by suppliers' cross-subsidy practices that result in higher prices. For example, the International Air Transport Association has made it clear that airlines, facing stiff competition and struggling to reduce operating costs, cannot afford the higher fees charged by government-owned or monopolistic airports, which then transfer these fees as a subsidy to recently privatized airports.

Deregulation and privatization often provide opportunities for a regulated business to use revenue from captive customers to fund operations in more risky or competitive markets. Beginning in the early 1970s, for example, the convergence of communications and computing technology created opportunities for phone companies to subsidize their computing ventures with the assets and profits from their noncompetitive regulated monopolies in telephone service. The new services fell outside the established accounting systems and routines and dynamic changes challenged capabilities to monitor and control the hazards of cross-subsidization.

In the 1980s, U.S. telephone companies began to enter competitive industries while simultaneously operating their regulated phone services. While telephone companies and customers for new services could benefit from the new ventures, local telephone customers were charged for more than their cost of service to subsidize the risky competitive ventures. One trade association reported an estimate for 1986 was a loss of $1 billion in unregulated ventures. In 1986, the U.S. Federal Communications Commission (FCC) decided to allow the phone companies to undertake new competitive ventures as long as they did not cross-subsidize the costs of these new ventures with their regulated monopolies and captive local phone customers. The U.S. Congress provided oversight of the FCC actions to provide cost allocation procedures to prevent such cross-subsidization. More recent examples of cross-subsidization in the United States continue to come from communications and computing technology in the provision of broadband, Internet, and cable services. In some cases, local electric utilities are subsidizing their entry into these digital businesses by significantly raising rates to their captive electricity customers.

Other U.S. industries also may have cross-subsidization opportunities created by deregulation. For example, a trade association for real estate companies expressed concern that large national banking conglomerates may be allowed to directly operate real estate ventures. The trade association fears that financial holding companies and their subsidiaries could compete unfairly with real estate companies and their affiliates by cross-subsidizing banking and financial operations. This cross-subsidization, by encouraging consolidation, could restrict consumer choice and competition. Furthermore, if banks compete in the commercial sector, there could be conflicts of interest that interfere with the banks' role as honest brokers of financial services.

The U.S. energy industry currently is undergoing deregulation as the development of a national energy policy changes the existing structure of regulatory oversight. The Public Utility Holding Company Act (PUHCA) is a depression-era law that prohibits large conglomerates from owning utilities and bars utility owners from cross-subsidizing or using secure ratepayer revenues to finance and guarantee other more risky business ventures. Big companies, such as investment banks, insurance companies, nonutility holding companies, and oil and energy companies, lobbied for PUHCA repeal to allow them to make large investments in the electric utility industry. Consumer groups contended that repeal of the depression-era law without adequate safeguards could undermine consumer interests. The law was recently repealed after congressional hearings about the impact on consumers, investors, and competitors.

Regulatory Approaches as Solutions

There are two regulatory approaches to prevent cross-subsidization—a structural approach and a nonstructural approach. In the structural approach, a business is not allowed to operate regulated, noncompetitive, or protected activities simultaneously with nonregulated, competitive, or risky business ventures within the same organizational governance structure. The structural approach prevents cross-subsidization by requiring separate subsidiaries with separate accounting systems. In the experience of breaking up AT&T and deregulating the telecommunications industry, the FCC found that the structural approach was an effective way to prevent cross-subsidization. The FCC also found, however, that the structural approach prevented management from taking some actions to increase productivity and, therefore, was not an economically efficient way to use assets. In short, the structural approach traded the costs of cross-subsidization for the costs of inefficiency, and therefore, it did not serve the public interest, nor did it serve the interests of owners or of local phone customers.

In the nonstructural approach, one organizational structure can operate in both regulated and nonregulated industries, there is no need for separate subsidiaries, but there must be separate accounting systems for the regulated and nonregulated activities. The nonstructural approach requires the separation of revenues, expenses, and asset investments among the regulated and nonregulated activities. This separation in accounting is made complicated when the separation by type of activity does not exactly match the physical separation of assets. For example, accounting is complicated if there are expenses for production or marketing activities that handle both types of products and customers, if capital is allocated across such mixed activities, or if the overhead of corporate technology and infrastructure supports both types of activities.

Allocating Costs

Cost allocation can be subjective, so regulatory oversight, annual independent audits, and cost allocation standards are essential parts of an oversight program to ensure that regulated profits do not subsidize competitive operations. This raises the issue of balancing the need to maintain the confidentiality of proprietary data versus the needs for transparency and honesty in disclosing expenses, revenues, and investments.

Determining who benefits and who is harmed from a cross-subsidy cannot be settled from theory alone, but requires specific data. If the operation is regulated, then there may be a state auditing agency that must be alert to cross-subsidization concerns. There also must be an ethic of transparency and integrity in sharing the information for these audits. As illustrated by recent auditing problems in the Enron case, the independence of auditors from potential conflict of interest is very important. Also, whistle-blowers need protection from any risk of retribution for their communications.

Cross-subsidization has significant impacts that are considered by many to be not fair for the interests of all stakeholders. Cross-subsidies link a tax or premium payment on some consumers and a subsidy to others, but they give the least help to the poorest people who do not have the means to be consumers at all. Also, if a corporation's cross-subsidies go from its business customers to its individual consumers then the businesses must pass the tax on in higher prices. Thus, cross-subsidization is not an effective remedy for issues of either commutative or distributive justice.

Cross-subsidies are not transparent, and they are difficult to coordinate. There must be regular attention to the effectiveness, fairness, and efficiency of the means put in place to mitigate harms from cross-subsidization. Because there is not one right way to do this, there must be a fair procedure for the many stakeholders to participate in decision making.

For these reasons, there are many legal limits and constraints on cross-subsidization activities between regulated and nonregulated business activities. In addition, trade associations advocate for the interests of their membership when they are placed at risk by cross-subsidization activities. Professional codes of conduct, to foster good relationships with stakeholders, also may state prohibitions against cross-subsidization activities.

—Greg Young

See also Altruism; Codes of Conduct, Ethical and Professional; Commutative Theory of Justice; Competition; Conflict of Interest; Consent; Consumer Rights; Corporate Governance; Corporate Social Responsiveness; Deceptive Practices; Disclosure; Economic Efficiency; Economic Incentives; Fairness; Federal Communications Commission (FCC); Federal Energy Regulation; Finance, Ethics of; Justice, Distributive; Pricing, Ethical Issues in; Procedural Justice: Social Science Perspectives; Productive Efficiency; Profits; Redistribution of Wealth; Regulation and Regulatory Agencies; Resource Allocation; Stakeholder Responsibility; Whistle-Blowing

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Cultural Imperialism

Cultural imperialism occurs when one community imposes or exports various aspects of its own way of life onto another community. The *cultural* part of the term refers to local customs, traditions, religion, language, social and moral norms, and so on—features of a way of life that are distinct from, though often closely related to, the economic and political systems that shape a community. The *imperialism* part of the term indicates that the imposing community forcefully extends the authority of its way of life over another population by either transforming or replacing aspects of the target population's culture. That is, *cultural imperialism* does not typically refer to occasions when a population voluntarily appropriates aspects of another culture into its own. Rather, the term usually designates instances of forced acculturation of a subject population. Today, issues of cultural imperialism in business arise most commonly in the context of international business and globalization.

A Brief History of Cultural Imperialism

The Ancient World

While the term *cultural imperialism* did not emerge in scholarly or popular discourse until the 1960s, the phenomenon has a long record. Historically, practices of cultural imperialism have almost always been linked with military intervention and conquest. The rise and spread of the Roman Empire provides some of the earliest examples of cultural imperialism in the history of Western civilization and highlights both negative and positive aspects of the phenomenon. In an effort to assimilate the Etruscan people into Roman culture, the Romans replaced the Etruscan language with Latin, which led to the demise and virtual extinction of that language and many other aspects of Etruscan civilization. Rome spent the next several centuries expanding its empire, culminating in a period known as the Pax Romana. During this time, through a unified legal system, technological developments, and a well-established infrastructure, the Romans secured a fairly long period of relative peace and stability among previously war-torn territories. However, this peace was secured, in part, by the forced acculturation of the culturally diverse populations Rome had conquered.

Cultural Imperialism and Colonization

During the modern period, cultural imperialism became one of the primary instruments of colonization. Colonization is the forced extension of a nation's authority over people outside its own boundaries to expand economic domination over their labor force and resources and political control of their territory. While colonization was almost always initiated by some kind of military intervention, its full effects were achieved through practices of cultural imperialism. Fueled by a belief in the superiority of their own way of life, colonizers used law, education, and/or military force to impose various aspects of their own culture onto the target population. Motivated, in part, by a desire to purge local populations of allegedly barbaric, uncivilized customs and mores, colonizers also knew that the best way to mitigate resistance by the colonized was to eradicate as far as possible all traces of the former way of life.

One of the clearest examples of the forced acculturation of a colonized population was the Spanish influence in Latin America, beginning with the conquest of the Aztec empire by Hernan Cortes during the early 16th century. After securing their physical presence in the region, the Spanish suppressed Mesoamerican culture, forbidding the Indians to learn and transmit their culture while simultaneously requiring them to read and write Spanish and convert to Christianity. This behavior was certainly not unique to the Spanish; other examples include the British influence in India and the Dutch and French presence in the Caribbean. Today, charges of cultural imperialism often still carry this legacy of association with the historical experience of colonization.

Contemporary Understandings

During the 20th century, cultural imperialism was no longer so closely linked with military intervention but rather with the exertion of economic and political influence by some more powerful nations such as Russia and the United States on less powerful countries. Many observers view Russia's forceful attempts during the Soviet period to impose communism on neighboring countries as a form of cultural imperialism. More recently, however, charges of cultural imperialism have been aimed primarily at the United States. Critics allege that imperial control is now being sought economically by creating a demand for American goods and services in other parts of the world through aggressive marketing. This "Americanization" of other cultures occurs when the mass exportation of American films, music, clothing, and food into other countries threatens to replace local products and to alter or extinguish features of the traditional way of life. Some countries have attempted to thwart this cultural threat through various kinds of legal action. For example, during the 1950s, France attempted to ban the sale of Coca-Cola and more recently McDonald's, and Canada has required that a portion of all radio air time must be devoted to Canadian music and subject matter.

Cultural Imperialism and Business

Imperialism Versus Relativism

Issues of cultural imperialism in business arise most obviously in the context of international business, in particular regarding business ethics in an international setting. Companies operating in foreign countries often experience significant tensions between respecting cultural differences, maintaining a sense of integrity to their own moral standards, and successfully conducting business. How should companies conduct themselves when the moral values and social norms of the home country seem to conflict with, and especially when they appear higher than, the prevailing moral and social norms of the host country?

One possible response to this problem is a strict cultural imperialist stance, which contends that the home country's moral and social norms are absolute and ought to be extended to all countries within which a company does business. According to the imperialist, when values clash a company ought to follow its own standards in all contexts without any consideration of the host country's moral, social, and/or legal codes. One strength of this approach is its emphasis on maintaining integrity to a company's own code of ethics, especially in cases where the moral standards of the host country seem lower than those of the home country and when a company might benefit financially from following these norms. For example, the strict imperialist would demand that if conducting business in a county with a record of gross human rights violations, a U.S.-based company should maintain and extend Western liberal values that aim to protect the basic rights of all human beings, even if doing so would compromise the bottom line. The imperialist stance acknowledges that commitment to one's own moral standards is important.

However, the paternalism implicit in an imperialist stance clashes with the fairly widespread view that we ought to respect cultural differences, at least to some degree. Moreover, critics also point out that an imperialist stance violates a community's right to self-determination and can have disastrous consequences. For example, in his discussion of the imperialist stance, Thomas Donaldson considers a case when members of a U.S. company operating in China caught an employee stealing. Following company policy on stealing the company turned the employee over to the legal authorities, which in this context resulted in the employee's execution.

At the opposite extreme in response to questions about how companies ought to behave in an international setting is the relativist stance. In contrast to the imperialist, the relativist contends that no way of life is any better than any other; "our" moral norms are simply different, not better than "theirs." The relativist argues that when practicing business in a foreign country companies should simply follow the host country's moral, social, and legal codes. While the relativist stance avoids the imperialist problem of unfairly imposing "our" standards on others, critics argue that relativism is unacceptable because it allows or may even require a company to engage in or support practices that are harmful to members of the host country. For example, Donaldson discusses a case of a group of investors who decided to restore the *SS United States*, a former luxury cruise ship. Prior to the restoration, the asbestos lining of the ship had to be removed. While a U.S.-based company proposed to do the work at $100 million, a Ukrainian company bid for the job at less than $2 million, which they were able to do because of significantly lower health and safety standards in that country. A relativist would allow investors to accept the Ukrainian company's bid without any consideration of the potential harms to workers there. Yet critics of this approach argue that while a country has the right to develop its own health and safety standards, if those standards fail to adequately protect workers from serious risks, then companies should object.

Beyond Imperialism and Relativism

While the strict imperialist fails to respect cultural differences, the relativist fails to oppose gross injustice. Most theorists agree that the correct approach is somewhere in between these two stances. To mediate between cultural imperialism and relativism when values clash, companies need to be able to differentiate between practices that are merely different and practices that are morally wrong and intolerable. Companies should balance respect for cultural differences with a commitment to maintaining a certain moral minimum. According to Donaldson, we can construct a moral minimum by noticing a set of core values found in nearly all cultures, such as reciprocity, respect for human dignity, a decent standard of living, and so on. Collectively, these overlapping values form a moral threshold that imposes limits on the extent to which companies ought to respect cultural differences. If the host country's moral and social standards violate this moral minimum, a company should not simply capitulate to a relativist stance but is obligated to object.

Determining whether values and practices of another culture are simply different or morally intolerable is often difficult. Most actions exist in what Donaldson and Thomas Dunfee call moral free space, meaning that they are neither right nor wrong until we consider them in context. While in the United States extravagant gift giving is seen as a potential form of bribery and raises questions about conflict of interest, in Japan this practice is central to cultural understandings about loyalty and respect. Thus, a U.S.-based company might respect practices of extravagant gift giving when conducting business in Japan given the meaning these practices carry in Japanese culture coupled with the fact that they do not appear to violate any core human values. In contrast, if a country permits child labor and if employing children prevents them from receiving a basic education, this would violate the moral threshold and companies ought to object. According to Donaldson, the key to balancing respect for cultural differences and moral decency is allowing context to inform judgments about ethical behavior.

One way context can inform these judgments is by identifying the nature of the conflict when a clash in values or norms occurs. Donaldson distinguishes between two of the most common kinds of conflicts: conflicts of relative development and conflicts of cultural tradition. Conflicts of relative development occur when moral and social norms conflict because the home and host countries are at significantly different levels of economic development. For example, two countries may have considerably different views about child labor or wages, but these disparities may be due in large part to economic differences rather than a substantial clash in values. In contrast, conflicts of cultural tradition occur when moral and social norms conflict because of genuine disparity between two different value systems. For example, countries might disagree on the role of women in the workplace, which may reflect significantly dissimilar cultural understandings about equality.

To resolve conflicts of relative development, Donaldson suggests that company leaders ask themselves if the practice would be tolerated in the home country if the home country were at a similar stage of economic development as the host country. For example, some countries may permit workers to be paid extremely low wages, wages that may seem appalling in the United States. Yet if higher wages in the host country would lead to loss of jobs and investment there, and if the wage rates are sufficient for maintaining a decent standard of living in that country (i.e., if there is no violation of the moral minimum), then paying the lower wages may be permissible. However, when a conflict is due to a real clash between moral and social values, Donaldson contends that company leaders must determine whether it is possible to conduct business in that country without engaging in the practice in question and whether the practice violates a core human value. If the answer to these questions is no, then a company should object.

Social Obligations of Multinationals in Foreign Settings

Questions of cultural imperialism surface not only when values, traditions, and customs conflict but also when considering what positive moral and social responsibilities multinationals have to the host communities within which they operate. Many observers contend that multinationals have at least some obligations to be "good citizens" of the host countries where they do business, but what kinds of obligations do they have and to what extent? At minimum most agree that companies ought to behave appropriately within the customs and mores of a host community and support local social institutions, but what if these customs and institutions violate the moral minimum? What responsibilities, if any, do multinationals have to address gross human rights violations or other moral and social ills that may be occurring within the host community? Some have suggested that multinationals should use their power and influence with local governments to promote moral and social reform where needed. Other theorists are much more cautious about ascribing positive social responsibilities to multinationals in a foreign setting.

For example, Patricia Werhane argues for considerable constraints on the moral and social responsibilities of companies conducting business in a foreign country. Werhane contends that multinationals certainly have obligations not to cause more harm than is caused by the status quo in a particular country, and they should redress any harms that the company itself may have caused. However, beyond this, companies should not interfere in the political and social life of the host country. While it might seem initially plausible and admirable for a company to work toward improving the social and political environments within which they operate, Werhane worries that this kind of behavior violates a nation's right to sovereignty and self-determination.

There is a danger that companies engaging in activism will unrightfully impose their own moral and social beliefs and values within host communities. Multinationals do not have the expertise to adequately address social ills, and as Werhane points out, if a nation's sovereignty can be overridden by another nation only on the most rigorous moral grounds, the occasions when corporate interference might be justified are rare indeed. A company may be permitted to engage in "quiet cooperation" with host governments to address social ills, but beyond this, Werhane maintains that if a company cannot uphold its own moral standards while practicing business in a foreign country, then it should refrain from conducting business there.

While concern that multinationals avoid unwarranted paternalism is important, critics point out that this approach overlooks the complexity of a multinational's relationship with the host countries where it operates. For example, in 1995, Ken Saro-Wiwa was executed by the Nigerian government for protesting certain activities of Shell Oil in the region, specifically environmental degradation and the economic exploitation of the native Ogoni people living there. Many observers argued that Shell should have used its influence with the Nigerian government to intervene on behalf of Saro-Wiwa, as this was a life or death matter. In response to these criticisms, however, the company claimed that it would be wrong to intervene in the case because multinational corporations do not have the right to interfere in the political and legal affairs of sovereign states. However, some critics maintain that Shell Oil's economic presence in the region was already a form of interference that had disastrous political and social consequences for many people living in the region. Thus, while companies certainly need to avoid being unduly paternalistic, they also need to be aware of the ways in which economic relationships with foreign governments are not always morally and politically neutral.

Contemporary Approaches

The views discussed thus far explore issues of cultural imperialism as they arise in business practice within the current global economy. These approaches take a global free market system as given and then consider how, while conducting business within this economy, multinational corporations can maintain a balance between respect for cultural differences and integrity to their own moral and social standards. However, concerns about cultural imperialism also surface in discussions about the processes of globalization and development that have led to the dominance of free market capitalism on a global scale.

One stated goal of globalization is to aid and encourage the economic development of struggling, impoverished nations. One of the more popular development strategies known as catching-up development recommends that by expanding free market capitalism on a global scale poorer nations will be able to compete in the global market, increase their economic development, and eventually "catch up" to the levels of economic maturity that wealthier nations now enjoy. However, critics of this development approach worry that the extension of neoliberal economic policies on a global scale is itself a form of cultural imperialism. For example, Maria Mies contends that free market economic models and the development strategies based on them are not value neutral, but promote a particular conception of the good life—namely, one that is characterized by a consumer culture, materialism, individualism, competition, and profit maximization. Development strategies premised on the extension of free market logic take a conception of the good life popular in many Western nations as the standard to which all nations ought to aspire.

There are other possible models for economic development, such as sustainability models. The dominance of free market economic policies makes it difficult if not impossible for countries to explore other economic models that might be more compatible with their own cultural values and ideas about what constitutes a good human life. For example, Vandana Shiva argues that indigenous populations in India have been successfully conserving water and living off of the land for centuries in part because of an emphasis on communal ownership and management of natural resources. The extension of a free market economy on a global scale has fostered the privatization and commodification of water in India by large multinationals, threatening not only the livelihood of native peoples but also their traditional agricultural practices and ways of life.

The phenomenon of cultural imperialism is complex, and as we have seen, it emerges in a number of different contexts. As processes of globalization lead us to form unprecedented economic and political relationships with distant others, finding the proper balance between respect for cultural differences, moral decency, and successful business practice becomes increasingly more important and also considerably more difficult.

—Theresa Weynand Tobin

See also Cross-Cultural Consumer Marketing; Multiculturalism; Relativism, Cultural

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Dalkon Shield

The Dalkon Shield was an intrauterine birth control device (IUD) manufactured and sold from January 1971 to October 1974 by the A. H. Robins Company, maker of Robitussin cough syrup and Chapstick lip balm. Sales were suspended at the request of the Food and Drug Administration (FDA) because of a high number of reported incidents of inflammatory pelvic infections and spontaneous septic abortions as well as four deaths. Also, many children were born with defects linked to the device. In 1985, after 9,500 cases had been litigated or settled, the company filed for bankruptcy and set up a $2.3 billion fixed-asset trust fund to deal with the thousands of pending cases.

The Shield was invented by Dr. Hugh Davis and Irwin Lerner in 1968. After promoting the device at medical meetings, they named their company Dalkon Corporation. Dr. Davis published an article in the February 1, 1970, issue of the *American Journal of Obstetrics and Gynecology* that described a study of 640 women using the Dalkon Shield with a pregnancy rate of 1.1%. The article also described the device as "modern," having "superior performance," and being a "first choice method," words not normally used in a rigorous scientific study. He also neglected to say that he was the inventor. A. H. Robins bought the manufacturing rights in June 1969 for royalties and $750,000, hired Davis as a consultant, and modified the design, adding a small amount of copper and a multifilament wick. They also made a smaller version.

At the time, there were more than 70 IUDs on the market, so Robins began an aggressive marketing campaign to doctors and clinics, touting the device as safer, easier, and more painless to insert, and having the lowest pregnancy rate. They also used Davis's article as a marketing tool, without disclosing his ties to the company. Because the Shield was a device and not a drug, it was not subject to the extensive testing required by the FDA. Problems began in 1971 with patients becoming infected and/or pregnant. By June 1974, there had been four deaths linked to the Shield as well as countless spontaneous abortions and pelvic infections leading to continuous pain and sometimes sterility. Many studies showed that the pregnancy rate was much higher than originally thought, some showing it at 5.5% or even higher. The FDA requested that it be taken off the market. In the United States, 2.2 million devices had been sold; global sales were 4.5 million. Sales continued in foreign countries for another 9 months.

Court records of litigated cases showed inadequate testing, false claims about both safety and rate of pregnancy, and a high incidence of pelvic infections and other complications. Robins's first response was to blame the doctors for improper insertion. Aetna, their liability insurer, cut off coverage in February 1978. One of the cases was in 1984 in Minnesota, where Judge Miles Lord, after taking a deposition from company officials, castigated them for defending rather than recalling the Dalkon Shield. His remarks were later struck from the record, but his statements were widely publicized and encouraged more victims to sue the company. In October 1984, Robins voluntarily withdrew the Dalkon Shield from the market and, the following February, launched an advertising campaign urging women still wearing Shields to have them removed at the company's expense. By the end of March, 4,437 women had complied and filed claims for removal expenses. That year, Robins filed for Chapter 11 reorganization, which prevented more lawsuits. Part of the plan was to consolidate all future claims in a trust fund following the precedent of Johns-Manville.

It was not until December 1989, with American Home Products' acquisition of Robins and their $2.48 billion trust for claims, that the trust began to be administered. The last case was settled 10 years later. The trust, the first fixed-asset trust fund ever administered, had handled 400,000 cases from more than 100 countries and paid 170,000 claimants. All claimants had to provide medical records, and for many, this was impossible. Also, lawyers for the trust used two tactics to avoid payment: The claimant waited too long or other sexually transmitted diseases were to blame for the injuries. In foreign countries, countless women were never recompensed because of faulty records. A. H. Robins never took complete responsibility.

—Carol H. Krismann

See also Bankruptcy, Ethical Issues in; Corporate Accountability; Deceptive Advertising; Fraud; Johns-Manville; Product Liability; Scandals, Corporate; U.S. Food and Drug Administration (FDA)

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Darwinism and Ethics

Darwin produced two hugely influential books on the subject of evolution: *The Origin of the Species* in 1859 and *The Descent of Man* in 1851. The former belongs properly to the science of biology, whereas the latter offered more to thinkers in terms of "social theory." Darwin's writings influenced ethical thought through a biological approach to social theory, which formed the basis for the social and ethical implications of evolutionism. The social and political thought of the later 19th century drew on themes and metaphors found in Darwin's work such that its principal ideas became known as "Social Darwinism." In the 20th century, Darwinism took a new direction with the synthesis of Darwinism and Mendelian genetics or "neo-Darwinism." This development generated the disciplines of sociobiology and evolutionary psychology with corresponding influences on social and ethical thought. Moreover, Darwinian thought must be continually viewed in the context of the ongoing disputes between political conservatives and leftists as they engage with evolutionary theory through various strategies of rejection or co-option.

Historical Background

The belief in the organic evolution and the gradual transformation of organisms through history from preexisting forms through a natural law process has existed at least since the middle of the 18th century. Empirical studies at the time had made discoveries concerning the nature of organisms and their reproduction, the distribution of species, and the existence of fossilized remains of earlier and spectacular life forms. Thinkers such as Erasmus Darwin (the grandfather of Charles Darwin), and slightly later Jean Baptiste de Lamarck in France, offered an intellectual background to these empirical studies through a commitment to cultural and social progress. Evolution as a secular religion complemented utilitarianism in the belief that progress increases and maximizes happiness. Evolution and ethics become indistinguishable as the world picture that evolution conveyed also offered moral direction. This direction was interpreted to mean the increased application of industrial ideas and techniques in a market environment free of intervention. On this view, the division of labor and human-driven direction would be sufficient to ensure continuing social and economic improvement.

Charles Darwin, the grandson of Erasmus, transformed the theory of evolution from at best a pseudo science or as it was for Erasmus Darwin, a secular religion, into a genuine scientific doctrine. *The Origin of the Species* published in 1859 was an impressive empirical work. Darwin used facts from the organic world and drew on, for example, paleontology, systematics, morphology, and embryology to demonstrate his theory of natural selection. The principle of natural selection can be summarized in the following propositions. First, the populations of animals and plants manifest variations. Second, some variations provide an organism with advantages over the others in the population in the struggle for life. Third, variation will be passed on to the offspring. Fourth, because the environment may not support all the offspring produced by a given population, a greater proportion of favorable variant will survive and produce progeny than the proportion of unfavorable variants. Finally, new species, variation, genera, and populations may result from a population that suffers continuous change.

Social Darwinism: Cooperation or Survival of the Richest

Unlike Erasmus Darwin, Charles Darwin's theory was not intended to provide ethical directives. However, his later work on our own species, *The Descent of Man*, especially in the later editions expressed sentiments that had application for the Social Darwinists. There is, for example, a reference to the virtues of capitalism. It is also significant that Darwin in this second work replaces the greatest happiness principle of utilitarianism with the goal of the general good entailing biological perfection. Darwin also addressed the issue of the moral sentiments and their place in the evolutionary process. Earlier in the 18th century, the hugely influential Scottish philosophers David Hume and Adam Smith had both offered nuanced interpretations of sympathy and its role in the motivation of moral acts. For Darwin, sympathy belongs to the noblest part of our nature and has been vital in the development of the human race. He speaks of the acquisition of the habit of aiding one's fellows as originally motivated by the self-interested desire for reciprocal aid. He argues that the habit of performing benevolent actions certainly strengthened the feeling of sympathy, which gave the first impulse to benevolent actions. Thus, habits of benevolence followed during many generations tend to be inherited. But at the same time he urges that sympathy must be regulated and checked; otherwise, the weak and inferior survive and propagate to the detriment of biological perfection. Thus, for example, he urges limitations to ensure that the weak and inferior do not marry freely.

Although Darwin did make some tentative ethical conclusions from his scientific work, the so-called Social Darwinism is most famously associated with the philosopher and political activist Herbert Spencer. Spencer regarded evolution as more than a scientific theory; it was a world picture that applied throughout creation, and to a certain extent, it served as a substitute for a declining religious faith. For Spencer, evolution is a progression that begins from the simple and leads to the more complex. He believed that this process of continual development and improvement applied to the cosmological, the natural, and the social world. Spencer argued for a laissez-faire socioeconomic philosophy as he applied the natural mechanism of the "survival of the fittest" to the realm of ethics and sociology. But Spencer himself was an ardent opponent of militarism, regarding it as wasteful, and as with Thomas Hobbes, associating militarism with the disruption of trade and commerce and, therefore, the abnegation of free and open competition. Moreover, though Spencer advocated laissez-faire policies, he also held that in the struggle for survival men come to recognize that cooperation is necessary. The pleasures that derive from our natural sociability are the rewards that guarantee a continuing cooperation among members or society. Ultimately, he believed that the evolutionary process would gradually replace egoism with altruism as something similar to an inherited acquired characteristic.

On the other hand, William Graham Sumner's thought more perfectly embodies the familiar view associated with Social Darwinism that holds that the fittest must struggle to succeed at the expense of their peers if social progress is to be achieved. Promotion of the ongoing struggle for existence is necessary for the evolution of the species. Just as species are weeded out by the struggle for existence in nature, so too, the argument runs, should the weakest of humanity be weeded out by a similar process in society. Disease, poverty, and early death are the mechanism of ridding the human species of those who are the least "fit." In the natural evolutionary process, those parts of society that are least fit to survive succumb and the species gradually improves as its weaker components are eliminated. It is wrong to interfere with this process because this only prolongs the suffering of the unfit while their continued existence and proliferation retard the progress of the human species.

This belief in the close association between competition and evolution served as an apology for capitalist social relations at the end of the 19th century, because according to this interpretation of Social Darwinism self-made millionaires became viewed as the paradigm of the fittest. These views were endorsed by American industrialists such as John D. Rockefeller and Andrew

Carnegie who also saw competition as essential to capitalism and the evolutionary process. According to this interpretation of Social Darwinism, those who are the fittest will achieve high status within society and a high level of material wealth and those who are not fit for survival will languish in poverty and have no influence on the public. Ultimately, the lower levels of humanity die off and will be replaced by others more suited to survival, much as unfit organisms in nature fail to survive and are replaced by the better adapted organism. The outcome of this process will be the eradication of poverty and a human population that exhibits the superior qualities.

At the same time, however, there were American Marxists who argued for socialism as essential to human progress.

Ultimately, 19th-century Social Darwinism was often rich in variety and often used to support contradictory positions. Both the left and the right on the political spectrum accommodated Darwinian ideas to support their positions. In reality, a diversity of political positions drew on Darwinian themes and adapted them to different forms of liberalism. These Darwinian ideas were used, for example, to give ethics a scientific foundation, to argue for state intervention in the economy and social welfare programs, to defend Fabian as opposed to revolutionary socialism, and to relate liberalism with empiricism in philosophy.

Social Darwinism and Its Critics

But others began to question the association of evolution with morality. T. H. Huxley in his famous essay "Evolution and Ethics" argued that evolution that promotes competition and the survival of the fittest cannot support ethics or morality because morality requires not that people look after their own self-interests but that they look after the interests of others. It is wrong that a man seek some positive form of pleasure for himself at the expense of inflicting pain on another. As Huxley understood morality, it is essential to overcome the natural desires of the individual when they conflict with the needs of society. Huxley further objected that nature is an inappropriate model for moral behavior. He pointed out that the process of evolution is basically an a-moral force and, therefore, cannot serve as a foundation for morality. Perhaps even more significantly G. E. Moore in *Principia Ethica* criticized Spencer's form of Social Darwinism as an illegitimate form of reasoning. Moore accused Spencer of committing the naturalistic fallacy. This fallacy refers to the attempt to derive ethical imperatives through reference to nature or natural phenomena.

Darwinism and Ethics in the 20th and 21st Centuries

However, despite the critiques from T. H. Huxley and G. E. Moore, "evolutionism" continued to influence social and ethical thought in the 20th century. Julian Sorel Huxley, the grandson of Thomas Huxley, promoted the synthesis of Darwinism and Mendelian genetics or neo-Darwinism. He argued that evidence of evolution indicates a gradual improvement and progress that also applies to human development. For Julian Huxley, evolution is to be seen as a secular religion. But he envisioned natural selection operating at the group rather than at the individual level. He argued for the promotion of an evolutionary perspective in which one would promote principles and norms that would be of final benefit to the entire mankind. As against free market capitalism, he was a strong believer in central planning at the global level. He regarded the United Nations as an evolutionary success that ought to be used as a basis for world peace. As the influence of Social Darwinism continued through the 20th century, it even had an influence on nonsecular religious thought. Most significantly, the Catholic philosopher Pierre de Chardin attempted to transform evolution from a secular to a nonsecular religion.

In America, George Gaylord Simpson, a contemporary of Huxley, also believed in the importance of evolution and the evolution of the ethical faculty in the evolutionary process but held that evolution cannot function as metaethics or a normative justification. Simpson's progressivism led him to reject state-run programs and the socialist approach, preferring to emphasize the individual and his or her right to free choice. He believed that this individualist approach would best promote an intellectually dynamic society, which would ultimately enhance social progress.

In 1975, Edward O. Wilson's landmark work, *Sociobiology: The New Synthesis*, introduced neo-Darwinism to the public. Wilson's sociobiology sought to demonstrate in rigorous detail how Darwinian selection molded the various ways in which all animals—from the lowly corals to the social insects to the highest primates—compete and cooperate with others of their own species. Wilson suggested numerous analogies between animal and human societies. Others such as Aesop in his *Fables* argue along similar lines; however, Wilson's work sought to unify a vast body of knowledge of natural history and neo-Darwinian theory in a project to reduce social science to a branch of biology. Many found these ideas controversial. Left-leaning thinkers felt uncomfortable with the implication that emphasis on the individual, family, and ethnic self-interest is an innate heritage that cannot be modified through social change. This implication severely undermined the possibility of a utopian social order. In his later work, Wilson used sociobiology to promote environmental awareness if not an environmental ethic. He argues that humans have evolved a symbiotic relationship with the rest of the natural world, and because of this mutual dependency, we ought to promote biodiversity, if we are to promote the human species. In this sense, evolution, as a substitute for religion, must serve as a basis for moral action, he argues.

Ultimately, the sociobiology controversies of the 1970s transmuted into those over the rebranded sociobiology of the 1990s, with its emphasis on human "evolutionary psychology," a belief that contemporary moral behavior and value judgments are predetermined by genetic impulses created through an evolutionary process. Again, this view in many respects runs counter to the left's fundamental belief that individuals can be reconstructed through a redesign of the social order. At the same time, the view that there exist innate moral sentiments such as love, compassion, generosity, shame, and guilt militates against the metaethical doctrine of ethical relativism as it endows certain ethical attitudes with universal application.

Despite the "green" tendencies in Wilson's later work, left-leaning thinkers have remained uneasy about the implications of sociobiology and evolutionary psychology, while conservative thinkers have also been critical. In particular, the religious right objects to evolution as contrary to "creationism." Nevertheless, some conservative thinkers, such as Lawrence Arnhart, argue that evolution remains a body of empirical science and solid theory that displays and supports bedrock conservatism. These ideas include the inextricability of present and future from the past, the inevitability of variation in individuals and systems, differential survival of useful variations and the containment of damaging ones, and the omnipresent control of everything by environment, itself changing as its inhabitants change in response to itself. This is a system of thought, which is consistent with conservative thinking because it is entirely opposed to radical utopianism that the left has advocated since 1860. The utopian vision commonly assumes that the communal sharing within a single family can be extended to an entire society and so advocates the abolition of private property and private families to achieve the communal spirit. Evolutionary psychology tells us that the bond between the families is a natural disposition that has evolved and cannot be readily discarded contrary to the thinking of the utopians. At the same time, people such as Arnhart push the view that there is nothing about evolutionary biology that denies let alone disproves the Creator's role in the World. True conservatives, he argues, are committed to realism about human nature and its future.

But not all left-leaning thinkers subscribe to the view that evolutionary theory runs counter to its social program. Peter Singer, for example, argues that evolutionary theory leaves space for a Darwinian left that would focus on the importance of cooperation and altruism, matters that were not widely understood as being part of evolution when Social Darwinism first gained favor. One reason given as to why the left should use Darwinism is the focus, starting in the 1960s, on cooperation as a factor in survival and genetic success. Cooperation, Singer says, is an important part of Darwinism and it is in keeping with the values of the left, despite Social Darwinism's focus on competition, which has fueled the left's perfunctory dismissal of Darwinism. However, Singer argues that many on the left of the political spectrum have to accept that evolution has overthrown certain of their traditional leftist beliefs. For example, the Marxist belief that the individual is entirely a product of one's social environment fails to acknowledge that biological nature largely influences individual lives and the enveloping social reality. Moreover, evolution gives strong indications that humans are not, and never will be, perfect, thereby precluding the possibility of realizing the goal of a perfect society, a Marxist utopia. If one recognizes that this goal is unreachable, it is much better, he argues, to understand the inherent imperfections and try to work with them. Our ideas and politics are a product of our evolution, and we need to see how they have come about in order to properly address the problems created by them.

From the foregoing, it is obvious that Darwinism has had a profound influence on social and ethical thought through the last two centuries. On the normative level, it has promoted a range of different positions from liberal individualism and laissez-faire economics to communitarian collectivism and state-run enterprise. At the metaethical level, it has struggled to overcome the naturalistic fallacy criticism and the critical division between facts and values. But despite the logical objections, evolution is a theory that ineluctably introduces value-laden concepts such as "progress," "improvement," "development," and "sophistication," which will continue to exert an influence on ethical and social thoughts through the 21st century.

—David Riordan Lea

See also Altruism; Biodiversity; Carnegie, Andrew; Communitarianism; Egoism; Empathy; Environmental Ethics; Evolutionary Psychology; Free Will; Hobbes, Thomas; Hume, David; Individualism; Laissez-Faire; Marx, Karl; Metaethics; Smith, Adam; Socialism; Spencer, Herbert

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Deadweight Loss

A deadweight loss indicates the amount of economic welfare lost to the economy due to either (1) a market failure or (2) interference by government in an otherwise efficient marketplace. The deadweight loss comes at the expense of consumer or producer welfare, or both (in varying degrees).

A producer's monopolization of a market leads to a market failure when successful in restricting the quantity sold and raising the price per unit sold. This monopolization is a market failure because if the price could be lowered and the quantity sold increased this change would create a net benefit to society. In fact, the marginal (i.e., extra) benefit to consumers exceeds the marginal (i.e., extra) cost to the producer up to the point where the marginal social cost curve crosses the marginal social benefit curve. Simply put, this point is where supply equals demand. A market characterized by perfect competition would achieve that socially desirable result.

Figure 1 shows the standard model of a monopoly market. The deadweight loss from monopolization is the shaded triangle.

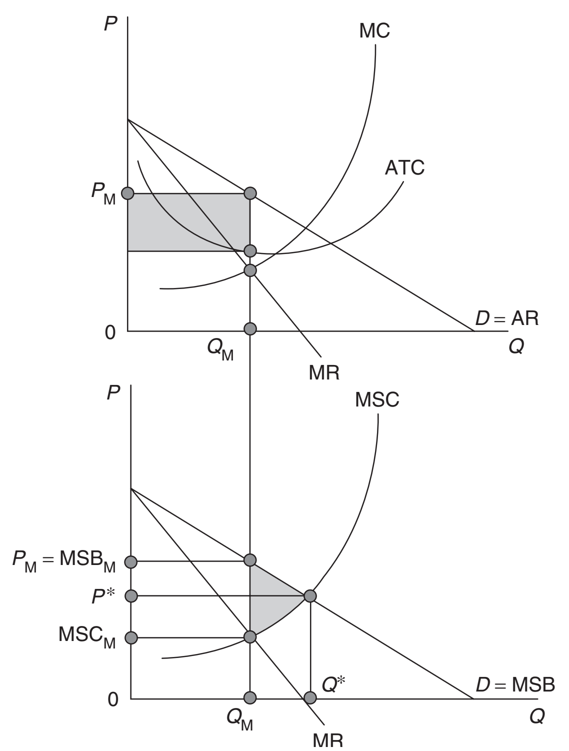

Figure 1 Deadweight Loss From Monopolization

In the upper panel, the monopolist uses the available degree of market power to set the price (P_M) and quantity to be sold (Q_M), thus securing an economic profit (defined as above the competitive outcome) as shown by the shaded rectangle. This profit arises because the average revenue (AR) exceeds the average total cost (ATC) at the quantity sold. The lower panel takes this market and redefines it in economic welfare terms. By assuming there are no spillovers of this activity (i.e., externalities) into other markets, (1) the marginal cost (MC) will equal the marginal social cost (MSC) and (2) the demand (*D*) will equal the marginal social benefit (MSB). From this perspective, it can be seen that Q_M is characterized by MSB_M exceeding MSC_M, and this condition means that society would receive a net marginal benefit if further output could be produced. Of course, the monopolist has no incentive to lower economic profits by doing so. In fact, net marginal benefits occur up to a level of output equal to Q^* (where MSB = MSC). The total of all the marginal benefits foregone because Q^* is not produced at a price of P^* is shown by the shaded deadweight loss triangle.

It may also be the case that the deadweight loss from monopolization could be significantly more than what the triangle indicates. If rent-seeking activity occurs before a producer can achieve market power, then both the monopolist and his rivals will be devoting funds to obtain a government license in order to dominate the market. Examples of this situation occur in the market for taxi medallions and television broadcasting licenses. Those rivals who spend money and yet ultimately lose the fight for the license have been encouraged by a regulatory environment in which the winning strategy is not clear. All resources spent in this inefficient process must be added to the deadweight loss triangle. In the extreme case, the entire economic profit rectangle could be dissipated because of destructive competition to achieve monopoly rights.

Deadweight losses can also occur if the government interferes in a market which is otherwise efficient; that is, there are no externalities into other markets that need to be accounted for by government action. Taxes on producers to correct for negative spillovers can add to economic welfare. For example, it makes sense to tax industrial producers whose pollution adversely affects a river and, subsequently, the market for fish. But taxes on production for their own sake, or as a simple source of revenue, can generate a deadweight loss as shown in Figure 2 for the instance sales taxes.

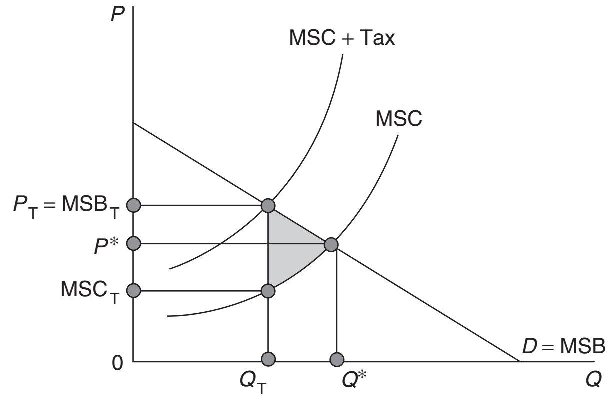

Figure 2 Deadweight Loss From Sales Taxes

The socially optimal quantity (Q^*) and price (P^*) occur where MSB = MSC. If the government decides to tax every unit sold, then producers will build the tax into their costs of production. In this way, the supply curve shifts upward by the amount of the tax. At the lesser quantity sold (Q_T) at the higher price (P_T), it can be seen that $MSB_T > MSC_T$, meaning that net marginal benefits would occur if more could be produced. In the same fashion as the monopoly market, a deadweight loss triangle is the sum of all the net marginal benefits foregone because of the sales tax. The government has the monopoly power to tax.

In the reverse case, a subsidy paid to producers can lead to a deadweight loss if it serves to increase production beyond the efficient amount indicated by the market. Only a positive spillover of the producers' activity into another market would indicate that a subsidy is necessary to improve economic welfare. A subsidy paid to beekeepers, for example, may lead to increased productivity on the part of flower gardeners because of the extra pollination taking place. In other words, the subsidy accounting for this externality provides a social gain. But when there are no such spillovers, a deadweight loss occurs as shown by the shaded triangle in Figure 3.

For the government to induce producers to sell more than Q^*, a subsidy will have to be paid to them because the cost of production (MSC_S) is higher than the price that the consumers are willing to pay (MSB_S) for the extra quantity. In other words, the subsidy paid is equal to the amount necessary to cover the premium in MSC_S over MSB_S. In this way, producers will charge a price of P_S to their consumers. But since producing units beyond Q^* have marginal social benefits less than marginal social costs, a deadweight loss

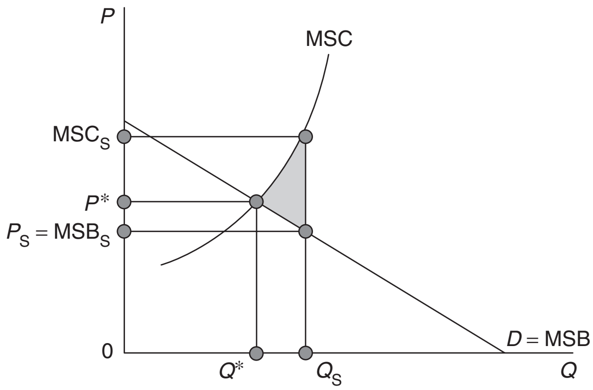

Figure 3 Deadweight Loss From Subsidies

triangle comes about. Simply put, the subsidy induces more than the efficient amount of resources to be devoted to producing the item in question.

In fact, the deadweight loss could be larger than that indicated in Figure 3 because the subsidy paid by the government may have been financed out of tax revenue gathered from other markets in such a way as to create other deadweight losses. Also, if the subsidy paid out more than covers the cost of production, an economic rent would accrue to the producers. If not all producers are subsidized, there may be rent-seeking competition for such subsidies. The deadweight loss would increase in the same way as described in the monopoly market above. Only taxes charged to correct for negative spillovers to other markets, and subsidies paid to account for positive spillovers to other markets, will eliminate any deadweight losses in those markets generating such spillovers.

—Darren Prokop

See also Externalities; Market Failure; Monopolies, Duopolies, and Oligopolies; Rents, Economic; Tax Incidence; Welfare Economics

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Deceptive Advertising

As it is used by regulators, the courts, and social scientists, *deceptive advertising* is a technical, legal term: A deceptive advertisement is one that involves a representation, omission, or practice likely to mislead a reasonable consumer. To be regulable under the law, however, a further condition must be met: The deception must be "material," which is to say that it must be likely to detrimentally affect the consumer's purchasing decisions. While injurious effects on consumers account for much of what is objectionable about deceptive advertising from a moral and ethical point of view, deceptive advertising also harms competitors and generally weakens trust in the marketplace.

The above legal definition agrees with the one operative in European Union (EU) countries in essential respects, although the means by which many EU countries regulate deceptive advertising differs from the United States. In the United States, the Federal Trade Commission (FTC) has primary federal responsibility for preventing deceptive advertising in both broadcast and print forms, although consumer protection agencies of the various states have authority over local advertisements. The major source of industry self-regulation is the National Advertising Division (NAD) of the Council of Better Business Bureaus. Some enforcement also occurs through private lawsuits, most commonly those brought by competitors under the Lanham Trademark Act. Nonetheless, many deceptive advertisements that meet the legal standard for deception persist, either because they have not been challenged or because government agencies have limited resources. In general, the greater the amount of potential physical and economic injury to consumers, the greater is the incentive for regulators to act.

"Deception" in Its Ordinary and Legal Senses

Setting the issue of materiality aside, the sense of "deception" found in the legal notion of deceptive advertising can be usefully contrasted with our "ordinary" concept of deception in two respects. First, at least insofar as issues of moral concern are raised, the ordinary concept of deception, like that of lying, applies only to acts done intentionally and purposefully. For regulatory and legal purposes, however, an advertisement need not be *intentionally* deceptive. Rather, the legal notion focuses exclusively on false consumer beliefs caused by the advertisement. Second, deception in the ordinary sense requires a measure of success; there cannot be a deception without at least someone who is actually deceived or misled. Deception differs from lying in this respect, as one can be lied to without being taken in by the lie. The legal notion of deception is also outcome oriented, but in a special way. Since a deceptive advertisement must be likely to mislead a consumer acting reasonably under the circumstances, strictly speaking, the law does not require that anyone has actually been deceived. Consequently, one might say that the legal definition focuses on deceptiveness rather than deception—the likelihood that an advertisement will cause false beliefs rather than whether it in fact has done so.

In terms of actual regulatory practice, however, the issue is somewhat more complicated. The likelihood that an advertisement will mislead a consumer depends not only on the advertisement itself but also on the background knowledge and sophistication possessed by the consumer. For a time, backed by decisions of the U.S. Supreme Court, the FTC applied an ignorant person standard according to which an advertisement need only mislead the most gullible consumers in order to be deceptive. Invoking this criterion, the FTC once found deceptive Clairol's claim that its hair coloring would color hair permanently on the grounds that some (particularly naïve) consumers might interpret this to mean, falsely, that Clairol would color all the hair to be grown in a user's lifetime. More recently, however, the FTC has adopted a more lenient approach. Since advertisers typically dispute FTC allegations that their claims are likely to mislead, the agency often relies on extrinsic evidence, usually in the form of consumer surveys, to show that a significant percentage of consumers have formed materially false beliefs as a result of exposure to particular advertisements. Typically, the threshold percentage for FTC prohibition is in the range of 20% to 25%. In this way, regulators can be seen as attempting to strike a balance between the costs of suppressing informative claims and the benefits of suppressing deceptive claims.

In both its ordinary and legal senses, however, deception is a much broader concept than either that of lying or falsity. One can deceive without lying, because while lying necessarily involves an explicit statement by the speaker, deception can occur by variously distorting, withholding, or manipulating the truth. Deceptive advertising is, thus, often quite different from false advertising, if by "false advertising" we simply mean advertising that makes false statements, even though the two expressions are often treated colloquially as synonyms. Advertisements can be deceptive without explicit falsity, such as when they mislead by omitting crucial facts or by taking advantage of consumer ignorance. They can also make false claims without being deceptive, such as when what is literally claimed is so improbable or ridiculous that no one is likely to be deceived by it. Exxon gasoline's once-famous claim to put a tiger in your tank is a case in point.

The Variety of Deceptive Advertisements

FTC cases have involved a wide range of practices that the agency has found deceptive in particular instances, including false written and oral representations, misleading price claims, sales of dangerous or defective products without adequate disclosures, the use of bait-and-switch techniques, failure to disclose information pertaining to pyramid sales, and a failure to meet warranty obligations.

The most straightforward cases involve explicit misrepresentation of a product or service, which thanks to regulatory efforts are now relatively rare. The more common and controversial cases, however, involve claims that advertisers imply but do not explicitly state. The pain reliever Efficin, for example, was claimed to contain no aspirin. Although literally true, the FTC found this advertisement deceptive on the grounds that consumers would naturally interpret this to mean that Efficin lacked many of the side effects caused by aspirin. This implied claim was false, however, since Efficin and aspirin are chemically very similar. A different sort of implication was involved in the famous Volvo advertisement that depicted a big-wheeled "monster truck" rolling over a line of cars, crushing all of them except the Volvo. The spot failed to disclose the fact that both the Volvo and the other cars had been specially rigged to produce this result. The implication that only a Volvo can withstand a monster truck intact was thus false. Advertisers are as responsible for the message consumers draw from an advertisement as they are for what is actually stated or shown.

A special kind of implication is addressed by the FTC's advertising substantiation doctrine, according to which advertising claims that do not have a reasonable basis are deceptive if the ad implies that such a basis exists. When Bayer claimed its children's aspirin to be superior to any other children's aspirin in terms of its therapeutic effect, the FTC held that Bayer implied a factual basis for this claim which the company lacked. Interestingly, even if such a claim is ultimately proven to be true, the advertisement making it can still be prohibited if the advertiser lacks a reasonable basis for the claim when it is originally made. In another case, advertisements for Promise margarine used the slogan "Get Heart Smart" and showed heart-shaped pats of the product on food items. The FTC found these advertisements deceptive because the manufacturer could not adequately substantiate the implied claim that using Promise helped diminish the risk of heart disease.

Comparative advertising raises especially thorny questions of implication. While relatively rare in Europe, comparative advertising has flourished in the United States since restrictions on it were lifted in the 1970s and 1980s. One kind of issue arises in incomplete comparisons. Suppose it is claimed of Brand X pain reliever that Brand X relieves pain faster—faster than what? Another kind of problem is raised by implied superiority claims. Suppose that Brand X is advertised with the line that no other pain reliever works faster. If Brand X relieves pain faster than some competitors but only as fast as others, is the advertisement deceptive? A further issue results if Brand X is claimed to both relieve pain faster than Brand Y and be long-lasting. Consumers may infer that Brand X is longer-lasting than Brand Y, which may be false.

This last issue arose in connection with Kraft's advertisements of its Singles line of cheese products. After years of losing market share to lower-priced imitation slices, Kraft began advertising the fact that Singles were made from five ounces of milk per slice versus hardly any for the imitation slices. Although these claims were true, the FTC objected to the fact that the same ads touted the calcium content of milk. As it turns out, much of the calcium contained in milk is lost during the cheese-making process, and many brands of imitation slices actually had more calcium than Kraft's Singles. Without knowing these details, however, consumers would likely infer that the calcium content of the Kraft product was higher than that of imitation slices.

Deceptive advertising in its various forms should be distinguished from mere puffery, which has long been treated permissively by regulators and the courts. A *puff* is an evaluative claim used by an advertiser, such as when a product is described as "the best," "best tasting," "the freshest," or "amazing." Strictly speaking, a puff cannot be legally deceptive. This is partly because the law regards such claims as mere subjective opinions that cannot be disproved. It is difficult, for example, to pin down the precise meaning of Tony the Tiger's exclamation that Frosted Flakes are great. Regulators also tend to assume that puffs are forms of hype and exaggeration that customers do not take seriously. This point is sometimes questioned, however; were it really true that customers do not believe puffed claims, advertisers would stop using them. Particular examples sometimes raise difficult questions as to the distinction between evaluative and factual statements. If, for instance, the claim that a certain brand of beer has more flavor than competitors is taken to imply that a majority of consumers agree, the implied claim is factual and not purely evaluative. In general, the more vague and imprecise the puff, the less likely it is to be found legally actionable.

Advertisements directed at children are also a special case. It is widely acknowledged that children are particularly vulnerable to advertisers' enticements, and the FTC has accepted special responsibilities in this regard. Still, many authors complain that regulators have not done enough to curb abuses, especially since in much programming aimed at children the lines between commercials and entertainment have become blurred.

Product placements and the so-called stealth advertising are increasingly common forms of advertising that also seem at least potentially deceptive. A product placement occurs when an advertiser pays producers of a television show or movie to integrate its product into the story. The potential deceptiveness of the practice is that viewers may not be aware that the product has been included only because a fee has been paid. Stealth advertising is a practice whereby people are paid to tout a product under the guise of doing something else. For example, a camera company might hire representatives to pose as tourists, standing on street corners in a large city and asking passersby to photograph them with a new camera the company is marketing. Those who agree to the request end up holding and using the new camera—the purpose of the ruse, from the company's perspective—although the passersby may quite naturally believe that they are merely doing a stranger a favor. Thus far, however, both these practices have escaped serious regulatory attention. As advertisers invent new methods of pitching their products, however, further questions about deceptive advertising can be expected to arise in the future.

—Samuel V. Bruton

See also Advertising, Subliminal; Advertising Ethics; Bait-and-Switch Practices; Bluffing and Deception in Negotiations; Consumer Fraud; Deceptive Practices; Fraud; Honesty; Marketing, Ethics of; Truth Telling

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Deceptive Practices

Deceptive practices are incidences of unfair or deceptive acts that are deliberately made against consumers by businesses. In commerce, sellers may not omit, misrepresent, or make false statements that lead to a consumer decision that is injurious. Deceptive practices are formally defined in Section 5 of the Federal Trade Commission Act (FTCA) and administered and enforced by the Federal Trade Commission (referred to here as the Commission).

The FTCA prohibits unfair and deceptive practices in or affecting commerce. The Commission is an independent federal agency and the only organization sanctioned to enforce the FTCA. It is empowered to act in the interest of all consumers to prevent deceptive and unfair practices and protect consumers from commercial enterprises that mislead or affect consumer behavior or decisions about a product or service. It also has the authority to stipulate interpretive rules and general statements of policy. The Bureau of Consumer Protection is a part of the Commission, and it works directly with the consumer to enforce federal laws, provide information to educate consumers, and process fraud or identity theft complaints. The Commission's jurisdiction encompasses a wide variety of entities and individuals, including interstate and foreign commerce.

As incidences of deceptive and unfair practices have increased, consumer protection laws have expanded. For example, the Fair Credit Billing Act requires businesses to investigate billing errors and provide the consumer with a written acknowledgment of the complaint before the consumer's credit rating is affected. There are many more laws that are aimed at protecting consumers from harmful, unfair, and deceptive business practices. Most states have chosen to enact additional laws that increase the level of consumer protections and, in some cases, include both criminal and civil penalties. It varies by state.

The Commission is authorized to investigate, prohibit, and enforce the laws under its jurisdiction. Victims of deceptive practice may file a claim with the Commission. Following a review, the Commission will determine whether a harmful or deceptive practice has been committed. The accused must dispute the claim that is being investigated. If an appropriate rationale is not offered, the Commission will request a cease and desist order. If the issue perpetuates, it may be addressed in the civil courts in which the Commission will make a recommendation and report its findings to enforce a ruling. The Commission is involved with only civil suits, and it may impose fines up to $11,000.

Under the FTCA, commercial enterprises must not engage in harmful practices that deceive consumers. Some examples of deceptive practices include scams, false advertising, identity theft over the Internet, monopolistic practices, and bait-and-switch advertising techniques. For example, Microsoft Corporation was sued when it introduced its Vista operating system. It was accused of deceptive practices because the company had allowed personal computer makers to promote computers as "Windows Vista Capable" before the product was released in order to, allegedly, maintain strong sales between the time of the announcement and the release date. When Vista was released, consumers discovered that its compatibility with PCs bought the prior year was only applicable to one version of the software, the more basic version. Microsoft was accused of a "bait-and-switch" technique, where it lured its customers into buying PCs that did not support the functionality of all versions of the Vista software.

There are numerous ways in which an entity or individual may engage in deceptive practices. Two large areas include deceptive advertising and security of information on the Internet. Advertising claims must be truthful and not mislead consumers. If there are disclaimers, disclosures, warranties, or guarantees, they must be obvious and clear. In addition, a typical consumer must be able to replicate the claims made in testimonials and endorsements. If a seller engages in deceptive practices, it must refund the customer if the promise cannot be fulfilled.

There is an immense amount of personal data on the Internet that includes confidential and sensitive information. It requires a high level of security and protection. Privacy is at issue. Despite the steps to deter security breaches, unauthorized individuals can gain access and immediately collect, analyze, package, and disseminate personal information. These deceptive practices may result in identity fraud. In 2006, 8.9 million people were victims of identity fraud in the United States, and the 1-year cost was estimated to be $56.6 billion. Both businesses and individuals are victims. A common example of identity fraud is when consumers respond to an official-looking e-mail and supply personal information such as credit card numbers. The e-mail may request a contribution for a new business venture, for example. Actually, this information is then used to deceptively represent the person in another financial transaction. These transactions can be costly—the average cost to victims of identity fraud was $6,383 in 2006. Consumers must be cautious and aware, and businesses must be truthful and clear.

Conclusion

Businesses have dual responsibilities with regard to consumer protection and preventing deceptive practices. First, they have an obligation to the consumer to not mislead or deceive when advertising and promoting products and services. They must consider consumer protections and business integrity in strategic plans and business conduct. Second, businesses have a commitment to the consumer to inform them of how they will use and protect information privacy. Businesses must take the necessary steps to ensure that data are safeguarded and maintained properly for consumers. Businesses have an opportunity to provide a leadership role in developing industrywide practices that endorse and promote consumer protections and ethical operations, minimizing the opportunities of those who choose to engage in deceptive practices.

—Pamela C. Jones

See also Bait-and-Switch Practices; Better Business Bureau (BBB); Deceptive Advertising; Federal Trade Commission (FTC); Identity Theft; Unfair Competition

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Decision-Making Models

There is no one model of decision making. Rather, there are many theories of decision making, each of which tends to be associated with a particular area of scholarly inquiry and has different assumptions about human nature, the manner in which decisions are made, and the quality of the decisions made.

This entry organizes the many theories and approaches to decision making into four broad approaches that inform, or are found in, business and society literatures, other than ethical decision making since that theory has its own entry. First, *rational decision making* is an orderly, cognitive process where individuals form probability estimates of outcomes to select between different courses of action. Second, *political decision making* emphasizes power and dependence; the balance of power among people influences decision makers' assessments and results. Third, the *garbage can model of decision making* emphasizes decision makers' uncertainty and lack of control over external and internal factors key to a decision. Finally, *improvisational decision making* views decision making as a real-time process where decision makers harness their intuition and spontaneity to identify, evaluate, and pick options. This last model was developed largely in response to the shortcomings of the first three models. When decision makers consistently rely on a single style of decision making, it can influence their ability to make moral judgments (explore the ethical implications around a decision) and take moral action (behave in a way that is ethical).

Rational Decision Making

The rational model of decision making claims that individuals engage in strict cerebral rationality when making decisions. Decision making is viewed as a sequential process that consists of (1) problem definition, (2) alternative generation and evaluation, and (3) decision selection and implementation. During the first two stages of rational decision making, individuals engage in an exhaustive and systematic search for information. To arrive at a selection among alternatives, individuals typically engage in a detailed cost-benefit analysis. However, cognitive constraints limit individuals' ability to explore alternatives comprehensively; they commonly readjust objectives and usually settle for a "satisfactory" instead of an "optimal" decision. These constraints generally come from two sources. First, many individuals lack full information; thus, the selection among alternatives is necessarily limited to selection among known alternatives. Second, human cognitive limitations contribute to this lack of information. For example, individuals cannot accurately foresee or predict all the possible consequences of their decisions, and thus, complete evaluation of the consequences of alternatives is not humanly possible. This is a variation of the model known as boundedly rational decision making; individuals who intend to be perfectly rational are limitedly so.

Many managers employ a decision-making style that is consistent with the boundedly rational decision-making model. When faced with a decision, the individual first generates a comprehensive list of pros and cons of various alternative paths of action. They will also describe using procedural methodologies to distill alternatives in order to arrive at a decision. Ultimately, decision making is viewed as a measurable, mechanistic, and routine process that they can control and over which the individual has significant authority. Most economic theories are based on the assumption that individuals are rational decision makers.

When individuals rely predominantly on one form of decision making such as the boundedly rational model, the way in which they view the decision-making process also mirrors how they view the associated ethical implications—that is, how they make moral judgments and take moral action. Decision makers who rely on rational decision making typically develop a rigid and formal set of rules to negotiate the ethical implications of their actions. Their moral judgments sometimes lack depth, as they view ethics as a systematic series of rights and wrongs with little room for gray. They tend to see moral action as a behavior that must be justified by a favorable cost-benefit analysis; efficiency tends to dictate individuals' (particularly managers') interest in ethics and morality. Decision makers often force their interpretations of the ethical implications around decisions into neatly identifiable parcels of information; they do their utmost to simplify ethical dilemmas and make them unambiguous.

Power and Politics Decision Making

The power and politics model of decision making advocates that decisions are the result of individuals competing with one another to satisfy their individual interests. Since self-interests are often conflicting, the decision-making process involves the use of influence, political tactics, and negotiation between different power bases across individuals and organizations. Decision makers who employ the power and politics model of decision making are frequently less concerned with developing reliable and valid decisions and more concerned with finding ways to ensure that their decisions are accepted and supported by others in power. They view decision making as a social interactive process where political gaming is the key function of the decision maker. Decision making consists of lobbying in key individuals both formally and informally to rally behind certain decisions. Political decision making consists of manipulating information, forming coalitions, stacking groups to influence decision evaluations and outcomes, and even attempting to remove naysayers. Individuals' understanding of the established power bases in the internal and external environment substantively influences their decisions.

Managers using power and politics decision making tend to be unconcerned that politicking often distorts information, usurps a tremendous amount of valuable time, and omits input from less powerful, although key, stakeholders within the organization. Managers who rely on the power and politics model of decision making are more concerned with outcomes than process. Increasing one's own power is also a key goal of managers who invoke the power and politics model.

Ultimately, self-interest guides the moral judgments for individuals and managers deeply involved in the power and politics model of decision making. Depending on their goals, managers will often repress their own moral judgments, espousing instead the ethical views of the most powerful stakeholders within the organization. However, if invoking a certain stance on morality and ethics can help influence members of the powerful coalition, managers will make strong moral judgments. Insightful and reliable moral judgments and consistent moral action are not strengths of individuals and managers who rely heavily on the power and politics model of decision making.

Garbage Can Decision Making

The garbage can model of decision making stresses the roles of chance, luck, and timing in decision making. Decisions are a random convergence of problems, solutions, participants, and opportunities. The garbage can model assumes that decision makers face so much complexity and ambiguity that decision making is essentially a haphazard, anarchical process. Unlike other models of decision making, garbage can decision making is not deliberate and purposeful. Managers do not consciously identify issues and problems and undergo a logical process to arrive at a decision. Instead, decision makers often stumble accidentally on a decision or are forced to make a decision with almost no preparation or time for deliberation. The quality of decisions made in this manner is often poor.

In this model of decision making, the context of the decision has a larger influence on the actual decision outcome than the characteristics of the decision maker. This is because the individual has so little control or power over the decision. Individuals employing garbage can decision making typically cannot consciously make moral judgments or take moral action, because this would require some level of intentionality on the part of the decision maker. Under the garbage can model of decision making, a problem randomly meets an opportunity and the decision maker makes a decision. The decision itself is unlikely to be rich and insightful, drawing a discerning path toward success. Instead, the decision will likely be superficial and one dimensional. The associated moral judgments and actions are also likely to look similar.

Improvisational Decision Making

Of all the models of decision making presented thus far, improvisational decision making is in the early stages of theoretical development and empirical support. Its development was a response to the inability of existing models to address dynamic decision-making contexts. Many of today's individuals and managers are under pressure to make fast, adaptive, and innovative choices. Under such pressure, individuals are likely to behave rationally but will also have to improvise; in short, decisions are not random but rather intentionally spontaneous and action oriented. Moreover, almost no decisions are as exclusively rational, political, or haphazard as the rational, power and politics, and garbage can decision-making models, respectively, imply. Theories of improvisational decision making are being developed both in response to increasingly high-velocity and uncertain business environments and also in response to the complexity of goals that managers should and do pursue. Improvisational decision making makes use of any relevant information and resources, including intuition, insight, real-time information, creativity, emotional sense making, opinions of others, and trial-and-error learning.

Individuals who rely on an improvisational decision-making process tend to depend less on common sources of knowledge and more on peers for information. For example, managers regularly engage in constructive conflict to quickly evaluate alternative paths of action and rely on role playing, scenarios, and frame-breaking techniques to stimulate discussions while defusing interpersonal tension. They are committed to being open, repeatedly listening to alternative and out-of-the-box points of view without discarding them instantaneously. This principle does not mean that managers who invoke the improvisational decision-making model agree with everything they hear but that they seek, value, and consider diverse viewpoints when making decisions. To be successful, managers find themselves in fast-paced environments in which there is frequently no time to engage in the detailed cost-benefit analyses suggested by rational decision making. Instead, in fast-paced environments, surprise, urgency, and uncertainty are commonplace and individuals must put aside power struggles, focus on the common goal, and rely at any moment on the most appropriate person to lead the decision. Shared leadership is an important characteristic of improvisational decision making.

Strict rules or rigid processes do not significantly govern individuals who use improvisational decision making, thus engendering a certain degree of latitude in the kinds of moral judgments they can make around specific decisions. For example, ethical decision making requires managers not only to wade through issues around right and wrong, but they also have to consider the consequences of their decisions on themselves, their business unit, their organization, and society. It is reasonable to assume that this wading-through process will be challenging, iterative, and nonlinear and require a great deal of cooperation between various stakeholders. Given that managers who engage in improvisational decision making are open to other ideas and perspectives, are willing to work with stakeholders both inside and outside the organization, operate in team environments, and are able to tap into the inherent rhythm of their organization, the moral judgments that result are likely to be diverse and inclusive. However, the relationship between moral judgments and moral action is unlikely to be consistent as managers rely on information that is changing and share control with those around them. Moreover, the velocity associated with improvisational decision making can lead to inexperienced managers glossing over key ethical implications surrounding decisions.

Unfortunately, the mainstream management literature has made minimal progress so far in integrating ethics with the well-established decision-making models such as bounded rationality, power and politics, garbage can, and improvisation. This is unfortunate since decision-making styles have important implications for how individuals and managers make moral judgments and take moral action.

—Ariff Kachra and Karen Schnietz

See also Bounded Rationality; Business Ethics; Cost-Benefit Analysis; Economic Rationality; Ethical Decision Making; Ethical Role of the Manager; Expected Utility; Information Costs; Motives and Self-Interest; Perfect Markets and Market Imperfections; Rationality; Satisficing; Self-Interest; Strategic Planning; Strategy and Ethics; Transaction Costs

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Deep Ecology

Deep ecology is primarily an environmental philosophy—or "ecosophy" as some call it—which holds that there is a pressing need for humans to radically change their relationship to nature and to recognize that nature has an inherent value and is not to be taken as valuable solely for its usefulness and instrumentality to humans. Deep ecology also offers a new definition of the self that differs from traditional notions, and it designates a social movement that sometimes has religious and mystical undertones. This philosophy, taken together with a number of other competing schools of thought and environmental practices such as the science of ecology, conservationism, and protectionism, among others, comprises the general idea of environmentalism. But taken as an ecosophy, deep ecology distinguishes itself by making broader and more basic philosophical claims about matters in metaphysics, epistemology, and social justice.

The practitioners of deep ecology often draw a contrast between their own position and what they refer to as "shallow ecology." This designation is employed since they hold that the movement of ecology reflects a hidden bias. At first glance, it seems to be concerned with topics such as pollution, resource depletion, and overpopulation, but on examination one will find (according to the deep ecologists) that these concerns are real only to the extent that these topics have a negative effect on the ecology of an area and have the result of disrupting human interests. From the perspective of the deep ecologists, then, the main concern of environmentalists is not the environment, but how humans will be affected. Ecology or environmentalism is shallow in this view, since its focus is narrow on humanity rather than on the whole of the biosphere, and its bias is a form of anthropocentrism that needs to be rectified by replacing this attitude with that of ecocentrism or biocentrism where the biosphere becomes the focus of concern instead of humans.

What the deep ecologists would rather see is the prevalence of an attitude or belief system that moves away from anthropocentrism toward a more inclusive philosophy where respect for nature and the role of humans in nature are central. Anthropocentrism is typified as a human-centered attitude that sees humans as the source of all values and disproportionately tips the relationship between humans and nature toward benefiting humans. It contains an instrumentalist view of nature and a view of man as the conqueror of nature, subduing it into submission and standing in domination of it. Anthropocentrism gives credence to practices where man only values nature for its uses, and then goes on to abuse nature to the point of environmental degradation. Such a relationship is descried by deep ecologists as being unproductive and destructive and standing in need of change.

Arne Naess and Deep Ecology

Deep ecology first appeared in the early 1970s and was developed and promoted in the writings of Norwegian Arne Naess. By the time Naess had introduced the phrase "deep ecology," environmentalism was already under way as a grassroots movement. Conservationism and environmental protection were being advanced as intelligent responses to what was becoming more and more obvious about the natural environment thanks to the science of ecology. Ecologists were demonstrating the interconnectedness between living things and their environment, and it was being suggested that human activity, especially the products and by-products of industrial activity, was disrupting the balance between them. Steps needed to be taken, according to the environmentalists of the day, which would conserve and protect nature so that humans could continue to flourish. This can be taken as the beginning of the modern environmental movement that has evolved today into practices that strive to achieve sustainability.

In this context, Naess suggested that much more than just some steps toward conservation and protecting the environment were necessary. He held that we needed to reevaluate our understanding of human nature in a radical way. In particular, he claimed that environmental degradation was likely due to an inadequate realization of the human self that had been ill defined in the past. According to Naess, the self traditionally has been seen in too narrow a form as a kind of solitary and independent ego among other solitary and independent egos. This propensity to understand the human as primarily an individual, cut off from others and from its surrounding world, leads to the pitfalls of anthropocentrism. What is now necessary, given the insights of the environmentalist movement, is a new understanding of the self that Naess has referred to as "self-realization."

In the deep ecology view, the self should be understood as deeply connected with and as part of nature and not disassociated from it. Deep ecologists often call this conception of human nature the "ecological self," and it represents humans acting and being in harmony with nature and not in opposition to it. According to Naess, when this ecological self is realized, it will also recognize and abide by the norms of an environmental ethic that will end the dominance, subservience, and abuses of nature that typifies the traditional ecological self that is trapped in the anthropocentric attitude. The ecological self respects the diversity and richness of nature, sees itself as part of nature and as part of an "ecological holism," and acts accordingly. Moreover, it will see the virtues of practicing a kind of "biocentric egalitarianism" in which each natural entity is held as being equal to every other entity with regard to their inherent value. In short, Naess holds a nontraditional view of the self that connects it with nature and defines it according to environmental dictates.

The Deep Ecology Platform

In 1984, along with George Sessions, Naess devised an eight-point statement or platform for deep ecology that the two wrote while on a hiking trip in Death Valley, California. Unlike other platforms, this set of planks was not offered as a rigid or dogmatic manifesto. Instead the deep ecology platform was designed as a set of fairly general principles that could help people articulate their own deep ecological positions. It was also meant to serve as a guide toward the establishment of a deep ecology movement. The ensuing social movement had as its aim the formulation of new policies that would reflect the ideological base of deep ecology, and the platform also suggests that there is some ethical obligation for people who espouse the intellectual claims of deep ecology to go on and engage in activism that would result in the new policies called for in the platform.

Among the eight planks in the platform, there is a consideration of topics such as biocentric egalitarianism and ecological holism, although these more academic-sounding terms are not used in the document itself. What is claimed early in the eight points is that both living and nonliving entities have intrinsic worth independent of any instrumental value that they may have. Furthermore, because the richness and diversity of natural life are also valuable, humans have no right to reduce the levels of richness and diversity except to satisfy human need. But, nonetheless, humans have interfered with the nonhuman world excessively, and this interference grows worse as the human population continues to grow exponentially, presenting various dangers to the natural world such that there is a necessity for a decrease in the human population if nature is to flourish at all in the future. These ideas comprise the first five points of the platform.

The remainder of the document is a call for activism based on the expressed beliefs that anthropocentrism and human activities that promote only human interests are a threat to the richness and diversity of nature. Here, one finds a more sustained critique against both human economic activities and the advances of technology that the platform suggests can be cited as reasons for the degradation of nature. The platform expresses the need for changing public policies in these areas so that they reflect an appreciation of life rather than the promotion of an increasingly higher standard of living. What is also at issue in this section of the platform is an attempt by Naess and Sessions to underscore a belief that business and commercial enterprises have played a major role in the interference of the nonhuman world and in the reduction of the richness and diversity of nature. Their negative references to the ever-present goal of increasing people's standard of living might be taken as a backhanded critique of what has been called "conspicuous consumption" that has created the "consumer society," which is often defined as an overconsumption of those people living in the more economically developed nations and egged on by businesses eager to engage in production to meet the increasing consumer demands. These references may also be taken as some of the deep questions that Naess said needed to be posed for deep ecology to surpass shallow ecological thinking.

Deep Ecology as a Social Movement

The eighth and final plank of the deep ecology platform by Naess and Sessions is one that refers less to any ideological axiom of deep ecology as it does to the practical obligations of those who adhere to the claims and critique of the first seven planks. Here, the emphasis is on doing and a call to activism. The plank says that those who have agreed with the foregoing ideological aspects of deep ecology have an obligation to participate in the attempts at change. Of all the differing philosophies that can be said to compose environmentalism, deep ecology is the one that has generated a following such that it has been called a social movement, and this call for activism in the deep ecology platform counts as one reason why this has been the case.

Deep ecologists formed something of a grassroots movement made up of those who held a set of diverse positions on the environment. It should come as no surprise that in its early days the social movement of deep ecology was more akin to a loosely knit array of followers and factions coming from the ranks of groups such as feminists—who in this context are often called "ecofeminists"—pacifists, "social ecologists," mystics, and postmodernists. Each of these diverse groups brings to bear its own perspective in its interpretation and critique of what deep ecology ought to be and in what directions it ought to proceed. The ecofeminists, for example, argue that *andro*-centrism, rather than anthropocentrism, is the genuine cause of the degradation of nature. They claim that "male centeredness" as seen in traditional, power-wielding patriarchal society is responsible for the striving to dominate nature. Just as males have always tried to dominate women, so too have they tried to make nature subservient and bend to its will, according to the ecofeminist critique.

Another faction forming the grassroots of the deep ecology movement was called "social ecology." According to this view, the problems of environmentalism are due to a defect in society that manifests itself as an authoritarian hierarchy that, this group says, is also responsible for such social ills as racism, sexism, and classism. For social ecologists, environmental problems such as global warming or species decimation are caused in the same way as major social problems such as poverty and widespread crime. These can all be attributed to a social structure where only some enjoy real power, while the majority remain powerless. For the social ecologists, how humans treat one another in society gives evidence as to why there is environmental degradation, and until such social conditions are addressed, environmental concerns will continue.

Some critics of deep ecology stand external to the social movement that bears the name and here the claim is often that deep ecology is a movement based on mysticism and that it appears to be more of a religion than a rational approach to environmental matters. In fact, these critics will point to the creation of the "Church of Deep Ecology" that was formed in Minnesota in 1991 as an example of how this movement had devolved into more of a spiritual and mystical approach to nature than as a way to solve environmental problems and issues. The claim was that deep ecology was similar to the religions of the American Indians or to pantheists and pagans who worship nature. This matter came to a head in a lawsuit, *Associated Contract Loggers v. United States Forest Service*, in which it was argued by the timber industry that Forest Service decisions were tantamount to privileging deep ecology–related environmentalists who they understood to be part of a religious movement. Their argument was, therefore, based on the required federal separation of church and state, but the case was dismissed in 2000.

As this legal case suggests, the deep ecology movement has made attempts to have an impact on business and industrial practices. As seen above, the deep ecology platform is openly critical of the culture of industry for having encouraged the creation of an overly consumptive society and for allowing nature to be reduced to a mere instrument to fulfill human desires. The Foundation for Deep Ecology has taken up an antibusiness, pro-environment theme by backing projects that have offered changes in social policies that have been established by the industrial development model. It has published books dealing with the "tragedy of" forestry and agriculture, for example, and another that is critical of livestock production. The Foundation for Deep Ecology was created by Douglas Tompkins, who has dispersed much of his fortune earned in the fashion industry (he and his wife had helped start The Northern Face and the Esprit brands) to ecologically minded groups. It is therefore with some irony that money made in business transactions has found its way into the deep ecology movement that has been anything but a friend to business.

—Peter Madsen

See also Anthropocentrism; Biocentrism; Biodiversity; Environmentalism; Environmental Protection Agency (EPA); Environmental Protection Legislation and Regulation; Global Business Environments; Green Revolution; Green Values; Individualism; Instrumental Value; Intrinsic Value; Moral Standing; Natural Resources; People for the Ethical Treatment of Animals (PETA); Self-Realization; Speciesism; Stewardship; Terrorism; Wilderness

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Deferred Compensation Plans

Deferred compensation plans refer to arrangements in which employees defer some portion of their current income until a future date. Wages earned by an employee in one period are actually received by the employee at a later date. The overall effect is to postpone taxation for the employee until compensation is received, usually in retirement.

Deferred compensation plans are either qualified or nonqualified. Qualified deferred compensation plans receive certain tax preferences under the Internal Revenue Code; most notably, employers are entitled to a tax deduction for the amount of money they contribute to the plan. While the funds remain in the plan, the benefits grow on a tax-deferred basis to the employee until they are actual paid. Qualified deferred compensation plans are designed mainly to provide cash payments in retirement or to defer taxation to a year when the recipient is in a lower bracket. To be a qualified deferred compensation plan, the benefits available under the plan have to be nondiscriminatory, which prohibits an employer from providing benefits for highly compensated employees to the exclusion of all other employees. In addition, the employer has to comply with regular reporting requirements and is limited in the amount of contributions it can make to the plan.

A nonqualified deferred compensation plan is also used to postpone taxation for the employee until compensation is received, but employers do not receive favored tax treatment. Employers are not entitled to tax deductions until these benefits are actually paid to the employee or the employee receives the rights to the benefits. The advantage of a nonqualified deferred compensation plans is that the employer can choose who receives the benefits without regards to years of service, salary, or any other criteria. Often the recipients of this type of plan are officers, executives, and other highly paid employees. Nonqualified deferred compensation plans are less expensive to set up, there are no significant reporting requirements, and employers can contribute unlimited amounts of money to them.

Social and Ethical Issues

A major component of nonqualified deferred compensation plans is stock options grants. These grants represent the right to purchase stocks at a given "grant" price within a certain time. If the underlying stock increases in value, the option becomes more valuable as the employee is able to exercise the option and purchase the stock at the grant price, which is below market. If the underlying stock decreases in value below the grant price or stays the same in value as the grant price, then the option becomes worthless. Corporations use stock options grants not only as a tool to delay compensation into the future but also as an incentive for executives to make decisions that will result in an increase in future value of his or her holdings. In other words, an executive who holds stock option grants will make company-based decisions that will increase the value of the firm, thereby increasing the value of the stock option grants and, thus, their personal wealth. Some of the social and ethical issues surrounding the use of stock option grants in deferred compensation plans include the accuracy and disclosure of stock option grants, distributive justice in the case of large stock option grants, the relationship of actual performance to the award of stock options grants, and their use in "golden parachute" arrangements.

Accuracy and Disclosure of Deferred Compensation

Disclosure to stockholders and other stakeholders of the actual compensation paid to executives under deferred compensation has been an ongoing concern. Although gains from exercising nonqualified stock options are treated as an expense for tax purposes, historically there is usually no accounting expense recorded either at the time the stock options are granted or exercised. Concern exists about what is the true value of compensation received by executives and whether the value of stock options granted are more than the direct cash payments the executive receives.

The failure to expense the value of stock options granted to executives appears to contradict the objectives of financial statements, which are supposed to be fully transparent and report the fair values of all assets, liabilities, exchanges, and transactions that could potentially affect the investor's equity position. Proponents of expensing stock options argue that expensing them would provide more informative financial statements and improve the credibility of reported earnings. Furthermore, expensing them would discourage pay plan designers from using excessive amounts of stock options and would make executive compensation more transparent to stakeholders.

In 1995, in response to stockholders and other stakeholders concerns, the Financial Accounting Standards Board (FASB) recommended that companies expense the fair market value of stock options granted. However, due to pressures by these same nondisclosing firms, FASB allowed firms to disclose the value of stock options in a footnote to the financial statements instead. Until late 2003, only a handful of companies adopted FASB's recommended approach of expensing stock options, and the rest chose to disclose the value of stock options in footnotes. FASB readdressed the issue of expensing stock options after the accounting scandals of the early 2000s. Effective June 30, 2005, FASB mandated that all stock option compensation be expensed. The Securities and Exchange Commission granted a 6-month deferral to the implementation of these standards, moving the effective date of expensing stock option to the end of 2005.

Distributive Justice and the Size of Grants

In the early 2000s, on average, 60% to 70% of a company's CEO compensation was composed of stock options received under nonqualified deferred compensation plans. The average annual value of total stock options granted by Fortune 500 companies was more than $230 million, with the average CEO receiving just more than $7 million in stock options. For larger firms, the total value of CEO stock options granted exceeded $100 million.

Stakeholders of firms are often concerned about the size of these stock options grants and wonder whether they are excessive. Some argue that the total value of these grants violates the principles of distributive justice inasmuch as the large stock option granted to executives are in effect transferring wealth from shareholders to executives as the additional shares purchased by executives dilute the value of each share of stock held by the shareholders. Critics also argue that the concentration of wealth in the hands of corporate executives results in society's wealth being distributed unjustly and that new social arrangements aimed at preventing this concentration are needed to achieve justice.

Incentive Base

Corporate boards and executives often justify the use of stock options as part of deferred compensation plans on the grounds that they effectively link pay to performance. Critics argue that company executives are overpaid for the value they provide to the firm and are given stock options regardless of performance. Research has found little evidence to support management's argument as study after study has found no significant relationship between executive compensation and firm performance. Thus, many stockholders and stakeholder activists are pushing boards of directors to more closely align executive pay to corporate performance.

This issue has regained increased interest in response to the accounting scandals of the early 2000s. The questionable behaviors of highly paid executives at Enron, WorldCom, Global Crossing, and other companies have been caused allegedly by the escalation in stock option grants due to the excessive risk taking and an excessive fixation on stock prices by company executives. The perception is that the compensation committees of these companies did not act independently of management when determining their compensation and just rubber-stamped management desires.

The result of these perceived abuses has led to the passage of the Sarbanes-Oxley Act of 2002. The act creates pressure on the compensation committees to do a better job of evaluating performance (company and personal) before making base salary changes, awarding stock options or other variable payments, or approving any other special financial treatment. In addition, the act requires full disclosure of all executive compensation and allows shareholders to sue if they suspect that company's profits are being siphoned off through excessive executive compensation. It is hoped that making compensation committees more responsible for executive compensation and making compensation information more transparent will more closely align executive compensation levels with firm performance.

Golden Parachutes

Golden parachutes are provisions in employment contracts of top management that provide for compensation in the event of a loss of job following a change in the organization's control. This provision is usually adopted as an antitakeover strategy and is used as a precautionary measure against mergers and takeovers. Golden parachutes can come in a variety of forms, including additional stock option grants along with earlier vesting of stock option grants. Companies argue that they need to use gold parachutes in order to attract and retain qualified management personnel who will act in the best financial interest of shareholders and to maintain a competitive executive compensation package.

There has been increasing criticism from shareholders and other stakeholders concerning the size and use of the golden parachute clauses. From a stakeholder viewpoint, golden parachutes provide one group of stakeholders, management, with protection against hostile takeovers, while other lower-paid employees often receive layoff notices. They also argue that golden parachute payments seem unnecessary because managers of a firm are paid to act in accordance with their fiduciary duties to shareholders. Thus, golden parachutes should not be necessary to align managerial interest with shareholder interest. Others argue that if a golden parachute clause is necessary to align stockholders and managerial interest, then the preferable alternative would be stock options. This argument further contends that insofar as managers are already compensated with stock and stock options, the interests of shareholders and managers are already adequately aligned without the need of a golden parachute.

Conclusion

The size of deferred compensation plans given to top company executives continues to be the focus of much stakeholder attention. These large awards often lead to discussions concerning fairness, corporate governance, greed, ethics, and CEO compensation. The large gap between executive pay and that of other employees of the firm supports the view that some injustice must account for the difference. Furthermore, stakeholders question whether firm performance justifies the size of these awards. As a result of this controversy and dissatisfaction, improved rules on the proper accounting and disclosing of stock options grants have been put in place. Increasingly, new accounting rules and regulations are putting more pressure on boards of directors, compensation committees, and CEOs to be clear and transparent about the deferred compensation plans they receive and to ensure that the decisions they make are justifiable.

—Lois S. Mahoney

See also Agency, Theory of; Communitarianism; Consequentialist Ethical Systems; Executive Compensation; Incentive Compatibility; Justice, Distributive

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Deontological Ethical Systems

Deontological ethical systems maintain that an action can be morally right (a duty or an obligation) even if an alternative action in a given situation would have better overall consequences. Theories of this type thus deny what consequentialist ethical systems affirm, namely, that morally right actions are all and only those that have optimal consequences. (*Nonconsequentialism* is often used as a synonym for *deontology*.) While deontological and consequentialist views sometimes differ as to whether particular actions are morally right or wrong, these disagreements stem from a more basic dispute about what *makes* right acts right and wrong acts wrong. In contrast to consequentialists, deontologists generally hold that actions are morally right insofar as they accord with principles or rules that require something other than simply bringing about desirable states of affairs. A wide variety of moral principles fit this description, and deontological ethical systems encompass many conceptions of moral justification. The theories of Immanuel Kant and W. D. Ross are the ones that deontologies most frequently encountered in business ethics, but John Rawls's influential theory of justice is also deontological, as are contractarianism, some natural law theories, libertarianism, rights-based theories of ethics, Divine Command theories, and the Golden Rule.

Variations and Misconceptions

Although the term derives from the Classical Greek words for duty (*deon*) and study or science (*logos*), deontology began to be used in the 20th century as a way to refer to moral theories that lacked the structure distinctive of consequentialism (and act consequentialism in particular). Consequentialist views begin with a conception of the ultimate nonmoral good, such as happiness for the utilitarian, and then define moral rightness instrumentally, as that which maximally produces or most effectively promotes the good. Deontological theories deny that rightness is dependent on goodness in this way. Some deontological theories are pluralistic in the sense that they posit a set of unrelated and nonderivative moral rules or precepts. The Ten Commandments and Ross's theory of prima facie duties take this form. Other deontological views are founded on a single overarching principle. The Golden Rule and Kant's Categorical Imperative are foundational principles of this sort. In virtue of their principle- or rule-oriented structure, deontological ethical systems are often considered to better reflect commonsense morality than consequentialist views. We seem to believe that lying, stealing, promise breaking, exploitation, discrimination, and the like, are wrong even when their results are desirable; even noble ends do not always justify the means.

In virtue of their nonconsequentialism, it is sometimes thought that for deontological ethical systems the consequences of actions are irrelevant. However, denying that rightness is a matter of bringing about optimal consequences does not entail that the consequences of actions are of no moral significance whatsoever, and few deontologists have embraced this strong and implausible position. Rawls, whose theory of justice is decidedly deontological, writes that any moral theory that refused to take consequences into account in judging rightness would be irrational. And among Ross's list of prima facie duties is the duty of beneficence, which requires that we promote others' well-being. What deontologists deny, rather, is that the consequences matter *in the way* they do on consequentialist views. Similarly, in denying that rightness is a matter of maximizing good results, deontologists need not hold that rightness and goodness are unrelated in all respects. Kant claims that goodwill is the sole unconditional good. But since having goodwill, in his view, is a matter of being firmly committed to doing the right thing, goodwill is neither a nonmoral good nor an effect actions ought to maximize.

A related misconception is the thought that deontological theories are committed to absolute and exceptionless moral rules. In fact, few deontologists are absolutists in this sense. The tendency to associate deontology with absolute prohibitions is at least partly due to Kant, who notoriously argued that it would be impermissible to lie even to a would-be murderer to save a friend's life. It is doubtful, though, that either this harsh conclusion or an absolute rule against lying can be convincingly derived from any of Kant's various formulations of the fundamental moral law, the Categorical Imperative. Deontologists generally agree with ordinary moral thinking in holding that it is wrong to lie and yet there are situations in which lying is morally permissible. An analogous point would hold for other kinds of wrongs. Most business ethicists would say that the management of a firm has a fiduciary obligation to promote the financial interests of shareholders, but none would maintain that management should promote shareholders' interests at all costs whatsoever, for example, by disregarding the law or the basic human rights of employees, customers, and others.

Apart from their intuitive implausibility, deontologists have resisted endorsing absolutist rules because a system of such rules would produce irreconcilable conflicts of duty. Even still, any rule-based theory needs a means of handling situations where the rules give conflicting guidance. One strategy is to build exceptions into the rules themselves. In terms of the previous example, the relevant rule would not be "promote shareholder interests (no matter what)" but rather "promote shareholder interests unless doing so requires violating the law, basic human rights, or . . ." The problem with this approach, obviously, is that it is difficult to craft the rules so that all possible conflicts are avoided. Novel and unforeseen scenarios are bound to arise for even the most well-designed system. A second strategy is to incorporate a method for resolving conflicts of duty into the system as a whole. One way of doing this would be to prioritize or order the rules such that in cases of conflict, one rule takes precedence over the others. A firm's obligation to respect basic human rights, for example, might always have priority over the obligation to promote the shareholders' financial interests. Another way is suggested by Ross's theory. Ross posits various basic duties, such as the duty of fidelity that requires keeping one's promises and telling the truth. Although Ross's principles of duty are absolute in form, he maintains that these duties apply only at first glance. When two or more first-glance duties conflict, one's actual or all things considered duty can be determined only by weighing the significance of each duty to the circumstances at hand. Ross thus avoids claiming, say, that the duty of fidelity itself has exceptions or that another duty always takes precedence over it.

Deontology and Reasons for Action

The contrast between deontology and consequentialism can also be stated in terms of reasons for action. A consequentialist holds that reasons for action are always grounded in the goodness of the states of affairs that actions can bring about. From this perspective, however, the deontologist's claim that one can be morally justified in aiming at something other than optimal states of affairs can seem irrational. Why should one follow a rule when breaking it would produce more good? The response from the deontologist would be to deny the instrumentalist conception of rationality that the consequentialist's complaint presupposes. Consider Kant's respect for persons principle, which is of particular importance to contemporary nonconsequentialism. The principle commands that we treat persons as ends in themselves and never merely as a means. It rests on the idea that all persons have an intrinsic value or dignity—an incomparable worth "beyond all price"—in virtue of their status as free and autonomous rational agents. To Kant and many others, the appropriate way to respond to value of this kind is to respect the persons who possess it rather than trying to maximize the amount of it (e.g., by encouraging population growth), as a consequentialist approach would imply. In other words, according to Kant's principle at least some reasons for action direct us to act for the sake of values that already exist, as opposed to directing us to bring things of value or states of affairs into existence. It can be rational to act out of respect for someone without trying to produce a result beyond the action itself.

These divergent ways of conceptualizing the relationship between reasons for action and value can make a substantial difference in deontological and consequentialist analyses of particular cases. To a Kantian way of thinking, the reason that one ought to, for example, keep a promise to a customer is not that keeping the promise produces more good than breaking it (although it may do this). Moreover, the reason one ought not to subject employees to dangerous working conditions without their consent is not that doing so diminishes the total amount of well-being in the world (although this too may be true). Instead, the idea is that certain ways of treating people are incompatible with the intrinsic value and dignity of persons. The reason one should keep promises to customers, generally speaking, is that as persons, customers are owed the consideration and respect that promise keeping involves. Breaking a promise, particularly when this is done for questionable reasons, demonstrates disregard for the person to whom the promise has been made. Moreover, persons are entitled not to have their lives threatened without their consent in order to achieve higher profits or some other good. Using reasoning of this sort, the respect for persons principle is frequently invoked to ground and justify claims of human rights.

The Significance of Deontological Ethical Systems to Business Ethics

Although the instrumental conception of rationality found in consequentialism is also deeply embedded in economics, deontological ethical thinking is prominent in business ethics. While this is true for various reasons, two distinctive aspects of business ethics are worth mentioning in this regard. First, not only are contemporary moral claims commonly made in terms of rights, but rights are often the means by which we designate moral boundaries in competitive contexts such as business. Almost everyone acknowledges, for example, that an employee has a right to change careers if he or she so chooses, a right to not be treated in degrading and demeaning ways, and a right not to be discriminated against. Customers have a right not to be purposely deceived about the products they buy. Shareholders have a right to vote in electing members to the board of directors. And so on and so forth. Consequentialist theories, however, are poorly equipped to make sense of such rights claims. Briefly, the problem is that it would appear that the only right a consequentialist theory can coherently acknowledge is the right to be treated in ways that are consistent with bringing about the most overall good. Yet on the face of it, there is little reason to suppose that the overall good is always maximized by respecting the various rights that people in the world of business are commonly said to possess. By their nature, rights are rule oriented and not results oriented in the way consequentialism demands.

A second reason why deontology is of particular relevance to business ethics has to do with the importance of roles and role obligations in business. Deontology seems better able to account for role obligations than consequentialism. The problem for consequentialism, egoistic versions of the view aside, is that it demands that we give impartial consideration to the interests of everyone. But many obligations in the business world seem to depend crucially on specific job responsibilities and particular contractual relationships. A salesperson, for example, is morally obligated to promote the interests of the corporation that employs him or her. While this does not mean that a salesperson should promote the employer's interests at all costs, it does mean that in the ordinary run of things, a salesperson ought not to steer customers toward competitors when the employer offers a product that would adequately meet the customer's needs, even if doing so would somehow increase the overall good. The fact that the salesperson works for *this* business (and not *that* one) is of moral significance in itself. Likewise, a corporation is obligated to return excess profits to *its* shareholders, and not to whomever may be in the greatest need. Management, similarly, has obligations to *its* employees that it has to no others. The list of such role obligations in business could be extended indefinitely. The consequentialist is likely to respond by insisting that fulfilling role obligations does in fact bring about the greatest good. At best, however, this is an empirical generalization that is unlikely to be true in all cases.

—Samuel V. Bruton

See also Absolutism, Ethical; Consequentialist Ethical Systems; Divine Command Theory; Ethics, Theories of; Golden Rule, The; Intuitionism; Kantian Ethics; Natural Law Ethical Theory; Neo-Kantian Ethics; Rights, Theories of; Utilitarianism; Virtue Ethics

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Deregulation

Deregulation is the removal or reduction of the demands of regulation. It often takes the form of eliminating a regulation entirely (e.g., government deregulation of airline routes and fares in 1977) or altering an existing regulation in a way that scales it back (e.g., telecommunications in 1996).

One important issue with regard to deregulation is which level of government (multinational bodies, national, state, local) makes the decision to deregulate in different circumstances. Different countries will resolve this issue differently. In the United States, some deregulatory matters are within the purview of the federal government (generally when there is interstate commerce involved) and other matters will be decided by states and localities. Other countries have a different mix of local- and national-level regulatory decision making, and in still other contexts—such as the European Union—decisions about deregulation will be made by multilateral bodies.

There are a number of sources of deregulation. The most common source comes when a legislative body (with or without the concurrence of the executive branch) passes legislation that has deregulatory effects. Regulatory bodies, including government agencies, are also sources of deregulation—through the deletion or modification of the rules that enact a piece of regulatory legislation, one practical effect may be deregulation. Finally, courts may strike down a regulation as illegal or unconstitutional and such an action would also have a deregulatory effect.

In general, we should expect businesses and industries to support deregulation when a particular regulation is costly and limits their autonomy. (Some regulations are favorable to business and industries, and we should not expect deregulatory pressures in such cases.) Deregulation will almost always be in the interests of individual businesses, industries, and the institution of business. Whether the interests and desires of business will lead to regulation or deregulation depends in large part on the broader social climate and the prevailing political ideologies that have power at any given moment.

Rationales for Regulation

To understand better why deregulation occurs, it is necessary to understand the varying rationales for regulation. Regulation generally occurs for one of the four reasons:

1. The normal functioning of a market yields a result that is perceived to be socially undesirable. Minimum-wage laws, for example, exist when a society believes that a market-clearing wage for some workers is too low.
2. Regulation also occurs when there is a natural monopoly—electricity transmission being one example—that requires intervention to ensure that its monopoly position is not misused in ways that lead to higher prices and poorer service. Due to changes in technology, however, some industries that were thought of as natural monopolies (such as telephone service) no longer are.
3. Externalities—costs of production not paid by the producer—are another rationale for regulation. Pollution regulation exists because pollution harms parties other than the producer (such as surrounding communities) and in the absence of regulation more pollution than ideal would occur.
4. Market imperfections—such as imperfect information—are a final rationale for regulation. Consumers of pharmaceuticals lack enough information to make informed choices about what pharmaceuticals should

> be taken and what side effects and risks exist. Government regulation in this case takes three primary forms—approving a drug as safe and effective, requiring the disclosure of information when a drug is advertised, and requiring that a physician prescribe particular pharmaceuticals.

Rationales for deregulation can, therefore, be understood as the inverse of rationales for regulation.

Why Does Deregulation Occur?

Given the rationales for regulation identified in the previous, three broad reasons for why deregulation may occur can now be identified:

1. The regulation is no longer effective and thus ceases to produce a socially desirable result. When the airline industry was deregulated in 1977, it was largely because the system of price and route regulation in place at the time was perceived by policy makers to be holding back the industry's growth. After deregulation, the number of airlines competing in many markets increased and real prices for air travel fell. However, for many small communities, the federal government had to provide subsidies to ensure continued air service. Furthermore, airline profits have fallen along with consumer prices. Similarly, regulation of natural monopolies, externalities, and market imperfections may be lessened or eliminated when (1) substitutes for regulation are perceived to exist, (2) market changes make the original rationales no longer operative, or (3) the regulation is perceived to be too costly for whatever social benefits it generates.

2. Ideology plays an important role in determining whether deregulation occurs, both for particular industries and for the institution of business generally. The institution of government changes in terms of how dominant political ideologies believe that the institution of business should be regulated. Sometimes political leaders believe that business behavior needs to be reined in, and expansion of regulation is likely to occur. In other cases, political leaders believe that there is too much regulatory control over business, and a pattern of deregulation is likely to occur. Ideological commitments, therefore, shape when political decision makers seek to bring about increased regulation or deregulation.

   It should be generally noted that there are two competing ideologies with regard to regulation. One ideology posits that free markets (along with individual business and industries) relatively unfettered by regulation bring about the best results for society. The second ideology is more skeptical about this claim and tends to promote increased regulation of business. Deregulation is more consistent, of course, with a free-market economic and political orientation.

3. A regulated industry might seek to bring about deregulation through political pressure. Regulation often occurs after a triggering set of events—such as the 1929 stock market crash or the rash of corporate scandals that occurred in the late 1990s. When there is significant and negative public attention directed at an industry or business generally, regulatory pressures increase. But the passage of time may cause such pressures to decrease, providing opportunities for an industry to seek deregulation. In general, businesses and industries prefer less regulation to more regulation, and regulated industries will seek to bring about deregulation through political pressure. Industries have interests and will seek to bring about deregulation when doing so is consistent with those interests.

In short, regulatory decisions—including deregulation—are affected by a variety of contingency factors. The general preference of business is less regulation and more deregulation, and deregulatory pressures should be expected when deregulation is in a business's or an industry's interests. Economic and scientific analysis plays a role (or at least should), but so does political ideology. Policy makers can look at the same evidence and come to radically different conclusions with regard to the attractiveness of regulation or deregulation in a given context.

Problems With Deregulation

As is the case with regulation, deregulation can be fraught with problems. Sometimes deregulation removes a regulation that is costly to business (and by extension, society) and, therefore, leads to a societal benefit. But sometimes deregulation leads to bad outcomes for society.

Some regulatory areas—such as pharmaceutical safety—are probably poor candidates for deregulation. When a particular regulation corrects a market failure or helps consumers make better and more informed choices, deregulation is generally not in order. However, regulatory reform that seeks to better equilibrate costs and benefits may be sensible in such circumstances. Because regulation imposes costs on business and society, it is necessary to ensure that it is effective.

In other cases, deregulation can lead to businesses within an industry seeking to game the system in ways that benefit themselves at the expense of society. Deregulation of electricity markets in the United States is one example. Many states deregulated electricity markets in the 1990s and 2000s, with the general goal of allowing for competition that would supposedly lead to greater efficiency and lower prices for consumers. But because of the way the deregulation was structured in many states and because of the nature of electricity (which cannot be stored), there were strong incentives to behave in socially harmful ways. Some companies—Enron in California is one example—withheld power from the spot market to drive up prices and earn abnormal profits. Some states, because the rules for deregulation were poorly thought through, did not experience the electricity price declines forecast. At present, electricity deregulation has not lived up to what was promised for it.

Getting the rules right for deregulation, therefore, matters. Companies will—as is the case for regulation, of course—seek to find advantages for themselves when deregulation occurs. Hence, it is necessary to structure deregulation in a way that restrains misbehavior by corporations.

Substitutes for Regulation and the Public Control of Business

One of the most important issues with regard to deregulation is whether self-regulation and/or market forces are substitutes for regulation. If so, then deregulation is more likely to be socially beneficial than if not. This is an issue of political ideology at least in part—if one believes that markets are largely self-correcting in nature, businesses and industries are capable of self-regulation, and bad behaviors by businesses are punished accordingly, then deregulation will be attractive. If one believes that business is only prevented from behaving badly by coercive means, then increased regulation rather than deregulation will be attractive.

There is no one answer to the question of whether deregulation will or will not be effective generally. It is necessary to look at the structure of the particular market, the number of companies involved in it, whether self-regulation or markets would be effective substitutes for regulation, and the goals that regulation is trying to accomplish to determine whether deregulation in a given case makes sense. Although political ideology does affect whether the trend is toward regulation or deregulation at any given time, in many cases economic analyses can provide well-informed answers about the suitability of deregulation for a particular industry with regard to a particular kind of behavior.

Conclusion

The regulatory impulse waxes and wanes. Sometimes broad social and political sentiment is in favor of increased business regulation and sometimes in favor of deregulation. When regulation is no longer effective, deregulation will lead to an increase in social welfare. But political ideology also plays a role in determining both regulation and deregulation. Perhaps in an ideal world, economic analysis would determine the direction of regulation and deregulation. But policy makers are driven by ideologies that affect their views on the role of government, and those views in turn largely shape whether deregulation occurs.

—Harry J. Van Buren III

See also Administrative Procedures Act (APA); Airline Deregulation; Antitrust Laws; Cost-Benefit Analysis; Externalities; Market Failure; Public Interest; Sunset Laws

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Descriptive Ethics

Descriptive ethics can broadly be thought of as the study of morality and moral issues from a scientific point of view. It can be thought of as the branch of ethics that attempts to develop conceptual models and test those models empirically in order to enhance our understanding of ethical or moral behavior, moral decision making, and more broadly moral phenomena. This area or branch of ethics might also be referred to as behavioral ethics. Descriptive or behavioral ethics, then, describes and explains moral behavior and phenomena from a social science perspective or framework.

One might distinguish morality from ethics. Morality can be thought of as the set of norms, rules, standards, principles, or values that guide adherents in their behavior as to what is right and wrong, good and bad, or appropriate and inappropriate behavior. In this sense, virtually every human has some morality or moral code. Or morality might be considered the practice of such moral codes among members adopting such standards or codes. To the extent that the practice of business has such a code or set of norms, we might refer to that practice or practices as "business morality." "Ethics" may be thought of, then, as simply the study of morality. Accordingly, ethics is critical reflection or critical analysis of moral issues and moral phenomena. Furthermore, business ethics can then be defined as the study of moral issues in a business context, that is, an applied area of ethics or ethical inquiry. Organizational ethics can be thought of as studying moral issues in a broader organizational context.

To position descriptive ethics, we may distinguish different approaches to studying moral issues and phenomena. One distinction is between normative and descriptive or behavioral ethics. Critical reflection that attempts to answer questions as to what is right or wrong, good or bad, would constitute normative ethics. Such approaches are "normative" or provide guidance and direction in terms of making moral or ethical choices or living in morally acceptable ways. Such approaches tend to be philosophical or religious, providing frameworks and theories that are *prescriptive.* These analyses prescribe general principles or even specific guidance. These *normative or prescriptive* theories include typical philosophical approaches, such as utilitarianism and duty-based approaches such as Kant's. Some have said that there are only two normative ethics questions: (1) What is good? (2) What is right? Aristotle's virtue-based ethics represents a normative theory that answers the first question. Utilitarian and Kantian theories provide competing theories that provide decision rules or answers to the second question. What they all have in common is to approach ethical inquiry from a normative or prescriptive point of view.

Descriptive ethics, on the other hand, approaches the study of morality or moral phenomena by asking different questions. In general, this approach attempts to describe and explain moral action, moral decision making, and moral phenomena. For example, how do individuals process and resolve perceived moral conflicts? What are the most important influences or causes for individuals behaving ethically or unethically? What is the system of beliefs that guides individuals or groups in making the moral choices that are observed? Answers to these kinds of questions are descriptive or explanatory in nature. As such they use social science frameworks that often include theory building and hypothesis testing in terms of discerning answers. Engaging these kinds of questions in a business context, then, can be thought of as *descriptive business ethics*, or the application to the broader organizational context can be referred to as *descriptive organizational ethics*.

Moral Psychology and Social Psychology

One important body of research of descriptive ethics is cognitive moral development theory. This research grew out of the seminal work of Lawrence Kohlberg in the late 1950s in his study of modes of moral thinking and choice among adolescent boys. Kohlberg's theory describes the developmental processes used by individuals as they grow and develop in terms of how they resolve moral issues and make moral choices. It is thus a descriptor of individuals, who vary in terms of their level of cognitive moral development. Kohlberg's theory is the most widely disseminated and tested theory in moral psychology. It has been cross-culturally tested in more than a hundred cultures, and it has been used as an important variable in many descriptive studies of business and organizational ethics. One of the most important implications of cognitive moral development is its relationship to behavior or action. Numerous studies have been conducted, and the general result is a positive but modest relationship to decision making and action. Thus, those individuals having higher levels of moral development are more likely to make ethical choices and behave ethically. Of note in extending Kohlberg's research was James Rest, who developed a more general four-stage model of ethical decision making.

Other social psychology research from the 1960s and 1970s has been used in business ethics to show the influence of factors other than individual, rational processes. Of note here are the Milgram experiments from the early 1960s, in which Stanley Milgram and his colleagues designed experiments that demonstrated how ordinary subjects would comply with authority in carrying out orders that were patently contrary to standards of morality. Here social scientists advanced theories to explain the atrocities of Nazi Germany. Other social psychology experiments followed, including the Zimbardo experiments of the early 1970s, in which normal college students (absent direction from a perceived authority) allowed themselves to engage in abusive behavior in a prison simulation experiment. The Zimbardo experiments were related directly to the kind of behavior exhibited by guards in the Abu Ghraib prison outside Baghdad. These kinds of social psychology experiments and studies have been related to organizational behavior, in particular in business contexts.

Descriptive and Behavioral Business Ethics

Describing and Summarizing Data

One approach to descriptive ethics is just that to describe various aspects of business ethics. This might include surveys of ethical attitudes among employees and managers, for example, whether individuals feel pressure to compromise moral principles to achieve organizational goals. One might describe the kinds of principles that individuals use in making decisions. On the other hand, researchers might turn their focus on the organization itself rather than individuals as the object of study ("unit of analysis" in social science terminology), for example, describing the adoption rates among Fortune 500 firms of codes of ethics, appointment of ethics officers, and other such organizational characteristics. All these questions describe or summarize data about individuals or organizations. Even anthropological studies might be included in this kind of research. One might, for example, engage in a systematic study of the ethical aspects of Japanese business culture.

Theory Building and Hypothesis Testing

However, since the late 1980s and for more than 15 years there has been a growing body of research from which has emerged more complex and complete conceptual models of ethical decision making and ethical behavior. Of particular note is the seminal work of Linda Treviño in 1986. She proposed a person-situation interactionist model to explain ethical decision-making behavior in organizations. Citing the lack of a comprehensive theory to guide empirical research in organizational ethics, Treviño proposed a model that posited cognitive moral development of an individual as the critical variable in explaining ethical/unethical decision-making behavior. However, improving on previous models, Treviño proposed an interactionist model that posited individual variables (e.g., locus of control, ego strength, field dependence) and situational variables (e.g., reinforcement contingencies, organizational culture) as moderating an individual's level of moral development in explaining ethical decision making in organizational contexts. Other conceptual models followed proposing alternative frameworks and variables that describe and explain ethical decision making and behavior in business and organizational contexts.

These conceptual models posit various relationships that can be empirically tested, and this is another critical aspect of this approach, hypothesis testing. Hypotheses are derived propositions that can be tested empirically, and the results of these empirical studies lead to further refinement and modification of the conceptual models. There has been a significant amount of such hypothesis testing in the past 15 years. Such hypothesis testing requires attention to measuring variables, design for testing such relationships, and selection of the appropriate statistical methods for evaluating results. Thus, business ethics has developed as another branch of the social sciences.

To summarize this descriptive body of research would be impossible here. However, we can provide some of the more salient factors that have been studied. For example, it is fair to say, and not surprisingly, that the attitudes and behaviors of employees and managers are strongly influenced by organizational factors and context. Factors studied include the existence of formal ethics policies, the use of ethics training programs, and the commitment of top management in terms of implementing ethics policies and programs. Other organizational factors include the reward structure of the organization and whether and how sanctions are used for ethical/unethical behavior. Beyond such formal features of organizations, attitudes and behaviors are likely to be influenced by the ethical climate as well as the ethical culture of organizations. The behavior of peers and, more generally, the immediate job context in the organization are also likely important, as is the behavior and commitment of leaders in organizations. Included here would be perceived role conflict of one's position, what is rewarded in the unit, the behavior and attitudes of coworkers and management, and job pressure.

Besides organizational factors, individual characteristics are likely to influence decision making, attitudes, and behavior. Following a stage model of decision making, moral awareness or ethical sensitivity would be an important, initial factor. To the extent that individuals vary on such awareness and sensitivity, it is likely to have an impact on decision making. Moral judgment or level of cognitive moral development is perhaps the most widely studied individual characteristic. The ability to follow through on judgments made is also an important factor in the actual decision and behavior, what some refer to as ego integrity. Related to this ability to follow through is the extent to which individuals vary on whether they think they are able to control what happens around them, rather than being passive products of the environment, which social scientists refer to as locus of control. Among other factors thought to influence ethical decision making and behavior are gender, age, and tenure in the organization.

The overall objective of the theory building and hypothesis testing approach is not to just describe but understand and explain complex moral phenomena, and this has been a dominant approach among those social scientists engaged in business ethics in the past 15 years.

Case Development and Storytelling

While from a social science perspective, cases and other forms of descriptive storytelling would not be considered a form of descriptive ethics, a place of descriptive cases in business ethics is acknowledged. Cases and storytelling more generally involve an age-old approach to understanding and knowledge. That is the tale of an effective storyteller. Sometimes the most effective learning is from a good story that is described or told effectively and has important lessons to be drawn from the story. In business schools, the use of case studies is an old and venerable method of teaching and learning. While social science and its techniques have been discovered and developed as tools in business ethics, the description of situations, decisions, and the consequences that follow might also be considered part of the umbrella of descriptive ethics. Such "business case studies" are typically descriptions of situations, people, and decisions, leaving the analysis and lessons learned to emerge from the story itself. Those cases written with a particular ethical dimension might then be properly considered a form of descriptive business ethics. Beyond shorter case studies, any longer accounts (such as books) that describe or relate ethical stories may be considered another aspect of descriptive ethics. In summary, descriptive or behavioral ethics, in its many forms, can be thought of as a branch of ethics that attempts to describe, understand, and explain moral phenomena.

—Dennis P. Wittmer

See also Cognitive Moral Development; Cognitivism and Ethics; Economics, Behavioral; Ethical Culture and Climate; Ethical Decision Making; Hedonism, Psychological; Kohlberg, Lawrence; Normative/Descriptive Distinction

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DESERT

Desert is a three-place property uniting a subject, a thing or treatment, and a fact. When certain facts are true of certain subjects, they have the property of being deserving of certain things. Thus, claims that subjects deserve things (or, desert-claims) have the form, "P has the property of being deserving of (or deserves) T in virtue of F," where P is a subject, T is a thing, and F is a fact about P, also known as a "desert base." It is widely believed that people ought to get what they deserve—at least when other things are equal. There is less agreement about the conditions under which people come to be deserving, and hence about what in particular they deserve. After years of neglect, desert is regaining popularity among political philosophers as a principle of distributive justice. In business ethics, this concept has potentially wide application. It proves especially useful, however, for addressing the justice of personnel (e.g., hires and promotions) and compensation (e.g., salaries and profits) decisions.

The Nature of Desert

To understand what desert is, it is useful to contrast it with the closely related concept of entitlement. Deservers are said to be in a "natural" or "preinstitutional" sense worthy of what they deserve. Desert may incorporate institutional elements, but it is always in some sense independent of them. Entitlement, in contrast, is a wholly "institutional" notion. P becomes entitled to T by satisfying a set of public rules or criteria for the distribution of T. Unlike P's desert of T, P cannot be entitled to T unless there exist rules or criteria for its distribution.

Both desert and entitlement are thought to have normative significance—that is, to provide reasons for treating people in certain ways—but their significance is understood in different ways. According to the standard view, to say that P deserves T is to say that it is "fitting" or good, other things equal, that P has T. Desert is thought not, however, to create rights. If P deserves T, then to fail to give T to P would be bad, other things equal, but it would not violate or override P's rights. Entitlement, in contrast, is standardly understood in terms of rights. If P becomes entitled to T by satisfying the rules for its distribution, then P has a right to T, and to fail to give T to P would be to violate or override P's rights.

These points can be illustrated through an example, borrowed from Joel Feinberg. Suppose there are two candidates for the U.S. presidency, A and B. Candidate A is smart, hardworking, and magnanimous. A wants only what is best for the country and has great ideas about how it should be run. B is dull, lazy, and mean-spirited. B does not want what is best for the country and has terrible ideas about how it should be run. Suppose, moreover, that A works much harder than B to get elected. B, let us suppose, leaves all the work to advisers. Of these candidates, surely A deserves the presidency more than B. But suppose, in the election, B receives more votes than A. As a result, B is entitled to the presidency, and not to give it to B would be to violate B's right to it. Nevertheless, it makes sense to say that, because of A's superior qualities, A deserves the presidency, and because of this, there is some value in A's having it. This is so even though A is not entitled to the presidency. This example highlights desert's role as a critical notion: It can be used to critique the distributions (e.g., of offices) generated by institutions, even ones that are prima facie justified on other grounds.

Desert and Other Values

Desert matters in the sense that it provides a reason to treat people in certain ways, but it is not all that matters, and it may not matter most. Suppose C is a talented employee who deserves a promotion, but suppose the promotion was promised to D. Suppose also that it is more important to keep promises than to requite deserts. It follows that although there is a reason for C to get the promotion, D should have it all things considered. This does not mean that contrary to our original assumption, D actually deserved the promotion. This wrongly equates *desert* with "should have all things considered." C still deserves the promotion, and there remains some reason to give it to C, but for other reasons, D should have it all things considered.

This raises the question of how important desert is compared with other distributive criteria such as need, utility, equality, and entitlement. Few theorists have tried to say how important, in general, desert is compared with these values. But this question is unavoidable in debates about specific issues in business ethics. For example, it has been claimed that the value of equality justifies programs of preferential treatment. An objection to such programs is that, by denying jobs to the most qualified applicants, they conflict with desert. Similarly, it has been claimed that chief executive officers (CEOs) deserve less pay than they now receive. Defenders of the current level of executive compensation claim that, because boards of directors have freely agreed to pay CEOs these sums, CEOs are entitled to them, whether or not they deserve them. Implicit in these debates are disagreements about the relative value of desert—in the first case, compared with equality, and in the second, compared with entitlement.

In fact, more than one disagreement may be implicit in these debates. It can be plausibly denied that the most qualified applicant deserves the job, and that CEOs deserve less pay. On this ground, there is disagreement about the precise conditions for desert. More will be said about the role of desert in debates about specific issues below. First, more must be said about its nature.

The Elements of Desert

All theorists agree that some uses of "desert" are legitimate and some are not, but they disagree about which ones. This is manifest in the debate about the ranges of P, T, and F in desert claims, that is, about what subjects can be deserving, what things or treatments can be deserved, and what facts can serve as desert bases.

Deservers

It is undeniable that persons can be deserving. There is disagreement, however, about whether nonpersons can be deserving. It is natural to ascribe desert to subjects other than persons. We know what is meant by the claim "Everglades National Park deserves to be protected; its beauty is remarkable." But some consider this a misuse of *desert*. According to them, while Everglades should be preserved, it does not, strictly speaking, deserve to be.

It may be wondered where this leaves corporations. A claim such as "Frankfurter Industries deserves an award; it has done so much good in the community," is perfectly intelligible. Whether one thinks of this as a legitimate use of *desert* depends on whether one thinks of corporations as persons, or if one does not, whether one thinks nonpersons can be deserving.

What Is Deserved

Most writers agree that what is deserved must have some sort of value—it must be good or bad, desirable or undesirable. All these examples that we have used so far—promotions, offices, preservation, and awards—satisfy this constraint.

A point of contention concerns whether nondistributable goods can be deserved. We might say of a research chemist, "After all these years, G deserves a breakthrough." Some have claimed that, while it might be good for G to have a breakthrough, because human beings cannot distribute breakthroughs, G cannot, strictly speaking, deserve one. Others think that whether the thing can be distributed is irrelevant from the point of view of desert.

Desert Bases

When there is disagreement about whether P deserves T in virtue of F, it is usually due to disagreement about whether F is a desert base or the appropriate desert base for T. For example, the disagreement about how much pay CEOs deserve is not about whether CEOs can be deserving or whether pay can be deserved but about what the desert bases for pay are. As a result, there has been extensive discussion of the question of what facts can serve as desert bases.

Writers agree that the facts in virtue of which P deserves T must be facts about P. P cannot deserve T in virtue of facts about another person Q. Three further features of desert bases merit attention.

First, it is widely agreed that desert can be based on past actions. For example, H might deserve a high salary in virtue of making a valuable contribution to a firm. Some writers think that, in addition, people's present characteristics can serve as desert bases. They claim, for example, that J can deserve a job in virtue of being the most qualified applicant. Still fewer writers think that future actions also contribute to desert. They claim, for example, that people diagnosed with terminal illnesses deserve pleasant treatment now for the suffering they will later endure.

Second, the majority of writers think that desert is based only on appraisable facts. An appraisable fact is one that is, or should be, the subject of an appraising attitude, such as admiration, gratitude, disgust, or resentment. Suppose K takes a sip of tea. This behavior is not appraisable and, therefore, does not make K deserving of anything. But consider again H, who makes a valuable contribution to a firm. This behavior is admirable, so H can be deserving (e.g., of a high salary) in virtue of it. Note that, if this view is accepted, then people cannot be deserving (e.g., of assistance) in virtue of being in need. Of course, we can imagine exceptional circumstances in which need is appraisable, as when people carelessly squander their resources or when they admirably conserve them. But on this view needs are not normally desert bases, a result that some philosophers are reluctant to accept.

As the example of H suggests, the appraisals that desert involves are not necessarily moral appraisals, that is, appraisals of moral worth. H's making a valuable contribution to a firm makes H deserving and provides a reason to treat H in a certain way, but it does not make H a more morally worthy person. Thus, while all desert is morally (or normatively) significant, not all desert is moral desert.

Third, many writers think that desert is connected to responsibility, such that if P deserves T in virtue of F, then P is responsible for F. Again, the case of H is illustrative. Intuitively, H can be deserving of a high salary in virtue of making a valuable contribution only if H is responsible for that contribution. H must have acted voluntarily and intentionally, so that H can claim credit for what was done. If H's contribution was the result of luck or an accident, or if it was made under the influence of a mental illness or hypnosis, then it does not count toward H's deserts.

This view was the received wisdom until recently. Philosophers who reject it say that while some desert claims, such as H's, require responsibility, others do not. They point in particular to cases in which compensation is deserved. Innocents who are injured in accidents, they say, deserve compensation, even though they are not responsible for being injured. Indeed, they deserve compensation precisely because they are not responsible for being injured. Proponents of the view that all deserts require responsibility have responded by devising more complicated formulations of the connection between responsibility and desert or by arguing that desert of compensation is an illegitimate form of desert.

What Desert Requires in Specific Cases

Desert can conflict with other values, such as equality and entitlement. So it is thought that egalitarians endorse programs of preferential treatment, while desert theorists oppose them. And it is thought that desert theorists criticize the current level of CEO pay, while libertarians do not. We now see that these claims are insensitive to the fact that there are different conceptions of desert theory (as well as of egalitarianism and libertarianism). Some, but not all, desert theorists oppose programs of preferential treatment and object to the current level of CEO compensation.

The claim that the most qualified applicant deserves the job is intuitively plausible. If we think of jobs as prizes, and application processes as competitions, then it seems that, just as the fastest runner in the race deserves the gold medal, the best applicant deserves the job. But some reject this view on the grounds that people's qualifications are not sufficiently under their control. Qualifications consist of, among other things, native talents and acquired skills. It is obvious that people have no control over what native talents they have. Even the skills they have may be the product more of favorable genetic and social circumstances than free choice.

The claim that CEOs deserve less pay than they now receive is likewise controversial. What view one holds in this debate—and the debate about how much pay workers in general deserve—depends on what one thinks the desert bases for pay are. Several have been proposed, including the value of the worker's contribution (perhaps as estimated by the marginal revenue product of labor), how much effort they expend, the hardships they endure, how much responsibility they have (e.g., over other workers), or a combination of these factors. CEOs probably deserve less pay than they now receive if the desert base for pay is effort. Their jobs require about as much effort as the jobs of, say, university presidents, who are paid much less. CEOs might not deserve less pay if the desert base for pay is the value of their contribution. Because they command enormous resources, CEOs can make significant contributions to the organizations for which they work, as well as to the economy as a whole.

How much pay CEOs and other employees deserve has been treated separately from the question of whether entrepreneurs deserve their profits. Here again, there is debate about what the desert bases are. Profits may be deserved as compensation for risk taking, as a reward for the creative deployment of capital, or both. Worries about the role of luck in market outcomes figure centrally in these debates. Some deny that entrepreneurs deserve their profits on the grounds that how much profit they make is affected by factors beyond their control, such as sudden changes in the price of raw materials and the actions of competitors. Others downplay the role of luck, attributing profit instead to entrepreneurs' shrewd choices.

Skepticism About Desert

The difficulty of determining what people deserve has led some theorists to abandon desert as a distributive criterion. This is hasty. If desert is normatively significant, as many believe, then attention must be paid to it.

To assuage these worries, some defenders of desert have emphasized the relevance of comparative as well as noncomparative desert. Consider employee H, who makes a valuable contribution to a firm. It may indeed be impossible to determine how much pay H deserves noncomparatively. That is, it may be impossible to say whether H deserves $50,000 per year, $60,000 per year, or some entirely different sum. But this is compatible with it being possible to determine how much pay H deserves comparatively, that is, compared with other workers. H deserves more than workers who have made less valuable contributions (assuming contribution is the desert base for pay), but less than workers who have made more valuable ones. So if H gets paid $50,000 per year and L gets paid $60,000 per year, and H's contribution is more valuable than L's, then this is unjust from the point of view of comparative desert.

A more important skeptical challenge to desert has its source in John Rawls's work on distributive justice. Rawls and others make much of the fact, mentioned above, that people are not responsible for some of the traits and actions in virtue of which they are said to be deserving. There has been considerable debate about how precisely Rawls himself wanted to develop this insight, but two clear antidesert arguments have been built on this foundation. Some claim that people are not responsible for any of their traits or actions and hence are not deserving of anything. Others concede that people are responsible for some of their traits and actions but claim that we cannot tell which ones. The effects of natural and social endowments are thoroughly mixed together with the effects of free choice, and we cannot pull them apart. Worries about the robustness of human agency may be responsible for desert's relatively small role in recent theories of distributive justice, including Rawls's own. (Curiously, desert has continued to play a major role in recent theories of *retributive* justice.)

Unfortunately for desert theorists, there is no easy solution to this challenge. Some respond by arguing that not all deserts require responsibility. This is unsatisfactory. In the first place, it may not be true. Second, even if it is, it is likely that many kinds of desert—for example, desert of pay for work, desert of a job—do require responsibility. To rebut this challenge, the defender of desert must prove that, at least in some cases, people are responsible for what they do and who they are. This is a tall order. A strategy, which in the short run is effective, is to point out that most moral theorists—including most business ethicists—make this assumption. Desert theorists are no better or worse off in this respect than other theorists.

—Jeffrey Moriarty

See also Affirmative Action; Entitlements; Executive Compensation; Free Will; Justice, Distributive; Justice, Retributive; Meritocracy; Profits; Rawls, John

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Developing Countries, Business Ethics in

Business ethics of developing countries refers to the moral standards governing responsible business practices in countries that are still working toward an acceptable standard of living. Developing countries are generally characterized by lack of industrialization, low per capita income, and widespread poverty. Business ethics in these countries tends to relate to norms that have arisen largely independent of Western expectations and values.

The assumption is often that less industrialization is a sign of weaker moral standards. In fact, this is not necessarily the case—standards in developing countries are often simply "different," and "different" standards do not necessarily translate into "lower" standards. The reality is that societies in developing countries, absent Western influences, have tended to structure themselves according to different values. In

China, for example, there is an emphasis on the collective good, in contrast with the protection of individual rights often prioritized by Western values. It is worth noting that a strong argument can be made that, in some ways, people in developing countries—such as China—adhere to higher moral standards.

In considering business ethics in developing countries, it is important to distinguish between cultural values and moral problems. Business ethics in developing countries is heavily influenced by the particular cultural values (such as emphasis on the common good) that shape those societies, many of which are not prioritized in the same way in the West. It is, nevertheless, possible to identify moral problems that exist in business in developing countries, without challenging the legitimacy of the different underlying value systems. Although the value systems themselves do not necessarily promote corruption, atrocious labor practices, or intellectual property infringement, the operation of those values in the context of poor industrialization leaves those societies vulnerable to behavior generally considered inappropriate.

Corruption

One of the most pervasive themes that extends throughout developing countries is that of corruption. Corruption, in this sense, tends to relate to agents providing special considerations in their official capacity in exchange for financial payments (i.e., bribery, greasing payments) or other personal benefits. In many of these countries, the absence of legitimate political authority and/or proper infrastructure has left institutions and organizations vulnerable to this sort of corruption such that corrupt practices have become the dominant sort of behavior.

This is considered problematic from multiple perspectives. On the one hand, corrupt practices—that is, practices in which official duties or responsibilities are compromised by considerations of personal financial gain—are inherently morally questionable. At the same time, corruption threatens to distort the operation of business by influencing how the market works. The Foreign Corrupt Practices Act prohibits American companies, and their employees and agents, from engaging in bribery anywhere they conduct business. Many people contend that this places American enterprises at a competitive disadvantage. Other people argue that taking a strong position against bribery can be turned into a competitive advantage. Although the data remain inconclusive, a number of other countries have recently followed the lead set by the United States through legislation and other means aimed at deterring corrupt business practices.

While the United States and other Western, developed countries have traditionally condemned corrupt business practices, some view this as hypocritical, given the existence of corruption in the West as well. Others view this as an example of cultural imperialism as Western countries attempt to impose their standards for doing business on developing countries. In fact, the common understanding that this is how the markets operate in many of these countries has led to the development of predictable channels through which these payments are made. Although these countries still only aspire to industrialization and an acceptable standard of living for the majority of their people, to attempt to eliminate corruption categorically denies the reality of the dependence of local communities on the systems on which the bribes and other financial payments are based. For example, government officials in some of these countries receive salaries that are understood to be supplemented by financial payments from business entities seeking special assistance, similar to how waiters and waitresses in many countries, including the United States, receive under-market salaries because customers are expected to contribute tips. In fact, people in the service industry pay taxes according to actual or assumed tips.

Corruption, therefore, remains a complicated issue in the developing world. Viewed from the outside, it is considered problematic, while, from the inside, it is accepted sometimes neutrally as part of doing business. As the momentum builds against these sorts of business practices, it is important to keep in mind the different moral perspectives from which corrupt practices can be evaluated and the consequences of forcing the elimination of this sort of behavior from an economy that assumes the existence of corruption.

Labor Practices

Another key area of concern has to do with labor practices in developing countries, particularly because many of these countries are attractive to multinational enterprises seeking outsourcing opportunities. Working standards become a huge concern in light of the lack of local infrastructure protecting basic human rights. This is particularly true of China, which is becoming an increasingly attractive locus for new business growth, and where there is a long history of flagrant human rights violations. An inherent tension exists between the tradition of long-considered acceptable business practices in China and the Western values of new entrants to the Chinese market.

The trend in many of these developing countries has been toward the acceptance of standards consistent with the recognition of basic human rights. This has manifested itself in the form of concern about sweatshop labor practices. In sweatshops, a range of human rights violations have turned into the modus operandi for these factories, that is, child labor, unreasonably long working hours, failure to implement adequate safety precautions, absence of a living wage, and so on.

The movement toward fair global labor practices is complex. While the goal is the improvement of working standards, it is important to keep in mind the impact of these sorts of changes. For example, in many parts of the world, children are safer in factories than in local schools, which might be no more than a clearing with no protection from the elements. Furthermore, in many instances, families depend on the meager wages brought in by as many family members as possible—the immediate consequence of raising labor standards can ironically end up harming the people whom the change is intended to benefit. This occurs as children are put out of work or hours are reduced for workers whose families rely on the meager wages of all possible wage earners.

The issue of global labor practices thus remains a pivotal area of contention for business ethics in developing countries. Although there are compelling reasons for improving labor practices in these countries, it is essential to recognize the far-reaching consequences of the embeddedness of these practices in local cultures. The improvement of standards needs to be accompanied by measures that compensate for the financial losses the local laborers initially feel and by public or private initiatives that can, over the long term, contribute toward elevating quality of life.

Intellectual Property

Intellectual property is another area where business norms vary, particularly in developing countries as compared with developed, Westernized countries. Although the United States, and many other Western countries, extend significant protection to intellectual property rights (and grant reciprocity to rights guaranteed in other countries), this is not necessarily the case in developing countries. In China, for example, intellectual property violations are rampant. Many of the brand knockoffs (i.e., Rolex watches, Prada purses, etc.) are both manufactured and sold at cheap prices throughout Asia (particularly China and Hong Kong).

This is at least partially the result of the surplus of labor, much of which is already involved in the manufacture of the original merchandise. The absence of moral restraints regarding the valuing of intellectual property leaves the marketplace vulnerable to intellectual property infringement. While considered theft by Western values, local standards do not necessarily view this as harmful in that the perceived loss associated with the unauthorized use of the intellectual property is merely financial. It is possible to argue that there are not even any tangible financial losses: The individual who can afford a Louis Vuitton handbag or a Rolex watch is not going to bother with a fake. The market for knockoffs is a separate market—in general, buyers of knockoffs would not have otherwise purchased originals.

In fact, it can be argued that the harm to the brands extends beyond the loss of potential sales. The proliferation of counterfeit products jeopardizes the reputation and value of the brands. Furthermore, ownership of original products no longer necessarily carries with it the expected prestige. Companies who invest in high-end brands contend that widespread intellectual property infringement threatens future investments.

Conclusion

Globalization has resulted in the clash of cultures and values throughout developing countries as multinational enterprises have expanded operations. This has created tremendous friction. This has resulted in the adoption of cultural relativism by many people—that is, the view, "When in Rome, do as the Romans do." This is in contrast with the imperialistic view, "When in Rome, you should do as you would do." Freeman and Gilbert offer an alternative: "When in Rome, do as you and the Romans agree to do." The middle ground offered by Freeman and Gilbert reflects the notion that there are independent standards by which local practices can be judged inappropriate. Even from within a culture, it is considered possible to recognize the unreasonableness of particular practices.

As developing countries continue to move toward industrialization and to eradicate widespread poverty, business ethics also continues to evolve. Practices considered acceptable in those countries are increasingly challenged as multinational enterprises move in. Business ethics in developing countries, therefore, remains a moving target. It is important to remain cognizant of the potential consequences of change and, particularly for the companies involved in this process, to be prepared to assist in the development of initiatives and creation of infrastructure that becomes part of newly developed countries.

—Tara J. Radin

See also African Business Ethics; Bottom of the Pyramid; Child Labor; Corruption; Cultural Imperialism; Developing World; Fair Labor Association (FLA); Foreign Corrupt Practices Act of 1977 (FCPA); Global Codes of Conduct; International Business Ethics; International Labour Organization (ILO); Living Wage; Maquiladoras; Nike, Inc.; Nongovernmental Organizations (NGOs); Outsourcing; Relativism, Cultural; Sweatshops; United Nations Global Compact; Worker Rights Consortium (WRC); Working Conditions

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Developing World

The term *developing world* refers to countries that are poorer, less industrialized, and less technologically advanced than western Europe and North America. The label "developing" is contested, as are the criteria for its application. Similarly, what counts as poverty, what causes it, and what might lessen it are controversial. What is beyond question is that in much of the world the suffering caused by poverty, disease, and violence is profound.

According to the World Bank, in 2005, 1.1 billion people lived in extreme poverty, defined as less than $1 per day; 2.6 billion were living on less than $2 per day. Approximately 3 million people die each year from AIDS; 60 million people live with HIV infection, and there are 6 million new AIDS orphans each year. Three million die from diarrhea, 2 million from tuberculosis. Each year somewhere between 300 and 500 million people suffer from malaria, and a million die of it. Half a million healthy young women die in childbirth each year. Six to ten percent of all infants die before reaching their first birthday. Childhood malnutrition is rampant: The United Nations reports that 30% of the children in the world have been stunted in their growth, and only about 40% attend secondary school. In many areas, violence is endemic, in the form of civil wars, terrorism, warlordism, and criminality.

From these facts arise a number of ethical issues: about obligations to help, or at least not to exploit or hurt, and—assuming that such obligations exist—whether they apply not only to businesses but also (or instead) to governments, to nongovernmental organizations (NGOs), and to individuals. When such obligations exist, the next ethical question concerns how to compare them with other duties such as those to one's stockholders. For entities other than businesses, the conflicting obligations might be to one's citizens, neighbors, or family members.

The Term and Its Application

Most countries in Africa, Latin America, the Middle East, southern Asia and the Pacific islands count as "developing," with obvious exceptions (Israel, Japan, New Zealand) and borderline cases (South Africa, Turkey). The status of former Soviet countries and satellites is unsettled. Since pockets of poverty and of wealth are found in virtually every country, some would classify inner city regions in the United States (for instance) as "underdeveloped" or developing.

In spite of such disagreements, many find the UN Human Development Index useful for measuring and comparing countries. It too is the product of criticism and controversy over time. For years, the UN Development Program (UNDP) measured development in terms of gross domestic product (GDP), the fraction of GDP produced by manufacturing, and literacy rates. In 1990, a broader definition was adopted, in terms of what kinds of lives people could choose to live. This definition is operationalized in terms of the Human Development Index (HDI), which measures longevity (life expectancy at birth), knowledge (in terms of literacy and school enrollment), and purchasing power (in terms of GDP per capita).

The label "developing world" is controversial also for what it suggests: that industrialization, technology, and increased market activity are inevitable and desireable. "Developing world" may be the latest in a series of terms used for these regions and then rejected. The Cold War, for instance, produced the term *Third World*, originally meaning "nonaligned"—that is, countries allied with neither the Soviet Union nor the West—but quite soon coming to mean areas of deprivation. The phrase was discarded not only because the Cold War ended but also because the adjective *third* seemed to suggest "less important." "Developing world," with its own problematic connotations, may give way to "the Global South," although that term too is inadequate, on geographical grounds.

Causal Explanations

Many different explanations have been given for the enormous variation in standards of living around the world. Sometimes the role of geography is emphasized: Countries in temperate zones with access to the seas, for instance, tend to do better than others. Other physical factors—depleted soil, the presence of malaria-carrying mosquitoes—can also be blamed. Some of the proffered explanations are historical: Most countries with low HDI scores were colonies of European powers until the mid- to late 20th century, and their former colonizers enjoy high HDI scores; exploitative colonialism clearly played a role in shaping present inequities. Other theorists focus on the present: Corruption in government creates and perpetuates poverty. High birthrates put pressure on limited resources. Without democracy and a free press, governments are freer to let their people starve.

A larger frame implicates the present global political and economic system, which (for instance) needs cheap labor or needs to recognize de facto rulers, no matter how corrupt or oppressive, in order for business to continue. The World Bank (WB) and the International Monetary Fund (IMF) are often criticized for the Structural Adjustment Programs (SAP) of the 1980s and 1990s. These programs were imposed on debtor countries, who were not allowed to default on their loans (no international form of bankruptcy was permitted), and whose often overpowering debt resulted from factors in the world economy such as rising interest rates. Allowing the countries to default would have had a destabilizing effect on public and private lenders alike, and so these countries were required instead to deregulate and privatize much of their economy, including education and health. The SAPs also required lowering barriers to international trade. Wealthier countries, not subject to the demands of the WB and IMF, did not always reciprocate, and at times became able to exploit an uneven playing field. (See below for other aspects of the work of the two institutions.)

The adequacy of any single explanation is vigorously contested, but most of the above play some role. Some factors, obviously, are results of or reinforced by others. In the past two decades, HIV/AIDS has devastated much of the developing world, targeting as it does adults in their most productive years. HIV/AIDS is in fact a good illustration of the complexity of causal stories: The disease is caused not simply by the microbe, but also by sexual behavior, governmental inaction, a lack of condoms, the lack of antiretroviral drugs, and the subordination of women, for whom the greatest single risk factor is marriage, because in many cultures in Africa, a married woman has no power to refuse her husband sexually, even if she knows he has or had multiple partners, and even if she knows he is HIV positive. Nor can she insist on the use of condoms. Behind these factors are others; some argue that U.S. endorsement of "abstinence only" programs contributes to the lack of condoms, and it is clear that the World Trade Organization treaty on Trade-Related Intellectual Property Rights has impeded access to cheap antiretroviral drugs (because pharmaceutical companies, backed by their governments, have vigorously protected their patent rights). Activism is forcing some changes in these policies, and so the extent and nature of activism is also a causal factor.

Intervention and Its Goals

Closely related to questions of causality are questions about intervention. Some of these questions are empirical: What, if anything, would improve matters, and do so in the long run? More fundamental questions are conceptual: What should count as improvement? The UN Millennium Development Goals (MDG), like the HDI, reflect a practical consensus on certain goals: better health, longer lives, and more education. These goals were formulated as part of the UN Millennium Declaration, adopted by the General Assembly in September 2000. They are

- Eradicate extreme poverty and hunger
- Achieve universal primary education
- Promote gender equality and empower women
- Reduce child mortality
- Improve maternal health
- Combat HIV/AIDS, malaria, and other diseases
- Ensure environmental sustainability
- Develop a global partnership for development

Both the HDI and the MDG reflect the work of development theorists, prominently including Amartya Sen, a Nobel Prize–winning economist and philosopher. Sen argues that true development should be understood as the expansion of human capabilities, where a capability refers to the ability to exercise central human capacities, like the ability to live a full life in good health, the ability to learn, to marry, to work, to be politically engaged. The approach is Aristotelian; it focuses on what one can do, not on what one possesses. Neither Sen nor anyone working in the field believes a simple list of these capacities is available, although Martha Nussbaum offers a specific (and controversial) list to further the discussion. Importantly, a capability in Sen's sense requires more than the absence of interference. The ability to live a full and healthy life, for instance, does not exist unless enough food, clean water, and health care are available. And on the other hand, a capability can exist even if people choose not to exercise it—for example, those with enough to eat can choose to fast. Assuming a rough agreement on these sorts of goals, the practical question is how to achieve them.

Efforts to Help

Whatever objections can be raised against market activity as a criterion of development, markets can be instrumentally invaluable. They can provide meaningful work, increased income, and abundant affordable products, all of which play important roles in the development of human capabilities; markets also increase freedom in the sense of expanded, often greatly expanded, choice about what to buy and what work to pursue.

Because market activity can provide significant relief to the poor, the expansion of businesses into the developing world can sometimes be described as an effort to help. Some would argue that businesses—which is to say, profit-making organizations—cannot enter the developing world primarily to help. Their aim must be to make a profit. Yet this defining aim, at least in privately held companies, can be a side constraint rather than the single final purpose of all decisions. Publicly held companies, too, can take broad views of what is in the financial interest of their stockholders and can decide that assisting those in a poorer country is likely to improve the company's profit margin in the long run or in various indirect ways (such as contributing to a better public image or fending off misguided regulation). Finally, some have argued that direct humanitarian aid from businesses, using their special skills and strengths, is also justified, given an underlying social contract between business and society. Well-known examples of corporations that have, directly or indirectly, set out to help include Merck's development of a medication for river blindness, Citicorp's funding of microcredit projects, and Intel's support of scientific and mathematical education.

Both the WB and the IMF try to lessen world poverty, the IMF through efforts to increase market activity but also to make it more efficient and more stable. The WB's official motto is "Working for a world free of poverty," a goal it promotes through low-interest loans and grants to poorer nations for projects about health, education, infrastructure, communication, and similar work. The grants and loans are often conditional, requiring that the recipient country change its structures and policies in complementary ways. A loan for an environmental project, for instance, might require that the country pass stricter pollution regulations. When what the WB requires is fiscal restructuring along what are called neoliberal lines, criticism can be intense. In the face of such criticism, and of internal self-assessment, the WB's official strategies now specify that projects should be "owned" by the recipient country and by local stakeholders, and be led by the recipient countries themselves.

A vast number of NGOs, national and international, domestic and foreign, work in the developing world. Many began as relief organizations and later turned to "development" projects—for instance, an NGO might have first provided food aid, then tried to develop local agriculture. The line between relief and development is in fact hard to define. Some NGOs conduct their own projects (e.g., digging wells, building schools, providing micro loans) while others (particularly those from outside a country's borders) support such local projects with money, labor, or expertise. Some NGOs are primarily lobbying groups, pressuring governments to respect human rights or improve the conditions of the poor. There is by now a substantial body of literature questioning and criticizing NGOs: The initial impulse to help can be thwarted or deformed in a wide variety of ways, including the need to attract donors and the need to be accepted by powerful bodies in the host country (e.g., the military, the government, warlords, village elders).

The largest philanthropic organization in the world is the Bill and Melinda Gates Foundation, which spends hundreds of millions of dollars each year to improve public health around the world. Its efforts include funding of vaccine research, efforts to eradicate polio, and projects to help children with HIV/AIDS. Other significant organizations have different foci. The Open Society Institute (part of the Soros Foundations Network) promotes democracy and human rights. Oxfam works to eradicate poverty. The Aga Khan Development Network supports health, education, and cultural preservation within the Muslim world.

Ethical Issues

The developing world poses ethical questions for businesses, for governments, for NGOs, and for individuals. For businesses, ethical questions arise whenever maximizing value for stockholders conflicts with other ethical principles. Foreign workers, for example, can often be paid less than Americans and required to work longer hours and in less safe conditions. In some circumstances, this amounts to exploitation, but the issue is complex, since, for instance, local standards of living are probably also lower. But the claim that any job freely accepted must make the workers better off, and therefore cannot be exploitative, is also too simple. For one thing the improvement may be temporary; as businesses move from one country to another, the lives to which workers return may be worse than those which they left. For another, the term *freely chosen* needs interpretation. Legal and physical coercion clearly interfere with freedom; do hunger and poverty? The baseline against which to measure exploitation has been the subject of extensive philosophical analysis, as has the nature of coercion.

Hiring workers abroad is ordinarily accompanied by a loss of domestic jobs, at least in the short run. Economic theory predicts that in the long run the average amount of utility will increase, at least if something close to perfect markets exists. But it does not predict that the utility will be evenly distributed, and it has nothing to say about justice; questions of obligations to workers "at home" and to the communities in which one does business thus arise.

Furthermore, many developing countries have few or no environmental protections in place. As a result, products can be produced more cheaply but at the cost of environmental damage. Businesses must choose which value to honor.

Businesses must also choose how to lobby governments, since they can have significant impact on national policy. Should the lobbying be only in the corporation's self-interest? (There is also an interesting moral question of self-deception here, since it is natural to believe that one's own work contributes significantly to the general welfare. Combined with a simplified economic view, slogans such as "What's good for General Motors is good for the country" often result. Such slogans usually have at least a germ of truth, sometimes considerably more, and can make it difficult to recognize the situations in which what is good for a particular industry creates harm and injustice elsewhere.) In fact, since businesses could not exist outside legal and social frameworks, most of the ethical issues faced by business are intertwined with those facing governments, NGOs, and individuals.

Governments of developed nations have obligations to their own people. Should the welfare of those people be promoted at the expense of other, less powerful, countries? The issue is sometimes this blunt, but can be more complex. U.S. law, for instance, at the beginning of the 21st century required that food aid to starving nations be provided only with food (not money), purchased in the United States, and transported on American vessels. This requirement ensured that aid to other countries benefited American farmers and shippers. It also solidified political support for donations. But the arrangement was inefficient: Financial contributions would have entailed fewer transaction costs and would reach the needy sooner.

Governments themselves are not monolithic, and so general questions about their obligations usually entail further, more finely grained, questions. To use the example of the United States, decisions about treaties, trade arrangements, and so forth, are the result not only of the interplay between legislative, executive, and judicial branches but also of the nature of campaign financing, lobbying, and special interest groups. If one concludes, for instance, that food aid should be supplied through money rather than shipments of grain, the next question would be which of the various players affecting national policy bear responsibility for changing it. Should farmers and shippers lobby differently? Should the legislature filter and resist more courageously? Should campaign finance laws be changed so that legislators are more independent?

NGOs face any number of ethical questions. The most fundamental question was mentioned earlier: What should be their goals, specifically and generally? But even with something like a consensus on that question, many other vexing issues about means to the ends would remain. Some examples: Should one exaggerate the extent of threatened famine, since only that kind of media coverage brings enough donations? Should one deliberately allot some aid to local belligerents, knowing that in any case some of the aid will be diverted to them, and open books are better than covert ones? What counts as a bribe, and should one be paid if that is the only way to get help to those who need it?

Finally, for individuals the question is ultimately how much, and in what way, to try to help, where help can mean giving money, time, or effort, and where effort can mean anything from volunteering one's medical skills to organizing activist protests. The most well-known utilitarian answers to the question of how much one must help come from Peter Singer, who answers simply: as much as one can. Strictly speaking, utilitarianism requires that we give (money, time, or effort) until doing so causes more pain than it eliminates. For most people that bar is set too high, and so Singer simply urges giving as substantially as one can manage. Nonutilitarians such as Bernard Williams reject this way of approaching the issue, arguing, for instance, that obligations to those in one's family and community outweigh those to distant strangers; or that the kind of projects that gives one's life meaning cannot be simply measured against the happiness that one might instead produce for others.

The question of what and how to give, however, admits of no simple answers even for utilitarians, because making a difference might require pressuring one's government (an expenditure of time and energy), ethical shopping (requiring research, which also costs time and energy), or other sorts of commitments. Even simply giving money requires serious thought about where to donate.

Conclusion

The suffering in most of the world is so great that it requires an ethical response. But finding the proper response is complicated. Decisions about what to do rest on what one should be seeking, what sorts of tools are most likely to be successful, the relative moral weight of obligations within and beyond one's own community, and the morality of possible strategies for improving matters. These questions confront businesses, governments, and private organizations, as well as individuals in both their private lives and their lives as citizens.

—Judith Andre

See also AIDS, Social and Ethical Implications for Business; Aristotle; Business, Purpose of; Business Ethics; Capabilities Approach to Distributive Justice; Coercion; Developing Countries, Business Ethics in; Development Economics; Exploitation; Globalization; Gross Domestic Product (GDP); International Business Ethics; International Monetary Fund (IMF); International Trade; Newly Industrialized Countries (NICs); Nongovernmental Organizations (NGOs); Outsourcing; United Nations; World Bank

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Development Economics

Development economics is the application of economics to the study of low and middle countries that are typically characterized by more agricultural and less industrial economies and account for five sixths of the world's population. This broad definition of development economics encompasses a wide variety of topics and approaches. Most applied economics topics (and some theoretical ones) are relevant in the study of developing countries so that development economics overlaps with labor economics, industrial organization, monetary policy, public economics, environmental economics, and so on. Work in growth theory and information economics is also essential for the study of development. Some topics such as structural transformation and informal markets are relatively unique to the study of development, while others such as household models and the diffusion of technology originated elsewhere but have been greatly refined by development economists. There are a number of different analytical approaches, including neoclassical, structuralist, dependency/Marxist, and world systems. The first approach is more prevalent among economists, the latter three being more evident in the work of scholars in development sociology and other disciplines. With advances in the availability of data on developing countries and widespread interest in institutional and information economics, the lines between development and other branches of economics have become increasingly blurred.

The roots of the neoclassical approach to development can be seen in the origins of economics. Many introductory courses in economics start with Adam Smith's pin factory discussion in which Smith describes the productivity gains from specialization. David Ricardo's analysis of international trade identifies comparative advantage as the source of the gains from trade. We can apply these ideas to economic development starting from a subsistence economy. Such an economy is limited in its ability to develop because each family must perform a wide variety of tasks (grow staple crops, process them into food and clothing, gather water and fuel, educate children, care for the sick, etc.). The main potential for a higher standard of living is through specialization. Some farmers may specialize in food crops well-suited to their geographic and labor resources. Different ecological zones would specialize in different crops, perhaps including inputs for clothing, medicine, and shelter. If each specializes in the crop in which they possess a comparative advantage, the total amount grown would be greater. The various farmers could trade so that all had more than under subsistence. Likewise, villages might form with individuals to specialize in tasks previously performed by each household: processing crops into food and clothing, providing potable water, gathering and selling fuel, educating children in schools. The development of the economy continues through more specialization, including professions that provide the institutions necessary to facilitate specialization and trade. A natural extension of this is to the international arena where international trade allows a country to capture even more benefits through greater specialization.

Taking this perspective of development driven by specialization and facilitated by markets, development economics then focuses on ways in which markets or governments fail and how best to address these failures. The early approach, dominating policy in the 1950s and 1960s, focused on market failure. Adopting the attitude of colonial administrations, many development economists saw market failure as widespread and largely uncorrectable. Small-scale agriculturalists were bound by custom and tradition; private agents were deficient in entrepreneurship; missing capital and risk markets meant that private companies would not undertake large investments even when immensely profitable. Thus, government was seen as the prime mover, often using compulsion rather than market forces. This attitude also reflected the apparent lesson of the Soviet Union at the time, namely, that government planning could more rapidly propel a country from a simple agrarian system to an advance industrial power. This view was reflected in W. W. Rostow's "Stages of Growth" and Nurkse and Rosenstein-Rodan's "Big Push" where there was a critical level an economy must reach before achieving sustained, modern growth. Work in this area of "development planning" shifted its focus to include distributional issues as evidence accumulated in the 1960s that growth could have high social and environmental costs.

A competing perspective that focused more on markets developed alongside the planning apparatus, gaining more support through the 1970s. While Nurske and Rosenstein-Rodan envisioned market disequilibrium leading to paralysis (e.g., a shoe factory with no one to buy the shoes), Albert Hirschman saw disequilibria as the very source of growth. Backward and forward linkages would spread growth from one sector of the economy to another.

In the 1960s, T. W. Shultz emerged as an ardent critic of the view that small-scale agriculturalists were unresponsive to economic incentives. The traditional view implied that market-based policies to increase production of crops for sale to urban areas or for export would not succeed and that poverty in rural areas was thus largely self-inflicted. Shultz argued that outside observers had mistaken rational responses to extreme scarcity for economically irrational adherence to traditional customs. Shultz offered his "efficient but poor" hypothesis as an alternative, arguing that detailed analysis of the constraints facing small-scale agriculturalists would reveal decisions consistent with economic rationality once people had had sufficient time to adjust to changes in prices and other factors. Over time, the efficient but poor hypothesis has come to dominate the field of development economics, giving rise to increasingly sophisticated models of household decision making and providing a basis for governments to anticipate the likely response to different agricultural policies, including market-based policies that rely on a rational (i.e., self-interested) response to changes in prices.

One important application of the efficient but poor hypothesis is to explain the relatively slow and selective spread of the so-called Green Revolution, high-yielding hybrid crops and complementary fertilizers, herbicides, and pesticides engineered specifically for developing country conditions. With funding from the Ford and Rockefeller foundations, these varieties of rice, wheat, and other staple food crops were designed to dramatically increase yields regardless of farm size so as to assist small-scale agriculturalists. In time, the Green Revolution was successful in increasing yields and helping many less-developed countries to achieve food self-sufficiency. However, adoption was much slower than anticipated with wealthy farmers adopting quickly and, thus, receiving a large share of the benefits. Such behavior might be the result of tradition-bound peasants, but the evidence suggests that increased risk, credit constraints, access to irrigation, and limited information explain the slow and differential adoption. Lessons learned continue to inform agricultural policy and the design of agricultural extension programs.

The notion of efficient, albeit constrained, behavior on the part of poor rural agriculturalists is also reflected in the reconsideration of apparently inefficient institutions. Sharecropping, widely practiced in poor communities in South Asia and elsewhere, provides a good example. Sharecropping is a form of land tenure where the "rent" the tenant pays to the landlord is a fraction of the harvest, frequently one half. Sharecropping is an economically inefficient institution because it reduces the incentives for the tenant to produce. In a standard rental contract, the tenant pays a fixed rent but then keeps all the remaining harvest. If additional inputs will increase the harvest enough to justify their cost, the tenant will choose to use them since the full benefit accrues to the tenant. Likewise, if the landlord uses a fixed wage contract rather than a share contract, the landlord pays the fixed wage but then keeps all the remaining harvest. Again, if additional inputs will increase the harvest enough to justify their cost, the landlord will choose to use them since the full benefit accrues to the landlord. However, with a sharecropping system, the sharecropper bears the full cost of at least some inputs (e.g., labor) while only receiving a fraction of any increase in the harvest. The result is that the sharecropper will use fewer inputs and produce less output. Thus, sharecropping has historically been considered a "backward," inefficient institution. However, research in information economics has demonstrated that it may be a rational response to information asymmetry and risk aversion. The structure of agriculture is such that landlords cannot monitor workers well so that a fixed wage contract may result in very low labor productivity. The solution is a rental contract that motivates the laborer to improve productivity since all the gains of high productivity accrue to the laborer. However, the variability of weather and market prices introduces considerable risk, which a poor laborer is ill-equipped to bear. In contrast, the richer and more diversified landlord is much better suited to bear risk, an argument in favor of the fixed wage contract. Thus, sharecropping can be seen as a compromise between a fixed wage contract and a rental contract. It provides some of the "risk insurance" of the former and some of the incentives to improve productivity of the latter. This is but one example of institutions that can be interpreted as responses to failures in credit and risk markets due to incomplete or asymmetric information rather than being interpreted as "backward," that is, economically irrational.

The growing belief by the 1970s in the rationality of economic agents in developing countries helped fuel a broader debate over the appropriate role of government in promoting development. The early view of market failure being the central obstacle to development led directly to development planning and considerable government involvement in the economy. As an approach to industrialization, this was widely applied in import substitution strategies where the growth of selected domestic industries (infant industries) was fostered via tariff and quota protection from imports. The economic justification rested on arguments of capital market failures and positive externalities. If the cost of production falls with size (increasing returns to scale) or experience (a learning curve), small and inexperienced domestic firms may be unable to compete with cheap imports from larger, established foreign firms. If these domestic firms lack access to capital markets, they cannot survive an initial period of losses while they grow and gain experience to achieve lower costs. Furthermore, if experience is embodied in skills gained by workers, the investment a firm makes may be lost when the worker switches to a competitor. While such an investment is socially beneficial (since the competitor gains from the initial firm's investment—a positive externality), it would not be beneficial for the initial firm. Such problems can prevent the development of the industry despite the country's latent or dynamic comparative advantage in the industry. One solution to these problems is to fix these market imperfections; an alternative (seen as more feasible) is to provide some kind of support to infant industries as they grow and gain experience to become competitive. Import taxes (tariffs) and restrictions (quotas) achieve this by increasing the price of imported goods. Similar arguments can be applied to starting export industries though support usually took other forms such as cheap credit or direct subsidies. Overall, the activist state approach led to substantial government involvement across the economy in many countries.

Following initial impressive results in the 1950s and 1960s, the import substitution model appeared to falter in the 1970s and 1980s. The logic of import substitution had led to greater and greater government involvement in the economy as interventions caused price distortions (and consequently resource allocation distortions) that required additional interventions. Furthermore, the theory of infant industry protection—selective and temporary—rarely matched reality where political influence usually determined the selection of industries and guaranteed long-term rather than temporary protection. The oil shocks of the 1970s and ensuing 1980s debt crisis exposed the inefficiency of these regimes and often forced substantial change in the form of structural adjustment. The confluence of these events eroded support for the practice of import substitution among development economists.

Industrial policy in the form of export promotion has shown considerably better success but has sparked heated debates between development economists, particularly during the 1980s and 1990s. With attention focusing primarily on South Korea and Taiwan, some development specialists have argued that competent governments can accelerate development by selectively promoting certain industries over others. Others point to the same experience as support for a laissez-faire approach with limited government involvement in the economy. The first group highlights intense but narrowly focused interventions (via state control over bank credit and other means) as the source of rapid industrialization, exploding export growth and soaring income. The second group instead attributes success to relatively low average levels of government involvement across these economies. Even if the weight of the evidence supports the pro-industrial policy position in the cases of Korea and Taiwan, the question of government competence remains critical, and we return to the central question of whether market failure or government failure is the more important obstacle to development.

Recent research on barriers to development has focused on the quality of institutions, mostly linked to basic government functions. These include the security of personal and property rights, political institutions for policy formation and decision making, and basic market-facilitating institutions. This can be seen as something of a middle ground where the role of the government is emphasized but primarily in its capacity to provide the basic institutions of a market economy. Nonetheless, the "states versus markets" controversy is likely to continue to be an important subtext of debates in development economics.

Debates over globalization are closely linked to the choice of development strategy. From the perspective of neoclassical economics, where the cornerstone of development is specialization and trade, arguments against open markets are limited and typically temporary. Trade restrictions temporarily may act as bargaining chips to pressure other countries to free their markets. For a country large enough to influence world prices, the optimal tariff is greater than zero but typically still low. If consumption of foreign products has negative externalities (e.g., Western movies undermining traditional culture), some level of taxation to impose this cost directly on consumers (internalizing the externality) is appropriate, but this would typically stop short of a complete ban. While trade restrictions may address some market failures (e.g., the infant industry argument above), free trade solves others (e.g., local monopolies) and may function as a source for new technology and information. Many economists are more guarded about suddenly opening markets in cases where basic institutions such as secure property rights are weak, although the long-run prescription is to open markets after strengthening these institutions. Overall, neoclassical economists do not see most trade restrictions as supported by legitimate economic analysis but rather as driven by domestic distributive politics where narrow interest groups are able to impose restrictions in spite of the net loss to the country. In contrast, an antiglobalization argument advocating long-term restrictions on trade could be based on structural, dependency/Marxist, or world systems theories.

—Christopher Kilby

See also Asymmetric Information; Comparative Advantage; Developing World; Economic Efficiency; Economic Growth; Economic Incentives; Economic Rationality; Economies of Scale; Efficient Markets, Theory of; Externalities; Free Market; Globalization; Green Revolution; Incentive Compatibility; Industrial Policy; Interest Groups; International Trade; Invisible Hand; Laissez-Faire; Market Failure; Marxism; Monopolies, Duopolies, and Oligopolies; Newly Industrialized Countries (NICs); Perfect Markets and Market Imperfections; Privatization; Rational Choice Theory; Restraint of Trade; Smith, Adam; Tariffs and Quotas

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Digital Divide

The digital divide is the gap between those who have regular, easy access to digital technology and those who do not. U.S. Assistant Secretary of Commerce for Communications and Information Larry Irving popularized the term *digital divide* in a series of technology reports in the 1990s. The term is primarily used to refer to the uneven distribution of Internet access, although other information technologies are sometimes included. The digital divide cuts across nations and across demographic groups within nations.

The digital divide generates great concern among governments, nongovernment agencies, and the private sector. In 2006, a Google search on "digital divide" turned up about 27 million entries. From an ethical perspective, the digital divide raises questions of distributive justice—the fair distribution of goods relative to demand. Many believe that the digital divide both represents and reinforces socioeconomic inequalities. Inadequate access to the Internet diminishes opportunities to conduct business, communicate, find employment, interact with government agencies, research health issues, join groups, engage in distance learning, and participate in political processes. For the world's rural poor, the lack of Internet access forms a barrier to vital information about agriculture, fisheries, forestry, health, nutrition, and other keys to rural development. Such structural links between digital access and socioeconomic inclusion mean that the digital divide feeds the disparities that created it. Consequently, many observers have voiced fears that the growth of digital technology will further marginalize the information have-nots.

While the starkest gap appears between those who have at least some Internet access and those who completely lack it, significant differences also exist among those who go online. For example, one study found that having a broadband (high-speed) connection more strongly predicted users' range of Internet activity than did their number of years of experience in using the Internet. Differences in usage patterns also appear between those who must visit a school, library, or community center to go online and those who have home computers plus smaller devices that permit Internet access nearly anywhere, anytime. Much attention has been paid to the "democratic divide" between those who use digital technology to participate in political life and those who do not.

Closing the digital divide would help realize the unique potential of digital technology, some observers say. Older technologies, such as print and television, traditionally allowed users to receive content produced somewhere else by someone else. Digital technology can enable users to produce their own content and deliver it locally or globally.

Critics question the terms in which discussions about the digital divide are typically framed. For example, some argue that the divide will go away on its own as wireless technologies become cheaper. Others see the concept of a digital divide as "welfarist" or mainly as marketing for Internet service providers and e-commerce retailers. Still another viewpoint stresses effective Internet use rather than mere access. From this perspective, ignoring such questions as "access to what" and "access for what" will lead to an elite group of producers using the Internet to deliver content to an expanding group of passive consumers. Effective Internet use would mean ensuring "e-readiness"—the knowledge, skills, and financial, legal, and other necessary supports so that individuals and communities can both consume and produce content to achieve their objectives.

Global Digital Divide

Access to digital technology is expanding. Estimates indicate that global Internet usage quadrupled between 2000 and 2005 to more than 1 billion. Much of this growth has come from such populous nations as China, India, and Brazil. A significant portion of the growth can be traced to new wireless technology. Other factors include the development of smaller, more affordable digital devices and increased broadband capacity. Cell phone and Smartphone access to the Internet is expected to increase Internet usage in developing nations during the next decade.

At the same time, stark inequalities remain. A 2001 UN Development Programme report noted that all the bandwidth in Africa totaled the same as the bandwidth of São Paulo, Brazil, and the bandwidth available in Seoul, South Korea, equaled that available in all of Latin America. According to a 2006 report by the United Nations Conference on Trade and Development, people in low-income countries, which had 37% of the world's population, were 22 times less likely to use the Internet than were people in high-income countries. Internet access in high-income countries was not only faster and more stable but also more than 150 times more affordable than in low-income countries. Moreover, the slow, unreliable dial-up connections typically found in low-income countries often prevented Web browsing and limited users to character-oriented applications.

National levels of access to the Internet tend to correlate with levels of economic development, education, democratization, and investment in science and technology. Factors such as urbanization, foreign investment, and the presence of nongovernmental organizations also correlate with Internet access.

Culture can be an additional factor in Internet usage. In Japan, for example, unfamiliarity with English and with alphabetic typing has led many to avoid computers and the Internet.

Social Digital Divide

The digital divide within nations appears along lines of income, education, race, age, immigration status, urban versus rural location, disability, and gender. As overall Internet access expands, it penetrates different demographic groups at different rates. This pattern resembles the diffusion of older technologies, such as the telephone, radio, cable television, mobile phones, and fax machines.

Socioeconomic Factors

Income and education strongly influence Internet digital diffusion in the United States, where 68% of adults had access in 2005. In a 2006 Pew survey, 91% of those with annual incomes over $75,000 used the Internet, compared with 53% of those earning less than $30,000. Research from the 2005 Pew Internet and American Life Project found that 89% of college graduates had Internet access, compared with 29% of those who had not graduated from high school. African Americans and those aged 65 or older also had lower rates of Internet access. A steep drop-off occurred after the age of 70, and older women were far less likely to use the Internet than were older men.

Rural Internet penetration in the United States lagged about 10% behind the national average from 2000 to 2003. Some of the difference may have stemmed from lower incomes and higher percentages of older Americans in rural areas. Residents of rural areas report less access to broadband Internet connections, which are needed to receive quality audio and visual information. High costs and low returns create disincentives to bringing broadband to rural areas. China has a much larger rural versus urban penetration gap. Rural areas, home to more than 60% of the Chinese population, have less than 1% of the country's Internet connections.

An Internet access pattern similar to that in the United States appears in 15 European Union countries (EU-15), where 43.5% of the population had access in 2003. Despite growth in overall access, a 2005 report from the Commission of the European Community found a strong, persistent connection between higher Internet use and higher income and educational status. Gender, age, and whether one lived in a rural or urban area also affected Internet access. Digital divides related to income and geographical were wider in the New Member States and the Candidate Countries (Romania, Bulgaria, and Turkey) than in the EU-15.

Immigration status has recently gained attention as an influence on Internet access. In the United States, data from the 1997–2003 Current Population Survey (CPS) Computer and Internet Supplements showed a widening native-immigrant gap in home computers and Internet access. In 2003, more than 60% of native-born Americans could access the Internet from home, as compared with 48% of immigrants. The immigrant–native gap appears even within ethnic groups. For example, the home Internet access rate for immigrant Latinos was 15 percentage points lower than for U.S.-born Latinos, with the lowest access rates among Latino immigrant households where adults spoke only Spanish. Data on other language groups were not included in the CPS survey. Asian-born youths had slightly greater access to home computers and Internet than did U.S.-born Asian youth.

Disability

Inaccessible Web design has created a barrier excluding many people with disabilities. For example, the text in graphical Web pages typically cannot be read by audible screen readers used by people with visual or cognitive disabilities. Online forms designed to prevent keyboard navigation and input form a barrier for people with visual or mobility disabilities. A lack of captioning prevents people with hearing disabilities from accessing streaming audio and video clips. Such barriers hinder access to distance learning, governmental and business transactions, online textbooks, and work involving the Web-based environment.

Democratic Digital Divide

Theorists disagree about the impact of digital technology on civic life. Optimists say the Internet will enhance democracy by providing smaller, less powerful groups with lower cost and more effective ways to communicate, organize, and mobilize. Transnational advocacy networks and alternative social movements demonstrate the Internet's potential to gather people around issues of concern. Pessimists say the same people who already dominate political life will use digital technology to reinforce their dominance, while the politically apathetic remain so.

Solutions

Governments, intergovernmental organizations, nonprofits, and the private sector are working to close the digital divide. For example, the Federal Communications began an "E-Rate" program that offers discounts on telephone service and Internet access to U.S. schools and libraries. The discounts vary according to local incomes and rural or urban location. When the program began in 1996, 65% of U.S. schools had Internet access. By the end of 2002, the rate had increased to 99%. In 2003, Samsung launched its "DigitAll Hope" program to award grants to youth development programs using digital technology in eight Asian countries and Australia.

Other efforts focus on giving inexpensive laptop computers to economically disadvantaged groups or providing personal computers to schools, libraries, or community technology centers in areas with low access rates. Some groups seek to harness solar power to run digital devices in developing countries or to expand the availability of broadband connectivity in rural areas.

Many organizations give attention to factors beyond mere physical access that affect the Internet's effective use. For example, these organizations help underserved populations to understand how the Internet can help them achieve their goals. Advocates of greater Internet access also engage in planning to ensure a hospitable legal and business environment as well as locally relevant Internet content.

Meanwhile, researchers are assessing the effectiveness of the various efforts to close the digital divide. There will be an ongoing need for such research as digital technologies and plans for sharing them move forward.

—David P. Schmidt

See also Computing, Ethical Issues in; Developing Countries, Business Ethics in; Developing World; Globalization; International Business Ethics; Internet and Computing Legislation

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Dignity

To possess dignity is to be worthy of respect, and the concept of dignity is closely allied to ideas of self-worth and self-esteem. Because possessing dignity means that one has a claim to be treated with respect, the possession of dignity by a person implies a moral obligation of others to behave with respect toward that person. Not all forms of respect are a tribute to dignity, however. A race horse may be respected and appreciated for its speed and grace, but it does not, therefore, possess dignity. Similarly, one may well treat rattlesnakes with respect, but that does not imply that rattlesnakes have dignity.

Instead of being associated with general respect, in its core usage, dignity applies only to human persons, in virtue of their specifically human qualities. The possession of dignity seems to require a reflective consciousness that is not possessed by simple life forms or inanimate objects. In some sense, the possession of dignity requires the capacity to be indignant, that is, to feel offended by being treated with less respect than that to which one is entitled. Nonetheless, the concept is sometimes extended beyond the human realm to include other animals. Today many think that we owe a moral respect to nonhuman beings and even to the natural environment.

Dignity is often thought to attach to humans simply as a result of their being persons, the idea being that every person, just in virtue of being a person, possesses dignity or (equivalently) is worthy of that certain kind of respect demanded by a person's dignity. Beyond the dignity that belongs to each person simply in virtue of being a person, some persons may possess a special dignity. This incremental dignity can be associated with age, status, achievement, or the office that a person holds. Almost all societies regard elders as having greater dignity than the young. Similarly, persons of great achievement are often thought to possess greater dignity and to be worthy of additional respect. For example, great scientists, artists, and business leaders generally receive greater respect and possess greater dignity than the common person. In addition, greater dignity often attaches to those who hold special office or roles. Thus, a president or prime minister generally receives a treatment that is commensurate with their greater dignity.

Dignity plays a role of great importance in business. Different stakeholders who interact with the firm all possess the common dignity that attaches to all persons, but various stakeholders can also possess a differential dignity due to the role that they play with respect to the firm. For example, potential customers are typically treated with greater dignity than a vendor to the firm.

Philosophical Foundations of Dignity

Immanuel Kant is the great philosopher of human dignity, as he made the concept of human dignity and worth the basis for his entire moral philosophy. Kant gives several formulations of a principle that he regarded as a categorical imperative, that is, as a moral law that must never be disobeyed no matter what the consequences might be or other considerations might suggest. While Kant regarded the various formulations of his categorical imperative as equivalent, his second formulation bears the clearest relationship to the concept of dignity. The categorical imperative demands that we at all times treat humanity, whether in ourselves or others, as an end in itself, and never merely as a means. For Kant, this moral law imposes a perfect duty, one that can never be evaded or ignored. Thus, it can never be permissible to treat another human being as a mere means to some other end, but we must treat other humans with respect. To regard a person as an end in itself is to acknowledge that a person has his or her own interests and life plan and that it would be wrong to ignore that dimension of a person.

Kant does not prohibit treating others as an end to some other objective, but he does prohibit treating them merely as a means to an end. For example, when one gets a haircut one employs a barber as a means to an end. However, if we treat the barber merely as a means to getting a haircut, we fail to respect their humanity and fail to regard them as a being with their own interests. Probably, we have all seen situations in which a person treats an employee or social inferior with a great rudeness that ignores a person's humanity. For example, to treat a barber as a mere "haircutting appliance" fails to regard them as a person, refuses to recognize their dignity as a fellow human being, and violates Kant's categorical imperative.

Kant's moral theory laid the foundation for much of the modern Western understanding of what it is to be a person. His theory imbues the human individual with a status that can never be ignored justifiably. So Kant stands at the head of the great liberal Western tradition that focuses on the dignity of the individual, and his thought plays a major role in the philosophical justification of democracy, individual autonomy, and the right of each person to direct his or her life as the individual sees fit.

Dignity in Business

The concept of dignity within the context of business emerges most clearly in the relationship between employer and employee. Consider a manufacturing firm. The owner or manager hires employees to manufacture the firm's products. Thus, the employer uses the employee as a means to an end. The question of the dignity of an employee turns on whether the employee regards and treats the employee as a mere means to the production of the firm's output. If the employer makes clear to the employee that he is merely a "factor of production" and has value in her eyes only as labor input, then the employer fails to recognize the employee's humanity and treats the employee without dignity. Alternatively, if the employer recognizes the employee's humanity and acknowledges that the employee has his own desires and life plans, then she treats the employee with dignity and respect. Similarly, the employee should realize that the employer possesses a certain dignity as a person. This implies that the employee should not regard the employer merely as a means of gathering financial resources, but must treat the employer as a person having her own interests and life plans.

In most business situations, a potential customer is treated with considerable courtesy. After all, customers are essential to realizing any firm's main objective—the achievement of profit. While courtesy is a virtue, courteous treatment is not the same as recognizing the potential customer's dignity. For example, consider a sales situation in which a salesperson very courteously and knowingly misleads a potential customer about the qualities of a product and ultimately encourages the customer to buy a product that the salesperson knows will not meet the customer's expressed need. In this situation, the salesperson treats the customer only as a means to profit and fails to respect the customer's dignity as a person.

Perhaps most of us have witnessed something like the following situation. In a small grocery, the cashier is the only employee present and is serving a customer. At the same time, one of the store's vendors arrives to make a delivery. Most likely the cashier knows and has a friendly relationship with the delivery person, and may look forward to a pleasant social interaction with the delivery person. However, almost invariably, the vendor will have to wait in the background for the attention of the cashier. This situation emphasizes the relative importance of the customer and the supplier, with the customer receiving top priority. In this situation, the cashier virtually ignores or disregards the vendor. Is this an affront to the delivery person's dignity? Generally it is not, because the vendor, customer, and cashier all play specific roles in this situation. Not only is the customer likely to be more important in generating profit for the store, but the customer may be entitled to priority in attention due to the role the customer plays in the commercial interaction. The vendor knows and accepts a specific role in this situation. Of course, we may also have seen other situations in which a vendor appears and is treated harshly merely because the vendor appears as a petitioner and occupies a position of relatively low power. In all such situations, the question is to treat persons with the proper respect and dignity, with the proper behavior being governed to some extent by the relative roles that people play in the business situation.

Areas of Controversy

Some people believe that recognizing people's dignity is incompatible with the commercial world as we know it. Furthermore, there is considerable disagreement about what is required to treat people with proper dignity.

The most central aspect of Karl Marx's great critique of capitalism turns on the question of human dignity. Marx believed that the business enterprises of his time, as well as the entire class structure of industrial Western society, treated labor merely as an expendable factor of production. In doing so, Marx believed that employers failed to recognize the humanity of their employees. In virtually all business relationships, whether in Marx's time or ours, people are treated with some measure of respect and dignity. However, the great question is whether people are treated with the proper respect and dignity.

We have addressed this issue to some modest extent with the example of the grocery store and the delivery person. As another example, consider the differing conceptions of dignity that are implied by the agency theory of the firm and those who demand that all full-time employees receive a living wage. According to the agency theory of the firm, the firm is essentially an organization that enters into arm's-length transactions with the firm's stakeholders, such as employees, customers, suppliers, stockholders, and so on. On this view, the moral firm is the one that avoids fraud and deceit, keeps its promises, and fulfills its contracts. Advocates of this view of the firm believe that firms that behave in this way treat others as full moral agents capable of assessing their own interests and entering into contracts that benefit those stakeholders. So on this view, taking the employer–employee relationship as an example, treating an employee with dignity and respect is achieved when the firm contracts with the employee in an honest way and fulfills its side of the bargain. Other attitudes toward employees would be regarded as paternalistic or failing to respect the autonomy of the employee. The welfare and happiness of the employee is not a special concern of the firm—the firm's special concern and obligation are to contract honestly and to fulfill the contract.

In contrast, those who advocate that a firm pay a living wage (a wage sufficient to maintain some minimally decent standard of living) believe that such a wage is necessary to human well-being and to human dignity. For advocates of this view, a firm that does not pay such a wage to its full-time employees fails to treat them with dignity and fails to respect them as persons. This outlook seems to imply an obligation of caring toward employees that is not found in the agency theory. Those who demand that firms pay a living wage focus on the outcome to the employee, not just the procedures of honesty in contracting. They would argue that firms that do not pay a living wage offend against the employee's dignity.

This contrast between adherents of the agency theory of the firm and advocates of a living wage shows the diversity of views concerning human dignity and the kinds of attitudes and behavior that are compatible with respecting human dignity. The example also shows the centrality of the concept of dignity to business, as well as its great importance as a central moral concept of human life.

—Robert W. Kolb

See also Agency, Theory of; Autonomy; Empathy; Employee Rights Movement; Human Nature; Kant, Immanuel; Kantian Ethics; Liberalism; Living Wage; Marx, Karl; Marxism; Natural Law Ethical Theory; Other-Regardingness; Rights, Theories of; Roles and Role Morality; Stakeholder Theory

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Dilemmas, Ethical

An ethical dilemma involves a situation where there is uncertainty regarding what is the proper or right thing to do. This occurs when either of the following two conditions appears involving circumstances that require a resolution:

1. There is a conflict between two, equally valid ethical principles or values.
2. There is a conflict within an ethical principle or value.

Some of the more common ethical values or principles that frame ethical dilemmas include the following:

- *To whom do I have a duty*—self, family, friends, workers, investors, consumers, future generation, and so on?
- *How can I minimize the causes of harm*—harm that is physical versus economic versus psychological, or harm that is actual versus potential, or harm to many versus harm to a few, or harm that is severe versus harm that is minor, and so on?
- *What is a fair or just resolution*—is fairness or justice based on everyone receiving equal shares, or more to those who merit or have earned it, or more to those who have a greater need, or more to those of higher rank or status?
- *How do I protect the entitlements due others,* that is, protect the rights of others—the right to life, to be informed, to be safe or healthy, to be heard (free speech), to conscience (personal beliefs or opinions), to freedom, and so on?
- *How can I maintain or express the importance of* being honest, trustworthy, behaving with integrity, and the like?

A business moral dilemma places the decision maker in a situation confronted with making a decision where ethical principles or values discussed above are in conflict. For example, the classic Ford Pinto case of the 1970s found Ford's management struggling with the challenge of how to bring to the marketplace the new Ford Pinto to stem the tide of consumer purchases of the cheaper, fuel-efficient, Japanese-made automobiles. This quest was confronted by the discovery that the Pinto was highly susceptible to fires if involved in a rear-end collision. These fires placed occupants in the Pinto at greater risk of burns or even death. Ford management wrestled with the importance of offering the car to the American consumer quickly and cheaply versus delaying the delivery of the Pinto while outfitting it with a safety device to prevent or slow the spread of flames if the car was involved in a rear-end accident.

In this and other ethical dilemmas, the decision maker is asked to make a decision that requires placing certain ethical values above others—for example, the value of minimizing people's exposure to harm versus significant economic benefits accrued by other people, or the value of many benefiting versus the value of a few people being harmed. Despite the obvious ethical duty to act in a way that produces "good," sometimes a person is challenged to act in a way that will cause some harm or inflict harm on some people for the sake of the greater good or the benefit of the many.

Ethical dilemmas also may be framed in a way that pits different ethical theories or value structures against each other. For example, in the Pinto dilemma posed above, the answers generally are framed toward seeking the greatest good—maximizing the benefit received by as many as possible despite the suffering endured by some people. But one could also question whether there is ever justification for someone to take another's life or place someone in harm's way. The ethical principle of a "right to life" should be paramount for a decision maker, outweighing a preference for seeking to maximize the benefit for all affected by the decision.

How one addresses (or creates) an ethical dilemma may depend on the person's value structure or adherence to specific ethical principles. For example, a utilitarian reasoner might frame an ethical dilemma as "It is a question of seeking the greatest good for the greatest number." Whereas, a justice or rights reasoner might see the question differently: Life should be protected, or what is a fair resolution to the dilemma while protecting the rights of the individual involved?

Some ethical dilemmas may not be solvable. Again applying the Pinto dilemma stated above, the resolution to the dilemma may not be universally agreed by those struggling with the challenge. Utilitarian thinkers may reach a consensus and agree to a resolution based on a calculation that the greatest good will be served by bringing the Pinto to the marketplace and, therefore, providing profits to the company, growing job security for Ford employees, increasing the return on investment for Ford's shareholders, and offering the American consumer with an American-made, fuel-efficient, affordable automobile. But the deontological (justice and rights) thinkers may find the process of calculating benefits and costs to reach an ethically defensible resolution to be abhorrent.

The utilitarian thinkers may never convince the deontologists that principles should be violated or ignored for the sake of good outcomes. Yet the deontologists have a similar challenge—convincing utilitarian thinkers that sometimes it may be necessary to sacrifice good outcomes for the sake of a principle. For example, they might argue that some things may be worth dying for (the ultimate negative consequences) because of some stance or action that needs to be taken in the spirit of justice.

Ultimately, the ethical dilemma is a dilemma because of the character and intentions of the decision maker. If one callously does not care about the consequences to others, then the decision maker would not hesitate to ignore the life-threatening lack of safety associated with the Ford Pinto if it means achieving personal gain or recognition. For a situation to be considered a dilemma, the decision maker must be aware of and torn between two conflicting ethical values or principles. Yet others who hold precious the value of life may see the actions acceptable to the callous decision maker as a new dilemma—how do we save others from this callous person who would not hesitate to place people in jeopardy?

—James Weber

See also Ethical Decision Making; Ford Pinto; Justice, Theories of; Rights, Theories of; Utilitarianism; Values, Personal

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Directors, Corporate

Corporate directors are the elected representatives of shareholders, put in place to safeguard the interests of the investors who bear the residual financial risk of their firms. They make up one third of the corporate governance triumvirate of executives, investors, and directors. Corporate governance examines the roles of each of these groups, along with their interrelationships and their balance of power. Through most of the 20th century, directors in the United States held significantly more power than did diffused shareholders, although much less than the corporations' CEOs.

Director Responsibilities

In the United States, corporate law dictates that directors must monitor the leadership of the firm to ensure that the corporation is run in the long-term interest of shareholders. They owe investors both the duty of care, or due diligence, and the duty of loyalty, or putting the investors first in their decision making.

Boards of directors are generally recognized as having five key charges. First, and most important, they must select, monitor, evaluate, and when necessary replace the CEO of the firm, with a key underlying duty of engaging in careful, advance succession planning. Second, the board is responsible for ratifying the company's overarching vision and strategic plan, once it is developed by the CEO and his or her staff. Advising and counseling the CEO and other top managers as needed is a third function of the board, underscoring the importance of a board's diversity of expertise. The board's fourth responsibility is to locate and nominate high-quality board members and to evaluate the processes of the board and the performance of both the board and its members. Finally, the board is responsible for ensuring the adequacy of the firm's internal control systems, a duty that is now reinforced by the Sarbanes-Oxley Act.

Director Types

Corporate directors fall into three general categories: inside, outside, and independent. The newer, "independent" profile is replacing the "outside" moniker on most U.S. boards.

"Inside" directors are employees of the firm who also sit on the board of directors. Most commonly, the chief executive officer (CEO) is a member of the board, and often its chair. Chief financial officers, chief operating officers, presidents, and other confidants of the CEO have also frequently been tapped as board members. Inside directors are often credited with being the best informed about the firm and industry, but the presence of CEO subordinates on boards is also criticized because they are beholden to their superiors and likely to vote in their favor.

"Outside" directors are defined as those who are not employees of the firm. Outside directors have traditionally been acquaintances of the CEO or existing board members, invited onto the board to give an outsider's perspective on the firm's prospects and operations. Most often, CEOs or executives of other corporations have constituted the majority of these corporate directors, although retired government officials, celebrities, and academicians have also been frequent members.

In recent years, and particularly since the passage of the Sarbanes-Oxley Act, regulators and shareholders alike have focused on directors' "independence." Some ostensibly outside directors had been found to have significant nondirector relationships with their firms, leaving them subject to pressure from the executive office. "Independence" is defined as a director having no relationship with the firm beyond the individual's board seat.

In the wake of the corporate governance scandals of the early 2000s, the New York Stock Exchange and NASDAQ enacted rules requiring all listed companies to have a majority of independent directors, and that the independent directors meet regularly without the inside directors present. While director independence is now a widespread corporate goal, the empirical investigations pursuing a link between the proportion of independent directors on a board and firm performance have led to mixed results. Board processes, director behaviors, and the "fit" between board and firm characteristics have all been suggested as potentially more reliable predictors of corporate success.

Director Selection and Compensation

As noted above, directors have traditionally been selected through their network of relationships with existing directors. More recently, with the move toward director independence, nominating committees are more frequently used to seek out qualified, yet objective, board nominees to present to shareholders for a vote.

While director pay averaged around $40,000 per year in the early 2000s for U.S. corporations of all sizes, it has risen sharply due to directors' increased legal liability, workload, and media scrutiny. Among the 350 largest U.S. firms, the median director compensation was $155,000 in 2004. Equity is also an increasing proportion of directors' packages, representing 55% of these directors' pay in 2004, up from 36% in 2003.

Board Characteristics

Recently, U.S. boards of directors have become smaller, more external, more diverse, and more focused on committees. As of 2002, boards had an average of 10.9 members, with one quarter of the S&P 500 having between 8 and 9, a significant reduction in size over the previous decade. Another radical change in board composition is in the insider/outsider mix, with one third of S&P 500 firms now having the firm's CEO as its only insider, as compared with only 10% of firms with that composition in 1992. The number of full board meetings has risen with the increase in board vigilance, with the average S&P 500 board meeting 7.5 per year, in addition to a variety of additional meetings of newly constituted and powerful committees. As of 2002, virtually all S&P 500 firms had compensation committees, while 75% had formed nominating/corporate governance committees. Diversity among board members is also increasing, although the overall proportion of female and minority directors in the United States is still very small.

—Lori Verstegen Ryan

See also Chief Executive Officer (CEO); Corporate Governance; Executive Compensation; Market for Corporate Control; Mergers, Acquisitions, and Takeovers; Minority Shareholders

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Disability Discrimination

Individuals with disabilities have physical or mental impairments that prevent their executing one or more major life functions in the species-typical way. This general conceptualization orients discussions of the moral and political dimensions of disability discrimination. For legal purposes, however, who is subject to and protected from disability discrimination is determined by statutory language or judicial interpretations, both of which vary from jurisdiction to jurisdiction.

Individuals considered to have disabilities under the U.S. Americans with Disabilities Act (ADA) must have or be regarded as having a physical or mental condition that substantially limits a major life activity. Under the California Fair Employment and Housing Act (FEHA), however, individuals for whom success in a major life activity is fully achievable but made more difficult than usual because of a physical or mental condition also are protected from disability discrimination. Furthermore, ADA case law takes mitigating measures such as corrective lenses or medications into account in the determination of how limiting a condition may be, while California law explicitly provides for physical and mental limitations to be assessed absent consideration of mitigating measures.

When an individual who has disabilities, or thought to have disabilities, is for this reason treated less well than other people, or excluded from opportunities most others enjoy, that person has been subjected to disability discrimination. Often such discriminatory practice intentionally targets individuals with disabilities with the aim of ensuring that others need not suffer their presence nor have to interact with them. Just as often, however, disability discrimination is the result of thoughtlessness. Practices built on the presumption that only species-typical people will participate can have a disparately negative, and therefore discriminatory, impact on people with anomalous bodies or minds.

That a practice is discriminatory does not, however, establish for everyone that it is wrong. There are individuals who advance a moral claim to freedom of choice of their associates, which they understand as a right to treat some people less well than others, and to remain socially removed from them, on the basis of sex, race, religion, or national origin, or because the people have disabilities. The question this argument provokes is whether the harm of disability discrimination (and of race and sex and other kinds of discrimination as well) resembles the harm absorbed by an unpopular person bereft of invitations to dance or play or join the group for lunch, or whether the harm is of a more profound kind that commands moral consideration. That the harm caused by disability discrimination rises to the level of injustice has not been a commonplace view in the past, nor does this view command universal assent today.

Introduction to Disability Discrimination

Two years after the 1964 U.S. Civil Rights Act banned discrimination based on race and sex, Jacobius tenBroek, a leading legal scholar and founder of the

National Foundation of the Blind, wrote a law review article describing the pervasive harm rendered by disability discrimination and calling for the extension of civil rights protection to people with disabilities. He pointed out that individuals with disabilities were subjected to social and legal sanctions—in the form of inferior standards of care, conduct, risk, and liability that result in exclusions, penalties, and hurdles—when they attempted to participate equally with other people in civic and commercial activity. tenBroek characterized the placing of such barriers to discourage and delimit civic and commercial engagement of people with disabilities as a kind of house arrest that curtailed their ability to contribute as citizens. Despite holding a chair at a research university and winning the most competitive fellowships and book awards, tenBroek himself had no legal recourse when restaurants declined to serve him and banks refused to let him open an account, and he was denied transit on planes and trains despite having purchased a ticket, just because he was blind.

In such a discriminatory climate, comparatively few people with disabilities succeeded in the workplace. Race and sex discrimination keep their targets in low-paying jobs, maintaining a source of cheap labor. But disability discrimination forces its targets out of the workforce altogether, situating them instead as natural recipients of state or charitable support.

Five years after the Civil Rights Act, just as racial minorities and women were beginning their great strides toward employment equality, the United States initiated a program of Supplemental Security Income (SSI) to support people with disabilities from childhood to grave on the premise that they will not be in the workforce. A wide variety of programs, such as aid to the blind and aid to people with permanent and total disabilities, were consolidated under the Social Security Administration. The Social Security Disability Insurance (SSDI) process for determining whether workers are too disabled to be employed was extended to SSI, even though some SSI recipients were children who were thus labeled unfit for work even before they reach working age.

History of Disability Discrimination

Disability discrimination had long been embedded in every aspect of civic and commercial life. For many centuries, however, discrimination was more a matter of ignoring than of targeting people with disabilities. The example of the influential 18th-century literary figure Samuel Johnson is illustrative. Dr. Johnson was blind in one eye, had limited vision in the other, was deaf in one ear, was badly pockmarked, picked compulsively at his skin, suffered from spasticity or palsy and later in life from severe arthritis, and seems sometimes to have been so depressed as to remain bedridden. These impairments struck his contemporaries not as disabilities but as mere anomalies, facets of the life of a singularly independent-minded brilliant man, nothing that would mark a person as unfit for social participation.

Pre-19th Century

Before the 19th century, chronic impairments were considered inescapable features of ordinary life. A few, such as leprosy, condemned those who suffered from them to be shunned because they were believed to be contagious. Some were attributed to supernatural intervention. Blindness, for instance, sometimes was explained as punishment meted out by supernatural beings. As often, however, blindness was understood to render an individual able to commune with the supernatural and to function as a seer of the future or offer other insightful advice. In the main, however, people with disabilities were not banned from participating socially if they could do so despite their impairments.

At least from early sixth-century Athens, war veterans with disabilities were maintained at public expense. By Aristotle's time, men whose means fell below a specified line, and who were too incapacitated to work, received daily public payments through a treasurer elected by lot. Programs such as this, or such as the Roman pension plan for veterans of foreign wars with disabilities, were considered insurance against the bad luck of diminished ability to earn one's bread. Such benefits were protection due to individuals who had contributed to the community's welfare when they were able.

In general, people worked despite their impairments if they needed, and were at all able, to do so. Individuals with mild or moderate cognitive impairments, and hearing impaired individuals as well, engaged in the manual labor of agrarian societies. Guilds of blind musicians and fortune tellers survived for many further centuries in China; and in Japan there were guilds of blind acupuncturists, and of masseurs who often doubled as money lenders (the worth of coinage being discernible by feel).

In Western Europe, there also were groups such as the guilds of the blind who joined together to hire guides, work at certain crafts, and visit the sick. But in

European cultures the inclusion of people with disabilities in the workforce, whether in ordinary or in specialized roles, and in society in general, declined with the rise of a factory economy and the concomitant emphasis on standardization of workers. Before 1820, in the United States, for instance, most cognitively impaired people stayed with their families or were placed with other community members to do simple but necessary work in the household or on the farm. During the next 40 years, institutions meant to train these individuals so that there could be more productive sprung up, supported by charitable donations and local government funds.

19th and 20th Centuries

Beginning in the period after the Civil War, however, these facilities created to improve the life skill proficiency and productivity of cognitively impaired people and to return them to work in the community were transformed into custodial institutions. Several economic factors intersected to promote the change. First, waves of immigrants needed work so jobs in the community became scarcer, and other groups did not want competition for work from people with disabilities returning home from the training schools. Second, as populations became urbanized and their work industrialized, caring for an impaired family member interfered with wage earning. Third, the factory and office did not have the same tolerance for anomalous individuals as the house and the farm. Indeed, 20th-century efficiency experts have urged that work sites and tools be standardized and employment focus on individuals whose bodies and minds are of standard form.

To improve their financial condition, these "homes" vigorously recruited less-impaired inmates who, once they were institutionalized, were put to work caring for the others and doing the routine maintenance work. When inexpensive paid help was hard to find, institutional officials were especially reluctant to release better worker patients. Deaf, blind, and cognitively impaired individuals, and people with other kinds of biological anomalies, were forced into situations that resembled nothing more than slavery. Institutionalization was rationalized as a way of protecting ordinary people against individuals too damaged to observe proprieties and exercise proper moral constraint, and of relieving communities of burdens of care.

In the United States, intentional segregation of people with disabilities has been primarily a post–Civil War phenomenon, initiated at roughly the same time as racial segregation. The aim was to ensure that people with disabilities not delay progress by inserting themselves into civic and commercial activities. During the first half of the 20th century, and in some places through the 1970s, eugenics programs that sterilized people with disabilities against their will furthered this aim.

Hundreds of discriminatory practices abounded, ranging from banning people with disabilities from jury service to systematically denying custody of their own children to parents with disabilities. To have a recognizable disability was (and to some degree still is) to be disqualified from the ordinary guarantees of fair treatment and from the opportunities the state offers for a flourishing life.

Impact of Disability Discrimination

Intentional Disability Discrimination

The impact of this history of segregation continues to permeate and plague business activities today. Some businesspeople mistakenly believe that an individual's disabilities constitute a legally defensible justification for not doing business with that person. For example, in 2004 the largest number of complaints received about overt discrimination by landlords and rental discrimination violating federal fair housing laws came from people with disabilities. A test project conducted in Chicago as a preliminary to federal enforcement of the Fair Housing Act's antidiscrimination provisions found that people with disabilities had a one in three chance of being illegally denied housing because of prejudice such as overt policies of not renting to people with disabilities. It is similarly illegal (under federal or state law) for businesses to refuse to serve, transport, or otherwise engage with individuals simply because the individual has disabilities, or because other customers might be made uncomfortable by the presence of a person with disabilities, or because the person with disabilities relies on an aid such as a guide dog or wheelchair.

Intentional employment discrimination based on disability also is illegal. To illustrate, in 1999 a federal jury found for a plaintiff with intellectual disabilities who communicated using picture cards and a handheld computer device. Employed as a janitor at a Chuck E. Cheese establishment, the individual received excellent evaluations from the onsite manager but was fired by a regional manager who stated that the business did not employ those kind of people. The company CEO ignored coworkers' pleas to reverse the decision, and the company's attorneys argued that people with mental retardation are not distressed when ejected from the workforce. The jury disagreed, awarding $10,000 in back pay, $70,000 compensatory, and $13 million in punitive damages (reluctantly reduced by the judge because of statutory limitations).

Thoughtless Disability Discrimination

Instances of thoughtless disability discrimination vastly outnumber intentional discrimination, however. The historically embedded expectation that individuals with disabilities should not engage in commerce nor present themselves to work invites inattention to the existence of barriers to their participation. Examples of such barriers include construction practices that assume all customers are able to walk up stairs, informational practices that rely on broadcast announcements, and scheduling practices that ignore the regularity with which people with diabetes must ingest food.

Such practices that disparately disadvantage people with disabilities discriminate against them, and failure to remedy the resulting barriers may expose businesses to legal action unless the remedy is unreasonably costly, measured against the business's overall operating costs. That other customers may retreat from mingling with people with disabilities, or other employees resent working alongside a colleague with disabilities, is never a legal defense for discrimination. But employers have defended successfully if they demonstrate that an individual's disability results in higher absenteeism or earlier retirement, so that other employees absorb the burden of doing extra work.

Improving Social Participation of People With Disabilities

Employing People With Disabilities

Far from being generally burdensome, employees with disabilities appear to have more reliable attendance records and greater longevity and loyalty than do people without disabilities, according to the national surveys conducted regularly by the National Organization on Disability. Embedded discriminatory attitudes and practices, nevertheless, make it twice as difficult for qualified people with disabilities to find employment. In both the United States and the United Kingdom, roughly 80% of working age people have gainful employment, but only roughly 40% of people with disabilities with demonstrated work capability find employers willing to give them work. These individuals swell the roles of public benefits programs. Furthermore, the rarity of successful people with disabilities in the workplace strongly suggests to workers who become disabled the futility of attempting to support themselves.

Technology and People With Disabilities

Far from impeding progress, enabling the participation of people with disabilities stimulates innovations that have revolutionized business efficiency. For example, the typewriter was invented to enable people with visual impairments to record written text. Not all innovations meant for people with disabilities have benefited them, however. Alexander Graham Bell, son and husband of deaf women, was aiming for amplification to improve communication with them by inventing the telephone. But this device had a disastrous outcome for the group for whose benefit it was invented, for business communication no longer needed to be face-to-face, and individuals who relied on lipreading gradually found themselves forced out of the majority of work sites because they could not use the telephone.

Just about a century later, the situation reversed, as the Internet, which configures information for sight rather than sound, was invented and rapidly became a major route for business communication. Now, however, the already restricted opportunities for visually impaired individuals were threatened, for communication through text was as much a barrier to them as telephoned communication was to deaf people. This time, though, increased social commitment to eliminating inadvertent disability discrimination made for a very different story.

Computers can deliver aural as well as visual output. During the last decade of the 20th century a spontaneous disability community campaign, furthered by research in a few university sites, convinced software companies to make proprietary codes available to software developers specializing in voice output programs, and to fold voice output capability into their own development programs. Spurred by federal antidiscrimination measures, books may be purchased in computer-readable form, banks use this technology to offer talking ATMs, and businesses generally are more responsive to the integrated community that includes some for whom seeing, but others for whom hearing, is the vehicle of communication.

An Untapped Market

The National Organization on Disability describes the disability community, comprising nearly one fifth of the American population plus families and friends, as a market untapped because of residual discrimination but conservatively worth at least $220 billion in collective spending power. To remedy discriminatory practices, businesses have initiated a replete repertoire of strategies, from manufacturing items that meet the standards of universal design and thus are usable by individuals of varying degrees of dexterity, sensory acuity, and strength to fostering a culture of inclusion by ensuring that disability is a central topic in the organization's diversity training.

Legal Remedies

In the United States, the 1990 ADA is the main staging ground for federal investigative and judicial action to remedy disability discrimination in employment, housing, education, and access to public services. The Rehabilitation Act prohibits discrimination on the basis of disability in programs conducted by federal agencies, in programs receiving federal financial assistance, in federal employment, and in the employment practices of federal contractors. Its provisions predate and are reflected in those of the ADA. The Individuals with Disabilities Education Act (IDEA) requires public school districts to provide an appropriate education in the least restrictive environment for children with disabilities. The Architectural Barriers Act requires that facilities designed, built, altered, or leased with federal funds be accessible to people with vision, hearing, and mobility impairments. Under the Air Carrier Access Act, airline operators must provide equitable access to air transport for individuals with disabilities because carriers are prohibited from discrimination against qualified individuals with physical and/or mental impairments. The Fair Housing Act prohibits discrimination in any aspect of selling, renting, or denying housing because of an individual's disability. Reasonable exceptions to housing policies must be made if needed to afford equal housing opportunities to people with disabilities. States also offer many statutory protections against disability discrimination.

Many other nations also offer legal protection to people with disabilities. Most, however, situate these within a human rights rather than a civil rights frame. They tend to understand disability discrimination as a problem of failing to care for the special needs of people with disabilities rather than as a diminution of opportunity to satisfy ordinary needs. As a consequence, they are less likely to enact statutes that promote systematic social integration, but more likely to offer supportive services.

In the short run, businesses may prefer the latter approach, which expects government to support those with disabilities as compensation for the adverse effects of disability discrimination. By requiring businesses to do their part in improving the economic and social status of people with disabilities, however, the former approach may be more cost effective in the long run.

—Anita Silvers

See also Age Discrimination; AIDS, Social and Ethical Implications for Business; Americans with Disabilities Act of 1990 (ADA); Civil Rights; Egalitarianism; Equal Employment Opportunity; Equality; Equal Opportunity; Gender Inequality and Discrimination; Procedural Justice: Philosophical Perspectives; Racial Discrimination; Rawls's Theory of Justice; Reverse Discrimination; Rights, Theories of; Social Contract Theory

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Disclosure

Disclosure is the release of information that would not otherwise be known by the parties that receive it. Disclosure may be the release of information either to the general public or to a limited, selected audience, sometimes under conditions of confidentiality. The release of information may also be either voluntary or legally required. Although the disclosure of financial information is an important topic in accounting and finance, the concept of disclosure in business applies to all kinds of information that are released for many different reasons. Disclosure is studied in business, mostly in accounting and finance, primarily to determine its impact on firms' performance, but it also raises many ethical concerns. The main ethical issues concerning disclosure are the following: (1) When is disclosure morally required? and (2) when is disclosure morally permissible or morally prohibited? These two questions may also be asked of the law on disclosure, and in some cases, disclosure is legally required, legally permissible, or legally prohibited. In general, morality and law are in close alignment, but they may occasionally differ so that, for example, disclosure may be morally required but not a legal obligation.

Morally Required Disclosure

A person or an organization may be morally required to disclose information for three reasons: The release of information (1) may prevent some significant harm that cannot easily be prevented in other ways, (2) may be required to ensure fairness in markets, and (3) may manage a conflict of interest.

With regard to the first reason, a manufacturer may have a moral obligation to release information about a defect in a product in order to protect consumers from serious injury or even death, and they are also morally obligated to inform employees about some workplace hazards that can cause illness or injury. The disclosure of some product defects and workplace hazards are also required by law either directly through legal requirements, such as an order from the Consumer Product Safety Commission or the Occupational Safety and Health Administration, or indirectly by the standards for negligence in tort law. Thus, a manufacturer may be said to have a legal obligation to disclose a defect if the failure to disclose it could be considered negligence. The principle involved in both morality and law is that one ought not to knowingly cause harm to another. However, disclosure is only one means for preventing harm, and so it may not be morally required if other, more effective means are used. Thus, an employer may not have an obligation to inform employees of workplace hazards if the employer takes other, more effective steps to protect employees.

The second reason—to enable markets to operate fairly—arises from the fact that markets produce mutually beneficial outcomes only if there is perfect information. Fair, as well as efficient, markets require, in other words, that buyers and sellers have full information about what they are giving up and receiving in return. The need of markets for perfect information does not, by itself, entail an obligation on either party in a transaction to disclose except in two cases. One exception is fraud, which is committed when one party to a transaction makes a false or misleading statement or omission of a significant fact that the other party relies on to his or her detriment. Thus, a seller of a house is under a moral and a legal obligation to disclose significant defects since a failure to disclose is an omission that constitutes fraud.

The other case in which disclosure may be morally or legally required in market transactions is when it enables buyers to acquire information that enables them to benefit from market transactions and not be at an unfair informational disadvantage. For example, a consumer cannot easily determine the contents of packaged food products, and so federal consumer law requires the manufacturer to disclose certain information, including the weight or volume of the product, the ingredients, and certain nutritional information. Similarly, federal securities law requires the issuer of securities, such as stocks or bonds, to provide a prospectus that contains certain information about the issuer and the securities. More broadly, securities laws require that issuers make extensive disclosures in regular filings that are available to all investors. The law also regulates how information is disclosed. Thus, Regulation FD (for fair disclosure) requires that public companies make any disclosures to analysts publicly so as to avoid selective disclosure to some analysts but not others.

Although fairness in market transactions requires that both parties have certain information, it is not easy to determine what information either party has an obligation to disclose. For example, is it fair for an art expert who identifies a valuable painting at a rummage sale to buy it without telling the owner of its value? It might be argued that the art expert has a right to take advantage of superior knowledge and that the owner could have sought an appraisal. The information in question is itself a valuable commodity, and so, arguably, the art expert has no obligation to provide for free what the owner is not willing to pay an appraiser to provide. However, the legal obligations to disclose on labels and prospectuses may be morally justified on the ground that the government has a right to facilitate fair and efficient markets. In particular, such laws are based on the premise that buyers ought to have certain information and that the sellers can more easily provide it. Thus, social welfare is enhanced if these kinds of disclosure are legally required.

Government may legally require disclosure for reasons other than market fairness. For example, disclosure is an important means of regulation. The requirement that issuers of securities provide a prospectus is intended not merely to enable buyers to make rational decisions but also to ensure that securities are fairly priced. This could be achieved without disclosure by requiring approval from an agency that evaluates the price of stock and bond offerings, which is the approach of the so-called blue sky laws. However, disclosure, which allows the market to determine prices, is probably a more effective means of assuring fair prices than the use of a state agency. Disclosure may also be required by government to prevent restraint of trade under antitrust law. For example, the European Union has sought to require that Microsoft disclose its code for Windows so that other software companies could develop Windows-compatible software. Another example of the use of disclosure to regulate is the requirement of the Securities and Exchange Commission (SEC) that public companies disclose certain information about executive compensation. In this instance, the SEC, unwilling or unable to set limits on pay, has used disclosure to allow the market to prevent excessive compensation.

The third reason—to manage conflict of interest—is due to the point that disclosing a conflict enables the party who is potentially harmed to be aware of the conflict and take protective action. A conflict of interest arises when a person has a personal interest that interferes with an obligation or duty to serve the interests of another. Thus, a physician who owns a laboratory to which he or she refers patients has a conflict of interest because it may bias the physician's judgment, which ought to be exercised solely for the patients' benefit. However, if patients are aware of the physician's ownership, they may be able to question the physician's judgment and make a more informed decision. Disclosure in such a case may not be morally required because there are other means for satisfactorily managing conflicts of interest. However, morality requires that some means be employed to manage the conflict of interest and thereby enable the physician to fulfill the duty to serve the patients' interest. Disclosure is used in a similar manner to manage conflict of interest among public officials by rules requiring them to disclose their financial holdings.

Morally Permissible/ Prohibited Disclosure

The question of when the disclosure of information is morally permissible or morally prohibited arises mainly when the information in question is confidential and proprietary. The owner of a trade secret, for example, has a right that it not be released without authorization, so that its unauthorized release is morally, and perhaps legally, impermissible. However, it may be morally permissible in some circumstances for a person without authorization to release confidential, proprietary information.

For example, whistle-blowing, which is the disclosure of information to the public in order to protect people from the harmful activities of an organization, is sometimes held to be morally permissible and possibly, in some instances, morally required. The information released by a whistle-blower is generally proprietary, but its release is morally problematic only when the whistle-blower has a duty to preserve its confidentiality. For example, a journalist has no obligation not to publish proprietary information as long as it was not wrongly obtained, because the journalist, unlike an employee of a company, has no duty of confidentiality to the employer. In general, the disclosure of confidential, proprietary information by a whistle-blower is morally justified when, among other conditions, the good that results from protecting the public outweighs the violation of the information owner's right that it not be disclosed.

The permissibility of disclosure is an issue not only with the proprietary information of a business organization but also with people's personal information. An individual's right to privacy is respected when certain information about themselves is not known by others. Thus, it would be a violation of privacy for a person's medical or financial records to be disclosed to other parties without that person's consent. Accordingly, record keepers have an obligation not only not to disclose personal information but also to take steps to secure it from inadvertent disclosure.

The question of the permissibility of disclosing information also arises when disclosure could cause some harm. For example, software designers disagree on whether security flaws in operating software ought to be disclosed to the public. On the one hand, such disclosure could make the public aware of security flaws and lead to fixes that would provide greater protection. On the other hand, the disclosure of security flaws could aid hackers and lead to more breaches of security. There was a similar controversy in the 19th century when locksmiths debated whether weakness in lock systems should be publicized or kept secret. The enactment of the so-called Megan's Laws, which permit or require the disclosure of sex offenders' names, brings two legitimate moral concerns into conflict. Sex offenders who have served their sentences have a right to resume their lives without restrictions, and yet parents arguably have a right to know of sex offenders' presence in a community in order to protect their children. Whether disclosure of their names is morally permissible thus involves the weighing of two moral goods.

The World Wide Web has exacerbated the moral problems of disclosure by making access to information much easier. Much of the information available on the Internet has long been publicly available so that there has been little question of the moral permissibility of its disclosure. However, the impact of this information for good or ill has been of little concern since much of it could not be easily obtained. With the easy access provided by the Web, the benefits and harms of the disclosure of this information may need to be reevaluated.

—*John R. Boatright*

See also Blue Sky Laws; Confidentiality Agreements; Conflict of Interest; Consumer Fraud; Consumer Protection Legislation; Consumer Rights; Fairness; Fiduciary Duty; Fraud; Negligence; Occupational Safety and Health Administration (OSHA); Privacy; Product Liability; Regulation and Regulatory Agencies; Securities and Exchange Commission (SEC); Whistle-Blowing

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Discounting the Future

Discounting the future occurs when an immediate benefit is systemically valued more highly than a delayed benefit. As with other discounted cash flow projections, the variables are the size of the estimated cash flow, the number of discounted periods in the future, and a relevant discount or interest rate. In a case involving one cash payment or outflow (PV) and one future payment or inflow (FV) at a relevant discount rate (r) for a number of discount periods (n), the present value (PV) can be expressed as

$$\mathrm{PV} = \mathrm{FV} \div (1 + r)^n$$

A classic example is an amount of cash placed in a savings account (PV) to be redeemed on a future date (FV). All other things being equal, the present value of a cash flow decreases with a decrease in the size of the future cash flow, an increase in the number of discount periods, or an increase in the discount rate. Alternatively, the present value of a cash flow increases with an increase in the size of the future cash flow, a decrease in the number of discount periods, or a decrease in the relevant discount rate.

Cost-benefit analysis takes into account all present and future cash inflows and outflows expected to occur over the life of the project. The present value equation is at the heart of cost-benefit analysis. The discount procedure is essentially a way of reducing a stream of costs or benefits over time to a single sum. Thus, different projects with different cost streams are comparable.

Future payments and costs should be treated in the same way as future receipts and benefits. When future payments or costs and receipts or benefits are discounted to the present and added together, the resulting amount is the net present value (V_0). Therefore, the net present value at time $t = 0$ of a project, which has a duration of n years, and which has costs and benefits of C_t and B_t for $t = 0 \ldots n$, is given by

$$V_0 = (B_0 - C_0) + (B_1 - C_1) \div (1 + r) + \ldots + (B_n - C_n) \div (1 + r)^n$$

The project should be undertaken only if $V_0 > 0$. A value of 0 is the point of indifference with respect to accepting or rejecting the project.

Cost-benefit analysis is based on a number of assumptions that must be valid for the calculation to be accurate and relevant to the decision at hand. First, it is assumed that all costs and benefits can be reduced to monetary amounts. The problem of placing valuations on untraded goods and services or intangible factors such as environmental quality is difficult when market values are not available. The value of intangibles such as historical landmarks, Stonehenge or Mount Rushmore for example, is likely to vary widely among the populace. In the absence of market values, a consensus ranking might be used according to public opinion. However, consensus rankings cannot be expressed meaningfully in the same manner in which a consumer might express his or her preferences among economic goods.

A second assumption is that the costs and benefits in the analysis are the same for each person. Only in rare circumstances is everyone a beneficiary of a project. This situation is especially obvious in projects that are undertaken by a present society to benefit future generations.

A third factor is the discount rate. An objective discount rate for monetary costs can be determined by the opportunity cost of funds or the benefits forgone by investing in a given project. A discount rate may also be a subjective reflection of a consumer's preference for immediate rather than deferred benefits, expressed as the marginal rate of time preference.

Using a positive discount rate in cost-benefit analysis incorporates the assumption that today is more important than tomorrow. From this it follows that present generations discriminate against future generations. Using a discount rate of zero or a negative discount rate is one means of avoiding such discrimination in a cost-benefit analysis.

The discount factor is often modified in cost-benefit analysis by imposing a risk premium on projects that are perceived as more risky than others. Adding a risk premium is intended to place projects under comparison on equal footing. However, the addition of a risk premium increases the discount rate and magnifies the time preference for today.

Future Generations

As a branch of welfare economics, cost-benefit analysis is framed by considerations for morally correct or fair decisions. For example, the Hicks-Kaldor criterion asserts that a project should be approved only if those who gain from it could compensate those who lose and still retain some net benefit. Thus, the short-term and long-term effects of the decision are relevant. A utilitarian perspective focuses on the consequences of a decision with the objective to maximize the good for the greatest number. In actual practice, comparisons of gains and losses between groups and among individuals are rarely made. A utilitarian perspective does not necessarily include consideration of consequences borne by future generations. Utilitarian frameworks are commonly used to evaluate the costs and benefits of long-term decisions.

The Rawls's theory of justice differs from the tradition of Hume, Adam Smith, and Bentham in the sense that it is nonutilitarian. Rawls rejects the idea that the loss of freedom for some is justified by the greater good shared by others.

Rawls's theory of justice acknowledges the rights of future generations. Rawls establishes principles that exclude all forms of discrimination. Standing behind the Veil of Ignorance, no rational person would chose to be a member of a disfavored class. The principle of intergenerational equality is in fact the first principle of justice in Rawlsian theory. From the perspective of a society, pure time preference is unjust because it means that the living take advantage of their position in time to favor their interest. Second, the Difference Principle can be applied to future generations who are "least advantaged" in terms of consequences to a decision. Justice requires that if others profit from a practice or decision, the least advantaged must also benefit. One group should not benefit at the expense of another group or another individual. Thus, if the present generation benefits from a decision, future generations must benefit as well.

Weiss's theory of intergenerational equity derives from Rawls's arguments. The theory states that each generation has an obligation to pass on to the next generation the natural and cultural resources in no worse condition than the condition in which the resources were received.

Decisions That Harmed Future Generations

Cost-benefit analysis disfavors future generations when the benefits are received by current generations but the costs and consequences are delayed to future periods. Two prominent examples of economic decisions that provided current benefits to one group of people and heavy penalties to later generations were ecological disasters coinciding with the end of the native Anasazi and Mayan civilizations in North America. Recent examples appear in the 21st century.

In 2002, scientists reported the drying up of the Aral Sea, located in central Asia, as one of the worst ecological disasters of all time. The Aral Sea was once the world's fourth largest lake. However, diverting river water to the desert areas of Uzbekistan, Turkmenistan, and Kazakhstan for cotton farming for the past 30 years has reduced the lake to one third of its original size. Without the moderating effects of the large sea, the climate in the Aral Sea area changed producing shorter, hotter summers and longer, colder winters. The change in climate and shrunken sea destroyed the economic base of fishing and agricultural products. The community was affected by poverty, lack of drinking water, malnutrition, and disease.

In 2004, the U.S. National Aeronautics and Space Administration (NASA) compared Landsat satellite images taken in 1992 and 2000. Light sensors aboard the Landsat craft detect different features on the Earth's surface, such as the existence and condition of vegetation, soil conditions, and the existence of wetlands. Image comparison revealed a transformation in southern Iraq and a rapid shrinking of the Mesopotamian marshlands from their original size of 15,000 to 20,000 sq. km to less than 1,500 to 2,000 sq. km.

In the early 1990s, Iraqi dictator Saddam Hussein ordered the destruction of the marshes in retaliation for an uprising against his regime. Draining the marshlands reduced the yield from fisheries, shortened the supply of drinking water, and narrowed the habitat for migrating birds. Because the marshlands have historical significance and intangible religious value, the elimination of the marshlands is a cultural disaster as well as an environmental disaster. As a cultural disaster, it affects not only the Marsh Arabs who live in the marshes, but also those who ascribe to Christianity, Judaism, and Islam, whose origins are in the Mesopotamian marshlands. The marshlands are also known as the cradle of civilization and the site of the Sumerian, Akkadian, Babylonian, Assyrian, and Chaldean civilizations; the Epic of Gilgamesh; the Garden of Eden; the Great Flood; and the birthplace of the patriarch Abraham who is given credit in the Old Testament for founding the Jewish nation.

Current Decisions Affecting Future Generations

There are examples of current decisions and public projects that are communal in nature and accordingly affect current populations and future generations. Projects for the generation of nuclear power were started decades in advance of viable plans for the disposal of waste. Radioactive waste such as iodine-129 has a half-life of 17 million years. Current and future costs include those for devising safe and effective means of protecting the biosphere from radioactive waste, construction and waste removal transportation costs, monitoring costs, failure costs in the form of cleanups and health issues from accidents and exposure to waste, and the costs of decommissioning worn out nuclear power plants. Related costs are the development of alternative energy sources.

Global warming is attributed to man-made emissions of carbon dioxide and other greenhouse gases traced to the use of fossil fuels. The costs of climate changes and the resultant effects on future generations are inestimable. Major effects include floods, storms, and droughts and the loss of life for humans, plants, and animals. Along with private citizens and grassroots movements, several nonprofit organizations are actively involved in promoting international cooperation to reduce emissions. The World Wildlife Fund states that the most effective way to reduce emissions globally is for the world to work together under one agreement rather than multiple plans and agreements. The Kyoto Protocol, based on binding caps on emissions, is the first working treaty to counteract global warming. As of 2005, the Protocol has been signed by 152 nations. The United States and Australia have not signed the agreement.

In 1997, the Kyoto agreements set targets of a 5% reduction of fossil fuel emissions to be attained by 2012. By 2005, rapid industrial growth in a few highly developed countries had actually increased emissions. In the United States, industrialization and emission levels had grown such that a 5% reduction of the 1990s levels would have been approximately a 25% to 35% reduction of the levels produced in 2005. Cost-benefit analysis determined that the Kyoto protocol was unaffordable and, furthermore, too difficult to attain by 2012.

Forest restoration projects are an example of costs undertaken in the present to benefit future periods. The average maturity period for softwoods such as pines and spruce and hardwoods such as oak, beech, and ash range between 40 to more than 100 years. The costs of maintaining forests include the opportunity cost of the land, cost of planting and replanting, thinning and rotation, losses from fire and disease, and costs from tax levies. The distance of the benefits on the time line and the current costs of reforestation projects are calculable. However, some benefits are often overlooked in a cost-benefit analysis of the project. These include flood control, prevention of soil erosion, avalanche control, and protection of the tree species, recreation, and pollution abatement.

U.S. Congress has enacted several pieces of legislation that recognize obligations of current generations to preserve the global ecosystem and maintain a habitable planet for the future. Notable legislation includes the Clean Air and Water Acts and the Endangered Species Act. The World Wildlife Fund and the Defenders of Wildlife Organization are two of many nonprofit organizations that sponsor projects through private donations and grants from various entities. These groups emphasize the importance of protecting biodiversity for future generations. The global and international importance of safeguarding the natural resources of the earth, including air, water, land, flora, and fauna, is expressly stated in the Stockholm Declaration on the Human Environment following the 1972 Stockholm Conference on the Human Environment.

—Eleanor G. Henry and James P. Jennings

See also Acid Rain; Chernobyl; Cost-Benefit Analysis; Ethical Decision Making; *Exxon Valdez*; Hazardous Waste; Love Canal; Natural Resources; Rawls's Theory of Justice; Utilitarianism; Welfare Economics; World Wildlife Fund

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Diversity in the Workplace

Diversity may seem self-explanatory, yet it may have different meanings in organizations with respect to different contexts. The term is first defined, followed by a historical background, and contrasted with its definition in today's environment. Diversity issues from the management and employee perspectives are finally considered.

Until lately, diversity in the workplace has been implied as the ongoing interaction between employees and employers with different cultural, ethnic, and racial backgrounds that have significant influences on the operations and management of an organization. However, recently, diversity has broadly been redefined as the collective differences and similarities of different dimensions. For example, diversity issues related to demographic characteristics of employees are different from those related to diverse functional issues such as marketing, research, manufacturing, finances, and so on within an organization. Thus, employees' demography and organizational functions are two different dimensions of diversity. In other words, today's workplace diversity represents the complex multidimensional issues involving workers and management of similar and dissimilar nature.

The History of Diversity in the Workplace

Diversity and multiculturalism have gradually been a part of the workforce in the United States since the latter half of the 19th century. The melting pot and Americanization movements of the 1880s were directed toward removal of cultural and linguistic differences by assimilation. Throughout the history, politicians, educators, and industry leaders tried to eliminate the differences between new immigrants and contemporary American residents in society, as well as in the workplace. Their efforts were only partially successful, as it became obvious that blending into the American melting pot was not so easy for immigrants who had very different cultures and were visibly different from the early settlers from the European continent.

Policy makers started to recognize the issues related to diversity since migration from developing countries was growing faster than those from the developed nations. In 1940, more than 85% of immigrants were from Europe, whereas in 1995, 75% were from non-European countries. By early 1990s, the organizations felt the hard reality of managing a workforce consisting of immigrants from developing countries with diverse and "unmeltable" social, cultural, physical, and racial backgrounds. Increasingly, studies have shown the growing concerns of managers about diversity issues in the workplace. The two most important concerns were how to communicate with their employees and how to motivate them.

Today's workforce is more diverse than ever. According to the U.S. Bureau of Labor Statistics, of the 26 million new workers who came into the workforce in the United States between 1990 and 2005, about 80% were minorities, including women. Sometime between 2055 and 2060, the total minority population is projected to surpass the nonminority population, which now consists of Euro-Americans. At the same time, the buying power of the minority groups are increasing at a fast pace. For example, in 2005, African Americans spent $630 billion a year in goods and services, while the Latin American market continues to grow even faster and is comprised of the largest minority group with a spending power of more than $700 billion.

Diversity and Characterizations of Employees in the Workforce

The most important reason for diversity to become a major issue in organizations is the significant change in workforce population since the later half of the 20th century. The steady growth of minority populations is projected to make them the domineering force in the workplace in the future.

The earlier philosophy of the "melting pot" was to ignore the individual differences and thus form a unified society with a distinct hierarchy in the workforce. But it ceased to be effective with the increase in immigrant population from non-European countries during last few decades. It became more difficult for the new immigrants to be unified with a society with very different social and cultural values. They spent more energy on adapting to the existing organizational culture—this sometimes hindered their ability to develop innovative ideas and build personal strengths.

Based on ethnicity, gender, and other factors, the workforce populations can be categorized in many ways. Major groups (listed alphabetically), based on ethnicity and religion, are African Americans, Arab Americans, Asian Americans (e.g., Chinese Americans, Asian-Indian Americans), Euro-Americans, Jewish Americans, and Latin Americans, among others. Other groups based on reasons other than ethnicity and religion are the elderly; persons with disabilities; individuals with gay, lesbian, and bisexual orientations; obese people; and women. Characteristics of the three largest ethnic groups are briefly described in the following paragraphs.

African Americans

According to the statistics from the U.S. Census Bureau and U.S. Department of Labor, 12% of the workforce consisted of African Americans. Their resilient culture nourished certain key values and customs for surviving in the society, such as sharing and interrelating, expressing personal style and uniqueness, being genuine yet assertive, expressing feelings, and bouncing back. African American churches have had a major influence on their community life.

Latin Americans

The fastest growing minority group in the United States is Latin Americans. According to the U.S.

Census Bureau and U.S. Department of Labor, 12% of the employees is comprised of Latin Americans. The majority of Latin Americans are Mexican Americans (58%). The rest of this group consists of Puerto Ricans (10%), Cubans (4%), Central (5%), South (4%), and other Latin Americans (19%). The population of Latin Americans grew four times more than the growth of the U.S. population between the years 1990 to 2000. This trend of fast population growth will continue for this group because they are relatively young and have almost twice the birthrate of Euro-Americans. By learning and understanding the common Latin American culture, the efficiency and productivity of this group can be increased to its fullest.

Asian Americans

Asian Americans consist of 4% of total U.S. population according to U.S. Census results. The Asian American group consists mostly of people from China, the Philippines, India, Vietnam, Korea, Japan, and a few other countries from this continent. About 66% were foreign born, and 54% of them live in the Western region, mostly in California. They have the highest level of education, and their work achievements make them valuable assets in the workforce. Many of the Asian Americans have a reputation of working hard, being productive, willing to work long hours, maintaining a frugal lifestyle, investing in higher education, and identifying the American dream of hard work leading to a better life.

Strategies for Success for Minority Employees

The minority employees can follow several strategies to sort through the complexities in the workplace. At the outset, keeping an open mind about the management's diversity policies is very important. Sometimes, even well-intentioned managers may need to be educated about the cultural trends and personalities of minorities. It is also essential to socialize, acknowledge, maximize mutual interests, and empathize with supervisors, colleagues, and subordinates. The communications must be built to make the dominant group members comfortable.

Recognizing their differences as assets to the company will provide a positive attitude for the minority group members. Focusing on keeping their skill sharpened and improving them constantly will make them valuable for the company. Networking with people, taking risks, being creative, and promoting their past accomplishments are some of the ways to be noticed and be successful. It is equally necessary to learn how to accommodate some of the company requirements without losing the personal identity as a minority. The goals and vision of the minority group members should be complementary to the company's mission for the overall success of the individual.

Diversity Management in the Workplace

Most organizations now see diversity as an asset that offers valuable opportunities for innovation, networking, marketing, and similar benefits. If properly harnessed, the power of diversity will bring the corporation to the forefront by enhancing creativity and efficiency. The focus of diversity management is to promote people as a necessary factor to the organizational success. Although most of the medium to big corporations have a diversity management team, it is the CEO of the company who defines the importance and the effectiveness of that team. The CEO or head of the organization gives clear directions to the director of the diversity team, on which the scope of work is built. The director and members of a diversity management team often have prior experiences working in human resources, training, and social work. A senior-level manager with extensive experiences in the same industry is usually appointed as a director of the team. Additions of team members from the minority and majority groups, as well as cross-level and cross-functional groups, provide effective team-building experiences with a positive image of the diversity committees in the organization.

It is essential to educate the team members about the demographic data, policies, and practices in the organization, while introducing the plans and initiatives of diversity management. Activities in the company can be recorded regularly as a measure to check on the efficiency of the diversity committee. The process of diversity management involves clearly identifying the problem, the elements of diversity involved, traces of conflict, and the diversity tension, which involves stresses and strains associated with the various elements of diversity. The task of this committee is to provide alternatives to the managers in order to resolve the problems when diversity tension increases without any effective outcome. The options available to the managers can be categorized in eight different alternatives according to R. Roosevelt Thomas. The selection of a course of action usually depends on two criteria—the type of diversity mixture at hand and the internal and external factors that include the personal inclinations and mind-set of the manager and the employees, the organizational environment, the intensity, and the impact of diversity tension in the organization. The eight options can be summarized as follows:

1. *Inclusion/exclusion*: The perfect example of inclusion is affirmative actions or Equal Employment options in an organization, where the goal is to increase the number of the target-group members in the organization at all levels. Exclusion is the opposite of inclusion, for example, if a company tries to minimize stockholder participation in decision making. This option is usually legally and/or ethically unacceptable.
2. *Denial:* In many cases by denying that differences exist, the management tries to eliminate the question of change. This option is becoming increasingly difficult since the employees are more than ever wanting to be recognized for their differences.
3. *Assimilation:* For successful organizations, assimilation is the most common approach to all dimensions of diversity. This approach assumes that the minority group will fit in the dominant culture of the organization. However, when more of the employees become comfortable being different, they might not like to follow the requirements set up by the dominant group in the past.
4. *Suppression:* This approach recognizes and acknowledges the differences among the employees, yet discourages its exposure for the welfare of the company. The tradition of sacrificing for the organization used to be very common in the past. The policy of keeping business and personal lives separate and thus suppressing the employee's need to balance work and family is not effective in today's diversified work atmosphere.
5. *Isolation:* The management often finds it practical to isolate different functions in an organization with minimal contact among each other so that each group can operate independently with the fullest efficiency. They create isolated functional entities or "silos" that are best suited to thrive on their own. This option gives the manager opportunity to reduce the complexity by giving personal time to the minority groups without disrupting the order of the dominant groups.
6. *Toleration:* Sometimes diversity is added to an organization due to business reasons, but the new groups are only tolerated, not accepted functionally and/or culturally. This type of coexistence without connecting works well in established bureaucratic environments, where different departments rarely communicate. This option is the middle ground between exclusion and full participation.
7. *Building relationships:* Organizations are taking this approach to resolve problems among diverse groups by collaboration and communication. This option creates harmony among employees, and thus increases productivity. By focusing on similarities, this option is used to minimize the differences.
8. *Fostering mutual adaptation:* Only a few organizations have fully accepted this still-evolving holistic concept of acceptance and understanding of diversity. This option considers the requirements of the organization and the employees and finds the balance between the company mission and fulfilling the individual identity by pushing all the conventional ideas and organizational preferences away. This approach also allows the dominant and the minority groups to work together for necessary changes thus creating synergy. This enables the complexity of diversity to be truly eliminated.

As mentioned earlier, the management needs to make a conscious choice of the option(s) to be considered. It is a dynamic process, which varies according to different situations. None of the options should be considered as bad or good without understanding the contextual issues. They can also be used in different combinations as demanded by the situation. Before choosing an option, one should consider not only the differences but also the similarity of the diversity mixtures. Finally, only one of the above mentioned choices, that is, fostering mutual adaptation, is truly seeking into diversity as a part of the organization, whereas the rest are only partially trying to minimize or avoid the issue at all.

Diversity of Organizational Functions

After its initial success in the industry, an organization enters its growth phase. Then it is likely to divide itself into many different branches based on their functions, so that each division can be managed successfully.

By doing so, it creates the diversity of functions in the same organizations. The different branches of the company may have different work culture, different levels of formalities, and time-oriented goals. Self-containment of different functions is not a problem until they need to work together for the organization to strive for a creative way toward success.

The old business model has levels of managers between the top level and the workforce to relay the information back and forth between top-level management and workers. Technological advances assist companies in directly communicating with team leaders of different divisions to respond faster to the developing issues. The divisional teams increasingly consist of experts and workers with diverse knowledge base and perspective, thus creating an environment of creative thinking resulting in superior product innovation.

The goal of the diversity management team is to find a balance between the interdepartmental communication and the independence of each of the department. The same eight options discussed in the previous section are available to the managers to minimize the complexity of the functional diversities.

Conclusion

The mission of organizations in the 21st century is to create new models for workplaces that motivate and access the potential of each of those diverse workforces, thus striving toward the common goal of the organizational success and personal achievements of the employees. A proactive strategy is necessary for bridging a diverse workforce to the business goals.

The employers as well as the employees are required to be educated through experimental and informational seminars to make necessary attitudes shift in organizations. The multicultural approach benefits an organization in many ways, such as attracting and retaining talented people in the company, gaining and keeping greater market shares, reducing costs and increasing productivity, improving the quality of management, increasing organizational flexibility, solving problems more effectively, and contributing to social responsibility.

Mergers and acquisitions between companies have become commonplace these days, forcing employees of different companies and sometimes even competitors to work together. This imposes a challenge to employees' work ethics and capabilities. In a joint venture, managers have difficulty forming a cohesive group of workers from diverse functions.

With the growth of the minority population, including women in the workforce, managers are facing expectations of a wider range of accommodations from workers to balance their work and family lives. The only way to build an honest and fulfilling relationship between management and employees is by improving communications among them.

Managers in a diverse workplace should recognize their personal ethnocentricities. Learning about different cultures existing in the company will help them recognize their differences. Building trust among diverse groups can be achieved by expressing respect and appreciation of their contributions. It is essential to learn to listen and be open-minded about other points of view. With strong interaction skill, the management and the employees can work together toward common goals.

Over the last decade, many American corporations have expanded their organizations globally. Corporate success, more than ever, depends on managing their diversified workforce properly inside as well as outside the United States. The ever-growing complexity of diversity issues demands dynamic and innovative adaptation and implementation of new strategies to survive and succeed in business today and in the future.

—Mousumi Roy

See also AARP; Adverse Selection; Affirmative Action; Age Discrimination; American Civil Liberties Union (ACLU); Americans with Disabilities Act of 1990; Civil Rights; Employment Discrimination; Empowerment; Equal Employment Opportunity; Equality; Equal Pay Act of 1963; Equal Sacrifice Theory; Fairness; Family-Friendly Corporation; Gay Rights; Gender Inequality and Discrimination; Glass Ceiling; Human Rights; Lesbian Ethics; Minorities; Multiculturalism; Pluralism; Racial Discrimination; Religious Discrimination; Reverse Discrimination; Women in the Workplace; Work and Family

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Divestment

Divestment refers to the disposal of assets in any one of a variety of ways. For example, a new judge can divest herself of stock holdings that might generate a conflict of interest, or an individual investor might divest himself of computer stocks if he thinks they have a poor future. At the institutional level, divestment is a policy and set of economic sanctions used by corporations, groups of shareholders, individuals, and governments to put pressure on a company and/or a country, to protest either the company's or the country's policies and practices. It is a means of leveraging economic power to help bring about political, economic, legal, and/or social change in the target company or country. Divestment is a result of pressure from shareholders, consumers, activists, nongovernmental organizations, and/or government sanctions. Divestment can take several forms, including the withdrawal of new corporate investment, withdrawal of available credit from banks, the selling off of operating units, cutting off all operations, and reducing portfolio holdings in firms doing business in the target country.

There are four reasons for divestment at the institutional level: political, legal, financial, or moral, and these often overlap one another; a company may respond to shareholder and/or consumer pressures and close down its operations in a country with a poor human rights record, doing so for financial and moral reasons. Then the government may pass legislation banning an investment in that country, so the company is now complying with legislation. Because divestment has been used as leverage by corporations to bring political, social, and/or economic change in countries where human rights have been violated, it is considered to be an ethical or moral action by business that can be used to promote human rights. In this way, investment and divestment can be seen as either ethical or unethical, based on moral foundations. In both Burma and South Africa, the democratic opposition coalitions encouraged multinational corporations to return and reinvest only after a democratically elected government was established.

Sanctions, selective purchasing, and disinvestment are additional actions that can be used along with divestment to bring about political, economic, and social reforms in a targeted country. Another strategy, constructive engagement, is the continuation of economic activity between a corporation or government and a targeted country. Often those who oppose divestment support constructive engagement as a viable alternative, maintaining that the ongoing economic relationship will bring about dialogue or pressure for change in the targeted country.

Divestment for Moral Reasons

In the 1970s and 1980s, businesses and governments throughout the world protested the apartheid regime of the white-ruled government in South Africa by divesting. Some examples of multinational corporations that partially or fully divested from South Africa during the 1980s include Eastman Kodak, IBM, CocaCola, General Electric, and Xerox. In 1987, the state of California divested by restructuring its investments so that $90 billion would be divested from companies doing business with South Africa. Divestment has been used to protest the military-ruled government of Burma. During the 1990s, multinational corporations that divested from Burma include PepsiCo, Eastman Kodak, Texaco, Hewlett-Packard, and Federated Department Stores.

In practice, in South Africa and in Burma, while some companies withdrew their direct holdings, they would sell to local companies or third parties, creating licensing or franchising arrangements so that their products or services would still be available. Kodak is an example of a corporation that did this in South Africa, while Sony has done this in Burma.

In 2006, because of continuing genocide in the Darfur region of the Sudan, several states in the United States such as Illinois, Louisiana, Oregon, and New Jersey have passed legislation requiring public pension funds to divest companies operating in Sudan. In addition, institutions of higher education, such as University of California, Harvard, Amherst, Yale, and Stanford, have passed policies divesting their portfolios of investments in companies doing business with Sudan. In spite of this, more than 130 companies continue to do business with Sudan. Most of those companies are based in Europe and Asia, but many are listed in U.S. stock exchanges and have access to U.S. capital markets.

In 2004, the governing body of the Presbyterian Church in the United States, with $8 billion in investments, approved selective divestment from corporations doing business with Israel. It would divest from multinational corporations that sell goods and services used by the Israeli military to maintain the occupation, expand settlements, and otherwise violate the human rights of the Palestinians. Similarly, investors have campaigned against Caterpillar, a U.S. firm that manufactures armored bulldozers used by the Israeli military to level Palestinian homes. Some supporters of Israel are hostile to these divestment activities, interpreting them as anti-Semitic and an attempt to weaken a strong yet vulnerable nation that needs economic and political support throughout the world.

Divestment for Reasons of Public Policy

Because of changes in antitrust public policy, in 1982 AT&T was mandated by the U.S. government to divest itself of its local telephone companies. In addition, several of the examples of divestment for moral reasons are also examples of changes in public policy, as in the example of the United States passing legislation imposing a ban on imports from Burma.

Arguments in Favor of Divestment

Arguments supporting divestment fall into two categories: (1) a positive assumption of rationality or (2) a negative assumption that economic force is the only means for change. Both arguments assume a long time line and the necessity for cooperative effort by the divesting firms and/or governments. The assumption of rationality assumes that the host country will eventually understand that respect for human rights contributes to economic growth. Furthermore, when multinationals divest, they pressure repressive regimes to step down and allow democratic elections, leading to political, economic, and social reforms and to higher economic standards and political and social stability. Not assuming common moral values, Archbishop Desmond Tutu, supporting divestment in Burma, said it was sanctions, not constructive engagement, that brought the end to the apartheid regime in his country of South Africa. He believes that economic might, not moral reasoning, is the only language tyrants understand.

Arguments Against Divestment

Opponents of divestment claim that continuing investment assures employment for the local population and predict that through economic ties the host country is exposed to democratic and free-market processes and will eventually move in that direction. They argue that divestment would jeopardize already tenuous possibilities of democracy. Withdrawing investment leads to shutting down factories, mining, and/or drilling activities, which leads to unemployment. As an example, when the United States banned any new imports from Burma in 2000, reports indicated that 35,000 factory workers lost their jobs. In addition, in the case of Burma, because it is a state-controlled, military-led government, with a state-controlled economy and poor human rights record, and shares a border with China, its largest trading partner, the West fears that any sanctions will force Burma to rely even more on China. The partnership between Burma and China, with its own state-controlled economy and poor human rights record, is seen as threatening to the hope of democracy and capitalism in that region. In contrast, South Africa did not have an economically or politically powerful country as its neighbor, thus posing no particular threat to eventual democratic reforms.

—Judith A. White

See also Corporate Moral Agency; Global Codes of Conduct; Shareholder Activism

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Divine Command Theory

Business leaders, along with society in general, rely on ethical frameworks to guide daily decision-making processes and logically confirm gut feelings. Prominent ethical frameworks such as deontology, utilitarianism, and virtue ethics are popular tools employed in this process. However, various alternative ethical frameworks are also commonly used to determine the morality of contemplated actions. The Divine Command Theory (DCT) is such an alternative ethical framework based on a belief in God and an acceptance that the morality of actions stems directly from God's commands. According to the DCT, an action is morally acceptable if God commanded such action or if a divine command motivates someone to take a morally appropriate action. As commonly formulated, the DCT can be divided into three ethical subframeworks: (1) Religious Communities, (2) Command as Motivation, and (3) Created Morality. All three alternatives are found throughout the Judeo-Christian tradition and certain other theistic religious traditions. The DCT has faced prominent criticisms since its inception beginning with a dilemma posed by Socrates during a heated discussion with an early adherent of the DCT. Over time, many DCT theorists responded to these objections by positing philosophical and religious counterarguments and defending the DCT, whereas others modified the DCT into various iterations addressing such objections while faithfully retaining the core idea that God's commands dictate and/or motivate morality.

Subframeworks of the Divine Command Theory

The Religious Communities Framework

The Religious Communities framework of the DCT posits that God's commands, and only God's commands, define what is morally right and morally wrong. However, this version of the DCT requires that only members of DCT-adhering religious communities are required to interpret and then abide by the commands of God. For instance, certain Christian denominations view the appointment of females in ministry to be contrary to God's commands and, therefore, morally wrong, while other Christian denominations do not interpret God's commands in such a manner and consequently appoint females to ministry positions. Interestingly, many adherents of the Judeo-Christian tradition fall outside of this Religious Communities version of the DCT because they view God's commands as only a partial source of their ethical responsibilities. For example, a Christian might believe that loving a neighbor is morally good even without a corresponding commandment issued by God. This framework acknowledges that the DCT is meaningless to a nonbeliever as one cannot be forced to abide by God's commands without a corresponding belief in a supreme deity. Finally, the Religious Communities framework accepts the idea that groups outside the religious community define morality independent of God's commands and that these interpretations of morality might significantly differ from the interpretations of the religious community.

The Command as Motivation Framework

The Command as Motivation framework of the DCT claims that certain actions are moral independent of any divine command but that God's commands provide people with the necessary and proper motivation to act morally. Therefore, like the Religious Communities framework, the Command as Motivation framework only applies to individuals who sincerely believe in God and are, therefore, motivated to follow God's commands. For example, honesty is a practice explicitly commanded by God in the Judeo-Christian tradition. Assume that an atheist is presented with an opportunity to lie and chooses instead to act honestly. In this instance, the atheist's decision to act honestly is a moral decision—because honesty is moral independent of God's commands—but the honest action in this instance is viewed as coincidence because the atheist will not have the divine motivation required to consistently act honestly. This version of the DCT places God as the motivating force behind ethical actions but relinquishes the idea that moral actions depend on God's will.

The Created Morality Framework

The Created Morality framework of the DCT states that God's will, expressed through God's commands, is the exclusive determinant of morality and that no action can be considered moral if performed without regard to God's commands. In other words, a person must believe that an action is moral because God wills such action to be moral—not because the action is good in and of itself—and then must take action (or refrain from taking action) solely because God has commanded (forbidden) such action. For example, if an atheist refrains from committing adultery based on a deontological belief in a duty to be a faithful spouse and not because God has commanded people to refrain from committing adultery, the atheist has acted unethically under the Created Morality framework. This is true even though the atheist abided by God's command and refrained from committing adultery because the atheist operated under a belief that refraining from adultery was moral without regard to God's commands. Although all three subframeworks of the DCT require that certain people comply with God's commands, only the Created Morality version of the DCT claims that God defines morality for everyone in all circumstances.

Objections to the Divine Command Theory

The most prominent objections to the DCT stem from a Socratic dialogue commonly referred to as the "Euthyphro Dilemma." The dialogue began when Socrates entered into a friendly discussion with an early Athenian adherent of the DCT. The two men were discussing the Athenian gods and the virtue of piety. Euthyphro—the other participant in the discussion—argued that piety was a virtue loved by the gods when Socrates posed the question as to whether the gods love piety because piety is good or whether piety is good because the gods love piety. Over time, this two-part question has been modified—removing the plurality of Athenian gods and replacing them with a singular God and also replacing the virtue of piety with the more generally concept of moral goodness—to form the modern version of the Euthyphro Dilemma. The modern version asks the following question to an adherent of the DCT: Is an action morally good because God commands such action or is the action morally good in and of itself and this goodness constitutes the reason why God commands such action? An affirmative response that an action is good because God commands it can be met with two objections—the Abhorrence Objection and the Emptiness Objection. An affirmative response that an action is good and, because the action is good, God commands such action can be met with the Irrelevance Objection.

The Abhorrence Objection

If an action is good only because God commands such action, then what would happen if God chose to issue an abhorrent command? This criticism can be referred to as the Abhorrence Objection. What if, instead of God commanding that a person love a neighbor, God issued a command that a person must be cruel to a neighbor? Under the DCT, an adherent would now be required to be cruel to a neighbor in order to act in a morally acceptable manner. This type of action contradicts the believer's expectations of God and God's nature, yet strict adherence to the DCT would seemingly require such abhorrent action simply because God commanded it.

The Emptiness Objection

In addition, if any particular action is good only because God commands it, then God serves as the ultimate arbiter of what is morally right and what is morally wrong. An issue then arises as to whether the sentence "God is good" has any meaning in a world where God determines what is good. This criticism can be referred to as the Emptiness Objection. For example, DCT proponents state that "God is good," while the DCT itself claims that "Good is whatever God commands." The Emptiness Objection transposes these statements and claims that saying "God is good" is the same as saying "God is whatever God commands." The argument is then made that this statement is empty, trivial, or entirely without meaning. Because adherents of the DCT strongly believe that the concepts "God is good" and "Good is whatever God commands" have meaning, then any suggestion that these belief statements are meaningless tautologies undermines a core principle of the DCT.

The Irrelevance Objection

Alternatively, a response that an action is good and this goodness is the reason God commands such action is met with the Irrelevance Objection. This objection states that if an action can be considered good regardless of God's commands then God's commands cannot be the source of all moral goodness. This places a stumbling block in front of the DCT argument that all moral correctness and moral wrongness stem solely from God's commands. For instance, if loving one's neighbor is good in and of itself and this goodness is why God commands people to love their neighbors, then God's specific command becomes irrelevant to moral goodness—the action of loving a neighbor is already good.

Responses to the Euthyphro Dilemma

Many philosophers and religious adherents over many centuries have attempted to counter the objections presented by the Euthyphro Dilemma. These defenders of the DCT argue that the logical flow of Socrates' argument is flawed and that a believer in the DCT is not limited in choosing either the first or the second prong of the Euthyphro Dilemma. DCT adherents also attempt to specifically counter each of the three objections presented by the Euthyphro Dilemma.

Some defenders of the DCT counter the Abhorrence Objection by claiming that God is a loving God and would never issue abhorrent commands. This counterargument makes the Abhorrence Objection meaningless because there is no possibility that God would issue abhorrent commands. Other DCT proponents argue that God's nature prevents God from issuing abhorrent commands. This specific counterargument makes the Abhorrence Objection irrelevant because God is restrained from issuing abhorrent commands.

The Emptiness Objection can be countered by the idea that it is not an empty statement to claim that "God is what God commands." This counterargument states that because God is omnipotent and has the power to act differently than specific commandments, it is significant that God chooses to act in accordance with such commandments. Therefore, the statement that God is what God commands is not a meaningless tautology and, indeed, shows that God has made a choice to comply with specific commandments.

The Irrelevance Objection can be countered with the idea that God cannot be considered irrelevant even if good is determined to exist independent of God's specific commands. The counterargument is as follows: If God, before issuing any commands, defined what good is and then, at a later time, commanded that people act in accordance with what is already good, this process makes God relevant and not irrelevant. Without God, good would not exist in the first place.

A Modified Divine Command Theory Framework

The philosopher Robert Adams, unsatisfied with responses to the Euthyphro Dilemma objections—particularly the response to the Abhorrence Objection—created a new iteration of the DCT. This new version modified the idea that moral wrongness stems from violating the commands of God with the idea that moral wrongness stems from violating the commands of *a loving* God. This modified DCT renders the Abhorrence Objection meaningless because a loving God would never issue abhorrent commands. This theory is further supported by the fact that a loving God is the theistic model prominent in the Judeo-Christian tradition and, therefore, such a nature of God makes logical sense to believers.

A major criticism of this modified theory relates to the believer's concept of the supremacy of God and the corresponding requirement to obey God in accordance with this supremacy. For instance, when a person believes that an apparently abhorrent command would not come from a loving God, that person is allowed to freely disregard the command. This decision would be considered ethical under the modified theory even though the actor is purposefully disobeying the commands of the supreme authority.

The Divine Command Theory Today

The DCT is as old as God's first commandment. The theory has gone through various iterations culminating in three commonly known subframeworks. Today, the DCT is viewed as a substantive ethical framework whose merits and flaws continue to be debated in the public square with input coming from various arenas—including philosophy, religion, and even the business community. These debates continue to focus on the objections created by the Euthyphro Dilemma, and the DCT continues to be modified into new versions with the continuity of a consistent focus on God's commands as defining or at least motivating appropriate moral conduct.

—Corey A. Ciocchetti

See also Ethical Decision Making; Ethics, Theories of; Golden Rule, The; Islamic Ethics; Jewish Ethics

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Doctrine of Double Effect

The Doctrine of Double Effect is an ethical principle that is used to explain how certain actions that would cause considerable harm can be morally permissible where the bringing about of such harm is a side effect of the promotion of some good end. This principle is usually invoked by ethicists who subscribe to a deontological, or rule-based, approach to ethics, especially those who subscribe to the Judeo-Christian ethical tradition. (Indeed, Thomas Aquinas is credited with developing the first formulation of this Doctrine in his discussion of self-defense in the *Summa Theologica.*) Such ethicists are unwilling to hold that the good that could be brought about by the infliction of such harm would itself justify the bringing about of the harm, as would, for example, a utilitarian ethicist.

According to the proponents of the Doctrine of Double Effect, four conditions must be met in order for it to be justly invoked to explain the moral permissibility of an act whose performance would cause harm as a side effect. First, the act itself must be morally good or at least morally neutral. Second, the agent performing the act must not intend the bad effect, but must merely foresee that it would occur as a result of his action. Third, the good effect that is intended must be produced directly by the act that the agent performs; it cannot be produced through the bad effect. That is, the bad effect cannot be used as a means to secure the good effect; it can only flow from the agent's act as a corollary effect of it. Finally, the good effect must be proportionate to the bad effect.

To illustrate this, consider an example where a developer builds a housing project, knowing that to do so will have the side effect of causing environmental damage as a result of the increase in fuel emissions from the increased use of cars in the vicinity. According to the proponents of the Doctrine of Double Effect, the developer is permitted to build the housing project, even if his doing so will lead to environmental damage, provided that he only intends to build the houses and merely foresees such damage occurring. The building of houses is itself a morally neutral act, the bad effect is foreseen but not intended, the good effect is not produced through the building of the houses; this is merely a corollary to the developer's act, and the badness of the environmental damage is outweighed by the goodness of providing housing.

The Doctrine of Double Effect is, however, subject to the criticism that there is no more than a semantic distinction between what is foreseen and what is intended in the cases where the Doctrine is invoked. Thus, when the developer above builds his houses he must intend to do, and not just foresee, environmental damage, since the two effects are inherently linked. As such, it is argued, the core distinction of the Doctrine is untenable.

—James Stacey Taylor

See also Deontological Ethical Systems; Utilitarianism

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Doha Development Round of 2001

The Doha Development Round of 2001 was a forum created by the World Trade Organization (WTO)—the international institution responsible for overseeing the world trading system and policy—to negotiate and discuss issues related to global trade. It was named after the city in which the conference took place. Ministers from 144 WTO member countries gathered in Doha to reach consensus on how to integrate the world's poorest nations into the world economy in November of 2001.

Arranged by the WTO, the declaration of the Fourth Ministerial Conference in Doha, Qatar, was the eighth round of trade liberalization held since 1948. Following the Uruguay Round of 1986–1994, which created the WTO as the successor to the General Agreement on Tariffs and Trade, the Doha Round was held to bring to the forefront the needs and special interests of developing countries to the WTO's agenda. The Doha conference marked the start of a new series of multilateral trade talks scheduled to end in 2004.

The agenda set at Doha and discussed at successive meetings in Cancun in 2003 focused on dismantling trade barriers for developing nations to promote growth. Toward this end, the main issues centered on agricultural subsidies, liberalizing trade of manufactured goods and services, and intellectual property rights protection.

Related to agriculture, the declaration defined the objective of establishing a fair global market-oriented trading system that would allow market access to all developing nations. The intent was to reduce and eventually eliminate all forms of export subsidies for these countries and to significantly reduce any domestic trade support within nations. The discussion on the reduction of export subsidies also covered industrial goods. Tariff reduction and all nontariff barriers on clothing, textiles, and other nonagricultural products were also agreed by the ministers for the least-developed countries. However, none of this was to be at the expense of the environment. The Ministerial Declaration included a commitment to environmental sustainable development in all member countries by defining, in part, the relationship between WTO trade rules and environmental agreements.

One of the more pressing issues negotiated at Doha involved trade-related aspects of intellectual property rights (TRIPS). The stated goal of the declaration was to allow access to existing medicines and to encourage the development of new pharmaceutical drugs to improve public health in developing nations. These countries lobbied for relaxed rules on pharmaceutical inventions from developed nations. Building on talks held at the Uruguay Round, Third World nations demanded greater access to essential medicine to deal with epidemics such as AIDS. This accessibility involved offering lower-priced generic drugs to countries unable to solve public health crises. Demonstrating the grand importance placed on this issue, the ministers at Doha created a separate declaration on TRIPS. Member governments of the WTO are not to be prevented from taking measures to protect their country's right to public health under the TRIPS Agreement. The council set out to discover solutions for compulsory licensing of medicines and agreed to extend the deadline for underdeveloped nations to establish provisions on drug patents until January 2016.

The WTO expanded its membership at Doha to include China and the Taiwan Province of China. This accession reinforced the WTO's goal of facilitating the addition of other less-developed nations. Related to WTO membership, the Doha meeting emphasized the importance of transparency of operations and information and nondiscrimination of negotiated agreements for all members. Special provisions were established for developing countries to receive special and differential treatment to implement the agreements resulting from the round. The desired long-term implications of the discussions were to bring about the benefits of free trade and the opening of markets to developing countries. This has yet to be determined.

—David M. Wasieleski

See also Agriculture, Ethics of; AIDS, Social and Ethical Implications for Business; Free Trade, Free Trade Agreements, Free Trade Zones; Property and Property Rights; World Trade Organization (WTO)

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Domini Social Investments

After her clients expressed concern about investing in defense contractors, tobacco firms, and other types of companies, stockbroker Amy Domini realized the opportunity and importance of screening firms for environmental, social, and ethical concerns. It was the early 1980s and, at the time, there was only a small group of professionals and investors dedicated to this area. In 1984, Domini coauthored *Ethical Investing*, one of the first books to summarize and popularize the strategies for linking values and beliefs with investment portfolios. More than two decades later, Domini's name is synonymous with socially responsible investing. *Time* magazine named Domini one of 2005's 100 most influential people.

In 1989, Domini, Peter Kinder, and Steve Lydenberg launched the Domini 400 Social Index, a market capitalization–weighted common stock index. The Domini 400 index serves as a benchmark for examining the performance of firms that pass broad social screens on diversity, the natural environment, employee relations, and product safety. Companies included in the index are, on the whole, relatively strong in these areas. Firms that generate more than 2% of sales from military weaponry, receive any revenue from alcohol or tobacco products, use nuclear energy, or engage in gaming activities are ineligible for the index. Since its inception, the Domini 400 Social Index has provided evidence that social and environmental screens do not limit financial performance.

After launching the index, Domini and her colleagues introduced the Domini Social Equity Fund to track the index. The fund uses a full replication strategy, which means it invests in the 400 public companies found in the index. Investors in the fund can expect a return just short of the index's performance, since operating expenses must be covered for the fund. In addition to social screens, the fund also advances its social and environmental goals through a variety of strategies. Domini strives to create an open dialogue with top executives and other stakeholders in order to advance its goals and create corporate change. When dialogue stalls or management is unresponsive, fund representatives will often file shareholder resolutions, usually in conjunction with other social investment groups. Domini has filed nearly 100 shareholder resolutions on a variety of issues, including recycling, human rights, sweatshop labor, diversity, global warming, and sustainability reporting. Domini considers these resolutions a success when they are withdrawn because the company has agreed to pursue some or part of the request. Domini was also the first fund to disclose its proxy voting guidelines and actions to investors.

In addition to the index and fund, Domini has introduced the Domini Social Bond Fund and the Domini Money Market Account. These products support community economic development loans and initiatives. Domini is also affiliated with KLD Research & Analytics, Inc., a firm that specializes in corporate accountability research. In all its activities, Domini focuses on the three pillars of social investing, including (1) social and environmental screening, (2) shareholder advocacy, and (3) community investing.

—Debbie M. Thorne

See also Shareholder Activism; Socially Responsible Investing (SRI)

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Double Taxation

Double taxation refers to situations in which the same financial assets or earnings are subject to taxation at two different levels. For instance, one form of double taxation occurs when income from foreign investments is taxed both by the country in which it is earned and by the country in which the investor resides. To prevent this type of double taxation, many double taxation treaties currently exist between countries that allow income recipients to offset the tax already paid on investment income in another country against their tax liability in their country of residence.

Another example of double taxation can occur with regard to the taxation of corporate earnings. This happens when corporate earnings are taxed at both the corporate level and again at the level of shareholder dividends. That is, the earnings of a corporation are first taxed as corporate income and then, when that income has been distributed to the shareholders of the corporation in the form of dividends, these earnings are taxed as the personal income of the shareholders. Since the shareholders are the owners of the corporation, they are effectively paying taxes twice on the same income, once as the owners and again as part of their personal income tax. In the United States, this type of taxation is widespread, because the tax on corporate profits and the personal dividend income tax are federal, and thus universal, taxes. Many states have personal income taxes that include the taxation of dividends as well.

This latter form of double taxation is particularly contentious and has been the subject of much debate, particularly in the United States where recent efforts to reduce or eliminate this form of double taxation have been widely disputed. Opponents of double taxation on corporate earnings contend that the practice is both unfair and inefficient. They claim that the practice is inherently unfair in treating this type of corporate income differently than other forms of income in subjecting it to taxation twice. Opponents also claim that the practice engenders economic inefficiency since it encourages companies to finance themselves with debt, which is tax deductible, and to retain profits rather than pass them on to investors. Opponents also argue that the elimination of dividend taxes would stimulate the economy by encouraging individual investment in corporations.

On the other hand, proponents argue that the economic effects of reducing or eliminating double taxation of this form are overstated and that such cuts would only benefit the wealthiest persons, whose earnings are substantially constituted by dividend income. Here, for example, proponents argue that eliminating dividend taxation could actually stifle capital reinvestment and thus discourage economic growth. Some proponents also question whether the taxation of dividends truly constitutes a form of double taxation. In this regard, they argue that there is a legal and conceptual distinction between a corporation and its shareholders because the former, as a unique legal entity, has rights, privileges, and obligations that are distinct from those of the latter. As such, they argue that there is nothing unfair in taxing the income of the corporation distinctly from the personal income of its shareholders.

—Daniel E. Palmer

See also Corporate Rights and Personhood; Fairness; Tax Ethics

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Dow Corning

Dow Corning Corp. was established in 1943 as the joint venture between Dow Chemical and Corning Glass to produce silicones for commercial purposes. Later, Dow Corning gained notoriety for its manufacture of the controversial silicone breast implants. In 1992, after thousands of lawsuits and several multimillion dollar jury awards, Dow Corning discontinued the manufacture of its silicone implants and filed bankruptcy in 1995. A Mayo Clinic study published in the *New England Journal of Medicine* in June of 1994 showed that there was no difference between women with silicone implants and those without with respect to the incidence of connective-tissue disease. Twenty other large-scale clinical studies have also shown no correlation between silicone and any other disease. This case highlights several social issues: corporate responsibility for the safety of their products, scientific studies versus public opinion, and patient safety versus patient choice.

Dow Corning silicone breast implants were first made available to plastic surgeons in 1964 along with silicone chin and testicular prostheses. Since that time numerous companies both domestic and international have manufactured implants. It is estimated that over 1 million American women now have silicone breast implants.

In the 1960s, the implants were not subject to any government regulations. In 1976, Congress gave the U.S. Food and Drug Administration (FDA) authority to regulate all medical devices. Because implants had been on the market for 15 years, they were "grandfathered" in and classified as "Class II" devices, meaning that they did not need testing to remain on the market.

In the 1980s, women with silicone implants reported certain patterns of illness, including severe joint and muscle pain, fatigue, and weight loss. It was alleged that leaky silicone bags were responsible for various autoimmune disorders such as rheumatoid arthritis, lupus erythematosus, and scleroderma, the latter being a disease in which the body's immune system attacks its own connective tissue. Because of these concerns, the FDA reclassified silicone implants as "Class III" in 1986. Thereafter, all manufacturers of the silicone implants were ordered to file Premarket Approval Applications (PMAAs), backed by valid scientific data to prove the safety and effectiveness of their devices. The PMAAs were due by 1991 at which time the FDA would have 180 days to review the data and rule. The FDA's advisory panel composed of experts from various fields, including plastic surgery, oncology, epidemiology, internal medicine, immunology, radiology, pathology, toxicology, as well as industry and consumer groups, complained of a lack of hard scientific data. The symptoms the women who brought lawsuits complained of were not uncommon in the general population. For example, connective-tissue disease strikes 1% of all women. The percentage of women who suffer from connective-tissue disease with implants is statistically indistinguishable from the population at large and thus impossible to distinguish coincidence from causation. Furthermore, not only does silicone appear to be chemically inert, but silicone from a ruptured implant will remain trapped inside a fibrous capsule of scar tissue. After studying the data submitted by the various manufacturers the panel ruled that the manufacturers had failed to prove that their devices were safe; neither was there evidence that they were harmful. The FDA could not vouch for the safety of implants without more clinical research. The panel advised the implants to be made available to women on a limited basis.

In 1991, an Alabama jury heard the case of *Toole v. Baxter* and awarded Brenda Toole, who showed only preliminary symptoms of autoimmune problems, $5.4 million. In the same year, Dow Corning was found guilty of negligence in a case brought by Mariann Hopkins and ordered to pay $7.3 million. After the Hopkins case, the new chairman of the FDA, David A. Kessler, called for a moratorium on breast implants, but advised women who had implants not to have them removed. The moratorium terrified women who had received implants and galvanized legal forces against manufacturers of silicone bags. Meanwhile, nine medical and cancer survivor groups petitioned the FDA to make breast implants accessible to women after breast cancer surgery. In April of 1992, silicone implants were made available only to women who agreed to participate in clinical studies.

In March 1994, the largest ever class action settlement was finalized with manufacturers Dow Corning, Baxter, Bristol-Myers Squibb/MEC, and 3M. The manufacturers claimed that there was no scientific evidence linking silicone breast implants with autoimmune diseases. Nonetheless, set monetary amounts were awarded to women with specific medical conditions with no requirements to prove that implants caused their ailments.

In 1994 and 1995, several new studies were published in the *New England Journal of Medicine*. They included the Mayo Clinic and the Harvard Nurses epidemiologic studies, both of which showed no increased risk of connective-tissue disease in women with implants. The American College of Rheumatology issued a statement saying the evidence was compelling that implants did not cause systemic disease. The *Journal of the National Cancer Institute* published a review of scores of medical studies in September 1997 that concluded breast implants do not cause breast cancer. Reports from two large Scandinavian studies published in April 1998 also concluded that silicone implants are not linked to neurological disease.

Facing 20,000 lawsuits and approximately 410,000 potential claims that had been filed in the global settlement, Dow Corning filed for Chapter 11 bankruptcy in May of 1995. The bankruptcy essentially halted all litigation against Dow Corning.

In June of 1999, Dow Corning filed for bankruptcy reorganization that included a $3.2 billion settlement with women who said their implants had made them ill. Dow Corning emerged from bankruptcy protection on June 1, 2004, after a group of Nevada women dropped their opposition to a settlement plan. The reorganization efforts under Chapter 11 took longer than any in history, lasting 3,305 days. Dow Corning continues to be a major supplier of silicone for everything from cleaners and adhesives to automobiles and buildings.

On November 17, 2006, the FDA ended the 14-year ban and approved silicone implants. Dow Corning does not plan to manufacture the implants.

—Lori S. Kolb

See also Bankruptcy, Ethical Issues in; Corporate Accountability; Corporate Ethics and Compliance Programs

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Downsizing

Downsizing is a reduction in a company's employees and positions undertaken as an intentional, proactive management strategy to improve the company's performance. Companies such as Cisco, Dell, Aetna, AT&T, General Motors, and many others have at various times implemented large-scale downsizing programs. Downsizing differs from terminations for cause, in which employees are released in response to issues with their behavior or performance, and from attrition, in which electing to not fill positions as they are vacated reduces staffing levels. Downsizing is also different from situations in which a company is forced to lay off all employees because it ceases operations, by choice of owners or by bankruptcy. During a downsizing, employees whose performance may be satisfactory or even above average are terminated through no fault of their own.

Intended reductions of employees have become common practices in both the U.S. corporate and public sectors. During the 1990s, downsizing became a favorite strategy of many companies in response to fundamental structural changes in the world's economy. The term *rightsizing* is commonly used to describe downsizing that companies believe to be a proactive approach to dealing with overstaffing. Between 1979 and 1999, approximately 43 million jobs were downsized in the United States. Companies have settled into a routine of reducing and rebuilding large segments of their workforce in a continuous restructuring process. Many companies may now feel pressured to downsize because they want to be perceived as operating "lean and mean."

In general, companies adopt a downsizing strategy to achieve one of three goals—to save, to improve, or to change the company. Downsizing to save the company may be undertaken when a financial crisis requires the company to reduce labor costs as a last resort before bankruptcy. Downsizing to improve the company may be undertaken as a preventive measure to reduce labor costs to fend off a looming financial crisis.

Reducing staff is usually the fastest way to affect the bottom line because of accounting rules that allow all costs associated with downsizing to be expensed in one quarter, a tactic that is usually viewed favorably by financial analysts. Downsizing can also cause considerable stress and heartache for the individuals affected as well as those in management who must develop and/or implement the downsizing plan.

Downsizing to change the company may be undertaken through strategic staffing reductions, perhaps as part of a merger or acquisition, or in response to a decision to outsource a function. Many companies believe downsizing to facilitate organizational change will have a positive impact on their long-term viability; however, researchers have been unable to find consistent evidence that downsizing is positively correlated with future financial performance. Adopting a downsizing strategy is more ethically murky, therefore, when the company is performing well and is in no imminent financial danger.

The stock market generally reacts favorably to a decision to downsize, with a company's stock price rising in response to the announcement. Over time, however, companies that downsize to improve performance often do not attain the desired results because of the emotional impact on the survivors, increases in uncertainty, and changes in individual work responsibilities for which employees are ill prepared. In addition, when companies elect to downsize to save or improve the business, it may be unclear as to whether this is the best option for the company or just the most expedient.

The pressures associated with downsizing can only be justified if it does in fact improve the company's performance; however, there is contradictory evidence as to the actual benefits. There are several ethical theories that may be applied to assess the morality of a downsizing strategy. Utilitarian theory contends that a decision is moral if it results in the greater good for the greatest number of people. This is the most commonly used justification for downsizing to save or improve the company, that is, laying off 1,000 employees will save the company from bankruptcy and thus save the jobs of 20,000 employees.

Kantianism and rights theories contend that individuals have rights that preclude treating them as a means to the ends of other people. As such, the organization has a duty to act in a way that doesn't violate individual rights. These theories may not necessarily dictate that companies desist from conducting layoffs under any circumstances. They can, however, influence how companies implement layoffs in terms of notifications, and providing severance packages and outplacement services.

Social contract theory suggests that people expect companies to be good corporate citizens in keeping with the values and mores of the community. The degree to which downsizing is considered acceptable may depend on what the community finds acceptable. The terms of the social contract may also be defined by the norms of the industry; if downsizing is widely accepted in an industry, it is more likely that a company in the industry will adopt a downsizing strategy.

Justice theory suggests that downsizing may be perceived as fair if the layoffs are evenly distributed throughout the organizational hierarchy, adequate notice is given, the downsized employees are given fair compensation, and impartial procedures are used to determine who is downsized. Perceptions of fairness are also enhanced if employees believe that external forces are driving the downsizing decision and the downsizing is for the overall good of the organization.

The manner in which the reduction plan is designed, implemented, and communicated is, therefore, critical to mitigate negative repercussions from downsizing. Many companies prefer to move quickly when downsizing, but investing time in planning and consideration of all the implications can greatly enhance the outcomes. In determining the appropriate mix and level of staff to meet its strategic goals, companies must also consider fairness issues related to Title VII, that is, age, race, sex, and so on, as well as the terms of labor agreements if applicable.

Companies can minimize the backlash from employees and the public by providing emotional and financial support to the employees affected. Providing advance notice of the pending layoffs, outplacement counseling, extended benefits, and severance pay will benefit the employees who are being terminated and may also help alleviate the "survivor's guilt" of the employees who are retained. Frequent, consistent, and honest communication to employees throughout the downsizing process is also critical to minimize the effect on employee morale and performance during the downsizing and in its aftermath.

—Carmen M. Alston

See also Dilemmas, Ethical; Egoism; Employee Rights Movement; Ethics, Theories of; Integrative Social Contract Theory (ISCT); Justice, Theories of; Kantian Ethics; Rights, Theories of; Social Contract Theory; Utilitarianism

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Due Care Theory

A consumer expects, as a matter of course, that a product purchased is as safe as possible. In recent years, the issue of product safety and the question of the locus of responsibility for unsafe products has been an important topic in business ethics. One approach to product liability is that of "due care."

The "due care" approach is based on the assumption that in commercial transactions, the consumer and manufacturer do not meet as equals in the relationship. The manufacturer, and to a lesser degree the retailer, has greater knowledge and expertise. This leads to assigning the duty to deliver a product that lives up to the expressed and limited claims made about the product to these individuals. The manufacturer is held to the duty of "due care" even if an explicit disclaimer of responsibility is made. The manufacturer in virtue of having greater expertise has a positive moral duty to take whatever steps necessary to ensure the safety of a product. The manufacturer is obligated to take all reasonable precautions to ensure that products are free of defects that could potentially cause harm to the consumer. Every individual has a moral duty to refrain from any action that could harm another, and conversely, every individual has a right to expect such treatment from others. Failure to take "due care" is a breach of moral duty and violates the rights of the consumer who may be injured. The right of the consumer to have a safe product rests on the need of the consumer to rely on the expertise of the manufacturer.

Legal Context

The legal expression of the "due care" theory is expressed in the law of torts, which holds persons liable for acts of negligence. The definition is contained in the Second Restatement of Torts, Section 2820, as a conduct that does not meet the established legal standard for the protection of others against unreasonable risk of harm. Product liability falls under the law of torts, which governs private transactions in which there is no written contract. Under tort law, a person has a claim against another if one has been harmed due to an act or omission that constitutes a breach of duty. Tort law has three purposes. First, it is designed to compensate the injured party, and second, it intends to provide incentives to manufacturers to take precautions in the production of goods and services. The third purpose of tort law is to punish offenders. The standard of care is the "reasonable person" standard expressed as what care a reasonable person would exercise in a given situation. The standard is obviously higher for those persons possessing greater skill or knowledge. In this case, the manufacturer can be assumed to have greater knowledge about the product and its use than the consumer. Therefore, the manufacturer can be held legally liable for harm caused by the product.

The standard applies to all areas of product development and production. In design, the product ought to be in accordance with government and industry standards. It must be designed to be safe under all foreseeable conditions, including possible misuse by the consumer. To ensure design integrity, many manufacturers have established review boards to evaluate the product for safety. There are also external firms such as the Underwriters Laboratory that reviews electrical products for safety and quality.

Another area covered by the standard is the choice and use of materials. These materials must meet government and industry standards and have the necessary strength to withstand normal and reasonable use by the consumer. The manufacturer is obligated to test the product adequately to be able to guarantee durability in ordinary use. Due care must be exercised in the production process as well. Parts must be fabricated to stated specifications, assembly ought to be carefully done, and adequate inspections conducted. It is critical that employers provide employees with the training and working conditions needed to perform their work satisfactorily. Quality control must be a central concern. The manufacturer must conduct systematic and thorough inspections of design, materials, and the production process. These inspections may be done by either trained personnel or specially designed and calibrated machines. In certain situations, every individual product is inspected, while in other situations only sampling is done. The manufacturer is obligated to maintain accurate records of inspections. Care must also be exercised in the packaging and labeling of a product to ensure that the product is not damaged in transit and that sufficient directions are included so that the consumer has clear directions on the use of the product and is warned of any dangers that may be associated with use or misuse. The manufacturer is obligated to warn the consumer of any hazards that are discovered later. For example, automobile manufacturers issue recalls when safety and mechanical defects are discovered after the model has been in use for a period of time.

The U.S. Court of Appeals has held that the manufacturer's obligation to ensure product safety to use as intended or anticipated under all conditions under which injury could occur extends to foreseeable misuse by the consumer. In *Larsen v. General Motors Corp.*, due care included a duty to design the product so that it would meet any emergency use that could reasonably be anticipated. Generally, the courts have held to a flexible standard derived from Justice Hand's formulation of the negligence rule, such as in *United States v. Carroll Towing Co*. This formulation states that negligence involves the probability of harm, the severity of the potential harm, and the burden of protecting against harm. Manufacturers have a greater obligation to protect consumers when injury is more likely to occur; when harm is likely to be greater and when the cost of avoiding injury is relatively minor—the case of the Ford Pinto.

Due care is difficult to apply legally because the fact that a product is defective is not, in itself, sufficient for holding that the manufacturer has failed to exercise due care. For negligence to be proven, one must have knowledge of specific acts that the manufacturer either performed or failed to perform that lead to injury.

Ethical Justification of Due Care

Morally due care rests on the principle that agents have a moral obligation not to harm or injure others by their acts. This obligation is particularly stringent when those who might be harmed are vulnerable and dependent on the judgment and actions of the agent. Various moral perspectives support due care.

The Aristotelian principle of compensatory justice holds that an agent who harms another owes the injured person compensation. Compensatory justice traditionally possesses three characteristics. First, the action that causes the injury must involve wrong or negligent behavior on the part of the agent. Second, the action taken by the agent must be the real cause of the harm or injury, and finally, the injury must have been voluntarily inflicted. The manufacturer who fails to exercise due care is responsible for compensating injured parties. An "ethics of care" approach can also justify due care theory by holding that the well-being of those with whom one has a special relationship, particularly one of dependence, imposes the requirement that one ensure that one's care for the dependent person meets that person's needs and qualities.

Utilitarianism holds that the morality of actions is determined by the consequences of that action. An action is right if it leads to the best possible balance of good over bad consequences, thereby maximizing benefits and minimizing harm for as great a number of people as possible. Rule Utilitarianism, a form of utilitarianism, holds that actions can be justified by an appeal to abstract moral rules. These rules can be justified by an appeal to the principle of utility. These moral rules are not subject to change in light of specific circumstances. Utilitarian rules are, then, firm and protective of individuals. Rule Utilitarianism defends the principle of due care on the grounds that if the rule is accepted, everyone's welfare will be advanced.

Due care can also be justified using a Kantian approach, which argues that persons ought to be treated as ends and never exclusively as means to other ends. One is obligated to respect others as autonomous agents. Respect for human life is a necessary, not optional, component of the obligation that manufacturers have with respect to product safety. The motives for human action are central to a Kantian analysis because this theory expects persons to make correct decisions for the right reasons. A manufacturer must do the right thing, not because it is profitable or to avoid bad publicity but because the action is the right thing to do.

The application of the principles of due care presents difficulties because there is no clear method for determining when due care has been adequately exercised. There is no tried and true way to determine how far a producer must go to ensure that due care has been taken. No product is intrinsically risk free. If one was to apply a utilitarian analysis, one could hold that the greater the probability of harm, the more a corporation is required to do with respect to ensuring the safety of the product, but even here it is difficult to evaluate the balance between higher risks in relation to higher costs. Due care assumes that risks can be identified before the product hits the market. This is not necessarily a valid assumption because many defects take an extended period of use of the product to emerge. Some argue that the due care approach is an overly paternalistic one that places too much responsibility on the manufacturer and too little responsibility on the consumer who uses the product.

—Marilynn P. Fleckenstein

See also Accountability; Consumer Protection Legislation; Justice, Compensatory; Kantian Ethics; Liability Theory; Negligence; Paternalism; Product Liability; Utilitarianism; Utility, Principle of

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Due Diligence

Due diligence is a standard of vigilance, attentiveness, and care that is often exercised in various professional and societal settings. The effort is measured by the circumstances under which it is applied, with the expectation that it will be conducted with a level of reasonableness and prudence appropriate for the particular circumstances. Due diligence is generally expected in any interaction when one party owes a duty of care to the other party, although it is most often associated with professionals and businesses. For example, a patient expects his or her doctor to exercise due diligence when prescribing medications to ensure there are no allergic reactions or harmful interactions with other medications the patient may be taking. Professionals such as lawyers, psychologists, and consultants must also exercise due diligence by protecting the privacy of their clients and guaranteeing confidentiality with regard to sensitive personal information that should not be shared with others. Expectations of due diligence can also evolve with changing social norms. For instance, organizations are now expected to be greater advocates for their stakeholders through various responsible business activities that improve both economic and social well-being. Politicians are also expected to acknowledge and address emerging and sometimes controversial social issues that interest certain groups within the general public. In addition, accounting professionals are incorporating due diligence services for their clients, and services include reviewing benefits plans for funding sufficiency and compliance with regulatory requirements, checking an entity's accounting systems and internal controls, and assessing the potential costs savings in combining the operations of a target entity with those of a client enterprise.

Due diligence is also essential in commercial real estate. Potential investors in commercial real estate recognize that they must look beyond the traditional priority of location and verify factors such as compliance with zoning laws, the structural soundness of buildings, and most important, compliance with environmental laws. The new owner of commercial property can be potentially liable for millions of dollars of remediation costs and fines as a result of a prior owner's violations.

Due diligence is often considered an ethical issue in business because without such reasonableness and prudence there is an opportunity for management to misrepresent information to key stakeholders. Furthermore, managers might ignore questionable behavior in a company or not take appropriate action to prevent workplace misconduct. Proper due diligence should therefore be viewed as a responsible business practice, and the practice should be included in the strategic planning of an organization.

The process of due diligence is most commonly applied to business transactions, often in the context of the sale of a business. Due diligence is expected of the buyer to ensure that all relevant facts regarding the acquisition target have been ascertained prior to consummation of the purchase. Due diligence is also expected in other business contexts, most notably mergers or consolidations, funding new ventures, performance of partnership duties, as well as within the mutual fund industry. These due diligence expectations arise from, and are enforced by, the common law of the United States (which is a body of law evolving from numerous court decisions).

The standards of due diligence can also be applied through federal statutes. For example, Section 11 of the Securities Act of 1933 may protect issuers of publicly traded stock from liability for inaccurate statements if they can show they performed adequate due diligence in ascertaining the veracity of those statements. In addition, Chapter 8 of the Federal Sentencing Guidelines allows for the reduction of sanctions for organizations that have exercised due diligence by establishing compliance and ethics programs.

Due Diligence in Business Acquisitions and Venture Funding

When a business is being acquired, whether through outright purchase or through a merger or consolidation, it is incumbent on the acquiring entity to perform due diligence on the acquisition target. Due diligence primarily involves, but is certainly not limited to, examining the financial books of the acquisition target to ensure their accuracy. Due diligence also includes examination of the legal, strategic, and operational aspects of the target. The goal of the due diligence is to ensure that all is known about the business and risks associated with the acquisition target. Thorough due diligence may ultimately lead to the terms of the transaction being altered or even the acquisition being abandoned altogether.

During the due diligence process, there exists a potential tension between the acquirer and the acquisition target. Due diligence is an obligation of the acquirer, performed for its own financial benefit. To what extent must the acquisition target participate in the due diligence process? Obviously, the target must supply access to the relevant supporting information. And the information supplied must be truthful—the acquisition target can be liable for fraud if it misrepresents material information. On the other hand, must the target disclose information the acquirer fails to ask for? The acquisition target can also be liable for fraud if it fails to disclose significant information that causes the transaction to be materially misrepresented. Short of this legal standard, the issue is whether the acquisition target is ethically bound to be more forthcoming than if it strictly complied with only the literal requests of the acquirer.

These same issues apply when an investment is being made in a new business venture. Reflecting how the standards of due diligence vary with the particular circumstances, due diligence performed on a new venture is necessarily going to be less thorough, as the venture has less history to examine. In this regard, the potential investor must accept a higher level of risk, regardless of the level of due diligence performed.

Due Diligence in Joint Ventures and Mutual Funds

It is important to understand that there is risk associated with any business transaction. Due diligence does not guarantee the success of a venture or transaction—although its purpose is to minimize the risk of failure. For example, where a joint venture seeks to acquire another business, some members of the joint venture may rely on other members of the joint venture to perform due diligence as part of the acquisition process—and failure to do so could constitute a breach of the fiduciary duty that all members of the joint venture owe to each other (a fiduciary relationship is one of trust and confidence). But the due diligence process does not alone guarantee success of the joint venture. Bad business judgment leading to the failure of the venture, despite due diligence, does not constitute a breach of a fiduciary duty.

Due diligence also plays an important role in emerging trends in the mutual funds industry. As the popularity of hedge funds has grown, so has the popularity of funds of funds, which are portfolios of hedge funds. (While there is no exact definition of hedge funds, their most common attribute is engaging in short-term, highly speculative trades in an effort to achieve above-average returns regardless of market conditions.) To protect their investors, managers of funds of funds are expected to perform due diligence on the funds in which they invest. However, as the collapse of the multimillion dollar Bayou Group hedge fund has exposed, the same managers who are to perform due diligence on a hedge fund are also paid a percentage (up to 3%) of the assets they invest with the fund. While funds of funds extol the extensiveness of their due diligence relative to the funds they invest in, the fact remains that receipt of fees for investing in the hedge funds raises significant conflicts of interest. The obvious concern is that a fund manager may be less prudent to receive the hedge fund fees.

Due Diligence Requirements Under U.S. Securities Laws

Under the Securities Act of 1933, certain securities cannot be sold unless the seller has registered them by filing a registration statement with the Securities and Exchange Commission. If any part of the registration statement is false or misleading, any purchaser of securities sold pursuant to such registration statement can bring suit under Section 11 of the Securities Act against certain people involved in the publication of the registration statement, including the issuer of the securities, directors of the issuer, anyone who signed the registration statement, the underwriters of the issue, and experts named as having prepared or certified a false part of the statement. Under certain circumstances, a defendant against a Section 11 claim may be able to assert a due diligence defense and, thus, escape liability. To successfully assert a due diligence defense, the accused will have to prove it had, after a reasonable investigation, reasonable grounds to believe, and did believe, that the statements in the registration statement were true.

Generally, the more experience with, and control over, the issuer a person has, the greater the standards required in performing due diligence—because it is assumed that someone so close to the issuer would be aware of any mistakes or omissions in its registration statements. For example, inside directors (i.e., directors who are also officers of the corporation) have not generally been able to use the due diligence defense, on the basis that they are intimately involved in the operations of the business. Outside directors (i.e., directors who are not also officers of the corporation), however, have been considered to have shown due diligence and, therefore, escaped liability for a fraudulent prospectus, by pursuing a reasonable investigation of the accuracy of the securities registration statement by relying on independent audits and investigations by accounting firms, underwriters, and the company's management. However, some courts have held outside directors did not show adequate due diligence by merely relying on information supplied by other officers and directors of the company. Likewise, auditors have been found to have failed to show adequate due diligence by relying solely on answers given by the corporate officers without making an independent investigation.

Underwriters of a securities offering have been deemed to have performed due diligence in investigating a corporation that was issuing securities by, for example, thoroughly analyzing the issuer, its finances, management and future plans, the state of the relevant industry, and the reputation of the corporation in its industry. There may, however, be obstacles to performing adequate due diligence when the possessor of information is adverse to the process. For example, where a company was raising money through a public offering to acquire another company, the owner of the "target" company refused to provide certain information. The underwriters of the public offering were deemed to have performed their due diligence despite being unable to obtain the information in question—even though the omission of the information was deemed to be material.

Due Diligence Under the Federal Sentencing Guidelines

In 1984, Congress passed the Sentencing Reform Act in an attempt to eliminate disparity in sentencing for federal criminal violations. The Sentencing Reform Act of 1984 created the U.S. Sentencing Commission that issued guidelines for compliance with the act. Chapter 8 of the *Federal Sentencing Guidelines* applies when an organization is convicted under federal criminal law. The guilty organization's fine can be reduced if it has in place an effective compliance and ethics program that decreases the likelihood that questionable conduct will occur in the workplace. This is done to offer an incentive to organizations to reduce and ultimately eliminate criminal conduct by providing a structural foundation from which an organization may self-police itself through an effective compliance and ethics program. Under the *Federal Sentencing Guidelines*, an organization demonstrates due diligence to prevent and detect criminal conduct by promoting an organizational culture that encourages ethical behavior and a commitment to compliance with the law (through the establishment of an effective compliance and ethics program under the requirements set forth in the *Guidelines*). Such an environment at work can be advanced through the development of codes of conduct that prescribe ethical values and behaviors, as well as through professional training that increases employee awareness of noteworthy ethical issues that occur in the organization or industry. Managers should also consider developing a system for the identification and reporting of questionable conduct when it occurs and identify a top leader who is directly accountable for the management of these ethical programs. Finally, management must initiate appropriate disciplinary action when questionable acts are identified in an organization and develop action plans to prevent recurring ethical problems. By taking these steps to promote an ethical culture in an organization, managers demonstrate a level of attention and commitment to ethics recommended by the *Federal Sentencing Guidelines*.

In January 2005, however, the U.S. Supreme Court, in the case of *United States v. Booker*, held that the *Federal Sentencing Guidelines*, particularly by allowing a judge to increase a criminal defendant's sentence, violated defendants' Sixth Amendment right to a jury trial and were therefore unconstitutional. The Supreme Court concluded that the *Federal Sentencing Guidelines* could not be compulsory, though they could be advisory. As a result, there is a significant amount of confusion as to whether the organizational due diligence requirements under the *Federal Sentencing Guidelines* will continue to be used to reduce an organization's criminal sanctions, and thus remain an incentive to implement effective compliance and ethics programs.

As discussed above, due diligence applies in a number of contexts, though primarily in business settings. While the notion of due diligence can be fluid, requiring different standards in different contexts, common traits can be found. Primarily, due diligence is a standard of investigation into the background and facts surrounding a business activity. And that investigation must be conducted with thoroughness and care. In addition, conducting or complying with due diligence may involve ethical standards that go beyond merely complying with the applicable law. Managers must proactively advance principled and socially responsible standards to ensure that all stakeholders recognize the company's position on ethical practices. Companies must also select ethical leaders and take action when questionable conduct occurs to demonstrate this commitment to business ethics. More important, the resulting ethical organizational culture will encourage employees to make ethical decisions and behave in an appropriate manner while at work.

—Robert Sprague and Sean Valentine

See also Accounting, Ethics of; Business Ethics; Certified Public Accountants (CPAs); Corporate Ethics and Compliance Programs; Directors, Corporate; Ethics

Training Programs; Federal Sentencing Guidelines; Fiduciary Duty; Hedge Funds; Mergers, Acquisitions, and Takeovers; Sarbanes-Oxley Act of 2002

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Due Process

Due process involves following established procedures in the enforcement of laws, rules, or policies and enforcing each in a fair and just manner rather than arbitrarily or capriciously. Due process serves to protect the rights of individuals facing adverse actions by the government, organization, or other entity.

In the United States, due process is based on principles from the U.S. Constitution and Bill of Rights that protects a person from being deprived of life, liberty, or property without due process of law. As applied to actions of federal, state, and local governmental entities, a person cannot be deprived of life, liberty, or property without appropriate legal procedures being followed and without the actions being legitimate and reasonable. While due process protection extends to employees working in government organizations, employees in private sector organizations have no guarantee of due process. However, employees in private sector businesses may have due process protection provided either through union contracts or formal policies of their employers. Such due process policies may govern employee grievance procedures, disciplinary actions, and appeal processes. From a broader stakeholder perspective, due process procedures governing the relationship between businesses and stockholders, suppliers, customers, and other stakeholders are generally provided through the legal system in the United States rather than through specific due process policies of businesses. Because the majority of due process issues concern the employment relationship, this entry will focus on due process policies and practices governing businesses and their employees.

History

The concept of due process can be identified in ancient historical records and in many different cultures. Due process has been found in the laws of ancient Egyptian, Greek, and Roman civilizations. Teachings from different religions and philosophies also include concepts of due process.

The use of due process in the United States can be traced to the Magna Carta (Great Charter) of 1215, a document drafted by King John of England, who under pressure from his barons, agreed to limit his power and provide certain rights to England's citizens. Rather than being subject to arbitrary or capricious decisions of the King, the Magna Carta established a code that delineated the power of the government and the rights of its citizens. Actions against citizens could only be taken based on the lawful judgment of peers, or by the law of the land. The specific phrase "due process of law" appeared in a 1354 revision of the Magna Carta. The phrases "law of the land" and/or "due process of law" were incorporated into the U.S. Constitution and many states' constitutions.

Due process is specifically mentioned in two amendments of the U.S. Constitution. The Fifth Amendment, ratified in 1791, states that no person will be deprived of life, liberty, or property without due process of law. The Fourteenth Amendment, ratified in 1868, says the same with respect to the individual states.

Procedural and Substantive Due Process

Two components of due process are recognized: procedural and substantive. Procedural due process focuses on whether the actions against an individual are carried out in accordance with established laws, rules, or policies. Substantive due process concerns the reasonableness and legitimacy of laws or policies and whether the laws or policies are fair and just in and of themselves. For both aspects of due process to be achieved, established procedures for handling an individual's offense must be followed (procedural due process) and the law or policy must be reasonable and serve a legitimate purpose (substantive due process).

Whereas the Bill of Rights, ratified in 1791, applied specifically to the laws and actions of the federal government, with the ratification of the Fourteenth Amendment in 1868, procedural and substantive due process protection was extended to individuals with respect to state laws and actions. This meant that state laws could now be reviewed by federal courts to determine not only the appropriateness of procedural processes in enforcing the law but also whether the state laws and actions were reasonable and legitimate (substantive due process).

Determining whether actions taken against an individual meets procedural due process standards has been less controversial as compared with deciding whether laws and actions meet the substantive due process standard. In determining whether procedural due process has been attained, the courts examine whether the actions taken against a party were based on existing law and that the law was appropriately applied and enforced. However, in deciding if a law fulfills the substantive due process criteria, the courts must look beyond the words of the law and determine whether the law is reasonable and serves a legitimate purpose, a much more subjective approach to interpreting the law's meaning and application. The more subjective nature of substantive due process has created continuing disagreements and controversy.

Some argue that the term *due process* should be applied only to issues concerning procedural due process and that decisions based on subjective determinations of reasonableness and legitimacy allow the courts to legislate from the bench and assume power over state legislation not intended by the Constitution. On the other hand, adherents of substantive due process argue that even if laws passed by legislatures are enforced appropriately, no protection is provided against unjust laws. Allowing the courts to rule on issues regarding substantive due process protects individuals against unfair and unjust laws. Although the courts have largely accepted substantial due process protection, controversies remain with regard to how extensively substantive due process should be applied to laws regarding liberty and privacy issues such as abortion and gay rights.

Public and Private Sector Employees

Because the Fifth and Fourteenth Amendments apply to actions of the federal and state governments, only employees of federal, state, and local government entities (referred to as public sector) are guaranteed due process. While union members in private sector companies often have due process procedures included in their employment contracts, employees in a large number of private sector companies (including public and privately held companies) have no guarantee of due process. Rather, the employment relationship in many private sector companies is governed by the employment-at-will doctrine.

Employment-at-will employees work with no assurances regarding the terms or conditions of their employment. The employment relationship can be unilaterally altered or terminated at any time, for any reason (good or poor), or for no reason. While employees also have the right to end the employment relationship at any time for any reason, generally the employer has the stronger position to alter the relationship.

Constitutional guarantees of due process have not been extended to private sector employees as the courts have considered such relationships to be private contractual relationships between consenting parties. In other words, each party is able to freely negotiate the terms and conditions of employment and arrive at a mutually agreeable contract. While certain state and federal laws protect the rights of employees in the private sector, employers and employees have been largely free to establish the provisions of the employment relationship.

Every state except Montana recognizes the at-will employment relationship, although, as will be explained below, some restrictions exist. In 1987, Montana passed the Wrongful Discharge from Employment Act that requires that terminations be based on "good cause" once an employee has completed the probationary period of employment (6 months maximum).

The courts have generally supported the employment-at-will doctrine although various state and federal laws provide some restrictions. For example, federal antidiscrimination laws such as Title VII of the Civil Rights Act of 1964 restrict an employer's right to make employment decisions that cause discriminate treatment (intentional) or disparate impact (unintentional or unintended) on protected classes of employees. Other restrictions that prevent employers from terminating or taking adverse actions against at-will employees include public policy reasons (whistleblowers) or when due process procedures are explicitly or implicitly included in an employee's contract (including provisions in employee handbooks).

Although these laws provide employees some protection against unfair and unjust actions of their employers, critics of the employment-at-will doctrine argue that such employment relationships remain unfair because employers are still largely not held accountable for many other types of adverse employment decisions that may still be capricious, prejudiced, or maliced. Thus, critics argue that for at-will employees not to be disadvantaged, due process should be extended to all employees. In this way, all employees are more likely to be treated ethically, that is, in a fair and just manner.

Due Process Methods

Although private sector companies are not legally required to provide due process for their at-will employees, many companies have opted to implement such procedures. The reasons why companies adopt due process procedures vary. Companies may adopt due process procedures to better ensure that ethical decisions will be made when employees face adverse employment actions. Companies may also adopt due process policies as a means of avoiding litigation costs or unionization. A more pessimistic view of why companies implement due process procedures is that such policies restrict employees' access to the courts for settling disputes. By requiring all employment-related disagreements be settled through company due process procedures, management also has greater control over the process.

Three methods commonly used to ensure due process for employees when resolving employment-related problems will be discussed in this section: progressive discipline policies, grievance procedures, and alternative dispute resolution (ADR) methods. While each method helps ensure due process, each serves a different purpose. Progressive discipline procedures are initiated by managers and seek to provide steps for corrective action when employees' conduct or behavior falls below acceptable standards. Grievance procedures adopted by companies allow employees to raise problems or complaints with management. Finally, ADR methods (mediation and arbitration) permit employees to appeal adverse employment-related decisions.

Progressive Discipline

One method adopted by companies to provide due process to employees is a progressive discipline policy. Such policies incorporate escalating penalties for unsatisfactory employee performance. Penalties vary in severity depending on the nature of the offense, whether unsatisfactory performance continues, or if offenses are repeated. For serious offenses, employees may face immediate suspension or termination.

Progressive discipline systems can provide procedural due process to employees when clearly delineated step-by-step procedures are adopted to govern the process that managers must follow when disciplining employees. In general, a manager would inform an employee about a performance or behavior problem, explain to the employee what needs to be done to correct the problem, provide a reasonable period of time in which to improve, and ensure that the employee understands the consequences for failure to improve. The legitimacy and reasonableness of the manager's action (i.e., substantive due process) can be demonstrated as each action by the manager is documented. An appeal process, perhaps using an ADR method (explained below), is also often included as part of the progressive discipline system. In this way, decisions by managers are more likely to be ethical, fair, and just.

Grievance Procedures

Besides progressive discipline policies, companies may also provide grievance procedures for employees. Unlike progressive discipline systems in which actions are initiated by managers, grievance procedures allow employees to bring concerns, problems, or complaints to management's attention. Such issues may include terms and conditions of employment, harassment, work policies and practices, and discriminatory practices among other issues.

A company's grievance procedure may encourage employees to initially follow an informal process perhaps using an open-door policy where an employee can discuss the situation with a manager of the employee's choosing. If the situation is not resolved satisfactorily, employees often have the option of filing a formal, written grievance, which is investigated by the company. If the employer's decision regarding the grievance is not acceptable to the employee, an appeals process may be initiated perhaps through an ADR method. Again, the goal for providing grievance procedures for employees is to provide a fairer and more just workplace.

Alternative Dispute Resolutions (ADRs)

ADR methods such as mediation or arbitration (mandatory or nonmandatory) are another means that companies can use to provide due process to employees. ADRs can be used to settle employees' disagreements regarding disciplinary actions, grievance decisions, or other adverse employment-related decisions.

In a mediation process, the two disputing parties attempt to settle their disagreement by involving a neutral third party or mediator as part of the discussion. The mediator does not make a decision about how the disagreement should be resolved but instead facilitates the discussion between the parties in search of a mutually agreeable solution.

A more commonly used ADR method is arbitration. Employment arbitration agreements are governed by the Federal Arbitration Act (FAA) of 1925, which permits arbitration agreements between employers and employees. The FAA preempts state laws that restrict or constrain the use of arbitration agreements. Besides the FAA, other legislations such as antidiscrimination laws include language that encourages arbitration as a means of settling employment disputes.

Companies may require employees to sign a mandatory arbitration agreement, often as a condition of employment. Such agreements require employees to arbitrate all employment-related conflicts, including claims of discrimination, and generally prohibit further litigation. The arbitration decision is generally binding on both parties and provides a final resolution of the conflict.

Because the arbitration process is largely designed by the employer, critics argue that there may be bias built into the arbitration process that favor the employer and force employees to give up certain rights, especially the right to seek resolution of the conflict in the courts. Critics further argue that companies that require mandatory arbitration agreements have little incentive to ensure that standards of procedural or substantive due process are fulfilled as employees have no further recourse beyond the arbitration process.

Rather than adopting mandatory arbitration agreements, critics would urge employers to adopt nonbinding and nonmandatory arbitration agreements as a means of better ensuring that ethical and fair decisions are reached. In nonbinding arbitration systems, employees retain the right to pursue a case through the courts, if the decision of the arbitrator is not acceptable. Nonmandatory arbitration agreements allow employees to decide whether to take part in the arbitration process. Such approaches would strengthen employees' due process protection.

In addition to the differing views regarding the use of mandatory arbitration agreements, decisions by different federal courts regarding arbitration have also been in conflict, which created additional uncertainly in the application of such provisions. However, in 2001 in *Circuit City Stores v. Adams*, the Supreme Court ruled that mandatory arbitration agreements were permissible and that the agreement could include virtually all employment disputes, including questions of discrimination. (Only employees involved in interstate transportation were considered exempt from the FAA.)

While there remains disagreement regarding the provision of due process for employees, especially with regard to mandatory arbitration agreements, a number of procedures can be adopted by companies to better ensure that employment decisions are ethical, fair, and just. In adopting due process procedures, companies should meet the following criteria:

- Provide notification to employees regarding any adverse employment decision.
- Permit employees sufficient time to appeal the decision or action.
- Grant employees full access to evidence and information relevant to the case.
- Permit employees to use an attorney they so choose.
- Allow sufficient time for employees and their representatives for discovery.

If a company adopts a mandatory arbitration process, the company should further ensure that

- arbitration agreements are clearly written and thoroughly explained to each employee,
- an unbiased arbitrator, mutually acceptable to both parties, is selected, and
- a written copy of the arbitrator's decision is given to the employee.

Including such procedures will better safeguard employees' rights and strengthen employees' sense of fairness and justice while providing companies the ability to take adverse employment actions against an employee when good cause exists.

Conclusion

Within certain legal parameters, companies have the right to adopt employment policies and practices that management deems appropriate and applicable in the workplace. However, how these policies and practices are applied and enforced raise ethical concerns that should be thoughtfully considered by government and company officials. Are appropriate procedures followed when making decisions that adversely affect the employment relationship? Are actions reasonable and legitimate, and have the decisions been reached in a fair and just manner?

Currently, employees in federal, state, and local governmental entities have a guarantee of due process provided by the U.S. Constitution. In addition, some employees in private sector companies, mainly union members, also have due process rights included as part of their labor contracts. However, a large segment of the workforce, namely at-will employees, has no guarantee of due process and may not be protected from unethical decisions and actions by their employer. Thus, one question to consider is whether due process protections should be extended to all employees so that all will be treated equally and better ensure fair and just treatment in the workplace.

While there is currently no legal requirement that due process be provided to at-will employees, some companies have adopted such procedures. Companies may implement such policies with a genuine desire to ensure that their employees are not subject to arbitrary or capricious decisions and actions. Other companies may adopt such policies as a means of protecting themselves against costly and less easily controlled litigation processes. Thus, while arbitration systems may provide safeguards for employees against arbitrary and capricious employment decisions, concerns remain that such processes may fall short of ensuring ethical and fair treatment.

A company's arbitration process may introduce a certain level of bias into the process that favors the company rather than ensuring a level playing field. Since employees who sign mandatory arbitration agreements have no recourse through which they can appeal unsatisfactory arbitration decisions, it would be more difficult to ensure that the process is fair. Thus, a second question to consider is whether safeguards should be established to better ensure fair and just treatment of employees when mandatory arbitration agreements are used. While employees have some protection against antidiscriminatory practices through the Equal Employment Opportunity Commission, changes or restrictions regarding mandatory arbitration agreements could allow employees to litigate a dispute through the courts if a satisfactory resolution is not reached through the arbitration process.

Companies may determine that implementing due process procedures and providing more diverse options for employees to resolve adverse employment actions will provide not only a fair and just workplace for employees but also benefit employers. In this way, fair and just treatment can be better ensured while at the same time allowing companies to apply just and fair disciplinary actions against employees for good cause, thus protecting the rights of both employees and employers.

—Mark Barnard

See also Alternative Dispute Resolution (ADR); Fairness; Procedural Justice: Philosophical Perspectives

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Dumping

Dumping refers to a business practice in which a foreign company sells its products into the domestic market at a lower price than it sells in its home market, sometimes called "less than fair value" (LTFV), and causes substantial injury to the domestic producers.

For example, a Chinese company might sell a bolt of cloth in the United States for U.S.$3 and the same cloth in China for the equivalent of U.S.$5 causing U.S. producers to lose money or go out of business. This practice is sometimes deemed to be unfair by national trade authorities and brings the remedy of antidumping duties that are assessed on those products. National dumping laws are in accord with the World Trade Organization's (WTO) Anti-Dumping Agreement (General Agreement on Tariffs and Trade [GATT] Article 6). Dumping can be contrasted with the practice of subsidies, such as export subsidies, done by national governments and not businesses, and which may be subject to countervailing duties as allowed by the WTO's subsidy agreement. Dumping, as defined here, differs from the business practice of selling products in foreign markets that are banned in the domestic market. For example, sometimes chemical companies sell products in developing countries that are banned in developed countries, such as the gasoline additive TEL or lead, and this practice has been termed "dumping."

Originally, dumping was seen as a pernicious business practice in which a strong international competitor would drop its prices in certain foreign markets, sometimes called international price discrimination, in order to knock out competitors and to obtain a strong market position, perhaps even a monopoly, in that domestic market. Once the international competitor gains market power in the foreign market, it could then raise its prices, hold back output, and engage in other anticompetitive practices. To illustrate from our example above, the Chinese company might drop its prices for its bolts of cloth in the U.S. market until all the U.S. companies go out of business and then raise prices above U.S.$5 per unit as its competition dwindles. The dumping laws allow the injured domestic companies to file a petition for relief on behalf of the injured industry. With their remedy to set a duty at the level of the dumping margin, in this case U.S.$2 per bolt of cloth, the dumping laws are meant to discourage this business practice. The dumping laws are in theory consistent with utilitarianism because they attempt to minimize market distortions by unfair trade practices that result in lower prices and more wealth for consumers.

Much controversy exists about both the concept of dumping and the administration of antidumping laws. With the concept, many believe that with the globalization of commerce, especially stemming from the joint effects of improved technology, communication, and transport, it is much more difficult for a company or a national industry to achieve a monopoly position in a foreign country for any substantial length of time. This is so because if profits are very high in a given market, producers from other countries, as well as new domestic competitors, are likely to enter. For example, if after knocking out the U.S. companies, the Chinese company raises its price in the United States to U.S.$9 per bolt of cloth, substantially higher than the original sales price and with a higher profit margin per unit, many firms from other countries, including the United States, are likely to enter the market to capture some of these profits. So in most cases, it is doubtful that the foreign company could afford to practice dumping for long. The second conceptual problem is that the focus on differences in prices across national markets ignores many important differences across markets such as demand conditions, substitute products, and other factors. A third problem is that in considering injury, it is sometimes difficult to isolate the deleterious effect on a domestic industry of trade as opposed to other factors such as changes in technology or shifts of consumer tastes away from one's products.

Nevertheless, at present, the greatest problem surrounding dumping is not conceptual but instead the administration of the antidumping laws by national governments. Most countries have developed an administrative system that receives complaints or petitions from the domestic industry or companies representing that industry. This system solicits evidence and makes recommendations based on both national and international law. The controversy is that several countries, notably the United States, are charged with creating an obtuse and opaque process for evaluating dumping cases that is biased toward domestic companies. For example, in the calculation of LTFV, the United States has promulgated many technical rules about the calculation of foreign and domestic prices, currency conversions, constructed costs (when price data are difficult to obtain), accounting rules, and the like. Furthermore, the process is allegedly tilted against the foreign companies that must respond to the dumping petitions. As a result, many foreign companies pull their product from the U.S. market at the onset of an antidumping investigation.

Most countries feel that the United States uses its dumping laws to protect some of its internationally weak industries such as steel and fishing. In 2000, the United States signed into law the so-called Byrd Amendment, which in effect remits any dumping duties collected in successful investigations to the

U.S. companies that filed the petition. In 2004 and 2005, Canada, the European Union, Japan, Mexico, and Thailand each challenged U.S. antidumping cases or portions of antidumping law before the WTO's dispute mechanism. The Byrd Amendment was also targeted. The WTO's dispute panel ruled in 2004 that member nations could take retaliatory measures until the United States changes its antidumping laws.

Controversy surrounding antidumping is not limited to the United States. In 2004, 10 of the 20 trade disputes between nations were in the dumping and antidumping areas, including cases against Egypt, the European Union, India, and South Korea. Because of this, the WTO is likely to revisit its dumping rules in the current round of trade negotiations.

There are several ethical implications of antidumping laws that favor domestic petitioners, typically producers, over other interests. If antidumping laws are used by national authorities to protect less efficient domestic producers over more efficient foreign producers, antidumping duties represent a transfer of wealth to domestic producers from domestic consumers and foreign producers (depending on price elasticity of demand). In effect, this is a form of distributive justice (or injustice, depending on where you sit). If "biased" antidumping regimes, however, are used as part of a larger package of liberalization reforms for the entire economy, such as to gain the support of sectors that are likely to be harmed by international competition in the home market, then antidumping might be seen as part of a redistribution of wealth from winners of the liberalized economy to sectors that are likely to lose without some assistance. In this light, an antidumping regime that is tilted toward internationally weak domestic producers might be the most politically expedient way to gain a set of trade policies that liberalize most of the economy, which creates in turn efficiencies, consumer welfare, and overall social wealth and is consistent with ethical utilitarianism.

—Doug Schuler

See also International Trade; Justice, Distributive; Utilitarianism; World Trade Organization (WTO)

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DUTY

In daily speech duty is often conceptualized as a requirement that a person has to fulfil. It is typical of this everyday conception that duty is supposed to overrule other considerations a person might have concerning the choice of his or her actions, considerations that may, for example, be based on his or her desires or particular inclinations such as self-interest. Failing to acknowledge or live up to a duty means that a person's conduct is morally wrong.

It is, however, characteristic of thinking on duty in Western culture that "right action" is not necessarily equivalent to conduct that fulfills a duty. The concept of "right action" has an ambivalent or double meaning. If we say that a person acted "right," we can indeed mean to say that his or her conduct fulfilled a duty. In this sense, we can say that if a person helped a little child from drowning, he or she acted right or obligatorily. However, when we say that a person acted "right," we can also (just) mean to say that he or she did not act contrary to duty. If a pharmaceutical company decides not to hand out all its supplies of AIDS medicines to patients who lack the resources to buy them, we may still say that the company acted right. We commonly do not attribute a duty of beneficence of this intent to pharmaceutical companies; the company, therefore, does not act wrong by holding on to its stock. The ambivalence in the concept of right reveals that Western societies are free societies.

One implication of freedom is that conduct cannot simply be divided into right and wrong. Many actions are permissible. They do not fulfill a duty but also do not violate one. So when a person decides to have tea in the morning instead of coffee that is permissible in this sense. The same goes for the decision to become a carpenter instead of a doctor, the decision to stay childless instead of having a big family, or to buy a small car instead of a big one. Especially, the last example makes it clear that even if a freedom-oriented culture will always try to make the category of permissible action as extensive as possible, it is not true to say that what is morally permissible under specific social and historical circumstances must necessarily be morally permissible under all circumstances. We can think of social and historical circumstances in which the choice between a big car and a small car is not morally neutral. Environmental and economic circumstances may force on us a duty to at least seriously consider the consequences of one's choices in this regard.

The concept of duty is employed in many domains of action. We distinguish, for example, parental duties and professional duties. Still, the two most important contexts in which the concept of duty is employed are the law and morality. The law gives rise to legal duties; morality to moral duties. This explanation will focus on the concept of a moral duty since that is exemplary for our understanding of the concept.

Multiple Interpretations of Moral Duty

The concept of duty has three rather different meanings. First, we can use the concept "duty" to refer to the conclusion of a process of deliberation that strikes the actor involved as a commandment he or she must obey. Thus, a person might say,

> It was my duty to steal this bread in the aftermath of the hurricane Katrina even if it violated the principle that a person ought not to steal; given the circumstances my obligations toward my family provided a higher ground of obligation.

In this interpretation of moral duty, one of the most important questions to be answered is how (by what power) an actor is necessitated to obey this commandment.

Second, the concept of moral duty can also refer to a principle or the set of principles that we (intersubjectively) use as directive or even authoritative in the process of deliberation mentioned before. Thus, we can, for example, say that it is our moral duty to respect others, respect humanity, care for the natural environment, be beneficent, and defy servility, as well as not to kill others and not to steal. None of these principles can be transformed into a simple rule that can always be applied in practice in a clear-cut way. Still, when it comes to the relation with action, there is a lot of difference between the principles. The implications at the level of action of some of the principles are pretty clear. These principles imply rules that allow for little exceptions. Examples are the duty not to kill and the duty not to steal. There are only a few circumstances in which violating these principles does not constitute moral wrong conduct. For other duties, such as the duty of beneficence, the implications at the level of action are far less clear. The duty surely does not implicate that we must always help others, but it also requires much more than the proposition that we must sometimes do other people a favor. With regard to this interpretation of the concept of duty, several important questions arise, such as what is the content of the authoritative set of principles, who determines the content of this specific set, how can this specific set be justified, and is the acknowledgment of these principles and the possible rules they imply enforceable.

Yet another meaning of the concept of moral duty is identical with the phrase "to act as a person ought." In the line of this interpretation of the concept, we can, for example, say that "corporations that embrace corporate social responsibility do their duty" or that "the soldier performed his duty by defending his outpost against an enemy attack." The main question to be answered in relation to this interpretation of the concept is how we are to value dutiful conduct.

Moral Duty as a Contested Concept

The concept of moral duty does not only have three meanings. The concept also is contested. This means that with regard to each of the three interpretations, many different answers are given to the questions posed in relation to that interpretation. One striking difference, for example, is that the philosopher J. S. Mill claimed that if we may compel a person at all, we may compel him or her to perform his or her moral duties. Over against this the philosopher Kant claimed that exacting moral duties goes against their nature. Another striking difference is that according to some beneficence is indeed one of our central duties, while others claim that even if it is morally valuable, it is not a moral *duty*. Again, some will hold that moral duties derive their legitimacy from the fact that they are the commandments of God, while others will say that they are grounded in the specifics of human nature as both free and rational beings.

Here, the specific Kantian account of moral duty will be clarified. Kant's interpretation of duty is quite complex but also one of the most elaborate accounts. What is more, on close inspection our cultural understanding of duty also happens to be quite complex. The contested nature of the concept of duty is acknowledged by touching on some of the main differences with other traditions in the process.

Kant on Duty as a (Subjectively Felt) Commandment

Kant believes that humans are intentional beings. They have the ability to set ends and makes choices. By itself this conception of humans is quite commonplace. But Kant also holds that the human capacity to choose is always mediated by our rationality and, thus, never directly influenced by desires or incentives (such as self-interest). The Kantian model of human motivation, therefore, fundamentally differs from the account prevalent in many modern academic disciplines such as economics and psychology. Here, the human faculty of choice is conceptualized as a "vector model": The decision made by a person can be modeled as the result of the game of push and pull of various desires and incentives that directly influence the faculty of choice.

Still, when it comes to many normal choice situations the differences between the Kantian vision and its rival may not have grave implications. Kant allows for the situation in which our rationality only mediates in a choice situation by permitting our capacity to choose to be temporarily ruled by the struggle between various desires. However, sometimes a person may have to conclude that *duty* requires that he or she must display a particular conduct. In this situation, the fundamental difference between the vector model and Kantian thinking becomes manifest. In the vector model, duty is simply just another vector power, even if it may be a strong power. Kant holds that when it comes to duty our rationality overrules any incentive or desire; they are placed out of order. This view seems to be in accordance with the way we experience duty in practice and also seems to be better able to explain situations such as the behavior of soldiers under fire.

Duty thus has a very special place in the Kantian thinking on human motivation. Kant articulates this special structure of duty by claiming that duty as a commandment is unconditional. The binding force of duties does not depend on some contingent desire or on the contingent fact that a person has set himself or herself a specific end. Moral duties as commandments are categorical. What is more, moral duties are the *only* categorical commandments. Even legal duties do not have that status according to Kant. Legal duties only bind if a person has set himself or herself the end of wanting to forego the direct—penalties—and indirect—social isolation—consequences of living outside the law. (A complicating factor, however, is that according to Kant we also have a *moral* duty to obey all legal duties.) This view of the uniquely categorical nature of moral duties is commonplace in modern moral philosophy even if there are many views as to the exact status of legal duties and their relation to moral duties.

Necessitation

A central question of modern moral philosophy is how we have to understand that when persons come to the conclusion that duty requires something of them, how are they able to subjectively necessitate themselves to obey the moral command? Who or what imposes the subjective *necessity* to obey a moral command? This question is sometimes grasped as the *obligatory* aspect of moral duty (but the difference between a duty and an obligation is sometimes not acknowledged or seen in a different light). Before Kant—and also after Kant—the obligatory aspect of moral duty has been explained by referring to an innate sense of duty that all humans have. Many have also referred to the necessity of obeying the will of God or to man's pursuit of (individual) happiness. Kant's conclusion is that the necessity is grounded in the structure of rationality itself. When we act on duty we are necessitated by the force of pure rationality itself. Kant calls this pure rationality a priori rationality. Kant argues for his position in many ways. One is that duty as moral choice is by its nature a free and autonomous choice. However, only if we ground morality into rationality are we able to maintain that moral choices are autonomous choices. Any other ground would have as its effect that duty implied some form of obedience to something external or contingently related to ourselves. Some contemporary Kantians still argue along these traditional Kantian lines. Others are no longer convinced or fear that this type of argument overburdens the concept of rationality.

Implications

An interesting implication of the Kantian view of the necessity of duty that is still embraced by all modern Kantians is that a distinction is rejected that is common in a lot of modern academic literature on morality. It is quite common nowadays to distinguish the rational process of deliberation that persons go through, leading up to the conclusion that "*X* is their duty," from the emotional process that persons must go through to motivate themselves to actually do or acknowledge *X*. To make a fundamental empirically based distinction between these two processes is improper in Kantian thinking. The rational process of deliberation itself is motivating. Reasons have the power to motivate humans. Reason is not just an instrument or a slave of the passions, as Hume had it.

To those who say that we do sometimes experience a sense of duty, Kant replies that this experience does not cause us to obey our duty but that it is the effect on the level of our emotions of the discursive process that convinced us. Another radical implication of Kant's view that is shared by most modern people, Kantians and non-Kantians alike, is that morality is fundamentally democratic. Everybody is rational, and everybody, therefore, is qualified when it comes to moral matters. Kantian theory fiercely objects to the medieval position that some people are superior to others in moral matters because they stand somehow closer to God or any other origin of morality. Our rational nature is the ground of duty and rationality characterizes any human being.

Kant on Duty as a Requirement (or Set of Requirements)

In his thinking on duty as a set of principles, Kant makes a fundamental distinction between duties of justice and duties of virtue. These two types of duty differ at multiple levels, such as their justification, their structure, their enforceability, and the ways in which we can be motivated to perform them. Kant considers both the duties of justice and the duties of virtue as moral duties. Still, as regards their *structure* the duties of virtue are exemplary as moral duties in Kantian thinking.

Duties of Justice

Examples of principles typically belonging to the duties of justice are the duty not to steal, the duty not to kill, and the duty to resist injustice. As a special category, the duties of justice find their justification in the fact that they are conditional for the possibility of a free society. Without the duties of justice being instituted, the idea of a well-organized society is simply impossible. Because of their specific justification, Kant holds that the duties of justice may be exacted from a person. They are the minimum rules of social coexistence and, therefore, enforceable. Again, because of their specific justification the duties of justice are closely related to—or translatable in—clear practically relevant rules. Otherwise, they could not be enforced. One last characteristic of the duties of justice is that there can be several reasons why a person decides to obey the duties of justice. According to Kant, it does not matter what this specific reason is, as long as a person decides to obey. Given their structure, the duties of justice are related to the legal system. We can maintain that in a society with a perfect legislator and a perfectly working legal system, the content of the duties of justice is completely encompassed within the legal system. In actually existing societies, the duties of justice will not be completely encompassed due to imperfections of both the legislator and the legal system.

Duties of Virtue

In contrast, the duties of virtue find their justification in man's aspiration to become a moral person or man's pursuit of perfection. Given this origin, it goes against the nature of the duties of virtue to try to enforce them or push people into acknowledging them. It follows from this that with regard to the duties of virtue, we can only be motivated by the sincere conviction that we want to acknowledge the duty on account of the fact that it strikes us as the necessary thing to do. Or as Kant says, "Duty itself must be the incentive when it comes to the duties of virtue" (see below). Again, because of their origin, duties of virtue cannot be transformed into rules that can be directly applied to action. With regard to structure, duties of virtue are always principles (Kant calls them maxims) that a person must take into account in the process of taking a decision. An example is that in our decision making we must always take into account that we must help other people (in dire straits). It follows that other people can never determine whether a person has fulfilled the requirements of the duties of virtue. There is no result that is externally measurable. Persons can only be their own judge here. They are both the legislator of their own interpretation of the duties of virtue as well as their own judge when it comes to specific judgments in particular situations. Examples of principles that typically fall into the category of the duties of virtue are beneficence, respect, and sympathy, as well as the duty to resist envy. All these duties are complexly related to the fundamental moral categories wrong, permissible ("right" as not contrary to duty), and obligatory ("right" as fulfilling a duty). We can say that to be beneficent or to help another in dire straits is an obligation. But in the way we materialize these duties, there are various degrees of latitude. So a good swimmer will jump into the water to save a drowning person. But for someone who cannot swim well—or who is uncertain as to his capabilities in this regard—it is permissible to call the attention of someone else, to throw a life-saving device in the water, or to do something else that is proper given the circumstances.

Perfect and Imperfect Duties

To consummate his taxonomy of duties, Kant introduces several distinctions that all are complexly related to the main distinction between the duties of justice and the duties of virtue. Several of these distinctions are also commonly employed outside the specific Kantian context. One important distinction is between perfect duties and imperfect duties. A perfect duty directly refers to a rule or requires a specific action that a person should or should not perform. An example of a perfect duty is the duty not to kill another person. An imperfect duty is a duty that refers to a principle that must be taken into account in one's decision-making process. The distinction almost completely overlaps the distinction between justice and virtue but—as always—Kant makes a few exceptions.

Another important distinction is the one between duties of narrow obligation and duties of wider obligation. Duties of narrow obligation are duties that allow for little latitude in interpretation. With regard to duties of wider requirement, the person involved has (quite) some latitude with regard to the interpretation of the principle in practical situations. Logically, most duties of justice are of narrow requirement. Some duties of virtue are of narrow requirement, such as respect; most are of wider—or even widest—requirement. It should be noted, however, that modern literature often blurs the difference between perfect and imperfect duties on the one hand and duties of narrow and wide requirement on the other. Thus, it is spoken of imperfect duties as duties that provide actors with some leeway as to their interpretation.

Beyond Duty

A striking difference between the Kantian edifice on duty—as a set of requirements—and other traditions is that though the duties of virtue are often considered important morally speaking, they are sometimes not conceptualized as *duties*, precisely because they are not considered to be enforceable. Duties of virtue are then considered to be supererogatory or beyond duty (even if some authors classify a few specific duties such as beneficence that Kant classifies as a duty of virtue in the set of enforceable duties). Apparently, there is a tendency in Western moral thinking to link duty and enforceability. This may be related to the fact that in many accounts duty is only grounded in the need of coordination of action within society, and not—as Kant has it—also in man's pursuit of perfection. Kant maintains that grounding duty simply in the need of coordination of action is spurious because it grounds duty only in strategic or prudent considerations.

A similar kind of comment is that many accounts of duty maintain that the concepts of "duty" and "right" completely mirror each other. If there is one person having some duty, then there is also one (or more) other person(s) with rights and vice versa. Kant rejects this mirror view of duties and rights. It applies to perfect duties but not for all imperfect duties.

Another difference with other, in particular contemporary, accounts of duty is that Kant does not make a big issue of what the exact set of our moral duties is and how can we determine this set. For him and for his contemporaries, that was pretty clear. In our pluralistic times, it, however, is a major issue. Many authors specifically try to determine what the (minimum) set of duties is that everyone has to abide by. They also try to find a position of authority needed to justify that specific set. Again, Kant did not discuss the question whether we have moral duties at all. Moral scepticism did not bother his time, as it does ours. A notable difference between Kant and contemporary neo-Kantians is that the latter seem to renounce or at least question whether each person is the sole legislator and judge with regard to the duties of virtue. The question "what do we owe others" is made relevant both with regard to the duties of justice and part of what falls under Kant's interpretation of the duties of virtue.

Kant on Duty as "Doing What We Ought"

The third interpretation of duty is as "to do as one ought." In relation to this interpretation, an important question is how to value dutiful behavior. For example, how are we to morally value the actions of a shopkeeper in a situation in which he deals fairly with inexperienced customers (which is his duty) but only because he wants to avoid a bad reputation? And how are we to morally value the actions of a sympathetic person who helps another person in dire straits, primarily—or also—because of the joy that helping others brings him or her? And what if this helping person was not a sympathetic person but one who had lost all love of the world and who helped only because he or she considered that to be his or her duty?

In answering these questions, Kant makes the distinction between acting in conformity with duty and acting out of duty. Acting in conformity with duty means doing what is right for whatever reason. Acting out of duty means doing what is right solely because one knows this to be one's duty and one is rationally committed to do one's duty. Kant calls this "the motive of duty." According to Kant, acting in conformity with duty does not deserve moral esteem, only acting out of duty does. This means that the shopkeeper and the sympathetic person do not deserve esteem for their action, only the action of the person without love of the world does.

This view of moral esteem does seem to be too strict and inhumane. However, we must take two Kantian distinctions into account here. First, we must distinguish the question of whether an action is morally right from the question of whether the action deserves esteem. All the actors in the examples acted right, according to Kant. Second, we must sharply distinguish the evaluation of actions from the evaluation of persons. According to Kant, the person without love of the world does not deserve esteem, only the person's particular action does. The reverse is true with regard to the sympathetic person. Their action is nothing special morally speaking, but they do, of course, deserve esteem for the personality (at least if their sympathetic character is not something that is completely a gift of nature).

Kant's theory of moral value has been fiercely criticized by many. Most of this criticism, however, is based on misinterpretations. A common one is to confuse the moral value of an action with its moral rightness. On the basis of this confusion, it is said that Kant held the ridiculous view that a person who helps a friend out of sympathy acts morally wrong. Still, however much Kant's theory of moral value is contested it is also—at least partly—in line with the daily understanding of moral value in Western society. For example, when Milton Friedman claimed that most of what goes under the banner of corporate social responsibility (CSR) is not CSR at all because it simply can be explained by referring to the self-interest of corporations, he was talking along Kantian lines.

—Wim Dubbink

See also Charity, Duty of; Coercion; Fiduciary Duty; Goodwill; Hume, David; Kantian Ethics; Rights, Theories of; Virtue Ethics

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E

Economic Efficiency

Economic efficiency studies production, distribution, and consumption assuming that the goal of these activities is to gain a return from using or moving resources. It is similar to the concept of mechanical efficiency, which measures the efficiency of physical processes by relating energy output to energy input.

However, unlike physical processes, in which output and input measures are the same—for example, newtons—measuring the efficiency of an economic action involves transforming physical quantities of resource inputs into physically different outputs, which may be valued in monetary units, or utility (i.e., satisfaction) units, or by some other measures, for example "equity" or "fairness," on which unanimous agreement may be lacking. Without agreement as to what is the relevant output measure or goal (e.g., your satisfaction or mine?), discussions of efficiency quickly become debates about what it is that should be valued by individuals, producers, and society at large. That debate is not addressed here.

An economically efficient action leads to more of the quality being sought, be it profits for producers, satisfaction for consumers, equity for citizens, or whatever the chosen measure, while using no more resources than were used before. Studying resource use in production, distribution, and consumption has been the main focus of economics since the first sustained writing on the subject in ancient times—for example, Xenophon's *Oeconomicus*, written in approximately 380 BCE. It is considered in both microeconomics and macroeconomics.

To examine the concept of economic efficiency, it is necessary to define it in production, distribution, and consumption. Production combines resources into one or more outputs constrained by the quantity of resources, the available technology, social concerns, rules, regulations, and any other considerations producers face. Exchange activity consists of using resources in moving goods and services through space and time, again under given technological and social considerations. Exchange is another form of production, where moving a good from Place A to Place B is a substitute for producing that good at B. Consumption activity consists of using goods and services to derive satisfaction subject both to consumers' resource constraints and to social considerations.

Efficiency requires that changes made in any allocation, using the same resources and technologies, improve the situation of at least one party without at the same time reducing the well-being of any other. Usually, a change in a producer's profits—total revenue minus total cost—is the measure of a change in productive efficiency. However, profits need not be the measure, and even if they are, this does not exclude the fact that producers have to work within both technological and social constraints. For consumers, efficiency requires that any change from the status quo raising at least one person's satisfaction does not result in the worsening of anyone else's utility or satisfaction.

Economic efficiency may be consistent with equilibrium, a state where all opportunities have been explored and no profit- or utility-enhancing opportunity (including side payments by gainers compensating losers) remains. This condition is known as Pareto efficiency (or a Pareto optimum), after Vilfredo

Pareto. However, equilibrium is not the necessary outcome of a search for efficiency as search behavior, experimentation, random acts, changes in the state of the world, changes in technology, change in the legal system and rules and regulations, and so on can easily be seen to keep an economy in motion as opposed to a state of rest.

Production Efficiency

Production efficiency requires that any resource user produce as much output per monetary unit (e.g., the dollar or euro) spent on that resource as any other user. Stated technically, for the last, or marginal, unit of output produced, the opportunity cost per unit of output must be identical across all producers.

If this equalization does not take place, at least one producer will have a cost advantage and, hence, higher profits than the competitors. Self-interest (profit seeking) as one motivator will compel that user to hire more input and expand output to the point where its comparative cost advantage is eliminated. A central authority with knowledge of the comparative costs and efficiencies could also direct this result.

Efficiency is seen to be good because it leads to more of what is valued without expending more resources. Moving toward greater efficiency is a win-win situation. This begs the question of how resources—for example, labor—might feel about shifting from one producer (e.g., firm) to another or moving from location to location even if a rising wage is attractive and whether or not these costs are included in the modeling.

Also assumed, following Milton Friedman's views on ethical firm behavior, is that firms act according to prevailing laws, honestly, and in the long-run best interests of their ownership. This may also mean that extralegal, nonbinding social constraints are rationally being followed and that the interests of third parties, or stakeholders, may be a relevant decision criterion for the firm or, if the firm is centrally directed, that social interests are also being taken into consideration by the decision makers.

In the more realistic case of multiple inputs, the production efficiency condition is slightly more complex. All resources must be used to produce output such that the ratio of the marginal products per unit of cost of the inputs moves toward equality across all inputs and all users. If the marginal product per unit cost differs across goods or users, then output can be increased by shifting resources.

It must be remembered that while this discussion focuses on economic efficiency using monetary measures, as is most common in the economics literature, a monetary measure is not the only measure of efficiency. Societies value other measures—for instance, fairness, equity, justice—and these can be the ones that are used to measure efficiency.

The guiding principle of efficiency is the same: Use a resource to the point where its production of what is valued (e.g., equity) is the same per unit of input for all firms. There would be balances between equity, the distribution of work between capital and labor and between labor of various types, and the other social measures, including profits. So society may find it socially efficient to hire some labor beyond its narrowly defined marginal product rather than have it suffer unemployment or have it forced to undergo dislocation, retraining, or education that might raise its marginal product.

Competition and Production Efficiency

One startling result of economics, the first theorem of welfare economics, states that a competitive market system may lead to economic efficiency. For this, markets must be perfect: There should be no impediments to entry and exit; producers sell identical products, and they are small relative to the market; information is perfect; and producers are self-interested profit maximizers. For production efficiency, the ratio of the marginal products of the inputs must be the same across producers and across outputs. Why should producers necessarily end up having identical ratios of marginal products of inputs for the same products? If markets are competitive, they will arrive at this condition by seeking their own advantage.

To decide on how much to produce and how many resources to hire, a producer will look at the cost of inputs and the prices received for outputs and its own cost structure. In perfect competition, prices for goods and resources are identical for all producers. By the definition of perfectly competitive markets, no one producer can gain a more favorable wage rate for labor or rental rate for capital or land than another; no producer can get a higher price for any of its outputs than another, nor can any resource owner gain a better wage or rental rate.

Producers face the same input costs per unit and the same prices for their output. In the process of maximizing profits, producers will hire resources to the point where the marginal product per dollar spent on each input is equalized across inputs. So, MPL/wage rate = MPK/rental rate for each firm, where MPL is the marginal product of labor and MPK is the marginal product of capital. Cross-multiplying yields MPL/MPK = wage rate/rental rate for each firm. Given that perfect competition ensures that each producer faces the same input prices (wage and rental rates), this ensures that each will hire inputs to the point where the ratios of the marginal products are identical.

What about product mix? Again, perfect competition ensures that producers will produce different products to the point where the ratio of the marginal products of inputs is equalized across products. In perfect competition, inputs are hired to the point where the price of the input (e.g., the hourly wage rate) equals the marginal revenue product of the input. The marginal revenue product is the price of the output times the marginal product of the input. Producers, facing the same output and input prices, hire inputs to the point where their marginal revenue products are equal to the input price: MRPL = Po × MPL = wage rate, where MRPL is the marginal revenue product of labor and Po is the price of the output. This implies that the marginal product of the input for each firm will be equal, MPL = wage rate/Po, and that equalizes the MPL across producers. A similar argument may be made for other inputs.

For multiple products 1 and 2, the market-determined output prices, Po_1 and Po_2, respectively, are given. As above, each user will hire inputs to the point where the marginal revenue product of each input is equal to the price of the input divided by the price of the product for each good: MPL_1 = wage rate/Po_1, and MPL_2 = wage rate/Po_2. The wage rate is common to both, so wage rate = $Po_1 \times MPL_1 = Po_2 \times MPL_2$, or $Po_1/Po_2 = MPL_2/MPL_1$. Since all producers receive the same product prices, Po_1 and Po_2, they all hire inputs to the points where the ratios of the marginal products are equal.

Thus, the competitive process yields production efficiency. The second theorem of welfare economics, a corollary to the first, is that any equilibrium may be shown to be consistent with a competitive process.

In neoclassical economics, these are important results because they show that self-interest may be consistent with a coordinated social outcome. In the broader view, this need not rule out the fact that self-interest may also include concern for our fellows and that equity, fairness, and justice may be built into the motivations of both producers and consumers. As a benchmark, the perfectly competitive model may yield some clues as to how changes in the underlying variables—for example, a change in a tax or a subsidy—may alter the behavior of both producers and consumers.

The perfectly competitive result is highly artificial in that most markets deviate from the perfectly competitive conditions required. Consequently, there are arguments in favor of making markets more like the perfectly competitive ideal—for example, by making wages and prices more flexible, making information more readily available, and reducing monopoly advantage.

A counterargument is that a market mechanism is inherently noncompetitive due to manipulation by those with more power, and consequently, adjustments to market results must be made by governmental or quasi-governmental bodies. For example, in the United States, a floor is put on wages at rates determined by legislatures; in Europe, laws on layoffs affect firm behavior. Almost all countries have health and safety legislation that affects both firms and consumers. Naturally, this is only a short list of social influences on markets, and it is for this reason that modern economies are typically referred to as mixed economies, to reflect the existence and influence of nonmarket mechanisms, such as local, state, national, and even international governments.

Consumption Efficiency

For consumers the situation is similar to that for producers. Assuming self-interest means assuming that consumers will seek to maximize their utility derived from their own—and possibly others'—consumption of goods and services subject to prices, their budgets, and possible social constraints.

Consumption efficiency dictates that for a given budget, consumers purchase goods to the point where the marginal (or additional) utility (MU) per unit of cost is equalized across goods. If not, a consumer can raise the total utility by rebalancing expenditures from goods with lower to higher marginal utilities per dollar.

For example, for two goods 1 and 2, if $(MU_1/Po_1) > (MU_2/Po_2)$, where Po_1 and Po_2 (as above) are the prices to the consumer of a unit of Product 1 and Product 2, respectively, then the consumer could gain utility by reducing expenditures on Good 2 and raising expenditures on Good 1. Diminishing marginal utility in consumption causes the ratios to move closer together as more of Good 1 is consumed (and less of Good 2). Total utility will increase until the ratios are equilibrated.

Rewriting the utility-maximizing result as $MU_1/MU_2 = Po_1/Po_2$ shows that utility is maximized where the ratio of the marginal utilities is equal to the ratio of the prices. This is consumption efficiency, because once this point has been reached, no further increases in total utility are possible. The consumer is squeezing out the most utility possible.

Consumption Efficiency and Perfect Competition

If markets are perfectly competitive, all consumers face the same prices for the same goods and all producers receive the same prices for the same goods. Hence, for all consumers, $MU_1/MU_2 = Po_1/Po_2$, and the ratio Po_1/Po_2 being common to all means that all consumers consume to the point where the ratios of their marginal utilities are equal. This is what exchange allows consumers to do, and they will do so to the point where all gains have been tapped. The ratio of the marginal utilities, MU_1/MU_2, is also known as the marginal rate of substitution in consumption of Good 1 for Good 2. In equilibrium, it is equal to the ratio of the prices and is the same for all consumers. As in production, it can also be shown that any efficient consumption allocation is attainable through a competitive process, a corollary to the above result where the efficient allocation was shown to be consistent with the competitive process.

Implicit in the above discussion is the fact that consumers know both the short- and the long-run benefits (and costs) of consuming goods. Again, a "perfect-information" condition is assumed to hold, and it is arguably the case that for some goods, this information is not available, not disseminated, or ignored in the short run to the long-run dismay of the consumer. This occasions more social involvement in markets in aid of consumers. For example, antismoking campaigns seek to lay bare the long-run health consequences of smoking; antidrug campaigns criminalize certain activities based on superior information about production and consumption residing with governments. Equity considerations may also indicate that those with low—or nonexistent—budgets may also be able to exchange and consume—as opposed to starve—by the use of tax and transfer programs.

Exchange Efficiency

To complete the neoclassical illustration of economic efficiency, we show that self-interest and markets will ensure that producers produce what consumers wish to buy. As above, markets and self-interested behavior determine input and product prices. In equilibrium, markets determine the ratio of the product prices, Po_1 and Po_2. In perfect competition, that ratio of prices is identical across buyers and sellers. As long as the price ratio is common to both, as long as the production possibilities set exhibits nonincreasing returns to scale, and as long as the preferences of consumers exhibit diminishing marginal rates of substitution (which denies addictive-type goods), then there is a unique equilibrium of the system as a whole. These are the strong assumptions behind neoclassical economics' perfect markets, profit, and utility maximization.

If the product price ratio is common to all, as it will be if markets are perfect and there is self-interested behavior, then in equilibrium, producers are just able to produce the goods at the same relative prices as consumers are willing to pay for them. The producers' marginal rate of transformation in producing the goods (the ratios of the marginal products of the inputs, reflecting technical considerations and cost) is just equal to the consumers' marginal rate of substitution, reflecting their preferences in the consumption of the goods. There are neither shortages nor excesses of products. Markets and self-interest yield economic efficiency.

Relaxing Assumptions

The assumptions of perfect markets, profit maximization, and utility maximization, taken as a set, are sufficient conditions for economic efficiency. However, they are not necessary and, as discussed above, are not present in many—if any—markets. Etzioni has shown that cooperation rather than competition may also lead to an economically efficient result. It is also conceivable that economic efficiency could be engineered by other means—for instance, a central authority, though, as Hayek famously argued, the informational and knowledge requirements would be daunting. Thus, for this reason and his stress on personal liberty and freedom, he argued for competition, markets, and policies enhancing them.

The realism of many of the assumptions underlying the concept of economic efficiency is sometimes ignored by those proposing "free market" policies based on partial equilibrium models. These advocates ignore the fact that imperfections in one set of markets, for which they may be recommending "deregulation" or other market-"freeing" prescriptions, may require more rather than fewer regulations or constraints in other markets to come closer to overall efficiency. This is the theory of the "second best."

The underlying assumptions used to arrive at economic efficiency are open to serious question, and to the extent that the assumptions deviate from reality, actual societies are some distance from textbook economic efficiency. Imperfect markets occur in actual economies due to the existence of public goods, common property resources, externalities, nontrivial transaction costs (thus vitiating the Coase theorem), imperfect/asymmetric information, and increasing returns. If, contrary to the assumption of self-interest, consumers do not maximize utility (or if producers do not maximize profits), then again, prevailing prices are not quite "right" for economic efficiency, quantities are "incorrect," and deadweight losses result.

Obviously, producers seeking goals other than immediate profit maximization might purposely stop short of that goal. For example, Henry Ford may have missed out on opportunities to earn greater short-run profits when he famously raised workers' pay to $5 a day. However, in a longer-run and dynamic context, this move may have brought the firm more worker loyalty, higher productivity, lower turnover rates, and lower costs in the myriad other dimensions that encompass the labor-management relationship.

Goals of "good" corporate citizenship may also be seen in a similar light. In fact, it becomes difficult to distinguish acts of good corporate behavior—for instance, publicly donating to charitable organizations or creating foundations—from advertising or other revenue-enhancing activities for the firm. Thus, Milton Friedman claims that an assumption that firms behave *as if* they maximize profits—at least in the long run—is more useful than trying to build a model of a firm's behavior dotted with assumptions on corporate preferences. Friedman's "as if" methodology is a way of putting certain economic assumptions—for instance, self-interest, profit maximization, utility maximization—beyond question as he argues that the purpose of theory is predictive power (an instrument), not a perfect description of reality. Finally, if consumers exhibit envy, the desire for status, bandwagon, or snob appeal, along the lines argued by Thorstein Veblen, with one's utility falling when the utility of others rises, then defining "mutually advantageous" trade is problematic and there would be no trade.

—David L. Hammes

See also Arbitrage; Asymmetric Information; Coase Theorem; Comparative Advantage; Competition; Consumer Preferences; Deadweight Loss; Economic Incentives; Equilibrium; Externalities; Friedman, Milton; Hayek, Friedrich A.; Invisible Hand; Marginal Utility; Opportunity Cost; Pareto Efficiency; Perfect Markets and Market Imperfections; Private Good; Public Goods; Resource Allocation; Self-Interest; Side Payments; Utility; Welfare Economics

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Economic Growth

Economic growth is most commonly defined as the rate of increase in the value of a country's output over a period of time. It is often presumed that economic growth is necessary and valuable to a society because it is accompanied by an improved quality of life for that society's citizens. For example, increased economic growth may allow a society to become better educated. As a result, more effective medical systems will be developed that allow for healthier lifestyles within that society. In this example, societal gains are achieved from both fiscal and health perspectives.

Thoughts About Economic Growth: Then and Now

As a means of gaining a more comprehensive understanding of economic growth, it is instructive to look at the theories of some of the topic's thought leaders over time. This perspective will make it easier to understand the wide array of successful and unsuccessful economic development or growth policies used by various government entities. Although ancient Greeks and Romans demonstrated an understanding of economic security and growth as the foundation for social and political health, most of the discussion about the topic has occurred in the last 250 to 300 years.

Some of the economic writings from the 16th through the 18th centuries dealt with the growth of commerce resulting from European expansion. The Mercantilists sought limitations to trade between countries while expanding their own contiguous territorial or colonial trading systems. On the other hand, one of the most highly regarded anti-Mercantilists was David Hume, who wrote *Political Discourses* in 1752. Hume argued that international trade is not a zero-sum game and that the growth of international trade was directly related to the strength and diversity of the trading partners. Today, the viewpoints of both the Mercantilists and Hume are endorsed by political leaders as they struggle to achieve economic growth in a global economy.

One of Hume's contemporaries, Adam Smith, provided additional thoughts about economic growth when he published *An Inquiry Into the Nature and Causes of the Wealth of Nations* in 1776. Smith's premise was that the self-interest of individuals drives them to compete. This competition will in turn result in the production of goods and services that society wants, in the amounts that it wants, and at appropriate prices.

In other words, it was Smith's belief that an evolving capitalist system, driven by economic growth, would benefit society as a whole. More than 200 years later, Smith's beliefs about growth benefiting society were highlighted in a series of articles in *The Economist* in 2005. The discussion cited examples of how economic growth had improved people's lives, with the production of ample food supplies, the provision of adequate housing, the facility to travel freely, and a sharp reduction in chronic diseases.

In 1798, Thomas Malthus prepared *An Essay on the Principle of Population.* In this writing, he suggested that the population would grow at a geometric rate, while the food supply would only grow at an arithmetic rate. This writing was in direct conflict with a popular notion at that time that a productive society, or one that experienced growth, was a society that maintained a high fertility rate and ultimately a larger workforce. It was Malthus's belief that population growth would decrease output per worker, particularly in agriculture, thus reducing the standard of living. Malthus held the lower class responsible for this situation and suggested that the British government should establish restrictive policies to hold the middle and lower classes responsible for maintaining the proper rate of population growth. To a certain extent, his premise is followed today in certain countries, such as China, which has implemented a policy of one child per family.

In the early 19th century, David Ricardo added to the work of Malthus by suggesting that as economies grow, they will ultimately reach a point where the law of diminishing returns takes effect, forcing the economy to come to a standstill. Karl Marx built on some of these ideas in his criticism of capitalism. Marx and his followers challenged capitalism on social, moral, and economic fronts, pointing out the peaks and valleys of business cycles and the inherent exploitive tendencies of capital accumulation as weaknesses in the capitalistic economic system. Marx believed that communism was a preferable economic system to capitalism because it provided economic growth at a controlled rate, thus eliminating the human suffering associated with class conflict and sharp downturns or recessions. The Austrian economist Joseph Schumpeter offered a more positive assessment of economic turbulence within the capitalist system, arguing that economic growth and change arose from an entrepreneurial gale of creative destruction.

Finally, John Maynard Keynes should be acknowledged for his 1936 publication of *The General Theory of Employment, Interest, and Money.* Through his in-depth analysis of business cycles, Keynes suggested that recessions could be eliminated and economic booms controlled through the selective use of government fiscal and monetary policy. While Marx and Keynes shared the viewpoint that the economy should have fewer peaks and valleys, their methods for accomplishing this goal had different real-world implications for society as a whole.

Determinants of Economic Growth

Economic growth is driven by a variety of factors. By definition, the primary determinants of growth are frequently classified as either factors of production or factors of supply and demand.

Factors of production include natural resources such as land, minerals, or other inputs. Most resources are limited and often scarce. This is in sharp contrast to the unlimited needs and wants of people. For example, countries in the Middle East are rich in oil, yet the long-term demand for petroleum products exceeds the supply of oil in the Middle East and other countries combined.

In addition, labor and human capital are factors of production. It should be noted that there is a portion of the goods and services produced by workers such as housewives or volunteers that is not recorded in the gross domestic product (GDP). A second factor for consideration is human capital, which is the quality of labor resources. Obviously, not all laborers are of the same quality. Their level of production can vary based on such factors as their education, age, training, experience, happiness, health, and family environment.

The final factor of production is capital. While capital can refer to the money used to run a business, it is more frequently thought of as the investment in "capital goods" that can be used to generate other goods. In other words, computers, machinery, and other equipment are purchased and placed in buildings for the creation of specific products, such as automobiles, televisions, and cellular phones. The factors of supply and demand relate to the range of prices and quantities of the resources, the capital goods, and the trained workforce that is available for use in the production process.

It is also necessary to acknowledge the role that technology and technological advancements play in economic growth. While there is no doubt that technology played a major role in economic growth and productivity gains during the late 20th century and early 21st century, there does not seem to be a consensus about how technology should be included as a determinant of growth.

The combination of increased affluence, desires for instant gratification, technological advancements, and growing concerns about built-in obsolescence within a disposable society has altered the demand for goods and services in the more affluent parts of the world. To some extent, desires for a cleaner and safer environment and higher quality of life are being factored into growth expectations. As a result, the factors of production are being looked at more closely, and alternate methods of evaluating economic growth are evolving.

More About GDP Growth

As mentioned previously, the most common measure of economic activity is the GDP. This rate of change in the value of goods and services produced within a country is typically calculated on a quarterly or annual basis. It is also possible to look at real GDP growth, or the change in the value of production with the effect of inflation factored out. The real GDP per capita is useful for comparing economies of different sizes because it provides a measurement of how much each person produces during a designated period. It is calculated by dividing the real GDP by the size of the population. Potential GDP growth is the optimal rate at which an economy should grow. Finally, gross national product reflects the value of goods and services produced by an economy, regardless of where its citizens are located.

The following example describes economic growth in the United States. Table 1 shows U.S. economic growth by decade, based on changes in the GDP and real GDP. The data series, produced by the Bureau of Economic Analysis, was initiated in 1929. It can be seen that the periods of highest GDP growth for the eight periods occurred during the 1940s and 1970s. A closer look at the inflation-adjusted data shows that the decade of the 1970s was actually ranked fifth, below the overall average, with real GDP growth of only 3.2%. The lesson from this example is that it is often instructive to use more than one data set when evaluating economic growth.

Table 1 GDP Growth in the United States Between 1929 and 2005

Period	*GDP (%)*	*Real GDP (%)*
1929–1940	−0.2	1.6
1941–1950	11.2	5.6
1951–1960	6.0	3.5
1961–1970	7.0	4.2
1971–1980	10.4	3.2
1981–1990	7.6	3.3
1991–2000	5.4	3.3
2001–2005	4.9	2.6
Overall	6.5	3.4

Source: Bureau of Economic Analysis.

Other Measures of Economic Growth

A variety of economic growth measures are used at lower levels of government. At the state level, it is slightly more difficult to evaluate productivity. While the gross state product exists, it often has limited use because it is not published in as timely a fashion as its national counterpart and because commerce is not necessarily dictated by state boundary lines. As a result, it may be necessary to look at other measures or a combination of them to monitor changes. Other common means of measuring economic growth in a region or state are to evaluate changes in population, employment, unemployment rates, personal income, per capita income, annual average wages, and retail sales.

Many of these data sets are also available for evaluating geographic areas smaller than states, such as cities, counties, or special districts. In addition, some data sets evaluate economic characteristics specific to the local area. For example, tourism-based economies may focus on the number of hotel rooms occupied, average hotel room rate, rounds of golf played, or number of skier days. Communities that place an emphasis on intellectual capital may look at patents awarded, R&D expenditures, grants awarded, or the number of high school or college graduates. At the local level, factors such as traffic congestion, social service funding, quality of public schools, crime rates, housing affordability, public safety, and air quality are examples of indicators that measure social or environmental welfare associated with economic growth.

Economic Growth, Social Welfare, and Environmental Responsibility

Many discussions about the impact of economic growth automatically assume that the expansion of the economy is good for society and translates into a higher standard of living for the general public. This is an assumption that may not necessarily be true.

For example, during the first years of the new millennium, the business infrastructure of China improved. A review of data from the World Bank reports that the number of aircraft departures, telephone subscribers, and Internet users has risen dramatically. Growth in these and other areas has allowed China to experience real annual GDP growth of 8% to 10%, over twice the annual growth rate of the United States.

In some cases, China's rampant growth has imposed societal costs that have not been adequately addressed or measured. For example, increased energy and electric power consumption has been accompanied by greater pollution. Anecdotal evidence also suggests that growth has occurred without regard to workforce safety, employment security, and environmental sustainability. In addition, unemployment in China during the early 2000s was about 20%, compared with 6% in the United States. This example illustrates that increased productivity, or GDP growth, for an entire country does not necessarily translate into quality-of-life gains for society as a whole; nor does it ensure that the income gap between the rich and the poor is narrowed.

Consider another situation that occurred on June 23, 1969, in Cleveland. On that date, the Cuyahoga River caught fire for at least the third time in less than 30 years. The fire was caused by various forms of human and industrial waste dumped in the river by the city sewage plant and by chemical and petroleum companies that resided on its banks. In the short term, the city waste plant and companies along the riverbank achieved a high level of productivity and prosperity, factors favorably associated with economic growth. On the other hand, the societal and environmental impact of polluting the river to the point that it caught fire should be included in an assessment of the welfare benefits of economic growth.

These two examples suggest that there is value in having a broader, more balanced definition of economic growth. Such a definition might take into account the triple bottom line (measuring social and environmental as well as financial performance), economic stability, and sustainability. It would consider not only the production of goods and services but also any social or environmental impact brought about by their production and delivery throughout the world.

The genuine progress indicator (GPI) is offered by its developers, Venetoulis and Cobb, as a more accurate measure of economic growth than the GDP. This indicator evaluates both personal consumption and the well-being of households. The latter component attempts to measure the social costs associated with the labor force, such as crime, divorce, or loss of leisure time. It also considers the depreciation of the factors of production—in other words, the impact of growth on environmental assets and natural resources. Research conducted by the GPI developers shows that GDP economic growth is substantially greater than the GPI. In this case, pure economic growth is diminished by the impact of societal and environmental factors.

An expanded definition of economic growth could include measurement of efforts to maintain a balance between profits, the planet, and the people affected by the production of goods and services. It might also evaluate the give-and-take between companies within an economy and the members of society.

Finally, consideration could be given to the organization's integrity, transparency, and willingness to be held accountable for the social and environmental impact of its economic actions.

—Gary R. Horvath

See also Capitalism; Development Economics; Economic Incentives; Environmental Ethics; Federal Reserve System; Free Market; Gross Domestic Product (GDP); Gross National Product (GNP); Income Distribution; Invisible Hand; Marxism; Population Growth; Smith, Adam; Triple Bottom Line; U.S. Bureau of Economic Analysis; U.S. Bureau of the Census

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Economic Incentives

A fundamental tenet of economics is that human behavior is explained by the combination of preferences and incentives. Preferences reflect the wants, needs, and desires of humans, while incentives are what actually motivates behavior. If people prefer to maximize their utility (or satisfaction) and if businesses seek to maximize profits, then those things that will result in increased utility or profits are by definition economic incentives. Economic incentives cannot be understood without taking account of preferences. For instance, people who prefer only wealth will likely respond differently to monetary rewards than people who prefer power or social status rather than wealth. When explaining and predicting human behavior, economists assume that preferences do not change. Therefore, changes in behavior are explained by changes in economic incentives. Much of economic analysis involves the study of institutional and organizational structures that give rise to and alter economic incentives.

Incentives can be either extrinsic or intrinsic. Extrinsic incentives are external to a person. These may be monetary rewards, such as cash payments, income, and profits, or they may be nonmonetary rewards, such as peer recognition and fame. In contrast, intrinsic incentives are psychological and, thus, internal to people. Knowing that you will receive a good feeling for doing something right is an intrinsic incentive. Extrinsic and intrinsic incentives often complement each other. People may be motivated to take a certain action because they are paid to do so and because they take pride in performing the work. However, many researchers have shown that extrinsic incentives often crowd out or diminish the effect of intrinsic incentives—for example, volunteerism declines when people are offered money for their services. The classic example here is donation of blood in the United States. In a 1971 book titled *The Gift Relationship*, Richard Titmuss contrasted the voluntary system of blood donation in Britain with the mixed commercialized and voluntary systems in the United States. He showed that paying donors resulted in a decline in voluntary blood donations and an increase in chronic and acute shortages of blood.

If incentives promote behavior, then disincentives discourage behavior. Societies use combinations of incentives and disincentives to motivate people to behave in socially desirable ways. Prizes and social accolades have the function of encouraging people to do things that are in the public interest. In contrast, fines, incarceration, and social ostracism are disincentives designed to discourage socially undesirable behavior. Similarly, feelings of guilt, shame, and regret are intrinsic disincentives for unethical behavior.

Many ethical problems can be explained by the incentives people face. Dishonesty, deception, bribery, theft, fraud, misrepresentation, plagiarism, and falsification are examples of unethical behaviors that can be largely explained by the incentives people face. Some scholars believe that unethical behavior in business is a response to the pressures people face in their employment. If economic incentives help explain why people in business engage in unethical behavior, then economic incentives can also be used to promote ethical behavior.

—Harvey S. James Jr.

See also Motives and Self-Interest; Profits; Utility; Volunteerism

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Economic Liberalism

See Liberalism

Economic Rationality

Economic rationality refers to the conception or conceptions of rationality commonly found and used in economic theory. While there is no single notion of rationality appealed to by all economic theories, there is a core conception of rationality that forms the basis of much economic theorizing. This view of rationality, termed the neoclassical conception of economic rationality, takes rationality to consist largely of the maximization of subjective utility. While it has sometimes been assumed that subjective utility is equivalent to self-interest, these notions are not identical. The notion of subjective utility allows that an agent might have preferences or desires that are not purely self-interested.

This view can be taken as either a normative account of how rational agents ought to act or a methodological assumption used by economists to study and predict the economic behavior of individuals. In either case, it is not meant as a purely descriptive account, since ordinary agents often fail to maximize their own utility. Furthermore, this view can be taken as a global view of rational behavior in general or as a narrower view of rationality in contexts of market exchanges. In either case, the concept of economic rationality treats reason instrumentally, insofar as it merely specifies the adoption of certain means with regard to given ends. This economic theory of rationality has little to say about the proper choice of goals or ends but sees irrationality as primarily a failure to eschew the means most productive of one's chosen ends.

Criticisms of Economic Rationality

The conception of economic rationality as the maximization of interests or utility has been subjected to a number of criticisms, several of which are ethical in nature. For instance, some critics contend that in failing to provide any criterion for the selection of basic goals or ends, the theory fails to discriminate between legitimate and illegitimate pursuits on the part of individuals. While it is true that accounts of economic rationality have little to say about the choice of ends or goals themselves, this criticism, if sound, would not necessarily show that the theory was false but merely that it was incomplete. Thus, many proponents of the economic account of rationality as maximization, particularly when taken in the narrower sense above, see the theory not as a complete account of rationality but solely as a means of understanding the rationality of certain economic choices and decisions that can be supplemented with an independent account of the rational choice of ends.

A more forceful criticism of economic rationality is that this account is intrinsically incompatible with the demands of morality if taken as a normative account of rationality. According to this criticism, in requiring agents to maximize individual interests or utility, the economic account of rationality will necessarily lead persons to violate the interests and/or rights of others. That is, in this view, economic rationality will often recommend immoral behavior when interests come into conflict. Furthermore, even when the theory is merely used as a methodological tool for the analysis of economic behavior, critics see a tendency on the part of economists to begin to view the theory as if it was normative in nature and to use it as a de facto standard of normative evaluation.

Defenses of Economic Rationality

Defenders of the economic theory of rationality have responded in a number of ways. For one, some defenders argue that as long as the narrow scope of the economic account of rationality is clearly defined, it provides the most powerful learning tool available to analyze market behavior. Such an account, they argue, is not incompatible with a more robust account of normative rationality that includes deontological considerations. On the other hand, some defenders of the neoclassical view of economic rationality as a normative account of rationality argue that the pursuit of maximization on the part of individuals will lead to cooperation with others and, through the invisible hand of the market, ultimately to the common good of all. However, the extent to which such a utilitarian defense of economic rationality, even in limited spheres, can alleviate all concerns about moral obligations to others is still the subject of much debate.

Models of Human Rationality

Even those economists who use a very narrow conception of rationality as preference maximization recognize the limitations of applying this notion of rationality to actual human behavior. Such a model of rationality may allow for the resolution of certain theoretical problems and a model that approximates some forms of economic behavior, but human beings often reason in ways that fail to meet the logical demands of this ideal of rationality. As such, some economists have appealed to the idea of bounded rationality as an alternative means of modeling economic behavior. The notion of bounded rationality appeals to the cognitive limitations and psychological factors that influence the less than rationally perfect reasoning of real individuals. The idea of bounded rationality has become central to the discipline of behavioral economics. Behavioral economists seek to incorporate empirical research and experiments from cognitive psychology and related disciplines in developing alternative models of economic rationality. In using empirically grounded representations of decision-making processes, behavioral economists believe that they will be able to model and predict real-world economic behavior better.

—Daniel E. Palmer

See also Bounded Rationality; Cost-Benefit Analysis; Economics, Behavioral; Economics and Ethics; Expected Utility; Invisible Hand; Pareto Efficiency; Rationality; Utility

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Economic Recovery Tax Act (ERTA)

The Economic Recovery Tax Act of 1981 (ERTA) contained numerous provisions that helped businesses and individuals. Businesses were aided by accelerated capital recovery through new depreciation rules, special tax treatment for acquirers of troubled thrift institutions, an increased amount of retained earnings not subject to taxation, relaxed rules for Subchapter S corporations, and encouragement of merger activity. However, ERTA is best known for a large reduction in personal income tax rates across the board. The act also helped individuals through a significant increase in the nontaxable portion of inheritances and gifts and by raising the maximum limits on contributions to individual retirement accounts and Keogh Accounts for the self-employed.

ERTA was the first major legislative activity in President Reagan's administration. He came into office at a time when the U.S. economy was in the doldrums, experiencing a situation called stagflation, meaning modest economic growth during a period of high inflation. ERTA was proposed as a way of stimulating the economy in an approach based on supply-side economics, which holds that increasing productive resources should be the focus of economic policy. The tax cuts were controversial because of their size and the opinion of some that this would reduce federal government revenues and further damage the economy. ERTA proponents relied on an economic theory, the Laffer curve, propounded by the economist Arthur Laffer. It is represented by an inverted "U," which shows federal revenue at zero when tax rates are zero and again at 100%. When tax rates are zero, no taxes are collected. When tax rates are 100%, no one has the incentive to work, so revenues are again zero. According to the theory, along the Laffer curve there is a point where the tax rate can be set to maximize revenue.

The economy did prosper during the Reagan administration, although federal deficits grew during the later years. ERTA was credited as the first major victory of supply-side economic theory. Opponents responded that the economy grew on its normal cyclical track following a recession and would have recovered without ERTA and that the large deficits would burden the economy in the future.

ERTA reduced the highest tax rate from 70% to 50% and reduced the lowest tax rate from 14% to 11%. The act also included a provision to index tax brackets beginning in 1984: As the earnings of taxpayers increased, the brackets would move in proportion, keeping taxpayers with modest increases in taxable income at about the same tax rate.

The accelerated cost recovery system (ACRS) was introduced by ERTA, which changed the recovery period for depreciation from useful life to an amount determined by the Internal Revenue Service. This allowed businesses to recover expenditures for capital development more quickly. ACRS was modified by the Tax Act of 1986 to reduce the impact on federal revenues.

—David D. Schein

See also Supply-Side Economics; Tax Incentives; Tax Reform Act of 1986

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Economics, Behavioral

Behavioral economics uses insights from human psychology to investigate how individuals actually make decisions. In contrast to neoclassical economics theory, which generally posits that individuals are rational decision makers who are capable of maximizing personal welfare, behavioral economics theorists build models of economic decision making that take account of human errors and limitations. The work of early behavioral economics theorists such as Herbert Simon, Daniel Kahneman, and Amos Tversky has applicability for work in business ethics.

Key Ideas From Behavioral Economics and Their Applicability to Business Ethics

Three key ideas from behavioral economics are helpful for the study of business ethics. *Bounded rationality* captures the idea that human beings have limited cognitive abilities that inhibit their abilities to make optimal decisions. Herbert Simon argued that bounded rationality leads to decisions that are perceived to be satisfactory to the decision maker, not optimal. *Framing* suggests that the way a decision is presented to a decision maker affects the kind of decision that is made. Finally, *bounded self-interest* suggests that individuals are not simply selfish personal welfare self-maximizers but are capable of true altruism.

If the idea of bounded rationality is true, then it follows that people making ethical decisions in business might (and likely will often) make mistakes. The ability of any individual to factor in all the possible outcomes of a decision, weigh them against some set of criteria, and then make an optimal decision is limited. Trying to make an optimal decision is also time-consuming. No human being can predict the future with complete certainty, and when the outcomes of a decision are hard to forecast (as is the case with many ethical decisions), then ethical decision making will frequently look in hindsight to have been faulty. Stakeholder analyses, for example, require decision makers to account for stakeholder interests and to use forecast benefits and harms to different stakeholder groups in ethical decision making. But in an environment of bounded rationality, it is possible that a decision maker will either forget to include a stakeholder group or forecast the effects of a business decision on one or more stakeholder groups incorrectly—leading to a suboptimal ethical decision. For the same reason, bounded rationality makes utilitarian analyses of decisions—often used in business—problematic in ethical and instrumental terms.

Framing—the idea that the way in which an opportunity for a decision is presented to a decision maker affects the kind of decision that is made—also is useful for analyses in business ethics. Perceptual frames naturally affect the kinds of conclusions that people come to. For ethical decision making in business, framing suggests that the same decision maker can come to different conclusions for the same ethical dilemma. Organizations that want to promote ethical decision making and are cognizant of framing effects might therefore seek to explicitly include ethical considerations in the analysis and framing of business decisions rather than make a decision that everyone commits to and then ask if the decision is ethical or not.

Finally, bounded self-interest suggests that people are willing to sacrifice their own self-interests to help others without hope of return. While the notion of bounded self-interest might seem to represent obvious common sense, it is controversial within the field of economics. If people are capable of bounded self-interest, then it is possible to appeal to motives other than profit maximization or career advancement. Bounded self-interest suggests that people (say in business) are motivated by a variety of goals: Some of these goals are self interested to be sure, but others might be altruistic. It seems that there might be more freedom for humans to behave ethically within organizations if bounded self-interest accurately describes how most people make decisions.

Implications for Practice

Behavioral economists have sought to bring nuance to analyses of human behavior. People are more complex than the caricature of selfish welfare maximizers, typical of work in neoclassical economics, would indicate. The study of behavioral economics might yield richer analyses of business ethics and ethical behavior.

First and foremost, the idea of bounded rationality raises an interesting question: How can people make better ethical decisions? It is true that the ability of individuals to account for stakeholder interests is limited. But can it be made better, say, through education and training?

Second, framing theory suggests that decisions differ based on how they are presented. Here it might be interesting to speculate on how decisions in organizations can be framed in ways that will bring about more ethical behaviors. Furthermore, the relationship between societal expectations of business and how ethical dilemmas in business get framed merits consideration.

Finally, the notion of bounded self-interest suggests that ethical behavior is possible and even likely in particular circumstances. Organizations can inculcate ethical behavior by appealing to individual goals beyond self-interest—and by extension, organizations themselves can act to achieve a variety of goals, including but not limited to organizational self-interest.

There are significant opportunities for organizations to use insights from behavioral economics to improve ethical decision making and behavior. Similarly, business ethicists would benefit from using the work of behavioral economists to develop better frameworks for channeling the goals and behaviors of businesspeople toward more ethical and socially desirable ends.

Conclusion

More realistic models of human economic behavior have helped better explain why people make the decisions that they do and why those decisions are sometimes wrong. Work in behavioral economics offers cause for hope and for pessimism from the standpoint of business ethics—hope in that people are more than their desires but pessimism in that people often make mistakes in their decision making.

—Harry J. Van Buren III

See also Stakeholder Theory; Utilitarianism

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Economics and Ethics

Studying the complex and evolving relationship between economics and ethics can provide interesting and important insights to improve the theory and practice of socially responsible business management. Economics is concerned with the development and application of positive (i.e., scientific) means to achieve efficient allocation of productive resources to enhance material prosperity and satisfy consumer preferences. Ethics is concerned with the development and application of normative rules to guide human behavior toward realization of the good life, based on expectations of personal fulfillment, fair treatment, and equitable social outcomes. While both efficient and equitable outcomes are desirable and to some extent complementary, they are not necessarily equivalent. This gives rise to the ongoing tension between economic and ethical theory and practice and the recent search for ways in which economics and ethics can better overlap to mutual advantage.

During the late Middle Ages, ethical moralizing took precedence over economic rationalizing as the Church sought to mitigate the impact of economic self-interest on the traditional social order. Calls for a "just price" on life-sustaining goods during periods of famine, as well as a ban on Christians charging "usury" (interest) for moneylending, reflect a theological urge to curb the selfish pursuit of economic gain. Such constraints on self-aggrandizement were deemed necessary to preserve the social fabric while also shielding threatened souls from the temptations that could deny them entry at Heaven's gate. Even so, it is interesting that some Scholastic theologians recognized the complementary relationship between economics and ethics by advocating private property ownership on the grounds of encouraging economic efficiency.

As a notable figure of the 18th-century Enlightenment, Adam Smith offers an intriguing juxtaposition of ethics and economics. His two major works, *The Theory of Moral Sentiments* and *An Inquiry Into the Nature and Causes of the Wealth of Nations*, reflect his simultaneous, seemingly paradoxical, stature as a moral philosopher and as the father of modern economics. Resolution of the "Adam Smith problem" can point toward a potential, albeit partial, reconciliation and integration of ethical and economic modes of thought and action in the 21st century.

This potential arises from a growing recognition that business managers currently encounter difficulty balancing their imperatives to "do well" (i.e., pursue profits) and "do good" (i.e., treat stakeholders in an ethical and socially responsible manner), since they are expected to understand and apply two alternative and seemingly contradictory ways of thinking and acting. R. Edward Freeman launched a search for a more integrative approach to business decision making in 1994, challenging the conventional "separation thesis," which held that the assumptions and methods of economics and ethics must be regarded as logically distinct approaches to sense making and problem solving. A more integrative balance between economics and ethics in business decision making requires consideration of the normative claims of a wider range of stakeholders. However, a more integrative perspective must take into account the continuing contribution of allocative efficiency to human welfare. Such consideration calls for some rethinking of the ways in which facts and values have been employed in the past to make sense of human experience.

Positive and Normative Perspectives

Through much of the 19th and 20th centuries, economics and ethics have coexisted, conceptually and methodologically, as largely distinct fields of study. This distinction arose from the decision to separate facts and values as sources of meaning within the positive and normative traditions of scholarship. Scholars in the positive camp strive to discover an objective reality (the realm of "is") by carefully scrutinizing empirical evidence for cause-and-effect relationships within factual data. The expectation of such scrutiny is a replication of experimental results, which opens up the possibility of prediction and control of natural or social phenomena. Normative scholars strive to characterize the preferred realm of "ought" by extracting ethical norms of socially desirable behavior from universal moral principles, aggregate measures of social usefulness, or context-specific community practices.

Following the publication of Adam Smith's *Wealth of Nations* in 1776, a large and highly influential school of classical and neoclassical economists has striven to elevate their field of study to the status of a positive social science. Today, this branch of the field is called positive economics. It is associated with the ever more sophisticated application of mathematical techniques to the analysis of empirical data, distilled by the *ceteris paribus* (other things being equal) assumption that value-laden "opinions" or "emotions" of human actors must be excluded to allow scientific study of the presumably rational, utility-maximizing behavior of "economic man." This inclination to separate facts from values is reinforced by the seeming fragmentation, since the 18th century, of philosophical approaches to normative scholarship. This has created the impression, especially within the positive camp, that the study of ethics is entangled in arid definitions and abstract, hypothetical, or emotional (and hence value laden) assertions that, even under the best of circumstances, fall outside the realm of scientific inquiry. By adopting the utilitarian assumptions of Jeremy Bentham, positive economists assume that the "greatest happiness of the greatest number" can be determined via a cost-benefit calculus comprehensible exclusively to economic man. Many economists argue that they are concerned with rational analysis of the *means* by which productive ends are realized, without regard for the value-imbued *ends* to which the economic surplus may be distributed.

This entry will suggest that the modern tradition of separating economic analysis and ethical analysis has retarded the development of a more robust theory and practice of socially responsible business management. It will also point to the recent call for a new, more integrative framework for thought and action that transcends the sharp distinction between facts and values and opens up the possibility of bringing closer together the descriptive/scientific realm of "is" and the normative realm of "ought" in business and society interactions. Ironically, the linkage between ethics and economics has a long intellectual history, which achieved one of its fullest and most creative expressions in the parallel writings of the 18th-century Scottish moral philosopher and economist Adam Smith.

Economics, Ethics, and the "Adam Smith Problem"

Early in his *Wealth of Nations*, Adam Smith made the claim—formative in shaping the assumptions of modern economics—that appeals to benevolence are less effective than appeals to self-love in motivating the butcher, brewer, and baker to provide for our supper. It follows that indirect outcomes shaped by the "invisible hand" of the competitive free market tend to serve the public interest better than the deliberate "visible hand" of supposedly benevolent public or private agencies. Some economists and business practitioners, taking this lesson literally, conclude that ethical motivations are irrelevant to economic transactions and relationships. A recent reconsideration of the thought and legacy of Adam Smith, focusing more on *The Theory of Moral Sentiments*, has drawn a different conclusion—that Smith regarded ethical norms and inclinations toward benevolence and law-abiding behavior to be complementary with the economic rationality of self-love in promoting the public good. Thus, Smith, in *The Theory of Moral Sentiments*, concludes that the pursuit of wealth and greatness prompted economic man to seek "mere trinkets of frivolous utility." While Smith accepts self-love as necessary to promote economic growth, he does not consider it sufficient to secure human happiness. It follows that self-regarding and other-regarding motives and actions are complementary. The division of labor generates material progress and an economic surplus, which provides the basis of support for other-regarding institutions and moral sentiments. Legal institutions ensure compliance with market agreements by protecting private property rights and claims that arise from their exercise. However, legal compliance is not sufficient to ensure the effective functioning of a liberal, market-based political and social order. In the absence of a shared moral sentiment that encourages economic actors to exercise voluntary self-governance of their selfish passions out of concern for the rights and interests of others, legal restraints will expand to encompass a Leviathan police state, thereby violating the conditions necessary to support individual liberty and economic prosperity. Thus, moral sentiments are both an outcome of and a precondition for efficient and fair market processes.

For Smith, the shared moral sentiment that can animate in each self a benevolent regard for others arises from a process of empathetic reflection. We can know what others feel only by imaginatively putting ourselves in their position. This enables us to develop moral judgment over time by learning how to triangulate an action we are contemplating from multiple points of view. By imaginatively combining and comparing the views of various spectators, we develop the capability to evaluate and integrate partial perspectives, thereby approaching the moral maturity of an "impartial spectator." The useful fiction of an impartial spectator helps us rein in our selfish and unsocial passions to control opportunistic urges while also enabling us to enjoy the shared benefits of social passions, such as generosity, humanity, kindness, compassion, and mutual friendship.

Successors of Adam Smith, concerned with developing a more positive, fact-based science of economics, tended to forget that market transactions and relationships are not sustainable in the absence of moral sentiments that arise from interaction between the warm workings of the human heart and cool calculations of the head. Thus, the Adam Smith "problem" was the artifact of later economists, who preferred to generalize about a partial view of human nature based on the presumption of self-love without incorporating Smith's complementary emphasis on the role of moral sentiments in facilitating and guiding market processes.

Positive Economics as a Value-Free Scientific Study of Market Interactions

In the early 19th century, the British economist David Ricardo abandoned Smith's judicious, if discursive, blend of historical anecdotes, illustrative arguments, and wry observations about market-based behavior. Ricardo preferred to focus on the long-term consequences of the working out of abstract, a priori economic principles, such as the "iron law of wages," which predicted that wage rates in a competitive labor market would fall to a level of bare subsistence. He discounted the short-term impact of the economic forces of supply and demand on immediate human circumstances, arguing that sentimental concerns about human misery would distract attention from the rationally determined long-term benefits of market efficiency.

Later in the 19th century, Léon Walras elaborated on these assumptions within a general equilibrium model of economic interactions. Individuals and firms engaged in both the demand and supply sides of the equation are subsumed within a complex and highly abstract set of relationships between inputs and outputs. The economic problem becomes a matter of finding mathematically the equilibrium solution to a complex interplay of input and output variables. Utility maximization among market participants is expressed as an equation rather than a value judgment. Indeed, value-laden ethical judgments are allowed in the ceteris paribus world of neoclassical economics only if they can be objectified in behavior that is quantifiably verified by measurable facts. Ironically, Walras was inspired by his father's socialist leanings to develop a model of an economic "engine" that could improve the lot of everyone, including the poor. Thus, the aspiration toward more complementary outcomes from positive and normative modes of analysis persists, even when assumptions and methods seem to be at odds.

Recent Questioning of the Normative-Positive Distinction in Economics

Some prominent scholars have begun to question the separation of facts and values by positive economists. Kenneth Boulding, a leading Anglo-American economist of the mid-20th century, expressed the dissenting view that at the policy level, economics without ethics is like a lever without a fulcrum. Since economic policies can have differential impacts on a wide variety of stakeholders, it would seem reasonable to consider the normative implications of economic policy alternatives, particularly with regard to the issue of social justice or equity.

Welfare economics addresses more directly the normative implications of economic policies; however, it does so by trying to subsume ethical considerations and value judgments into an economic mode of analysis. Amartya Sen's critique of some of the underlying assumptions of welfare economics has been influential in breaking down the positive-normative distinction. A move toward Pareto optimality is defined as a change where productive resources are allocated in a manner that improves the well-being of some without diminishing the welfare of others. Sen questions whether Pareto optimality is necessarily consistent with social justice, since different equilibrium points for the optimal allocation of productive resources are possible. Thus, the location of an optimal point on the production possibilities frontier is conditioned by the original distribution of resources. An extremely unequal initial distribution may result in an optimal solution that is normatively objectionable on the grounds of equity. A Pareto optimal move could improve the welfare of the already better off without diminishing the welfare of the worse off. Thus, Pareto optimality compares absolute differences in welfare without taking into account the relative positions.

Sen also questions the normative-positive distinction in his essay "Rational Fools." He argues that the positive assumption that utility maximization arises from the satisfaction of self-interest is no less a value judgment than is the assumption that human motivation arises out of sympathy or commitment to others. Both assumptions reflect judgment about which values are relevant to the study of human behavior. Thus, either competitive or cooperative behavior can generate utility. Under closer scrutiny, the fact-value distinction starts to break down, and "foolish" other-regarding cooperative behavior can make sense.

Do Economics-Based Management Theories Drive Out Ethical Business Practices?

Agency, transaction cost, resource dependence, and other influential management theories share with orthodox economics the fact-value dichotomy, the homogenizing ceteris paribus assumption that economic man is driven by self-interest, and the aspiration to discover causal patterns that can suggest a "scientific" basis for exercising management control, or more generally for predicting market-based producer and consumer behavior. Thus, agency theory adopts a narrow and (some would say) pessimistic view of human nature, assuming that self-interested motives will lead to shirking and opportunism without governance controls and incentives (e.g., stock options) that bind managerial agents to the interests of shareholders. Such assumptions prompted Milton Friedman's famous dictum that the true corporate social responsibility of business managers is to pursue profitability "within the rules of the game," which includes both law and ethical custom. Morality in the economic sphere may well boil down to obeying the law, avoiding deception and fraud, and living up to contractual agreements. However, critics insist that morality cannot be subsumed exclusively within the economic sphere; morality also involves a balancing of responsibilities across overlapping, value-laden economic and noneconomic spheres of social action. Thus, the unitary objective function of profit maximization to enhance share value (and trigger the exercise of stock options) may have achieved broad acceptance in the business world not so much because it reflects an objective reality as because it privileges powerful ownership interests. In addition, profit maximization is easier to model mathematically than the more complex, interdependent relationships within pluralist stakeholder networks. The positive stance holds that management theories must necessarily be amoral, since morality or ethics is inseparable from human intentionality. Since human intentionality arises out of mental states, which are necessarily value laden and idiosyncratic, proponents of management "science" are forced to exclude mental states because they are not subject to measurement and, hence, prediction and control. The recent spate of corporate scandals have been attributed to top management's preoccupation with a narrowly defined bottom-line performance and to the perverse application of management incentives such as stock options to achieve this financial performance, without regard to their effects on other stakeholders. Thus, some argue that management theory must move away from its envious emulation of natural science assumptions and methods and embrace the value-laden pluralist position that business organizations will perform best overall when they take into account the values, interests, and concerns of their multiple stakeholders. This more integrative stand, which requires recognition of the interdependence between economics and ethics and the relevance and legitimacy of different approaches to sense making, can be construed from Adam Smith's insight that self-regarding market behavior is not sustainable in the absence of other-regarding moral sentiments embedded within community relationships. Thus, the Adam Smith problem can be reconfigured as an Adam Smith–inspired solution.

Getting Past the Separation Thesis

In 1994, R. Edward Freeman, a leading proponent of stakeholder theory and of critical and feminist theory perspectives on business ethics, issued a call for business ethics and business and society scholars to abandon the prevailing "separation thesis." This conventional distinction between ethical and economic rationality bifurcates management theory into the normative, value-laden realm of "ought" and the positive, fact-based realm of "is." Standard management practice calls for economic rationality to prevail in business operations until an ethical dilemma or stakeholder confrontation triggers the exceptional and temporary intervention of an alternative logic of ethical rationality. Freeman and others argue that this bipolar swing between "normal" amorality and exceptional morality in business decision making imposes unacceptable risks and costs not only on society but also on business organizations, which can no longer afford this reactive, occasionally accommodative stance toward their stakeholder relationships and responsibilities.

The search for an integrative alternative to the separation thesis is diverse and riddled by paradox, since multiple stakeholder perspectives, values, and voices flow into a pluralist and unfolding/developmental sense-making process in which facts and values are intermingled and fused. Two leading contemporary normative approaches associated with this rejection of the separation thesis are the integrated social contracting theory (ISCT) of economic ethics and neopragmatism. The ISCT is designed to provide business managers with a comprehensive arsenal of universal "macrosocial" ethical norms, such as obligations of promise keeping and expectations of reciprocity, as well as context-specific "microsocial norms" that specify ethical business practices within the moral free space of particular economic communities. A criticism of the ISCT is that it tends to accept prevailing macrosocial and microsocial ethical norms as given. It does not specify the dynamic social contracting processes, especially at the microsocial level of particular communities, where ethical norms can evolve over time. Neopragmatism is less inclined to specify normative rules. It envisions a pluralist contest of competing stories, which achieve normative justification not from an appeal to an "essentialist" or absolute source of moral truth so much as from the pragmatic test of whether the story helps mankind, or particular communities, move toward shared visions of the "good life." Thus, Richard Rorty, a leading neopragmatist moral philosopher, argues that the world needs more poets to tell better and more imaginative stories to spark in us an imaginative sympathy for others that can help guide us toward better relationships and the good life. Neopragmatism is vulnerable to the charge that it may open the way to ethical relativism or normative nihilism. The matter of who decides on what constitutes the best poem about the good life remains an open question.

Recent developments in the theory and practice of global corporate citizenship may overcome some of the limitations and thereby help realize the full integrative potential of the ISCT and neopragmatism. The campaign for global corporate citizenship practice calls on corporate managers to embrace a more integrative, systems-based perspective in defining and fulfilling their managerial responsibilities. This would involve replacing the unitary emphasis on profit seeking on behalf of shareholders with a more pluralist emphasis on improving relationships with multiple stakeholders. "Business as usual" managerial assumptions and methods can still apply when market conditions are relatively stable and predictable. However, a "messy" complex and interdependent problem, such a coping with the human rights implications of sweatshop conditions among a firm's developing country subcontractors, could summon up a shared problem domain occupied by a number of contentious, potentially obstructionist stakeholders. Given this pluralist concern and community discord, managers are encouraged to think of the corporation as a citizen within an extended stakeholder network or community. As network citizens, corporate managers are encouraged to convene a community conversation and engage with other stakeholder representatives in exploring different perspectives on the nature of the problem. Such multistakeholder learning dialogues can be helpful in finding common ground, which can serve as the basis for cooperatively working on the problem. Thus, in 1997, Nike managers engaged with representatives of other affected apparel manufacturers, governments, and human rights and labor nongovernmental organizations to develop a voluntary "no sweat" industry code of conduct.

Such voluntary international codes of conduct define standards of corporate citizenship practice, thereby opening up the prospect for increasing transparency and holding corporations accountable to stakeholders for their social and environmental performance. The Global Reporting Initiative is an effort to extend this approach to developing and enforcing voluntary codes in multiple industries around the world. Expanding the definition of corporate performance to encompass a "triple bottom line" of financial, social, and environmental performance is at the heart of the effort to incorporate normative value considerations into corporate decision-making processes. Developing such codes of conduct and devising methods for measuring and enforcing voluntary standards are outgrowths of multistakeholder learning dialogue and engagement. This process of engagement calls on participants to place themselves imaginatively and empathetically inside the minds, hearts, and shoes of others as a precondition for finding common ground. Such imaginative sympathy for the plight of others is the essence of the moral point of view. A true triple-bottom-line approach must also embrace self-interested behavior, profitability, and economic growth as necessary complements of a sustainable corporate citizenship practice.

Conclusion

Adam Smith recognized that moral sentiments are necessary complements of rational self-interest within liberal market societies. This insight still holds in the more complex, networked world of the 21st century. Economists and ethicists are struggling to understand and apply this insight to contemporary management theory and practice. By recognizing the need to move beyond the conventional separation thesis that frames the normative and positive dimensions of conventional business practice, some economists and ethicists and scientists and poets continue to search for common ground in the minds and hearts of managers.

—Jerry M. Calton and David L. Hammes

See also Agency, Theory of; Corporate Citizenship; Corporate Social Responsibility (CSR) and Corporate Social Performance (CSP); Economic Efficiency; Ethics of Dialogue; Global Reporting Initiative; Kantian Ethics; Nike, Inc.; Pareto Efficiency; Positive Economics; Positivism; Postmodernism and Business Ethics; Pragmatism; Social Capital; Stakeholder Engagement; Stakeholder Theory; Triple Bottom Line; Utilitarianism; Welfare Economics

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Economics of Well-Being (Post-Welfarist Economics)

Welfare economics seeks to evaluate the acceptability of alternative economic choices by examining their effects on the sum total of individual utilities. A limitation of this approach is that utility functions are ordinal concepts; their use is based on the assumption that individuals can rank alternatives but they cannot take into consideration the intensity of satisfaction they derive from them. Consequently, the utilities of individuals or groups cannot be directly measured and hence compared. For example, the utility of a corporate executive cannot be compared with the utility of a rural dairy farmer. This restricts the types of problems welfare economists examine so that concerns such as justice and equity are largely ignored. This means that while the level of income enters into a welfare economics analysis, the distribution of income does not. For instance, increasing a person's income can be welfare improving. However, transferring income from a wealthy executive to a poor rural farmer might not be welfare improving. The reason is that it is not obvious that the pretransfer utility of a rural dairy farmer is less than the utility of a wealthy corporate executive.

Post-welfarist economics is based on the premise that people form subjective valuations of their well-being. Although happiness might be important to people, it is not the only thing of value—justice, relationships with others, and equality might also be important to people. Consequently, post-welfare economics attempts to incorporate ethical considerations and constraints into the evaluation of alternative economic choices. For example, if justice is important to people, then they might be willing to give up material wealth in exchange for improved fairness in the economic system. This has implications for economic policy analysis because factors other than economic growth might be more desirable to people.

Post-welfare economics also accepts the subjective statements of individuals regarding things that are important to them. This means that researchers can measure the well-being of individuals through surveys or personal interviews. For instance, a survey might ask respondents to indicate how satisfied they are with their lives or how happy they are. Post-welfare economists accept these statements as meaningful measures of personal well-being, thus establishing the foundation for empirical studies designed to identify factors correlated with self-reported subjective well-being.

An important question in post-welfare economics is whether money buys happiness. Research has shown that income is positively correlated with reported well-being, at least up to a point. At low levels of income, subjective well-being increases as income increases, but at high levels of income, reported subjective well-being does not increase and has even been found to decrease slightly. For this reason, some scholars believe that relative wealth is more important for subjective well-being than absolute levels of wealth. In other words, people might report an increase in well-being only when their income increases more than their neighbor's. From a policy perspective, this means that raising one person's income might make that person happier, but raising everyone's income might have no effect on reported well-being.

—Harvey S. James Jr.

See also Utility; Welfare Economics

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Economies of Scale

A production process has economies of scale when the cost to produce each unit falls as the quantity of output increases. Some of the reasons why costs may fall when production quantity increases include volume discounts for supplies, longer utilization of equipment without downtime, increased time for learning to improve process expertise and quality, and enhanced productivity from resources (such as labor or capital equipment) that do not need to increase at the same rate as the quantity of production output. Each of these reasons explains, for example, why it costs less per car to produce many cars in an automobile factory than it does to produce just a few cars.

Ethical issues associated with *economies of scale* include honest measurement and equitable assignment of cost burdens, commutative and distributive justice, social responsibility, and management-labor relationships. The validity of the relationship between *economies* and *scale* assumes that all production costs are accurately quantified and all costs created by the production process are assigned to the process. Economies of scale may be apparent but not real—for example, if pollution costs are not completely measured or if they are borne by society rather than by process owners.

Commutative justice, or buyer-seller exchange relationships based on fairness, calls for the availability of information and knowledge in the marketplace. In a market for goods produced in processes characterized by economies of scale, sellers may consider if commutative justice requires informing current buyers that future unit costs will be lower as production scale increases. For example, sellers can factor into current prices both the current costs and the lower future costs.

While commutative justice suggests that the market should receive true and complete cost information, distributive justice calls for the value created by lower production costs to be equitably shared among a broader set of stakeholders. For example, the value of cost savings derived from economies of scale may be distributed as profit to equity owners or as wage increases to labor, two important stakeholder groups.

Processes characterized by economies of scale may increase their resource usage as they scale up but without increasing the overall contribution to social development. For example, if toy production scales up and increases its usage of plastic, then the cost of plastic may increase for other uses, such as the production of medical devices.

Managers must increase their application of coordination, monitoring, and control functions for business operations to achieve the potential cost efficiency offered by economies of scale. At the same time, ethical issues associated with management-labor relationships go with the increased scale of management functions.

When economies of scale are present, organizations that produce more output may come to dominate markets and communities. When this happens, it causes an increase in sensitivity to social responsibility and citizenship behaviors of large organizations, particularly concerning pollution, contribution to social infrastructure (e.g., community water, roads, and schools), boom and bust employment during business cycles, and business influence on government.

—Greg Young

See also Barriers to Entry and Exit; Commutative Theory of Justice; Economic Efficiency; Market Power; Opportunity Cost; Profits; Public Goods; Resource Allocation; Social Efficiency; Unintended Consequences, Law of

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Efficient Markets, Theory of

The theory of efficient markets postulates that in a well-functioning capital market, the best estimate of the value of a financial security is today's price. This relationship holds because the current price of an asset reflects all the information available to buyers. According to the efficient markets hypothesis (EMH), stock prices change only when new information becomes available or discount rates change. In defense of the theory, EMH advocates point out the so-called random walks of stocks and (more generally) securities through time; that is, price changes are unpredictable because prices respond only to *new* information (and the newness of information, by definition, makes it unpredictable). In case of investor disagreements about the value of a security, share price valuations will converge around the "true value" over time because either incorrect valuations disappear due to a presumed process of natural selection (learning) or arbitrageurs interpret information correctly and can profit from these disagreements among investors. Overall, these market dynamics decrease market volatility, which is a central prediction of EMH. Furthermore, EMH predicts trading volumes in financial markets to be limited because rational investors cannot agree to disagree when they have the same information.

The general definition and explanation of EMH above are most consistent with the semistrong form of EMH: Current market prices reflect all *publicly* available information. Other forms are the weak form (all information contained in past price movements is fully reflected in current market prices) and the strong form (current market prices reflect all pertinent information, whether publicly available or privately held). Studies generally found that whereas the weak form and the semistrong form of EMH typically hold, the strong form generally receives little or no empirical support. These conclusions about strong-form EMH are supported by the fact that inside traders are able to make abnormal profits.

The theory of efficient markets has had a lot of success since its conception and further theoretical development by, among others, Eugene Fama and Myron Scholes. EMH became widely known after Fama's seminal article in 1970. Over time, it was widely accepted as the orthodox model of academic finance and spawned the options-pricing model that created the derivatives industry. Moreover, investment strategies tied to indexed funds are a manifestation of the idea that no investor can consistently second-guess or outperform the market.

Undoubtedly, this latter implication of efficient markets theory usually holds: It is very difficult for any investor to beat the market consistently. However, there is no empirical evidence that markets are always right or that market prices represent rational assessments of fundamental values. Behavioral finance scholars, such as Robert Shiller, Andrei Shleifer, and Hersh Shefrin, have shown to what extent psychological heuristics and biases can affect buyers' and sellers' behaviors and, thus, make markets less than efficient. Specifically, irrational exuberance can first lead to an overpricing of securities, which in turn may lead to various drastic reactions to such mispricing, such as investors' panic selling. This happened, for example, in the stock market crash of 1929 and the bursting of the dot-com bubble at the turn of the millennium. (Peter Garber pointed out that the most famous market bubble, the 17th-century tulip mania in Holland, should actually not be regarded as an example of irrational mispricing.)

Research that casts doubt on the validity of EMH has wide-ranging implications for business ethics. If markets are not efficient, market prices cannot really reveal the intrinsic value of securities at any particular moment. In a broader sense and in contrast to arguments by Ayn Rand and others, market prices are not revelatory of value in moral terms if markets are inefficient due to the irrational behavioral dynamics of most market participants. This would cast doubt on the frequently presumed equivalence of "value in/for society" and "economic value." According to Shiller, opinion leaders may also have a moral obligation to direct the public's attention to possible over- and underpricing errors.

In sum, there is growing evidence that markets can be irrational and inefficient. The new and expanding area of behavioral finance shows human psychological responses and emotions to be important in pricing. This evidence seems to undermine the previously broadly held assumptions of EMH. At the same time, there are also several methodologically sophisticated studies demonstrating the validity of EMH. The field has yet to reach firm conclusions, but the most accurate view might be the middle-ground position that the extent of the validity of EMH depends on the nature of the stock concerned. When stocks can be categorized easily in industry classifications, conditions may in fact approximate the postulates of efficient markets theory. However, when a stock cannot be easily classified, it becomes more difficult for investors to interpret information about it. This cognitive uncertainty in the market may increase trading volumes and stock volatility to levels beyond those predicted by EMH. In other words, either extreme view of the market (as either highly efficient or highly inefficient) is most likely false; the truth most likely lies in between this dualism set up by orthodox finance theory and behavioral economists and may depend on a variety of contingencies, or scope conditions, which future research may reveal.

—Marc Orlitzky

See also Economic Efficiency; Economic Rationality; Financial Derivatives; Free Market

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EGALITARIANISM

Egalitarianism suggests that there should not be different levels of equality or preference given to some. Inequality violates the basic notion of the same rights for each person irrespective of one's education, occupation, age, ethnicity, or social class. The core idea of egalitarianism is the view that all humans are equal and should be treated as equals not only in terms of political rights but also in the allocation of resources. This is true not merely with respect to property and other forms of wealth but in political, social, cultural, and other aspects of life as well.

The English word *egalitarian* is derived from the French word *égal*, meaning equal. In this entry, five main topics will be considered, beginning with a definition of egalitarianism. A brief history of the term is followed by a discussion of the various different types of egalitarianism. A critique of egalitarianism will be provided, along with an analysis of the case for egalitarianism.

Egalitarianism Defined

Egalitarian doctrine essentially advocates equality of some sort, although there is considerable diversity in egalitarian theory and practice. Equity in business dealings and equality of corporate opportunity would certainly be hallmarks of business or corporate egalitarianism. No one should receive unfair preferential treatment, according to egalitarian philosophy.

Specialized, field-specific definitions may also be consulted. According to one respected perspective, egalitarianism is the moral principle espousing the belief that all human beings are and should be treated the same. All persons should be treated equally in some respects. Similarly, egalitarians believe that everyone is fundamentally and essentially of equal worth and moral status. In the Western European and Anglo-American traditions, the most significant influence on this thought is the Christian concept that God loves everyone equally. Egalitarianism must be considered to be a protean doctrine, because there are numerous types or categories of equality.

Egalitarian History

Egalitarianism has been an evolving concept subject to diverse interpretations. It is appropriate that the term *egalitarianism* is French in derivation, as the French revolution was probably the first modern manifestation of the philosophy. The Englishman John Locke may have supplied one of egalitarianism's initial modern foundations with his idea of moral rights. In the mid- to late 1600s, Locke contended that all people should have equality of moral rights, which he termed "natural rights."

Marxism, and its corollaries socialism and communism, represented the next major step in the history of egalitarian thought. Karl Marx's socioeconomic studies in the late 1800s realized that complete revolutionary structural change would be necessary in the industrialized nations to achieve the Marxist goals of common ownership and collective economic enterprise. Both socialist and communist political philosophy has been used to guide governments in the 20th and 21st centuries in Cuba, Eastern Europe, China, and the former Soviet Union, with very limited success.

A third noteworthy development in egalitarian thought involved the work of John Rawls. According to Rawls, there are "primary social goods" of basic importance, which should be equally available to everyone. The two most important aspects of egalitarian philosophy, according to Rawls, were as follows: (1) All persons have equal citizenship and personal liberty rights, and (2) the only justified exceptions to an equal division of income and rewards would be those helping the most disadvantaged, and only if offices and positions of leadership were equally accessible to every possible aspirant. Rawls's work on egalitarianism is still considered important and influential egalitarian thought.

Different Types of Egalitarianism

Egalitarianism is often mentioned with respect to social and political rights and economic privileges, but there are also other types of egalitarianism, as this theory can be applied to many specific domains. These areas include economic egalitarianism, moral egalitarianism, legal egalitarianism, political egalitarianism, gender egalitarianism, racial egalitarianism, and asset-based egalitarianism.

Economic Egalitarianism

Economic egalitarianism or material egalitarianism refers to the notion that people should be and/or are equal with regard to material possessions. Political movements such as communism, socialism, and Marxism developed from the central egalitarian idea that all people in society are created equal and that all humans should have economic equality. Social control of resources is necessary to avert the usurpation of vast amounts of wealth by the wealthy. With equal distribution, there is no room for economic inequality, thus solidifying economic egalitarianism. Economic egalitarianism is incompatible with capitalism and free enterprise economic systems.

Moral Egalitarianism

Moral egalitarianism suggests that all people are equal with regard to each person's intrinsic individual moral worth. Although people have different moral backgrounds and religious beliefs, each person has the same moral worth as another and should be treated with an equal amount of respect and dignity. Moral egalitarianism contributes to many religious ways of thinking.

The principal idea of moral equality is one of equal dignity and respect, an ideology that is widely accepted as a standard of Western civilization. In fact, the basic idea of equal respect being paid toward all humans is a standard for religions and schools of political and moral culture worldwide, including Christianity, Islam, and Buddhism. A business operated under this philosophy would treat all customers and clients exactly the same, without substantial dissimilarities in prices, discounts, terms, or other preferential business practices.

Legal Egalitarianism

Legal egalitarianism asserts that all people are equal under the law. One of the prominent portions of the U.S. Declaration of Independence includes the moral and legal aspects of egalitarianism with the main philosophy, "All men are created equal." Without the foundation of egalitarianism, the modern civil rights movement could not have advanced thus far in society.

Most contemporary American businesses probably already assume a legal egalitarian philosophy as the basis for their corporate legal posture. Examples or manifestations of legal egalitarian philosophy in the corporate world would involve policies as different as equal opportunity employment practices and corporate benevolence and charitable giving. Emphasis on legal equality is both natural and commonplace in the corporate environment.

Political Egalitarianism

Political egalitarian philosophy advocates the belief that all people are equal in political power or influence. Political egalitarianism is considered by some to be the founding principle of democracy. It is essentially a political doctrine above all else.

Political egalitarianism played a key role in women's suffrage and the civil rights movement. Political egalitarians believe that each person should hold an equal vote in political power. This is an important basic belief in democracy because every person has the right to vote in all elections and every person's vote will count equally toward determining who wins and who will govern. An organization conducted in accordance with political egalitarian values would prize participatory decision making and encourage employee empowerment enterprises.

Gender Egalitarianism

Gender egalitarianism asserts that both genders should be treated equally. Gender egalitarianism was publicly advocated during the equal rights movement and the women's suffrage movement in the United States. The suffrage movement sought women's right to vote; women's right to own property; and equal rights and opportunities in employment and education, with equal pay.

Racial Egalitarianism

Racial egalitarianism perceives biological equality among the human races. This was an especially important concept during the civil rights movement in the United States during the 1950s and 1960s. During that time, African Americans and other minorities in America fought to abolish public and private acts of discrimination against minorities. The civil rights movement was similar to the women's suffrage movement in that both sought equal rights to vote, own property, and receive identical or comparable opportunities in work and education, including equal pay. The American Jewish community empathized with and supported the civil rights movement.

Racial egalitarian policies in business might involve fair employment, diversity, and human resources issues internally and racially sensitive marketing practices externally. Racist tendencies have been noted in the American workplace in a variety of contexts and situations. Since both individual and group-oriented egalitarian concerns are present in cases like this, these can be complex and potentially litigious situations.

Asset-Based Egalitarianism

Asset-based egalitarianism involves the sudden acquisition of vast amounts of wealth, such as through inheritance or corporate transactions. The doctrine states that equality can be made possible by a redistribution of resources, usually in the form of a grant. In an economy where asset-based egalitarianism is an actual policy, the redistribution of wealth is provided by giving everyone a lump sum of money, usually at the age of majority. Inheritance is a significant point of controversy in discussions between egalitarian-minded people and their critics.

Some national governments have practiced asset-based egalitarianism. Both Saudi Arabia and Venezuela have distributed oil-generated annual stipends to their citizens. While the motivation behind these policies probably did not involve egalitarian philosophy, the net effect of these payments is to improve the standard of living of all citizens by an equal amount.

Critique of Egalitarianism

At first sight, egalitarianism would seem to be a desirable goal for our modern world to achieve. As time moves on, the gap between people who have "value" to society and those who do not grows deeper. Some people are born into wealthy families and never have to work a day in their lives, while most others must work their entire lives to attain a meager standard of living.

The issue that many philosophers take with the primacy of equality in egalitarianism is that the doctrine merely advocates equality or near-equality between people without a solid understanding about what that equality gives us. In this section, two criticisms of egalitarianism will be voiced: (1) Egalitarianism is not necessarily progressive or beneficial, and (2) egalitarianism conflicts with other values.

Egalitarianism Is Not Necessarily Progressive or Beneficial

Egalitarianism must be considered a controversial concept in social and political philosophy, in light of the contentious issues confronting its advocates and critics. A major initial problem with this belief system is that egalitarianism, in the strictest sense, is not at all concerned with the well-being of people. It is more concerned with the fact that every human is equal.

The principles of equality that egalitarianism advocates do not *necessarily* mean that everyone should get to live in beautiful houses, have access to high-quality medical care, and eat three square meals a day. Egalitarianism advocates equality between people, which means that it would fulfill the concept of egalitarianism just as well if everyone were emaciated and starving, without any sort of medical aid or shelter. As long as *everyone* is emaciated and starving, the core principles of egalitarianism would be fulfilled.

This argument has been consistently noted by critics: A society that facilitated formal egalitarian philosophy might conceivably do so by providing a harsh and generally grim standard of living for those who are unsuccessful in the individual Darwinian competition for an advantageous position at the workplace and in society. In fact, if a perfect meritocracy satisfied the rigorous Rawlsian equality standard of the fair opportunity principle, it might impose the same harsh and grim conditions of life on those lacking marketable merit and salable skill. It is important to note that Rawls's concept avoids "harsh and grim" conditions through voluntary and self-organized collective society, as common activity is negotiated and pursued for mutual individual advantage.

Egalitarianism Conflicts With Other Values

Egalitarianism cannot be fully realized without conflicting with other important Western values, because of the relatively extreme nature of the concept. One such value conflict would place the parental values of helping one's children squarely in a clash with the basic tenets of egalitarianism. Some parents have considerable resources to facilitate the education and intellectual development of their children, while others lack those means to assist their offspring. The traditional interaction of parents with their children thus becomes an obstacle to the achievement of equality of fair opportunity.

Taken in isolation, egalitarianism is attractive because it emphasizes notions of equality and fairness that are traditional human values. The trouble is that one cannot take a political philosophy such as egalitarianism in a vacuum, because it must coexist in a world with other, mutually exclusive values. Egalitarian doctrine does not favor personal initiative, nor is a strong individual work ethic valued, because they lead to positions of advantage for some. No one wants to be disadvantaged in any way, but does that mean that others should not be advantaged?

The Case for Egalitarianism

The philosophical criticisms of egalitarianism could arguably be wrongly directed by focusing too much on the material well-being of humans. Most of the critiques that philosophers direct at the concept of egalitarianism end in assuming that egalitarian beliefs focus only on the value of what we attain in our lives and what kind of family we are born into. However, the values that egalitarianism promotes are never clearly defined as being only wealth, power, and material goods.

—Dirk C. Gibson, Tabatha Roybal, and Marc Olivas

See also Absolutism, Ethical; Affirmative Action; Age Discrimination; Animal Rights; Buddhist Ethics; Capabilities Approach; Capabilities Approach to Distributive Justice; Capitalism; Christian Ethics; Commonsense Morality; Communism; Darwinism and Ethics; Disability Discrimination; Diversity in the Workplace; Employment Discrimination; Equal Employment Opportunity; Equality; Equal Opportunity; Fairness; Gender Inequality and Discrimination; Human Rights; Intergenerational Equity; Justice, Distributive; Justice, Theories of; Libertarianism; Locke, John; Marx, Karl; Marxism; Natural Law Ethical Theory; Preferential Treatment; Racial Discrimination; Rawls, John; Rawls's Theory of Justice; Redistribution of Wealth; Rights, Theories of; Social Capital; Socialism

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Egoism

Psychological Egoism

Psychological egoism (sometimes called descriptive egoism) claims that every individual does, as a matter of fact, *always* pursue his or her own interests. In other words, it claims that people never act altruistically for the good of others or for an ideal. Since psychological egoism claims to state what is the case, it is a descriptive theory and so is very different from a normative theory such as ethical egoism, which purports to say how people ought to act.

Psychological egoism seems to rest on either confusions or false claims. If self-interest is interpreted in a narrow or selfish sense, then psychological egoism is simply false. There are clearly many generous people who often sacrifice their own interests, including their money and time, to help others. Indeed, most of us are generous on some occasions. Some defenders of psychological egoism admit this fact but claim that it is irrelevant because even a person who is generous is acting on his or her *own* desire to be generous and, hence, is really being self-interested. The problem with this defense of psychological egoism is that it reduces psychological egoism to a logical necessity; the motive for any action must be that agent's motive—this is logically necessary, for obviously it cannot be someone else's motive. Other psychological egoists argue that what appear to be generous motives are always a front for some hidden self-interested motive. For example, Mother Teresa was really, they claim, motivated by a desire for fame or respect or a desire to get into heaven. The problem with this form of psychological egoism is that there is no reason to believe it is true. It is mere speculation and must always remain so since we can never have access to a person's "genuine" motives. It may be believed mostly by people who are generalizing from their own ungenerous character.

A final form of psychological egoism rests on a confusion regarding the nature of desires and motives. Some psychological egoists argue that whatever selfish or generous desire motivates us, what we really want is the pleasure of satisfying our desire; thus, all human motivation is really self-interested. This misunderstanding was laid to rest in the 18th century by Bishop Joseph Butler and others, who pointed out that a person needs to have generous desires in the first place in order to get any pleasure from satisfying them. They also pointed out that supposing we have a second-order desire to fulfill our desires is redundant and involves an infinite regression.

Ethical Egoism

Ethical egoism is very different from psychological egoism. Ethical egoism is a normative ethical theory that claims that every individual ought to *always* pursue his or her own self-interest and only his or her own interests. An ethical egoist believes that people should never altruistically pursue the good of others and that people should never make personal sacrifices for an ideal. Ethical egoism is not limited to a person's economic interests but applies equally to all types of interests a person may have, such as family interests, love interests, religious interests, and so on.

Advocates of ethical egoism often view it as a fundamental moral principle that cannot be justified using any more basic moral assumptions. However, there have been some attempts to make ethical egoism morally plausible, the best-known being Ayn Rand's claim that putting the interests of other people before one's own is demeaning and humiliating and does not show proper respect for oneself. According to Rand, if people have a morally proper concern for themselves, they will always consider themselves first.

Several aspects of ethical egoism require clarification. First, it needs to be emphasized that a belief in ethical egoism does not prevent a person from being cooperative with others. If the egoist benefits from cooperation, then he or she is required by his or her moral belief in egoism to cooperate. This is true not just of cooperating directly with other people but also of cooperating with social rules, norms, and ethical customs; if following the rules or norms will pay off for the egoist, then he or she ought to follow the rules. Perhaps an ethical egoist ought to defect in a one-shot prisoner's dilemma or be a free rider when there is no chance of being caught, but life rarely resembles such situations. A good egoist is always concerned for his or her reputation for honesty and cooperation because it is generally in a person's interest to be accepted as a part of cooperative endeavors. It can be argued that even in situations when one's reputation with others is not at stake (such as in a highway service center one does not plan to visit again), an egoist has an interest in preserving the habits of honesty, politeness, and cooperation. The human ability to detect liars and cheats is sufficiently subtle so that egoists who want to be thought of as honest and cooperative serve their own interests best by always cultivating the social virtues, even when among strangers. It can be argued that it is generally in a person's interests to have an honest personality as well as a reputation for honesty. An egoist will guard against the corruption of his or her character. In fact, if virtue ethicists are right in saying that cultivating the virtues is an essential part of human happiness, then ethical egoism from the broadest perspective would be compatible with virtue ethics.

Ethical egoism should not be thought to advocate selfishness. Ethical egoists advocate that we pursue our own interests, but they often do not claim that our interests are narrowly selfish. Most people have genuine interests in their family, friends, community, nation, and religion, among other interests. They do not just want these to thrive so that they will themselves benefit; they have direct interests in many aspects of society even when no personal advantage can result. Furthermore, some egoists point out that many people are inherently generous, which gives them an interest in helping others, not just an interest in mutually beneficial cooperation with others. Most ethical egoists include satisfying social desires and generosity as part of pursuing their self-interests.

A similar point can be made about narcissism; excessive attention to oneself is probably suboptimal from an egoist point of view. A thorough pursuit of one's own interests requires that one's calculations take into account the larger picture, including other people's interests and emotions, their likely behavior and reactions, social rules, laws, politics, and so on. Nor is it likely that an egoist will benefit from excessive self-regard, lack of self-awareness, or obsessive ambition, even though such characteristics are often loosely associated with egoism.

Numerous objections can be raised against ethical egoism. These include claims that as a fundamental moral principle, ethical egoism is plainly wrong; that people have a purpose in life other than just pursuing their own goals; that we have moral obligations to other people and not just to ourselves; that there are universal moral principles that prohibit some egoistical actions; that altruism is a moral duty that extends beyond feelings of generosity; and that ethical egoism misuses moral language and violates our most basic moral intuitions.

These are powerful objections to egoism in its pure form, but rejecting egoism altogether violates the common moral intuition that pursuing one's own interests is often morally permissible or even required. A compromise position might be to accept what can be called constrained ethical egoism. It is important to note that constrained ethical egoism as discussed here is not a form of ethical egoism as that phrase is usually used; it uses the word *egoism* in its ordinary meaning and appeals to many people's intuitions about egoism and the ethical limits of egoism. It is, however, some sort of normative egoism insofar as it maintains that people *ought* to pursue their own interests, albeit within constraints, and not just that it is permissible to do so. Possible constraints on egoism are either some religious or deontological moral principles or the more simple constraint of not doing serious harm.

A deontological moral theory labels certain types of actions as unethical regardless of their consequences. The moral principles of many religions are of this type. Immanuel Kant's categorical imperative is the most sophisticated philosophical deontological theory we have. Constraining ethical egoism by the categorical imperative would give this principle: Everyone ought to pursue his or her own self-interest by any action that does not violate the categorical imperative. Since the categorical imperative is clear (or so Kant claims) on what actions are unethical but vague about the purpose of human actions, this form of constrained ethical egoism is possible.

A simpler form of constrained ethical egoism may be this principle: Everyone ought to pursue his or her own self-interest by any action that does not cause serious harm to anyone. What constitutes "serious harm" may be vague, but at a minimum it would include death, physical harm, or psychological trauma. The seriousness of financial harm is more difficult to determine. Although not without problems, constrained ethical egoism seems closer to our normal moral intuitions than ethical egoism in a purer form.

How common is it for people to seriously commit to ethical egoism in either its pure or its constrained forms? Are there many people who believe that one ought always to pursue only one's own interests, or even that one ought always to pursue only one's own interests within certain ethical constraints? It is difficult to say because it is probable that admitting that one is an ethical egoist, or trying to get others to be ethical egoists, is seldom in one's own interests. It is generally a much better idea to get other people to be mindful of the needs of others, including your needs. If this is true, then truly serious ethical egoists would never admit that they are ethical egoists, nor would they ever advocate ethical egoism; it would never be in their interests to do so.

Egoism in Business

Using egoism in the general sense of the pursuit of a person's own self-interest, many people believe that in a capitalist economy, business is founded on egoism and runs on egoism. Egoism is thought to be one of the primary motives for workers to take jobs and pursue careers, for management to run corporations, and for entrepreneurs to build new businesses. Egoism is viewed as the key incentive for people to save, invest, take risks, and innovate. I will refer to this form of egoism as business egoism to distinguish it from ethical egoism and psychological egoism. By business egoism, I mean the belief that it is morally acceptable, or even required, for every individual to pursue his or her own economic interests when engaged in business.

Business egoism is not inherently unethical. Its ethical permissibility can be justified in two ways. The rights justification is based on a person's right to own private property, freely exchange property and services, and freely enter into consensual contracts. Since all people have (or should have) these rights, they have the moral right to pursue their own interests by exercising them. Business egoism can also be justified on utilitarian grounds by using the invisible hand argument. This claims that if everyone pursues his or her own interests, it will lead to a thriving and dynamic economy from which everyone can benefit.

The moral justifications of business egoism do not justify unlimited egoism. First, business egoism includes only economic activities; it does not include other areas of life such as politics, family, or community. Business egoism cannot even be extended to other occupations. Both the rights and the utilitarian justifications of business egoism suggest that in many cases a corporate employee's egoistical pursuit of his own career goals is limited only by his employment contract and not by other obligations to his employer; on the other hand, dedicated physicians, teachers, and professors have fiduciary obligations to their patients, students, and the truth that transcend and may sometimes limit their own egoistical career interests.

Second, business egoism has three significant constraints on it. Neither the property rights nor the utilitarian justifications of business egoism can justify violations of law and ethics. Furthermore, both justifications assume a morality of respect for the free market, including respect for private property and honest contracts. These three constraints are an essential part of business egoism because without them, neither the rights nor the invisible hand justifications of business egoism will work.

These reflections raise the issue of the status of business egoism as a moral theory. Clearly, it is not a form of pure ethical egoism because it requires significant constraints on egoism. It is a form of constrained ethical egoism only insofar as it recommends that people ought to pursue their own interests in business. However, many people's moral intuition is even weaker in that they would only want to claim that it is *permissible*, not obligatory, to pursue one's own interests in business. Constrained business egoism as most people intuit it is not a form of ethical egoism as most philosophers use the term.

Business egoism has many critics. Both the rights and the utilitarian justifications for business egoism have been criticized—the utilitarian justification on the grounds that business egoism does not in fact lead to the greatest good even in a free market and the rights justification on the grounds that property rights are less basic and more limited than the argument requires. Other criticisms include the claim that business egoism corrupts one's character and tends to become obsessive; that business egoists tend to ignore the moral constraints on egoism even though these are an essential part of the justification of business egoism; and finally, that business egoism trivializes life into the pursuit of economic gain.

Business egoism is often discussed in the context of Milton Friedman's famous article defending the obligations of corporate managers to try to maximize the profits of their corporations. Many people interpret Friedman as defending business egoism when he advocates a stockholder theory of corporations, but there are problems in viewing stockholder theory as a form of egoism. First, viewing corporations as egoists when they try to maximize profits raises the question of whether corporations are moral agents that have the kind of interests that egoism requires. Second, Friedman is recommending to senior corporate executives a morality very different from egoism: Executives should, according to Friedman, pursue the interests of the corporation's owners, not their own interests. Executives should not be egoists because they have fiduciary obligations to act in the interests of other people. Viewing Friedman's theory as a form of egoism may come from extending the legal fiction that corporations are persons into ethical discussion, thus raising the possibility of a corporation being an egoist. This extension needs more justification than it has yet been given.

Business Egoism and Ethical Egoism

Business egoism is very different from normative ethical egoism both because it applies only to a person's economic activities and because it needs to be constrained by law, ethics, and respect for private property and honest contracts. However, if one accepts ethical egoism, business egoism would seem to follow from it: If people believe that they should always pursue their own interests, then they would do so in business as well as in other areas of their life. If ethical egoism is used in this way to justify business egoism, business egoism changes slightly. Since under ethical egoism one is committed to a general pursuit of one's own self-interest in all areas of life, one's business interests would have to be balanced with one's other interests. Excessive concentration on one's business interests harms a person in ways that violate a more general egoism. This is the point that Dickens is making with Ebenezer Scrooge in *A Christmas Carol.* Scrooge greatly prospered in business but at the expense of everything else in life. He lost his fiancée, his family, his friends, and the pleasures of society and generosity. Before he saw the ghosts, Scrooge was an excellent businessman and a great business egoist but a very poor ethical egoist.

Conclusion

Of the various kinds of egoism, psychological egoism, which claims that all people as a matter of fact will always pursue their own interests, can be dismissed as either confused or false. This leaves the normative question of whether people *ought* to pursue their own interests and in what contexts they should do so.

Business egoists will pursue their own interests in business without necessarily accepting egoism in other areas of their lives. They can morally justify this on either rights or utilitarian grounds. Many people believe that egoism lies behind the immense productivity of capitalist economies, though the sustainability of that productivity in the medium and long terms has been questioned. Business egoism, whether justified by rights or utilitarian arguments, necessarily has three constraints on the pursuit of self-interest: People should obey the law, follow ethical principles, and respect private property and honest contracts.

A business egoist is not necessarily an ethical egoist because ethical egoists pursue their self-interest in all aspects of their lives, not just business. An ethical egoist would likely be a business egoist insofar as he or she is involved in business, but the nature of business egoism would change if a person were an egoist in all areas of his or her life. Ethical egoists would have to balance their business interests with other interests, including family, friends, community, religion, and so on. They would never sacrifice their other interests entirely to mere economic gain. They do not necessarily recognize constraints on the pursuit of their self-interest, but if business egoism is to be compatible with most people's moral intuitions, then a business egoist is likely to recognize the constraints of religion, morality, or at least the principle of not doing serious harm to others.

Neither business egoism nor ethical egoism should be confused with selfishness, narcissism, excessive self-regard, or even obsessive ambition. Egoists pursue their own interests, but this does not mean that they do not have interests that involve the promotion of the good of other people. Egoists may cooperate with others, and with laws and social norms, as a means to their own ends. But egoists may also include the interests of others as a constitutive part of their self-interest. If an egoist loves his or her family, for example, then their interests constitute a part of his or her interests.

—John Douglas Bishop

See also Absolutism, Ethical; Altruism; Amorality; Buddhist Ethics; Business, Purpose of; Christian Ethics; Corporate Moral Agency; Descriptive Ethics; Friedman, Milton; Hedonism, Ethical; Hedonism, Psychological; Hobbes, Thomas; Invisible Hand; Islamic Ethics; Jainist Ethics; Jewish Ethics; Kantian Ethics; Normative/Descriptive Distinction; Normative Ethics; Professional Ethics; Property and Property Rights; Rand, Ayn; Reciprocal Altruism; Self-Interest; Utilitarianism; Virtue Ethics

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Electronic Commerce

Electronic commerce, also known as "e-commerce," refers to the marketing, distribution, sale, and exchange of products and services via the Internet and encompasses a multitude of Web-based (often called "virtual") commercial transactions. Through e-commerce, funds are transferred, supply chains are managed, and data are collected. E-commerce depends on and is the result of the application of new technologies to traditional forms of business. The commercial transactions that result are considered virtual or simulated—in contrast with traditional, or "real," brick-and-mortar transactions—because they take place invisibly. The *e*, for "electronic," reflects the technological systems that facilitate commerce, and e-commerce thus entails the complete network of systems and processes that enable commercial transactions to take place electronically via the Internet.

E-commerce is a vehicle through which businesses reach out to a virtual marketplace of customers united by need, desire, and/or mere curiosity. It enables firms to transcend barriers such as time and geography and thereby allows businesses to reach a broader audience than might otherwise be possible. It also provides businesses with the opportunity to collect massive amounts of information about their stakeholders—particularly their customers. Finally, use of the Internet by firms enables them to exercise significant control over operations and marketing.

At the same time, e-commerce can serve as a Pandora's box for firms, for there are just as many, if not more, obstacles as there are opportunities for businesses as they operate in the virtual world. Because the Web is largely unregulated, the Net creates an illusion of freedom for businesses and individuals and lulls them into the idea that conventional business practices and the law no longer apply. Businesses and individuals have sometimes discovered the hard way that customary business practices are important and that the law and the public can be unforgiving when people feel violated by online transactions.

Historical Development

E-commerce has evolved considerably during the past 30 years. The term *electronic commerce* originated in the 1970s in connection with technology that enabled the electronic transfer of data in commercial transactions. Electronic Data Interchange (EDI) and Electronic Funds Transfer (EFT) are two examples of the technology developed during this time. EDI facilitates the computer-to-computer exchange of information over private or public networks and remains even today the primary data format for electronic transactions. EFT, in a similar fashion, is used for financial transactions. It, too, continues to exist, albeit expanded far beyond its initial use.

During the 1980s, businesses began to rely increasingly on such electronic means of exchanges to enhance the efficiency and minimize the costs associated with their transactions. Individuals became more familiar with electronic exchanges as automated teller machines (ATMs) proliferated and grew in importance and popularity and as the use of debit and credit cards became more widespread.

It was not until the 1990s, however, that the term *e-commerce* took center stage as the Internet became widely accessible and commercialized, particularly with the establishment of the .com registry, which establishes ownership and regulates the use of domain names. From that time onward, businesses began accessing new and untapped markets, and individuals were able to engage in commercial transactions without having first to establish a physical presence. This heralded what has become known as the "dot-com" era, because of the multitude of Internet-based start-up companies that emerged in a short period of time, along with the use of e-commerce by traditional brick-and-mortar companies.

The term *dot-com* commonly refers to the extension ".com" in a Web address or domain name and indicates a Web site that is commercial in nature. Although .com remains the most commonly recognized extension, other domain names are also available. The extension ".biz," for example, was introduced in 2001 and is restricted to business use. Specific countries have adopted their own extensions, such as ".au" for Australia, ".br" for Brazil, ".co.jp" for Japan, ".com.mx" for Mexico, and ".co.uk" for the United Kingdom.

The Dot-Com Bubble

The late 1990s witnessed a tremendous surge in the emergence of dot-com companies, and a new era began to take shape as businesses adopted Internet addresses, either as their main market presence or as a way to augment existing business. This move had a profound positive effect on Western stock markets, particularly in the United States. Between 1997 and 2001, markets grew suddenly and to unprecedented levels, and this created a speculative bubble that has become known as the "dot-com bubble." A bubble occurs when stock prices boom in a particular industry and speculators, recognizing the rapid increase in share price, invest further, not because they believe the stock is undervalued but in anticipation of continued growth. This bubble is called the dot-com bubble because it was linked to the emergence of a new group of Internet-based companies, commonly referred to as "dot-coms."

Stock values of Internet-based companies soared on the crest of a tremendous wave of opportunity and enthusiasm. Triggered by the shocking rise in value of Netscape's initial public offering (IPO) and allegedly manipulated by some of the world's leading investment banks and venture capitalists (CS First Boston, Goldman Sachs, Morgan Stanley, Merrill Lynch, and others), speculators hoping to get rich quick drove up the stock values of Internet-related businesses. Millionaires were born overnight as venture capitalists invested billions of dollars to fund incipient ideas, while traditional business models seemed to be largely set aside if not altogether abandoned. Low interest rates in 1998 and 1999 increased the availability of capital for entrepreneurial, Internet-based ventures. It was during this time that a number of today's Internet-based leaders emerged, including Amazon.com, eBay, Google, and Yahoo!

The Dot-Com Crash

The ethereal and fragile nature of the bubble quickly became apparent, however, as the bubble burst almost as quickly as it had grown. Between 1999 and 2000, the economy began to slow as the Federal Reserve increased interest rates six times. The failure of these businesses had a cascading effect such that, by 2001, the dot-com boom was over and many of the enterprises viewed so promisingly just a year before were now considered "dot-bombs."

The dot-com crash put hundreds of companies out of business almost overnight and cost thousands of people their jobs. Investors lost millions of dollars. In 1999 alone, there were 457 IPOs of stock of private companies—most of them linked to the Internet and technology. Of those IPOs, 25% doubled in price the first day their stock was traded. By 2001, there were only 76 IPOs, none of which doubled in price the first day of trading. Between March 11, 2000, and October 9, 2002, the NASDAQ fell 78%. The lesson of e-commerce was clear: It holds the potential for tremendous opportunity, but the path toward realizing that potential is fraught with challenges and not that far removed from traditional good business practices.

Ethics and E-Commerce

By 2006, the dot-com market gradually began to rebound. The popularity of enterprises such as Skype (an Internet-based telephone service) and YouTube (a vehicle for Internet-based video sharing) signaled a renewed growth in technology. Even so, ethical issues continued to nag the sector. The unbridled opportunism and manipulation of markets during the bubble had never been fully addressed, and the lure of windfall profits never completely left the psyche of some speculators, despite the legal, financial, and social costs of such behavior.

With the implosion of the dot-com bubble, questions have arisen regarding whether or not e-commerce calls for a new set of ethical guidelines. On the one hand, many maintain that e-commerce is unique and needs an ethic separate from mainstream business and marketing ethics. Others claim that e-commerce is just another form of business and should be subsumed within the broader fields of applied ethics. The chief assertion here is that the problems associated with electronic commerce are merely new manifestations of old business issues that can be addressed adequately through established ethical processes. E-commerce simply contextualizes, in new form, traditional considerations such as fair pricing, distribution, responsible advertising, and respect for privacy.

Not surprisingly, considerable debate has ensued regarding the Internet as a new or variant form of business. Questions persist regarding the Internet's encroachment on individual privacy, but concern for privacy has been a prominent theme in other contexts for decades. The mistake that many companies make lies in framing questions in e-commerce as new territory, for in doing so, they deprive themselves of the years of experience in dealing with those same sorts of issues in the brick-and-mortar marketplace.

Distinguishing Features

While the fundamental difference or sameness of e-commerce is disputed, virtuality—a defining characteristic of e-commerce—certainly alters the dynamics of commercial transactions. While being online might not render it necessary to create a distinct code of ethics for e-commerce, it is important to recognize the presence of significant attributes that exacerbate concern about this way of doing business.

Availability of Information

Information is a valuable commodity, and corporate use of the Internet for marketing purposes presents managers with a pressing problem regarding how to handle the metaphorical mountain of information that the Internet makes available to them. Because firms cannot afford to market their products to everyone, managers must cull through information with a strategic purpose in mind. In other words, it is not enough to acquire information; that information must be handled in such a way as to create value for the firm. To aid in this process, support businesses have emerged whose primary purpose lies in collecting information to be sold for marketing purposes. In addition, businesses themselves are becoming increasingly adept at collecting information about customers and then selling that information to other firms.

Unrestrained information gathering is a concern to many people, especially those who care about individual privacy protection. In their view, while information gathering per se is not necessarily worrisome, how that information is used matters. The magnitude of the information available via the Internet coupled with the temptation to misuse it has exacerbated privacy concerns among a number of stakeholders in e-commerce. Because the Internet enables businesses to distribute widely the data they collect, the monitoring, control, and use of information have become focal points of concern.

Lack of Transparency

As odd as it might seem, an online presence often diminishes corporate transparency. While e-commerce allows firms to harvest large amounts of information about people, it also enables corporations to cloak themselves and their practices in deceptive anonymity.

Although many firms volunteer information about their goods and services, a significant number do not. Xfleas.com, for example, is a low-cost distributor of pet supplies. Although its Web site states that the company only sells products licensed in the United States, the only information available about the company is an e-mail address, a mailing address, and a fax number. There is very limited information about the specific products offered, and no information is provided about expected delivery times and other particulars associated with purchase and delivery.

Although customers might choose not to patronize such a company, many do so without being bothered by the lack of transparency in their transactions. Any qualms they might have are overridden by the lure of comparatively inexpensive products. In this case, the product offered is a 12-month supply of Interceptor, a popular heartworm preventative, which costs $25.54, including shipping. This compares favorably against Interceptor at $38.98 with $3.99 for shipping from 1-800-PetMeds, another popular Internet competitor—and so individuals willingly give their information to Xfleas.com.

Absence of Accountability

Accountability is noticeably absent in e-commerce as well. This can be a concern for customers who anticipate the possibility of mistaken delivery or defective products. Xfleas.com, for example, does not post any sort of return policy on its Web site. While it is uncommon for companies not to publish a return policy, they are not required to do so, and many opt out of this. Even in situations where the company does publish an explicit return policy, customers still encounter problems. Policies can be placed on Web sites such that they are not easy to find; the style in which policies are written can render them difficult to understand and/or apply; and the policies themselves can be replete with loopholes.

Product delivery is another area where accountability can be absent. Delivery is often delayed. Sometimes the product shipped is not the one that was ordered. It is frequently impossible to reach someone by phone or e-mail to handle or respond to complaints. While customers can choose which companies with which to do business, the reality is that the absence of accountability remains a significant concern regarding online transactions.

Perception of Vulnerability

The physical and metaphorical distance between firms and their customers, coupled with the ongoing flow of information (both accurate and deceptive), enhances Internet users' feelings of vulnerability. Customers complain about failed transactions and the lack of easy means of redress. Similarly, firms constantly strive to weed out customers who do not honor their debts. Other stakeholders express similar concerns about their vulnerability when engaging in online transactions.

In the end, stakeholders of all sorts recognize the value of information afforded by the Internet as well as the fact that the volume of information gleaned can be overwhelming and lead to inaccuracies, deception, increased financial risk, and feelings of vulnerability. The presence of these attributes serves to impose an obstacle to online trust. Ironically, it is trust that is arguably the linchpin for successful e-commerce. It is therefore essential for e-commerce ethics to incorporate consideration of such attributes in making ethical decisions regarding e-marketing.

Data and Discrimination

As destructive as improper use of data can be by brick-and-mortar enterprises, it is even more dangerous in the electronic domain because of the lack of formal restraints. Even so, a number of companies, failing to exercise proper judgment, have found that laws and ethical norms are unforgiving when it comes to the exploitation of personal data for commercial purposes.

DoubleClick and Data Miners

DoubleClick introduced people to "cookies," the term for information users leave behind as they surf the Internet. Cookies contain records of the keystrokes that Internet users enter and are stored on personal computers. They provide a record for return visits to Web sites, and the information they contain enables companies to construct profiles of customers.

Not long ago, DoubleClick, through the manipulation of cookies, created an extensive database of 100,000 online customers. When this was discovered, the company received harsh criticism by those who were unknowingly profiled. Early customers/surfers who had agreed to share information about themselves with DoubleClick had done so with the assurance from DoubleClick that their information would remain confidential. People felt betrayed and became outraged when DoubleClick attempted to merge with Abacus Direct, an offline marketing company with a database of information on 88 million households in the United States. Even before DoubleClick had the opportunity to use the data, the proposed merger alerted people to the dangers of intrusive target marketing that databases such as these could trigger.

Interestingly, although the DoubleClick merger issue was heavily publicized, it was not the first instance of such activity. Earlier, in 1998, Geocities was sued for selling personal information to third parties after guaranteeing its Web site users that their information would not be shared. Toysmart, too, was sued in 2000 for similar behavior in violating its privacy agreement during bankruptcy proceedings when it attempted to sell personal information to settle its debts with creditors.

While this type of activity occurs more frequently within e-commerce, where data can be more easily and opportunistically collected and disseminated, it echoes a similar situation relating to a database that Lexis-Nexis offered in the mid-1990s. At that time, Lexis-Nexis established what it called its P-TRAK Person Locator service. It provided address information along with aliases, maiden names, and social security numbers for millions of people in the United States. Although there is no public record of a lawsuit, the P-TRAK service was short-lived. Even though the data had been collected through legitimate means, their availability and accessibility posed a significant threat to the public. Both situations underscore the message that it is not the legitimacy or manner of obtaining the data that is necessarily determinative but their susceptibility to being used for manipulative or malign purposes that renders such databases questionable.

Amazon and Price Discrimination

Amazon has used data monitoring to develop customer profiles that it uses toward multiple ends—ostensibly to enhance customer service. For instance, Amazon uses historical purchase information to tailor Web offerings to repeat customers. Interestingly, there are serious questions about the accuracy and reliability of this sort of customer-driven information. When customers input the information themselves, it is often accepted without verification. Although this is troubling in itself, the underlying assumptions are even more problematic. With regard to purchases, not every single purchase can be interpreted as indicative of a customer's overall taste. Some purchases, for example, are made as gifts, others as one-time extravagances. In the end, Amazon was constructing profiles that appeared accurate but very likely were not.

In addition, Amazon allegedly used data profiling to set prices. In September 2000, Amazon customers discovered that they were charged different prices for the same CDs. Although the company claimed that the price differentiation was part of a randomized test, the result was price discrimination that appeared to be based on demographics. In other words, Amazon appeared to be redlining, or "e-lining" (redlining via the Internet)—a practice of price discrimination that differentiates financial opportunities on the basis of demographics such as race. Redlining is widely considered both unethical and illegal.

In the end, Amazon found that its use of information derived from online sources led to all sorts of complications. In this regard, Amazon is not alone.

Kozmo and Delivery Discrimination

Kozmo is another e-tailer identified as an e-liner. This company—a provider of 1-hour delivery services—excluded certain neighborhoods as a result of its racial redlining practices. In short, it refused to deliver merchandise to customers in undesirable neighborhoods, identified by their zip codes, which were predominantly black. Again, such behavior is considered legally and ethically inappropriate, for it deprives classes of people of opportunities available in the marketplace.

PayPal.com and the Global Marketplace

PayPal's less publicized e-lining behavior is particularly disturbing because of its influence on global e-commerce and its extensive relationships with people in different countries around the world.

E-commerce tends to be unique in that it renders geography virtually moot. PayPal, an e-commerce giant, emerged as a way of streamlining payments in arms-length purchases. As a disinterested third party, PayPal links parties for payment purposes in secure transactions. PayPal can link anyone, anywhere. The problem is that PayPal became selective with regard to the people with whom it chose to do business. In doing so, it effectively redlined groups of people on an international scale. In the United States, businesses can redline neighborhoods; in the global marketplace via the Internet, the ramifications are huge because e-businesses can e-line entire countries. This is what PayPal did by eliminating or not allowing transactions with parties in countries that are disfavored.

PayPal attributed its reluctance to do business with people in certain countries to the rampant corruption, lack of infrastructure, and risks associated with not receiving payment. While it is true that particular countries are notorious for "carding" (passing off illegally obtained credit card numbers), the problem was that the people of entire countries were denied access to a service and thereby forcibly limited in their access to e-commerce (since PayPal is a major e-payment tool). PayPal effectively engaged in discriminatory behavior, even though that behavior was for a legitimate business purpose (i.e., the minimization of financial risk). Unfortunately, although such behavior is considered illegal in the United States, there is no legislation to prevent it in e-commerce and in the global arena. PayPal thus engaged in practices via e-commerce that it could not have legally engaged in as a brick-and-mortar company in many countries, including the United States.

E-Trade

An emerging area of concern is that of e-trade. E-trade refers to the online trading of securities and financial products. Buyers and sellers connect through the Internet in e-marketplaces. It used to be that stock markets were physical locations where buyers and sellers met to negotiate prices. The Internet renders this moot.

Although NASDAQ set up the first electronic stock market in 1971, it took more than 35 years for the New York Stock Exchange to automate its trading process. This step is significant in that it signals the potential end of traditional trading room floors. If this is true, it is imperative that those involved in this business enhance online security and privacy measures, both to preserve trust and to protect customers.

Conclusion

The e-marketplace remains an amorphous domain, rife with both promise and danger. Where neither legislation nor regulation provides clear direction and where moral norms are not clearly defined, businesspeople must determine for themselves how to navigate through ambiguous ethical situations. The examples of companies such as DoubleClick, Amazon, Kozmo, and PayPay underscore the problems associated with the emergence of new technologies and online transactions. The experiences of these companies also suggest good reasons for the need to establish and articulate guidelines for e-commerce, whether they are the same as or different from existing brick-and-mortar business principles.

—Tara J. Radin, Martin Calkins,
and Carolyn Predmore

See also Computing, Ethical Issues in; Digital Divide; European Union Directive on Privacy and Electronic Communications; Identity Theft; Internet and Computing Legislation; Marketing, Ethics of; Privacy; Trust

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Electronic Surveillance

Electronic surveillance may be defined as the use of electronic devices to monitor people, their communications, and their physical environment. Electronic surveillance techniques and equipment allow people to gather data in an automated manner, usually with the goal of concealing the surveillance efforts from one or more of the monitored parties.

There are many examples of electronic surveillance that predate the computer era. These include the use of radio and television equipment to monitor conversations, and wiretaps of telecommunication lines.

Cameras have been used for surveillance almost since their invention. The video camera is particularly well suited for this use, as it can be set up to record customers, employees, and remote locations. The recording of video surveillance has become less expensive. Film is fragile and difficult to process. Recording tape does not need to be developed, but it shares some problems with film, in particular physical damage and capacity limitations. Modern video surveillance equipment can record images directly to a hard drive, thus allowing the operator to record far more information than with film or on video. It is also relatively easy to store, transmit, and analyze digital video, and the employees who perform these functions do not need physical access to the camera or location.

By adding a computer to the surveillance equipment, data gathering may be performed in a continuous or random manner, with or without human control. Recent examples include the methods described above, along with keystroke monitoring, satellite imagery, and radio-frequency identification or tagging.

Physical access to the monitored persons and environment is not always required. Some electronic surveillance can be performed in a remote manner. This can be achieved by using monitoring equipment set up at a distance from the user. Other remote techniques require an individual to place only one visit to the person or site to perform the initial setup of the required devices. Examples include the use of global positioning system (GPS) transceivers to monitor the movement of a person or an object with a high degree of precision in real time.

The emergence of trusted computing technology has offered organizations the possibility of monitoring the patterns and details of a computer user's activities. In 1993, the federal government proposed that telephones include the so-called Clipper cryptographic chipset. This chipset used a classified cryptographic algorithm and a key escrow approach that would allow authorized investigators to monitor encrypted telecommunications. After several researchers demonstrated flaws in the encryption techniques, the government abandoned the proposal in 1998.

More recently, a consortium of hardware and software companies have proposed that personal computers, media players, game consoles, and other devices include a trusted computing module. This module is a chipset that is physically integrated into the device in such a manner that removing or disabling the module would also disable or destroy the entire device. A trusted computing module can be used as a key for encryption and as an electronic serial number to uniquely identify hardware. This module could also be employed to license or restrict any digital media, including a program, file, or document, to one or more specific computing devices. The licensing transactions could then be used for surveillance purposes.

The widespread use of personal computers, mobile phones, and personal digital assistants (PDAs) in point-of-sale, inventory, and e-commerce applications raises the possibility that investigators could use a computing device's records to find and identify the participants in any financial or communications transaction, with or without the individuals' knowledge. Mobile phone networks and wireless networks can record and report data about a specific device's physical location and state. This is already being done in practice, with the use of GPS hardware and physical tokens such as radio-frequency devices. These devices may easily be installed in vehicles with or without the user's knowledge or consent. In fact, as more automobiles are equipped with sophisticated computer systems, it has become possible for law enforcement authorities to retrieve data about a car's speed, direction, and performance. This is particularly useful in forensic investigations of automobile accidents. Thus, computer or mobile phone users may incriminate themselves by using their own electronic equipment or simply by turning on the device.

There are several ethical concerns involved in this type of monitoring. A utilitarian approach is often used to support electronic surveillance before, during, and after criminal activities. Depending on the political climate, the severity of the crime, and other factors, the utilitarian ethic tends to override concern for the individual's privacy.

Electronic surveillance techniques may be used to extend or alter the scope and purpose of existing natural surveillance programs. Natural surveillance relies on the everyday human activities in a neighborhood as a monitoring tool. Criminals seem less likely to commit offenses if they believe they will be noticed or caught.

Criminal Activities

In the United States, the Fourth Amendment of the Constitution provides the basic protections against search and seizure. All three branches of the federal government and several state governments have weighed in on the legality of electronic surveillance methods in public life, the workplace, and the home. The USA PATRIOT Act is a recent example of how electronic surveillance has been used to address a variety of issues, including public safety, national defense, and economic security. The American Civil Liberties Union, the Electronic Frontier Foundation, and various labor unions are among the chief advocates for greater restraint and care in the use of electronic surveillance.

In some ways, the European Union (EU) regulates electronic surveillance in a stricter manner than the United States. Transborder electronic surveillance is a special concern. The EU's long emphasis on freedom of personal movement has sometimes collided with the enforcement and extradition efforts of European and international law enforcement agencies. However, several EU countries, such as Germany and the United Kingdom, have deployed vast networks of video cameras and other surveillance equipment throughout their larger cities to control crime, prevent terrorist attacks, and monitor traffic.

Marketing and Advertising

Electronic surveillance of consumers has become a normal activity in most industrialized countries. The data gathered from observations of shopping, browsing, and other normal activities can be used by manufacturers, distributors, retailers, and other parties to improve service, increase revenue, and provide better performance. Along with the methods mentioned earlier, this can include programs designed to reduce theft, increase customer turnover, and enhance workplace safety.

This use of electronic surveillance can also involve affinity programs that provide the consumer with discounts or other incentives in return for continued access to detailed information about finances, transactions, and other areas of interest. The retail, travel, finance, and banking industries have all employed various kinds of programs to collect detailed consumer data, which can be used in-house or rented to other suppliers and customers.

This kind of electronic surveillance seems permissible under both the utilitarian and the Kantian perspectives. The utilitarian ethic promotes the goal of the greater good versus the sacrifice of personal privacy, while the Kantian approach emphasizes an organizational responsibility to provide users with complete information, under the auspices of informed consent.

Employers and Employees

Electronic surveillance has also become an important issue in the workplace. Many electronic surveillance methods are easily used to monitor employees. Coupled with the growing reliance on the Internet and computers in many jobs, this trend has escalated sharply in recent years.

The widespread use of GPS tracking systems to monitor and locate vehicles and individuals provides one example. These tracking systems can be installed in a vehicle to monitor historical usage and location. When a GPS receiver is coupled with a transmitter, the resulting system can report the current location and approximate speed of the GPS receiver. Employers have installed and used such systems to monitor taxi, bus, and truck drivers in the United States, in the interest of enforcing workplace rules and increasing overall performance levels. In some cases, employees and users were not informed as to the capabilities of these devices. Behavior patterns that previously seemed normal to employees may no longer escape the detection and discipline of management.

Within the workplace, the principles of pervasive or ubiquitous computing, coupled with the advancing speed of telecommunications and computers, already allow users to store their data in a centralized location and to access such data with the computing client of their choice—a mobile phone, PDA, personal computer, or terminal.

It is far easier for an employer to monitor and control sensitive information in a centralized environment. In the United States, legislation such as the Sarbanes-Oxley Act of 2002, the Family Educational Rights and Privacy Act of 1974, and the Health Insurance Portability and Accountability Act of 1996 has led many organizations to consider the pervasive and centralized models as a compliance strategy for privacy, archiving, and other standards.

—William A. Sodeman

See also Informed Consent; Privacy; Sarbanes-Oxley Act of 2002; USA PATRIOT Act; Workplace Privacy

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EMINENT DOMAIN

Eminent domain is a U.S. legal term referring to the state's power to take private property from landowners without their consent. The U.S. Constitution does not explicitly refer to eminent domain, but the premise underlying the Fifth Amendment is that the government has that power: "Private property [shall not] be taken for public use, without just compensation." Recent U.S. Supreme Court interpretations of this clause and the limits it puts on governmental powers pose legal and ethical questions to both the government and the owners of private property, whether businesspeople or homeowners. The original conception of "public use" was that the government should not take private property unless that property was to be used by the public. In addition to this argument that takings for private purposes are unjust and tyrannical, some argue that such takings are inadvisable as they may weaken the concept of private property, weaken the incentive to invest in property, and ultimately weaken the economy. However, current Supreme Court authority allows local legislative bodies to take property from one private owner and give it to another if the taking is for purposes of economic development. In addition to controversies concerning whether *public use* includes economic development, there are recognized problems concerning what compensation is "just."

Historical Background

The term *eminent domain* was originated by Grotius, the 17th-century jurist, who held that the state possessed the power to take or destroy property for the public's benefit but when the state so acted, it was obligated to compensate the injured property owner for his losses. Prior to Grotius, political philosophers such as Plato believed that there was nothing to prevent a state from taking private property in the interest of the polis. James Madison picked up on Grotius's limitation of state power in his drafting of the U.S. Constitution's Fifth Amendment, which imposes two distinct conditions, two checks, on the exercise of eminent domain: "The taking must be for a 'public use,'" and "just compensation must be paid to the owner." Originally, this power applied only to the federal government, but the passage of the Fourteenth Amendment expanded its scope to include state and local governments as well.

Public Use

Historically, the courts have employed two interpretations of the public use exception to the bar against governmental takings: a narrow view and a broad view. The narrow view was that property could be taken only if it was to be used by the public in general: the "public purpose" line of cases. So, for example, in the colonial era, one constructing a mill (the equivalent of a public utility) under the Mill Acts was liable only for limited damages if his mill caused flooding to upstream neighbors: "Apparently, the contribution of water power to the general well-being and advancement of the public trumped the rights of the private landowner." In the 19th century, many early decisions held that governments lacked the power to permit the nonconsensual taking of private property for private use, based on natural law theories or state constitutional language. They held that actual control by the government or use by the public was essential to justifying a taking. However, this "use by the public" standard, which was adopted by the majority of the states, became difficult to apply because of the loopholes, limitations, and evasions created by 19th-century state and local courts that wanted to encourage industrial development.

Another line of cases interpreted *public use* more broadly and deferred to legislative interpretations of the term. These courts stated that when the legislature has declared the use or purpose to be a public one, they would respect that interpretation unless it was completely unreasonable. Finally, in a 1954 case, *Berman v. Parker,* the Supreme Court formally abandoned the "narrow" definition of public use entirely, defining the phrase as a generalized benefit to the "public welfare": "The concept of the public welfare is broad and inclusive. The values it represents are spiritual as well as physical, aesthetic as well as monetary." *Berman* allowed takings for purposes of economic development and also formalized the policy of deferring to the legislature in defining the limits of "public use." Mr. Berman owned a department store in an area of Washington, D.C., that the U.S. Congress wanted redeveloped because much of the residential housing was in a deplorable condition. However, Mr. Berman's store was not blighted. The Supreme Court's decision meant that Berman lost his non-blighted commercial property, which was ultimately to be transferred to another private party.

A more recent Supreme Court case, *Kelo v. City of New London*, is consistent with *Berman*; its only real change is to openly authorize legislative bodies to exercise eminent domain for purposes of economic development. The city of New London wanted to redevelop the area around a defunct Navy facility and created a rejuvenation plan that involved a large pharmaceutical company's promise to build a new plant in the area. That plan involved the exercise of eminent domain to gather the land that would eventually be transferred to the pharmaceutical company or other private entities. Susette Kelo and several other homeowners filed suit, arguing that the taking of their properties was a violation of the public use limitation on eminent domain. The Supreme Court rejected their argument, stating that it had "repeatedly and consistently rejected" the narrow test because it had fallen out of favor due to the difficulty of its application and the changing needs of society. The Court found that the city's plan was designed to create jobs and increase the community's tax base, as well as provide residential and recreational use, so that it "unquestionably serve[d] a public purpose," which was enough of a public use to justify the exercise of eminent domain powers.

In dissent, four justices argued that the majority decision deleted the words "for public use" from the Takings Clause of the Fifth Amendment. In his separate dissent, Justice Thomas agreed. He further argued that in keeping with the Constitution's common-law background, the clause was intended to be a most-needed limit on the government and worked in context with other carefully chosen language in the Constitution. The government is allowed to take private property only if it provides "just compensation" and only if the taking is for the government's or the public's own use.

Just Compensation

Just as the definition of *public use* is controversial and involves policy issues, so does the definition of *just compensation*. Under common eminent domain practice, if the taking is for purposes of redevelopment, the area must first be declared "blighted." Then, the condemning agency must attempt to purchase the property through free negotiation on the open market before resorting to condemnation. Thus, because the owner of the property at issue will usually have refused to sell on the government's terms, the assertion of eminent domain is coercive. Once the owner refuses to sell and the property is taken according to certain procedural requirements, *just compensation*, as interpreted by the Supreme Court, requires that the owner of the condemned property be put in as good a position financially as if his property had not been taken.

Although the condemned owner is due a full and perfect equivalent to the property taken, determination of that value has proven difficult. The standard measure used is that of "fair market value." Unfortunately, this measure has been widely criticized as failing to ensure that landowners are fairly compensated for their loss, failing to promote efficient use of the Takings Clause, and failing to prevent opportunistic entities from driving the price up for the government. Landowners are compensated only for the loss of their land and buildings. No "consequential" damages are awarded, and thus business owners lose business profits and goodwill, removal costs, litigation costs, and demoralization costs for which they would otherwise be compensated under common-law principles if a private party, rather than a government, took their business. Homeowners and neighborhoods lose, in addition to litigation costs and objective undervaluation of their property, any value that could be attributed to emotional or historical attachment to the property.

In addition, the market value method is criticized as inefficient because the government cannot calculate in advance the costs associated with the takings and therefore fails to consider opportunity costs. The only costs it can accurately anticipate are the fair market value costs, not the administrative or litigation costs. The administrative costs associated with takings can be extraordinarily high and include the costs of obtaining legislative authority, drafting and filing the complaint, serving process, securing a formal appraisal, and so on. The litigation costs associated with takings can also be extremely high. In one case, a homeowner who paid $778,000 for his property and then added improvements costing $100,000 was eventually awarded $1,070,000 by a jury, plus $620,000 in attorney's fees. Therefore, the fair market calculus may prevent opportunistic behavior on the part of property owners to drive up governmental costs, but it does not discourage the same kind of behavior by administrators, attorneys, or litigants.

In addition to being ineffective, some argue that the market value method is poorly defined. Fair market value is defined as the price that a willing buyer would pay a willing seller in the open market. The willing buyer is the government, but there is no willing seller. Thus, the definition of fair market value is based on a fiction. Furthermore, some criticize the courts' methods of calculating it as inconsistent with the way an appraiser would value a property's worth. A real estate appraiser estimates what a buyer would offer, ignoring the seller's willingness and instead assuming that the seller will accept the highest price offered after a reasonable time. Other concerns include when fair market value should be assessed, because the value of a property can change dramatically once it becomes known that a legislature has granted eminent domain power to a developing agency. Consequently, some argue that fair market value, as defined by the courts, should be eliminated and the proper measure of just compensation should include both market value and compensatory damages.

Fiscal and Ethical Issues Raised by Eminent Domain

Kelo led to a firestorm of debate concerning both fiscal and ethical concerns when economic development is used to justify the exercise of eminent domain. One argument was that government-sponsored redevelopment projects often fail, that allowing such projects can easily lead to overreaching by legislators in concert with business entities, and that the market is a more efficient means of encouraging economic development. Furthermore, even where an economic-development taking led to an economically improved area, it was argued that the area at issue would have improved on its own, through the operation of the market, without the use of eminent domain.

There is historical justification for the first part of this argument. For example, the Washington, D.C., redevelopment project at issue in *Berman* ultimately failed and was repealed. A similar project in the Poletown area of Detroit, Michigan, involving General Motors, similarly failed, leaving a strip of abandoned and burned-out properties instead of the pretaking busy commercial area, and Cincinnati's downtown area gained only a municipal parking lot when Nordstrom ultimately backed out of a redevelopment plan.

It has been further argued that the allowing of economic redevelopment takings encourages overreaching on the part of legislators and business interests: Business interests that want to purchase property for redevelopment at a low cost will ask legislative bodies for eminent domain support, and legislative bodies greedy for additional tax dollars will seek business interests that will agree to use eminent domain power in keeping with that interest. In either case, the concern is that private parties and small businesses may be victimized as a result.

As with the economic efficiency concerns, there have been instances of legislative misbehavior in connection with economic redevelopment. According to news reports, a city council hired first one appraiser and then another in an effort to have an aging, working-class subdivision declared blighted so that it could be slated for redevelopment. The council wanted to replace the subdivision with a shopping mall in an effort to increase tax income for the city, and so the World War II–era development was termed "blighted" despite the fact that the only problems the appraiser could find were bedrooms in some basements, front porches that had settled, and some windows that were too small to allow escape in an emergency. The developer hired to redevelop the area could not secure financing, and so the project eventually failed.

Perhaps in response to perceived or realized ethical and practical problems posed by the exercise of eminent domain for economic redevelopment purposes, 32 states passed or were in the process of passing legislation banning economic development as a public use within a year of the *Kelo* decision. Even the U.S. Congress passed a bill preventing the use of federal money in connection with a federal, state, or local economic redevelopment taking. Whether or not just compensation theories will follow this trend of change in eminent domain law remains to be seen.

—Nadia E. Nedzel

See also Civil Rights; Common Law; Consent; Economic Efficiency; Efficient Markets, Theory of; Free Market; Industrial Revolution; Integrity; Justice, Compensatory; Property and Property Rights

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Emissions Trading

Emissions trading is a relatively new and creative market approach to reducing pollutant emissions by allowing entities to trade emission allowances or credits issued by the government. An entity operating within the pollution standard, which refers to the levels of specific pollutants that are allowed in the ambient air and water in a particular location or from specific sources, can sell or trade its credit or allowance to an entity that cannot meet that standard. The overall pollution emission levels in an area or at a specific source must meet the specified standard.

Emissions trading permits greater flexibility in meeting state emission standards. Flexible emissions-trading programs are designed to capitalize on the efforts of entities able to reduce their emission levels below the level required by the relevant standards. The emissions-trading programs were originally designed to allow entities to trade credits granted them for attaining lower emissions than allowed by the state.

Types of Emissions-Trading Policies

Emission trading involves trades of emission allowances or credits. In the credit trading program, to the extent that an entity's emissions are produced at a level below the amount permitted under the applicable emission standard, such an entity can apply for certification of the excess as an emission reduction credit (ERC). The entity is then allowed to trade its ERCs to another site whether under common ownership or not.

Allowance trading is a refinement of the credit trading program. Allowance trading measures emissions themselves rather than emissions over a period of time. Allowances are granted to an entity for a certain amount of emissions that entity is allowed to produce rather than focusing on just the incremental difference between the amount allowed by regulation and the amount produced. Allowance trading bears a relation to emission standards in that entities will only trade allowances to the extent that they hold allowances that enable them to produce emissions at a level that will result in compliance with the applicable emission standards. Conversely, credit trading depends on the level of the relevant emission standard to determine the amount of ERCs available to an entity at a particular time.

Trading of emission credits and allowances occurs in the context of differing policies allowing for the use of such credits. The policies are referred to as netting, offset, banking, and bubble policies, and the specific policy applied depends, in part, on whether the emission source is new or existing and on whether the currency being traded is credits or allowances. Credit trading uses the bubble and offset policies, while allowance trading uses the netting and banking policies.

The offset policy permits the creation of new emission sources in areas that have not attained good air or water quality by requiring such sources to result in emissions that are at least 20% lower than would otherwise be required for a new source in an area that has attained good air or water quality. The bubble policy involves aggregating multiple emission points and regulating the level of emissions within the bubble through the use of standards and credit trading.

Emission sources that are expanding or undergoing modification are subject to the netting policy, which eliminates the requirement for such sources to achieve the relevant emission standard as long as the overall increase in emissions due to the expansion or modification is negligible. Credits can be used to offset any increase that would be deemed to be more than negligible to allow the modified or expanded source to remain compliant with emission standards. Finally, the banking policy allows entities to store, or "bank," their allowances or credits for use in reducing actual emissions at some point in the future, either when their emissions increase or when the emission standards call for a decreased emissions level that the entity has not yet achieved.

Legislative Background

The availability of emissions trading stems from the existence of federal and state legislative mandates to reduce pollution levels. In general, the legislative framework to achieve such levels consists of targeting certain pollutants for reduction, setting limits on the amount of pollutant emissions that companies may acceptably produce, and levying fines against those companies that are out of compliance with such levels or even types of pollutants.

The Federal Clean Air Act represents the federal government's most significant legislation in this area. The Clean Air Act was first promulgated in 1955 and underwent numerous substantial revisions. The Federal Clean Air Act, as amended, requires the Environmental Protection Agency (EPA) to periodically set standards for specific pollutants. The Clean Air Act specifies the maximum levels of pollutants that a power plant is allowed to emit. There is then an enforcement mechanism under which fines are assessed against any company exceeding such limits.

The EPA established standards for smog and soot at various points between 1971 and 1987. New rules, added in 2004 to address specific pollutants, include the following: (1) Clean Air Ozone Rules, (2) Clean Air Fine Particles Rules, (3) Clean Air Interstate Rule, (4) Clean Air Mercury Rule, and (5) Clean Air Non-Road Diesel Rule. Carbon dioxide has not been addressed and remains a point of contention.

Creation and Distribution of Allowances Under the Clean Air Act

Title IV of the Clean Air Act amendments of 1990 concerns the control of acid deposition. The rules proposed by the EPA to implement Title IV of the 1990 amendments provided for nationwide free trading of allowances. Allowances are a fairly straightforward concept. Once the allowable pollution limits were set for various pollutants, allowances were distributed at no cost to companies in the amount of such limits. Each allowance was equal to the right to emit 1 ton of the particular pollutant. Essentially, such businesses were distributed "rights to pollute." The allowance signified the business's right to emit that amount of pollutant. The company's emissions were then reviewed. If the company's emissions were less than the target level, the company had the option of banking the credits for later use either in its own business as it grew or in its business of the same size as the emission standards were reduced. On the other hand, if the business was exceeding the emission standards, it was allowed to enter into a trade for emissions credits either from another of its own sites or from another entity entirely, provided the credits were being purchased or traded from a site that had reduced its emissions below the required level. Using the emissions-trading system, businesses were able to continue in existence rather than allowing regulation to result in their closure or in significant fines.

Availability of State Restrictions on Emissions Trading

Not all constituencies agreed that the standards provided by federal legislative response to the pollution problem were sufficient. Under the Clean Air Act, states were allowed to develop their own plans once it was determined that there were areas that did not attain the reduced emission levels imposed by the national standards. State plans were developed to address those specifically designated areas. The state plans have come under attack, and in the 2002 case of *Clean Air Markets Group v. Pataki,* the state of New York's response was found to have violated the Supremacy Clause of the U.S. Constitution and was also determined to be an impermissible burden on interstate commerce.

In the *Pataki* case, the state of New York objected to provisions in the federal Clean Air Act that allow emission credit trading. New York enacted its own, tougher, statute, which was later struck down in court. The problem for New York, and potentially for other states that lie upwind of sources of pollution, was that the emissions from certain states upwind of New York do not remain upwind; they travel up to hundreds of miles and contribute significantly to acid depositions in particularly susceptible areas in New York State, such as the Adirondacks. New York objected to the free trading of pollution allowances and requested that such trading should not include the so-called upwind states. The EPA disagreed and retained its free-trading provisions.

In response, the New York legislature enacted the Air Pollution Mitigation Law in 2000 to encourage New York utilities to protect sensitive areas from acid deposition and to make business decisions regarding the utilities' participation in the federal allowance credit trading programs. The Air Pollution Mitigation Law required that all transfers of sulfur dioxide allowances were to be reported to the New York State Public Service Commission (PSC), the regulatory commission responsible for utility rates and service in New York. The PSC would then charge an offset to any company that sold emission allowances to an upwind state or to a nonupwind state if such a sale did not include restrictive covenants against its later sale to an upwind state. The amount of the offset would be equal to the proceeds from the sale of the allowance.

The U.S. District Court for the Northern District of New York found that the restrictive covenants lowered the value of the emission trading allowances and struck down the law. States were not to be allowed to enact regulations that were more restrictive of pollution than those required in the Clean Air Act. The EPA had considered and rejected geographical restrictions on the trading of allowances and had clearly mandated the free transferability of such assets. Therefore, a 100% penalty on such a transfer would constitute a significant restriction on such free transferability and is therefore contradictory to the purposes of the federal law. States do not have the power to broadly regulate emissions but rather only have the power to restrict the emissions within their own jurisdiction.

Mercury Emission Challenges

In 2004, the EPA announced new regulations applying to mercury emissions, which became final in 2005. Mercury was added to the pollutants for which power companies were able to purchase trading credits. A coalition of 11 states challenged the federal rule that allows coal-fired power plants to buy pollution credits to avoid lowering their mercury emissions. The lawsuit claimed that the new rule slows attempts to decrease dangerous mercury emissions and poses grave health risks to those exposed to such emissions. The lawsuit claimed that the credit trading system would create "hot spots" around some plants that purchase the rights to emit more mercury. Reducing overall pollution at the cost of increasing it in particular areas results in the decrease in pollution at one location, beneficial for a particular population, and a concomitant increase in exposure to the detriment of another population.

Courts have been used to address issues stemming from emission-trading laws and regulations. One argument advanced against using courts to determine pollution cases is that the constituency affected is too broad for redress in courtrooms. Carbon dioxide is an emission that is currently not regulated in the United States. The proposition has been advanced that if carbon dioxide is found to be reasonably likely to cause the harms that some believe, then Congress will be better suited than a court to consider what level of emissions will maximize the benefits provided by the utility companies while minimizing the harms of the emissions. The Clean Air Act's "cap-and-trade" system's successful reduction of the overall level of emissions through the use of market forces serves as evidence in support of such a theory. However, the question still remains as to how to balance any harm stemming from the use of an efficient market system that results in the shifting of the percentage of the burden of pollution onto alternate populations.

Interests Affected by Emissions Trading

It appears that emissions trading allows a business such as a power plant that is unwilling, or economically unable, to reduce its emissions to the level required by law to use the credits to maintain emissions in excess of those required by such law. A legal right to emit at that level has been created that may be efficient from an economist's perspective but that in effect results in a selection as to which populations remain exposed to increased pollutant emission levels. The ability of high-pollutant-source areas to maintain their existing levels of emissions rather than decrease them, which was the main stimulus behind the law, highlights the issue of the disproportionate effect that the trading of allowance credits permits. Hot spots, or high concentrations of pollution in particular locations, could be created under this system when the allocations are purchased by companies in such a manner as to allow for clustering of the highest emission levels.

Desirability of Emissions Trading

The public is one of the primary constituents to be considered in determining whose interests are affected by the pollution rights trading laws. The question that arises is, To which public are we referring? The public as a whole may be benefiting from decreased overall pollution levels if the free market theory of pollution credits is the most cost-efficient method of pollution reduction, but a question remains regarding the interests of the public residing nearest to the areas containing the businesses that are buying the pollution credits. For that segment of the public, the level of pollution is increasing or, at the very least, not decreasing to the same degree as pollution near power plants that have opted to purchase emission-trading credits for the right to continue to pollute in excess of the thresholds targeted by law.

One of the continuing conflicts between economists and the environmental community with respect to emission trading has been the issue of whether such permits constitute a secure property right under the law. Economists prefer the treatment of the permits as property rights to protect the investment in the resource, while the environmental community consistently argues that the environment belongs to the people and, as a matter of ethics, should not become private property. If the emission allowance is a property right and the emission allowance is reduced, it could give the business that held the emission allowance the right to claim compensation from the government for the reduction of the allowance. The practical resolution of this conflict has been to attempt to give a minimum level of security to the permit holders with respect to their rights while making it clear that permits are not a property right. The Clean Air Act clearly attempts to resolve this debate with respect to its provisions by including a provision in the law that declares that the allowance to emit a limited amount of sulfur dioxide is not a property right. One of the benefits of this declaration is that in the event that an awarded pollution right was limited in future years, the declaration, if accepted, would forestall a challenge to such reduction being compensable by law.

Another issue is the determination of the level of emissions actually occurring. Typically, the government relies on businesses self-reporting their emissions, which has the potential to create concern for the integrity of the information received.

Finally, one of the stated purposes of pollution credit trading is to give firms flexibility to comply with pollution regulation in a least-cost manner. The fact that the business may elect to buy pollution credits rather than decrease its emissions because such purchase results in the least cost to the company may raise ethical issues. More pollution is allowed, but the company is maximizing its bottom line and staying within the limits of the law.

Generally, the trading of emissions credits is viewed in many circles to be a beneficial commodity that decreases overall pollution in a profitable market system. The question remains whether the ability to purchase the right to pollute at a lesser cost to a business than it would incur by decreasing its pollutant emissions is a laudable societal goal that should be encouraged and legalized.

—Mary Ellen Wells

See also Environmental Ethics; Environmental Protection Legislation and Regulation; Pollution; Pollution Right; Public Utilities and Their Regulation

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Empathy

Empathy refers to the capacity to put ourselves in the place of others and thereby vicariously experience and understand their emotions, experiences, and values. In this sense, it describes an activity of communication and knowledge. In everyday usage, the term often carries the connotation of sympathizing with another's pain.

The concept of empathy was popularized in late-19th-century German aesthetics by Robert Vischer and Theodor Lipps, who used the term *Einfühlung* ("to feel one's way into") to help explain how people were able to respond emotionally to nature and art through a sympathetic inner imitation of an object. The term *Einfühlung* was translated as "empathy" by the American experimental psychologist Edward Titchener in 1909, a translation that added the connotations of suffering and sympathy.

In some systems *empathy* is sharply distinguished from the everyday meaning of the term *sympathy*—namely, pity or compassion. However, the term *sympathy* as used by philosophers such as David Hume, Adam Smith, and Arthur Schopenhauer (*Mitleid*) primarily denotes the transmission of emotions, which is the key component of empathy. Likewise, psychology has a number of terms ("ejective consciousness," "perspective taking," "role taking") that are analogous to empathy. The term *nacherleben* has been translated as "empathic understanding" and refers to a mode of inquiry in the social sciences (associated with Max Weber and Wilhelm Dilthey) where the investigators attempt to fully put themselves in the place of a historical figure to help explain that figure's actions.

Empathy is frequently listed as one of the most desired skills of an employer or employee. Many businesses administer personality and "emotional intelligence" tests as part of preemployment screenings or promotion decisions, and most of these tests claim to measure a person's empathic skills. While developmental and social psychologists see empathy as a measurable capacity that can be tested and quantified, there is no common standard among the wide variety of tests available. Some have argued that such tests benefit women, who are assumed to be generally more empathic than men. Such "empathy tests" raise questions of invasion of privacy and adverse impact on particular classes of people.

The Nature of Empathy

Commentators generally agree that empathy is an innate human capacity but offer various accounts of how it functions. Some stress a neurophysiological basis for empathy, such as motor mimicry, where the muscles of an observer tense in imitation of the postures of another and thus help produce identical emotions. The role of motor mimicry and other forms of "emotional contagion" suggests that visual stimuli play a particularly important role in empathy, and this in turn relates to presentations of suffering in various media. If images of suffering are more likely to inspire empathy than written accounts, then this must be taken into consideration in public relations campaigns and charitable appeals. Other accounts place more stress on the role of imagination, suggesting that it is the capacity to suspend disbelief and imagine oneself in a different situation that creates a path from idea to impression to emotion. In this account, it is less our registration of another person's emotion and more our cognitive comprehension of that person's situation that leads to empathy.

The exact nature of empathy is also a matter of dispute. For Hume, there is no practical difference between the observed emotion and the empathic emotion. Smith, on the other hand, stresses the secondary quality of such sensations in both intensity and kind, as they are removed from the partiality and immediacy of personal pain. Commentators also differ on the related question of the degree to which empathy involves a dissolving of the boundary between self and other. Schopenhauer, for instance, thinks of sympathy as a complicated procedure through which the ego is temporarily set aside while the distinction between self and other is still preserved.

Ethical Role of Empathy

The ethical role of empathy can be divided into three claims—namely, that empathy (1) is an ethically positive activity, (2) can function as a guide for moral judgments, and (3) is a motivator for ethical action. In moral and character education, empathy is typically listed as one of the key qualities to be developed in students and is treated as a positive in and of itself. Hume regards empathy as a moral end in itself because of its other-directed nature. But it is difficult to make the case that a skill of understanding in itself has a positive moral status. When empathy is invoked in a business context, it is usually at an amoral, cognitive level, such as possessing the skill to understand what a customer wants. Similarly, a malicious individual can use the skill of empathy to better manipulate another person, a case of empathy being deployed for immoral ends.

The two most extensive attempts to systematically ground moral judgment in empathic feeling come from Hume and Smith, and indeed later accounts are most often merely elaborations on their positions. Hume argues that spectacles of virtue and vice arouse in an observer particular feelings of pleasure and pain that function as a moral assessment. But for Hume, these very specific feelings of approbation and disapprobation are only felt when we set aside our own self-interest and instead sympathize with the motivations of others.

In a similar vein, Smith argues that to entirely sympathize with another's emotions means that we view those emotions as appropriate to the circumstances from which they arose; our inability to fully empathize means that we sense an inappropriateness in that person's feelings. If we do not share in the laughter of a coworker telling a racist joke, for instance, our inability to share that emotion carries with it a moral judgment. This comparative understanding of right and wrong extends also to judgments about our own behavior; we regularly construct an imaginary, impartial spectator as a general standard against which to examine the relative appropriateness of our own emotions. Although the ethical duties of empathy are usually placed on the shoulders of the sympathizer, Smith argues that those who suffer also have a duty—namely, to modulate the expression of their pain to a level that makes the communication of that pain possible. But at the same time, he warns that an excessive degree of stoicism can result in less sympathy for others and less of a disposition to relieve their suffering.

Empathy is sometimes invoked when attempting to answer the question of why people do good even when it seems to go against personal interest. Hume assumes that the natural inclination to put ourselves in the place of others helps us move beyond narrow self-interest. A benevolent action that contributes to the common good, such as extending health benefits to domestic partners, may not benefit us directly; however, it is precisely sympathy that interests us in the public good. Some commentators assume that sharing the pain of others automatically leads to the desire to relieve their suffering. What is unclear is whether the motivation is truly to relieve the suffering of another or to do away with the secondary feelings of suffering in ourselves. In any case, the line between self-interested and selfless behavior is by definition blurred in the case of empathy, which involves some weakening of the boundary between self and other. This raises the familiar conundrum of whether behavior can be counted as moral in the strict sense if some degree of self-interest is involved. Nevertheless, empathic feelings can motivate people to do good with a zeal that rarely arises from a merely abstract sense of duty.

Empathy has come under renewed attention in some strands of feminist ethics, in part because it is a capacity that is commonly associated with the culturally feminine. According to these accounts, empathy represents a key element of women's moral experience that is undervalued in traditional ethics, which emphasizes autonomy, universality, and reason at the expense of relationality, particularity, and emotions.

As this dichotomy suggests, the embrace of empathy by empiricist and subjectivist moral philosophies finds its strongest challenge in rationalist schools. Certainly, it is possible to point to examples where empathy can lead to faulty moral judgments, such as overempathizing with an employee who embezzles funds to help support a sick parent. It is also questionable whether a rational, universal moral system can be created from emotions that often seem fickle and fleeting. Such objections are not unnoticed by promoters of empathy. For instance, both Hume's distinction between natural and artificial virtues and Smith's discussion of the influence of custom and fashion on moral sentiments point to their concerns that a moral system built on emotions and empathy might fall prey to social relativism.

Limits of Empathy

Most commentators acknowledge empathy's bias toward the familiar and the "here and now." They argue that it is much easier to imaginatively put ourselves in the place of those who are most similar to us and that we are more likely to feel sympathy for people and situations that are familiar. Likewise, the immediate appearance of someone in pain claims our imagination much more fully than an account of suffering removed in time and space. Despite its relative banality, the pain of a friend who failed to get a holiday bonus may be felt more acutely by a colleague than the pain of thousands of coworkers laid off in another country.

Some thinkers stress that dissimilarity is not an insurmountable barrier. Schopenhauer, for instance, believed that true sympathy erased all difference, the *principium individuationis* that hides the metaphysical identity of all humans. Smith noted that while men are physically unable to experience the pains of childbirth, they nonetheless could empathize with women in labor. He also felt that while our sphere of action is of necessity constricted in time and space, there are no inherent limits on sympathy, and humans can in fact cultivate a universal benevolence. However, the fact that we are much more inclined to empathize with those who "look like us" raises troubling questions as to the usefulness of empathy in making moral judgments or motivating ethical action.

The issue of similarity also applies to the role of empathy at the borders of the human, a topic taken up in the area of animal rights, which poses the question of whether animals are similar enough to humans to inspire true empathy. Many people will claim a sense of empathy when shown an image of a rabbit undergoing an eye irritation experiment for a cosmetics company. More people might pause when faced with PETA's (People for the Ethical Treatment of Animals) 2004 "Fish Empathy" campaign, which uses studies about the complexity of the social and mental activity of fish to encourage people to recognize that fish suffer. Studies of people's willingness to support endangered species find that they favor spending money on larger animals, ones that are presumably easier to identify with. Such examples raise the question of whether a rational or ethical policy of animal rights or environmentalism can be built around capricious identification with dogs and dolphins at the expense of moths and mollusks. Along with the fear that empathy is unable to push past the dissimilar, examples such as these suggest an equal danger of inaccurate projections where the emotions of the self occlude the object. In its original aesthetic sense as outlined by Lipps, the experience of empathy encompasses the pathetic fallacy of projecting human feelings onto the inanimate world, so that an architectural pillar or a leaning tree, for instance, might be felt by an observer to be painfully burdened. If empathy can imaginatively humanize our surroundings, it must be asked how we can assure ourselves that we are not doing the same thing in relation to animals or, indeed, other human beings.

—Clark Farmer

See also Animal Rights; Ethics of Care; Feminist Ethics; Golden Rule, The; Moral Sentimentalism

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EMPLOYEE ASSISTANCE PROGRAMS

Employee assistance programs (EAPs) are a benefit provided by employers to give employees access to confidential assistance to address personal issues, preferably before they affect job performance. When personal problems do affect job performance, EAPs may coach supervisors to effectively support employees as they address those problems, seek and receive counseling or treatment, and return to work.

Employers increasingly turned to EAPs in the 1970s to help employees cope with problems that were adversely affecting job performance and/or conduct. Performance-based interventions to address the individual and organizational costs of substance abuse were widely adopted. Gradually, the EAP's role has expanded to include a variety of support services, including counseling in most work/life issues, as well as conflict and crisis management. Most EAP programs also provide services to the members of the employee's household.

Studies have documented that reduced productivity, increased accidents, increased absenteeism, and increased health care expenditures that result from workplace stress cost U.S. businesses approximately $300 billion annually. The most often cited causes of employee stress are personal, not work related; however, the impact of these issues in the workplace is undeniable. Employers responded to these findings by developing programs to help employees deal with work/life stress. According to the Society for Human Resource Management 2004 Benefits Survey Report, 70% of all U.S. employers offer an EAP.

EAPs may vary considerably in design and scope. Some programs focus primarily on substance abuse problems, while others take an across-the-board approach to a range of individual and family problems. EAPs may include proactive prevention and health and wellness activities, as well as problem identification and referral, and some are directly linked to the organization's employee health benefit plan.

EAPs may be administered internally or externally. An internal EAP is managed directly by individuals who are employed by the company the program serves. The advantage of the internal EAP is that the program can be specifically tailored to meet the needs of the company; however, it may be more difficult to engender the employee confidence in the competence and trustworthiness of internal EAP staff that is critical to the program's success. In addition, internal EAP staff may be challenged to determine if the employee or the employer is the client to whom they have the greater responsibility.

With this in mind, external EAPs have increasingly become the preferred model. An external EAP uses outside counselors who provide services on a contractual basis. EAP contracts may be established for a fixed fee based on the number of employees, regardless of program usage, or on a fee-for-service basis, with the employer paying only for the services that are used. External EAPs tend to have enhanced confidentiality, a broader variety of available services, greater convenience, and lower overall program costs.

In addition to being the right thing to do, employers may realize significant tangible and intangible benefits from providing EAPs to employees. Studies have shown that employers may realize a return of $5 to $16 for every $1 invested in an EAP, resulting from reductions in absenteeism, tardiness, workplace accidents, and insurance claims. Intangible benefits include improvements in employee work quality, motivation, commitment, loyalty, and morale that result from a strengthening of the psychological contract between employer and employee.

—Carmen M. Alston

See also Benefits, Employee; Crisis Management; Employee Relations; Family-Friendly Corporation; Loyalty; Outsourcing; Stress, Job; Work and Family; Work-Life Balance

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EMPLOYEE MONITORING AND SURVEILLANCE

Companies have always been concerned about the loss of trade secrets and misrepresentations by employees with respect to performance, hours, and expenses. Furthermore, because of new laws requiring extensive protection of client data, organizations are resorting to measures more extensive than ever to make sure that such data are not compromised by employees. Employee monitoring and surveillance involve the activities taken on by an organization to observe its employees and their activities, usually, but not always, related to the employees' jobs. Employee monitoring often begins before the hiring decision is made, as the organization performs a variety of background checks. An organization may also administer tests to uncover the employee's personality as well as the nature of after-hours activities, such as the use of illegal substances. After being hired, the employee is often subjected to an even greater degree of scrutiny by being monitored through video surveillance, phone recordings, network scanners, and computer scanners. An employee's location may also be registered through smart-chip identification badges.

The ethical issues surrounding employee monitoring involve the organization's right to manage the workplace toward profit and the employees' right to privacy. In a competitive economy, the employer has the right to hire the ideal individual for the job. To make such a decision, the employer requires background information that can only be obtained via background checks, credit reports, and drug testing. Since all employers are under an obligation to provide a safe and productive environment, many employers perform such checks to address the potential liability under the "negligent hiring" tort. Furthermore, in several countries, many industries, including child care, are required to perform background checks on potential employees under the law. Employers justify employee monitoring after the hiring decision as a way to drive efficiency, performance, and productivity, all of which positively contribute to profit. While the organization seeks to learn more about its employees, the employees are driven by the right to privacy, protected primarily by the Fourth Amendment, statutes, and the common law in the United States and by equivalent laws in other countries. Privacy has been argued to be a matter of prudential interest, a utilitarian concern, and a moral right. In all these cases, privacy is implied to be a sphere of noninterference that requires protection. However, the resulting protections are not independent of circumstances but are rather subject to trade-offs in society's welfare, including fulfillment of the rights and obligations of the employer.

Background Checks

Many employers subject their employees to at least one type of a background check. The background checks are used in making hiring, promotion, and retention decisions. The most common types of background checks are related to an individual's credit, personality, lifestyle, and reputation. These reports are often delivered by consumer reporting agencies (CRAs), and the privacy and accuracy of the reports are protected by the Fair Credit Reporting Act (FCRA). The amendments to the FCRA, as implemented in 1997, have dramatically increased the employers' responsibilities when conducting background checks.

Credit Reports

Perhaps the most common type of background check used by employers is the credit report. One of the reasons for obtaining a credit report is that an employee who is deep in debt may not have solid financial management skills and is arguably more likely to embezzle money from the company. In most industries (trucking being the exception), the employer must first notify the individual in writing that a report may be used and obtain a written authorization for its use. However, if the credit report—or any other form of consumer report for that matter—results in an adverse action against the individual, such as termination or the denial of a job, the employer must take a series of steps to comply with the FCRA. Before the adverse action is taken, the individual must be given a pre–adverse action disclosure, including a copy of the consumer report. The purpose of this step is to allow the individual to verify that the data gathered are correct and to provide a chance to dispute the report with the CRA and the employer. If the employer does decide to take the adverse action, the employee must once again be notified after the adverse action is taken. From an ethical perspective, the investigation of an individual's financial background—an infringement on the person's privacy—may be difficult to justify for a job where money handling and the possibility of embezzlement are limited.

Driving Records

Employers also frequently request the driving records of employees, future and current. Although information concerning traffic violations, license status, and accidents is open to the public, personal Department of Motor Vehicles data are somewhat protected by the Drivers' Privacy Protection Act of 1994. It is typical for an employer to monitor the public domain of an employee's driving record if he is involved in a job where frequent driving is required, such as food delivery or courier services. Moreover, in accordance with utilitarianism, the employer has a moral obligation to do so in order to ensure that the employee's driving ability is not negatively affecting the public. Even the theories of ethical egoism support the notion of driving record monitoring because it is in the employer's best interest to have safe drivers since these people are less likely to get into accidents that will negatively affect the company's bottom line.

Criminal Records

Although criminal record checks are legal, there are once again restrictions on their use. The employer may reject a potential employee based on a felony conviction, but the felony must be related to the job duties. For example, a bank has the legal right to deny a convicted bank robber a job as a teller. On the other hand, denying a job based on past arrests (where a conviction did not occur) and past drug treatment is illegal in many U.S. states and many countries. It may be argued that the employer has a moral responsibility to investigate employees' criminal backgrounds for the sake of the safety of their coworkers and that the employer has a financial motivation to do so in order to limit the costs of potential litigation. However, the moral consequences of these actions are less clear-cut. If the employer wrongly assumes that the potential employee will inflict harm on the company or its staff and decides against hiring him or her, the employer may be harming the individual and society as a whole. After all, if all employers were to make this assumption and take the same action, a convicted individual would not be able to find employment at all and would thus effectively be forced into a life of criminality to be able to survive. At the center of this debate lies the notion of whether society, including its commercial organizations, has a moral obligation to assist previously convicted individuals and whether an individual with a history of criminal behavior can be aided in not exhibiting that behavior in the future. Although the discussion above highlights the reasons for criminal record investigation, it is difficult to strike the right balance between privacy rights and employee safety. Privacy rights are often supported by the claim that their protection is necessary to protect a value, such as self-determination, which is essential to the individual's status as a person.

Drug Testing

Safety, security, competence, and efficiency are all negatively affected by employees' substance abuse. Employers frequently subject potential employees to mandatory drug tests, and some organizations have extended drug testing to be done throughout the employees' careers with the company by implementing random mandatory drug-testing programs. Although opponents to testing have argued that random drug testing is not a proper way to test for sobriety in the workplace since the employees' time off is their own, U.S. government employees are held to a higher standard than private sector workers. In accordance with President Ronald Reagan's Executive Order 12564 and the Drug-Free Workplace Act of 1988, government employees are expected to abstain from illegal substances on and off the job. While, on average, government employees are held to a higher standard, many private organizations followed suit by implementing similar measures. In the case of a positive drug test and evidence of negative behavior, the organization has an ethical responsibility to protect its staff and other stakeholders from harm caused by a nonsober individual. However, returning to the argument of reforming previously convicted individuals, the organizations may have an ethical responsibility to aid present employees with a substance abuse problem.

In addition to the more common urine and saliva tests, polygraph tests are also frequently used to determine an individual's substance use, in addition to these tests' other uses for security-related reasons. However, the polygraph test's use among private commercial investigators has been restricted by the Employee Polygraph Protection Act. This act was enacted in response to the polygraph's frequent erroneous results and the relative ease with which the test results can be compromised. With exceptions granted to certain security positions and holders of government contracts, the law prevents employers from using the test as a preemployment screening method and from firing an employee based only on the results of the test since the employer obviously has an ethical obligation not to take adverse action against an employee based on information that is likely to be faulty.

Audio Surveillance

The Electronic Communications Privacy Act of 1986 (ECPA) has attempted to limit the amount of audio surveillance that an employer can use. This law prohibits employers from intercepting employee wire communications, including e-mail and facsimile in addition to telephone. However, exceptions exist if the employer maintains the system or the employee's consent for monitoring has been obtained; there is also the so-called business-use exception. The business-use exception covers cases where there is a legitimate business purpose for surveillance, such as screening for employees making personal calls when the company has a policy of not allowing personal calls to be made on their phones. However, further limits exist on the business-use exception. To extend the personal call example, the employer can only monitor so much of the conversation as to be able to tell that it is a personal call.

Audio surveillance, as well as video, time, computer, and networking monitoring (discussed below), is widely used by superiors to track those working for them. However, these methods are not usually consistently implemented. For example, while it is rapidly becoming a common practice for executives to be able to read the e-mail and monitor the phone conversations of regular employees, the regular employees are not able to survey the activities of the executives. Alternatively, organizations are cautioned to institute a more equitable rule, one that compromises or protects the privacy of all employees equally, regardless of their rank in the company.

Video Surveillance

Closed circuit television (CCTV) is increasing in popularity as a tool to monitor the workforce. Employers and proponents argue that CCTV discourages theft, physical confrontations, and sexual harassment. The manner of its use must also be lawful, and it must not unreasonably intrude into the employee's personal business. In addition, employees must be made aware that they are under video surveillance, unless the employer can expect to prove that informing the employees is not feasible or would distort the data collected. In the United States, CCTV regulation falls under the ECPA. CCTV operation has also been addressed extensively by the British Data Protection Act of 1998.

The balancing act of profit versus privacy is a difficult one for organizations using CCTV. It is clear that an organization can use CCTV to reduce adverse actions by its employees and customers against itself and its staff, thus increasing its profit via cost reduction. However, CCTV can rob employees of their privacy without just cause. For example, some CCTV operators have been observed to be using CCTV to zoom in on body parts of female customers and coworkers.

Time, Labor, Access, and Location Monitoring

Employers have been able to justify the use of extensive time, labor, access, and location monitoring of their employees by arguing that it is necessary for day-to-day business operations. In the United States, there is currently no law specifically addressing the location privacy of employees, a critical component of tracking access, time, and labor. Furthermore, emerging technologies such as biometrics allow for major extensions to the traditional employee-tracking systems and require little human power and money to implement and operate. The locations of factory floor employees can now be traced as a part of companies' time and labor systems (T&L). In typical contemporary implementations of T&L, employees record their time and labor location by scanning their magnetic badges while transferring between machines. Technologies have been developed to prevent identification scams, such as badge swaps. Some T&L security modules call for employees to enter personal information, such as their social security numbers, in addition to scanning their badges. The expectation is that the employees will be disinclined to share such information with their peers, thus preventing purposeful misidentification.

For decades, access to restricted areas has been controlled by security guards and identification badges. However, automation via biometric-based systems, such as fingerprint and eye retina scanning, are becoming more common in work areas in need of high security. For applications where very accurate identification of individuals is needed without the extensive hardware required by biometric methods, radio frequency identification (RFID) tags can be implanted into an employee's skin, making the mapping of the device to the user rapid and precise. Such futuristic measures are only likely to be needed in workplaces requiring the highest security.

In addition to granting clearance to restricted areas, RFID tags can also be used to track the location of employees. However, whereas RFID is capable of tracing an individual only in localized areas, technologies based on the global positioning system (GPS) can place employees around the world. For example, companies with a large sales force can easily trace the locations of their traveling salespeople around the globe by using the GPS capabilities of employees' cellular phones.

Unlike audio, video, computer, and network surveillance, access and location monitoring tends to be more universally implemented. After all, even high-level executives need a badge to pass a security guard who does not know them. On the other hand, T&L systems are rarely used for employees working in white-collar settings. Furthermore, time, labor, and even expense monitoring tends to be more relaxed for executives than for lower-level employees, resulting in more privacy for individuals of higher rank. It is difficult to draw a clear conclusion on whether the extensive infringement on employee privacy results in greater gains for the organization as a whole.

Computer and Network Monitoring

As computers saturate the workplace, organizations have found it necessary to monitor employees' use of their networks, servers, and personal computers. This type of surveillance was not just a result of the desire to protect trade secrets and prevent employees from submitting false time and expense reports. As consumer data protection legislation, including the Financial Modernization Act, also known as the Gramm-Leach-Bliley Act, and the privacy component of the Health Insurance Portability and Accountability Act, passed into law, companies found themselves legally bound to protect sensitive customer data from internal as well as external risks. The most typical tools used by companies are keystroke loggers for tracking workstation usage and packet monitors for examining network traffic.

E-mail monitoring, especially, has received a lot of attention because it has led to a number of employees being fired for distributing offensive and harassing e-mail using the employer's e-mail system. It is considered imperative that a contemporary employer have a clear policy delineating the rights of employees on the employer's e-mail system. Many companies have chosen to state that their e-mail systems are for business use only. Others allow the use of their e-mail systems for nonbusiness purposes but maintain ownership of all the e-mail sent through the system. Regardless of policy, U.S. employees have rarely succeeded in legally proving that they have a right to privacy when it comes to company e-mail systems. Because the system is maintained by the employer and is used for day-to-day business operations, it can be monitored under the exceptions to the ECPA.

As with T&L as well as audio surveillance methods, the extent of computer and network monitoring often depends on the employee's status within the organization. The decision to use a particular policy must consider privacy rights and the organization's right to profit. While the employees should have the right to do as they wish with their own time, it is in the interest of an organization to obtain maximum levels of productivity from its employees. Computer and network monitoring can be used to discourage non-work-related activities such as personal communication and online gaming. On the other hand, as discussed in connection with audio surveillance, an organization ought to consider pursuing an equitable monitoring policy, in addition to one that compromises employees' privacy rights to the smallest extent required to achieve significant productivity gains.

Conclusion

The level of employee surveillance and monitoring differs around the world, with U.S. employers and those in developing economies having the most far-reaching surveillance abilities and European and Australian/New Zealand employees having the most privacy protections. Overall, however, employees can expect little protection for their privacy in the contemporary workplace. The desire of employers to verify that employees are being honest about their work is not the only explanation for this situation. In fact, new laws calling for extensive consumer data protection have led to the high level of employee surveillance today. However, in monitoring the activities of current and potential employees, organizations must take into careful consideration the ethical impact on their employers, their stakeholders, and finally, society as a whole.

—Zoya A. Voronovich and Kai R. Larsen

See also Internet and Computing Legislation; Privacy

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Employee Protection and Workplace Safety Legislation

Employee Protection in the Workplace

Employee protection and workplace safety address the question of who is responsible for ensuring that employees have protection from various dangers on the job. While employees certainly bear some responsibility for their own protection and safety, the employer may be held responsible for not only providing protective equipment and information but also ensuring that employees properly use that protection. When the cost of workplace protections in more heavily regulated markets increases, demand for labor in less regulated, lower-cost markets may increase, resulting in potential trade-offs between cost competitiveness and worker safety.

Early Perceptions of Protection Needs

A century ago, agriculture and small-scale retail were the dominant work settings, although manufacturing was growing. Agriculture has long been a major area of inadequate worker protection, from both an economic and a social perspective. Many agricultural pursuits were small-scale and family owned. The economic pressure of having limited financial resources sometimes led to inadequate worker protection. Often equipment was not well maintained, and farmers could not afford the latest technology of the era. Poor maintenance precipitated many accidents, but few records were maintained.

As manufacturing grew, the same mind-set was transferred from the agricultural sector; thus, employees were not viewed as resources to be protected. There were plenty of able-bodied men, and the pay was better than in agriculture. The major motivation for work was regarded as financial. Manufacturing plants, especially in clothing and textiles, were not considered safe by the employees. Fire was a critical threat, given the massive cotton dust accumulated each day. No one considered that employees needed protection from the dust in the air; lung damage was not a well-understood issue in health circles. A similar unknown problem in the lumber mills of the early to mid-20th century was sawdust. The most common cause of employee fatality in the lumber, textile, and clothing mills was fire. Yet, 100 years ago, there was little effort or apparent interest in fire safety.

Employer's Role in Hazard Identification

Each workplace is unique, and different hazards are likely to be found in each. However, some common categories of hazards can be identified. Equipment hazards abound in most industrial settings: Equipment is often large, heavy, and at times dangerous. Regretfully, employers have not always taken the time to instruct their employees about the hazards, emphasizing instead the use of the machine and the need to minimize downtime. When rushed, employees act like anyone else; they become careless, and accidents occur.

Lumber mills, metal-stamping plants, and firefighting situations are among the highly accident-prone job sites. Proper use of equipment must be continuously emphasized by the employer.

Numerous environmental hazards may be present, ranging from explosives to chemical leaks to malfunctioning equipment. Each work site will have its unique environmental hazards. The employer is charged with having an inventory of all potential hazards and working to reduce such hazards to the lowest levels. Protective equipment and protective clothing are crucial in some work areas. For example, persons in construction sites may be required to wear hard hats. However, a typical site visit reveals that many managers and some workers avoid wearing protective gear. The equipment may be provided, but whose responsibility is it to ensure that a worker uses the equipment? Legally, it is the employer's. Regretfully, the consequences of not assuming that burden are minor, and many employers do not even enforce their own work rules.

Unsafe Conditions and Whistle-Blower Protection

In many workplaces, employees best understand the conditions requiring management attention. Employees may be aware when conditions are dangerous and senior management is unaware of the problem. In some cases, there may be an organizational culture that communicates to employees that they are to maintain silence about the workplace. The Occupational Safety and Health Administration (OSHA) addresses this concern by offering protection from reprisals brought about by reporting hazards or other data under OSHA. If an employee is subjected to reprisals, the employee may complain to the Department of Labor for protection.

Violence in the Workplace

In the contemporary media, workplace violence has received increased attention. Employees have been attacked, in rare cases even murdered, on the job, by both fellow employees and strangers. Violence in small retail establishments has led to the installation of electronic surveillance cameras, but the electronic records are only valuable as evidence after the fact. Banks, and their large stores of cash, are also vulnerable, as are taxi drivers and other cash-carrying workers. However, employers have rarely viewed the problem as one of employee protection. In manufacturing facilities, there is often more restricted access as compared with retail and banking. Thus, the violence has tended to be more work-community related; for example, disgruntled employees have instigated violent episodes.

The National Institute for Occupational Safety and Health reports that an average of 20 workers are murdered each week in the United States. Homicide is the second leading cause of workplace deaths, second only to motor vehicle crashes. The majority of workplace homicides are robbery-related crimes, with only about 10% committed by coworkers or former coworkers.

In addition, there are 18,000 victims of nonfatal workplace assaults each week. Most nonfatal workplace assaults occur in service settings such as hospitals, nursing homes, and social service agencies. About half the nonfatal assaults in the workplace are committed by a health care patient. Nonfatal workplace assaults result in more than 800,000 lost workdays annually.

Employer Strategies for Workplace Violence Prevention

A number of strategies have been developed for reducing the occurrence of workplace violence. A few examples of prevention strategies include improving the visibility within and outside the workplace, policies for handling cash, physical separation of customers from employees, brighter lighting, security devices, escort services for employees, and an emphasis on employee training. A workplace violence prevention program should include three variables: a system for documenting incidents, well-communicated procedures to be taken in the event of incidents, and truly open communication between employers and workers. An effective employee education program is crucial to making a meaningful difference in preventing workplace violence in any type of business.

Smoking in the Workplace

Until the 1980s, it was common for a large proportion of the work population to smoke, even on the job. Some employers were in fact protective of the employee's right to smoke. By 1990, most employers were developing no-smoking policies based on OSHA standards. By 2005, a majority of workplaces were nonsmoking.This is an example where research, legislation, public pressure, and potential large penalties in court have reduced the threat of a known danger. Public pressure was a major force.

Workers' Compensation

One reason employers have directed attention to employee safety and protection is the potential cost incurred in not paying attention to the early warning signs. Early in the 20th century, states found that workers injured on the job became a drag on the economy. Thus, states began to develop protective legislation to protect workers' future earnings and minimize the impact on the employer. Workers' compensation laws seek to ensure that employees who are injured or disabled on the job are provided with fixed monetary awards, eliminating the need for litigation. Benefits are also provided for dependents of workers who are killed because of work-related accidents or illnesses. Laws in some jurisdictions protect employers and fellow workers by limiting the amount an injured employee can recover from an employer and by eliminating the liability of coworkers in most accidents. State statutes establish this framework for many types of employment, from office work to metalworking to hospital employment. Federal statutes are limited to federal employees or those workers employed in some unique and significant aspect of interstate commerce, such as stevedoring. The laws in the 50 states are similar but differ greatly in the fixed-income formula and in the ease of receiving the funds.

Workplace Safety Legislation

As the U.S. workplace has evolved, both in physical and in human dimensions, the interest in minimizing the dangers in the workplace and encouraging safe conditions and behavior has grown, as have the number and breadth of stakeholders. Since 1902, there have been safety statutes at the state level. Each state has reacted to safety concerns within its borders and offered protective legislation. For example, Virginia has a safety statute relating to coal mining, whereas Arkansas does not. Critics have often been vocal about the enforcement of the state statutes, claiming that workers have no real protection. Ultimately, the subject gained sufficient support for the federal government to consider the workplace safety issue.

Union Influence on Legislation

During the 1960s, labor unions noted an increased concern among their members about poor safety conditions and increased accidents and fatalities as workplace changes took place and efforts to control costs began anew. The United Steelworkers of America used a modified nominal group technique in several of its university-cosponsored summer leadership programs and came away after 2 years with a clear notion of some major concerns: a perceived lack of concern for workers, which was growing especially in larger firms; lack of maintenance of safety equipment or lack of needed equipment; lack of training in the safety area; lack of government inspections; and discharge of workers involved in safety mishaps.

The result of an intense union lobbying effort was the (Williams-Steger) Occupational Safety and Health Act of 1970. One indication of the success of the statute is the inclusion of safety provisions in 9 out of 10 labor agreements today. Unions have been the moving force in the law's establishment and in its evolution during employer-dominated legislative sessions since its passage. The major OSHA provision is its "general duty" clause; the employer is required to provide each employee with a safe and healthy working environment. The workplace must be free of all recognized hazards that may cause illness, injury, or death to an employee. Furthermore, the employer must comply with all the occupational safety and health standards adopted by the Department of Labor. Recognizing that not all employers would receive the act in a positive manner, OSHA requires employers to provide access to federal safety inspectors and post any notices and maintain an extensive array of records on employees and on the actions taken by the employer to meet the OSHA standards.

Workplace Inspections

Workplace inspections, designed to reduce hazards to workers' health and safety, may be of two types. Random inspections usually target specific industries where hazards are known to exist. The targets are changed periodically in an attempt to alleviate the more serious problems first. While there have been very significant investments of time and money by employers and the federal and state governments, the injury rates changed little in the first 30 years. The Department of Labor has initiated a new infusion of funds for employee safety training, with an emphasis on personal hazard identification and self-protection.

OSHA responses to employee complaints under the law yield more effective enforcement. Usually, an employee complaint is made only after some effort has been made internally to have potential hazards addressed. However, the problem often becomes one of enforcement of inspector orders and the relatively small monetary penalties available under the law. The collective bargaining process and the use of joint safety and health committees have minimized the risks in major industries. Employees in smaller firms and in nonunion firms are fearful of filing complaints, although there is a whistle-blower protection clause in the act. While the act provides protection, an affected employee must file a complaint within 30 days of the alleged reprisals.

Major Impediment to Higher Priority

Employee protection can impose costs that affect global competitiveness. Employers in developing markets may not face the same level of safety and health regulation and thus face lower economic costs. In recent years, employers have lobbied heavily against increasing regulatory requirements, arguing that higher costs lead to diminishing returns.

—Jerald F. Robinson

See also AFL-CIO; Employee Assistance Programs; Free Speech in the Workplace; Labor Unions; Occupational Safety and Health Administration (OSHA); Violence in the Workplace; Women in the Workplace; Working Conditions

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Employee Relations

Employee relations refers to the interactions between employees and their employer. Some similar, but slightly different, terms are human resources, human relations, labor relations, industrial relations, and personnel administration or personnel services. Generically speaking, the term includes an array of employer efforts, such as recruitment and selection, orientation, training, performance appraisal, safety, equal employment opportunity (EEO), handling of employee complaints, discipline, and even management training and, in some instances, union relations.

Terminology Evolution

The terminology has clearly evolved in this business functional area. During the 1930s and 1940s, the department overseeing the interaction of the employer with employees was known as the Payroll Department, a central area of interaction. From the 1950s to the 1960s, it came to be known as the Personnel Department, run by low-level staff and with negligible power within the organization. Some have referred to it as the maternal arm of the employer, with mostly women employees, who are primarily clerical, dealing with tax and insurance forms along with payroll. In work organizations with labor unions present, the department often became known as the Industrial Relations Department. If the organization was not in an industrial setting and yet was unionized, the usual term of the era was Labor Relations Department, and the emphasis was on dealing with the union.

The terminology evolution was accelerated by legislation in the 1960s and 1970s. Federal statutes changed the organizational outlook on both the employee as a resource and the significance of the staff function. The staff evolved from clerical work to developing professional and technical skills to cope with the implications of the new statutes. In the mid-1970s, professionalism became a central theme as the American Society for Personnel Administration (ASPA) evolved to meet the needs being expressed. The membership demanded more professional tools to cope with their new responsibilities. The various legislative acts placed penalties on the organization and even on senior management for failure to comply; senior management suddenly needed assistance internally, and providing that competence internally gave the newly minted professionals power within the organization. ASPA has since become SHRM, the Society of Human Resource Management.

Employee Relations Function

Employee relations is usually charged with each of the following functions.

Recruitment and Selection

Word of mouth during the pre-1960s was a key method of locating new employees. Existing employees had friends or family who wanted to work, and the employee was a natural referral agent for the current employer. For those jobs not filled in that manner, newspaper classified advertising served well. For senior positions, professional recruitment firms (headhunters) were used, but at a significant cost.

Employers changed their techniques during the period from the 1970s to the 1990s to meet the nondiscrimination mandates of legislation. By the 1990s, the nondiscrimination philosophy was more entrenched in large firms and government agencies. Also, a new recruitment method had arrived: online computerized recruitment sites such as Monster.com.

Selection is always a challenge; finding the best person for any job proves precarious due to the potential subjectivity. Today, it has evolved to a committee process involving several persons at various levels and in various functions of the organization. The employee relations staff choose what appear to be the top candidates, based on published job specifications and the qualifications presented on paper by the applicants. Naturally, the job may be in evolution, and the specifications may be changing even as the process unfurls; and the qualifications on paper are not always error free. Beginning in the 1990s, new software has allowed better screening as applicants often apply online, and the forms used are matched against the job specifications, and each applicant is scored. Still, the same criticisms are possible, but the screening itself is quicker and likely to be less subjective.

Once the screenings have been completed for an opening, the candidates' credentials are forwarded to the department manager requesting a new employee. A selection committee normally interviews the candidate and seeks to offer a realistic assessment of what the job entails and any unusual aspects of the work to be done. At the end of the interview, the committee writes an evaluation of the candidate based on its perception of the candidates as compared with what is needed. Sometimes this will yield a written score (1–100 scale). When all the candidates have been interviewed, the committee makes a recommendation. The employee relations staff will contact the candidate's references, if they have not earlier, and ultimately, after a short period, make an offer of employment to the recommended candidate. No one person is able to dominate the process, which results in reduced potential for discrimination. The process is expensive to the employer compared with earlier processes but likely yields a higher-quality employee as well as one who will be better able to work in a diverse workplace.

Orientation

The new employee of the 1940s to 1960s would spend a short period in the employee relations department to complete forms, for taxes and insurance, and then receive some form of employee rules. The new employee would then go to the work area to meet fellow workers and be given a description of the work to be done and the machinery to be used. In most subsequent business research, this orientation model was found to be inadequate.

By the 1970s and into the 1990s, a renewed emphasis on orientation was obvious. One reason was the need to reduce turnover, which had been documented often, as well as to maintain a safer workplace. The orientation often became a multiweek effort to ensure that the new employee not only was able to do the required work on the appointed equipment but also understood the company culture and was able to work in a safe manner. At the turn of the century, much of the orientation information can be provided on a DVD to be watched at home and shared with family members who might be more supportive of the work ethic and company culture. The bottom line for orientation is to reduce turnover and maximize the productivity potential.

Training Programs

Training in the 1940s and 1950s was narrow and directed completely at job skills and provided at the operator level with no employee relations involvement. Training departments developed during the 1960s in response to EEO legislation and became more widespread in the 1970s after the Occupational Safety and Health Act (OSHA) was enacted. Training became an employee relations function and more behaviorally based. Supervisory development programs were instituted during this period. EEO workshops laid a heavy emphasis on management at all levels. Some programs were offered to enhance preparation for promotion. Universities, community colleges, vo-tech (vocational technical) schools, consulting firms, and new training and development firms now present an array of programs for all levels of employees. Given the growth of external offerings, in-house offerings have often been reduced. Another trend is placing the burden of preparation for future jobs on the employee. This is both a cost-cutting tool and an effort to encourage self-help among employees. In many cases, the state will offer skills training at a public facility as part of an incentive package to recruit an employer to locate a new facility or expand an existing facility. These training incentives can often make or break a location decision.

Performance Appraisal

Beginning in the 1960s, performance appraisals (reviews) became common, partly in reaction to EEO mandates. The employee relations staff maintains the personnel records of all employees and schedules appraisals according to organization policy or labor agreement. Typically, an appraisal form is provided to managers with a due date. After the form is completed and the employee meets with the supervisor, the form is returned to the employee relations department. The form is always signed by the supervisor and may be signed by the employee. The performance appraisal may be used to correct poor job behaviors and also as a basis for pay increases.

Safety

Prior to the 1970s, safety legislation was state based and varied widely in coverage, regulations, and corrective actions. Their administration was handled by line managers and not by the employee relations staff. All that changed with the passage of OSHA. A new federal coverage was developed, with periodic unannounced work-site inspections and employer fines. To prepare for the implementation of this massive new program, many employers developed a safety program for assisting management in ensuring workplace compliance. Having no other place to house the program, the employee relations department had the safety function added to its portfolio. The insurance industry, which provides workers' compensation coverage, has worked closely with business firms to enhance the safety programs and, usually, expand the employee relations staff.

Equal Employment Opportunity Efforts

The EEO office was established in most firms and public bodies following the 1964 Equal Employment Opportunity Act. Although in some organizations it has developed into a freestanding department it was started in the employee relations department—a best-fit spur-of-the-moment decision in most organizations. The staff in this function has grown as employees have learned about the provisions of the act and its amendments. Employee counseling has proven to take the largest share of the total time, while receiving complaints and their investigation is a close second. Management has needed training sessions.

Handling Employee Complaints

A major tool for employee relations was introduced in the 1930s, although most firms fought its use then. As unions were certified in many industries between the 1930s and the 1950s, one major ingredient in their agreements was a grievance procedure. Such mechanisms were costly in terms of work hours lost. In nonunion firms, employees may view the employee relations staff as almost neutral and may gravitate there when a problem develops, usually with the supervisor or the company system or policy. Most public bodies and some nonunion companies have developed an employee complaint process. Most do not use a professional arbitrator but have developed a variety of final adjudication methods to differentiate them from the union procedures. This has proven to be an effective tool in resisting the organizing of unions.

Discipline Oversight

Until the 1960s, discipline was dispensed by managers without recourse under the laws of most states. Since then, most companies and public bodies have a progressive discipline policy, with the employee relations department as the final applicator of the discipline that has been recommended by line managers. For discharges, many company policies provide for a review of the case by the employee relations staff.

In the 1980s, a new tool, the employee assistance program (EAP), was developed to reduce discharge situations. While it began as a means of helping employees avoid discharge due to a list of special reasons, it has grown to be offered to all employees. While most plans are sponsored by individual companies or public entities, unions have also formed EAPs for their members, especially for drug, alcohol, and family financial rehabilitation. Some EAPs are housed in the employee relations department, while others are housed off-site and even operated outside the work organization by contract agencies.

Management Training

Management in industry was not worker oriented during the rise of heavy industry operations, and so unions arose. In the 1950s, industry became the primary employer of military leaders, and a new leadership approach was instituted. By the late 1960s, an alternative management style was being promoted, and management training offices were developed to institutionalize the new ideas, many of which were the product of research beginning in the early 1960s. The management development efforts have grown to include programs in total quality management, continuous improvement, and EEO and diagnostic programs such as Myers-Briggs Type Indicator and leadership studies. The management training efforts of some firms are now being subcontracted to emerging training and development companies, which can provide a multitude of programs more cheaply and on an on-call basis.

Employee relations can contribute to the development of a motivated diverse workforce to achieve success in a competitive environment. Senior management support is critical, however.

—Jerald F. Robinson

See also AFL-CIO; Diversity in the Workplace; Employee Assistance Programs; Labor Unions

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Employee Retirement Income Security Act of 1974 (ERISA)

The Employee Retirement Income Security Act of 1974 (ERISA) is a federal law that sets minimum standards for most voluntarily established pension and health plans in private industry to provide protection for individuals in these plans. ERISA requires plans to provide participants with plan information, including information about plan features and funding; establishes fiduciary responsibilities for those who manage and control plan assets; requires plans to establish grievance and appeals procedures for participants; and gives participants the right to sue for benefits and breaches of fiduciary duty.

While private sector pension plans have been in existence since the latter part of the 19th century, their period of greatest growth occurred following the decision by the Supreme Court in the Inland Steel Case of 1949. The Court upheld the ruling by the National Labor Relations Board that pension benefits constitute wages and are thus subject to collective bargaining, as are other conditions of employment. By 1974, nearly 31 million workers were covered by private pensions, with 27 million enrolled in defined benefit plans. Private retirement plans had become a major source of income for many retired workers.

In the early 1970s, the U.S. Senate held hearings on deficiencies in the pension system, which included the high rate of ineligibility for pension benefits among plan participants and the forfeiture of pensions even after many years of service. These hearings set the stage for the eventual passage of the ERISA. Among its other objectives, ERISA established the minimum standards employees must satisfy to ensure the receipt and protection of benefits when they either leave their jobs or die. Among other things, ERISA established participation rules and vesting requirements for pensions (and other covered benefit plans) to qualify for preferential tax treatment.

In 1974, ERISA established funding rules that in their most basic outline require sponsoring employers to calculate the present value of future payments the plan owes, plus the present value of future benefit payments the plan is likely to owe in the future. The plan sponsor then is required to compare those obligations with the value of the assets held by the plan. If the present value of the liabilities exceeds the value of the assets, a contribution is required. However, the act, and the rules promulgated to guide sponsors in compliance with the act, goes into extensive detail related to the assumptions to be used in valuation and the terms and conditions related to funding adequacy.

ERISA also sought to protect benefit plan assets by designating as fiduciaries those who control, manage, or provide investment advice relative to plan assets, subject to fiduciary responsibilities. The primary responsibility of fiduciaries is to run the plan solely in the interest of participants and beneficiaries and for the purpose of providing benefits and paying plan expenses. Fiduciaries are required to act prudently in order to minimize the risk of large losses. In addition, they must follow the terms of plan documents and avoid conflicts of interest. Fiduciaries who do not follow the requirements stipulated may be held personally liable to restore any losses to the plan or to restore any profits made through improper use of plan assets.

To further protect the benefits promised to employees under a qualified pension plan, Title IV of ERISA established the Pension Benefit Guaranty Corporation to ensure the payment of plan benefits under specified conditions.

ERISA requires plan sponsors to provide to every participant in a retirement or health benefit plan, or a beneficiary receiving benefits under such a plan, a summary of the plan, called the summary plan description (SPD). The SPD must provide participants with information on what the plan provides and how it operates. It must provide information on eligibility to participate, how service and benefits are calculated, when benefits become vested, when and in what form benefits are paid, and how to file a claim for benefits. If a plan is changed, participants must be informed, either through a revised SPD or in a separate document. In addition to the SPD, the plan administrator must give participants a copy of the plan's summary annual report each year. This report is a summary of the annual financial report, which most plans must file with the Department of Labor on Form 5500.

Initial ERISA regulations stipulated that most defined benefit plans should allow employees to participate on attaining the age of 25 or after the completion of 1 year of service, whichever comes later. Later, the Retirement Equity Act of 1984 required almost all plans to lower the age requirement to 21. ERISA also established rules related to an array of plan provisions, including vesting, breaks in service, survivor benefits, payout options, and many other plan features that are beyond the scope of this summary.

While most equate ERISA with pension plans, the act also covers self-funded welfare plans—for example a group health plan in which the organization pays the claims against the plan versus purchasing coverage through a third-party insurer. Historically, states have controlled traditional health insurance sold within a state. However, ERISA exempts those employers that "self-insure" their health benefit plans from state regulation, taxation, and control. Under these plans, the employer pays the health care claims directly, instead of purchasing an insurance policy to pay claims, and thus escapes state regulation of insurance.

The exemption from state regulation that ERISA provides self-insured plans has been an important feature for many large organizations that have operations in multiple states, enabling them to provide a common benefit plan for all employees versus purchasing plans on a state-by-state basis that comply with the requirements imposed by each state. In 1974, only 6 million Americans were insured through self-funded plans. Today, that figure stands at 55 million, or approximately 40% of all group health care coverage in the United States. Research indicates that the majority of employers that converted to self-insurance did so to avoid state regulations.

There have been a number of amendments to ERISA, expanding the protections available to health benefit plan participants and beneficiaries. One amendment, the Consolidated Omnibus Budget Reconciliation Act, provides workers and their families with the right to continue their health coverage for a limited time after certain events, such as the loss of a job. Another amendment to ERISA is the Health Insurance Portability and Accountability Act, which provides protections for employees and their families who have preexisting medical conditions or might otherwise suffer discrimination in health coverage.

Social and Ethical Issues

While ERISA has provided a set of standards and rules for plans to follow in order to receive favorable tax treatment, some critics have argued that the regulatory burden imposed by the funding rules of the act on defined benefit pension plans are at least in part responsible for the dramatic decline of such plans in favor of defined contribution plans. Others point to the act as weakening the ability of states to mandate various types of health care coverage for employers providing such benefits to workers in their states. Since ERISA preempts state control over self-funded health care programs, state legislatures that mandate coverage—for instance, coverage for same-sex partners or for mental health services—are unable to do so except for health insurance programs purchased by an employer from a third-party provider. As such, most of the largest employers are able to avoid the mandates to expand coverage sought by states through the protections afforded by the act.

—Ken A. Sloan and Joanne H. Gavin

See also Benefits, Employee; Moral Hazard; Pension Benefit Guaranty Corporation (PBGC); Pensions

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Employee Rights Movement

Employee rights refer to the entitlements that employees have vis-à-vis their relationship with their employers. These rights dictate how employers are expected to treat their existing employees. Such entitlements are, however, contingent on the nature of the workplace environment—that is, whether it is "public" (linked to the government) or "private." Whereas public employees benefit from the protection afforded by the United States Bill of Rights, private employees do not, except where explicit protection is offered by other state or federal legislation.

Public/Private Distinction

Which rights are protected depends first and foremost on the nature of the workplace. Workplaces are distinguished as either public or private depending on their relationship to the state. Public workplaces are those that are operated by and for the state—that is, governmental agencies. Private workplaces, on the other hand, are defined as those that are separate from the state—that is, privately owned corporations. Although this distinction is often hidden and arguably artificial, the classification of a public workplace versus a private workplace is instrumental in determining the rights granted to employees and the responsibilities assigned to employers.

An employee of the public workplace is protected by the Constitution and its Bill of Rights. Many of the rights protected by the Bill of Rights are considered natural rights or fundamental rights. Even so, these rights are not protected for employees in private workplaces. The private workplace is therefore void of many rights—that is, freedom of speech, due process, and so on—considered fundamental outside the workplace.

The reason for this is quite simple: The original intent of the Constitution was based on the history of the American colonies and their relationship with England. The purpose of the Bill of Rights was to protect American citizens from excessive encroachment by the government, not to isolate citizens from one another. The founders of this country focused on civil society, without knowledge of the strong presence that business would have on the future United States and without anticipating in any way the significant impact this would have on the evolution of distinctly public and private workplaces. Although the operation of these workplaces is remarkably similar, the rights granted to their respective employees remain distinct.

Employment at Will

The default rule for employment in the majority of jurisdictions in the United States is employment at will (EAW). EAW operates in the absence of an employment contract and is recognized as the ability of either the employee or the employer to terminate their relationship at any time, for any reason, or for no reason at all. No justification for termination is required. The only prohibition is against reasons specifically deemed illegal (i.e., whistle-blowing, in those states where whistle-blower protection is in effect, gender or racial discrimination, and so on).

Unless otherwise specified, employees in the private sector are considered employees "at will" and can be terminated at any time. Except in cases where legislation has carved out specific exceptions or in Montana, the single "right-to-work" state, employees have no job security.

Although both employers and employees are ostensibly granted equal rights according to EAW, it can be argued that these rights are equivalent but not equal. There is a significant power imbalance often at play in that it is typically easier for employers to find new employees than vice versa. Furthermore, because no reason for termination is required, employees are stripped of their rights to due process and their prior investment in their work is ignored.

Due process is also a concern. Due process refers to the rights that individuals have not only to be notified of the charges made against them but also to respond to these charges. Due process is linked to employee rights in that whereas public employees are guaranteed due process, private employees enjoy no such protection.

Legislation

With EAW as the prevailing norm, legislation has been passed to carve out rights for employees. There currently exist significant legislative and statutory exceptions to EAW. The Family and Medical Leave Act of 1993, for example, mandates that employers allow employees in both private and public workplaces to take an unpaid leave of absence due to illness, maternity, or caring for a sick family member. Employers are required to keep open the position of the employee on leave, who has a protected right to return to his or her job at the end of the leave.

There also exist several pieces of legislation regarding discrimination in the workplace. For instance, the Americans with Disabilities Act prohibits discrimination based on disabilities in the workplace. Firing an employee based on a disability is deemed inappropriate and illegal. The Civil Rights Act of 1964 forbids employers from discriminating against employees according to race, color, religion, sex, or national origin. Discrimination based on age is also prohibited by the Age Discrimination in Employment Act of 1967. Though these pieces of legislation are not without certain exceptions, they provide employees with rights not otherwise granted to them according to EAW.

Privacy and Technology

Advances in technology have further limited the rights of employees in the private workplace. Legal systems have experienced difficulty keeping up with the fast pace of technological innovation. This has resulted in numerous challenges to privacy. In fact, employees in the private sector enjoy no reasonable expectation of privacy. Furthermore, what little privacy they previously enjoyed is slowly being eroded.

An example of this stems from e-mail in the workplace. People today communicate frequently by e-mail in both their work and their personal lives. This form of communication is very different from other forms of communication because it is more difficult to destroy and much easier to trace. Although many people consider this personal communication, in fact, it is not. Employers have the right, which many exercise, to monitor employees' e-mail. Some consider this not only a right but also a responsibility, in light of the possibility of inappropriate exchanges taking place via e-mail. Furthermore, monitoring applies not only to work-related e-mail but to any e-mail accessed by the employee in the workplace. The rationale is that the employer has the right to monitor anything that takes place at the workplace, with or without the employee's knowledge.

Pre- and Postemployment

The relationship between employees and employers is strictly defined. Job candidates (preemployees) and retirees (postemployees) have interests but few if any protected rights. Employee status differs from pre- or postemployee status in that employees have a current existing relationship with their employers. This is not the case for preemployees, since no relationship has been established. Postemployees had a previous relationship with their employer, but this relationship is no longer in existence.

This is significant in that while the rights of employees are limited, the rights of pre- and postemployees are virtually nonexistent. The rights protected for pre- and postemployees are only the fundamental civil rights—that is, the right to not be discriminated against on the basis of age, skin color, sex, disability, and so on. Job candidates are subject to any means of testing the employer deems appropriate, which can include inquiries into credit histories, driving records, medical records, and so on. Neither permission nor disclosure is required. Failure to concede to the "requests" of the potential employer constitutes a justifiable reason for not hiring a job candidate. Employers are not required to provide the reasons for not hiring potential employees, and they are permitted to test them by any means they deem acceptable.

As for retirees and other postemployees, because they no longer have a relationship with their employers, the same conditions apply. This is unfortunate in that postemployees still have a stake in their employer. They might need job references, and many have invested in pension plans and the like.

Conclusion

The workplace in the United States has changed drastically in the past 20 or 30 years. Employment relationships have beginning and end points in terms of rights, whereas previously, employment relationships were considered to be indefinite. Issues connected to preemployment and postemployment rights, EAW, and public versus private workplaces were not at the forefront. Today, however, long-term employee-employer relationships are becoming increasingly rare.

Although Americans tend to assume that they receive the greatest workplace protection, in fact, this is not always the case. Cultural values in many workplaces outside the United States, such as in Europe, create very different workplace standards. This is interesting, particularly as compared with other countries, where the balance of power is tilted much more in favor of employees. For example, in Canada and in many countries in Europe, women are guaranteed 1 year of paid maternity leave. This is just one example of how workplace norms differ around the world.

—Tara J. Radin and Megan E. Dayno

See also Age Discrimination; Americans with Disabilities Act of 1990 (ADA); Civil Rights; Disability Discrimination; Due Process; Employee Monitoring and Surveillance; Employee Protection and Workplace Safety Legislation; Employee Relations; Employment Discrimination; Equal Employment Opportunity; Equal Pay Act of 1963; Free Speech in the Workplace; Genetic Information in the Workplace; Hostile Work Environment; Human Rights; Job Security; Just Wage; Labor Unions; Right to Work; Workplace Privacy

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Employee Stock Ownership Plans (ESOPs)

Employee stock ownership plans (ESOPs) are employee benefit programs that make a company's employees owners of that company's stock. Two features of ESOPs make them unique among qualified employee benefit plans. First, ESOPs are required to invest mainly in the employer's stock. Second, these stock plans can borrow money from or on the credit of the employer, allowing ESOPs to serve as a tool of corporate finance.

ESOPs are the main form of employee ownership in the United States. At the end of 2004, the approximately 11,000 ESOPs in the United States owned an estimated $600 billion in assets and covered 10 million employees. Most U.S. ESOPs are large enough to exert a major influence on company strategy and culture, and about 2,000 ESOPs have total ownership of their companies. ESOPs also operate in Canada, the United Kingdom, Europe, India, Egypt, South Africa, Argentina, Japan, and elsewhere.

ESOPs are deferred compensation plans, with employer contributions growing tax-free until the employee leaves the company. At that time, the employee can roll the proceeds from the ESOP into another tax-advantaged retirement plan, such as an individual retirement account. ESOPs are "defined contribution" plans, meaning that the employer makes yearly contributions without specifying the resulting benefit in advance. ESOPs are called "qualified" plans because their sponsors can qualify for tax benefits by following laws designed to protect participants' interests.

ESOPs differ from cooperatives, collective ownership, and ownership by trade unions. ESOPs give individual employees ownership while professional managers accountable to a board of directors handle day-to-day operations. The company remains private and for-profit. ESOPs also differ from stock option benefits and 401(k) plans.

Companies use ESOPs for a variety of purposes. The most common use is to transfer ownership of closely held companies. In such cases, an ESOP provides tax advantages, a ready market for the owner's shares, and the opportunity to transfer ownership gradually. These features make ESOPs valuable planning tools as business owners near retirement. Companies also use ESOPs to borrow money at a lower after-tax cost. Many companies use ESOPs to motivate and reward employees. Research suggests that ESOPs boost employee loyalty and productivity when combined with management styles that encourage employee input.

A small but highly publicized number of ESOPs are formed to defend against potential or imminent takeovers. Such ESOPs generally fail to stand up in court because they appear to entrench management rather than serve the interests of employees. For similar reasons, setting up an ESOP to fend off unionization is considered an abuse.

ESOPs embody an economic theory called "ownership economics," "binary economics," or "economic democracy." This theory supports the ownership of productive assets by a broad-based group of citizens rather than by the state or by a wealthy minority.

History

San Francisco investment banker and corporate lawyer Louis Kelso is credited with inventing the ESOP in the 1950s. Kelso argued that allowing workers to share in owning capital-producing assets would strengthen capitalism. The first ESOP was established in 1957. At that time, ESOPs lacked clear legal authorization to borrow money in order to acquire shares, and few companies showed an interest in the idea.

The 1974 Employee Retirement Income Security Act (ERISA) provided a statutory framework for ESOPs, and other laws gave ESOPs tax advantages. By 1990, 10,000 ESOPs were operating in the United States. The number peaked at 11,500 ESOPs in 2002 and 2003. Several times, Congress has modified the laws governing ESOPs. Important laws affecting ESOPs include the 1984 and 1986 Tax Reform Acts, the 1996 Business Job Protection Act, the 1997 Taxpayer Relief Act, and the 2001 Economic Growth and Tax Relief Reconciliation Act.

How ESOPs Work

To start an ESOP, a company first sets up a trust fund. How the fund gets its money determines whether the ESOP is "basic" or "leveraged."

In a basic ESOP, the company gives cash or new shares of stock to the trust fund. If the employer contributes cash, the ESOP buys stock from the company or from one or more of its shareholders. The company provides additional cash or securities to the ESOP each year so that the ESOP can continue buying stock. These contributions are tax deductible up to 15% of the payroll.

Leveraged ESOPs borrow money to buy shares. The company then contributes cash so that the ESOP can repay the loan. Company contributions are tax deductible up to 25% of the payroll.

Typically, all full-time employees over the age of 21 participate in an ESOP. Each employee has an individual ESOP account. Employees increase their ownership rights to the account by accumulating seniority, a process called "vesting."

Vested employees receive their shares when they leave the company. Unless there is a public market for the shares, the company must buy the shares back at fair market value. Private companies must obtain an annual, independent valuation to determine their share price.

In ESOP companies, groups of employees may form an ESOP committee to work on the company's strategic ownership objectives. This committee may be called an "Ownership Committee" or an "ESOP Advisory Council."

ESOP Participants' Rights

Participants of ESOPs in publicly traded companies have the same voting rights as other shareholders.

ESOP participants in private companies have the right to direct the trustee to vote their allocated shares on major issues such as liquidations and mergers.

ESOP participants have legal rights to the information they need to protect their interests. For example, ESOP sponsors are required to give participants a Summary Plan Description explaining matters such as how the ESOP works, where to take questions and complaints, and sponsors' and fiduciaries' names and addresses. In addition, the sponsor must let participants see and copy a summary annual report on ESOP activities and assets. This report must be issued on a Department of Labor 5500 form. Sponsors must give participants a shorter version of the report. Each year and at other times specified by law, ESOP participants must receive a benefit statement. The statement must include the fair market value of the ESOP shares and other assets, as well as the employees' vesting status. Participants have the right to challenge the accuracy of this information. ESOP participants also have the right to view trust documents.

Contrary to some media reports, ESOPs do not give participants legal rights to information such as officers' salaries and who owns how many shares. However, most ESOP companies disclose some non-salary financial information.

Fiduciary Duties

ERISA requires ESOP fiduciaries to run the ESOP solely for the benefit of its participants and beneficiaries. This requirement is called the "Exclusive Benefit Rule." The participants' and beneficiaries' interests are defined as receiving benefits and defraying the plan's administrative costs. Incidental benefits to other parties are allowed. If the fiduciaries' impartiality appears uncertain, they may seek independent advice.

ERISA also requires ESOP fiduciaries to adhere to the "Duty of Prudence." Fiduciaries must behave with the same skill, care, prudence, and diligence that one would expect of a prudent person facing similar circumstances.

At times, ESOP fiduciaries must make difficult decisions. For example, they may have to vote on whether to tender shares, how to respond to a tender offer, and how to manage financial difficulties in the company.

Ethical and legal issues most often arise when companies form an ESOP to defend against a tender offer. Conflicts of interest can arise when trustees are also officers or directors of the company or lack independence from management.

Advantages of ESOPs

ESOPs provide a number of advantages to companies. U.S. law gives these plans significant tax breaks. For example, when a company borrows money through an ESOP, repayments for both the principal and the interest are tax deductible. Business owners who sell their share in a company to an ESOP can often defer or avoid capital gains taxes. In addition, ESOPs can produce substantial savings when partly or completely substituted for defined benefit pension plans. Some experts say ESOPs help businesses recruit, keep, and motivate employees.

ESOPs offer several advantages to employees. For example, employees participating in an ESOP can accumulate company stock tax-free. In addition, ESOP participants gain access to certain information about the company and have at least some voting rights regarding their shares.

Disadvantages of ESOPs

Not all companies find ESOPs suitable. Start-up and administrative costs are high, strict reporting is required annually, and ERISA rules are complicated. As a result, very small companies and those with high turnover are likely to find ESOPs too expensive. The obligation to buy back stock from employees who leave or retire restricts a company's cash flow. Resentment can grow if ESOP participants feel that managers do not treat them as part owners of the company. Partnerships and most professional corporations are barred from setting up ESOPs. An S corporation—a type of corporation that passes income, losses, and tax items on to shareholders rather than being taxed as a corporation—has lower contribution limits and lacks the rollover advantage given to other corporations.

ESOPs have a number of disadvantages for employees. Unlike defined benefit plans, ESOPs put all the risk on employees. The concentration of ESOP assets in company stock makes ESOPs riskier than plans with greater diversification. If the company declines, the employee cannot sell the stock, and the Pension Benefit Guaranty Corporation, which insures many ERISA plans, does not cover ESOPs. The debt involved in setting up a leveraged ESOP can restrict a company's cash flow, adding to ESOP participants' risk. Critics say the Department of Labor, which has responsibility for overseeing ESOP fiduciary guidelines in the United States, lacks the resources and political freedom to protect employees. On the other hand, diversification rules, plus the tendency of ESOPs to move out of company stock in the long term, help reduce these risks. Another offsetting factor is companies' tendency to contribute a higher percentage of pay to ESOPs than to other retirement plans. Nevertheless, experts advise employees to view ESOPs as an investment rather than as their only or main retirement plan.

—David P. Schmidt

See also Conflict of Interest; Employee Retirement Income Security Act of 1974 (ERISA); Individual Retirement Accounts (IRAs); Job Security; Market for Corporate Control; Self-Ownership

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Employment Contracts

An employment contract is a legal agreement that governs the terms according to which one or more parties provide personal services for one or more other parties, typically in the context of an employer-employee relationship. A contract may be *express*, that is, reciting terms for performance between the parties, or it may be *implied* in the law according to the behavior of the parties. The regulatory frameworks, policy justifications, and business practices that govern employment relationships vary widely across jurisdictions, with the two principal approaches being employment-at-will and for-cause regimes.

Types of Personal Services Agreements: Employment Agreements and Independent Contractor Agreements

There are two primary categories of personal services agreements: employment agreements and independent contractor agreements. The criteria for distinguishing between these types of work relationships in the common law include the degree of the worker's integration into the operations of the employer's organization, the scale and scope of the worker's service, whether the worker uses his or her own tools and materials, the number of employers the worker serves, whether the worker risks a financial loss in the relationship, the employer's degree of oversight and approval for the work product, and, especially, whether the employer retains the *right* to control the manner and pace of the work.

If applying these common-law factors supports the conclusion that the provider of personal services is an independent contractor, then the parties are acting at arm's length and are truly separate legal entities. The legal rules governing their relationship would be the general rules of contract. However, if applying the common-law factors supports the conclusion that the provider of personal services is an employee, then the relationship constitutes employment in the strict sense, with concomitant common-law duties of agency owing to the employer, including fiduciary duties of care, loyalty, and good faith. To sustain a practicable scope for this analysis, the remainder of this discussion will deal with the employment relationship.

Types of Employment Contracts: Express and Implied Contracts

An employment contract is a personal services agreement between an employer and an employee that is legally enforceable. The two typical forms of contract in the common-law tradition are express contract and implied contract. An express contract is one in which the parties enumerate the terms of their agreement in ways that allow it not only to be clear for practical purposes but also to be legally sufficient and enforceable. For example, an express contract should specify the identities of the parties, their respective performance commitments, their respective consideration, the timing and means for payment, the standards for assessing the sufficiency of the work product, the term of service, the governing law(s), the procedure(s) for giving notice of termination, and the means for adjudicating disputes.

In addition, the formation process for an express contract must satisfy legal standards for the document to be enforceable, including the legality of the subject matter, the mental competency of the parties, the real or apparent authority of the parties, and the legal majority of the parties (typically the age of 18 for natural persons). A contract may be in writing or oral, but it is prudent—and in many cases legally necessary under the statute of frauds in the applicable jurisdiction—to execute it in writing, particularly when the term of service exceeds 1 year from the date of the agreement.

An implied contract is an agreement that a court construes and interprets as legally enforceable retrospectively, on the basis of the actions of the parties. If a court finds that the parties behaved as though they believed that a contract existed between them, then it is likely that it will rule that there impliedly was a contract, as a matter of law.

Regulatory Frameworks for the Employment Relationship: Employment-at-Will and For-Cause Regimes

The two main regimes for construing the nature and durability of employment relationships before the law and in the context of business practices are (1) employment at will and (2) a for-cause framework. Under the employment-at-will doctrine, the employee ("servant," in legal parlance) serves at the pleasure of the employer ("master"). The employer may terminate the employee's service for a good reason, for a bad reason, or for no reason at all. This has been the default rule for most jurisdictions within the United States since at least the middle of the 19th century, and it is in the United States that this policy continues to enjoy its widest favor.

Against the backdrop of this default rule, there are four principal categories of exceptions that circumscribe the scope for employment at will in the United States—that is, four examples of situations in which a justification for an employment action may be necessary. First, for employees of the federal government, there are due process protections that arise from the Fifth Amendment to the U.S. Constitution. Such protections stem from legal constructions of incipient property rights in this employment and the special dual roles of the government, not just as an employer but also as a civil power with the capacity to deprive people of such property as well as life and liberty. Under the Fourteenth Amendment to the Constitution, this protection likewise extends to employees of state and local governments, under the doctrine of equal protection. (The principal exception to this protection for government employees relates to attorneys who serve the government in the role of counsel; it is a long-standing public policy and standard for professional practice that a client must remain free to choose its counsel.)

Second, statutory prohibitions protect employees from arbitrary or discriminatory employment actions based on (1) activities that are beneficial or even necessary as a matter of public policy and (2) status factors—for example, gender, age, family relationships, ethnic origin, religious beliefs, and national origin.

An example of the first type of statutory protection is the National Labor Relations Act of 1935, which prohibits retaliation against employees for union activity, litigation against their employer, or testifying against their employer in court. Other statutes, including the Occupational Safety and Health Act of 1970, prohibit retaliation for reporting or helping investigate dangerous, unethical, and/or illegal situations. This act also authorizes the Occupational Safety and Health Administration to administer the whistleblower provisions of 13 other statutes, such as trucking, airline, nuclear power, pipeline, environmental, and securities laws.

Other statutes extend the second major type of protection by prohibiting arbitrary or discriminatory employment actions based on the aforementioned status factors, which the federal and state governments have determined to be worthy of protection as a matter of public policy, particularly because these factors tend to be irrelevant to the substance of the employment relationship. Examples of such legislation at the federal level include the Civil Rights Act of 1964, the Age Discrimination in Employment Act of 1968, the Pregnancy Discrimination Employment Act of 1978, the Americans with Disabilities Act of 1990, and the Family and Medical Leave Act of 1993. (While some local jurisdictions include sexual orientation among these protected status factors, the federal government does not.)

Third, common-law protections on the basis of precedent and public policy help prevent arbitrary employment determinations that curtail employees' basic rights and duties when it comes to political participation. For example, it generally is illegal for an employer to terminate or penalize an employee for exercising his or her right to vote or for serving jury duty.

In the same way, common law and public policy generally prohibit employment policies and practices that constrain employees from acting in the public interest. For example, employers generally may not threaten or retaliate against employees for reporting serious dangers to life or property or information about crimes, at least without risking lawsuits for retaliatory discharge. Substantive codes of conduct of professional associations have complemented the aforementioned statutory protections by providing frameworks for assessing the legal and ethical reasonableness of their members' actions in whistle-blowing about such matters, particularly in light of the aforementioned long-standing fiduciary duties of care, loyalty, and good faith, and these codes have provided a measure of additional protection in some state jurisdictions.

Fourth, parties to an employment relationship may contract away their right to at-will terms either through individual contracts or through group contracts—for example, collective bargaining agreements. Courts tend not to consider the question of the sufficiency of legal consideration in contracts between parties that bargain in good faith and at arm's length. As a result, the primary constraints on employment contracts are those that apply to contracts generally, including the aforementioned factors of majority age, mental competency, and real or apparent authority of the contractors, as well as legality of the subject matter of the contract.

Because of the aforementioned doctrine of implied contract, parties must exercise care not only in the legally cognizable terms to which they expressly assent but also in their behavior toward one another, which a court may construe as evincing a willingness to form a bond of obligation. In the past, factors such as a long period of service, an employer's oral or written assurances about long-term employment, the wording of job application forms, the offering of service-dependent benefits, and the content of employee procedure manuals have supported findings of implied contract. In light of such rulings, employers, particularly corporate employers, have implemented prophylactic procedures to minimize such risks, for example, in the form of express disclaimers of contract and notices that all employment is at will, sometimes with requirements for written employee acknowledgments.

While these are the principal exceptions to the policy of employment at will in the United States, two points are worth noting. First, these legal restrictions derive their legitimacy from substantive moral principles. Hence, it is meaningful to interpret these justifications and assess their normative sufficiency apart from the positive laws by which constitutional framers, legislators, judges, and contractors attempt to express them. The discussion below demonstrates this in terms of the principle of autonomy, the freedom to contract, and the duty to promote efficient markets for labor and capital.

Second, despite differences in legal systems—for example, common-law and civil law frameworks—and business and litigation practices around the world, the systematic questions regarding the nature and scope of employment contracts persist across societies, including how to balance interests in efficient employment markets with just treatment of employers and employees. The language surrounding issues of employment at will often is jurisprudential, but the issues are deeper than the idiomatic exigencies and concerns of countries' legal systems.

The other major framework for governing the employment relationship is a for-cause regime, which limits significant employment actions, including terminations, to justifications on the basis of "good" reasons, upon some articulable due process arrangement that takes into account factors relevant to the substance of the employment relationship, including employee performance, market conditions, and resource constraints on the employer's ability to continue to employ the employees. Montana has been the principal jurisdiction to follow a for-cause regime (for postprobationary employees), with the passage of the Wrongful Discharge From Employment Act in 1987.

In August 1991, the National Conference of Commissioners on Uniform State Laws proposed the Model Employee Termination Act (META). This act represented a compromise that provided an example set of laws for states to consider for adoption, to promote just treatment for employers and employees across the United States, by preserving incentives for effective job performance, reducing uncertainty, and lowering costs for litigation and damages. The provisions also extended the scope for legal protections to classes of employees beyond the typically wealthier groups that were willing and able to risk the costs of litigation. Although many states have considered provisions along the lines of the META, none has adopted its terms legislatively, and employment at will remains the default rule throughout most of the United States.

Justifications for and Critiques of Employment-at-Will and For-Cause Regimes

While the employment-at-will regime seems harsh from the perspective of employees, a principled justification for it lies in the right of the parties to contract freely—that is, without coercion or deception (at a minimum). Even though the language of this principle invokes "contracting," it does not refer principally to a legal notion of contract. Rather, the usage in this normative context is similar to the meaning of a social contract, in that it refers to the ground rules for the relationship between the parties. (It is not exactly the same because a traditional social contract approach typically looks at a broader scope of relationships.) A key feature that this notion of employment contracting holds in common with the social contract model is the focus on ex ante agreements between employers and employees, as demonstrative of the freedom of the parties. The moral legitimacy for contracting arises from the autonomous judgment of the parties in (1) discerning their respective interests and (2) forming agreements that they *intend* to be resilient enough to govern ongoing, evolving relationships, even through adverse conditions beyond their control.

A corollary to this rights-based contractual claim is the right of each party to protect and to determine the use of its property—namely, the capital of the employing organization in the case of the employer and the productive capacity, or personal capital, of the worker in the case of the employee. The ownership rights of the respective parties reflect their capacity for autonomous contracting. One of the ways in which they manifest this autonomy is in forming employment relationships, with few or no barriers to entry and exit.

This reciprocity in contracting capacity lends a formal legitimacy to employment at will, in that either party may enter or terminate a contract provided it does not coerce or defraud the other. To enjoin an employee from terminating an employment relationship on the basis of his or her autonomous judgment would be to constrain unjustly his or her freedom to contract and, what is just as important, his or her freedom to terminate contracts.

The correlative argument for employment at will is that it likewise would not be justifiable to restrict the freedom of the employer to terminate the relationship. Public policy would not support imposing an employment relationship on either party, and so, despite incidental ex post claims, deprivations, and hardships that individual employers and employees might experience, their rational ex ante preferences would be to preserve the freedom to contract. In other words, the logic of employment at will as a moral argument and a public policy assumes that employers and employees as respective classes of contractors agree to support this regime as the most effective way to protect their respective interests.

When they are not discrete classes, that is, when employees own all or part of their employer, then the justification for employment at will involves recognizing a principled proportionality between the employees' interests as workers and as owners. Such owner-employees seek to safeguard their autonomy by preserving in a balanced way the capital in their personal productive capacities and the organization's capital. As they do this, they consider the respective markets for these resources in the short term and over the long term. As employees, they have options for finding other jobs, and as capitalists, they have options for holding or trading in their investments. Balancing these risks and opportunities in a practicable proportion is an ethical duty that employee-owners owe to themselves, to one another, and to those who depend on them for the prudent management of these stores of wealth. As a consequence, owner-employees should consider that the advantages they might gain as workers through constraints on the practice of employment at will might pale in comparison with the long-term costs they bear as capitalists.

The ethical justification for a for-cause regime lies principally in appeals to the autonomy of the parties and to justice as due process, both substantively, in terms of the bases for entering, modifying, or terminating an employment relationship, and procedurally, in terms of the recourse that the parties have for appeal and possible revision or reversal of the decision. Under a for-cause regime, only "good reasons" suffice for making significant employment decisions, because the emphasis is on the cogency of the determinations as they implicate the parties' autonomy rather than on the mere license to make them.

Out of respect for this autonomy, such a policy does not permit "bad reasons" as bases for such decisions, nor does it permit facially arbitrary or unreasonable decisions. The constitutional, statutory, common-law, and contractual exceptions to the employment-at-will rule above effect a similar result, by disqualifying large classes of bad reasons. However, these exceptions do not exclude merely "unreasonable" bases for employment actions. Defenders of the practice of employment at will would argue that the law should permit parties the discretion to act arbitrarily—even foolishly—provided that they do not act coercively or fraudulently, and that it is preferable to leave the regulation of arbitrary and foolish behavior to the forces of markets for labor, capital, and reputation.

In addition to invoking the moral autonomy of employees to justify a for-cause regime, one can point to the moral benefit of promoting efficiency in markets by distributing information essential for markets to function. When employers inform employees of the reasons for their termination, this can strengthen the efficiency and effectiveness of the market for labor. Current and prospective employees can learn the expectations of employers and the standards for performance that will merit recruitment, retention, and promotion. On a macroeconomic scale, this will benefit the participants in the labor market, both employers and employees.

However, such practices also can increase the legal liability and risk for employers significantly, since these revelations involve others in the bases for management's deliberative process regarding employment decisions. Putative reasons for dismissal may not fare well under scrutiny by those inside and outside the employing organization, who may view the reasons as pretexts for discriminatory and/or retaliatory policies or actions. Even when the employing organization observes a demonstrable discipline in such practices and carefully documents its contemporaneous judgments, it can become vulnerable to a broader scope of litigation than under an employment-at-will regime—that is, for retaliatory discharge, discrimination, and even defamation.

While an analogy with the aforementioned protections that public sector employees enjoy would be facially appealing as an additional justification for a for-cause scheme, critics would argue that such a construction would risk conflating substantive enduring differences between the public and private sectors, not the least of which are the qualitatively distinct constitutional and ethical interests of government employees in protection from government expropriation of their property, liberty, and lives. Regardless of the comparative scale, scope, and power of corporations and other private organizations, they do not pose the same qualitative threat to these fundamental rights that a government agency does when it functions as both an employer and a promulgator and enforcer of laws. It is possible to draw analogies with constitutional conceptions of due process in order to justify a for-cause regime, without insisting on a de facto extension to the private sector of practices for government employees.

A for-cause framework does not reject the freedom to contract that underwrites the doctrine of employment at will. Rather, it focuses on the material circumstances of the asymmetries in knowledge and power that obtain between employers and employees in the bounded rationality, the opportunism, and, especially, the asset specificity of the parties—for example, in the investments they make in training, in career development, and in serving clients, customers, stockholders, and other stakeholders. The assumption underlying a for-cause regime is that there are normatively significant barriers to entry and exit from the employment market and employment relationships and that these conditions pose particular risks for the moral autonomy of employees.

As a result, support for a for-cause regime does not require abandoning the ex ante contracting model—for example, on grounds that subsequent breakdowns in employment relationships, or other circumstances, justify abrogating a "social contract" in favor of protecting employees to the detriment of employers. This would open the door to special pleading and arbitrary conditions that would endanger the interests of all parties to employment relationships, if only because it would raise the cost of contracting.

Rather, one can preserve a contracting model and structure procedures that reflect these asymmetries and give preference to the interests of employees for substantive and procedural due process. A contracting model need not impose a policy of employment at will. Contracting is consistent with a for-cause regime as well, as long as there are ethically justifiable procedures to protect the interests of the parties to the employment relationship, with special deference to the moral autonomy of employees. (Such policies likewise should protect the interests of employers when asymmetries of information and power favor employees—for example, when an employee exerts significant influence on the employer's prospects for success, through his or her level of authority or specialized talents.)

—Lester A. Myers

See also Employee Monitoring and Surveillance; Employee Protection and Workplace Safety Legislation; Employee Relations; Employee Rights Movement; Employment Discrimination; Equal Employment Opportunity; Ethical Role of the Manager; Freedom of Contract; Free Speech in the Workplace; Gender Inequality and Discrimination; Hostile Work Environment; Procedural Justice: Philosophical Perspectives; Property and Property Rights; Regulation and Regulatory Agencies; Religious Discrimination; Reverse Discrimination; Right to Work; Whistle-Blowing; Working Conditions; Workplace Privacy

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Employment Discrimination

Employment discrimination is basing employment decisions on criteria unrelated to the applicant's qualifications for the job, generally related to race, gender, ethnicity, and so on. In an effort to have employees and applicants for employment judged on the basis of their qualifications for the job rather than on the artificial basis of prejudgments about a group the employee or applicant may belong to, in the United States, it is illegal for an employer to discriminate against employees or applicants for employment on the basis of certain criteria set out in federal and state statutes. Under federal law, it is illegal for an employer to discriminate primarily on the basis of race, color, gender, religion, national origin, age, or disability. Employers cannot discriminate regarding workplace benefits or decisions for employees including their hire, termination, discipline, training, promotion, pay, job assignment, or any other term or condition of employment.

In the United States, there are laws prohibiting employment discrimination at the federal as well as the state level. Most states also have their own employment discrimination laws, generally called fair employment practice laws, which are virtually the same as the federal laws. While the state laws may be stricter than the federal laws, they cannot be less strict. Therefore, some state laws have added categories not included in the federal law or included less stringent thresholds for application of the laws (e.g., requiring an employer to have only 4 employees before the law applies rather than 15). Some states have added categories such as marital status, sexual orientation, physical appearance, or political affiliation as a basis for employment discrimination. State claims are generally handled by the state's fair employment practice agency.

Applicants or employees who believe that they have been victims of illegal discrimination have a right to take their claim to the enforcing agency to seek redress. For violation of federal laws, this is the

Equal Employment Opportunity Commission (EEOC). Claims are handled by the EEOC free of charge (though if claimants wish to engage an attorney, they may do so at their own cost). Handling of claims may involve mediation, investigation, or adjudication, as appropriate. If the applicant or employee is not satisfied with the EEOC's final decision on the claim, he or she can then generally seek relief in a federal court. If the employee is found to have been discriminated against by the employer or someone working for the employer, he or she may receive as a remedy, as appropriate, reinstatement, back pay, front pay (for failure to hire because of discrimination), compensatory damages, punitive damages, restoration of lost seniority, injunctive relief, or other relief as the agency or court deems appropriate.

Employment discrimination claims must be based on the theory of disparate treatment or disparate impact. Disparate treatment is discrimination on the face of the employer's policy itself—that is, a policy that does not allow women to be hired for construction work or men to be hired as receptionists. While disparate treatment discrimination is deemed intentional discrimination, the discriminatory intent need not be stated by the employer and instead can be gathered from the policy itself.

Disparate impact employment discrimination involves an employment policy that is facially neutral but that has a greater negative impact on one group than on another. It is statistically based. Disparate impact is generally defined as one group not performing at least 80% as well as another group under an employer's policy. For instance, a policy of hiring only those who are at least 5 feet 4 inches in height and weigh 140 pounds or more has been found by courts to have the impact of screening out a disproportionate number of women, who tend to be shorter and slighter, as well as men from ethnic groups whose members tend to be, on average, shorter and slighter, such as Asians or Hispanics, than are most American men. If the policy is found to have a disparate impact on a group protected by law, the employer must show that the policy has a business necessity. Even if business necessity is shown, the employee or applicant has the right to prove that what the employer sets forth as business necessity is actually a mere pretext for discrimination. For example, the employer has a policy requiring all employees to be able to lift 50 pounds. This may have a disparate impact on women since many more women than men may not be able to lift 50 pounds. The employer shows that the employees will be required to lift heavy packages as part of the job. The employee then proves that most packages weigh only 25 pounds or so and males who cannot lift 50 pounds have been hired. If this is so, the employer is liable for gender discrimination.

After passage of the Civil Rights Act of 1964, subsequent legislation was passed barring employment discrimination on the basis of age, disability, medical leave for care of family members, or pregnancy and against Vietnam veterans. Before the Civil Rights Act, there was the Equal Pay Act of 1963 and the Post–Civil War Statutes. Although they were not passed specifically for employment protection as the later statutes were, the Post–Civil War Statutes were used to a limited extent for that purpose.

There are several statutes governing employment discrimination. Below is a brief description of the main statutes and their coverage.

The *Civil Rights Act of 1866* was passed to allow blacks, who had no right to contract under slavery, to have the same right to enter into and enforce contracts as whites. Before the Civil Rights Act of 1964, it was used to challenge racial discrimination, using the employer's refusal to enter into a contract with the black applicant as a basis for suit. It was of limited use for discrimination on the job, however, since it did not cover performance of contracts, only the entering into and enforcing of them. In the 1991 amendments to the Civil Rights Act of 1964, Congress amended this 1866 law to include also contract performance so that job discrimination could be covered by this law. However, since Title VII provides a comprehensive administrative structure for employment discrimination claims, it is preferred and the one most often used.

Executive Order 11246, first issued as Executive Order 8802 in 1941 by President Franklin D. Roosevelt and the final version by President Lyndon B. Johnson in 1965, is the law from which affirmative action arises. Affirmative action is conscious inclusion of those who have been shown to be excluded from employment. The executive order requires that anyone who wishes to contract to provide the federal government with goods and/or services of $10,000 or more must agree not to discriminate in employment on much the same basis as required by Title VII of the Civil Rights Act. If the contract is for $50,000 or more, the employer must also agree to conduct a workplace assessment showing the female and minority representation in the employer's workplace. The expectation is that their presence in the workplace should be roughly proportional to their availability in the area from which the employees are drawn. If there is a pronounced underrepresentation and the employer wants to contract with the federal government, the employer must agree to work to remedy the underrepresentation. This is generally called an affirmative action plan.

Quotas, or absolute numbers of employees mandated to be hired or promoted, are prohibited under the executive order but remain a persistent source of resentment for those who think quotas are actually required by the law. Many also have the misconception that employees hired under an affirmative action plan need not be qualified for the job. There is no such requirement under the executive order, nor can jobs be taken from qualified whites or men and given to unqualified blacks, women, or other minorities. Affirmative action is based on present-day underrepresentation and is not intended to make up for slavery, as many mistakenly believe. There is no set form that an affirmative action plan must take; however, the approach of the Office of Federal Contract Compliance Programs, which oversees the law, is that careful and thoughtful attention to seeking out and providing equal opportunity for underrepresented minorities and women will result in a workforce more reflective of the racial and gender makeup of the area from which the employees are drawn.

The *Civil Rights Act of 1964* is the primary, and most comprehensive, of the statutes prohibiting employment discrimination. In one of the greatest social experiments in the history of the United States, the U.S. Congress passed the Civil Rights Act in 1964, which became effective in 1965. The law was introduced by President John F. Kennedy and signed into law by President Lyndon B. Johnson. The law prohibits discrimination on the basis of race, color, gender, religion, or national origin in employment, education, public accommodations, and the receipt of federal funds. The act is divided into titles, each of which addresses a different context for discrimination (education, employment, etc.). Title VII of the law addresses discrimination in employment.

Title VII prohibits discrimination in employment by employers with 15 or more employees, unions, and employment agencies, in hiring, firing, discipline, pay, raises, training, or any other term or condition of employment. The goal of the law is to have applicants judged based on qualifications rather than preconceived notions about a group they may belong to. Exceptions are made for religious employees of religious groups, in favor of Native Americans living on or near Native American reservations, and Communists.

If an employee or a job applicant feels that he or she has been discriminated against, he or she may file a claim with the EEOC, the agency created by the act to enforce the civil rights laws and that now handles virtually all claims of workplace discrimination. Since Title VII is a remedial statute, the EEOC prefers to pursue mediation and conciliation rather than the more adversarial litigation. If employment discrimination is found, the employer can be liable to the employee for back pay that the employee should have received had he or she not been terminated in violation of the law, to the applicant for front pay that the applicant would have received he or she not been illegally rejected for the job, medical expenses, compensatory damages, and, except for governmental employers, punitive damages for willful discrimination.

The employer has defenses available under the law. The employer can show that the discrimination was necessary because the basis for the discrimination was a bona fide occupational qualification (BFOQ) reasonably necessary for the employer's particular business. This is generally used when the employer has a policy that excludes certain types of applicants from a job. For instance, there is usually an age cutoff for commercial bus drivers. Transportation companies have been able to show that their particular business is safely transporting passengers from one point to another and that they need an age cutoff because it takes about 15 years to become a really good driver and the physical attributes that a driver needs to accomplish this begin to deteriorate after age 50. Therefore, being age 35 or less is a bona fide occupational qualification that is reasonably necessary for their particular business of safely transporting passengers from one destination to another.

The employer may also use the defense of business necessity discussed above. It is not a defense to a discrimination claim for an employer to allege that he or she did not intend to discriminate. The law looks at the outcome of the employer's actions rather than the mental state behind the action. The law provides a separate cause of action for retaliation for employees filing claims under the law to enforce their rights. Below, each of Title VII's categories is addressed.

Race Discrimination

Race discrimination against blacks was actually the main impetus for passing the Civil Rights Act, though the law applies to everyone. Before passage of the law, there had been a formal and informal system of racial segregation against blacks known as “Jim Crow,” which had been in place since shortly after the Civil War ended. Racial segregation was complete and total. For instance, employment classified advertisements were divided by race and gender. The Civil Rights Act outlawed this practice.

Race discrimination has greatly diminished since the passage of the act but remains the reason for the majority of claims received by the EEOC. Many of the claims are for systemic, widespread discrimination rather than individual discrimination. That is, employers have allowed blacks to be paid less, not advance at the same rate, and generally be treated more poorly than other similarly situated, nonblack (usually white) employees. Racial harassment is also a type of race discrimination, where an employee is harassed on the basis of his or her race. Discrimination on the basis of color (rather than race) has seen fewer claims, and they are generally filed by blacks who allege that others of their race receive better treatment because their color is different from other similarly situated employees.

Gender Discrimination

This includes discrimination on the basis of pregnancy, and sexual harassment. Unless gender is a BFOQ, it cannot be used as the basis for employment decisions. Because of the country’s history of excluding women from employment, most gender discrimination claims are filed by women, but men are also protected. Denying a job because an employer thinks that it is inappropriate for a man to be a secretary or for a woman to be a construction worker violates the law. The Equal Pay Act of 1963 prohibits wage discrimination on the basis of gender for jobs that are of equal skill, effort, or responsibility performed under similar working conditions. The law permits differences in pay based on quantity or quality of production, seniority, a merit system, or any factor other than gender.

Sexual Harassment

It is illegal for an employer or other employees to make unwanted advances, requests for sex, or exchanges of workplace benefits for sex. There are two theories of sexual harassment: quid pro quo and hostile environment. Quid pro quo sexual harassment involves requesting sex in exchange for workplace benefits. For example, a manager refuses to give an employee a deserved promotion unless the employee has sex with him or her. Hostile environment sexual harassment involves engaging in sufficiently severe and/or pervasive unwanted acts that create a hostile or offensive working environment (using a reasonable employee standard) that unreasonably interferes with the employee’s ability to do his or her job—for instance, male employees in a workplace subjecting female employees to unwanted sexual jokes, teasing, groping, pornography, and so on. Claims may be filed by either males or females, and while Title VII does not explicitly include discrimination on the basis of affinity (sexual) orientation, the harasser and harassee may be of the same gender.

Pregnancy Discrimination (Pregnancy Discrimination Act of 1978)

It is illegal to discriminate in employment on the basis of pregnancy, childbirth, or pregnancy-related illness. For instance, an employer cannot refuse to hire a pregnant applicant simply because she is pregnant. In the workplace, pregnancy must be treated just as any other short-term disability. For instance, if an employer provided short-term disability leave for an employee with a heart attack or a hernia operation, a pregnant employee would also be able to take leave for the absence due to pregnancy.

Religious Discrimination

Employers cannot discriminate against employees or applicants on the basis of religious beliefs or conflicts. Religious obligations must be accommodated by the employer unless doing so creates an undue hardship on the employer, as determined by the court. For instance, if an employee cannot work on Saturdays because of his or her religious beliefs, the employer can attempt to find another employee to exchange days so that there is no conflict. If an accommodation cannot be found or would cause the employer undue hardship, the employer has met the legal requirements of the statute. An employer may not refuse to accommodate an employee’s sincerely held beliefs that take the place of religion in the employee’s life simply because the employer may be unfamiliar with the belief.

National Origin Discrimination

This category includes discrimination against employees from other countries, those whose ancestry is from another country, or those with accents. An employee's ethnicity may not serve as the basis for employment discrimination.

Other Kinds of Discrimination

The Age Discrimination in Employment Act of 1967 prohibits employers from discriminating against employees or applicants on the basis of age if the employee or applicant is 40 years of age or older. If the discrimination is intentional or willful, the employer must pay treble damages. Employees under the age of 40 are not protected by federal law. Except for certain groups such as educators or top-level management of businesses, there is no mandatory retirement age. Employers cannot terminate older employees as part of a plan to make their workplace look younger to appeal to a younger clientele; get rid of older, more highly paid employees so they can hire younger employees at lower salaries; or otherwise allow age to be the determining factor for workplace decisions.

The Vietnam-Era Veterans Readjustment Assistance Act of 1974 protects Vietnam-era veterans, especially veterans with disabilities, from discrimination. Due to the hostile way in which Vietnam veterans were treated on coming home from the largely unpopular war, Congress passed this law to give the veterans some measure of protection from employment discrimination. It applies to federal government contractors with contracts of $25,000 or more. They must agree not to discriminate against Vietnam veterans, take affirmative moves to hire them, and make accommodations for any such employees with disabilities.

The American With Disabilities Act of 1990 prohibits discrimination in employment against an employee or an applicant with a disability if that employee or applicant is otherwise qualified for the job, does not present a risk to person or property, and can be accommodated without undue hardship to the employer. A person with disabilities has a mental or physical impairment that substantially limits one or more major life functions (defined as breathing, walking, etc.), has a record of having a disability, or is perceived as having such a disability.

Certain conditions have been deemed by the courts as not constituting a disability because they do not affect a major life function. These include visual problems that can be corrected by wearing eyeglasses, high blood pressure corrected by medication, fear of heights, and so on. Active drug users do not have to be accommodated.

If accommodation of an employee with disabilities would present an undue hardship to the employer, then the employer does not have to hire that employee. Undue hardship is not defined in the law and is specific to each case and each employer. The courts, however, have made the threshold fairly low, and the accommodation need not be shown to cause the employer to suffer a great financial loss in order to meet the requirement of undue hardship. The court is the final arbiter of undue hardship.

The Family and Medical Leave Act of 1993 permits employees to take up to 12 weeks of unpaid leave from work because they are ill or to care for a newborn or newly adopted child or a sick parent. Male employees have brought suit under it when employers have not granted them leave to take time off for situations traditionally handled by females—for example, a new father who wishes to stay at home with the new baby.

—Dawn D. Bennett-Alexander

See also Affirmative Action; Age Discrimination; Comparable Worth; Equal Opportunity; Gender Inequality and Discrimination; National Origin Discrimination; Racial Discrimination

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EMPOWERMENT

Empowerment is a term that is applied to individuals and groups in society and in organizations. Literally, it means the taking of power by individuals or groups; alternatively, it means power being granted to individuals or groups by an authority. Thus, empowerment is the organizational or social practice by someone in a position of power giving some of that power or authority to others. Typically, those receiving power would be a group in a subordinate or disadvantaged position. As an example, a manager might empower employees to take charge of their own quality control process in a production line rather than having a quality control check at the end of the line.

Sometimes, empowerment is viewed as a psychological state of mind for individuals or groups, which allows them to feel a degree of control over their own goals and accomplishments. Empowerment enables people to feel motivated to accomplish goals while feeling a sense of self-determination, self-efficacy, and capability to bring about impacts or changes. In business and other organizational settings, empowerment most frequently means giving employees decision-making authority over various aspects of their working situation. In the organizational context, empowerment simply means that power is shared by leaders and managers with employees, which frequently means employees taking responsibility for setting up and managing their own work rather than constantly working under supervision.

Empowerment is also used in society. For example, *empowerment* has been applied to educators, who empower students to take responsibility for their own learning; to women, empowering or liberating themselves from oppression by various authorities or from men; and to disadvantaged or minority groups in society, which empower themselves in relationship to majority groups. The term has also been applied to organizational teams in the context of their taking responsibility for achieving their own performance goals. Empowerment tends to be applied in situations where a group in some way is, or feels, oppressed by another group that is in authority and has more control over the circumstances faced by the less dominant—less powerful—group. The notion of empowerment in this sense suggests that by becoming more empowered, the oppressed group will take charge of its own fate because it has more self-confidence or self-efficacy and will be motivated to institute changes in its circumstances that will lessen inequities in the system; that is, the group will assume, or be granted, more power. In organizational contexts where various sorts of empowerment programs are implemented, however, it is frequently assumed that it is the managers who "empower" their subordinates by giving them more authority, decision-making capacity, or control typically over their work rather than the employees empowering themselves by overtly seeking those changes.

The Process of Empowerment

The process of empowering an individual or group involves several steps. The person in authority must make a decision to give up some current level of power and communicate that decision to those who are currently not empowered. The individuals who are to be empowered need to be given training and education about their new tasks, responsibilities, or authorities. Then, any necessary organizational and reporting shifts must take place, including appropriate changes of the reward structure. Over time, the situation should be monitored and evaluated so that feedback about how well the process is working can be given to all the involved parties.

In societal contexts, as in organizational settings, empowerment suggests that groups that have been oppressed by some sort of authority, whether management or other groups in society, will be freed or will free themselves, through the empowerment process, from that oppression. Viewed through individual, organizational, and societal lenses, empowerment can be said to have two important facets. One facet highlights the process aspects of empowerment—that is, the delegation of power by an authority to others, a process of empowering others to take charge of themselves and/or their work in some new way. The other facet is an end state of being empowered, which is more related to the psychological state of someone who has either been given control over key issues that are important to him or her or has assumed that control. Thus, a dominant thread in definitions of empowerment is that it is a psychological term applied to individuals, encompassing attributes of meaningfulness, competence, self-determination, and impact.

Empowerment in Organizations

Empowerment in the organizational sense refers to employee-related practices within organizations that attempt to devolve some degree of power to employees.

Numerous ways of empowering employees have been developed, including the use of suggestion boxes that permit employees to give input into how the organization should operate and related mechanisms for giving voice to employee concerns. Other organizational approaches to empowerment include total quality management, employee participation, and quality of working life programs. Such programs frequently attempt to give employees some degree of control, mainly over their own working conditions and processes, and thereby foster feelings that their work is meaningful and that they have self-determination over their work or that they have self-efficacy or the capability of performing specified tasks. Underlying the application of empowerment programs in organizations is the belief that the empowerment of people who previously had little or no power even over their own work will better motivate them to perform their jobs and thereby improve results for the organization.

Empowerment in Society

Broader uses of the term *empowerment* also exist. The term *empowerment* has been applied in educational settings to the development of self-efficacy, competency, and confidence in students and politically to disadvantaged groups, which are urged to take responsibility for themselves in society. A good deal of feminist literature has focused on the empowerment of women, suggesting that women have been historically oppressed by men and need to develop their own internal sense of power.

Empowering others is considered to be a highly ethical thing to do in most circumstances, provided it is done with the proper motivations, training, and reward structures in place. Not all responses to empowerment are positive, as some critics believe that the so-called empowerment programs do not provide much real decision-making capacity to those who are being empowered; that is, only the appearance of empowerment exists. Some empowerment programs fail when managers do not really give up their own power, in part because they cannot envision a new role for themselves. At other times, empowerment programs are added to existing systems in organizations without really changing the important systems that support the empowerment process, such as training managers and employees about their respective new roles or changing the reward system to reflect the empowerment process.

—Sandra Waddock

See also Freedom and Liberty; Power, Business; Total Quality Management (TQM)

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Engels, Friedrich (1820–1895)

Friedrich Engels is perhaps best known for his collaboration with Karl Marx on *The Communist Manifesto.* Their collaboration also involved the publication of *The German Ideology* of 1846 and other less well-known works, such as *The Holy Family* of 1845 and *Wage Labour and Capital* of 1849. The relationship between the two men was a complex one. It appears from their correspondence that they worked independently, primarily sharing political views. Many commentators, such as Leszek Kolakowski, suggest that Engels was more adept at relating theory to practice than was Marx. Others suggest that it is fiction that Marx and Engels worked in a perfect intellectual relationship and even suggest that Engels's work was more influential than was traditionally thought in shaping Marxism.

Friedrich Engels was born on November 28, 1820, in Barmen, in the industrial region of the Rhineland, now Germany. His politically and religiously conservative father was a well-to-do manufacturer. Engels's early education was received in local schools operated by the Protestant Pietists. In 1838, before he had completed his formal education, his father sent him to work as a clerk in Bremen, where he discovered that he had a great love for learning, a great dislike for political tyranny, and a capacity to enjoy life. In this period of social and political upheaval, he read extensively in philosophy, theology, history, and literature. He was drawn to revolutionary writers and thinkers of the period, such as the literary figures who called themselves "Young Germany." He was also attracted to the radical Young Hegelians, moving in 1841 to

Berlin to volunteer in the Brigade of Artillery. His joining this Brigade had two purposes. First, he fulfilled his military obligation, and second, he was able to participate in the vibrant intellectual life of the city. During this time, Engels wrote articles under the name of Frederick Oswald.

Engels met Karl Marx, an editor at the radical daily newspaper *Rheinische Zeitung*, in 1842 in Cologne. This first meeting, along with subsequent ones in Paris in 1844 and Brussels in 1845, began a remarkable 40-year partnership. Before meeting Marx, Engels had published *The Condition of the Working Class in England* of 1845, which described the social impact of the Industrial Revolution, making particular reference to the poor conditions of factory workers. This work was produced during the period in which Engels worked as a clerk for 21 months in his father's firm in Manchester.

In late November and early December 1847, Marx and Engels attended the Second Congress of the Communist League in London, where they were charged with writing the League's program. What they produced as the League's program was *The Manifesto of the Communist Party*. It appeared in February 1848 in London.

The Manifesto set out the principles of scientific socialism, rejecting other forms of socialism as inadequate. The term *scientific socialism* was coined by Engels to describe the sociopolitical-economic theory set forth by Karl Marx. The theory purports to be scientific because observation is required, as in the method of empirical science. Soon after the publication of *The Communist Manifesto*, the revolutions of 1848 broke out, resulting in the deportation of Marx and the subsequent escape of Engels to Switzerland. Later, Engels joined Marx in London. Breaking with the Communist League, they devoted themselves to theoretical work. In 1864, following a revival of the working class movement, the General Council of the International was formed. Engels became a member of this Council in 1870.

Engels was never merely Marx's interpreter or assistant, but he was always an independent collaborator. In their writing, they attacked capitalism, claiming that this economic system promoted injustice and undermined society. Capitalism and the system of private property exploit workers by failing to pay workers the full price of their labor, providing the worker with subsistence wages, and appropriating the surplus to the employer. Capitalism necessarily produces inequalities of wealth and power. An alienated laboring class is produced, which is inherently unjust. This injustice was based on their belief that workers were exploited since the "surplus value" produced by workers was appropriated by the owners of the means of production. Workers were therefore alienated from their product, their work, and, ultimately, themselves. In addition, the interests of the economic ruling class took precedence over the interests of the worker and even national interests. The abolition of the system of private property would allow property to serve a social function by belonging to every member of the community and serving the needs of each member rather than the interests of the few. Engels died of throat cancer on August 5, 1895.

—Marilynn P. Fleckenstein

See also Capitalism; Communism; Market Socialism; Marx, Karl; Marxism; Political Economy; Socialism

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Enron Corporation

Enron Corporation's December 2, 2001, Chapter 11 reorganization filing was the largest bankruptcy in history, until it was exceeded in 2002 by WorldCom. Enron, headquartered in Houston, Texas, had grown quickly into a superficially giant and well-regarded company. It rapidly collapsed following the sudden disclosure of massive financial misdealing, which revealed the company to be a shell rather than a real business. During 2001, Enron stock fell to about $0.30—an unprecedented collapse for a blue-chip stock.

The Enron scandal helped propel passage of the McCain-Feingold Bipartisan Campaign Reform Act of 2002 (March). While Enron was neither the biggest nor the most important source of political funds, it had been active in making political contributions and attempting to influence legislators. Part of the Enron scandal involved political connections to President George W. Bush (former governor of Texas) and Vice President Dick Cheney (formerly CEO of a Texas-headquartered company). In May 2005, a U.S. appeals court dismissed a related lawsuit against the vice president on the grounds that an administration must be free to seek confidential information (including Enron) concerning energy policy.

Enron, quickly followed by WorldCom, helped propel the Sarbanes-Oxley Act of 2002 (July), the most significant change in U.S. securities laws since the early 1930s. As shocking as the sudden bankruptcy of a blue-chip company was, the subsequent revelations were worse: The traditional U.S. corporate governance watchdogs—attorneys, auditors, and directors—had either aided and abetted the responsible executives or been grossly negligent in the supervision of those executives. The United States and several other countries were rocked by multiple revelations of corporate scandals that ultimately also included analysts; auditors; banks; brokerages; mutual, hedge, and currency trading funds; and the New York Stock Exchange.

Arrogance, Corruption, Greed, and Ruthlessness

Enron was not the first or the last or the largest of the corporate scandals in recent years. Nevertheless, Enron became, above all other companies, the emblem for management fraud, director negligence, and adviser misconduct. Enron is easily the most widely studied and best documented of the recent corporate frauds. Enron was a prolonged media event.

The high education levels and intelligence of Chairman Kenneth L. Lay (Ph.D. in economics), CEO Jeffrey K. Skilling (Harvard MBA and top 5% Baker Scholar), and CFO Andrew Fastow (Northwestern MBA) raised serious questions about business school treatment of ethics and law. In January 2005, the documentary movie *Enron: The Smartest Guys in the Room*, based on Bethany McLean and Peter Elkind's 2003 bestseller of the same name, premiered at the Sundance Film Festival in Utah. Spring 2005 releases took place in Austin and then Houston. The theme of the book and the movie is that smart guys can outsmart themselves as well as everyone else.

The most astonishing aspect of the Enron scandal was that a significant number of executives had engaged in improper actions despite the company having in place the key elements and best practices of a comprehensive ethics program. There was a detailed 64-page "Code of Ethics" with an introductory letter from Chairman Ken Lay and a "Statement of Human Rights Principles" together with a sign-off procedure on the code for each employee, an internal reporting and compliance system, visible posting of corporate values (banners in the headquarters building, signs in the parking garage, and so forth), and an employee-training video—*Vision and Values*—discussing ethics and integrity. Enron issued a 2000 annual report on corporate responsibility. The "Code of Ethics," like other Enron paraphernalia, was later auctioned on eBay. The Smithsonian Institution reportedly obtained a copy of the code for its permanent collection.

The publicized "values" of Enron were respect, integrity, communication, and excellence. The real "ethical" climate at Enron was a combination of arrogance (or hubris), corruption, greed, and ruthlessness. The gap between words and deeds at Enron was dramatic. This gap suggests that it is not particular corporate governance devices that matter most but the probity and integrity of individuals in relationship to the ethical climate within a company.

The executives were arrogant in attitude and conduct. The company strategy was one of revolutionizing trading by breaking traditional rules. The "vision" at Enron was to become the world's leading energy company—in reality, by any means necessary. There were rumors of sexual misconduct by executives. Expensive vehicles and power-oriented photogenic poses were commonplace.

The weight of evidence suggests that the lure of wealth had suborned the corporate governance watchdogs. It turned out that the directors must have been asleep at the switch or mesmerized by the rising stock price. It turned out that the external attorneys and auditors could not afford to lose such a successful client. Enron executives did not hesitate to bully the external safeguards, such as analysts, when and if necessary. A corruption machine was at work, whether intentionally or inadvertently.

In the 1987 film *Wall Street*, the character named Gordon Gekko announces that greed is good. Enron—whose logo became known as "the Crooked E"—epitomized that slogan. Greed is a morally disturbing paradox at the heart of the market economy. Bernard

Mandeville, in the *Fable of the Bees, or Private Vices, Publick Benefits* (1714), argued that individual vices and not individual virtues produce public benefits by encouraging commercial enterprise. An economic actor engages in selfish calculation of interest or advantage. This consequentialist perspective emphasizes outcomes over intentions or means. The Enron executives carried this perspective to its logical extreme. Adam Smith's telling criticism in *The Wealth of Nations* of the East India Company's personnel suggests that he would hardly be surprised.

The company culture embodied ruthlessness toward outsiders and insiders alike. Skilling emphasized a process of creative destruction within the company. The rank and yank system of employee evaluation by peer review, reportedly installed by CEO Skilling, annually dismissed the bottom 20% of the employees—and perhaps corruptly rather than objectively. It has been reported that traders were afraid to go to the bathroom because someone else might steal information from their trading screen. In such a culture, no one would report bad news. In such a culture, individual achievement was everything and teamwork was nothing. Enron culture emphasized bonuses, hardball, take no prisoners, and tacit disregard for ethics and laws.

The Rise of Enron

Ken Lay, then CEO of Houston Natural Gas, formed Enron in 1985 by merger with InterNorth. Lay had worked in federal energy positions and then in several energy companies. He was an advocate of free trade in energy markets and had experience in political influence peddling. Enron was originally involved in transmission and distribution of electricity and natural gas in the United States. It also built and operated power plants and gas pipelines, and similar industrial infrastructure facilities, globally. Allegedly, bribes and political pressure tainted contracts around the world—most notoriously a $30 billion contract with the Maharashtra State Electricity Board in India.

Jeff Skilling was a senior partner at McKinsey & Co. and in the later 1980s worked in that capacity with Enron. Skilling joined Enron in 1990 as chairman and CEO of Enron Capital & Trade Resources. In 1996, he became president and COO of Enron. The company morphed into an energy trading and communications company that grew to some 21,000 employees, and its stock price rose to about $85. Enron grew to the seventh largest publicly listed company in the United States. Strategy emphasized bold innovation in trading of power and broadband commodities and risk management derivatives—including highly exotic weather derivatives. Trading business involved mark-to-market accounting in which revenues were booked, and bonuses awarded, on the basis of effectively Enron-only estimates of the value of contracts. *Fortune* magazine named Enron "America's Most Innovative Company" for five consecutive years (1996–2000). Enron made *Fortune*'s "100 Best Companies to Work for in America" list in 2000. The company's wealth was reflected in an opulent office building in downtown Houston. Business school cases on Enron's business practices and culture were circulated for teaching purposes. Skilling served briefly as CEO of Enron from February to August 2001. Then, he abruptly resigned from Enron and Lay took over as CEO.

The Fall of Enron

Following the bankruptcy filing, there were multiple investigations, including one commissioned by the Enron board of directors and directed by William C. Powers Jr., dean of the University of Texas at Austin's law school. The U.S. Department of Justice announced (January 9, 2002) a criminal investigation of Enron, and various congressional hearings began (January 24, 2002). The hearings also revealed the role of Sherron Watkins, a certified public accountant, who had warned Lay about Fastow's offshore devices after Skilling suddenly resigned. Watkins's experience helped propel into law the whistle-blower protection elements of the Sarbanes-Oxley Act. The investigations emphasized two key matters, revealing how Enron had been built as an empty house of cards.

Enron was deeply involved in manipulating the California energy crisis. John Forney, a former energy trader, was indicted in December 2002 on 11 counts of conspiracy and wire fraud and pled guilty. Tape recordings revealed Enron traders on the phone asking California power plant managers to get a little creative in shutting down plants for repairs. Forney was a *Star Wars* fan. His "Death Star" strategy involved shuffling energy around the California power grid to generate state payments relieving congestion. Death Star deliberately created congestion. He named other devices JEDI (Joint Energy Development Investments) and Chewco (after the character of Chewbacca).

The other key revelation concerned CFO Andrew Fastow's creative use and alleged partial ownership of offshore special purpose entities (SPEs) or limited partnerships. These devices separated debt from revenues and kept mark-to-market losses off Enron's books temporarily. Fastow had been a *CFO Magazine* award for excellence winner. Fastow was indicted (November 1, 2002) on 78 counts, including fraud, money laundering, and conspiracy. He and his wife, Lea Fastow, former assistant treasurer of Enron, accepted a plea agreement (January 14, 2004) in exchange for testifying against other Enron defendants. Mr. Fastow received a 10-year prison sentence and a loss of $23.8 million; Mrs. Fastow received (for income tax evasion charges in concealing Mr. Fastow's gains) a 5-month prison sentence and 1 year of supervised release, including 5 months of house arrest. The Enron board had waived conflict of interest rules in its own Code of Conduct to permit Fastow to oversee some of these SPEs. Most important were the "Raptors" (after *Jurassic Park* creatures) or "LJM1" and "LJM2," named for Fastow's wife and two children. It was alleged that Fastow had engaged in unauthorized self-dealing and benefited directly from these supervised devices.

The Enron bankruptcy resulted in the criminal conviction for obstruction of justice and, thus, forced auditing license surrender of its auditor Arthur Andersen, which collapsed. The audit partner assigned to Enron, David Duncan, pled guilty to ordering large-scale destruction of work documents. Some 28,000 Arthur Andersen employees had to find other employment. On May 31, 2005, the U.S. Supreme Court unanimously overturned the firm's conviction on grounds that the trial judge's jury instructions were too vague and broad. Federal prosecutors decided in November 2005 not to retry the case. Duncan was allowed to withdraw his guilty plea, although other charges could be filed against him.

As of July 2005, there had been 16 guilty pleas and six convictions (one thrown out) in the Enron cases. Former Merrill Lynch bankers and Enron executives were convicted in the Nigerian barge trial. (One executive was found innocent.) Nonexistent barges (to be built) were flipped between Enron and Merrill Lynch to generate paper profits and bonuses. In July 2005, three former executives of Enron Broadband Services (EBS) were acquitted of some charges; the jury deadlocked on other charges against them and two other defendants. The charges had argued intentional overpromotion of EBS's value. The judge dismissed the remaining charges against all defendants. In November 2005, a special grand jury issued three streamlined indictments against the five codefendants. Skilling was indicted in February 2004 and Lay in July 2004, both on multiple counts. Both pled not guilty; their trials had not commenced as of November 2005. The prosecution wanted to try with Lay and Skilling the former chief accounting officer of Enron Rick Causey. He had pled not guilty to more than 30 charges of fraud. He was indicted in January 2004.

Employees and Shareowners

Enron's bankruptcy had serious effects for many individuals and organizations. The Houston Astros paid Enron $5 million to rename Enron Field as Astros Field, subsequently changed to Minute Maid Park. *Playboy* (August 2002) featured a pictorial "The Women of Enron." David Tonsall, former Enron employee, became rapper "N Run" (i.e., Enron and "never run") on a December 2003 CD *Corporate America.*

Shareowners lost virtually everything. Several employees lost their jobs and their life savings that they had invested in Enron stock. Like former Arthur Andersen employees, former Enron employees may have damaged résumés. The Enron bankruptcy reorganization was a lengthy affair under a new management and bankruptcy examiner. The state of California is attempting recovery of monies from various parties. Eventually, shareowners and employees may begin partial financial recoveries from various parties, including banks and insurance companies. As of November 2005, Citigroup had settled for $2 billion, J. P. Morgan Chase for $2.2 billion, and the Canadian Imperial Bank of Commerce for $2.4 billion. These figures represent the largest securities class-action settlement on record, and there are still a number of other prominent defendant banks remaining. The U.S. bankruptcy court finalized a settlement in May 2005 of about $3,500 on average for more than 20,000 current and former employees (about $69 million total). Civil lawsuits are still proceeding against Lay, Skilling, Enron, and others. The directors of Enron (and WorldCom) personally paid damages.

—Duane Windsor

See also Adelphia Communications; Arthur Andersen; Campaign Finance Laws; Global Crossing; Grasso, Richard; Mandeville, Bernard; Parmalat; Royal Ahold Company; Sarbanes-Oxley Act of 2002; Scandals, Corporate; Tyco International; Whistle-Blowing; WorldCom

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ENTITLEMENTS

Someone is *entitled* to something if a relevant institution has rules assigning that kind of thing to someone in the position of the person who is claimed to be entitled to that thing, given his or her position; the word *entitlement* can refer either to the thing to which he or she is entitled or to the fact of that person's being entitled to it. The notion of *entitlement*, then, is strongly rule governed. Often these are legal rules. It is disputed whether, but not obviously impossible that, one can be entitled by moral, as opposed to strictly legal, rules. In any case, clubs, businesses, and all sorts of other organizations and informal arrangements among people have rules that specify entitlements or what amount to entitlements.

The idea is perhaps best explained by comparing it especially with the idea of *desert*, and both need to be considered in relation to the more general topic of distributive justice. Plato long ago considered the question of whether justice is "giving every man his due" (and rejected it). *Due* is not far removed from *deserve*, certainly, and sometimes it is not far removed from *entitlement* either. But the idea of entitlement does have a fairly distinctive meaning, where it is not the same as either of these other ideas.

Both desert and entitlement are primarily concerned with relations among individuals. Jones may deserve something of Smith but of no one else in the world; Robinson may be entitled to something from Larson that no one else is. More interestingly, Robinson may be entitled to it even though he doesn't deserve it—and vice versa. In a classic kind of case, Robinson might be the heir in his father's will, despite being a ne'er-do-well. Jones may have deserved the prize but not be entitled to it. What's the difference?

Both entitlement and desert are usually normative or evaluative ideas, but they work in divergent ways. When someone *deserves* something, we think especially of there being some kind of valuable quality in that individual, such that the appropriate response on the part of someone or other, or perhaps everyone, is to give the person that thing. Judges at a dance competition, say, are there to see which of the competitors danced the best. Points might be awarded for gracefulness, speed, and overall artistic merit, for example, the idea being to track these virtues well enough to determine who should get the prize, or prizes. If Competitor A is superior to Competitor B in these respects, then A is more deserving than B. Characteristically, though not necessarily always, we deserve something by virtue of something we have done. (We could be claimed to be deserving on the basis of possession of some natural trait too—e.g., intelligence or beauty.)

Entitlement works very differently. The background to entitlement is, broadly speaking, institutional, and the institutions in question are framed by rules, specifying which persons in which positions are to have this or that. Go back to our dance competition, and suppose that the judges conclude that Couple X should get the prize. Now suppose that much of the audience on hand thinks otherwise. Well, the rules of the competition specify that the judges decide who gets it—not the audience. Perhaps we would side with the audience if we had seen the show, but there it is—the judges have decided, and the couple they specify is *entitled* to the prize. Or suppose there is an election, and Ms. Graf is found to have more votes than Mr. Hawley. Then she is *entitled* to the office. She may not deserve it, in the view of many, and perhaps those people are right. Still, there was the electoral result, and given that it is such, that settles the question of who occupies the office: Ms. Graf does.

Entitlement, in that sense, is a more formal notion than desert. We can, generally speaking, dispute claims of desert: This candidate, we may think, really had more merit than the other; and it may be very difficult or perhaps impossible to decide. But if the rules are clear, then who is *entitled* to some position, some item, or some distinction can be settled, whatever we may think about the comparative *deserts* of different people.

Relation to Justice

It is instructive to compare both notions with the broader idea of *justice.* It is possible to hold—and it is often held—that the just thing to do is what is "for the best." And it is often enough held that we are all fundamentally equal, so various goods should be distributed in equal shares to all. If that is so, then justice works against desert, which characteristically varies greatly from one person to another. And the egalitarian is likely to have no use at all for entitlements, which tend to award goods to persons on the basis of considerations quite foreign to either equality or desert.

However, another view of justice is that the basic determinants of who is to have what should, after all, be entitlements. That we should have what we are entitled to is a recognizable and widely held but not self-evident view of justice. For example, it is often held that the individual who happened along first and undertook use of some item, say a bit of land, is entitled to it. Some other person, it might be thought, would make better use of it and perhaps, in a sense, deserves it more; but, alas, this other person came along too late. "First come, first served" may be held to be the rule framing the institution of property. This kind of view, advocated by many American writers as well as philosophers from centuries ago, has come especially to be identified with the thought of the late Robert Nozick.

An Example: Contracts

Another rule determining entitlements is that people are entitled to what they have contracted into, or otherwise seriously agreed to. Suppose that A and B make a bargain or a deal, A proposing to give x to B in return for B's giving y to A, and B agrees. If x and y are clearly the ex ante possessions of the two, and if the agreement is made without fraud, duress, or misrepresentation, then when A has turned over x, it is plausibly held that A is now entitled to y from B. The terms of the agreement, we will suppose, are clear, and the conditions fulfilled. Then that, it may be held, settles the matter of whether A is entitled to the item. And if A is indeed entitled, then it would be very difficult to deny that A is the one who ought to get it.

These are striking differences from other possible theories. First-comers need not address the question whether they deserve to be where they are; bargainers need not consider whether the other party merits participation in the bargain. Neither need consider whether he or she ends up better or worse off than innumerable outsiders. In any case, they proceed in the secure knowledge that others will respect their right to the results, whatever they may be.

The question arises, Why should we employ entitlements as we do? Why are there entitlements, or, more guardedly, why might we think that we ought to be using that kind of notion rather than some other? To discuss this matter, we need to shift gears and look at the entire institution from a larger perspective—that of society as a whole.

Fundamental Questions

What is the "perspective of society as a whole"? It is difficult to deny the merits of the theoretical stance known as *methodological individualism*, which has it that anything normatively interesting about society stems, basically, from the properties of individuals, though of course in the realization that those individuals interact with others, with whatever that entails. And the most popular form of individualism for this purpose is the *social contract* idea: that the principles for society as a whole are those to which all individuals would be ready to commit, as being the best each can do in light of the presence and general characteristics of all the others. The big advantage of the social contract idea is that it works from the perspectives of individuals, which are by definition already normative for them—their "perspectives" being what they are interested in, along with how they see the world. But, of course, when we contemplate the idea of an agreement with the 6 billion others around us, we have a severe problem of abstraction and generalization. We also, of course, have a problem with the sort of terms that it is plausible to think of as eventuating from this exercise.

Getting the Two Concepts Together

There is, however, an argument for adopting an entitlement format, at this fundamental level, that is very strong. Entitlement has the advantage of being based on the status quo. People are what they are and where they are—how could they not be? It makes no sense to suppose that a person can be the person he or she is because he or she *deserved* to be, for prior to birth, there is no person there to do any deserving, while afterward, of course, the thing has been done. The entitlement perspective, in contrast, gives them the right to both—we don't have to do anything to earn our entitlement to life and liberty, say. They simply come with the package of being a person. A perspective of desert, on the other hand, makes things chancy. What do we deserve? Who decides this? It is easy to conjure up chilling images of Central Committees making decisions about this, decisions that will drastically affect us in unforeseeable ways. They might decide that persons of a certain race, say, do not "deserve" to live. And while they could also create legal rules or institutions in the context of which those people are not even entitled to life, defending such a decision on the basis that humans are not fundamentally entitled to exist is nearly unintelligible.

Furthermore, it is important to see that a perspective of desert can be derived from that of entitlement. If we start with entitlements to various things, and to ourselves, then we can get into relations with others in which person A, who has something to award or distribute or confer, proposes to do these things on the basis of certain kinds of performances or features that others have that are of interest to A; A then advertises, say, that some of the items in question can be got by the appropriate performances, which will then be said to constitute the desert basis for such distributions. In this way, desert can be handled as mutually beneficial arrangements between two or various parties, all of whom accept the general criteria of performance and proceed accordingly.

This account makes entitlement the prior notion, sidestepping the enormous problem that would be posed by making people's fundamental rights a matter of desert. Yet it also anchors desert in the knowable and conveyable interests of particular persons, enabling those hoping to qualify to know what sort of things they must do or be in order to do so. This enables the two notions to get along well together instead of being seriously at odds, as it can easily seem if we try to proceed the other way around, making desert the prior notion.

Why Should Society Adopt Entitlements?

Making entitlement prior to desert, however, does not mean that it is prior to any sort of general evaluation. That we will have entitlement-like notions is itself justifiable by reference to general human interests, as well as general properties of persons familiar to all.

Entitlements can be a function of specific sets of rules laid down by various institutions. The rules of an institution specify, to a greater or lesser extent, who gets what: positions with powers and responsibilities, procedures for getting persons into those positions, and so on. Is that acceptable? A plausible answer is that it is, if those party to the institution have good reason, from their own points of view, to accept it as such. And a suitable criterion for supposing this to be true is that they do in fact accept it, so long as their acceptance is uncoerced. Many institutions meet that criterion handily—dealing with supermarkets or clubs, for example. On the other hand, institutions such as an area's government do not, on the face of it. For we come under the jurisdiction of governments whether we want to or not.

The social contract perspective has the effect of making the general procedure for assessing society's fundamental institutions the same, in principle, as the procedure for assessing some particular institution's rules. The difference is that many particular institutions have identifiable memberships, and those members are so voluntarily. When they are, the rules from the point of view of insiders can be very different, even unrecognizable, as compared with how they might be viewed by outsiders. But the general social contract view makes this unsurprising. So long as the institution takes care not to visit untoward effects on outsiders, the general social contract finding as outlined above says that this is entirely acceptable.

If we return to the example of wills, this discussion should be helpful. Outsiders may think that Offspring B is much more deserving than Offspring A. But those same outsiders can see that the maker of the will should have the power to decide who will get his or her estate, even if they suppose he or she might misuse that power in relation to the desert criteria they are likely to employ.

Philosophical advocates of an entitlement approach to distributive justice argue in the same way—that the fundamental features of the human social situation are such that rights based on the historical realities of time and place are called for rather than schemes based on visions of good societies that may not look so good from the point of view of many of the people seriously affected by those schemes.

Contemporary Issues About Entitlements

Burdens of Entitlement

In contemporary times, many government programs in numerous countries have created legal entitlements to various benefits, such as medicines, pension incomes, educational facilities, and many more. When commentators speak of "entitlements" in current sources, they most often are speaking of these. In addition, businesses may do this. The pension and other entitlements promised by very large corporations to their employees in decades past now create very large demands on the budgets of those corporations as their employees live much longer, retire earlier, or both. Meeting those demands can be difficult, even ruinous; and the problem with specifying that they are *entitlements* is that this makes it extremely difficult to evade or even to revise them, they having been created, perhaps, long in the past. The same may be true, according to many critics, of many government programs as well. The relation of this type of entitlement to the more general account given in the preceding paragraphs is clear: The institution's rules assign these things to people in various positions, notably employees, and those rules have the force of requirements, imposed or imposable by legal means. Correspondingly, there is room to question whether various such programs are wise or even morally acceptable.

Corporate Entitlements

One context in which the force of entitlements has become an issue is that of compensation packages for high-ranking officers of corporations, notably CEOs. In the United States, especially, the earnings of such officers have reached remarkable heights, and often their salaries have been nearly inverse to the success of their corporate efforts as measured by profits and sales. The packages have been, in general, negotiated with the relevant members of boards of directors, and so the executives in question become entitled to these very large payments, which the corporation in consequence is obliged to pay, despite tottering sales and declining or negative profits. This has caused criticism of the idea of entitlement among social critics. But of course, it can also simply be criticism of the boards of directors, or their construction, that has enabled such ruinous pay packages to be assembled.

Affirmative Action

Programs aimed at rectifying claimed discrimination in the past have been frequent in the past several decades. Characteristically, members of selected minorities that are perceived to have suffered from discriminatory treatment in the past are specified as being entitled to a position farther up in some queue or a higher wage, and so on, than those who are considered on the basis of the normal criteria for the situation in question. The benefits specified for such persons are known as entitlements, since legislation, or in some cases corporate procedures, specify them as recipients at the hands of the appropriate administrators. Such programs have been the occasion of considerable conflict, as persons who are normally regarded as more deserving of some level of wages or other benefit are, as they see it, pushed aside in favor of others who are less qualified. This is an example where an alien social philosophy leads to the utilization of a concept that is usually criticized by theorists of the same persuasion, who would normally object to the employment of entitlement notions. This illustrates the fact that entitlement notions are not uniquely aligned with one moral or political philosophy rather than any other.

Entitlement and Normativity

Both entitlement and desert are usually taken to be normative or evaluative ideas. But the word *usually* here has to be taken seriously. The mark of a normative notion is that when someone applies the expression, we infer that the user is for or against some action, or regards the action as something that *ought* to be done by someone. However, the use of *entitlement* is variable in this respect. Someone might say, "Well, he's entitled to it, but he oughtn't to get it!" In that case, the speaker is dissenting from the structure of institutional rules that underpins the claim of entitlement in question. It is common for an opponent of a program generating entitlements to speak of them as such but in the same breath to deny that the people who get them should really be getting them. The speaker might take either of two options, however. He might agree that given that the program is actually in place, the people thus legally entitled to those benefits should get them, at least for now, say until the program is dismantled by an act of Congress or the board of directors. Alternatively, the speaker might insist that even those getting them now should not get them and perhaps that those getting them in the past really ought to return the money, or part of it, or otherwise be required to do something to compensate the taxpayers for the expense to which they have been put.

It would, however, make little sense for the actual architect, legislator, or business executive who helps actuate such a program to deny that it *should* be carried out. In that sense, entitlement is always a normative notion, and has been so treated in this entry. Deleting the normative forces of entitlements among those who agreed to or constructed the rules that lead to them would undermine any institution, whose employees, beneficiaries, and administrators would find it difficult or impossible to know where they stand. Entitlement, in short, is a powerful idea that we probably have no option but to live with.

—Jan Narveson

See also Affirmative Action; Business Law; Contracts; Economics and Ethics; Executive Compensation; Game Theory; Hobbes, Thomas; Integrative Social Contract Theory (ISCT); Justice, Distributive; Locke, John; Meritocracy; Nozick's Theory of Justice; Political Theory; Prisoner's Dilemma; Rousseau, Jean-Jacques; Social Contract Theory

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Entrepreneurship, Ethics of

Writing on the ethics of entrepreneurship has generally taken the form of defenses of free market capitalism, with particular attention given to the libertarian ideals supported by this system of wealth creation and distribution. Consequentialist critiques have pointed to the distributive inequities that attend concentration of wealth in the hands of a few entrepreneurs. Stakeholder theory has been invoked as one means by which to legitimize the claims of those constituent groups that are negatively affected by entrepreneurial activity. Theorists have usefully outlined moral imagination as one mechanism that is both consistent with the entrepreneurial drive toward innovation and inclusive of a variety of stakeholder interests.

With respect to the "rightness" and "wrongness" of entrepreneurial praxis, the potential ethical pitfalls facing entrepreneurs have been usefully outlined. It has been argued that entrepreneurs have a "bent" toward the profit imperative; this bent predisposes entrepreneurs to privilege their own interests above the interests of other legitimate organizational constituents.

Entrepreneurship

Entrepreneurship research has been categorized into at least three literature streams: economic, characteristics of the entrepreneur, and new venture performance. The first of these explores the role of the entrepreneur as the creator of new enterprise, the second attempts to describe entrepreneurs according to psychological attributes, and the last focuses on how the performance of the venture itself is influenced by the entrepreneur.

Definitions matter. Venkataraman identifies an entrepreneur as one who realizes or conjectures, whether through insight or luck, that some resources are underutilized in their current occupation and recombines them into a potentially more useful and fruitful combination. This focus on economic values is a consistent theme throughout much of the literature on entrepreneurship.

Numerous writers suggest that entrepreneurship is the exercise of individual freedom with a view to creating value, whether economic or social (or, less commonly, both). This focus on personal liberty offers one perspective as to what an ethical justification for entrepreneurial activity might begin to look like. Milton Friedman is chief among the writers who argue that an individual's right to personal freedom provides the strongest possible moral defense for free market activity. Such personal freedoms extend to both the consumer (as to consumer choice) and the producer (as to autonomy and independence). No activity better epitomizes the free market than entrepreneurship.

Entrepreneurship has also been defined as the process of converting a private idea into a social idea—or as intelligence in the service of greed. Kirzner bridges the gap between these two perspectives by conceiving of entrepreneurship as the seeing of a profit opportunity—often misinterpreted as merely an opportunity for personal gain—and the taking of necessary actions to realize that opportunity.

Drucker consistently argues that the defining characteristic of entrepreneurial activity is innovation, seeing innovation as the means by which entrepreneurs exploit change as an opportunity for a different business or a different service. One important implication of this perspective is that entrepreneurship can be both learned and practiced. Given this formulation, entrepreneurs search in a deliberate manner for sources of innovation, paying particular attention to societal changes that signal opportunities for successful innovation. Venkataraman similarly identifies organizational creativity as the raw material of both innovation and entrepreneurship, seeing the latter as the essential ingredient for corporate survival in a world of increasing competition and rapid, discontinuous change.

Perhaps what is common in virtually all the extant literature on entrepreneurship is the paucity of reference to the ethical dimensions of entrepreneurial activity. For the purposes of the current overview, it is not important which definition of entrepreneurship one prefers; of greater importance are the ethical dimensions of entrepreneurial activity and the variety of approaches taken to either bolster or criticize such activity.

Entrepreneurship: The Ethical Landscape

A good place to begin an exploration of the link(s) between entrepreneurship and ethics is the literature review. Hannafey offers one of the few such reviews available. This review notes that most writing in the area adopts either the perspective of society or that of the individual entrepreneur, appropriately labeling the first of these "entrepreneurship and society" and the second "ethics and the entrepreneur." The former deals with broad questions related to the complex moral situations encountered by entrepreneurs and their organizations, typically examining the effects of entrepreneurship on social life by exploring the moral expectations society places on entrepreneurs. The latter focuses more directly on the moral situations encountered by entrepreneurs and the organizations they have founded. Using this distinction, the findings of research on the topic of entrepreneurship and ethics are categorized and reviewed.

Researchers studying entrepreneurs and their ethical drivers and business have found that the motivating factors for entrepreneurs are not limited to profit but extend to a drive for independence, freedom, personal satisfaction, and personal fulfillment. Consistent with this view, it has been found that entrepreneurs' traits include self-confidence, a great need for achievement, and a propensity to take risks—and a commensurate strong internal locus of control.

The entrepreneurial process brings special challenges to the handling of ethical problems. The good news is that based on empirical work, some have concluded that independent-thinking entrepreneurs may exhibit slightly higher levels of moral reasoning skill than corporate middle-level managers or the general public. Conversely, it has been found that the ethical culture in start-ups is usually undeveloped. Studies have shown that the entrepreneur may feel more pressure to act unethically. Promotion and innovation activities figure prominently in the literature. A major business task for entrepreneurs is to promote their new venture to different publics—especially to key resource controllers.

Some have focused attention on the requirement many entrepreneurs face to manage the complex network of personal relationships essential to the success of new ventures. Family, friends, employees, previous business associates, investors, and others have been seen to form an important social network within which entrepreneurs carry out their work. It has been discovered that entrepreneurs encounter various relationship dilemmas, which may lead to complex ethical problems—a particular difficulty as roles and relationships change from their preventure to their postventure status. As one example, an entrepreneur's relationship with a family member or personal friend will be transformed if such persons become investors in the new venture. Entrepreneurs who relate to others in strictly transactional or instrumental ways—regardless of the consequences to creditors, investors, employees, and others—will likely face serious conflicts with the basic principles of ethics that persons should never be treated as a means to an end but must be treated as ends in themselves. Furthermore, changes in an entrepreneur's relationships may well lead to potential or actual conflicts of interest.

The literature identifies the most noted problems facing entrepreneurs as those related to customers and competitors, with the second most noted being the way a company treats employees, including decisions regarding layoffs and workplace discrimination as well as fairness in promotions. By way of summary, the entrepreneurship literature suggests that while individual entrepreneurs may possess a more developed instinctual sense of the moral climate inside their organizations, the harsh demands of entrepreneurial environments may seriously complicate standard ethical perceptions and practices.

Entrepreneurship and the Good Society

Sarasvathy suggests that the task of entrepreneurship is to move us from the world we have to live in to the world we want to live in. As entrepreneurs craft a vision of the society we want to live in, it is argued that this should be a deliberative process rather than one that unfolds "willy-nilly." The entrepreneurial mind-set, and associated entrepreneurial activity, whether for good or bad, impresses its stamp on the social organism.

Venkataraman notes that both Schumpeter and Adam Smith have drawn a profound connection between the personal profit motive and social wealth. Entrepreneurship is particularly productive from a social welfare perspective when, even in the process of pursuing selfish ends, entrepreneurs enhance social wealth by creating new markets, new industries, new technology, new institutional forms, new jobs, higher standards of living, and net increases in real productivity. By implication, within entrepreneurial research, a measure of performance is needed that is simultaneously able to capture the economic performance at the individual level as well as social performance.

Several writers—perhaps the most notable among them is Brenkert—have outlined the positive social outcomes associated with entrepreneurial activity. These typically include the creation of millions of new jobs and a plethora of new products, significant improvements in how people live, and greater efficiency in meeting people's needs and wants. In addition, the value of self-determination plays a significant role in discussions of entrepreneurship. Keeble and Turner identify eight areas in which ethical behavior, in the form of good corporate citizenship, can reap financial benefits for entrepreneurs: reputation management, risk management, recruitment and retention of quality staff, investor relations (in particular the ability to attract capital), organizational learning and innovation, competitiveness, operational efficiency, and the license to operate.

Working from the premise that a free society is a good society, the connections between values and entrepreneurial activity are clear. The free market position holds that the entity that creates, discovers, evaluates, and exploits an entrepreneurial opportunity should profit from it. More specifically, it has been found that the Protestant work ethic has been positively related to the rate of entrepreneurship in the United States over time. And more than a few writers, in critically examining the Protestant ethic and its relationship to entrepreneurship, conclude that enterprise by its very nature is ethical.

Another connection between social principles and entrepreneurship emerges, premised on the view that the good society is an efficient society. The market process can be characterized as one in which entrepreneurs discover various maladjustments in the market caused by imperfect information. Consistent with the writings of John Locke, Kirzner concludes that the profit or income associated with entrepreneurial activity exploiting such information asymmetry is justified on the basis of a "finders-keepers principle." In a particularly interesting permutation of this perspective, not just information inequities but also value inequities or anomalies represent entrepreneurial opportunities for individuals. By definition, whenever there is an asymmetry in beliefs about the value of a resource, there exists inefficiency—introducing a major incentive for alert individuals seeking to profit from such inefficiency.

A cautionary note is sounded by those who, rather than equating equality of opportunity with the good society, instead focus on the fairness of the outcomes of entrepreneurial activity. Derry in particular suggests that the environmental and social impacts that have followed the adoption of entrepreneurial values be carefully considered. Her suggestion is that the status conferred by entrepreneurial success contributes to severely entrenched poverty, increased consumption of disposable products leading to increased solid waste, and high rates of personal bankruptcy. The solution? Balancing economizing drives with ecologizing drives. Frederick similarly argues for such a harmonizing of these two value systems in ways that sustain human purposes within the constraints and opportunities of the still evolving system of nature and culture.

From an ethical perspective, it is particularly worth considering the claim that growing disparities of income and wealth will be matched by growing disparities of freedom. If this is the case, the libertarian justification for entrepreneurial activity is undermined by the distributive consequences of this very same activity.

Entrepreneurship and Stakeholder Theory

Stakeholder theory seeks to identify the variety of legitimate claims potentially disparate organizational claimants might have against the business enterprise. Stakeholder theory is alternatively viewed as a challenge to, or a derivative of, more traditional shareholder capitalism. The values underlying these two systems of thought are often contrasted, though some reconciliation of these points of view is sometimes offered—as when attempts are made at bridging the gap between altruism, which is the renunciation of personal well-being for the benefit of others, and entrepreneurship, which is the embodiment of individualism in the realm of economic activity.

Numerous writers on ethics have invoked stakeholder theory as a means of assessing entrepreneurship. Beyond the obvious references regarding the ethical duty of entrepreneurs to represent the interests of all stakeholders, most note that there is an element of trust in every transaction, further suggesting that trust is an efficient surrogate for more formal enforcement mechanisms, such as police and the courts. Links with transaction cost economics are invoked as it is argued that social contracts can be more efficiently discharged under conditions in which trust serves as a substitute for the more expensive mechanism of monitoring.

Entrepreneurship and Ethics: The Micro View

Here, the broader subject of seeking a social justification for entrepreneurship is supplanted by consideration of the ethics of entrepreneurial behavior itself. One primary view is that economic innovation is a moral response to others that arises out of the ethical obligation one person has for another. Crawford suggests that the notion of "being for others" be contrasted with "being for self"—the latter being the traditional perspective of entrepreneurs as utility-maximizing self-interest-seeking economic actors.

Brenkert outlines the specific dimensions of the ethics of entrepreneurship, offering the following questions to illuminate those areas of entrepreneurial activity that are most likely to present ethical challenges for entrepreneurs:

- Should entrepreneurs break various common social rules and practices?
- What are the moral limits of bluff and bravado in convincing others to join an entrepreneurial enterprise?

- What moral responsibilities does an entrepreneur have to others who have joined his or her entrepreneurial enterprise?
- What moral actions can corporations take to promote entrepreneurs within their ranks?
- What use may employees of a corporation make of corporate resources to explore their own entrepreneurial ideas?
- What justifies the profit of the entrepreneur and the greater disparity of income said to characterize an entrepreneurial society?
- What justification can be given for various measures—for instance, regarding bankruptcy laws, tax programs, and employment policies—that are said to foster entrepreneurship?

Moral imagination has been suggested as a bridge between ethics and entrepreneurship by Dunham and Werhane. Moral imagination refers to the ability to perceive that a web of competing economic relationships is, at the same time, a web of moral relationships. Philosophers have in some instances turned to moral imagination as a more relevant and workable approach to ethical decision making than traditional rule-driven ethical approaches. The premise here is that managers can foster higher levels of ethical performance—as well as greater innovation—by encouraging both the development and the exercise of moral imagination. Moral imagination enables entrepreneurs to distance themselves from the mental models that limit their perspective in specific situations—a concept not dissimilar to Schumpeter's notion of "creative destruction."

Moral imagination has much in common with the entrepreneur's more general habit of innovation. Creative problem-solving models are recommended as mechanisms for enhancing moral imagination. Such models amplify the cognitive abilities that are second nature to entrepreneurs, such as thinking metaphorically, maintaining flexibility and skill in making decisions, securing independence of judgment, coping well with novelty, and escaping perceptual sets and entrenchment in particular ways of thinking.

It is useful to join Moore in thinking of ethics as "constrained entrepreneurship." Constraints include the cognitive limits of entrepreneurs at the individual level, and at the macro level constraints result from the broader operational environment of entrepreneurship bounded by social norms and expectations. There are a number of ways in which entrepreneurs can differentiate themselves to economic advantage, including producing or marketing products and services that have an ethical augmentation and using inputs that are derived from sustainable sources. In an innovative twist, the rationale for the existence of entrepreneurial firms and corporations can be argued on the basis of economization of transaction costs—in this instance, *social* transaction costs. The idea of social transaction costs is intended to convey the notion that there are costs imposed by wider societal expectations and that these costs relate to the operation of an organization within these constraints.

Future Directions

The positive entrepreneurial opportunities that attend shifts in social consciousness have not been prominent in the discussion. As consumers are increasingly concerned with the human, social, and environmental impacts of their purchasing decisions, the possibilities for progressive entrepreneurial responses are virtually limitless. Calkins correctly notes that future entrepreneurs will likely be more socially concerned than those of the past—not necessarily as a result of their own value orientations but as a response to an evolution of thought regarding the social responsibility of business activity in general.

—Craig P. Dunn and Lance Schaeffer

See also Cowboy Capitalism; Economics and Ethics; Egoism; Friedman, Milton; Individualism; Justice, Distributive; Libertarianism; Marketing, Ethics of; Moral Imagination; Social Entrepreneurship; Stakeholder Theory; Transaction Costs

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Environmental Assessment

Environmental assessment integrates consideration of the environment within decision making that historically valued only financial and technical feasibility and property rights. Because the world's supply of natural resources is diminishing while the human population and its needs for those natural resources is increasing, most developed countries have established laws requiring some examination of a desired action's impact on the environment. Attention to environmental consequences *before* a project is implemented allows the public, and governmental agencies charged with the responsibility of ensuring environmental protection, a voice in decision making about the use of finite natural capital. As such, environmental assessment becomes an important tool in achieving the goal of sustainable development.

Environmental assessment does not necessarily stop the depletion of natural resources, but it is an extremely important practice. Property rights and the privileges of ownership—even national boundaries—are no longer the sole determinants of whether or not a project is undertaken. Rather, with environmental assessment, the value of the natural world is acknowledged.

U.S. National Environmental Policy Act (NEPA)

Most developed countries and governing agencies—such as the United Nations, the European Union, and the World Bank—have modeled their environmental policies after the United States' National Environmental Policy Act (NEPA), enacted in 1969. NEPA requires that any action by a federal agency must be examined for its impact on the environment; in practice, many state and local government agencies also perform similar examinations. Originally, NEPA was administered by the Council on Environmental Quality, which reports directly to the president of the United States; over time, the Environmental Protection Agency (EPA) became the primary reviewer for environmental impact statements (EISs) prepared by other federal agencies. The EPA also maintains a national filing system for all EISs, now available on its Web site. NEPA law seeks to encourage "productive and enjoyable harmony" between humans and their environment. Indeed, NEPA is often referred to as the environment's Magna Carta, ensuring a more balanced relationship by integrating environmental considerations with economic and individual interests.

Under NEPA, if a proposed action is assessed as potentially having a significant impact on the environment, the proposed action must be considered with a range of alternatives, including a "no-action" alternative. In the United States, two different public documents are created: an "environmental assessment" (EA) and, if needed, an EIS. The EA is written to determine if there is a significant impact. At least two "reasonable alternatives" (including one alternative of no action) must be identified.

If there *is* such a significant impact, a more involved analysis with several alternatives to the proposed project is required; then, a second report—an EIS—is written. So NEPA provides an indirect protection of the environment by increasing publicly available information on the environmental consequences of potential actions. From information comes awareness and potential civic engagement on behalf of the natural world.

The environmental assessment considers the short-term and long-term, direct and indirect effects of the project on humans, water, air, the climate, the soil, minerals, the flora and fauna, and the visual landscape. An important aspect of NEPA's required environmental assessment is the involvement of the American public, in addition to expected consultation with experts and other agencies. This part of environmental assessment is called "scoping": the full disclosure to the public of a proposed action, along with a solicitation of many diverse comments and recommendations from that public. Certainly that public includes business interests, so the scoping process provides an important forum for the discussion of all personal and commercial interests. All comments within the scoping phase of the assessment must be written down and addressed in the final environmental report.

In the United States, EA documents have become the principal tool used for investigating impacts on the environment. In 2001, approximately 50,000 EAs were created, with only 500 EIS reports. The process of creating these provides important opportunities for members of the public and scientists and planners to provide input to the decision-making process. This input must be made early in the process, before the desired action can be taken. Such a practice ensures transparency in decisions affecting the public.

EA requires both a clear methodology and a final report that has standard components established by NEPA. The environmental factors typically considered in EA include air, water, fish, soils, noise, minerals and energy resources, vegetation, wildlife, and cultural resources (archaeological, historical, and architectural). The consequences of alternative solutions must be examined for their impact on each of these environmental factors. This examination of such a wide variety of factors requires an interdisciplinary approach, with teams of specialists (e.g., biologists, geologists, engineers, and archaeologists) performing study, analysis, and documentation.

The process of examination and assessment may seem tedious to business developers and property owners (a simple EA typically will take at least 3 months to develop, while most take about 12 months; EIS documents can take 2 or 3 years). However, the end result is generally more beneficial to the public and the environment. Many times, the impact on the environment can be "mitigated" so that, with some caution and care, many projects are eventually approved but with a minimal, or reduced, impact on the environment. Business interests often challenge environmental assessments for exaggerating environmental risk and requiring too many concessions to the environment; environmental advocacy groups challenge these business interests because the impact on the environment seems too high.

Strategic Environmental Assessment (SEA) Directive

The most current and far-reaching governmental effort comes from the European Commonwealth and its Strategic Environmental Assessment Directive (SEA Directive 2001/42/EC). The directive was adopted on June 5, 2001. While NEPA seeks "productive harmony" between humans and the natural world, the SEA now seeks *protection* of that natural world. Furthermore, if a development (such as a nuclear plant, a toxic landfill, or an oil refinery) is found to have significant environmental effects across national boundaries, the affected member state and its public are informed and included in the discussion.

This latest form of environmental assessment not only contributes to more transparent planning and decision making but also fosters processes that assist sustainable development. While NEPA is a public policy requiring *disclosure*—that is, identifying the environmental impacts of the proposed action and requiring evaluation of several alternatives—the SEA Directive actively promotes *protection* of natural resources. As with other European Commonwealth directives, individual member states must create their own national legislation and government agencies to implement the SEA Directive.

United Nations' Millennium Ecosystem Assessment

The Millennium Ecosystem Assessment is a research program authorized by the United Nations in 2001 to study ecosystem changes over several decades and to assess the impact of those changes on future sustainability. Conducted by 1,300 experts from 95 countries over a 4-year period, the project conducted a global inventory of the state of our ecosystems, quantified the effect that human activities are having on them, and offered suggestions in its first published report in 2005. It warned that the world is degrading its natural resources quickly, with a serious, negative impact for future generations. Approximately 60% of the ecosystem services that support life on earth—such as freshwater, capture fisheries; air and water regulation; and the regulation of regional climate, natural hazards, and pests—are being used unsustainably. The assessment demanded that changes be instituted firmly and quickly, since humanity still has the power and ability to prevent irreversible damages to the planet.

—LeeAnne G. Kryder

See also Biocentrism; Economics and Ethics; Environmental Ethics; Environmental Protection Legislation and Regulation; Natural Capital; Natural Resources; Public Domain; Stewardship; Sustainability

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Environmental Colonialism

Environmental colonialism refers to the diverse ways in which colonial practices have affected the natural environments of indigenous peoples. Colonialism concerns the exploitation of native peoples through European expansion over the past 400 years. Although many peoples engaged in expansionist practices prior to this time, the magnitude of European expansion was unprecedented. Alfred Crosby has argued that European colonists were so successful partly because of the diverse ways in which they affected the native ecosystems. Colonizers introduced the pressures of foreign markets and political powers along with exotic invasive species and diseases. This two-pronged attack undermined the ability of indigenous peoples to ward off colonial invaders. The resulting damage to the native ecosystems made recovery more difficult. The colonial powers created a global infrastructure that encouraged the extraction of natural resources from poor peripheral countries by rich core countries while at the same time undermining sustainable native cultures. It is important to note that the damage caused by colonialism was not necessarily actively intended or executed with organized forethought. Indeed, R. Nixon has noted that some Western environmentalists who hoped to remediate the environmental damages caused by colonialism unwittingly further harmed native peoples and the long-term health of local ecosystems by reintroducing traditional colonial power networks in their habitat preservation efforts.

Environmental colonialism may also be referred to as ecocolonialism or ecological imperialism, although the term *imperialism* refers more explicitly to the practice, theory, and attitudes of colonizers, whereas colonialism refers to its effects. Environmental colonialism is one lens that may be applied to world-systems theory analyses of colonization. Under this lens, rather than focusing primarily on the impact of foreign military powers or economic changes, the analyst pays close attention to how the colonizing power has affected the natural environment; environmental impact is taken as a central rather than a peripheral concern.

Crosby notes that successful European colonies, or what he calls "the Neo-Europes," are located in temperate zones resembling the microclimates of Europe. This enabled colonists to raise European crops and livestock to the detriment of the diversity of native habitats. Today, these Neo-Europes are the largest exporters of grains and animal products that were utterly foreign to the colonized landscape only 500 years ago. The ecological impact of replacing indigenous species with European varieties cannot be underestimated. The famines of sub-Saharan Africa stem in part from agricultural practices introduced to the area by colonists. European agriculture requires repeated cultivation of cash crops for export to urban centers, in contrast to indigenous agricultural methods, whose emphasis on crop rotations had been traditionally successful in preventing desertification of the fragile African landscape.

Environmental colonialism continues in various guises. Companies make minor alterations to crop varieties developed by third-world farmers over centuries, and unlike the native farmers, companies have the necessary funds to patent these strains as their intellectual property. This is a contemporary manifestation of environmental colonialism. On the other hand, forced introduction of nonnative, genetically engineered organisms into third-world countries is yet another way in which colonial powers fundamentally alter the ecosystems of the colonized. This makes it even more difficult for native peoples to rediscover or to continue traditional sustainable patterns of living.

—Mary Lyn Stoll

See also Colonialism; Cultural Imperialism; Developing World; Environmentalism; Green Revolution

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Environmental Ethics

Environmental ethics is the study of the moral relations between human beings and their natural environment. Environmental ethics assumes that moral norms can and do govern human behavior toward the natural world. A theory of environmental ethics therefore seeks to provide a systematic account of such norms by explaining to whom, or to what, humans have responsibilities and how these responsibilities are justified.

Some approaches to environmental ethics argue that human responsibilities regarding the natural environment are only indirect. Anthropocentric (human centered) environmental ethics holds that only human beings have moral value. Thus, although we might have responsibilities *regarding* the natural world, we do not have direct responsibilities *to* the natural world. Anthropocentric environmental ethics typically involves the application of standard ethical principles to environmental problems. Many environmental controversies, such as air and water pollution, toxic waste disposal, and the abuse of pesticides, arise from an anthropocentric perspective, and many approaches to environmental ethics fit this standard-applied ethics model.

Much of the early work done by environmentalists and environmental ethicists followed this anthropocentric approach. Rachel Carson's *Silent Spring*, for example, warned of the potential long-term harms to humans from pesticide use. The philosopher William Blackstone argued that environmental threats created a need to recognize a new right, the right to a livable environment. While this right emerged out of the recognition of new environmental issues, it was firmly grounded in the traditional rights of life, liberty, and freedom from harm. John Passmore argued that generally accepted ethical principles, and generally recognized ethical faults, provide sufficient ethical grounding to conclude that we have a duty to refrain from pollution and that we have been ethically remiss in not doing so. Passmore also appealed to ethical and aesthetic values in his critique of materialist and consumerist culture.

A wide range of such environmental concerns are relevant for business and thus play a role in business ethics. The responsibilities of business organizations for air and water pollution and waste disposal are the most obvious issues to fit within this standard model. The ordinary ethical and legal categories of duty, harm, negligence, liability, and compensatory justice are easily brought to bear on these environmental concerns.

Ethical Extensionism

While much of the work in environmental ethics continues to fit this standard-applied ethics model, other issues challenge ethicists to extend mainstream ethical principles and values in new directions. In particular, long-term environmental problems such as nuclear waste disposal, population growth, and resource depletion led many environmental ethicists to a series of questions concerning our responsibilities to future generations. Responsibility to future generations remains within the anthropocentric approach in that human beings remain the only object of moral consideration. Nevertheless, this topic extends our responsibilities to include responsibilities to humans who do not yet exist.

Beginning in the late 1960s, population growth has become a major focus of environmental concern. Paul Erhlich argued that exploding population growth was responsible for widespread environmental destruction. Others, for example, Barry Commoner, argued that the consumption-driven lifestyle of industrial societies rather than population size per se was more responsible. In many ways, these debates represented a continuation of the applied ethics model. Debates concerning population involved common issues of individual freedom and social responsibility. Likewise, consumption debates often focused on economic rights and responsibilities to distant peoples. Both areas also focused on issues of social and economic justice to the poor and disenfranchised people living in the developing world. Standard ethical concepts and principles were applied to emerging environmental concerns. But these debates also began to focus philosophical attention on responsibilities to people living in the distant future. This shift from geographically distant people to temporally distant people raises philosophical questions seldom asked previously by philosophers. Ethical consideration began to be extended to something other than presently living human beings.

In considering responsibilities to future generations, ethicists often distinguish between two general issues: what responsibilities we have regarding future population size and what, if anything, we owe to those future generations that we assume will exist. The first set of issues, what we might call "population policy," is concerned with questions of population size, population growth, and population control. The second set of issues, often called "duties to posterity," focuses on the type of world that future people will inherit from us.

Consideration of both population policy and duties to posterity extended environmental ethics in ways that challenge standard ethical theories. For example, is there some ethically preferable population goal that utilitarianism would promote? Is the greater overall good better served by a small future population with a relatively high standard of living or a large future population with a relatively lower standard of living? If the former, does utilitarianism favor population polices that restrict reproduction among the world's poorest and encourage population growth among the world's elite? If the latter, do people living in the developed world have a utilitarian responsibility to reproduce at the highest possible rate?

Similar challenges arise for deontological approaches. Do humans have a right to procreate? Do they have a duty to do so? Do the desires of future people, desires about which we can only speculate, have a role to play in deciding what duties we owe them? Given that the different population policies adopted today would each result in a different future population (the problem of "disappearing beneficiaries"), does it even make sense to talk about responsibilities to future people? Is it meaningful to attribute rights to people who do not exist? Do justice and fairness demand that nonexisting future people have a claim to natural resources that is equal to the claims of presently living people?

Ethical theories that emphasize care and personal and interpersonal relationships also face similar challenges. Does it make sense to talk about caring for people who do not exist, and may not exist if we don't care enough to bring them into existence? Do we have greater ethical responsibilities to actual people than to possible people? Is there a sense in which there can be interpersonal relationships between temporally distant people?

While business institutions were seldom involved in population issues directly, economic and business institutions are greatly involved with potential duties to posterity. In the most general terms, the allocation and distribution of present resources will have significant consequences for people living in the future. The very question of economic development and sustainable development is the question of how economies can meet the needs of people living in the future. Normative environmental issues such as global climate change, resource depletion, waste disposal, agribusiness and agricultural ethics, and future energy supplies all involve the well-being of future generations.

It is fair to say that the topic of future generations stretches the boundaries of traditional ethics. While still within an anthropocentric framework, philosophers were forced nonetheless to address the question of moral standing explicitly. Developing a philosophically adequate account of energy or population policy, for example, required that philosophers consider the moral status of something other than presently living human beings. We can identify this practice of extending moral standing to include future humans or to develop new human rights as *anthropocentric extensionism.* Ethical concepts and categories are extended beyond traditional boundaries, but only human beings continue to possess moral standing. Our duties, such as the duty not to pollute, remain duties *regarding* the environment, but they are not duties *to* the environment. Our duties are to human beings, albeit humans who do not exist. But it is a short step from extending ethical consideration to human beings who do not, and may never, exist to the philosophical question of the very grounds for moral standing.

Moral Standing

Who and what counts morally? On what grounds do we recognize (or attribute) moral standing? Phrased in this way, we can recognize that many contemporary moral problems and public policy debates are located at the boundaries of moral standing. The abortion debate often focuses on the moral status of the fetus: Is a fetus a moral person? Does it have rights? Many debates in medical ethics concern euthanasia and the treatment of seriously impaired patients. These issues force us to consider the moral status of patients in irreversible comas, those who are brain-dead, frozen embryos, and severely impaired infants. Thus, in pursuing the question of our duties to the natural environment, it becomes necessary to examine a more fundamental philosophical issue: Where do we draw the boundaries of moral consideration? Who and what should have moral standing? On what grounds do we make these decisions? This question of moral standing, and the possibility of a nonanthroprocentric environmental ethics, became the focus of significant early work in environmental ethics as philosophers examined the possibility of direct moral responsibilities to the natural world.

One of the earliest contemporary discussions of the moral standing of animals and other living beings was developed by Joel Feinberg. Feinberg argued that to meaningfully say that we have an obligation *to* some object, rather than merely an obligation *regarding* that object, that object must have some welfare or good of its own. But to say that something has a good or a "sake" of its own is to say that it has interests, and for something to have interests, it must be capable of rudimentary cognitive experiences. On Feinberg's grounds, individual animals do, but plants, species, and nonliving natural objects do not, qualify for moral standing. Feinberg was one of the first among contemporary philosophers to make the claim that animals have more standing and deserve consideration in ethical matters.

Prior to the 1970s, ethicists within the Western tradition seldom considered such questions, and when they did, there was almost a universal consensus that only human beings had moral standing. In the *Politics,* Aristotle asserted that the entire natural world exists for the sake of man. Similarly, the medieval Christian philosopher Thomas Aquinas argued that God had created the earth and all things on it for human use. In the 17th century, René Descartes argued that animals were little more than thoughtless brutes or machines. Immanuel Kant, in the 18th century, concluded that only humans were subjects or ends in their own right, while plants and animals were mere objects and could therefore be treated simply as means to our own ends. Thus, while acknowledging that plants and animals were living beings, much of the Western tradition concluded that they lacked a certain characteristic by virtue of which living beings gain moral standing. In most cases, this missing characteristic would have been described in terms of some cognitive or spiritual capacity: reason, mind, consciousness, or the soul. As a result, much of that tradition was unsympathetic to the idea that humans have any direct moral responsibility to the natural world.

According to some critics, this Western tradition of philosophical and theological thought was not only unsympathetic to environmental concerns; it actually was among the root causes of the contemporary environmental crisis. Lynn White argued that one dominant perspective within the Judeo-Christian tradition has played a major role in bringing about environmental problems. This perspective views human beings as occupying a privileged position within all of creation. Being created in the image and likeness of God, humans transcend nature, which has been given to them by God to use as they wish.

But there have long been minority voices within that tradition. White acknowledges Christian sources such as Francis of Assisi, who advocated a much more harmonious relationship between humans and the rest of creation. Jeremy Bentham was one of the few philosophers within that tradition who questioned the exclusion of animals from moral consideration. As a utilitarian, Bentham was committed to the view that pleasure and pain were the ultimate determinates of moral value. The utilitarian axiom to maximize overall good was, on Bentham's account, equivalent to maximizing pleasure and minimizing pain. Given this, Bentham argued that the question of moral standing was not whether animals can reason or talk but whether they can suffer. On these grounds, it would seem that animals deserve moral consideration.

At about the same period when contemporary ethicists were first raising the possibility of moral standing for animals, Christopher Stone proposed that the time had come to recognize legal standing for natural objects such as trees and mountainsides. Drawing on a parallel with the legal standing already granted to things such as corporations, trusts, cities, and nations, Stone argued that natural objects deserved the same legal status. Natural objects have interests that can be represented by legal guardians, they can suffer injuries, and they can benefit from court-sanctioned relief. Stone proposed that courts should recognize the legal rights of natural objects and appoint guardians to represent their interests in cases in which they might suffer harm.

Environmental Ethics and Animal Welfare

The challenge of ethical extensionism directly raised the issue of direct moral responsibilities to natural objects. For the first time in the Western philosophical tradition, ethicists began to give sustained attention to the possibility that humans have moral responsibilities to other living beings. The question of moral standing for natural objects was most fully developed by those philosophers who addressed the question of our ethical responsibilities to animals. At least initially, these questions were thought to be central to a fully developed environmental ethics.

Perhaps the person most associated with the extension of philosophical ethics to animals is Peter Singer. Since the 1970s, Singer has argued that our exclusion of animals from moral consideration is on a par with the earlier exclusions of blacks and women. Singer popularized the term *speciesism* to draw a parallel with racism and sexism. Just as it is morally wrong to deny equal moral standing on the basis of race or sex, Singer argues that it is wrong to deny equal moral standing on the basis of species membership.

To explain which characteristic qualifies a being for equal moral standing, Singer cites the passage from Bentham referred to earlier: The question is not whether they can reason or talk but whether they can suffer. Singer uses the term *sentience* to refer to the capacity to suffer and/or experience enjoyment. Sentience is *necessary* for having interests, in that an object without sentience, a rock, for example, cannot be said to have interests. But Singer also believes that sentience is *sufficient* for having interests. Because all animals above a certain neurological threshold are sentient, all such animals deserve direct moral consideration.

While Peter Singer defended the moral standing of animals on utilitarian grounds, Tom Regan developed a rights-based defense of animals. Regan explicitly argues that some animals have rights and that these rights imply strong moral obligations on our part. Like Singer, Regan condemns on ethical grounds a wide variety of human activities that affect animals. These activities include the use of animals in scientific and commercial research; the use of animals as food; and recreational uses of animals such as in sport hunting, in zoos, and as pets. Regan believes that these practices are wrong in principle but not because of the pain and suffering they cause. They violate animal rights by denying the inherent ethical value that some animals possess.

Why is it wrong, in principle, to treat animals as food, targets, entertainment, or slaves? Regan's answer is that it is wrong for the same reason that it would be wrong to treat humans in such ways. Many animals are *subjects of a life.* Having a life, as opposed to merely being alive, involves a fairly complex set of characteristics, including having beliefs and desires, having interests, having a psychological self-identify over time, and having feelings of pleasure and pain. Regan argues that many animals can be subjects of a life. Most mammals, for example, possess the characteristics required for "having a life." These animals therefore have inherent value, and justice demands that we treat them with respect. Minimally, this means that we have a strong obligation not to harm them.

Both Singer and Regan have written extensively on the ethical implications of their views. Both would argue that we have a responsibility as a society to end most commercial animal farming. Likewise, sport hunting and trapping are unjust. Indeed, abusing and mistreating animals for any form of human entertainment is wrong. A third issue concerns the use of animals in science and research. Experimentation on animal subjects can be especially harsh. We ordinarily would conclude that experimenting on human subjects who have not given their consent is unjust at best and barbarous at worst. People have been convicted as war criminals for such behavior. So, too, should we judge experimentation on animals.

Despite the fact that both Singer and Regan defended extending moral consideration to natural objects, it soon became clear that the animal welfare approach raised serious environmental problems. While granting moral status to animals has some obvious implications for how humans ought to interact ethically with the natural world, it is not clear that granting animals moral status will prove to be an adequate *environmental* stance. These challenges shape the remainder of this entry.

First, in the view of some environmental ethicists, an ethics that begins with extended standard ethical principles remains fundamentally hierarchical and begs the question about the moral status of other living things. For example, both Singer and Regan attribute moral standing only to some animals. Other living things remain outside the range of moral consideration. This omission strikes many environmentalists as both an ethical and a logical mistake.

Second, these extensions remain thoroughly individualistic. Individual animals have standing, but plants, species, habitat, and relations have no standing in their own right. Yet environmentalism is strongly influenced by ecology, and so much of the science of ecology stresses the interconnectedness of nature. Ecology emphasizes wholes such as species, biotic diversity, populations, ecological communities, ecosystems, and biological, chemical, and geological cycles. Relations, communities, systems, and processes play a major role in the science of ecology. To preserve the ecological integrity of a certain ecosystem, it might, for example, be necessary to destroy members of a deer population or thin an overpopulated herd of elephants. Unfortunately, standard ethical theories and the animal welfare approach have little room for such concerns. Indeed, at one point, Regan dismissed the ethical focus on communities rather than individual animals as environmental fascism, a view that is willing to sacrifice actual living individuals for the sake of an abstract whole. To some environmentalists, this was an ethical prescription at odds with sound environmental policy.

Finally, ethical extensions to animals were not, nor were they intended as, comprehensive environmental ethics. Philosophers applied ethics to specific problems as they arose and as they were perceived, with little or no attempt at building a coherent and comprehensive theory of environmental ethics. This focus has had two unhappy results. First, the extension of ethics to cover, for example, the rights of animals can provide no guidance for many other environmental issues such as global warming or pollution. Second, extensionism tends to remain critical and negative. It often tells us what is wrong with various policies and actions but seldom offers anything about what the alternative "good life" should be. We turn now to approaches that develop out of these challenges.

Biocentric and Ecocentric Environmental Ethics

Two alternative approaches to environmental ethics, biocentricism and ecocentricsim, develop from these criticisms. Biocentric ethics argues that life itself provides a nonarbitrary criterion for moral standing. Biocentric ethics refers to any theory that views all life as possessing intrinsic value. (The word *biocentric* means life centered.) One criticism of the animal welfare approach suggests that the extension of moral standing to animals has remained, in a peculiar sort of way and despite its intentions, anthropocentric. Consider that the philosophical methods used by Feinberg, Singer, and Regan all begin by taking human beings as the paradigm of beings with moral standing. Thus, only animals that are enough like us can have (or only to them can we "give") moral standing. Moral standing seems a benefit that is derived from human nature and that living beings receive only if they are enough like humans.

Take the case of invertebrates. In the views of many environmentalists, preservation of invertebrates (animals that lack a backbone, such as insects, jellyfish, and mollusks) should be an ethical concern. So, too, should preservation of plants. Yet in the most obvious reading of the animal welfare ethics, these living beings lack the necessary criteria for moral standing. Invertebrates and plants are neither sentient nor subjects of a life. Biocentric ethics argues that although it may be plausible to say that sentience and subjectivity are sufficient, they are not necessary.

Ecocentricism is the second major alternative to ethical extensionism. Ecocentric environmental ethics develops out of a more ecological perspective of environmentalism. Most animal-rights-based ethics, like most traditional ethical theories, are *individualistic*. That is, ethics is concerned with protecting and promoting the well-being of individuals, not communities or societies or some one "common good." This puts them at odds with much environmental and ecological thinking, which is *holistic*. Many environmentalists emphasize "biotic communities," "populations," or "ecosystems" rather than individual members (including humans) of those communities.

But beyond this issue, the individualistic bias of the animal welfare approach seems to imply other consequences that many environmentalists find unacceptable. From the animal welfare perspective, an animal that is a member of an endangered species has no special moral status. The last remaining pair of bald eagles or spotted owls, if they lack the requisite neurological or cognitive apparatus, have less of a moral claim on us than a single whitetail deer. Preservation of the endangered blue whales is ethically no more important than preserving cows. We have no greater duty to mountain gorillas and black rhinos than to a stray cat, and we certainly have no direct ethical obligation to the millions of species of plants and animals that are not subjects of a life.

Similarly, Singer's views would also suggest counterintuitive conclusions to many environmentalists. Given the amount of suffering that can take place with intensive farming techniques, any one of literally billions of chickens would have a stronger moral claim against us (to relieve its suffering) than would the last remaining members of a plant or invertebrate species. Thus, according to critics, whatever else it might be, the animal welfare movement is not a central part of the environmental movement.

The critical point raised by an ecocentric ethics is that animals, like humans, are part of a complex ecological community. From within an ecocentric perspective, the equilibrium of natural ecosystems should be the goal of an environmental ethics. Giving special ethical protection to individual animals threatens to upset that balance and cause damage elsewhere within that system. Thus, culling a herd of deer or destroying an invasive nonnative species of rabbits to prevent damage to an ecosystem may be an ethically responsible action. Animal welfare ethicists would find such acts abhorrent. On the other hand, protecting the rights of individual animals might well lead to serious ecological harms. There simply is no guarantee that a species—or, more generally, an ecological community—would be preserved if only we protected the rights of individual animals living within that community. Ecocentric environmental ethics shifts attention to our ethical responsibilities to biotic and ecological communities such as species and ecosystems.

Environmental Philosophies: Deep Ecology

The issue of moral standing highlights the fact that environmental issues raise a range of philosophical questions beyond those normally considered within standard ethical theory. Ecocentric approaches, for example, can raise epistemological questions about biological purposes and functional explanations. They raise metaphysical questions about the nature of individuals. Are species, populations, or even genes more "real" than individuals? Perhaps more influentially, environmental issues also raise fundamental questions of social and political justice. Thus, in recent decades, philosophical attention has been paid to developing environmental philosophies that address broader questions than those of ethics alone.

Deep Ecology was one of the first more comprehensive environmental philosophies. The Norwegian philosopher Arne Naess first introduced a distinction between deep and shallow environmental perspectives. Naess characterized the shallow ecology movement as committed to the fight against pollution and resource depletion. It is an anthropocentric approach with a central objective to protect people in developed countries in terms of their health and affluence. Deep Ecology, on the other hand, takes a more holistic and nonanthropocentric approach. Naess's basic point can be made in terms of symptoms and underlying causes. By focusing on issues such as pollution and resource depletion, the shallow approach looks only at the immediate effects of the environmental crisis. Just as a sneeze or a cough can disrupt a person's daily routine, pollution and resource depletion disrupt the lifestyle of modern industrial societies. However, it would be a mistake for medicine to treat only sneezing and coughing and not investigate their underlying causes. So, too, it is a mistake for environmentalists to be concerned only with pollution and resource depletion without investigating their social and human causes.

What distinguishes Deep Ecology as a philosophical approach is its tenet that the current environmental crisis can be traced to deeper philosophical causes. Thus, a cure for the crisis can come only with a radical change in our philosophical outlook. This change involves both personal and cultural transformations and would affect basic economic and social structures. In short, we need to change ourselves as individuals and as a culture.

Deep Ecologists are committed to the view that a solution to the environmental crisis requires more than mere reform of our personal and social practices. They believe that it requires a radical transformation of our worldview. Thus, Deep Ecologists proceed in two directions. On the one hand, many are committed as scientists, artists, and political activists to work for the types of changes needed. On the other hand, Deep Ecologists also seek to develop and articulate an alternative philosophy to replace the dominant worldview that is responsible for the crisis.

The activist side of Deep Ecology has developed in similar ways as other radical social movements. Some practitioners have withdrawn from the social and cultural practices that they believe underlie environmental destruction and adopted alternative lifestyles. Other self-described Deep Ecologists have taken the more political roles of social protest and activism.

The philosophical side of Deep Ecology has focused on criticizing the so-called dominant worldview and articulating an alternative worldview. Deep Ecologists trace the cause of many of our problems to the metaphysics presupposed by the dominant philosophy of modern industrial society. The transformation they seek involves a shift away from the dominant model and toward an alternative worldview that takes its inspiration from ecology.

Deep Ecologists argue that the dominant metaphysics that underlies modern industrial society is fundamentally *individualistic* and *reductionistic*. This view holds that only individuals are real and that we approach a more fundamental level of reality by reducing objects to their more basic elements. But this dominant worldview also sees humans as fundamentally different from the rest of nature. Individual human beings possess a "mind" or "free will" or "soul" that exempts them from the strict mechanical determinism characteristic of the rest of nature. Thus, this traditional worldview creates a strict divide between humans and the natural world, a divide that explains and justifies seeing the natural world as made up of mere objects that can be used or exploited for human ends.

Rejection of these dominant beliefs is central to the metaphysics of Deep Ecology. Taking its cue from ecology, the metaphysics of Deep Ecology denies that individual humans are separate from nature. Instead, Deep Ecologists are committed to a version of metaphysical holism. Humans are fundamentally a part of their surroundings, not distinct from them. Humans are constituted by their relations to other elements in the environment. In an important sense, the environment determines what human beings are.

A philosophy that reduces humans to individuals that are somehow distinct from their social and natural environment is radically misguided. Human nature is inseparable from nature.

Deep Ecologists derive two ultimate norms, self-realization and biocentric equality, from this metaphysics. Self-realization is a process through which people come to understand themselves as existing in a thorough interconnectedness with the rest of nature. Biocentric equality is the recognition that all organisms and beings are equally members of an interrelated whole and, therefore, have equal intrinsic worth.

Social Ecology and Ecofeminism

The problem with Deep Ecology, in the view of many critics, is that it has overgeneralized in its critique of human centeredness, anthropocentrism, and the dominant worldview. From this point of view, not all humans or all human perspectives are equally at fault for environmental problems. When Deep Ecologists critique *the* dominant worldview, they fail to acknowledge that many humans are not part of that dominance. Thus, Deep Ecologists are too broad in their critique and, thus, overly broad in their positive program.

One version of this critique is raised by the Indian ecologist Ramachandra Guha. In Guha's view, Deep Ecology would have disastrous consequences, especially for the poor and agrarian populations in underdeveloped countries. Guha reasons that a policy of biocentric equality and wilderness preservation in a place such as India would effectively result in a direct transfer of wealth from the poor to the rich and a major displacement of poor people. At best, Deep Ecology is irrelevant to the environmental concerns of people in underdeveloped countries. At worst, it can be harmful to the very people who already are victimized by social and political dominance.

Similar critiques of Deep Ecology have been offered by thinkers associated with two other movements in environmental philosophy, *social ecology* and *ecofeminism.* These perspectives agree that in the search for the "deep" underlying causes of the environmental crisis, Deep Ecologists have focused their attention at too abstract a level. The more significant causes can be located at a much more localized level: the social, economic, and patriarchal structures of contemporary societies. Each philosophy claims that in faulting anthropocentrism, Deep Ecologists fail to recognize important distinctions between people. If there is *a* dominant worldview, Deep Ecology must recognize that many humans are also oppressed by it. Not all humans are equally at fault for environmental destruction, and not all humans were included in the "human-centered" dominant worldview. Instead of looking at some abstract dominant worldview, these critics seek to specify the particular practices and institutions that dominate both human and nonhuman alike.

Social ecologists and ecofeminists argue that the root of our ecological crisis lies in certain social factors. Specifically, social ecologists and ecofeminists believe that the domination and degradation of nature arise from social patterns of domination and hierarchy, patterns of social life in which some humans exercise control or domination over others. Thus, both approaches shift the philosophical attention away from questions traditionally associated with metaphysics and ethics and toward questions traditionally associated with social and political philosophy. Social justice becomes the primary focus of these philosophies.

A central insight of these views concerns the relations between individual humans and the patterns of social organization in which they live. Remember that societies are human creations, organized and structured by human beings in ways that serve human ends. Thus, when examining social problems such as environmental destruction, we should ask about the ends or purposes served by the particular institutions causing the problems. Who is benefiting from and who is being harmed by our social practices? In the views of social ecologists and ecofeminists, many social structures serve to oppress some members of society for the benefit of others.

This oppressive social structure in turn works to reinforce a way of thinking and living that encourages domination in all forms, including domination of the natural world. In this view, environmental and ecological destruction is best understood as a form of human domination, in this case the human domination of nature. To understand this crisis more fully, both social ecologists and ecofeminists agree that we need to understand the more general patterns of human domination of other humans. Thus, an adequate understanding of the ecological crisis must address fundamental questions of social and political philosophy. We must identify and analyze the patterns of domination and oppression within societies and evaluate these patterns in terms of philosophical accounts of justice.

Social ecology and ecofeminism can be distinguished by looking at their analyses of the various types of social domination and their alternative conceptions of justice. Social ecologists such as Murray Bookchin attribute environmental destruction to what they see as general and widespread forms of economic and political domination. These would include social practices and structures such as racism, sexism, and class structures as well as private ownership, capitalism, bureaucracies, and even the nation-state. These social practices and institutions establish social hierarchies in which some humans exercise power and domination over others.

Ecofeminists, such as Karen Warren, identify the oppression of women as a principal form of social domination. Ecofeminists identify many close connections between the oppression of women and the oppression of nature. As a result, they believe that the goals of the feminist movement closely parallel the goals of the ecological movement. However, ecofeminists offer various analyses of women's oppression and appeal to various accounts of social justice in critiquing this oppression and developing alternative nondominating models of society.

Ethics and Sustainable Development

The important insight of these environmental philosophies lies in the recognition that environmental problems cannot be separated from the broader concerns of social justice. It is easy for environmentalists to lose sight of an important truth. Environmental concerns are only one among several areas of ethical focus. As the social ecologists and ecofeminists remind us, environmental destruction must be understood within broader ethical contexts. Issues of social justice should not be ignored by environmentalists, nor should economic and political factors. To understand the implications of this claim, consider the environmental challenges that humans face in a broader context.

As environmentalists point out, the earth's biosphere is under severe stress. Economic growth and industrialization during the past two centuries has played a clear role in causing these problems. Worldwide population growth guarantees that pressure for continued growth will continue into the foreseeable future. Nevertheless, other ethical problems are at least equally demanding. Literally billions of people across the globe live in poverty and lack basic nutrition, health care, education, and employment. An ethically responsible stance must pay attention to both environmental destruction and human suffering.

But what is the role of economic markets, economic growth, and industrialization in this ethical stance? Paradoxically, it may be the case that the problem is part of the solution. On the one hand, unfettered markets and economic growth have been responsible for significant environmental damage. On the other, addressing the real human suffering of billions of people will require a dynamic and extensive economic system. The concept of sustainable development has been proposed as a resolution to this paradox. Future economic activity must be economically vigorous enough, and ethically focused, to meet the real needs of the world's population, and it must do so in ways that are environmentally sustainable. The three criteria of economic, ethical, and environmental viability have come to be called the "three pillars of sustainability," or the "triple bottom line" of sustainable economic activity.

From the perspective of Deep Ecology and some social ecologists and ecofeminists, sustainable development appears to be a capitulation to the economic forces that are at the root of much environmental destruction. Supporters offer two general arguments in defense of sustainability. First, sustainable development is a more pragmatic and realistic response than the radical programs associated with these other environmental philosophies. Sustainable development recognizes that it is not economic activity in itself that has caused environmental degradation but only a certain type of economic activity. Social and economic development, rather than unguided growth, should be the standard of economic activity. Second, sustainable development provides a more ethically balanced approach to environmental and social justice.

The field of environmental philosophy and ethics has often been driven by very practical policy concerns. Pressing social problems such as pollution, ecological destruction, species extinction, and resource depletion motivated ethicists to develop systematic accounts of environmental values. The goal for many is to develop a coherent and comprehensive theory of environmental ethics. However, a plausible case can be made that the ethical and value issues associated with the natural environment are too diverse and wide-ranging to be unified into one single environmental philosophy. Many now think that a more pragmatic approach is called for, an approach that recognizes the plurality of environmental values and principles and emphasizes a greater consensus on practical policy prescriptions.

—Joseph R. DesJardins

See also Animal Rights; Animal Rights Movement; Anthropocentricism; Biocentrism; Biodiversity; Deep Ecology; Environmentalism; Environmental Protection Legislation and Regulation; Gaia Hypothesis; Greenhouse Effect; Green Values; Land Ethic; Pollution; Population Growth; Sustainability; Triple Bottom Line; Wilderness

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Environmentalism

In general terms, *environmentalism* can be defined as a concern with safeguarding the natural world and its various elements and the differing ways in which such a concern is expressed by people. Specifically, environmentalism comprises differing philosophical approaches to nature and several social movements based on them. Conservation, preservation, "wise use," the wilderness movement in the United States, environmental protectionism, and sustainability, among other philosophies and social movements, help form and define environmentalism. Various scientific enterprises, such as the science of ecology, that have made the environment their subject matter should also be counted as part of this notion.

Individuals who were prominent in the early vanguard of the environmental movement include Henry David Thoreau, John Muir, Gifford Pinchot, and Aldo Leopold. The contemporary expression of the environmental movement is often said to have begun with the publication of Rachel Carson's *Silent Spring*, a book exposing the dangers of pesticides and the widespread production and commercialization of chemicals. Today, the movement is witnessing radicalization at the hands of some who have practiced "ecoterrorism." Environmentalism has had a major impact on how business conducts itself in the form of governmental regulations dealing with environmental protection. Indeed, the impact of corporate decision making on the environment has become a central social and ethical concern today to the point that business organizations have included the question of environmental impact in their own governance. After reviewing some of the basic concepts of environmentalism, this entry will turn to a survey of some of the major historical figures and theories of this movement.

Environmental Concepts

Environmentalism is partly defined by several concepts, some of which are in opposition to others. In fact, much of the controversy that surrounds environmental public policy formulation arises from this conceptual level, where views about the environment may greatly differ. In general, however, environmentalism is an expression of respect for nature and the natural environment that surrounds humans on this planet. Yet agreement about how this respect should be put into practice is not always easily reached. For example, at the beginning of the environmental movement, the distinction between the "preservationist" and "conservationist" environmental philosophies was problematic and led to great public policy debates that included factions from business and industry, the government, and environmental activists.

Simply stated, preservationism holds that respect for nature means that we are obliged to keep nature preserved and maintained in its pristine beauty, which must be passed on to future generations. Besides making such moral claims about the aesthetics of nature, preservationists usually also hold that nature has an intrinsic value that requires preserving and protecting. Some preservationists take this argument further and claim that nature has a high spiritual value for humans, since it was created by God, who is held to be immanent within it. Thus, for preservationists, nature is deserving of great respect from humans, and it is mandatory that it be preserved and kept intact for future generations, and public policy decisions should reflect this philosophy.

Conservationism is conceptually different from preservation, although the two terms are often used interchangeably in the popular literature of environmentalism. However, conservationists do express their understanding of how nature should be respected quite differently than do preservationists. To preserve nature is to keep it protected in its current state and quality without allowing any deterioration, but to conserve nature is to carefully use the natural environment as a resource in a way that does not exhaust or waste it and, thereby, to ensure its availability in the future. In conservationism, the emphasis is thus on use and productivity, and this reflects a philosophy of utility, which is not at all different from the idea of utility inherent in business, where nature is respected for the usefulness it represents to humans. Nature has only instrumental value, according to conservationists. Hence, the differing ways in which nature is respected in these two basic concepts of environmentalism account for a good deal of past and present public policy wrangling about the environment.

Conservationism was closely associated with the "wise-use" practitioners, who originally wanted conservation efforts to be guided by established scientific principles of management. This idea goes back to the end of the 19th century and the policies that emerged around how the United States would manage its wilderness areas, especially its vast western forests. Their managed, wise use within a kind of utilitarian conservation was proposed and accepted as the appropriate public policy, and this form of environmentalism became the hallmark of the Progressive Era politics embraced by President Theodore Roosevelt. This policy was favorable to industries such as lumber and mining, since it emphasized using natural resources and these businesses were in a position to profit greatly from such utilitarian policies.

Today, however, the term *wise use* often refers to a loosely organized coalition of mostly grassroots and special interest groups offering proposals that seem to be counter to the so-called green revolution or green movement. Specialized interests from the timber, mining, and chemical industries have entered the various public policy debates about the environment and have often provided funding for many of the wise-use groups that have become very vocal in environmental politics.

Hence, the concept of wise use has undergone something of an evolution in which its basic meaning has been transformed. Now *wise use* is a much more politically charged phrase. Wise-use advocates today will argue that the federal government should not only sell off public lands and privatize them but also not buy any more land in the hope of preserving ecosystem habitats, as it has done in the recent past at the urging of the green movement. In short, the environmental public policy arena has been characterized at times by the somewhat polarizing views of these two subgroups of the environmentalism movement. Some of the policy skirmishes in which they have been at opposite ends include the protection of animal habitats in logging areas (e.g., the northern spotted owl), policies on the growth of the ozone hole, laws preventing further global warming, the reduction of "greenhouse gases," the regulation of pesticide use, and so on.

Another central concept found within the context of environmentalism is that of *ecology*. This term actually designates several aspects of the idea of environmentalism, and it is even used as a synonym for it at times. First of all, it can be understood as designating the "science of ecology." In this sense, what is usually meant is the scientific study of how organisms—including humans—interrelate with their physical environment. The word can be traced to the writings of the German biologist and proponent of Darwin's theory of evolution Ernst Haeckel, who first used it in 1866. Haeckel derived the word from the Greek term *oikos*, which means house, home, household, or family, and so today, *ecology* has come to mean the study of the household of nature and how the members that make up the family of nature interrelate. Ecology has become that branch of science that predicts the effects that natural entities, especially humans, have on the environment.

The science of ecology is multidisciplinary. This means that it incorporates many other branches of science and devotes itself to various and diverse areas of study. So, for example, the fields of botany and zoology, chemistry and geology, and others are used by ecologists in their work, and they will study areas as different as individual organisms, populations, communities, ecosystems, and the biosphere itself. We have "arctic ecology," "tropical ecology," and "desert ecology," as well as considerations of "ecological crises" such as overpopulation, deforestation, and desertification. In short, the science of ecology is an eclectic field with wide applications.

Moreover, the term *ecology* also designates much more than just this scientific enterprise. The term has also come to designate the social movement that seeks public policies designed to protect the environment, especially from the ravages of pollution. The term when used in this fashion is, therefore, often a synonym for the term *environmentalism*, and then its meaning is much broader than when it is used to designate a branch of the biological sciences. So the phrases *ecological movement* and *environmental movement* are used interchangeably.

But the environmental concept that has become central in most discussions in this area is the notion of "sustainability." It could be argued that sustainability has become the premier concept in the environmental movement. It and the phrase *sustainable development* are banners of the contemporary environmental movement and are part and parcel of the social, economic, and political aspects of environmental matters. In general, the term *sustainability* refers to an ability to meet the current needs of a population while at the same time not harming the possibility for future generations to meet their needs as well.

This is the gist of the definition devised by the World Commission on Environment and Development, often called the Bruntland Commission after the Norwegian woman who chaired it, in its 1987 report titled "Our Common Future." The Commission, established by the United Nations, had identified a strategy in which economic development issues and environmentalism would be merged. This was necessary, according to the Commission, because it was concluded that the more developed nations were engaged in nonsustainable patterns of consumption and production, leading to the possibility that future generations would not be able to sustain themselves. This public policy debate about whether current levels of consumption and production are sustainable or not continues today.

The Bruntland Commission also urged that an international conference be convened to review the progress of steps taken in the direction of sustainable development, and in 1992, the so-called Earth Summit took place in Rio de Janeiro to explore topics such as climate change, preserving biodiversity, the problem of deforestation, and other environmental problems. The Earth Summit, officially called the United Nations Conference on Environment and Development, became the largest meeting of world leaders ever. A set of global strategies called "Agenda 21" was agreed to by 170 nations that established guidelines for environmental policies to be implemented in the 21st century by the convention's signatories. In the United States, Bill Clinton established the President's Council on Sustainable Development for the purpose of implementing Agenda 21 in 1993.

Of course, the terms *sustainability* and *sustainable development* were not and are not without their controversies, nor are UN commissions and conventions on the environment free from criticism. While the more left-leaning green movement promoted these ideas, the right wing of the environmental movement and the many critics of the "greenies" saw in them an undesirable political agenda. They believed that these ideas were designed to usher in a "new world order" where the sovereignty of nation-states and the free enterprise system would be replaced with a UN-sanctioned world government that would displace individual liberty and property rights. This critique of and objection to environmentalism was most pronounced in the reaction to the proposals of the Kyoto Protocol.

In brief, the Kyoto Protocol was agreed to by 84 nations in Kyoto, Japan, in 1997 as a major addition to the United Nations Framework Convention on Climate Change, which was another product of the 1992 Earth Summit. The main goal of the Kyoto accords was to fashion a plan that would cut greenhouse gas emissions (carbon dioxide, methane, nitrous oxide, hydrofluorocarbons, perfluorocarbons, and sulfur hexafluoride) as a strategy to address global climate change. The world's more developed nations—a total of 38 countries, including, at the time, the United States—agreed to reduce their emissions by approximately 5% below their 1990 levels. In February 2005, the Protocol came into force as Russia ratified it, and by the following September, it had been ratified by a total of 184 countries, representing approximately 60% of the world's emissions of greenhouse gases. However, the major exceptions in the ratification process were Australia and the United States.

President George W. Bush stated in March 2001 that he would not submit the Kyoto Protocol to the U.S. Congress for ratification since he believed that it imposes an unfair economic burden on the United States and that it treats other countries that are responsible for much of the world's greenhouse gas emissions, in particular India and China, much more favorably. So, the overall success of the Kyoto agreements is in doubt given that the United States is not a party to them. Nonetheless, a number of U.S. states and cities have decided to observe climate protections themselves and have agreed to meet, and in some cases to beat, the Kyoto Protocol emission targets. By December 2005, 192 cities in the United States, including many of the largest, such as New York, had pledged to adhere to the Kyoto agreement.

The History of Environmentalism: Thoreau and Muir

Although it might be difficult to demarcate the actual beginning of environmentalism in the United States, the first wave of the environmental movement can be traced to the nonconformist Henry David Thoreau (1817–1862). Thoreau has often been called America's first environmentalist, and his writings in philosophy, social criticism, and naturalism have been hailed for their spirited independence and freethinking. His observations on nature have been said to anticipate the science of ecology. His book *Walden, or, Life in the Woods* (1854) is a classic text that is part social critique and part environmental analysis but dedicated to the general issue of simple living, or what today might be called *sustainability*. *Walden* relates Thoreau's experiences in a home that he built for himself on the edge of Walden Pond near Concord, Massachusetts, on land that was owned by his friend Ralph Waldo Emerson (1803–1882), the well-known American essayist, thinker, and writer.

In *Walden* and in the journals that he kept for more than 24 years as well as in a variety of "nature essays," Thoreau displayed his respect for nature. This was also reflected and refined in the philosophical school that he, Emerson, and others from New England founded and called "Transcendentalism." This school of thought held that reality was divided into two spheres, the soul and nature. The Transcendentalists claimed that thanks to God's revelation as a force in nature and thanks to God's immanence, each person had a direct knowledge of God. But at the same time, Thoreau's collected writings reveal a preoccupation with environmental matters, and his surveying, lists, charts, and other systematic accounts demonstrate his desire to express his understanding of nature in a more scientific manner. It was likely this unique combination of a spiritual feeling for and a scientific approach to nature that had an impact on the second generation of environmentalists, such as John Muir, the founder of the Sierra Club.

Muir was first acquainted with Thoreau as a student in 1862, and he possessed an edition of *The Writings of Henry David Thoreau* that he had annotated heavily. There is a commonality between the two men on environmental topics, but Muir was not at all a carbon copy of Thoreau. Muir was much less reclusive than Thoreau, and he traveled greatly in his life, having been to Africa, Australia, South America, Asia, and Europe. Yet even with all his travels, it was the Sierra Nevada and the Yosemite Valley area that made a claim on his allegiance, and he devoted much time to political initiatives to preserve the grand beauty of this region, which is not to say that Muir didn't have ample familiarity with other sections of the United States. In fact, in 1867 he walked a thousand miles from Indiana to Florida. He had an exciting and interesting life as an inventor, explorer, farmer, and environmentalist.

Although he was born in Scotland, Muir's contribution to the environmental history of the United States was immense, and in recognition of his work, there are more than 200 sites in the United States named after him. Known as the "father of the national parks," Muir's activities as a persuasive writer did much to lead to the congressional creation of the Yosemite, Sequoia, Mount Rainier, Petrified Forest, and Grand Canyon national parks. He first came to California in 1868, where he explored and studied the Sierras, and based on his findings, he formulated what was to become a controversial geological theory about how glaciers had formed the Yosemite Valley. His writing career began around this time, just after the end of the Civil War, and he published a series of articles titled *Studies in the Sierra*. In the course of his life, he published more than 300 popular articles that appeared in magazines such as *Harper's Monthly Magazine*, *The Century Magazine*, and the *Atlantic Monthly*, as well as a dozen major books that recounted his experiences with nature.

In 1892, Muir founded the well-known environmental group The Sierra Club. The group has been lauded by the left wing of the environmental movement but lambasted by the right. The original goal of the club was to preserve and protect the Sierra Nevada, but since its founding, the club has become one of the leading voices in the environmental movement. For Muir at the turn of the century, the club served as a platform from which to launch a number of important campaigns, with the most challenging being his fight against the damming of the Tuolumne River at the mouth of Hetch Hetchy Valley to create a reservoir for the city of San Francisco.

To Muir and his followers, Hetch Hetchy was a "mountain temple" standing in need of preservation. He held that the wilderness should be left as is and that commercial interests should not take priority. For others opposed to Muir's idealism, using such sites to serve the needs of people trumped the idea that nature had some intrinsic value, and, in the eyes of this group, Muir's writings were seen as mystical and even at times misanthropic. In any event, the battle of the reservoir at Hetch Hetchy began the long-running debate, continuing on even today, between preservationists such as Muir and conservationists, who urged a kind of "wise use" of the environment. The latter group was well represented by Gifford Pinchot, who became the spokesman of conservation and the use of science in conserving natural resources.

The History of Environmentalism: Muir and Pinchot

The name Gifford Pinchot (1865–1946) is synonymous with forestry in the United States, and he is often called the "father of modern forestry." In 1893, there were serious concerns about the state of western forests, so a National Forestry Commission was established with Pinchot as one of the six primary members. Muir's poor health kept him from serving on this Commission, but he did serve as an unofficial adviser to it and traveled with members to collect data. This context would serve as the backdrop to the first meeting between Pinchot and Muir, and at the time, they became friends. This friendship was hard-pressed in later years, as the two became estranged thanks primarily to their basically different environmental attitudes and the battles that erupted over this difference.

The usual designations assigned to these two giants of environmentalism are preservationist and conservationist. As stated above, Muir's activism was based on the recognition of an intrinsic value in nature that he wished to preserve and protect. Muir saw the aesthetic qualities of nature as providing people with the chance for a spiritual renewal and a respite from the growing burdens of modern society. The preservationist philosophy was reflected in Muir's founding of The Sierra Club and his many writings, and the influence of Thoreau's Transcendentalism is seen in this aspect of environmentalism as Muir raises nature to an almost sacred level. For Muir, mountains and forests need to be preserved since they provide a perfect aesthetic antipathy to the artificial creations of society.

Pinchot is better known for his utilitarian conservationist attitudes, which he promoted as the first director of the U.S. Forest Service, a post he held from 1898 to 1910, and as the chief proponent of President Theodore Roosevelt's Progressive Era political goals in the area of nature conservancy. As a utilitarian, Pinchot saw the forests for what they could do for Americans and their economy. He was among the first to hold that science and the principles of scientific management could be applied to the vast forests of the West. Until his administration of the U.S. Forest Service, the lumber industry had been practicing a haphazard clear-cutting method that left huge areas denuded. Pinchot wanted to institute a more thoughtful use of the land and its lumber that would not only conserve forests but also sustain business into the future. He saw the scientific principles of forestry as the only way to achieve this goal, and while the timber industry feared that conservation would translate into its demise, Pinchot held that economic and business wise-use development was central to his understanding of conservation.

The first skirmish between Muir, the preservationist, and Pinchot, the wise-use conservationist, occurred during the National Forest Commission studies of how the wilderness of the United States should be treated. The contrasting positions of each became apparent. What was at stake was the type of public policy that would be approved and ultimately decide the fate of U.S. forests for decades, if not longer. What Muir and Pinchot disagreed about initially was sheep. Pinchot thought that sheep should be allowed to graze on public lands, while Muir thought that sheep were a menace to the natural environment of mountainous areas. Here, the opposing views of preservationism and a utilitarian conservationism rose to the fore, and it was enough to end any friendship that Muir and Pinchot had built up earlier. The next battle between the two was over the even bigger issue of whether Hetch Hetchy Valley should be turned into a reservoir serving the needs of the people of San Francisco for drinking water.

For Pinchot, the answer was clear and easy. As a conservationist, he held principles that were based on a view of nature as a resource to be used for human benefit and that it should be used wisely. He sided with those who wanted to dam the Tuolumne River and flood the valley. His argument was based squarely on the wise-use conservationist belief that nature has but an instrumental value. Muir and other preservationists saw this proposal more in terms of a business deal where tycoons were going to make profits from the dam construction, which would not only provide drinking water but also generate electricity to power San Francisco and create large revenues for utility companies. Muir spent 14 years fighting to preserve Hetch Hetchy, but in 1913, Congress approved the plan to make it into a reservoir. Muir was heartbroken by the decision, and he died only a few months after it was made. The O'Shaughnessy Dam was completed in 1923, but the controversy continues today as the two sides are now drawn into a debate over whether the dam should be dismantled in an effort to restore the Hetch Hetchy valley.

The History of Environmentalism: Pinchot and Leopold

Where Gifford Pinchot can be called the first advocate of the conservation movement, Aldo Leopold (1887—1948), also a forester, might be called the first environmental ethicist. This is because his writings took on the task of outlining the obligations that humans have to nature—which he preferred to call "the land"—and the role that humans should play with respect to preserving and protecting the wilderness and living within a "land ethic." Leopold's creative insights have led to the creation of environmental ethics as one of the more recent additions to the general field of applied ethics within the discipline of philosophy.

Leopold was a student at the Yale School of Forestry, where he earned both his bachelor's degree in science and his master's degree, and on his graduation in 1909, he entered the U.S. Forest Service, which was directed by Pinchot. Leopold was greatly influenced at the time by the conservationist philosophy of his superior, but he gradually drew away from the utilitarian thinking of Pinchot and embarked on a different way of thinking about wilderness and the responsibilities that humans had to it. He finally articulated an ethic of environmental responsibility that holds that human actions that do not enhance the biotic community are inherently immoral.

Leopold's philosophy is one that reconstructs the relationship of humans with the land or nature. Previous and more dominant philosophies of nature saw humans as occupying a superior position vis-à-vis it, often as the conqueror of the wild and savage aspects of nature. In his land ethic, Leopold argued, all natural entities, including humans, are equal members of the land community. This represents the first expression of an attempt to switch from the previous and dominant instrumentalist view of nature to a new philosophy that places a more holistic view of nature in a central role of moral consideration. In other words, Leopold's work ushered in and was the beginning of a paradigmatic shift from anthropocentrism to ecocentrism. Such a shift would have a lasting effect on the environmental movement, in general, and on the newly emerging field of environmental ethics, in particular. Moreover, his emphasis on the equality of all members of the land community is one of the first expressions of a rights-based approach to questions of environmental ethics, and it has led to the establishment of schools of thought that hold that nature in general and nonhuman animals in particular need to be considered morally as bearing certain inherent rights.

The History of Environmentalism: Rachel Carson

The contemporary environmental movement is often said to have begun with the publication of *Silent Spring* by the zoologist and biologist Rachel Carson (1907–1964). This landmark work, which took Carson 4 years to complete, diligently detailed the relationship between animal mortality and the use—now understood as the abuse—of man-made chemicals used as pesticides, especially DDT. One of the claims of the book that she tried to demonstrate was that DDT had the effect of softening the eggshells of birds as well as interfering with their reproduction, and that such effects would lead ultimately to their extinction if use of DDT were to continue. It would eventually create a springtime of silence when the songs of birds would not be heard. Her studies also found DDT to be a human carcinogen.

Born in Springdale, Pennsylvania, Carson graduated from the Pennsylvania College for Women in Pittsburgh (now Chatham College), where she majored in English until her junior year, when a course in biology inspired her to switch to zoology as her field of concentration. She earned a master's degree in this area from Johns Hopkins University and became an aquatic biologist at the Bureau of Fisheries in 1936. During this time, she wrote for various national magazines, and her first book, *Under the Sea-Wind*, was published. The Bureau of Fisheries became the Fish and Wildlife Service, and she went on to become its chief editor of publications.

Carson had concerns as early as 1945 about pesticides being used more and more by the government. But her cautionary claims in *Silent Spring* were met with outrage by the pesticide and chemical industries. Her credentials as a scientist were challenged, and it was held that her findings were just the rants of a hysterical woman. She was even accused of being a member of the Communist Party. Monsanto, a large multinational agricultural biotechnology corporation, published and distributed 5,000 copies of a parody of the book, titled *The Desolate Years*, in which it depicted the fate of the world without pesticides. To this day, there are those who hold that DDT is safe to use and that not doing so is resulting in the needless death of countless thousands around the world where malaria is still prevalent. According to Carson's detractors, she was guilty of imposing a kind of "ecological genocide," and they want to drop the ban on DDT since they hold that Carson's work was not scientifically definitive. Some go so far as to say that she perpetrated a lie and a fraud based on poor research findings and poor research ethics.

But even in the face of such great controversy, Carson is still heralded by environmental groups for her initial work in alerting the public to the perils of pollution and its disparaging effects. She is often celebrated as the founder of the contemporary U.S. environmental movement. Yet her work in *Silent Spring*, warning about the misuse of pesticides and other chemicals, has not as yet taken firm hold. Americans likely use twice as much the volume of pesticides that they did at the time she published her seminal work, and globally, their use is ever increasing. Powerful pesticides, herbicides, and bactericides are available to homeowners and sold over the counter, and their use is so widespread that many environmentalists are fearful that chemical runoff into streams and rivers is still contaminating the animals that humans eat and the water that they drink. In short, while the main intent of *Silent Spring* was to alert the public to the dangers of the overuse of pesticides and chemicals, nonetheless the public has embraced such use.

Environmental Management

Business and industry have been deeply affected by environmentalism. There have been many pressures on business organizations from environmental groups that seek to make environmentalism a significant part of corporate responsibility. Governments throughout the world have instituted environmental regulations designed to oversee business production and protect people from pollution and other environmental hazards that business activities can often cause. Furthermore, the public itself has rising expectations about the idea of corporate environmental responsibility, and there are even some who make their purchasing decisions based on the environmental records of the businesses that sell the products that they buy. In response to this growing awareness of and concern with the environmental responsibilities of business, many corporations have become proactively involved in implementing various measures that are designed to address their environmental impact and demonstrate good environmental practices.

The U.S. Environmental Protection Agency (EPA) has become one of the more prominent institutions with a major role to play in the regulation of business and its relationship to the environment. Richard Nixon instituted it in 1970 with one of its goals the establishment and enforcement of environmental protection standards according to which corporations had to measure themselves so that environmental degradation might be slowed. In addition, state governments throughout the United States have also established environmental standards, and some of these are often more restrictive than the federal standards. Indeed, decisions about adequate environmental standards and their restrictions on business activities have been controversial, with many case examples over the years, including standards regulating leaded gasoline and safe emission levels of gases such as chlorofluorocarbons, carbon dioxide, ozone, and mercury. Global warming and climate change are good examples of an environmental controversy in which businesses have lobbied against the severity of EPA regulations dealing with the so-called greenhouse gas emissions.

However, corporations have not always needed to be prodded by regulatory agencies, and there are a number of excellent examples of businesses that engage in proactive environmental responsibility. The term *natural capitalism* has become a catchphrase for a set of management practices that hopes to revolutionize corporate behaviors and make business more energy and material efficient. Natural capital signifies the stock of natural resources and the set of ecological systems found in nature, which provide the context for all living creatures. One principle of natural capitalism suggests that businesses can learn how to be more productive from the way nature operates. For example, "industrial ecology" is an environmental management strategy that prompts businesses to adopt a new business model and function in an environmentally sound manner by mimicking a natural ecosystem so that interdependence between business and the environment takes place, waste is eliminated, and sustainable economic development becomes attainable. Another principle of natural capitalism is that business and society need to be more cognizant of the true value of nature and that "environmental economics" should be practiced so that the costs of "negative externalities" such as pollution are also recognized and included in the price of products.

In addition to this more fundamental approach to the environmental responsibility of business, many corporations have taken the initiative by becoming environmentally friendly through the adoption of "green practices." As part of an environmental management system, green practices have as their main business objectives the reduction of negative environmental impact and an increase in efficiency. In fact, the field of environmental management has become a fairly large industry itself, with consultants, trade associations, and professional groups having emerged to promote best practices in this area and to spread the word about how to implement and be successful in the "greening of the corporation." A short list of the practices included in environmental management systems includes clean air emissions, the elimination of toxic waste, the reduction of solid waste, energy savings, wastewater reduction, and clean water initiatives. Today, almost all major corporations have a functional, high-level executive office dedicated to environmental management and/or compliance with governmental regulations pertaining to the environment.

What efforts in environmental management are beginning to reveal is that people often and mistakenly hold a false dichotomy between business revenues and corporate environmental responsibility. Many organizations are finding, for example, that being aware of the environmental impact of energy use may, at the same time, create energy efficiencies that will have the effect of cost reductions and increased profits. In short, the link between environmental management strategies and competitive advantages is being realized more and more by enlightened organizations. Thus, the business case for sustainable corporate green practices is being made and advanced in many business sectors, and many corporations today qualify as environmentally friendly.

Moreover, in the academic field of business ethics, responsible environmental management has become a central topic in recent years. It has been suggested that corporations need to be mindful of a "triple bottom line." In addition to being fiscally responsible and maintaining a profit—the original notion of the "bottom line"—and being accountable for its social impact, a corporation must also engage in practices that do not degrade the environment. "Doing no harm" is a basic principle in ethics and in the context of environmentalism, and it has been argued that corporations have a primary obligation to society and to a set of stakeholders not to engage in business practices that harm people or the environment. The topic of "environmental justice" is one that has emerged in this regard, and it refers to examples of environmental management decisions made by both corporations and governments that have had a disparate impact on certain sectors of society, especially those who reside in low-income areas.

A less savory aspect of corporate environmental responsibility is that of "greenwashing" (from *green* and *whitewash*). This is a negative label that is given by environmentalists, who see in the practices of a corporation the tendency to use environmental issues as part of their advertising or public relations programs and make it appear that they are engaged in green practices when they actually are not. While there are many corporations that are genuinely concerned with their responsibility toward the environment, there are some others that are willing to take a "free rider" attitude and make claims about their affinity for the environment when their real intention is to capitalize on the environmental concerns of the public.

Radical Environmentalism

Although environmentalism in the United States began in the 19th century with a kind of spiritual appreciation of nature, it evolved into a less serene and respectful scene that today is marked by animosities, "culture wars," and public policy skirmishes. In fact, one faction of environmentalism has become greatly radicalized and has found it necessary to engage in violent destruction of property and other acts of radical protest. According to the Federal Bureau of Investigation, "ecoterrorists," as they have been called, and radical animal rights groups have committed 1,100 criminal acts, resulting in $110 million worth of damage, since 1976. These domestic terrorists are considered to be more dangerous to U.S. interests than any foreign terrorist organization.

Condos and ski lodges have been set ablaze by ecoterrorists, who have also vandalized and burned sports-utility vehicles as a protest against what they saw as threats to the environment. The Earth Liberation Front, a spin-off of Earth First!, and the Animal Liberation Front have been among the most active and well-known radical environmental groups to perform violent acts that damage private property. One highly publicized form of "monkey-wrenching," the preferred term for violent actions perpetrated by Earth First! proponents, was "tree spiking." This act of "ecotage" (sabotage to save the environment) involves the use of long spikes hammered into a tree that has been spotted for harvesting. The next step is to warn loggers not to fell spiked trees because using their chain saws could be injurious or even deadly when the chains hit the spikes and the resulting shrapnel explodes into the air. However, no deaths have ever been attributed to tree spiking, although there has been one severe injury reported in a lumber mill due to the cutting of a spiked tree.

Other well-known groups have also espoused radical environmental messages but have engaged only in nonviolent protests, direct actions, and civil disobedience. Tree sitting as opposed to tree spiking is the preferred direct action for these environmental protestors. Greenpeace and People for the Ethical Treatment of Animals (PETA) are among the most recognized names of organizations that have found civil disobedience and nonviolent direct actions to be useful in getting their messages across to the general public. In its actions against nuclear testing, whaling, and the oil platform at Brent Spar in the Northeast Atlantic, Greenpeace has a long history of acts of civil disobedience. PETA has been widely criticized for its aggressive media campaigns, boycotts, and public demonstrations against corporations that it claims are exploiting animals.

The main argument of those who favor radical environmentalism is that such actions are necessary because public policies dealing with the environment are not currently sufficient and need substantial changes. Radicals hold that environmental regulations and law do not go far enough to protect the environment and that they are not sustainable. Rather, they claim, environmental public policies really favor special corporate interests while at the same time promoting rampant consumerism, which they also see as fostering values that run counter to those of sustainability and environmental protection. As a result, they hold that they have no choice but to partake in actions that may be illegal and violent and that if they don't, then, the environment will have no chance to survive and the planet will be doomed.

—Peter Madsen

See also Anthropocentrism; Biocentrism; Biodiversity; Bioethics; Consumerism; Corporate Ecology; Environmental Ethics; Environmental Protection Agency

(EPA); Environmental Protection Legislation and Regulation; Externalities; Greenhouse Effect; Green Revolution; Green Values; Greenwashing; Instrumental Value; Intrinsic Value; Moral Standing; Natural Capital; Natural Resources; People for the Ethical Treatment of Animals (PETA); Speciesism; Stewardship; Terrorism; United Nations Environment Programme (UNEP); Wilderness

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Environmental Protection Agency (EPA)

The U.S. Environmental Protection Agency (EPA) is a government agency charged with protecting human health and the environment, specifically the air, water, and land. It was originally established by the president and the U.S. Congress in 1970 to promote greater coordination between environmental agencies involved in enforcing the nation's environmental laws. It addressed cleanup and restoration issues that had arisen from decades of uncontrolled and harmful pollution. It was also chartered to develop and enforce policy to ensure future environmental protection and human health. In addition, the EPA was instituted to serve as a funding agency for support of external research to state environmental programs, nonprofit organizations, and educational institutions.

As of 2007, the EPA employs 18,000 individuals. It is headquartered in Washington, D.C., and has 10 regional offices and more than 12 laboratories located throughout the United States. The EPA headquarters houses the offices of the administrator and the executive staff and large programmatic offices. The 10 regional offices serve the local population, agencies, corporations, nonprofit organizations, and other stakeholders to provide information and conduct research and development. The EPA laboratories engage in environmental research and assess conditions to identify, understand, and solve current and future environmental issues.

The EPA serves as a regulatory agency, enforcing environmental laws and developing policy and national standards. It grants authority to states and Indian (North American) tribes for monitoring and compliance. In cases of noncompliance, the EPA has the authority to issue sanctions and enforce mandates to achieve the desired levels of environmental quality. It also works with industries and all levels of government in a wide variety of voluntary pollution prevention programs and energy conservation efforts.

EPA Enactments and Business

There are many enactments that determine how the EPA interfaces with business and society: The most notable are the Clean Air Act of 1970, the Clean Water Act of 1972, and the National Environmental Policy Act of 1970.

The Clean Air Act was enacted by the U.S. Congress in 1970 (as an amended act). It established air quality standards aimed at reducing smog and pollution. This was pivotal legislation, as it reflected the environmental conscientiousness of Americans and brought important issues to the forefront in Congress. Since then, many state and local governments have enacted similar legislation, either applying the regulations of the federal programs or augmenting the local programs that supplement the gaps in federal laws.

Clean Air legislation, whether federal, state, or local, is aimed at improving human health, primarily to reduce respiratory diseases in humans, and at protecting and sustaining the environment.

Through the Clean Air Act, the EPA has set limits on all types of emissions (whether they are from the smokestacks of a refinery or the exhaust pipes of an individual's automobile) through Clean Air Alert programs. Compliance is widespread, and violators are given limited time, if any, to rectify an emissions problem.

For business, upholding EPA air standards is difficult and complex. It is expensive and ongoing, usually requiring an additional financial commitment from the affected company. For example, retrofitting a fossil fuel power plant to comply with EPA standards is costly and time-consuming. And once modifications are made, the local and state standards may be amended to mitigate high levels of pollution, causing further compliance requirements to which industry must adhere. Businesses must incorporate these updated standards into existing operations or they may be subject to sanctions and penalties.

Society is affected by businesses that pollute the air, as human health and the environment are at issue. Humans and the environment are exposed to the pollution that businesses produce, not just within the state in which an individual resides but also in far-reaching locations. For example, in 1986, the plume of radioactive fallout produced by the Chernobyl nuclear power plant disaster in the Ukraine drifted over parts of the former Soviet Union, Europe, Scandinavia, the British Isles, and eastern North America. More than 336,000 people had to be evacuated or resettled. Although the disaster occurred in one country, it was large enough to affect populations across the globe.

The Clean Water Act of 1972 (CWA) established goals for drastically reducing toxic chemical levels in water. Before businesses and individuals release pollutants into navigable water, a permit must be approved and obtained through the quality-based standards set by the CWA. The CWA not only sets discharge limits; it also prohibits harmful spills of hazardous substances and oil. There are technology-based standards, known as effluent guidelines, that are set to enforce a national maximum of hazardous substances, with the goal of creating waters that are safe enough for activities such as fishing and swimming.

Businesses are affected by the CWA in that they must file a permit with the EPA that outlines the details of any waste they consider dumping into most bodies of water. Permits are deemed acceptable or unacceptable. In the case of an unacceptable permit application, the business must modify its plan to accommodate the EPA standards. In the case of a violation, adjustments are usually required before a permit will be issued. Excessive or repeated violations may result in litigious outcomes. For example, in 1989, the oil tanker *Exxon Valdez* ran aground on Bligh Reef in Prince William Sound, Alaska, spilling approximately 11 million gallons of crude oil. The environmental impact was immense, with an estimated 259,000 animals perishing immediately. In the original civil case, an Anchorage jury awarded $900 million in actual damages for restoration and replacement of natural resources and $5 billion for punitive damages. Exxon was also held criminally liable for $150 million. As of the beginning of 2007, the civil case is yet to be settled and resides in the appellate courts. The legal battle wages on as costs have escalated for what is now known as ExxonMobil Corporation, the insurance companies, the federal government, and the many individuals and businesses affected by the disaster.

The National Environmental Policy Act of 1970 addresses the consequences of soil contamination and the associated health risks on any federally funded project. The Resource Conservation and Recovery Act of 1976 and the U.S. Comprehensive Emergency Response Compensation and Liability Act (CERCLA) of 1980 were subsequently passed; they defined guidelines for handling, transporting, and hauling hazardous materials from soil cleanup projects, and they also put in place an infrastructure to identify and clean up specific sites. CERCLA authorized the first "superfund," allocating $1.6 billion to toxic waste cleanup sites. Each of these enactments significantly affected land use and land management practices.

Sources of soil contamination include petroleum, solvent leakage, solid waste disposal, water runoff, pesticides, herbicides, dust from manufacturing facilities, and lead. Areas of concern include any location where human beings have the potential of being in contact with hazardous materials.

Businesses are affected by the National Environmental Policy Act when they make decisions regarding the disposal of hazardous waste. There are few options for disposal that are endorsed by the EPA, so it becomes logistically expensive and complex to find alternatives. Nonetheless, a business must work within the standards to be in compliance.

EPA Compliance Implications

Environmentally conscious firms may strive to meet EPA standards and, in turn, ensure compliance with the requirements. In some cases, a firm may exceed the requirements in an effort to support a cleaner environment and publicly communicate its philosophies on sound environmental stewardship. Other firms may knowingly or unintentionally violate regulations to maintain cost-effectiveness. In extreme cases, some may choose to terminate operations in the United States and offshore them to countries that have lenient standards.

Businesses must decide whether to be accountable to the environment and human health. This implies that businesses possess a commitment to the economy, society, and the environment that demands a broader vision than just profitability and competitive advantage. It calls for a commitment to environmentally sound business practices and a greater level of disclosure.

Some perceive that businesses maintain a singular drive toward profit and will do whatever it takes to maintain and sustain profitability and compete in a global marketplace. Businesses that have this view are known to continually violate EPA standards, buying time to increase profitability while adversely affecting human health and damaging the environment. They contend that the costs outweigh the benefits. Other businesses maintain a strong view that environmental stewardship benefits society and it is an obligation of business to strike a balance between this philosophy and profit margins. These businesses may make a point of being public and visible about environmental stewardship, perhaps publishing an environmental "report card," for example.

Some advocate that an increasing number of consumers are opting to purchase from and work with companies that uphold high environmental standards. These individuals contend that environmentally friendly firms may actually increase profits and stakeholders as consumers make buying decisions based on a firm's philosophies.

It is the businesses' responsibility to make these ethical decisions. Agencies such as the EPA were established by the U.S. government to ensure that a business decides on behalf of the environment and the public good it serves.

—Pamela C. Jones

See also Acid Rain; Advertising Ethics; Chernobyl; Dumping; Environmental Ethics; Environmentalism; Environmental Protection Legislation and Regulation; *Exxon Valdez*; Natural Resources; Pollution; Pollution Right

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Environmental Protection Legislation and Regulation

National and international environmental laws and regulations are relatively new phenomena. For centuries, conflicts over land and water use were resolved at local levels, either informally or in courts of law. But since the Industrial Revolution, increasing numbers of humans, new technologies, and rising levels of consumption have seriously degraded natural resources, have created costly and negative consequences for many, and are even likely to have altered the earth's climate. Acid rain, Love Canal, the wreck of the *Exxon Valdez*, and Bhopal provide well-known examples of business activities that have imposed involuntary costs on others. Degradation of natural resources (depleting fisheries and forests, desertification, ozone depletion, aquifer and wetland losses) is not a new phenomenon, but the pace of consumption, population growth, and new technology has led to many new or contemplated legal restrictions on economic activity.

During the 20th century, economic activity has been particularly intense in the industrialized democracies.

William Rees and others have calculated the "ecological footprint" of various societies that depend on natural capital from beyond their own borders. The European Union (EU) has calculated that its 25 member states represent a declining portion of the world's population, but a rise in per person consumption means that, through global trade, they use an increasing portion of the world's natural resources. Home to 7% of the world's population, the EU nations generate 17% of humanity's ecological footprint. North America (Mexico, the United States, and Canada) generates even larger footprints. A perceived conflict between economic development and environmental protection emerges: If India, China, and other developing nations follow the same upward trend in consumption and generate ever larger demands on natural capital, strains on natural capital are likely.

Severe strains on natural capital can lead to collapse, as Jared Diamond has pointed out in his 2005 book, *Collapse: How Societies Choose to Fail or Succeed*. Because ecological disasters can bring an end to economic activity in that location, it may seem sensible to impose legal limits on the kinds or amounts of consumption or to encourage different technologies or activities. Effective or not, legal attempts to preserve old-growth timber, limit fish catches, or phase out ozone-depleting chemicals exemplify laws intended to avoid ecological degradation and thereby maintain natural capital for current and future generations. But each of these may inhibit profit making in the present. "The market," without governmental interference, is not inclined to place limits on the kinds or amounts of goods that are freely bought and sold; yet setting rational restraints on production, consumption, and inappropriate technologies has proven difficult without market-based rules and incentives.

Enough is known about the nature of corporations, unconstrained markets, and human behavior to conclude that some governance from the public sphere must be in place to protect the environment. Otherwise, chlorofluorocarbons would be freely bought and sold, no one could sue for damages from pollution, and preservation of wilderness would be unthinkable. The more trenchant issue is what kinds of rules and regulations will best serve society and its various constituencies. But we must first consider the meaning of *society and its various constituencies*.

As other entries in this *Encyclopedia* suggest, a biocentric or Deep Ecology perspective would take a broad view of society, rejecting "speciesism" and endorsing animal rights. In so doing, it would reject any public policy analysis that failed to consider nonhuman interests. For example, cost-benefit analyses that excluded nonhuman interests would be morally suspect. Yet as we shall see, most environmental laws and regulations in the United States and in Europe have had a decidedly more "anthropocentric" or human-centered slant. Most environmental laws also primarily aim to serve humans now living rather than provide fairness ("intergenerational equity") to future generations.

Several reasons are commonly offered for having rules that limit human activity in order to protect "the environment." In relatively rare cases, the intrinsic value of nonhuman life is given some weight; the Endangered Species Act or the Marine Mammal Protection Act are examples, along with the international Convention on International Trades in Endangered Species. More typically, cases are decided and statutes legislated to correct various market failures (e.g., negative externalities), secure rights, protect the commons, provide public goods, or provide incentives for technologies that pollute less. As we shall see, sometimes these goals are conflicting, and often there is disagreement about which laws or regulations will provide "better" results. Nuclear energy, for example, avoids carbon dioxide emissions (as greenhouse gas contributors) but creates other problems of safe storage and handling.

In looking at environmental law and regulation, it will be helpful to start first with the judicial decisions that try to balance the rights of individuals or corporations where there are no existing statutes or administrative regulations for the court to interpret. Next, U.S. federal and state statutes and administrative regulations will be discussed, along with the role of U.S. constitutional law. Last, international efforts to protect the environment will be examined and the impact of international trade agreements and institutions such as the North American Free Trade Agreement (NAFTA) and the World Trade Organization (WTO) will be considered.

Regulation Without Legislation: Basic Principles and the Common Law

Under Roman law, property owners were admonished to use their land in ways that did not harm others (*Sic utere tuo ut alienum non laedas:* Use your property in such a manner as not to injure another). English common law and U.S. state tort law require that property owners not create a nuisance on their property; damages are awarded to plaintiffs injured by other owners' negligence. The duty not to harm can also be seen in Principle 21 of the 1972 Stockholm Declaration, where nation-states are supposed to see that activities in their territories do not cause harm to neighboring states.

The underlying economic principle for these laws and principles is that negative externalities should be actively discouraged. In economic parlance, an externality is the cost or benefit of some activity that affects people who aren't directly involved with the activity. An externality can be negative (a new industrial facility can decrease property values of houses in the vicinity) or positive (repainting your house can provide an aesthetic or economic benefit to your neighbors). Pollution externalities are invariably negative; they impose a cost on someone who is not directly involved in the activity. One time-honored business strategy is to use "other people's money"; creating negative externalities in effect does just that. In the absence of legal rules and adequate compensation for the affected parties, the legal system encourages negative externalities and continuing environmental harm.

Common-law tort actions could potentially discourage people and corporations from generating pollution as a kind of negative externality. But tort actions in the United States have not systematically and efficiently encouraged polluters to pay the costs of their pollution to those who suffer harm. For example, in the "toxic tort" trial, made famous in Jonathan Harr's *A Civil Action*, the plaintiff families in Woburn, Massachusetts, were harmed by chemicals that had entered the water supply because of the nearby manufacturing activities of two companies. For some families, the harm was the death of a child. In Harr's account, the families were lucky to find a lawyer to take the case—even with major damages and the corporate defendants having "deep pockets"—because liability was far from clear. The difficulties of proving that trichloroethylene or perchloroethylene had caused the injuries complained of were considerable, as were the difficulties of proving that the chemicals had actually come from the defendants' facilities. The lay jury was overwhelmed by contradictory expert testimony, the statute of limitations cut off the otherwise valid claims of some families, the discovery process was seemingly subverted by one defendant's attorneys, and the plaintiff's small law firm went bankrupt trying to prove its case.

In the Woburn case, as well as other toxic tort cases, scientific uncertainty, multiple potential causes of environmental harm, and the economics of law practice make people's "rights" in their person and property difficult to assert. Moreover, the cost to defendants and to the government (in its Superfund investigation and lawsuit) was considerable; that it would have cost each company just a little to prevent the harm in the first place illustrates the somewhat natural inclination to let someone else pay. The push for maximizing profits may often lead to decisions that emphasize short-term benefits rather than the prevention of long-term costs. *A Civil Action* also illustrates the enormous waste of human time, talent, and money required to redress environmental harms in the courtroom. Because tort actions represent an uncertain and costly means of redressing negative externalities, one role of statutory environmental law is correctly seen as preventing harms by encouraging safer products and processes.

Thus, prevention of the pollution damage in the first place should be a goal for environmental law and regulation. In the United States, the decades of the 1960s and 1970s brought major federal legislation for clean air and clean water, established the Environmental Protection Agency (EPA), and authorized it to set mandatory standards (regulations) for clean air and clean water. Inspections and enforcement of the regulations were part of the preventive process. In the section that follows, we will see that federal legislation is potentially restricted by constitutional mandates. We will also see that states may not legislate without regard to federal legislation and may not legislate in ways that discriminate against "articles of commerce" originating in other states. We will also note that the command and control method of preventive environmental law (involving inspections, administrative adjudication, and enforceable orders against polluters) fell into disfavor; legislation and regulation that were more "market oriented" became more popular, although the use of prohibitions and planning regulations also continued.

In the international arena, more and more multilateral treaties were negotiated and ratified, including agreements on endangered species, the movement of hazardous waste across national boundaries, the depletion of the ozone layer, the protection of Antarctica, prohibitions on persistent organic pollutants, and, most famously, the Kyoto Protocol (implementing the United Nations Framework on Climate Change Convention of 1992). Nations, corporations, and nongovernmental organizations also began to appreciate the difficult interface between "free trade" and a healthy environment. Free trade rules in the General Agreement on Tariffs and Trade (GATT) seemed to favor the unrestricted movement of goods across national boundaries, while environmental groups and interests often favored restrictions on invasive species, limits on genetically modified organisms (GMOs), and the right of GATT member nations to limit the entry of products that had been produced or harvested in ways that posed a danger to particular species or the environment.

U.S. Environmental Laws

Structure of Environmental Law and Regulation

U.S. environmental law begins with state common law, which allows plaintiffs to sue on the basis of nuisance, trespass, or negligence for harms to person or property. States are free to pass environmental legislation, as well, and have historically done so to protect natural resources. At the federal level, Congress passed numerous laws, beginning in 1969, that sought to preserve clean air, land, and water. Congress also created the EPA to write regulations to implement each of the major environmental acts on clean air, clean water, hazardous waste, and chemicals and pesticides. The EPA, after appropriate notice to the public and a comment period, is empowered to issue regulations that have the same force and effect as an act of Congress. The EPA is also empowered to investigate and enforce these laws and regulations. Regulations can be challenged in court on several bases, however, and affected businesses have often been able to modify regulations that seem particularly onerous.

Constitutional Problems

The structure and content of the U.S. Constitution provide numerous issues for the courts to consider.

Commerce Clause

Congressional power in environmental matters derives from the Constitution's commerce clause, which says that Congress "shall have Power . . . to regulate Commerce with foreign nations, and among the several States" (U.S. Constitution, Article I, Section 8 [2]). From the days of Franklin Delano Roosevelt's "New Deal," the Supreme Court has given an expansive reading to the commerce clause; earlier, only laws that touched on the actual movement of goods in interstate commerce were deemed constitutional by the Court. In 1995, the Court withdrew some of Congress's power in ruling that a federal criminal statute prohibiting guns near school districts was beyond Congress's duly authorized powers. Subsequent to 1995, the Court has struck down numerous statutes as exceeding Congress's power under the Constitution.

Limiting congressional power under the commerce clause could limit the scope of the Clean Water Act to interstate waters, thus invalidating efforts to use federal law to protect purely intrastate waters (kettle lakes, canals, streams, ponds, wetlands that do not adjoin navigable interstate waters). Likewise, federal protection for endangered species that now live only in localized areas would be curtailed under restricted commerce clause powers.

Consider the southwestern arroyo toad. The arroyo toad was once found throughout coastal rivers and streams in southern and central California. It hatches in a river or stream and begins to develop in water; as an adult, it lives on land, where it lives on insects (mostly ants) and digs burrows on sandy terraces. The arroyo toad population of California has been drastically reduced over the past 100 years, and it now survives in only 22 small, isolated headwaters. The commerce clause issue is whether Congress, through the Endangered Species Act, can protect the arroyo toad even though it does not move in "channels of interstate commerce" and is not an "article of interstate commerce." In *Rancho Viejo, LLC v. Norton*, the U.S. Court of Appeals for the D.C. Circuit upheld Congress's power to regulate, but Judge (now Justice) Roberts declared in dissent that the developer's "incidental taking" of the arroyo toad could not be a matter of interstate commerce. His views may well represent the Supreme Court's future direction, limiting what Congress can do under its commerce clause powers.

Dormant Commerce Clause

When Congress does not legislate, the Supreme Court will still limit state action using the "dormant commerce clause." States may not overtly discriminate against articles of commerce from other states, nor may they place "undue burdens" on interstate commerce.

Undue burden cases. For state statutes that "regulate evenhandedly" to effectuate a "legitimate local public interest" with effects on interstate commerce that are "only incidental," the Court will assume constitutionality unless "the burden imposed on commerce is clearly excessive in relation to the putative local benefits." Under some interpretations of the dormant commerce clause, state environmental laws that are too burdensome to business may be challenged.

Discrimination cases. If the state statute by its own terms discriminates on the basis of geographical origin, the courts are likely to strike down the statute as contrary to the dormant commerce clause. A Nebraska law requiring the denial of a permit to withdraw and transport water for use in an adjoining state unless that state granted "reciprocal rights" to withdraw and transport water for use in Nebraska was held to be an explicit "barrier to commerce" between the two states. An Oklahoma law banning the transportation of minnows for sale outside the state was struck down despite legitimate local concerns for the conservation and protection of Oklahoma's ecological balance. A slightly greater "tipping fee" at Oregon state landfills for waste originating outside the state was held invalid as facially discriminatory, even though the lower in-state fees were defended on the basis that Oregon taxpayers were already paying for the inspection expenses and the infrastructure that supported the landfills.

Preemption

Congress may choose to create national legislation that will "trump" any state legislation or common law on the same subject. It can do so because of the supremacy clause in the U.S. Constitution, which says that the Constitution "and the Laws of the United States . . . shall be the supreme Law of the Land." Sometimes Congress preempts state law explicitly. For example, in creating the Nuclear Regulatory Authority, Congress made it clear that states would have no role in regulating the radiological safety aspects of constructing and maintaining nuclear power plants or ensuring nuclear safety. Where Congress does not do so explicitly, the courts may still find that Congress implicitly chose to preempt state law and will negate state laws that are in conflict with federal law or "frustrate the purpose of" federal law.

In *United States v. Locke*, for example, the Supreme Court set aside various sections of a Washington State law intended to better protect the waters of Puget Sound from oil spills. While the Court acknowledged that Puget Sound was environmentally significant, with "fisheries and plant and animal life of immense value to the Nation and to the world," it nevertheless found that the state's Office of Marine Safety had issued regulations that were preempted by existing federal statutes governing tankers, ports and waterway safety, and oil pollution. Washington regulations had imposed a strict training regimen on oil tanker crews, including oil spill prevention and response; the state laws mandated weekly, monthly, and quarterly drills. A trade association representing operators of oil tanker ships challenged the state regulations, and the U.S. government joined in the challenge, arguing that national and international rules for tanker navigation were essential to orderly trade and commerce and that inconsistent state and local rules should be preempted. The Court agreed.

Express or implied federal preemption may not always be so clear, however, and business interests have often found it useful to argue preemption where state environmental standards are stricter than federal ones. California's clean air laws, for example, are stricter than the federal standards and now require automakers to reduce carbon dioxide emissions from motor vehicles. Automakers argue that the federal Corporate Average Fuel Economy Standards (CAFE) expressly and impliedly preempt state legislation that would require CO_2 emission standards. The reasoning is that only enhanced fuel economy can deliver lower CO_2 emissions and that fuel economy is governed by the federal CAFE law. A challenge to those stricter state standards using preemption is pending.

Command and Control Regulations

The initial burst of federal environmental legislation in the 1970s typified what is known as command and control regulation, sometimes known as "direct regulation." From 1960 to 1979, 27 laws were passed to improve air, water, and land quality. Congress set the broader purposes and goals, and the EPA was charged with writing more detailed regulations to implement the statute. Typically, the laws and regulations aimed at controlling pollutants toward the end of the manufacturing process. The Clean Water Act and Clean Air Act were prime examples; standards were set in terms of total effluents or emissions allowed, and varied levels of technology were prescribed (e.g., "best available technology" or "best feasible technology"). Noncompliance by individuals or companies could result in civil and/or criminal penalties. The states were given an enforcement role; as long as states adequately enforced the EPA regulations, the EPA would not monitor compliance or bring enforcement actions.

The Reagan era (1980–1988) represented a reaction to command and control regulations, as businesses began to realize the high cost of complying with environmental regulations. Deregulation in this era at the EPA meant staff reductions, budget cuts, and reduced funding for renewable energy. Congress strengthened some environmental laws during the 1980s, however, and the first Bush administration's EPA brought a record number of prosecutions and fines for environmental violations. In 1990, a strengthened Clean Air Act was signed into law.

Still, resistance to command and control regulations by the business community was strong. The initial reductions in effluents and emissions had been fairly cost-effective; further efforts to reduce pollution were more costly and delivered more marginal benefits. Economic concerns surfaced, for instance, with the Competitiveness Council, which was instituted during the first Bush administration on behalf of business to ensure that all federal regulations would not cost business more than the benefits provided to society. Concerns over the economy would result in a shift from command and control regulation to laws oriented toward "market forces."

Incentive Regulations

Legislation oriented toward market forces began to play a greater role in the 1990s and beyond. The Clean Air Act amendments of 1990, for example, included emissions trading provisions that gave the most efficient manufacturers an incentive to not only meet standards but also exceed them. Excess "credits" could be sold to facilities that for financial reasons could not immediately comply with emission standards. Critics have described emissions-swapping programs as licenses to pollute; others note that while overall emissions of a certain pollutant (e.g., mercury) may be more quickly and efficiently lowered by means of emissions trading, "hot spots" are created around sources that are buying emissions credits, to the detriment of nearby residents.

Market-oriented regulations include pollution taxes, refundable deposits on hazardous materials, and bottle bills that encourage consumers to recycle. Such regulations also include tax incentives for consumers to purchase hybrid vehicles and for making investments in solar energy for their homes. All the above are "market oriented" because they impose costs on goods that impose negative externalities and confer benefits on the purchase of products that contribute to a better environment. For example, without a returnable cans and bottle rule, the typical soft-drink container is less likely to be recycled and more likely to create roadside litter for someone else to deal with. Without public encouragement of consumer purchase of solar energy panels, for example, the nascent solar energy industry cannot compete with oil for home heating when oil exploration and distribution are already given public assistance by federal tax law provisions and an overseas military presence that has historically served to secure oil supplies from abroad.

Other market-oriented regulations would include labeling laws that require products to include information to environment-minded consumers. The presence of labels claiming that "no animal testing has been done in the preparation of this product" attests to the growing influence of consumers who ask to know how a product is made. The regulation of the words *organic* and *natural* as labels represents an attempt to pin down the meaning of words that are important to a growing number of consumers. The underlying market logic comes from economics and from the basic tenet that buyers and sellers should have the best possible information for the market to function well.

Prohibitions and Planning Regulations

The tension between individual property rights and the collective good is well illustrated by zoning and planning laws. Under most state laws, local governments are allowed to restrict certain businesses to specific locations; noise, offensive odors, or unsightliness are widely held reasons for municipalities to impose zoning restrictions. Permits represent another form of planning regulation. Under federal law, a permit may be required to engage in mining or timbering or to create an office park or residential development. For example, the Army Corps of Engineers has historically enforced a migratory bird rule that has prevented filling in certain seasonal wetlands used by migrating species. If a species is protected as endangered under the Endangered Species Act, the permit for development may be refused. Finally, the sale of some items may be entirely prohibited if doing so seems prudent and rational; for example, to discourage the poaching and commercial sale of eagle feathers, the sale of eagle feathers can be outlawed, even though someone could show that they had found some eagle feathers without harming an eagle. In general, the courts have held that governments and their agencies are empowered to create prohibitions, set the terms for permits, and create zoning and use areas for the good of society.

Yet sometimes, planning efforts may run afoul of constitutional considerations. In *South Carolina Coastal Commission v. Lucas* (Supreme Court, 1992), the Commission studied beach erosion and storm flooding and concluded that oceanfront residences should be restricted. David Lucas had purchased two beachfront lots in 1986, intending to build houses on them. At the time, the state did not list his properties as being in a "critical area" that would require a permit for development. In 1988, the legislature's newly enacted Beachfront Management Act prohibited him from building residential structures on his lots. While there were defensible reasons for the act (preventing beach erosion mitigates storm damage, provides a habitat for numerous species of plants and animals, serves as a storm barrier that dissipates wave energy and contributes to shoreline stability in an economical and efficient manner, and helps maintain a vibrant tourism industry for South Carolina), the effect of the law was to deny him all "economically viable use of his land." In doing so, the Court held that the state law had effected a "total taking" and required the state to pay Lucas the full price he had paid for his two lots.

Following *Lucas*, then, a total taking will require the government to pay for the loss of "all economic value" due to regulation. The decision left open whether "partial takings" should also be compensable. In the wake of *Lucas*, a movement to require government to pay for "regulatory takings" has achieved some traction in the United States. A broad range of economic and political interests, including developers, small-property owners, timber companies, and others, have championed "property rights" to balance the growing government interference to protect the environment. The basic argument is that environmental regulations are trampling on the rights of private property owners, who know best how to act as stewards of the land in any case. Creation of new wilderness areas is strongly opposed by the "wise-use" movement, which would like to legislate an owner's right to payment for any reduced economic value due to environmental rules. Thus, the regulatory takings doctrine would go well beyond the *Lucas* case and require compensation for partial as well as total regulatory takings.

Proponents of takings legislation claim that it will relieve small-property owners, who are unduly restricted by wetlands ordinances, growth management laws, and other environmental statutes. Granted that government regulations may often generate strange and burdensome requirements, these claims may have considerable appeal. On the other hand, "property" consists of not only land (real property) but also personal property (cash and all other assets that may be bought and sold). Taken to its logical limit, then, all government regulations that diminished personal or corporate property would require payment to the extent of the diminished value. Thus, under the regulatory takings doctrine, prohibiting negative externalities such as pollution of air, land, and water would require the public (not the polluter) to pay the cost of pollution prevention. Regulatory takings advocates would counter that those whose property or health has been adversely affected could bring litigation to enforce their own rights; but, as we have seen, using courts to assert tort claims of negligence, trespass, or nuisance is an inefficient and uncertain remedy, with large transaction costs (see Regulation Without Legislation).

Several states have enacted some form of takings legislation since the early 1990s, and as of 2005, a number of new takings bills have been introduced. Takings legislation at the state level has one or both of the following components: assessment provisions (requiring governments to prepare a written assessment of whether a proposed action would constitute a "taking" of private property) and compensation provisions (requiring governments to compensate landowners for diminutions in property value that reach a certain threshold percentage). For example, the Real Property Rights Preservation Act became Texas law in 1995 and defines a taking as a government action that causes a "reduction of at least 25 percent of the market value of the affected private real property." Various bills have been introduced at the federal level, but none have passed both the House and the Senate.

Takings legislation has its counterpart internationally; the North American Free Trade Agreement's Article 1110 provides investor protection against measures "tantamount to nationalization or expropriation" of investments. This would be equivalent to a government's use of eminent domain in its own territory. But Chapter 11 of NAFTA also protects investors against the "measures" of a signatory foreign government relating to the "investment," and many claims have been brought by individuals and corporations against governments whose laws or regulations, either local or national, have adversely affected their financial situation. Moreover, some have been compensated through Chapter 11 arbitral tribunals even when the "taking" was a denial of a permit, an administrative determination, or a judicial decree.

International Aspects

International Environmental Law

There is a considerable body of "international environmental law" covering varied issues such as climate change, ozone depletion, movement of hazardous waste, endangered species, and maritime pollution. The efficacy of these various treaties and conventions varies, as each nation in the international order retains its sovereignty (i.e., the power to make and enforce laws within its own borders), and participation in such agreements is essentially voluntary.

The classic formulation of sovereign responsibility for transboundary pollution dates back (at least) to Principle 21 of the Stockholm Declaration from the 1972 United Nations Conference on the Human Environment. Principle 21 noted that states have the sovereign right to exploit their own resources pursuant to their own environmental policies and the responsibility to ensure that activities within their jurisdiction or control do not cause damage to the environment of other states or of areas beyond the limits of national jurisdiction. Principle 21 is consistent with the Roman law maxim discussed earlier, but those who are damaged by governmental transboundary pollution will be hard-pressed to recover; sovereign immunity is ordinarily granted by national court systems to governments for actions taken on their own territories. Nations might agree to hear transboundary pollution claims or other matters involving the environment in the International Court of Justice (see, e.g., The Hungary-Slovakia Danube River dispute, September 25, 1997), but participation is voluntary.

International Treaties and Conventions

Each nation-state can bind itself to agreements with other nation-states through treaties and conventions. A treaty is an agreement between two nations, and a convention or protocol usually connotes an agreement among a larger group of nations. Whether a nation signs a treaty or is a party to a convention, the agreement is voluntary; at any time, a nation that has ratified an agreement can also resign from that agreement.

There are many notable international environmental agreements, including the Montreal Protocol on Substances That Deplete the Ozone Layer, the Basel Convention on the Control of Transboundary Movements of Hazardous Wastes and Their Disposal, and the Kyoto Protocol, which sets national targets for certain kinds of greenhouse gas emissions. Given the extensive fossil fuel use in the United States, the decision by U.S. political leaders not to join the Protocol has been unpopular in many parts of the world. U.S. nonparticipation also illustrates the conflict between short-term economic goals and strategies for long-term sustainability. Also, even if the United States were to join the Protocol, economic exigencies could lead to a renunciation of the Protocol's voluntary commitments.

Trade Agreements: WTO and NAFTA

A more binding set of agreements can be found in global and regional trade agreements. Globalization of trade and commerce has strengthened the role of international institutions such as the WTO. Prior to the Uruguay Round of trade negotiations, global trading nations subscribed to the GATT. Under the GATT, tariff and nontariff barriers were to be gradually reduced, increasing free trade and global prosperity (under David Ricardo's theory of comparative advantage). While the GATT did include allowances for sovereign action to protect environmental resources within its borders (in Article XX[g]), it did not allow nations to take actions that would discriminate against products based on the way the product was created or taken from the environment. For example, the U.S. Marine Mammal Protection Act (MMPA) put limits on the import of tunas caught using purse seine nets, which injured and killed dolphins in the Eastern Tropical Pacific. A GATT panel rejected the U.S. restrictions on the ground that Article XX(g) could only apply to domestic environmental protection and that discriminatory treatment in terms of tariffs or quotas could not be based on the production or processing methods of "like articles." Given that tunas caught with dolphin-friendly methods were identical to tunas caught with purse seine nets, the MMPA limits were ruled to be inconsistent with U.S. GATT obligations.

Other environmentally inspired restrictions have also faced challenges in the WTO. The EU's refusal to accept GMOs was challenged by the United States in a WTO dispute resolution panel, as were the EU's restrictions on hormone-fed beef. U.S. companies were the primary drivers of these challenges, which were successful in using free trade laws to invalidate the precautionary measures adopted by the EU. In these decisions, and in others, the WTO must wrestle with the precautionary principle, which is found in (among other places) the 1992 Rio Declaration on Environment and Development. The precautionary principle has had various formulations, but in essence it holds that where there are threats of serious or irreversible damage, lack of full scientific certainty should not be used as a reason for postponing cost-effective measures to prevent environmental degradation.

WTO disputes about precautionary measures usually center on risk assessment and the scientific validity of potential risks. In the cases involving GMOs, hormone-fed beef, and other products (the Japan Apples case and the Australian Salmon case), the burden of proof is on the regulating nations to demonstrate the risk by means of fairly rigorous scientific evidence or an existing international standard. For developing countries, this burden is significant.

The 1993 NAFTA was the first trade agreement to specifically mention environmental considerations. An environmental "side agreement" created the North American Agreement on Environmental Cooperation and a strengthened binational process for environmental cooperation and protection along the border. But these institutions appear insufficient to arrest the pressures on the environment resulting from economic integration in the North American region.

Environmentalists had opposed the agreement because they feared that further trade liberalization between the United States and Mexico would worsen the already poor environmental conditions along the U.S.-Mexican border, a border contaminated by excessive air pollution, sewage discharges, and toxic dumping. Also, environmentalists feared that NAFTA could be used to attack state or national environmental standards as barriers to trade.

At least some of those fears have been borne out. Chapter 11 of NAFTA provides for significant investor protections. If a company from any of the three nations makes an investment in another nation and the investment is impaired in any way by the laws or acts of that nation, an arbitration panel can be convened at the investor's request. One arbitration has given a substantial award to a U.S. corporation whose waste facility was disapproved by local authorities; the denial of the permit may have been a politically motivated event, but there were some legitimate environmental concerns about the facility (*Metalclad v. Mexico*). A Canadian corporation (Methanex) has challenged California's ban of MBTE, claiming that the ban was politically inspired rather than environmentally motivated; the proceedings to date make it unlikely that Methanex will recover, but the company's ability to use the investor protection provisions of NAFTA's Chapter 11 make it clear that challenges to environmental laws are likely under NAFTA's investor protection provisions.

Threats to Developing International Environmental Law

Developing more effective international environmental law treaties and conventions depends, in part, on economic and political stability among nation-states generally. Economic and political stability is currently being threatened by numerous civil wars, terrorism, and the wide dispersion of military hardware. The phenomenon of "failed states" threatens to undermine cooperation between nation-states on critical international environmental issues. Uneven development within nation-states—not merely poverty—increases instability. Corrupt and ineffective governments can also give rise to opposition parties, warlords, ethnic nationalists, and rebel forces. Environmental degradation in one nation can lead to displaced refugees.

With all these potential difficulties, it is useful to recall that people worldwide want to live with healthy air, clean water, and uncontaminated land. Humanity has only recently come to realize that there are environmental harms inherent in overpopulation, overconsumption, and the indiscriminate adoption of new technologies. Businesses have also begun to realize that the economic system is not independent of natural capital and that preserving the goods of life as we know them will require intelligent shared sacrifices within a framework of sound environmental laws and regulation.

—Don Mayer

See also Acid Rain; Animal Rights Movement; Bhopal; Biocentrism; Coalition for Environmentally Responsible Economies (CERES); Corporate Average Fuel Economy (CAFE) Standards; Cost-Benefit Analysis; Deep Ecology; Emissions Trading; *Exxon Valdez*; Gaia

Hypothesis; Greenhouse Effect; Intergenerational Equity; Kyoto Protocol; Love Canal; Natural Capital; Nuclear Power; Ozone Depletion; Perfect Markets and Market Imperfections; Pollution Externalities, Socially Efficient Regulation of; Population Growth; Recycling; Rocky Flats; Speciesism; Tragedy of the Commons

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Envy-Free Theory

Envy-free theory addresses the dilemma of allocating scarce resources through the use of complex mathematical formulae so that each individual believes that his or her share is equal to or better than that of anyone else who takes part in this resource sharing. The purpose of devising these mathematical formulae is to reduce or eliminate the envy that one individual may feel against another after the resource in question is allocated.

Over the past 50 years, mathematicians have developed several theories on how to fairly distribute scarce resources and have used the cutting of a cake to represent these devised formulae. Curiously, the application of envy-free theory dates back to more than 2,800 years ago. In his literary work *Theogeny*, Hesiod cited an example in which Zeus and Prometheus killed an ox, which had to be divided between them. Prometheus cut the ox in half but hid the tender portion under the hide of the ox to make it appear unappealing, with the result that Zeus selected the inferior, bony portion, which enraged him. This unsuccessful "cut and choose" method led to more arduous attempts to create quantitatively based, envy-free theories so that when one party cut the symbolic meat in half and the other party chose his or her half, they both would be satisfied. However, it was not until the 1940s that mathematicians such as Hugo Stenhaus questioned whether an envy-free theory could be developed for application to more than two persons.

Following Stenhaus, several mathematical methods were devised to create an envy-free division of resources for more than two individuals. One of these envy-free theorists, William Webb, combined his theory with several others.

In Webb's method, three pieces of a rectangular cake are distributed. The first person places his knife at the left edge of the cake and is instructed by the second person when to cut it, as the knife is moved to the right. The second person now believes that this cut piece is equal to one third of the entire cake and it is his or her turn to cut the cake. The second person is then told by the first person when to cut the slice. At this point, the first and second persons believe that all cut slices are equal. Now the pieces of cake are to be distributed and are selected in order: first by the third person, next by the second person, and last by the first person.

The distribution of the cake is now envy free because all three persons believe that their choice is equal to or better than the choices of the others. This method is actually mirrored in John Rawls's "difference theory," which supports any action if the least advantaged party believes that he or she is in a better situation than before. Some of the situations where an envy-free theory may be applied include heirs inheriting an estate, employees splitting a list of duties, parties in a divorce mediation, or students renting a house together.

—Martin J. Lecker

See also Economic Efficiency; Equality; Equilibrium; Fairness; Justice, Distributive; Rawls, John; Resource Allocation

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Equal Employment Opportunity

This entry describes and explains the body of legislation and public policy known as equal employment opportunity (EEO). To best understand this complex and multifaceted set of issues, four main topics will be discussed: (1) definition of EEO, (2) the rationale and history behind EEO, (3) EEO and the Equal Employment Opportunity Commission (EEOC), and (4) EEO problems.

EEO Defined

EEO is employment practice that doesn't discriminate against applicants because of race, age, color, religion, sex, or national origin. The Civil Rights Act of 1964 proposed by John F. Kennedy (who was assassinated before he could see it passed) helped establish EEO. The Civil Rights Act of 1964 made racial discrimination in public places illegal, and it established the infrastructure and platform for EEO. Executive Order 11246, signed by Lyndon B. Johnson on September 24, 1965, required EEO. The order was a follow-up to Executive Order 10479, signed by President Dwight Eisenhower on August 13, 1953, establishing the antidiscrimination Committee on Government Contracts.

U.S. civilian employees, applicants, or former employees may file a complaint if they believe that they have been discriminated against in an employment matter on one or more bases of race, color, religion, national origin, sex (including sexual harassment), age (over 40), and disability (mental or physical). The workplace is supposed to be free of discrimination and offer equal opportunity for all.

The Rationale and History Behind EEO

There were many events that led to the establishment of EEO. The first presidential action ever taken against employment discrimination by private employers holding government contracts was Executive Order 8802, signed by President Franklin D. Roosevelt (FDR). It prohibited government contractors from engaging in employment discrimination based on race, color, or national origin. FDR signed this order in June 1941, on the eve of World War II, primarily to ensure that there would be no strikes or demonstrations disrupting the manufacture of military weapons as the country prepared for war.

In July 1948, President Harry S. Truman signed Executive Order 9981. The order required "equality of treatment and opportunity for all persons in the armed services without regard to race, color, religion or national origin." In December 1955, Rosa Parks, an African American woman, refused to give up her seat to a white man on the municipal bus in Montgomery, Alabama. She was arrested and charged with disturbing the peace. The arrest prompted a group of black citizens led by Dr. Martin Luther King Jr. to boycott the public bus system for 1 day, which resulted in a yearlong strike against the Montgomery public bus system. The boycott was successful and caused the desegregation of the Montgomery bus system.

School desegregation was a substantial challenge. In 1957, President Dwight D. Eisenhower had to send federal troops to Little Rock Central High School in Little Rock, Arkansas. Nine black students had been threatened by an angry white mob that opposed desegregation of public schools.

In March 1961, President Kennedy signed Executive Order 10925, prohibiting federal government contractors from discriminating on account of race and establishing the President's Committee on Equal Employment Opportunity. President Kennedy stated that this would help end job discrimination once and for all. In 1963, Congress passed the Equal Pay Act of 1963. This protected men and women who could perform equal work in the same environment from sex-based wage discrimination. The Equal Pay Act was the first civil rights legislation that focused on employment discrimination.

Also in 1963, approximately 250,000 American citizens of all races marched to Washington, D.C., for racial equality and justice. It was later called the March on Washington. The gathering was large but peaceful, and it assembled in front of the Lincoln Memorial, where the crowd heard Dr. Martin Luther King Jr.'s famous "I Have a Dream" speech. This was the largest demonstration in the country's history up to then.

Nearly 1 year later, after the longest debate in its 180-year history, Congress completed the Civil Rights Act of 1964 on June 19. The vote in favor of the bill was 73 to 27. On July 2, Congress officially passed the bill, and Lyndon B. Johnson signed the bill into law that same night. There were 500 amendments to the bill, and Congress debated on it for 538 hours. The Civil Rights Act prohibits discrimination on a broad spectrum of rights, including public accommodations, governmental services, and education. Title VII, a section of the act, prohibits discrimination based on race, sex, religion, and national origin. Title VII applies to private employers, labor unions, and employment agencies. The title became "the law of the land." The act prohibits discrimination in almost every aspect of employment, including recruitment, hiring, wages, assignment, promotion, benefits, discipline, discharge, and layoffs.

This title also created the EEOC. The EEOC opened its doors for business on July 2, 1965. The EEOC is a five-member bipartisan commission, whose job is to eliminate unlawful employment discrimination. The EEOC's primary responsibility is to receive and investigate charges of discrimination in the workplace. If it believes that the accusation is true, then it will attempt to negotiate a voluntary settlement.

EEO and EEOC

EEO disallows discrimination in employment based on race, color, disability, sex, religion, minority status, or national origin. EEO can affect anyone at any time and place where there is employment. The agency with jurisdiction over discrimination issues is the EEOC. The EEOC works to promote equity in employment practices and increase employment opportunities for those who suffer from employment discrimination problems. The EEOC investigates discrimination allegations through 50 field offices and determines when there has been employment discrimination. The agency is also responsible for reconciling organizations and employees, and in more serious cases, it is responsible for filing lawsuits. This commission is intended to provide support, assistance, and advice to management teams and their EEO programs.

The Civil Rights Act of 1964 protects people against employment discrimination based on race and color. EEO cannot be denied to any person because of his or her racial group or race-linked traits. EEO also cannot be denied to any person who is married to or resides with someone of a different color. The Civil Rights Act states that it is unlawful and unethical to discriminate on the basis of race and color regarding recruiting, hiring, wages and benefits, or promotions.

The EEOC supports five laws that protect people with disabilities. These five legislative acts were all meant to help reduce discrimination in employment for those with lifelong disabilities. These laws include the Americans with Disabilities Act (ADA), the Rehabilitation Act, the Workforce Investment Act, the Vietnam Era Veterans' Readjustment Assistance Act, and the Civil Service Reform Act. Most people with disabilities use the ADA. This law criminalizes discrimination again people with disabilities and promises equal job opportunities in employment as well as state and local government services. The ADA forbids employers from rejecting people with disabilities in everything from hiring to pay and benefits to promotions. Together, these five laws combine to help prevent and eliminate employment discrimination against individuals with disabilities.

EEO Issues

One major controversy confronting the EEOC concerned the pay of people who are victimized by discrimination. Generally, the minimum wage is a disadvantage to many minority groups and those who immigrate into the United States from other countries. Creating a minimum wage in the United States was intended to allow unskilled workers to earn enough money so that their families would not be in poverty.

However, it is alleged that the minimum wage has caused more unemployment of unskilled workers and that more teenagers are being employed because of the low pay. This was an important controversy for the EEOC because most of the people who receive the minimum wage feel that they are poorly compensated and rarely appreciated for their hard work. Although numerous nations such as the United States support the minimum wage, some argue that it causes inflation and unemployment, therefore not helping the poorest workers and slowing down economic growth.

A second controversy involved the male and female wage gap, or gender pay differential. Since the Equal Pay Act in 1963, the gap between women's and men's wages has decreased and narrowed; however, there still is a wage gap that has not been totally explained. Some evidence indicates that the law of supply and demand operating through the labor market was the main reason for this gap. However, many women argue that one explanation for this difference is gender preference. There is also the issue of comparable worth. Women point out that women are disproportionately represented in low-paying occupations such as primary school teaching, nursing, and social work. Yet it is argued these occupations require the same skills and qualifications as the higher-paying occupations dominated by men. Thus, gender discrimination in pay will end only when all persons in occupations with similar requirements get roughly equal pay.

Another basis of discrimination in employment is religion. Title VII of the Civil Rights Act of 1964 does not allow employers to discriminate on any terms of employment against people because of their religion. Employers cannot treat employees better or worse because of their religious beliefs and practices. Also, to make the workplace equal, employees cannot be forced to practice a religious activity as a form of employment. The EEOC monitors company compliance to prevent any discrimination involving religious practices by ensuring that employers do not place restrictions on religious expression. The need to avoid religious harassment has been emphasized by the EEOC, which also helps employers become accustomed to employees' legally guaranteed religious practices.

Some religious practices might interfere with the normal conduct of business. What if a Muslim must stop and pray five times a day during working hours? Can employees refuse to work on their religious holidays if they are needed by their employer at that time? These and similar vexing questions make reconciliation of employees' rights of religion and employers' right to require worker presence a difficult matter.

Excluded groups might constitute a final concern with regard to EEO. For instance, neither age discrimination nor sexual orientation is covered by EEO. On occasion, discrimination has been alleged by both extremes in the labor force, the youngest and the oldest. Gay and lesbian rights and privileges are not guaranteed or even recognized in EEO.

—Dirk C. Gibson, Christa Martinez, and Angelica Garcia

See also Age Discrimination; Americans with Disabilities Act of 1990 (ADA); Civil Rights; Employment Discrimination; Equal Opportunity; Equal Pay Act of 1963; Just Wage; Minimum Wage; Racial Discrimination

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Equality

Equality is a fundamental concept in the modern political lexicon, drawn from a philosophical presumption of the equal worth of human beings regardless of their endowments, attributes, or socioeconomic worth. Equality is defined legally as equal-standing rights and responsibilities of individuals under the law, and it is understood politically as equal rights of participation in the process of government. The etymology of equality (Greek, *isotes*; Latin, *aequitas, aequalitas*) suggests qualities of correspondence and proportional value, wherein two or more distinct entities may be related or referenced to one another in certain ways, more than sameness or identical likeness, wherein two entities are indistinguishable from one another. Assertions of equality do not presume undifferentiated identity.

The concept of equality has long been recognized as fundamentally problematic. Factually, it is readily observable that people are unequally endowed with gifts and liabilities. In what respects are human beings equal? In what respects are they different and unequal? Why should people of different intelligence, character, and abilities be considered equal? If people are unique and different, what is the basis of their equality? Or is equality simply an abstract assertion of human dignity with no particular requirement for measuring material or social consequences? This entry traces the development of equality as a concept in political, economic, and distributive justice theory and then examines the concept of equality as applied to economic justice.

Equality: An Evolving Concept

The basic notion of human equality has deep roots in Western thought, although the assertion of universal moral, political, social, and economic claims based on equality is clearly a product of modernity. Even in modern times, those vigorously asserting the principle of human equality have questioned whether factors such as gender, social class, race, ethnicity, or religion should disqualify consideration of a person as human. The theoretical grounds for asserting human equality have evolved in a struggle to define and rationalize the constitutive elements of a common humanity in light of inescapable evidence of difference. In light of these differences, why should humans be considered equal?

Until modern times, human inequality and social stratification were understood as an irrefutable expression of an ontological hierarchy or divinely ordained chain of being. In a narrowly drawn universe of full human beings, contrasted with barbarians and other lesser creatures, Greek philosophers considered the reflective search for wisdom as the essential and universal element of human equality. Capacities of the soul were the factual and normative basis for some measure of equality among persons. Aristotle asserted the basic equality of persons in *Nicomachean Ethics*, declaring that because all humans are endowed with a rational soul to cultivate the path of virtue, all are therefore capable of happiness.

In the Christian era, theories of human equality emphasized the commonality of all people as creatures made in the image of God. In integrating classic Aristotelian philosophy with Christian theology, Aquinas distinguished between "natural law," accessible to all human beings through observation and reason, and the "revealed law" of religious texts and traditions, reframing Christian thought to accommodate both reason and revelation as complementary pathways to God. While early modern theorists continued to argue for some measure of human equality on both rational and theological grounds, a persistent tension between reason and revelation can be observed in the development of divergent theories of equality based either on religious cosmology or on the empirical observation of human nature. It was Descartes who tipped the balance of Western thought by placing human experience at the center of inquiry and meaning. While Descartes himself did not reject the existence of God, his *homo cogitens* became the model of the rational humanism that dominated Western philosophy until the 20th century. This radical positioning of humanity as the measure of its own meaning opened the door to exploration of the full implications of human equality beyond the boundaries of received human hierarchies.

Political Equality

The primacy of the political dimension in modern Western notions of equality is rooted in centuries of struggle as Europe evolved from the feudal domains of lords and subjects to modern nation-states of citizens and elected leaders. Theories of the human person, human communities, government, and the natural order were paramount in establishing an intellectual foundation for claiming universal political rights and freedoms based on equality. While classical philosophy and traditional religions provided some foundation for a theory of human equality, they also were embedded in a stratified view of the political, social, and economic order, which was increasingly perceived as onerous and oppressive. Before the modern era, political equality among citizens was considered to be a different issue from the intrinsic equality of persons. Both classical Athens and republican Rome developed limited theories of political equality, and elements of classical theory remain in modern political thought. The Athenian city-state and the Roman Republic exemplified some practices of political equality, although the political order of both was destroyed by a combination of class warfare and external threats that resulted in the emergence of imperial regimes. Plato and Aristotle distinguished between political equality and other forms of equality; both were advocates of equal treatment among equals, but both also believed that people should be rewarded according to their merit.

As post-Cartesians reflected on their received political hierarchies, they sought an alternative to the divine right theory to explain their origins and provide reasons to justify the claims of government for obedience from citizens and the duty of rational people to submit to the authority of government. The concept of a social contract gained traction as a humanist explanation for a stratified social order. In a rather pessimistic view of the human condition, Hobbes theorized in *Leviathan* a "covenant" wherein human beings at some point in time relinquished their natural freedom in exchange for the social benefits of orderly government. Believing that the natural selfish desire of human beings was to pursue their own interests at the expense of others, thus rendering them incapable of cooperation in building a peaceful society, Hobbes justified absolute rule as a necessary remedy that could not be altered. While this explanation did not assert claims of equality, the theory of civic authority and citizenship outlined in *Leviathan* posited the absolute authority of government on the humanist grounds of an original condition of social consent.

Locke is often seen as a turning point in the development of modern theories of political equality in establishing consent of the governed and toleration of diverse religious conscience as the principles for legitimate government. Locke grounded his theory of human equality in the human capacity for rational understanding in which people seek to fulfill two basic and universal drives well established by Descartes and Hobbes: (1) to know and understand their experience of the world and (2) to live as part of a peaceful and orderly society. From this position, Locke argued in his *Treatises on Government* that freedom and equality were the natural human condition from which individuals come together in forming a social contract of governance. Directly challenging the absolutism of Hobbes, Locke did not believe that the condition of original consent was irrevocable, reasoning that all people, including rulers, are constrained by the law of nature and that any powers of rule bestowed for the common good can be revoked if the governed lose faith in their governors.

In contrast with Hobbes, Rousseau argued in his *Second Discourse* that the natural human condition is one of freedom and happiness; in his view, it is society, with its laws and restrictions, that transforms the "noble savage" into an unnatural social condition of vice, manipulation, and disharmony. Rousseau did not, however, view human beings as equal but observed two types of inequality: the natural inequalities of age, health, physical traits, and attributes of character and the political inequalities created by human convention. In *The Social Contract,* Rousseau advocated a return to the natural state of nature in which individuals collectively exercised their political will in pursuing the common good and respecting individual freedoms. Social contract theories implicitly ground human equality in their recognition of individual rights and freedoms.

The concept of political equality has had a lasting impact on Western government. It is well known that Lockean principles of equality, freedom, and governance by consent were incorporated into the charters of new governments later established as the United States of America and the Republic of France. The charters and constitutions of modern democracies include explicit declarations of human equality as a justification for self-governance. For example, the U.S. Declaration of Independence asserts that the equality of persons is "self-evident." Article I of the French Declaration of the Rights of Citizens declares that human beings are born to enjoy freedom and equality of rights. The Preamble of the more recent UN Universal Declaration of Human Rights begins with a recognition of the "inherent dignity" and "equal and inalienable rights" of "all members of the human family."

Moral Equality

In formulating a secular foundation for equal moral worth among human beings as an unconditional metaphysical equality free from contingencies of fact, Kant has had a profound impact on the understanding of human equality. A rigorously unconditional assertion of human worth framed his categorical prohibition of all instrumental actions that would treat persons as means rather than ends in themselves. In positing the intrinsic value of the human person as the end of his or her own good rather than the instrumental means of another's good, Kant gave depth and substance to claims of political and social equality. The concept of unique moral worth established a humanist basis for attendant human rights, with lasting influence on the development of modern theories of equality.

The Kantian assertion of human equality as equal moral worth established the moral claim of the individual on society, with concomitant duties of equal protection of rights and freedoms. Following Kant, later humanists grounded arguments for equality in the assumption of unique moral worth, entitling individuals to the social, legal, and economic protection of rights and freedoms in upholding their personal dignity. Utilitarianism, for example, is based on presumptions of the equal value of human beings. The concept of maximizing utility achieves distributive justice by treating equally every person's right to the good. Therefore, what is good for the greatest number, regardless of political role or social status, is seen as the greatest good. While utilitarianism fails to account well for minority interests, it is a powerful force in the institutions and social policies of modern democratic states.

Williams outlined the fundamental considerations of equality as common humanity, moral capacities, and equality in unequal circumstances. He pointed to the "desire for self-respect" as the deepest quality of common humanity requiring affirmation. The unique human capacity for moral agency is further identified as a foundation of equality. The principle of equal protection of individual persons and their rights as the duty of government is clearly articulated in the constitutions of modern democracies. Contemporary understanding of equality has been widely framed along the lines of Williams as universal protection of human dignity, moral worth, and equality of opportunity. Rawls defined citizenship as a political function requiring full powers of moral agency among people who are free and equal. For Rawls, moral agency includes a capacity to understand, apply, and act from principles of political justice as well as a capacity to understand, envision, and rationally pursue the good.

Equality and Distributive Justice

The justice tradition of equality can be traced to Plato and Aristotle, who considered justice the foundation of a well-ordered society. Plato outlined his political ideal of civic justice in *The Republic,* explaining that individuals are the functional elements of a whole society, each person and class of persons with a valuable and specialized role. Although Plato understood this ideal city as a hierarchy of three classes, the overall ethos was one of mutual rights and obligations among citizens. This social arrangement was not thought to benefit only the city as a whole; each person was best able to achieve happiness in a society that was structured to recognize and reward people according to their varying talents, yet all were guaranteed protection and care as citizens.

Aristotle identified justice as one of four cardinal virtues, distinguishing between two types of justice: *distributive justice*, a principle of proportional equality requiring that people be accorded benefits and burdens with regard to merit, and *retributive justice* (also *rectificatory, corrective*, or *commutative justice*), a principle of exchange requiring strict, mathematical equality of "tit-for-tat" exchange as compensation for an injury or punishment for a crime to balance an injustice. He further identified *equity* as a principle of justice operating above the law through judicial means to correct inequities to universal justice created by the laws. The Aristotelian principle of equity was not an equality of undifferentiated sameness but impartial treatment of each person according to relative merit to maintain the balance of civic order. Aristotle's conception of civic justice required that power be exercised for the common good, not for the benefit of the governors or the favored segment of the population. The Aristotelian formulation of justice is institutionalized in modern society through law, the judiciary, and notions of civic duty.

Equality and Economic Justice

In modern times, persistent conditions of unmitigated poverty among developing nations and communities in a global economy of unprecedented wealth have generated questions about equality and economic justice. Marx examined the material aspect of equality, arguing that claims of equality must encompass the physical and economic conditions of individuals and social groups. What is the value of a vote without a job? And what is the benefit of expanding wealth concentrated in the bank accounts of a few when large numbers of people are hungry or lack shelter? The Marxist solution to this challenge was to eliminate private capital and collectivize property in the hands of the citizenry. While the Marxist experiment failed to deliver on its promise of universal material equality, the collectivist approach has had a lasting impact on most modern societies in the provision of social safety nets and entitlement programs that guarantee standards of living and quality of life for all citizens.

Modern liberal theories presume abstract, intrinsic equalities (pursuit of happiness, free will, supreme ethical worth) and concrete, discrete differences (bodies, property entitlements) among individual persons. The legal and political dimensions of equality are expressed as rights and freedoms involving, for example, speech, association, voting, and property. Consequently, these same individual freedoms become the foundation for material inequality; a wealthy individual's right to purchase and retain unlimited amounts of private property is protected, while an impoverished individual's right to even a minimal amount of property for basic shelter and livelihood is not acknowledged. This abstractly individualist framework of human equality forms a social ethic within which societies such as the United States are logically consistent in considering themselves free and democratic if their notions of equality are not manifested in the concrete form of jobs, housing, or health care. Because this framework fails to concretize equality in human needs or capabilities, conditions such as hunger, homelessness, unemployment, and poverty can be viewed as diverse expressions of individual freedom. Several contemporary theorists have attempted to augment the social justice aspects of equality.

Framing the foundation of equality as justice, Rawls argues that justice is fundamentally about fairness, wherein free and equal citizens engage in social cooperation in building a democratic political society. The concept of justice as fairness provides a philosophical and moral foundation for a democratic political economy. The basic concept at the heart of Rawls's theory of equality is that the social cooperation of citizens in a well-ordered political society will include a concern for economic distributive justice.

Rawls outlines social cooperation around essential features that assume equality among participants, both in the present generation and from one generation to the next. Social cooperation is guided by publicly recognized rules and assumes operational conditions of reciprocity and mutuality in pursuing the common good wherein each participant cooperates as a means of seeking his or her own rational advantage. Rawls asserts that rational people would choose a just political system not only to protect basic liberties but also to provide for the less advantaged in the knowledge that conditions of relative privilege or disadvantage are subject to change and chance. A political framework of justice creates cumulative collective advantages over time that constitute a cross-generational legacy of social equality providing continued protection and security for citizens in the present and their heirs in the future.

Sen applies the principles of equality and distributive justice directly to economic conditions, proposing a human-capabilities-based foundation for equality. Although acknowledging difficulties with basic capabilities equality, Sen sees this approach as a natural extension of Rawls's concern for primary goods with their focus on human utility. In Sen's view, a capabilities approach is focused on concrete measures of human flourishing rather than on the distribution of goods that are instrumental to flourishing. In this view, the development of concrete human capabilities is the foundation of a democratic society of equals.

Zucker extends the understanding of equality to economics in positing a social theory of property rights, holding that the just distribution of material resources is a defining characteristic of democracy. Challenging the prevailing economic and political theory, Zucker defines capitalism as an economic community constituted by social as well as individual agents, thus justifying some degree of economic redistribution based on the degree to which economic productivity is generated by social agency. In this view, individuals have rights to equal shares of at least part of the total social income of an economy. Zucker argues further that the individualistic foundation of political theory—including liberal theorists such as Rawls—fails to account for the social formation of the human person. Zucker theorizes that individuals formed within a political economy of reciprocity and mutuality develop capabilities for both self-determination and social determination.

Despite numerous attempts to bridge the theoretical gap between political and economic equality, there is at present no universally normative consensus about the concrete consequences and material conditions constituting the moral claims of equal human personhood. The diversity of philosophical approaches and public policy approaches taken by nations, states, and local communities reflects a range of responses to addressing the normative material claims of human equality in its political and economic dimensions.

—Lindsay J. Thompson

See also Justice, Distributive; Social Contract Theory

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Equal Opportunity

Equal opportunity is the goal of laws, regulations, and policies attempting to ensure that similarly situated people are treated equally in virtually all aspects of life, including jobs, education, housing, public accommodations, and so forth. The United States has a long and difficult history regarding equality based on race, gender, ethnicity, and other characteristics. Women, blacks, Native Americans, Asians, Jews, gays, the differently abled, and others were variously denied the right to vote, not given equal pay for equal work, not allowed to have certain jobs, denied access to equal education, and denied access to public facilities and generally did not enjoy the same rights to pursue the same quality of life as white males. In an effort to live up to the statement in the Declaration of Independence that "we hold these truths to be self-evident, that all men are created equal, that they are endowed by their Creator with certain unalienable rights, that among these are life, liberty and the pursuit of happiness," the U.S. Congress has passed laws guaranteeing its citizens an equal opportunity to receive the basics determined to be part of a civilized and humane democratic society: housing, education, employment, voting, public accommodations, and receipt of federal funds. Equal opportunity encompasses a set of laws that are an attempt to rid the country of the effects of its history of denying equality based largely on immutable characteristics such as race, gender, or ethnicity.

The primary vehicle for providing equal opportunity is the Civil Rights Act of 1964. There are also other major laws providing equal opportunity on the basis of age or disability. States also have equal employment laws that by and large track those of the federal government, though some states have added other categories, such as affinity orientation, marital status, or political affiliation. The major equal opportunity laws are reviewed here.

Fourteenth Amendment to the U.S. Constitution

Arguably, the first major equal opportunity provision, the Fourteenth Amendment, ratified in 1868, undergirds much of the expectation that Americans have to be treated fairly and be treated the same if they are similarly situated. The amendment states that "all persons born or naturalized in the United States, and subject to the jurisdiction thereof, are citizens of the United States and of the State wherein they reside. No State shall make or enforce any law which shall abridge the privileges or immunities of citizens of the United States; nor shall any State deprive any person of life, liberty, or property, without due process of law; nor deny to any person within its jurisdiction the equal protection of the laws."

The Fourteenth Amendment was subjected to a great deal of resistance during its passage, since it was put in place to give the newly freed slaves the same rights as U.S. citizens, something they had not heretofore enjoyed. Under the law, the federal government, generally through the U.S. Supreme Court, could nullify state laws that operated to deny blacks the rights enjoyed by white citizens.

Despite passage of the Fourteenth Amendment, several southern states still maintained, either formally or informally, ironclad "Black Codes," which subjected blacks to a different set of rules and laws than whites. Such laws were in effect for nearly 100 years after passage of the amendment, until they were outlawed by the Civil Rights Act of 1964. The Fourteenth Amendment's denial of equal protection and due process has become the primary means of challenging laws that create barriers to equal opportunity in the United States.

Fifteenth Amendment to the U.S. Constitution

The right to vote was granted to blacks after the Civil War ended slavery in 1865 and Congress passed the Fifteenth Amendment to the U.S. Constitution in 1870. The Fifteenth Amendment provided that the right to vote "shall not be denied or abridged on the basis of race, color or previous condition of servitude," thus nullifying the laws passed by states to prohibit blacks from voting. The Enforcement Act of 1870, providing criminal penalties for interference with the right to vote, and the Force Act of 1871, providing for federal election oversight, allowed a brief time of Reconstruction-era voting and election to office by blacks. Since blacks outnumbered whites in five southern states and had substantial numbers in other southern states, this resulted in their election to office, and even to the governorship of Louisiana (which lasted only 1 month, due to white resistance). This period of seeming equality was, however, short-lived due to the rise of the Ku Klux Klan and its attendant violence designed to return the south to the pre–Civil War status quo. The Fourteenth Amendment required state governments, like the federal government, to ensure that citizens have a right to due process and equal protection, while the Fifteenth Amendment granted to blacks the right to vote.

Nineteenth Amendment to the U.S. Constitution

This provision, ratified in 1920, granted women equal opportunity in voting by allowing them to vote in elections. Gender-based disenfranchisement had been the norm since the country's founding and was nullified only after an acrimonious decades-long fight by those believing the disenfranchisement to be totally at odds with the Declaration of Independence and the U.S. Constitution. Women's suffrage, as the movement to gain voting for women was called, included a group called the Silent Sentinels, who staged an 18-month demonstration outside the White House to gain voting rights for women.

The Civil Rights Act of 1964

This major equal opportunity law was passed largely in response to the turbulence erupting from the Civil Rights movement in response to racial discrimination and "Jim Crow" segregation in the United States, primarily in the south; it guaranteed equal opportunity for all citizens in housing, education, employment, voting, and receipt of federal funds. The Civil Rights Act, one of the most ambitious pieces of legislation in the history of civilization, is divided into titles that address the various contexts for protection.

Title I: Voting

Equal opportunity in voting was included in the Civil Rights Act of 1964 because blacks were routinely denied the right to vote, particularly in the south, despite the Fifteenth Amendment and other legislation passed after the Civil War guaranteeing them the right to vote. In the same year that the Civil War ended, the Ku Klux Klan was born. Violation and intimidation by the Klan and other such white supremacist groups increased after the federal troops left the South in 1877. The federal troops had been in the South since the end of the Civil War in 1865, during the period known as the Reconstruction. Without the presence of the federal troops, life reverted to much the way it had been during slavery.

Blacks' homes were burned down, jobs were taken away, and poll taxes were imposed, with the knowledge that blacks would not be able to pay to vote. Blacks were routinely intimidated, harassed, beaten, and lynched for attempting to register to vote. Their economic lives were also threatened, as most were employed as menial laborers for whites, and it was understood that they would lose their jobs if they voted. Those who made it inside the voting registrar's office were often asked to explain extremely difficult arcane passages from the Constitution, asked questions such as how many bubbles there are in a bar of soap or how many grains of sand there are on the beach, or asked to pay poll taxes that were far out of their financial reach. This was not done to whites, which ended in leaving the voting to them. Blacks were effectively disenfranchised for the next nearly 100 years until passage of the Civil Rights Act in 1964.

Realizing that the Civil Rights Act of 1964 was not enough to curtail the continued harassment of black voters, the next year, Congress passed the Voting Rights Act of 1965, but not before the events of March 7, 1965, and what became known as "Bloody Sunday." In the Selma-to-Montgomery March for Voting Rights, 600 nonviolent civil rights protesters attempted to walk from Selma to Montgomery, Alabama, via the Emund Pettus Bridge, to demonstrate the need for federal voting legislation. They were met with mounted police on horseback and dogs, which were set loose on the crowd. Television coverage horrified the nation, and after obtaining a court order to allow the march, 25,000 marchers from across the country and world successfully made the trek on March 21, 1965. Less than 5 months later, the Voting Rights Act of 1965 was passed. The act outlawed the kinds of impediments to voting and registering to vote that had routinely been used to disenfranchise blacks since after the Reconstruction. The U.S. Department of Justice Civil Rights Division enforces voting laws.

Titles II and III: Public Accommodation

At various times, blacks, Native Americans, the Irish, Jews, and others were not allowed into public places or to use public facilities. Libraries, theaters, restaurants, public auditoriums, swimming pools, recreational facilities, parks, hotels, stores, public transportation, and other places were all off-limits to them, especially to blacks. If blacks were allowed in, they often had to sit in a different place from whites. For instance, in theaters, blacks often had to sit in the balcony or attend on different days from whites; blacks had to board public buses and pay the full fare, then get off, go to the back of the bus, and take a seat in the rear. If a white person needed a seat, the black person would have to get up and give his or her seat to the white person, even though both had paid full fare. If blacks were allowed into restaurants at all, they generally had to go to the rear entrance and order their food to take away. Some towns had special days for blacks to shop, and fairs had special days for blacks to attend.

The Civil Rights Act prohibited these practices and required equal access to public facilities. Blacks and others were no longer denied the right to enter into or use public facilities. Private clubs and facilities such as country clubs can still discriminate, however.

Title IV: Education

Prior to passage of the Civil Rights Act, many public schools remained segregated even though the

U.S. Supreme Court had outlawed them in its 1954 *Brown v. Board of Education* decision 10 years earlier. Black children were not permitted to go to school with whites and did not have access to the same funding, materials, facilities, and programs that were provided to white students. Black schools were generally in poor condition, with few supplies and books. Often, the first few days of school were spent taping up discarded, outdated books from white schools to be used by black schools since the white students had received new textbooks.

Such acts were outlawed by the Civil Rights Act of 1964. Equal opportunity in education is enforced by the U.S. Department of Education's Office of Civil Rights.

Title V: Housing

Prior to passage of the Civil Rights Act, segregation on the basis of race or ethnicity in housing was widespread. Restrictive covenants in property deeds were common. Such covenants dictated that the property could not be sold or rented to certain groups, such as blacks or Jews. Owners routinely refused to sell or rent their property to blacks or Jews regardless of their appearance, ability to pay, education levels, or jobs. If they did rent or sell to blacks or Jews, whites living in the area would soon move away, and the property values would decrease. Such practices relegated the groups discriminated against to enclaves exclusively peopled by those groups.

Under the provision that prohibited discrimination in programs receiving federal funds, the Civil Rights Act outlawed such practices. To further strengthen its commitment to equal opportunity in housing to ensure equal access to housing, in 1968, Congress passed the Fair Housing Act as Title VIII of the Civil Rights Act of 1968. The law prohibits discrimination in the sale, rental, and financing of dwellings and in other housing-related transactions, based on race, color, national origin, religion, sex, familial status (including children under the age of 18 living with parents or legal custodians, pregnant women, and people securing custody of children under the age of 18), or disability, and provides the structure for equal housing opportunity. Equal opportunity in housing is overseen by the U.S. Department of Housing and Urban Development's Office of Fair Housing and Equal Opportunity, which administers the federal laws and establishes national policy that ensures that everyone has equal access to housing on a nondiscriminatory basis.

Title VI: Federally Assisted Programs

From federally guaranteed school loans to welfare, from schools and universities that receive federal funding and grants to arts programs funded by government grants, no one can discriminate, and all must provide equal opportunity in their programs.

Title VII: Employment

Title VII of the Civil Rights Act of 1964 prohibits discrimination in employment on the basis of race, color, gender, religion, or national origin by employers with 15 or more employees, labor unions, and employment referral agencies. Sexual harassment and pregnancy discrimination are also prohibited as types of gender discrimination. Under Title VII, the prohibited categories cannot be used as a basis for employment decisions of any kind, including hiring, firing, discipline, promotions, raises, or any other term or condition of employment. The Equal Employment Opportunity Commission (EEOC) enforces claims of all bases for employment discrimination under Title VII, the Equal Pay Act, the Age Discrimination in Employment Act, and the Americans with Disabilities Act. By law, the EEOC must dispose of all claims filed, as appropriate, and does so through mediation, conciliation, investigation, and, if necessary, litigation. The agency's role has been strengthened over the years by Congress, and it is considered the top equal opportunity agency in the United States.

The Equal Pay Act of 1963

Enacted into law even before the Civil Rights Act of 1964, the Equal Pay Act prohibits pay discrimination based solely on gender. Under the law, men and women must be paid the same wages for work requiring equal skill, effort, and responsibility and performed under similar working conditions. Wages can be different based on other factors, such as the quantity or quality of production, a valid seniority system, a valid merit system, or any factor other than gender.

The Americans with Disabilities Act of 1990

The Americans with Disabilities Act of 1990 provides equal opportunity in employment and access to facilities to those who have a physical or mental impediment that substantially affects a major life function, who have a record of such an impediment, or who are perceived to have such an impediment. If the employee with disabilities is otherwise qualified and can perform the job, with reasonable accommodation that does not cause the employer undue hardship, and the employee presents no threat to the safety of people or property, the employer cannot discriminate against the employee because of his or her disability.

The Age Discrimination in Employment Act of 1967

Employees aged 40 years or older may not be discriminated against in employment and must be given an equal opportunity to work. Such employees may not be terminated and replaced with younger employees, have their job duties diminished solely because of age, be denied training, or be otherwise denied equal employment opportunity because of their age. The EEOC handles claims of age discrimination.

The Family Medical Leave Act of 1991

The Family Medical Leave Act of 1991 (FMLA) provides up to 12 weeks of unpaid leave for employees who take time from work because they or their child, spouse, or parents are ill or because they have a new biological, adopted, or foster care child. Men are often denied this leave based on gender stereotypes and expectations that women will handle such matters. Historically, women were often denied such leave or were given the leave but found on their return to work that they had been demoted or terminated and their benefits, leave, and/or seniority suspended during their absence. This is illegal under the FMLA. FMLA claims are handled by the U.S. Department of Labor's Employment Standards Administration, Wage and Hour Division.

Executive Order 11246

This is one of the most controversial sources of equal opportunity. The executive order, signed into law by President Lyndon B. Johnson in 1965, dictates that those who wish to provide goods and services valued at $10,000 or more to the federal government or through contracting with the federal government must agree not to discriminate on much the same bases as those mentioned in Title VII of the Civil Rights Act. If the amount involved is $50,000 or more, in addition to not discriminating, the contractor must also conduct a workplace assessment to determine the participation of women and minorities at all levels of the contractor's workplace. If there is a significant underrepresentation of women and minorities, given their availability in the area from which the contractor's employees are drawn, then the contractor must devise a plan to remedy this underrepresentation. This is generally called an affirmative action plan.

Those who feel adversely affected by the operation of an affirmative action plan have brought lawsuits on the basis of "reverse discrimination." That is, although Title VII is designed to protect everyone equally, they allege that the operation of the affirmative action plan to include those shown to have been excluded from the workplace discriminates against them and should not be allowed to be used. Affirmative action has also been used in the area of college admissions and minority set-aside programs. The theory is that unless there is a conscious effort to include groups traditionally excluded from the workplace and educational institutions, the underrepresentation will continue despite the laws prohibiting discrimination.

Affirmative action may only withstand court scrutiny if done properly. Quotas are prohibited, though the employer may set goals, setting forth appropriate numbers, to attempt to attain more representation of the underrepresented groups given their availability in the area from which employees are drawn, as well as timetables within which these goals should be accomplished. However, the plan is not cast in stone and can be adjusted as circumstances dictate. Availability only applies to those who are available for the type of job under consideration. For instance, if there are 38% females in the population, it does not mean that 38% are qualified to be doctors. Nothing in the law requires that someone who is not qualified be given a job or admission to college, and the law specifically prohibits employers from taking those presently in jobs out of them to make space for someone pursuant to an affirmative action plan.

The law provides no specifics as to what affirmative action must be taken to correct a significant underrepresentation, but certain approaches have been deemed by courts to be inappropriate. Setting quotas is not permitted. In the seminal 1987 U.S. Supreme Court case of *Johnson v. Transportation Agency, Santa*

Clara County, California, the high court ruled that plans that take into account factors such as race and gender are permissible if the plan is to address a manifest imbalance that reflects underrepresentations in the workplace of traditionally excluded groups, race or gender is only one of several factors considered, the plan is made to attain rather than maintain a balanced workforce, and the plan does not unnecessarily trammel the legitimate settled rights of other employees or create an absolute bar to their advancement. If these factors are adequately addressed in the affirmative action plan used by the employer, then the plan will be able to withstand judicial scrutiny in court when the plan is challenged as reverse discrimination.

In addition to the EEOC, there are several other federal government offices whose missions are to enforce equal opportunity in various contexts, including the U.S. Department of Justice, Office of the Attorney General, Civil Rights Division; the U.S. Commission on Civil Rights; the U.S. Department of Health and Human Services, Office for Civil Rights; the U.S. Department of Agriculture, Civil Rights Office; the Federal Aviation Administration, Civil Rights Office; the U.S. Department of Transportation, Civil Rights Office; and the U.S. Department of Labor, Civil Rights Enforcement for Department of Labor Grant Recipients.

—Dawn D. Bennett-Alexander

See also Affirmative Action; Age Discrimination; Comparable Worth; Disability Discrimination; Gender Inequality and Discrimination; National Origin Discrimination; Racial Discrimination; Religious Discrimination; Sexual Harassment

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Equal Pay Act of 1963

The Equal Pay Act of 1963 (EPA), signed by President John F. Kennedy, came into effect on June 11, 1964. It was designed to reduce the pay differential between men and women for substantially equal work within the same organization. The EPA is part of the Fair Labor Standards Act of 1938, as amended. This act, administered and enforced by the Equal Employment Opportunity Commission, prohibits all employers from wage discrimination between men and women in the same establishment who are performing under similar working conditions. If there is a pay differential, the employer must be able to demonstrate that it is based on seniority, a well-defined merit system, a system that measures the quantity or quality of productive output, or some factor other than sex. Employees filing claims under the EPA are not required to show that their employer intended to engage in sex-based discrimination. Although the concept of comparable worth was considered in the formulation of this act, it was rejected in favor of the definition of equal work. Equal work was understood to indicate substantially equal, but not necessarily identical, job tasks, effort, and responsibilities.

Congressional hearings in the spring of 1963 reflected the broad national debate that preceded and followed the passage of the EPA. The statement prepared for Congress by the National Retail Merchant Association (NRMA) exemplified the concerns of many businesses regarding the proposed act. While the NRMA asserted their enthusiastic support for the principle of equal pay for equal work, the bulk of their statement argued that federal legislation was unnecessary, burdensome, confusing, and unenforceable. Furthermore, they pointed out, higher rates of absenteeism for women increased the employers' cost of employing women. Additional costs included the necessity of constructing additional seats, lunchrooms, and bathrooms for women and the anticipated provision of longer meal and rest periods for women.

Vociferous contrasting views were presented to Congress by the Women's Department of the United Auto Workers' Union. In support of the EPA, they argued that unequal pay was immoral in depriving women of earned payment, unjust in penalizing the lowest-paid workers, inefficient in causing resentment among employees, uneconomic in incentivizing the inefficient use of workers, and contrary to the interest of the community in penalizing fair-minded employers while providing a cost bonus to employers who discriminated against women.

Since the passage of the EPA, sex-segregated job listings have disappeared, and overt sex discrimination in workplace compensation has diminished. However, the wage gap between men and women continues. In 1963, women earned 59% of the wages earned by men; in 2002, women earned 76% of men's wages. Although this oft-cited statistical indicator includes a measure of the wages of dramatically unequal positions as well as those with substantively equal tasks, it is widely acknowledged that the goal of equal pay for equal work articulated by the Equal Pay Act of 1963 has not yet been fully achieved.

—Robbin Derry

See also Comparable Worth; Employment Discrimination; Equal Employment Opportunity; Fair Labor Association (FLA); Feminist Theory; Gender Inequality and Discrimination; Hostile Work Environment; International Labour Organization (ILO); Women in the Workplace

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EQUAL SACRIFICE THEORY

Equal sacrifice theory maintains that all members and sectors of society should make equal sacrifice for the common good. This theory has been critical to political economy since the 18th century, particularly as it pertains to taxation. Yet the idea is broader than the economics of taxation: Both the Old and the New Testament of the Judeo-Christian Bible emphasize charitable personal sacrifice—the Hebraic requirement of tithing and Jesus's parable of the poor widow giving up two coins to the collective pot; the idea even appears in 20th-century American poetry—in Robert Frost's "In Equal Sacrifice." In economics, equal sacrifice theory developed from historically and ethnically diverse strains: the 18th-century Frenchman Jean-Baptiste Say; the Swiss Jean-Jacques Rousseau; and the British William Gladstone, John Stuart Mill, and F. Y. Edgeworth. Throughout the 1900s and into the 21st century, American and British tax debates have employed equal sacrifice arguments over the costs and burdens of pre– and post–World Wars I and II and in equitably sharing the costs of ongoing, global military conflicts and commitments for the greater good.

Equal sacrifice is subject to differing interpretations yet is often measured in absolute, proportional, and marginal terms: (1) equal absolute sacrifice (where each taxpayer surrenders the same degree of utility that one obtains from one's income), (2) proportional (where each sacrifices the same proportion of utility from one's income), and (3) marginal (where each surrenders the same utility from one's income). Typically, vertical and horizontal notions of equality enter into these analyses. Equal taxation (equal treatment of equals, dissimilar treatment of dissimilars) reflects horizontal equality; progressive treatment of unequals (rich vs. poor) reflects vertical equality. A "flat tax" indicates horizontal equality and "progressive taxation" indicates vertical equality of sacrifice. Political economists use equal sacrifice theories to balance the social benefits of equality with incentives to work and to profit from one's labor and productivity.

Although Smith's 18th-century maxim says that taxation should place the same pressure on everyone, as nearly as possible, equal sacrifice theory was not fully developed until it incorporated the "ability-to-pay" principle into a standard theory of political economy, Mill's *The Principles of Political Economy*, Book 5. Often viewed as the most equitable taxation policy, still used in most industrialized economies, this principle holds that taxation be levied according to one's ability to pay, making the wealthier pay a proportionately higher tax toward the national tax demand. Determining a fair measurement of input according to one's economic contribution, labor, and production and assessing equal values and tax burdens across such disparate bases are problematic. Government must also determine how the inequality of differing tax burdens and benefits, sacrifices and payouts, would yield economic growth without social exclusions and curtailment of individual freedom. Equity and efficiency then are not equivalent factors in evaluating equal sacrifice.

A progressive tax system seems equitable under utilitarian ethics, because under the general happiness principle, tax burdens are assigned only to maximize general welfare. The modern theory of income tax progressivity begins with the utilitarian calculation of the sum total of benefits and costs, viewing unequal taxation as the trade-off between the social benefits of an equal distribution of after-tax income and the potential fiscal damage imposed by highly progressive taxes. The result is not equality but a leveling of higher incomes, which leads to minimum aggregate sacrifice.

Questions concerning the degree of tax progressivity rely not only on the tenor of taxpayers' responses to high tax rates but also on core issues concerning the government's role in determining the "value" of a tax dollar taken from a low-income family versus that from an upper-income family. Tax burdens are not to be determined according to what taxpayers get from the government but according to their ability to bear the tax imposed—that is, to tolerate the sacrifice. What benefits citizens receive from their taxes and how tax dollars are distributed differently to meet competing demands and benefits must be politically negotiated.

—Mary Lenzi

See also Charity, Duty of; Equality; Mill, John Stuart; Smith, Adam; Tax Ethics; Utilitarianism

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Equilibrium

Equilibrium is a condition of balance in which all influences on a system are held in check and no change occurs. Disequilibrium is the condition of change resulting from some alteration in these influences. Market equilibrium, Nash equilibrium (NE), and reflective equilibrium are the three prevalent types in economic, strategic, and ethical analyses, respectively.

Market Equilibrium

Economists distinguish between general and partial equilibrium analyses in market systems. Partial equilibrium analysis examines individual markets or the decisions of particular firms or households, holding constant other considerations actually varying in general equilibrium analysis. Such partial analysis can therefore be wrong. General or static equilibrium represents the condition in which the equality of all quantities of supply and demand yields no incentive for market behavior to change. If supply exceeds demand, business production will increase. Business will lower product price until equality in supply and demand is restored to stable equilibrium. In supply-demand models, a unique price exists, the "equilibrium price." Algorithms and curves graphing dependent and independent quantitative terms and variables represent these common marketplace operations.

In examining market models, one considers those forces that make and maintain an equilibrium price. This determination lies in the reaction of sellers and buyers to disturbances or shocks in the market. For instance, market price can be forced above equilibrium such that supply decisions by producers with respect to output exceed the amount demanded by consumers; then, a surplus results. Competition provides its market gravity force to maintain or restore the equilibrium price. If surpluses exist, competition among sellers forces prices downward. If shortages exist, competition among buyers forces prices upward. In typical market behavior, surpluses are the result of market prices exceeding the equilibrium price such that price-cutting behavior helps restore this equilibrium price. Shortages occur when market prices assume values below the equilibrium price; bidding helps restore the equilibrium. However, this regulating, balancing act does not always obtain.

The market system has to operate efficiently by providing incentives to weigh costs and benefits. The profit incentive should make businesses competitive by aiming to minimize costs and to use the most efficient technology and means to make their products sell at the best price (equilibrium). When there are no "externalities" (e.g., requirements for clean air, potable water, public safety), businesses weigh private benefits and costs only in their production choices. Imperfect markets, subject to inefficiency, arise from imperfect information, incomplete or incorrect information concerning products, costs, and pricing. A monopoly indicates imperfect market competition (a form of disequilibrium).

The market itself cannot reveal all costs and benefits, nor can these be perfectly weighted to yield market efficiency. In any imperfectly competitive system, wide variations in production and monetary and human resources (labor) yield disequilibria points between supply and demand that interact over time. Further difficulties arise when computing and inputting untidy, historical changes and stressors into quantitative graph analyses. Variable economic growth, military engagements, unemployment, inflation, and natural disasters are not simple demand- or supply-side factors; hence, equilibria points cannot be fixed or mapped reliably. Other complications stem from unpredictable human inputs—anxiety-based behavior and uncertainty, cautious protective hoarding of resources or savings, risky consumer and investor behavior, and the gambling mentality of assuming high stakes and high debt. Such variables constitute hard balancing acts in maintaining equilibrium.

Nash Equilibrium

NE signifies an optimum game strategy whereby no one player can benefit by changing his or her strategy while all other players keep theirs the same. For market behavior, NE assumes that "average" agents act "as if" rational, and those who are not (rational) are competed out of the market. The "market" and its evolution presumably have the inherent capability of testing all strategies; thereby, any irrational agent or agency would disappear. However, NE does not always prevail, and one cannot assume such rationality over time.

Reflective Equilibrium

Reflective equilibrium applies in ethics when the consequences of one's general principles are consistent with one's opinions about individual cases. John Rawls described such a process whereby decision makers consider alternative judgments in deciding right action in a particular case and in providing reasons or principles for their judgment. Critics raise concerns about reflective equilibrium, deeming the regulatory role of rationality suspect when made supreme in decision making.

Conclusion

Even ordinary consumers and producers should take heed of such theoretical, ethical, or mathematical analyses, how algorithms are made, rules written, and decisions made. Much is at stake in using equilibrium or disequilibrium models in market analysis. Economic theories adopt premises such as "Markets are efficient," "A stock's price reflects actual value," and "Speculators are rational in their decisions to maximize their wealth." Presumably, all these suffice in eliminating other contrary factors, such as mob instincts, greed, and "irrational" speculative "bubbles." A bubble is an unsustainable increase in prices caused by investors' buying behavior, instead of correct information about value. Real estate and energy industry bubbles and market collapses such as the "dot-com" business in 2000 indicate the unpredictable side of economics.

In doing practical business ethics, controversy ensues over methodology and deliberative processes. Instead of being conceived as generalists in their principles and rule making and mathematical in their graph making and observance, perhaps deliberative agents should be studied as particularists and casuists, who in deciding and judging must employ a detailed understanding of the specific case and situation. Nevertheless, in decision making, using these general processes and strategies—market equilibrium, Nash equilibrium, and

Rawlsian reflective equilibrium—seems worthwhile as a starting point and in explaining economic behavior and market outcomes. Though there are other gauges for evaluating the intentions and outcomes of economic agents, equilibrium provides a viable model for this process.

—Mary Lenzi

See also Agency, Theory of; Arrow, Kenneth; Capitalism; Competition; Economic Efficiency; Economic Incentives; Economic Rationality; Efficient Markets, Theory of; Externalities; Free Market; Gambling; Game Theory; Nash Equilibrium; Pareto Efficiency; Rawls's Theory of Justice; Situation Ethics; Supply-Side Economics; Surplus, Consumer and Producer; Von Neumann-Morgenstern Utility Function

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Ethical Culture and Climate

Interest in ethical culture has increased since the U.S. Sentencing Commission revised its guidelines for sentencing organizational defendants in 2004. Because of concerns that organizations were developing "window dressing" ethics and compliance programs, these revised guidelines call for more attention to the ethical "culture" of the organization and the need to align formal ethics programs with this broader ethical culture.

Ethical climate and culture represent somewhat different but related ways of thinking about the environment in organizations, which can influence organizational members' ethics-related attitudes and behaviors. Like the organizational climate and culture literatures more generally, these ways of thinking about the ethical environment in an organization have developed somewhat separately, but both refer to aspects of the organizational context that are thought to influence ethics-related attitudes and behavior.

The term *ethical context* is a broader term and can refer to both ethical climate and culture. The idea that the ethical context in an organization would influence employee attitudes and behaviors is based on assumptions about employee susceptibility to organizational influence when it comes to matters of ethics. This assumption, based on social scientific theories of human behavior, studies of moral development, obedience to authority, and the like, argues that the behavior of human beings is often influenced by factors outside the individual. In work organizations, those factors might include peers, leaders, rewards, and punishments as well as the messages sent by the organization about appropriate conduct.

The ethical climate approach to thinking about ethical context was developed in the late 1980s by Victor and Cullen. The authors defined ethical climate as employee perceptions of ethics-related organizational practices and procedures and proposed that ethical climate would differ between organizations and would be associated with ethics-related attitudes and behaviors. As originally proposed, ethical climate included nine dimensions based on the intersection of three philosophical perspectives (egoism, benevolence, and principle) and three loci of analysis (individual, local, and cosmopolitan). The Ethical Climate Questionnaire was used to measure these dimensions. Each specific climate is accompanied by a normative expectation that is expected to guide attitudes and decision making. For example, employees in an egoistic-individual climate should be guided by self-interest, while those in an egoistic-local climate should be guided by company interest, and those in an egoistic-cosmopolitan climate are guided by an efficiency criterion. Organization members in a benevolent individual, local, or cosmopolitan climate are concerned about the welfare of individuals and groups inside and outside the organization, respectively. Finally, individuals in a principled individual, local, or cosmopolitan climate should be guided by their personal morality, organizational rules and regulations, or societal laws and codes, respectively.

In empirical investigations, researchers have found evidence of fewer than the nine proposed dimensions (generally five). Some of these dimensions overlap with the theoretically proposed climate dimensions, and some combine the aspects of different dimensions. Additional construct validity work will be required to confirm the dimensionality of the ethical climate construct and the relationships between those dimensions, the proposed theory, and outcomes.

Researchers have also explored the relationship between employees' perceptions of the ethical climate and employee attitudes (e.g., organizational commitment) and behaviors (e.g., ethical conduct). Multiple studies have found employees' organizational commitment to be positively related to benevolent climates and negatively related to egoistic climates. In addition, several ethical climate dimensions have been associated with ethical/unethical conduct on the part of organizational members.

Ethical climate was also found to vary between firms. But in refining thinking about ethical climates, researchers have asked whether ethical climates might also vary within organizations by work group or department. For example, a study in a large financial services firm found that different ethical subclimates exist in different departments, consistent with the departments' primary task and the external stakeholders served.

The ethical culture approach was originally introduced by Treviño as part of an interactionist model of individual and contextual influences on ethical decision-making behavior in organizations. This work was later expanded to develop an understanding of ethical culture as a combination of organizational structures, systems, and practices that can influence employees' ethics-related attitudes and direct their ethical conduct. Ethical culture was defined as a subset of the overall organizational culture that represents the interplay of multiple formal and informal cultural systems that either work together or at cross-purposes to support ethical or unethical conduct. For example, formal systems include policies such as codes of conduct, explicit leader communications, formal decision-making processes, reward and performance management systems, reporting systems, authority structures, and training programs. Informal systems include informal norms of daily behavior and leader role modeling as well as organizational rituals, heroes, and stories. Member behavior is expected to be more ethical to the extent that these systems are aligned and supportive of ethical conduct.

Because ethical climate and ethical culture were both proposed to represent the ethical context of an organization, which could influence attitudes and behaviors, it became important to attempt to understand the relationship between ethical climate and ethical culture. Treviño and colleagues incorporated measures of both ethical climate and culture and investigated the relationships of these constructs to each other and to employees' attitudes and behaviors. That 1998 study found 10 ethical context factors representing three ethical culture dimensions and seven ethical climate dimensions that were found to be separate from each other. However, at the same time, many of the culture and climate dimensions were statistically related to each other, making it difficult to tease apart their separate effects on outcomes.

The study found that ethical climate and culture measures were about equally able to predict an employee attitude, organizational commitment. Employees who believed that their organizations supported employees and cared about the community (ethical climate dimensions) were most likely to identify with the organization and share its values. The overall ethical environment (focused on the culture dimensions of leadership, reward systems, and organizational norms) and obedience to authority were the most influential culture dimensions. An obedience-to-authority culture is one that demands unquestioning obedience (e.g., "Do as I say and don't ask questions"). Employees whose organizations' overall ethical environment supported ethics and did not have a strong obedience-to-authority culture were more committed to their organizations.

When studying ethical/unethical behavior, the researchers found somewhat different results for those working in organizations with and without an ethics code. For those working in organizations with an ethics code, the overall ethical environment and obedience-to-authority dimensions of culture were again the best predictors. To the extent that leadership, reward systems, norms, and authority structures supported ethics, employees said that there was less misconduct in the organization. Two climate dimensions (law and professional code and self-interest climate) were also influential. However, for those working in organizations without an ethics code, a single climate dimension, self-interest climate, explained much of the variance in ethical/unethical behavior. This is a climate in which people are simply out for themselves. So, to the extent that employees perceive such an environment, more unethical conduct is also reported.

In addition, research has found that the existence of formal ethics programs that included codes, training programs, and reporting systems has less influence on important ethics-related outcomes (misconduct, willingness to report problems to management, etc.)

than more informal ethical culture factors such as leadership, reward systems, and employees' perceptions of fair treatment. These aspects of the ethical culture appear to combine to create an organizational message to employees about whether the organization cares about ethics as much as other important outcomes (e.g., bottom-line success) and whether its formal programs are to be taken seriously.

Leaders have been expected to play a particularly important role in creating a supportive ethical environment in the work organizations they lead, creating the tone at the top. But we are just beginning to learn more about how they do so. Among other things, leaders can influence followers by role modeling ethical behavior, communicating a set of ethical values, and holding employees accountable. In fact, research has found that executive leaders can influence perceptions of the ethical climate of the organizations they lead if they have high levels of cognitive moral development and their actions are consistent with these levels, meaning that the leaders are behaving to their moral development capacity and thus are more likely to role model ethical behavior. This appears to be especially true in younger firms.

Although questions remain about the best way to conceptualize and measure the ethical context of work organizations, and much more research will be needed to understand which aspects of ethical climate and culture are the most important, the research conducted to date suggests that the organizational context clearly does influence employees' ethics-related attitudes and behaviors. It also suggests that organizations must go beyond the establishment of formal ethics and legal compliance programs if they wish to create a context that truly supports employee ethical behavior.

—Linda K. Treviño

See also Cognitive Moral Development; Corporate Ethics and Compliance Programs; Federal Sentencing Guidelines; Kohlberg, Lawrence; Leadership; Moral Leadership

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Ethical Decision Making

Ethical decision making is a cognitive process that considers various ethical principles, rules, and virtues or the maintenance of relationships to guide or judge individual or group decisions or intended actions. It helps one determine the right course of action or the right thing to do and also enables one to analyze whether another's decisions or actions are right or good. It seeks to answer questions about how one is supposed to act or live.

Ethical Decision-Making Process

Many ethics scholars have developed models of ethical decision making or provided us with specific procedural steps enabling one to reach an ethically supported decision or course of action. In the abstract, this process is a fairly rational and logical course. In reality, ethical decision making is filled with abstractness, illogic, and even whim. Nonetheless, the following is a synthesis of these models and procedures.

Step 1: Identify the Ethical Dimensions Embedded in the Problem

In the first step of the ethical decision-making process, the decision maker must be able to determine if an ethical analysis is required. The decision maker must determine if there is a possible violation of an important ethical principle, societal law, or organizational standard or policy or if there are potential consequences that should be sought or avoided that emanate from an action being considered to resolve the problem.

Step 2: Collect Relevant Information

The decision maker must collect the relevant facts to continue in the ethical decision-making process. Related to Step 1, if an ethical principle, such as an individual's right, is in jeopardy of being violated, the decision maker should seek to gather as much information as possible about which rights are being forsaken and to what degree. A consequential focus would prompt the decision maker to attempt to measure the type, degree, and amount of harm being inflicted or that will be inflicted on others.

Step 3: Evaluate the Information According to Ethical Guidelines

Once the information has been collected, the decision maker must apply some type of standard or assessment criterion to evaluate the situation. As described below, the decision maker might use one of the predominant ethics theories—utilitarianism, rights, or justice. Adherence to a societal law or organizational policy may be an appropriate evaluation criterion. Others may consider assessing the relevant information based on a value system where various ethical principles or beliefs are held in varying degrees of importance.

Step 4: Consider Possible Action Alternatives

The decision maker needs to generate a set of possible action alternatives, such as confronting another person's actions, seeking a higher authority, or stepping in and changing the direction of what is happening. This step is important since it is helpful to limit the number of actions that it may realistically be possible to respond to or that may be required to resolve the ethical situation.

Step 5: Make a Decision

In Step 5, the decision maker should seek the action alternative that is supported by the evaluation criteria used in Step 3. Sometimes there may be a conflict between the right courses of action indicated by different ethics theories, as shown later in the illustration provided. It might not be possible in all cases for a decision maker to select a course of action that is supported by all the ethics theories or other evaluation criteria used in the decision-making process.

Step 6: Act or Implement

Ethical decision making is not purely an intellectual exercise. The decision maker, if truly seeking to resolve the problem being considered, must take action. Therefore, once the action alternatives have been identified in Step 4 and the optimal response is selected in Step 5, the action is taken in Step 6.

Step 7: Review the Action, Modify if Necessary

Finally, once the action has been taken and the results are known, the decision maker should review the consequences of the action and whether the action upheld the ethical principles sought by the decision maker. If the optimal resolution to the problem is not achieved, the decision maker may need to modify the actions being taken or return to the beginning of the decision-making process to reevaluate the analysis of the facts leading to the action alternative selected.

Applying Ethics Theories

The following is an illustration of Step 3 of the ethical decision-making process that applies three predominant ethics theories—utilitarianism, rights, and justice—to a common business problem: Should a company close an operating plant and lay off its workers?

When using a *utilitarian perspective*—where the decision maker considers the consequences or outcomes of an action and seeks to maximize the greatest good for the greatest number of those affected by the decision—it is critical for the decision maker to determine to the greatest extent possible who will be affected by the decision. In the example used here, those affected may include the company itself (since closing the plant may improve its bottom line by dramatically reducing plant overhead and employee payroll expenses); the company's investors, if a publicly held business (who may receive a greater return on their investment if the plant closes and employees are laid off); the company's employees (who will suffer if the plant closes and they are laid off from their jobs); and the local community where the plant is located (who will suffer a reduction in the municipal tax base as well as a loss of economic activity for businesses that relied on the plant and its employees).

One might argue that the greater good is served if some workers are immediately laid off and the plant is closed, ensuring the immediate financial viability of the company. Yet others might reason to an ethical solution that requests all employees to take a slight pay cut so that no workers are laid off and the plant remains open, thus achieving the greatest good for the greatest number of people affected.

A decision maker who considers a *rights perspective* would consider the entitlements of those affected by the decision. There are economic rights affecting the displaced employees and the community surrounding the plant in question, as well as the rights of the laid-off employees to be informed of the potential plant closing. These rights may be in opposition to the managers' right to act freely in a way that could be understood as acting responsibly, by closing the plant and thus benefiting the remaining employees of the company and the company's investors.

A rights reasoner might provide ample notice to the workers of the layoffs so that they could seek other employment. Or the rights reasoner might consider the economic rights of the community and actively seek a buyer for the plant in the hope that it would remain open and continue to employ the workers. Finally, the rights of the company and its investors could persuade the decision maker to conclude that closing the plant and firing the workers is the right thing to do.

Finally, one who considers a *justice perspective* may focus on either the equitable distribution of the benefits and costs resulting from the plant closing and employee layoffs (distributive justice) or the maintenance of rules and standards (procedural justice). For the distributive justice reasoner, the ethical decision process would focus not only on the benefits incurred by the company and its investors through the plant closure and layoffs but also on the significant harms or costs imposed on those employees laid off from work and the local community and businesses negatively affected by the plant closing.

The procedural justice reasoner would focus on the preservation of the social contract that exists between the employer and employees or would seek to minimize the harm imposed on the powerless (the employees and the local community) by the powerful (the employer and investors). The procedural justice reasoner would argue that the employees, community officials, and local business leaders should have a voice in this decision since they are significantly affected by the decision.

The decision maker may decide that a more just action would require the company to assume greater financial responsibility by providing job training and outplacement services for the displaced employees. The company could consider making some type of economic contribution to the local community to soften the blow of a reduction in the tax base or economic activity in the area. Or the company could involve the employees and local community leaders in developing a system that results in the plant closure occurring over a longer period of time to spread out the eventual costs endured by the community.

Conclusion

People during their daily routine at work or in society are called on to make ethical decisions. Therefore, their ethical decision-making process may be a frequent, yet subconscious, cognitive process. Do you drive the speed limit or come to a complete stop at the intersection where a stop sign is posted? An individual can decide to act in the right way almost without thinking about it, but the decision maker is implicitly considering and processing the steps delineated above to reach the ethically supported decision to obey the speed limit or stop at the intersection in the road.

—*James Weber*

See also Dilemmas, Ethical; Entitlements; Ethics, Theories of; Feminist Ethics; Justice, Theories of; Rights, Theories of; Utilitarianism; Virtue Ethics

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Ethical Imperialism

Ethical imperialism (which directs people to do everywhere exactly as they do at home) is the term used to describe a situation where a code of ethical behavior or attitude is imposed on another community or society. It is normally used in a derogatory or pejorative sense. Ethical imperialism is at one end of a spectrum with cultural relativism (where no culture's ethics are better than any other's) at the other. With respect to cultural relativism, St. Ambrose (339–397) is given credit for the notion of doing as the Romans do when in Rome. The theory behind ethical imperialism vis-à-vis relativism is absolutism. This means that ethical imperialists aka absolutists believe that, first, there is only one list of truths. This can be misleading because different societies may emphasize one value more highly than others—for instance, "loyalty" as in Japanese culture vis-à-vis "equality, fairness, and individual freedom" as in Western democratic countries. Second, these truths can only be expressed with one set of concepts such as the language of basic rights. This too can be misleading because Confucian and Buddhist traditions do not always recognize the same values as Western democracies. Furthermore, they have their own cultural traditions, which would have to be ignored if that path was followed. The third problem relates to following a global standard of ethical behavior. This would be impossible to do because context does matter when deciding what is right and what is wrong.

Ethical imperialism, a more specific form of cultural imperialism, is one of a number of cognate terms that emphasize the superiority of one set of values over another. Absolute domination describes a situation where a person or nation seeks to control events. Situations such as this can arise in business, international politics, or medicine when one individual or group seeks to impose its will on the conduct of other people's affairs. Ethical imperialism can be seen in a practical sense in the field of international business when an organization engaged in increasing its market share or making a takeover bid imposes its ethical and moral standards on the target group. In the field of international politics, the appointment of carefully selected representatives to bodies such as the World Trade Organization, the World Bank, the International Monetary Fund, and the United Nations suggests to critics of globalization that the concept of ethical imperialism is active. In the four examples above, the newly appointed incumbents can be expected to pursue a predictable line. There is also a suggestion that these key positions are being shared out among competing power blocs.

Cultural imperialism, a cognate and broader term, has been in common usage for some time and is easier to understand. However, imperialism, whether it be ethical, moral, or cultural, means that people, organizations, and societies with power, influence, and authority can and do impose or force their ethical, moral, or cultural standards on situations and people with less power, influence, and authority. Values that in Western democratic nations are assumed to be wholesome and virtuous, such as liberty, freedom, the rule of law, an open society, and recognition of an individual's rights, are not so easily imposed on less developed countries. For example, there are at the time of this writing, August 2005, many Iraqis who are determined not to accept a Western democratic style of government. If the West forces or imposes its values on countries that are perceived to be poorer or morally inferior, there is the risk of a negative reaction. Values and beliefs are best transmitted indirectly through trade, commerce, and higher education, whereby thousands of graduates return to their home countries with an awareness of Western democratic values.

Western ethical imperialism (WEI) is a more specific form of cultural imperialism. It has been likened to civilized/rich countries—that is, the Anglo-American, European Union group—imposing their values on countries they perceive as being uncivilized/poor or, worse, morally inferior. North Korea, Iraq, Serbia, and some African and Middle Eastern states come to mind. Libya was considered to be in this group but has redeemed itself and now takes its place with the rest of the world. WEI can be illustrated by the way some people in some Western developed nations take the high moral ground with respect to the conditions in which young children work in some third-world countries. They make judgments with respect to working conditions in Middle Eastern countries based on their own frames of reference. They impose their moral and cultural standards on situations that are very complex. There are many examples in which these cases have been documented; however, the alternatives for a young child working for a pittance in a carpet factory in Pakistan or an export-oriented shoe factory in Brazil could be much worse. The key challenge for companies and individuals working in the international arena is to avoid the extremes of both ethical imperialism and ethical relativism.

—Michael W. Small

See also Cultural Imperialism; Ethical Culture and Climate; Globalization; Multinational Corporations (MNCs); Newly Industrialized Countries (NICs)

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Ethical Naturalism

Ethical naturalism is the view that ethical claims are either true or false and that their truth or falsity is determined by reference to the external world, either facts about human nature or facts about the physical world beyond humans. Ethical naturalism contrasts with ethical nonnaturalism, which is the view that ethical claims are either true or false but their truth or falsity is not determined by facts about the natural, physical world.

There are two main versions of ethical naturalism. The first can be called virtue-based naturalism. According to standard versions of this view, the question of which acts are right and which are wrong for a person to perform can be answered by appealing to claims about which acts would promote and which would undermine that person's living a life that is good for human beings to live. This is a natural approach to ethics as it purports to explain when an act is right or wrong in a fully natural way, without referring to any nonnatural source of moral value. This virtue-based naturalism is based on the view that there is a distinctive way of living that human beings are best suited to pursuing and that if they were to pursue this, they would flourish. The primary objection to such virtue-based naturalism is that there is no such distinctively human life, and so it is not possible to determine if an act is right or wrong in terms of whether it is in accord with such a life or not. It is also often charged that this approach to naturalism faces an epistemological difficulty: that even if there was a distinctively human life that could ground claims about the rightness or wrongness of actions in this way, we would not know what form it would take. However, even if this last objection is correct, that we cannot have this access to the rightness or wrongness of actions, it does not show that this naturalistic account of what makes an action right or wrong is incorrect. It just shows that we cannot know when an action is right or wrong.

The second version of ethical naturalism, which can be termed metaethical naturalism, is the view that moral philosophy is not fundamentally distinct from the natural sciences. This is the version of ethical naturalism that is most often understood to be at issue in discussions of the "naturalistic" approach to ethics. On this approach to naturalism, moral value—that is, roughly, the rightness or wrongness of an action—should be understood as being defined in terms of (or constituted by, or supervening on) natural facts and properties. For example, John Stuart Mill's utilitarian approach to ethics was a naturalistic approach of this sort. For Mill, an action was morally right insofar as it tended to promote happiness and wrong insofar as it failed to do so. Since for Mill happiness was defined in terms of pleasure and the absence of pain, which are natural properties, the rightness or wrongness of an action can be explained in terms of natural properties.

Although not all metaethical naturalists accept Mill's account of what explains the rightness or wrongness of actions, they all share his belief that moral values (such as rightness and wrongness) can be understood in terms of natural facts about the physical world. For such naturalists, moral claims should be understood in terms of features of the natural world that are amenable to scientific analysis. This does not mean that moral philosophy should become simply another branch of science. Rather, it simply means that there are likely to be regular or lawlike relationships between physical properties and moral properties. Moral claims are thus claims about natural facts about the world. Metaethical naturalism is thus a type of moral realism, the view that moral claims are not merely expressive statements but are literally true or false. Thus, when people say, "Price-gouging is morally wrong," they are not merely expressing their personal view concerning price-gouging. Rather, they are stating that they believe that it is a fact that price-gouging is morally wrong—and so, like other claims about facts, this moral claim (and all others) is either right or wrong.

Like virtue-based naturalism, scientific metaethical naturalism faces some serious objections. Some object that this version of naturalism is untenable because it is not clear how to derive ethical claims from descriptions of reality. But, as was noted above with respect to the epistemological objection to the virtue-based account of naturalism, this doesn't show that this naturalistic approach to ethics is mistaken. It just shows that we cannot know when an act is right or wrong.

A more famous objection to metaethical naturalism was offered by G. E. Moore. Moore claimed that naturalists were guilty of the "naturalistic fallacy." This fallacy was to draw normative conclusions from descriptive premises. Thus, since naturalists infer from the fact that an action has a certain natural property (e.g., it maximizes pleasure) that it has a certain moral, normative property (e.g., it is right and should be performed), they are, according to Moore, guilty of this fallacy. Naturalists respond to this objection by noting that they do not need to rely on only descriptive premises in their inferences from natural properties to moral properties. They could insert into such inferences a premise such as "Whatever act has natural property X is a right act." With this premise in place, the naturalists' inferences are not fallacious.

A similar objection to naturalism was offered by Moore in his "open question argument." Moore argued that any naturalistic account of a moral property would face the difficulty of explaining how it is that a person who understood both the naturalistic account and the moral property could still question whether the moral property was present when the natural one was. For example, a person who understood what it was to maximize happiness and understood what it meant for an act to be right could still wonder whether an act that maximized happiness was a right act. If, however, the rightness of an act was instantiated by that act's maximization of happiness, this question would not be open in this way, just as the question "Is this unmarried woman a spinster?" is not open. In response to this objection, metaethical naturalists note that the meaning of moral terms might not be as obvious to people who seem to understand them as Moore assumes. Thus, a person might be able to use moral terms correctly but still be ignorant of what criteria must be met for an act to be a right act. Such persons would be competent users of the moral terms they deploy but would lack the understanding that Moore assumes they have.

If ethical naturalism is true, this will have important implications for business ethics. If it is true that ethical claims are either true or false and that their truth or falsity is determined by reference to the external world, then there will be objective ethical truths that are independent of the beliefs of humans. If this is so, then it will not be true that ethical practices vary across cultures. For example, it will not be true that bribery is ethically acceptable in some countries, whereas it is not in others. Instead, there will just be one set of ethical practices that applies universally.

—James Stacey Taylor

See also Aristotle; Mill, John Stuart; Moral Realism; Moral Reasoning; Moral Rules; Utilitarianism; Utility; Utility, Principle of; Vice; Virtue; Virtue Ethics

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Ethical Nihilism

Ethical nihilism is the supposition that any philosophical discussion of ethics and values is meaningless because of the observable fact of moral diversity and disagreements. (Thus, ethical nihilism is a thesis about the philosophical treatment of values, while nihilism is about knowledge and values themselves.) What can often be observed is that what some people perceive as "good," others perceive as "evil," and still others are indifferent to it (for instance, abortion, the death penalty, or stem-cell research). From that evidence, ethical nihilism takes a more radical step than ethical relativism, which only goes as far as postulating that ethics is ultimately relative to the moral agent or observer. Ethical nihilism argues that, in the end, nothing matters in the moral arena. Many ethicists argue that ethical nihilism is a consequence of subjectivism, the view that each individual is the sole authority concerning the selection and applicability of ethical principles.

Arguably, in everyday organizational practice, ethical nihilism may manifest itself in amoral management. Managers are said to act amorally when they are indifferent to ethical considerations in their decision making. But because ethical norms and rules are irrelevant to ethical nihilists, the typical outcome may also be immoral management, with its consequent violation of ethical principles. Immoral managers are continuously tempted to find loopholes in existing legislation to benefit themselves. This downward spiral from amorality to immorality and illegality is easy to understand with reference to, or in the context of, ethical nihilism. For if ethics were ultimately meaningless and irrelevant, nihilists would regard the law merely as governmental fiat without any compelling normative force.

It is important to keep in mind, though, that ethical nihilism has been considered a viable philosophical tradition. Among the world famous philosophers subscribing to (or at least often interpreted as subscribing to) ethical nihilism are some influential German philosophers of the 19th century. For example, Friedrich Nietzsche (1844–1900) called for the devaluing of old values, such as pity or compassion. After what he called the death of God, Nietzsche expected Western societies to pass through a transitional period of ethical nihilism until new values would be created. He was quite clear, though, that this nihilist period was a pathological yet necessary transition in his proposed "transvaluation" of values. Another German philosopher often considered an ethical nihilist is Arthur Schopenhauer (1788–1860), with his pessimistic philosophical views. However, such a view of Schopenhauer's moral philosophy is actually a misinterpretation because Schopenhauer was quite clear, in his book *On the Basis of Morality,* that compassion is the sole criterion of morally worthwhile actions. This book harshly criticized Kant's categorical imperative, but it cannot be considered nihilist because it ultimately substitutes a virtue ethic for Kantian deontology. In opposition to Schopenhauer, Nietzsche rejected any morally affirmative view of compassion and believed, more closely following a nihilist philosophical line than Schopenhauer ever did, that there could be no cultural or human progress without slavery or cruelty. (Nietzsche's approval of cruelty and slavery cannot easily be reconciled with the classification of Nietzsche as a virtue ethicist by some current scholars, although admittedly the *ultimate* outcome envisioned by Nietzsche may, in fact, be a particular antidemocratic type of virtue ethics.)

The French postmodernists of the 20th century can be considered exemplars of ethical nihilism as well. Skeptical postmodernists often emphasize the meaninglessness of life and the lack of any ultimate normative parameters for human action. Philosophers such as Baudrillard and Foucault deny the existence of any truth, so they embrace not only ethical but also epistemological nihilism. In other words, they question and indict the foundation and, thus, validity of any knowledge claim, whether ethical or scientific. However, it is important to recognize that the entire postmodernist tradition is not morally nihilist. The French existentialists, such as Jean-Paul Sartre, and the so-called affirmative postmodernists, such as Richard Rorty, do affirm the superiority of certain value choices over others. More broadly, the differentiation between "skeptical" and "affirmative" postmodernists as well as between Nietzsche's and Schopenhauer's philosophy above suggests that attributions of nihilism generally are quite controversial and subject to different interpretations.

An important philosophical work that tries to break through the modern and postmodern forms of ethical nihilism is Alasdair MacIntyre's *After Virtue.* MacIntyre regards today's moral disagreements as rooted in rationally interminable differences that are emotive in character. Emotivism, or noncognitivism, argues that positive moral judgments, such as "This is good," are actually expressions of individual, subjective feelings and, thus, are equivalent to saying, "I approve of this; do so as well" or "Hurrah for this!" In the wake of the "invention of the individual" and the (according to

MacIntyre) inevitable failure of the modernist Enlightenment project, society has lost all context for valid moral judgments. Because MacIntyre considers any philosophical affirmations of rights or utility, for example, as fictions, they cannot really provide, in his view, criteria for the moral good and, therefore, are doomed to fail. His solution to the problem of nihilism was quite different from Nietzsche's. Instead of a subjective transvaluation of values, MacIntyre tries to retrieve virtuous communities (in *After Virtue*) and a Christian moral philosophy (in *Whose Justice? Which Rationality?*). To summarize MacIntyre's perspective, ethical nihilism is an inevitable consequence of emotivism, subjectivism, and relativism. Like many other orthodox philosophers, MacIntyre recommends a particular kind of communitarianism in overcoming the modern or postmodern nihilist condition. Unfortunately, such communitarian or collectivist "solutions" present dangers similar in magnitude to those engendered in Nietzsche's autocratic moral philosophy.

—Marc Orlitzky

See also Absolutism, Ethical; Ethical Imperialism; Nihilism; Noncognitivism; Relativism, Moral

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Ethical Role of the Manager

In a broad construction of the ethical role of the manager, managing and leading can be said to be inherently ethics-laden tasks because every managerial decision affects either people or the natural environment in some way—and those effects or impacts need to be taken into consideration as decisions are made. A narrower construction of the ethical role of the manager is that managers should serve only the interests of the shareholder; that is, their sole ethical task is to meet the fiduciary obligation to maximize shareholder wealth that is embedded in the law, predominantly that of the United States, although this point of view is increasingly accepted in other parts of the world. Even in this narrow view, however, although not always recognized explicitly, ethics are at the core of management practice.

The ethical role of managers is broadened beyond fiduciary responsibility when consideration is given to the multiple stakeholders who constitute the organization being managed and to nature, on which human civilization depends for its survival. Business decisions affect both stakeholders and nature; therefore, a logical conclusion is that those decisions have ethical content inherently and that managerial decisions, behaviors, and actions are therefore inherently ethical in nature. Whenever there are impacts due to a decision, behavior, or action that a leader or manager makes, there are ethical aspects to that decision or situation. While some skeptics claim that business ethics is an oxymoron, the reality is that decisions and actions have consequences, and that reality implies some degree of ethics, high or low. Thus, ethics and the managerial role cannot realistically be teased apart.

Ethical Leadership

The ethical role of managers, or what the business ethicist Linda Treviño and her colleagues call ethical leadership, is a combination of being a moral person and being a moral manager. Being a moral person rests on a combination of key traits such as integrity, honesty, and trustworthiness. Integrity involves not only forthrightness and honesty or truthfulness but also consideration for the soundness of the whole entity that one manages as well as of the society in which the organization is located. Integrity also means firm adherence to a code, such as an ethical code of conduct. Thus, being a moral person suggests that the individual has integrity and can be trusted.

In addition to these traits, being a moral person also involves behaviors such as doing the right thing, concern for people, being open, and standards of personal integrity. The essence of ethics, of course, is doing the right thing, especially under difficult circumstances, and that involves being able to reason well about what the right thing to do actually is. To be able to reason well about a difficult ethical situation, a person needs to be open to learning from multiple sources about the situation while taking care not to harm people and actually attempting to treat people well in the decision-making process or when decisions are being implemented. To be able to make good decisions ethically, an individual needs to have thoughtfully developed his or her personal set of standards or values, a personal code of conduct or integrity. Personal standards allow an individual to think through a decision with a clear rationale in mind.

When decisions involving ethical considerations need to be made, Treviño and her colleagues argue, the moral person sticks to her or his core values, tries to be objective and fair, exhibits concern for society and the welfare of those in society, and follows ethical decision-making rules. But being a moral person is not the only requirement for becoming a moral leader. Moral leadership also includes being a moral manager, which involves recognition that the leader or manager serves as a role model for others in all his or her duties. It also means providing rewards and discipline around the ethical and unethical decisions made by others, so that a clear message is sent about what behaviors are and are not acceptable in the organization or situation. In addition, moral management means communicating openly, explicitly, and frequently about ethics and values.

One question that frequently arises in considering the ethics of management is whether individuals can be considered moral leaders or managers in their work lives if they act unethically in their personal lives or vice versa. Considering that an individual's character is reflected in all his or her decisions and actions, such an inconsistency would reflect badly on the individual as a whole. The branch of ethical theory called virtue ethics explores this relationship in depth.

Ethical Decision-Making Frameworks

Managers in both large and small enterprises face difficult ethical situations daily as they attempt to do their jobs. Since management decisions inherently involve ethical considerations, however, it is important that managers recognize the ethical elements that are embedded in their day-to-day job functions. They need to be able to reason through ethical decisions, just as they would reason through any managerial problem facing them. Many times, ethics-laden situations involve issues that are clearly right or wrong when judged by the manager's or organization's values or code of conduct. Furthermore, most managerial decisions and actions are legal, although there are occasions when a certain decision would clearly go beyond legal boundaries and be illegal. Assuming that the law itself is just, these decisions are not really ethically problematic in that what to do to make an ethically sound decision is quite clear. In these cases, making a decision to break the law or to do something that disagrees with a code of conduct or set of values is clearly unethical. It is not difficult to know what the right thing to do is in such situations.

Ethical decision-making problems arise for managers and leaders when decisions involve a moral conflict—that is, a moral situation in which a person must choose between at least two equally bad choices, or when there are multiple ethical considerations, some of which conflict with each other. In such circumstances, which are common in business, the manager has to be able to think through the consequences and ethical implications of the decision thoroughly and mindfully so that the best possible decision can be made given the constraints, implications, and ethical considerations. If the decision itself cannot be reframed as a situation in which all parties can benefit—that is, a win-win situation—then the manager needs a decision-making framework to help.

To help managers think through ethical moral conflicts, the business ethicists Gerald Cavanagh and his colleagues have developed a decision-making framework that relies on the ideas of philosophers and ethicists and applies those ideas to business decisions. This approach combines four methods of ethical reasoning—rights and duties, utilitarianism, justice, and the ethics of care—into a framework that helps managers and leaders step through a logical thinking process to sort out the ethical dimensions of a difficult and inherently conflictual situation.

Rights and Duties

Rights are justifiable claims or entitlements, frequently based on the law or other authoritative documents, such as treaties and international declarations, that allow people to pursue their own interests. Rights can be viewed as the positive things that people are allowed to do, but they come with an obverse side as well, in the form of duties or obligations that go along with the rights. For example, in democracies, one right is the ability to vote. Along with that right comes the duty to exercise that right by actually voting. In many countries, employees are granted certain rights, such as the right to safe working conditions or a minimum wage, and employers have corresponding duties to ensure that these conditions are met. These rights are based on laws and regulations. Other rights are based on moral grounds and are frequently written into international treaties, such as the United Nations Declaration of Human Rights and the Natural Environment. Such rights include respect for human dignity, which enables communities, organizations, and societies to thrive. In using Cavanagh's ethical decision-making framework to assess a moral conflict, one question that needs to be asked involves rights and duties: Would this decision respect the rights and duties of the individuals involved?

Utilitarianism

A second way of reasoning through a moral conflict involves using utilitarian analysis, or assessment of the greatest good of the greatest number. This type of cost-benefit analysis is a very common management approach, but as the framework suggests, it may not be a sufficient basis by itself to make an ethical decision in a moral conflict. In a utilitarian analysis, the harms and benefits of a decision to the different parties that would be affected by the decision are evaluated, with some sort of weight given to the various harms and benefits that assesses their degree. Most utilitarian analysis focuses on the good of the group or collective as a whole over that of any given individual, unless the most serious harm is to the individual—for example, if the decision would be fatal to the individual. Putting the collective, which can include an organization's interest, over that of the individual avoids the problem of self-interest. A second question in the ethical decision-making framework for managers, then, would be as follows: Who will be affected by the decision and to what extent will the various parties affected by this decision be harmed or benefited?

Justice

Principles of justice are a third way for managers to reason about ethical decisions. Just decisions require fairness, equity, and impartiality on the part of decision makers, particularly with respect to the ultimate burdens and benefits that will accrue from the decision. The philosopher John Rawls has discussed the justice criterion in terms of a concept of what he terms distributive justice, which invites decision makers to make a decision behind a veil of ignorance that suggests that they do not know where in the system they will be after the decision is made. This veil-of-ignorance consideration forces managers to take into account the fairness of the decision to any party that will be affected. Similarly, the philosopher Immanuel Kant suggests that justice can be taken into account using the concept of "categorical imperative"; that is, one should only act a given way or make a given decision if the decision maker can agree that it would be all right if any person in a similar situation acted that way. Alternatively, one can think of the categorical imperative as asking the decision maker whether this action or decision would be all right if it became a universal law. In considering justice, then, decision makers have to ask, How does this decision square with the canons of justice?

Ethic of Care

In addition to assessing a moral conflict from the perspective discussed above, ethical managers and leaders also need to look at the impact of a decision on the network of relationships that will be affected. This perspective is called the ethic of care. Based on feminist writings, the ethic of care proposes that one's moral responsibilities vary according to how closely one is linked to other people. That is, if a person is very close to another person, say, a family member, there will be more moral responsibility for ensuring the well-being of the family member than the well-being of an unrelated person. In an organizational context, using an ethic of care, more consideration might be given to the impact of a decision on long-term employees, who are more tightly connected to the organization and its goals, than to its impact on newly hired employees.

Making Ethical Managerial Decisions

Managers, according to Gerald Cavanagh, can use a combination of ways of moral reasoning based on rights, justice, utility, and care when they face a moral conflict and when these different ways of reasoning conflict, as they often do. To decide effectively, managers need to take several factors into consideration as they weigh decisions based on the principles of rights, justice, utility, or care. For example, they can consider whether there are overriding factors in the decision. If a decision might result in the death of a person made one way and the unemployment of a group of persons made another way, then the overriding factor might be the life-death decision. There are, however, no clear rules for making such decisions, and the judgment of the decision maker is needed to determine which of the relevant factors should carry the most weight.

Another consideration is whether one criterion is more important in a particular situation than others. For example, if the rights of a whole group of people are to be overrun by a decision, that factor might override the fact that one or two individuals would not be treated fairly when the decision is made. Similarly, a consideration might be whether there are incapacitating factors (such as force or violence) that would come into play in making the decision—for instance, to stop a strike, which might violate a person's right to strike but forestall the destruction and injury if the strike turned violent. The decision can be considered ethical when there is no intent to make an unethical decision, when a bad effect is simply a by-product, and when the good outcome is sufficiently good that it outweighs the bad.

Other decision-making aids for managers include thinking about whether they would want their decision made public—for example, to appear on the front page of a newspaper or on television. If they are uncomfortable with such transparency, it would be well to apply an ethical analysis to the decision. For managers operating in different countries around the world, it is useful to remember that virtually every nation of the world has at its core some version of the Golden Rule: Do unto others as you would have others do unto you. By keeping some of these principles in mind, managers can avoid the problem of relativism in their decision making. Relativism suggests that a decision is all right if it is apparently culturally acceptable, irrespective of the consequences or harms.

Moral Development

The ethical decision making framework for managers relies on reasoning using the principles of rights, justice, utility, and care. It presupposes that managerial decision makers have the capacity to reason from principles in making an ethical decision. Unfortunately, not everyone reasons from moral principles in making ethical decisions. A good deal of research on individual development suggests that people develop their cognitive reasoning skills over time and to different levels, generally termed preconventional, conventional, and postconventional.

Research on moral reasoning in men by Lawrence Kohlberg and on women by Carol Gilligan indicates that moral reasoning passes through similar stages, lagging behind cognitive development, which must come first. At the preconventional stage of development, the rationale for ethical decision making is rewards and punishments or self-interest. Most managers have passed beyond the preconventional stage to the conventional stage of development. In the early stages of conventional reasoning, individuals use their peer group as a reference point for determining what is right and wrong. At the later stages of conventional reasoning, individuals focus on the rules, regulations, and norms of society as bases for their ethical decisions. Only at the postconventional stages of development, which only about 20% of adults reach, does reasoning from principles emerge.

Reasoning from moral principles is a relatively high-level or postconventional skill. The fact that only about 20% of adults reach the postconventional level of development highlights the need for ethical leaders and managers who are able to reason not just from society's or their peer group's norms but also from core principles such as those discussed above so that decisions can be made with multiple stakeholders' needs and interests in mind. Some of the needed principles are laid out in organizational or more generalized codes of conduct, which can also help managers in their decision-making roles.

Codes of Conduct

Most large corporations today have developed codes of conduct internally, which are intended to provide guidance for managers confronting ethical situations and moral conflicts. Such codes of conduct need to be supplemented by internal systems, such as reward and information systems, promotion and hiring practices, recognition systems, and organizational culture and communication systems, that support their implementation. Strong top management commitment to and communication about values and ethical conduct is a core element of ethical leadership from the top of the organization. Ethical leadership is essential to managers and employees at all levels of the enterprise when they are faced with difficult ethical decisions and moral conflicts. Codes of conduct alone can seldom be sufficient for managers to come to good decisions unless they are supported by these other aspects of the organization.

In addition to company or organizational codes of conduct, many of which have been developed internally by companies to articulate their own value systems, a number of codes and principles have emerged globally to help managers think about their ethical responsibilities. Some of these are quite spare and lay out fundamental principles, based on globally agreed-on documents signed by many nations, such as the United Nations Global Compact with its 10 core principles or the OECD Guidelines for Multinational Enterprises. Others are more elaborate and have been developed by business groups or multisector alliances to help guide business decision making. Again, as with internal codes of conduct, these principles are helpful guides but cannot address every unique situation. As a result, codes need to be supported by the organization's managerial decision making, its culture, its reward systems, and the communication that exists about ethical practices within the firm.

Managers and Ethics in Organizations

Many managers find it difficult to speak about and sometimes even recognize ethical issues, a difficulty that the management theorists James Waters and Frederick Bird called the moral muteness of managers. Recognizing that management is an inherently ethical task and that the practices of the company embody a set of values or ethics, the management scholar Jeanne Liedtka suggests that there does exist a set of ethically based management practices that can help managers lead their companies effectively and so that they are competitive. By examining numerous organizational improvement initiatives, she determined that they shared common practices and common sets of values that could help an organization achieve its goals most effectively.

The ethics of effective and competitive business practices identified by Jeanne Liedtka include creating a shared sense of meaning, vision, and purpose that connect the employees to the organization and are underpinned by valuing the community without subordinating the individual and seeing the community's purpose as flowing from the individuals involved. A second characteristic that ethical leadership can provide is developing in employees a systems perspective, which is linked to the postconventional stages of cognitive and moral reasoning discussed above, so that a value of serving other community members and related entities in the broader ecosystem emerges. Another theme is that of emphasizing business processes rather than hierarchy and structure, which is based on valuing work itself intrinsically and focusing on both ends and means in decision making, not just the ends. Localized decision making, particularly around work processes, provides a value of responsibility for individual actions, and using information within the system is supported by values of truth telling, integrity, and honesty, the characteristics of moral persons, as well as transparency about and access to needed information.

Organizations with these types of ethically based approaches also focus on development for both employees and the organization as a whole, which means valuing individuals as ends, not as means to ends (a key ethical principle), and focusing on learning and growth. Such approaches also encourage dialogue and related freedom of expression with a commitment to seek common ground when there are differences of opinion. Ethical leaders can also foster the capacity of others and themselves to take multiple perspectives simultaneously—in other words, to move toward postconventional levels of reasoning so that they can understand other points of view and make better decisions. The final element that managers can think about in their roles as ethical leaders is creating a sense of commitment and ownership among organizational members by emphasizing promise keeping, instilling a sense of urgency about the tasks of the enterprise, and encouraging engagement rather than detachment among organizational members.

—Sandra Waddock

See also Ethics, Theories of; Ethics of Care; Fairness; Justice, Theories of; Kohlberg, Lawrence; Leadership; Management, Ethics of; Rights, Theories of; United Nations Global Compact; Utilitarianism; Virtue Ethics

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Ethics, Theories of

Ethics is the branch of philosophy that deals with morality. Ethicists are concerned with a wide range of topics, such as human nature; the meaning of life; the nature of value; how judgments are made; how judgments can be improved; how moral attitudes arise and change; and the workings of morally significant mental states such as love, hate, greed, envy, indifference, pity, desire, aversion, pleasure, and pain. Moral or ethical theories offer the means of understanding significant elements in these and other areas of inquiry.

Ethical theories tend either toward merely describing or toward both describing and judging. As a result, some moral theories seem to belong to anthropology, psychology, or sociology, while others look like instances of what ethics purports to study—that is, like moral doctrines or judgments. For this reason, a major distinction employed by moral theorists distinguishes descriptive from prescriptive, or normative, theories, or elements of theories.

Moral judgments tend to state that something is either good or bad or that something agrees or conflicts with our obligations. Consequently, a major division in moral theories is between theories of value (axiology) and theories of obligation (deontology). In each area, ethicists want to determine the meaning of moral judgments, their truth or falsity, their objectivity or subjectivity, how judgments are made, how they can be tested, how they can be justified, and the possibility of organizing judgments under first principles. A third major distinction places theories about the meaning of moral judgments in a category of their own called metaethics. Obviously, metaethical questions arise in all areas of ethics.

Prescriptive or normative moral thinking recommends at least one moral evaluation, or else it attempts the same for at least one moral obligation. Plato, Aristotle, the Stoics, the Epicureans, and the Cynics sought both to find the best kind of life and to strongly recommend the judgment that it was in fact the best. Others, such as Immanuel Kant, theorized about the nature of obligation and also provided grounds for justifying or recommending certain obligations. The theories of David Hume, Arthur Schopenhauer, Darwinism, and Logical Positivism exemplify the tendency to separate the task of description from that of prescription, or to eschew prescription altogether, in order to describe and organize moral judgments for the sake of understanding alone.

The unwavering pursuit of the metaethical question of the meaning of moral judgments brought many recent philosophers to the conclusion that moral judgments are not the sort of statements that can be true or false but instead express resolutions, preferences, feelings, demands, or other states of mind. Hume thought that they reported subjective feelings, so that a judgment such as "Insider trading is immoral" would not be understood as ascribing a predicate to insider trading but as saying something like "I disapprove of that act." A. J. Ayer, a Logical Positivist, believed that moral judgments did not report feelings but merely expressed them. For him, the statement "Insider trading is immoral" merely expresses a negative emotional reaction to stealing—along the lines of "Boo insider trading!" Such expressions are neither true nor false because they do not describe anything. Hume and Ayer represent the school known as Emotivism. A neighboring school, Prescriptivism, interprets "Insider trading is immoral" as an imperative, "Do not engage in insider trading," which is neither true nor false because it is a command rather than a description.

In value theory, the primary questions are first about the meaning of value terms, then about the status of value. With regard to meaning, the first question is whether value or goodness can be defined and, if so, how. For Plato and W. D. Ross, the good is indefinable, yet it names an intrinsic property of things, making it objective. For the Intuitionists, such as G. E. Moore, value is indefinable, objective, and absolute. Many ethicists believe that value can be defined so as to name something that is both objective and absolute, as did Aristotle, who defined the good as that at which all things aim. For others, the good has its seat in subjectivity and will be different for different persons or groups.

After the meaning and status of value, the chief concern in value theory has been the question of which things are of the highest value. The main answers have been a state of feeling, such as pleasure or satisfaction (Epicurus, Thomas Hobbes, John Stuart Mill); a state of the will, such as virtue (Epictetus) or power (Friedrich Nietzsche); or a state of the intellect, such as knowledge (Plato) or good intentions (Kant).

In the theory of obligation, similar questions have been posed. With regard to questions about the meaning and status of "right" and "wrong," Intuitionists hold that they name an indefinable, objective quality. Emotivists believe that right can have only an emotive, subjective meaning. Psychological and social thinkers typically hold that judgments of right and wrong indicate the attitudes of some person or group toward an act.

In response to the question of which things are right in the sense of their being morally obligatory, there are both teleological and nonteleological answers. For the teleologist, an act is right according to how much good it brings, or will probably bring, into the world. For the egoist, the amount of good brought to the agent is decisive (Epicurus, Hobbes), while for the universalist, it is the amount brought to the world as a whole (utilitarianism). Meanwhile, Thomas Aquinas and others have argued that an act is right according to its intent, so that an act with a comparatively better intent is a comparatively more righteous act. All these answers to the question of what is obligatory rely on a theory of value and, thus, make deontology dependent on axiology.

A fully deontological theory is supposed to hold that an act is obligatory regardless of its consequences for human happiness, ends, or other values. Deontologists, such as Kant, hold that right conduct can be determined by considering a priori principles, such as rights and laws. Kant's view was that objectively right conduct could arise from many sources, such as benevolence, prudence, or habit. However, the highest and the only morally significant motive for right action was respect for the moral law. If a course of action suggested by benevolence, pity, sentiment, or any other motive conflicted with the course indicated by moral law, respect for moral law ought to win out. The good will, the will truly searching for its duties so as to fulfill them, is supremely good for Kant, and the moral worth of an act is always guaranteed by the agent's intent to follow the moral law, regardless of any other motive or consequence.

Deontology is squarely opposed to teleological approaches to obligation because it holds that the end can never justify the means. Hence, violating another's rights cannot be justified by its serving a praiseworthy goal. Consequentialist theories, such as utilitarianism, hinge the goodness of conduct to its consequences and, hence, seem prepared to overlook a violation of rights as long as the consequences of the violation are highly valuable. In contrast, it has been said that the deontologist's motto appears to be "Let justice be done though the heavens fall." Kant argued that one must not lie even to save the life of an innocent man and that one must not commit suicide even when life has no further meaning or purpose. For Kant there can be no exceptions to moral laws because if they are to count as moral laws, they must at a minimum be universalizable. Hence, if suicide is immoral when life has purpose, it must also be immoral when it does not, and if lying to obtain a loan is immoral, lying must also be immoral in life-and-death situations.

Another version of deontology comes from theology, in which our moral duties are given by a deity. Divine command theories hold that regardless of any consequences for life or limb, we must do what the deity commands.

Virtue ethics is often described as an alternative to normative deontology because its normative elements concern the qualities of persons rather than the qualities of acts. Plato, Aristotle, and many Eastern systems of thought focus on what kind of person one ought to try to be rather than on which actions one ought to take or avoid. For Aristotle, who understood ethics as the branch of learning concerned with achieving the good life, the virtues are precisely those characteristics that make the character good and that lead to the good life. These include courage, prudence, wit, truthfulness, temperance, and justice, among others. Its detractors often say that virtue ethics is dependent on prescriptive moral judgments yet offers no insight into them.

Beyond theories of value and obligation, ethicists examine moral reasoning in their efforts to understand how our conduct is chosen and how moral judgments are or ought to be made. According to the Emotivists, a moral judgment comes about when one looks at an act or policy, consults one's sentiment, and pronounces morally about it. For teleologists, moral judgments are or ought to be made by considering the comparative amount of good or bad that an action can or does bring about. For Kantians, moral judgments ought to be made by considering the one obligation that determines all others—namely, to act so that you can at the same time honestly will that all others would act as you do. For divine command theorists, the will of the deity must be consulted in making accurate moral judgments.

One of the greatest challenges to all normative ethical theories lies in the problem of free will. We generally consider acts praiseworthy or blameworthy only if their agent could have acted otherwise. If we lack free will, we are apparently never able to do otherwise and, hence, our acts do not deserve either praise or blame. The school known as Compatibilism argues that belief in the moral status of human acts is compatible with an absence of free will. Incompatibilists, such as Nietzsche, argue that if we lack free will, statements about the moral status of human acts perpetuate a cruel myth.

A second, more contemporary challenge to normative ethics arises from the question of whether there are moral facts in the world and, if there are, whether moral judgments describe them. Moral realism answers that there are moral facts and that our judgments can describe them, and thus affirms at least three things: (1) that moral judgments are propositional, meaning that they can be either true or false because they attempt to describe features of the world; (2) that there are moral facts to be described; and (3) that moral facts are objectively present in the world, independent of our thoughts and feelings. Noncognitivism in ethics holds that moral judgments do not describe, and so are nonpropositional, and thus can be neither true nor false.

—Bryan Finken

See also Absolutism, Ethical; Aristotle; Cognitivism and Ethics; Consequentialist Ethical Systems; Darwinism and Ethics; Deontological Ethical Systems; Divine Command Theory; Free Will; Goodwill; Hobbes, Thomas; Hume, David; Intrinsic Value; Intuitionism; Kant, Immanuel; Kantian Ethics; Mill, John Stuart; Moral Realism; Moral Reasoning; Positivism; Relativism, Cultural; Relativism, Moral; Social Contract Theory; Utilitarianism; Vice; Virtue; Virtue Ethics

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Ethics & Compliance Officer Association (ECOA)

The Ethics & Compliance Officer Association (ECOA), formerly known as the Ethics Officer Association, is a nonconsulting, member-driven association established exclusively for individuals (i.e., ethics and compliance officers) who are responsible for their company's ethics, compliance, and business conduct programs. As the first global organization designed to serve the needs and interests of ethics and compliance officers, the ECOA provides training and hosts a variety of conferences and meetings for exchanging best practices. As of February 2006, the ECOA consisted of more than 1,250 members, representing nearly every industry. Member companies include more than half the Fortune 100 conducting business in more than 160 countries. In addition to corporations, ECOA membership includes nonprofit organizations, municipalities, and other organizations. The ECOA is headquartered in Waltham, Massachusetts.

The ECOA was officially launched in 1992. Its establishment was primarily based on two key developments, the Defense Industry Initiative (DII) and the U.S. Federal Sentencing Guidelines for Organizations (Guidelines). First, following allegations of waste and fraud in the U.S. defense industry in the mid-1980s, a blue-ribbon commission concluded that defense contractors must promulgate and enforce codes of ethics that address defense procurement problems and procedures as well as develop and implement internal controls to monitor these codes of ethics. As a result, the DII was created, made up of the largest defense contractors. Together they developed a model for internal ethics and compliance programs that were designed to prevent and detect waste, fraud, and other wrongdoing. The DII also created a network of executives who were responsible for each company's ethics and compliance program.

Following the DII, other companies in other industries also began to reflect on the importance of having an executive responsible for their ethics and compliance programs. The primary reason was the promulgation in November 1991 of the Guidelines. Not only did the Guidelines raise fines for white-collar crimes; they also provided a means for greatly reducing these mandatory fines. Under the Guidelines, if a company is determined to have in place an effective program for preventing and detecting wrongdoing, the fine can be reduced by up to 95%. One of the seven minimum elements in the Guidelines for an effective program was for organizations to have someone in place (high-level personnel) to be responsible for the oversight of the program. A sufficient justification for the establishment of a new ethics profession, the ethics officer, and the concomitant need for a networking organization for these professionals, now existed. However, although the DII provided a forum for defense contractors to share best practices, no multi-industry network existed.

The first meeting that led to the creation of the ECOA was held at Bentley College, in Waltham, Massachusetts, in June 1991. The meeting was co-hosted by the Center for Business Ethics and the Dreiford Group, with about 30 ethics officers in attendance. The group decided to create a new organization for peer-to-peer discussion, and on June 17, 1992, the ECOA officially filed as a 501(c)(6) nonprofit, Delaware-based corporation. At the time of incorporation, 19 companies were ECOA sponsoring partner members. Although originally named the Ethics Officer Association, the name was officially changed to the Ethics & Compliance Officer Association on January 13, 2006.

The ECOA has a mission statement, vision, and set of values. The mission states that the ECOA is committed to being the leading provider of ethics, compliance, and corporate governance resources to ethics and compliance professionals worldwide and to providing members with access to an unparalleled network of ethics and compliance professionals and a global forum for the exchange of ideas and strategies. The vision of the ECOA is to be the recognized authority on business ethics, compliance, and corporate integrity. The ECOA's set of values include (1) integrity, (2) confidentiality, (3) collegiality, and (4) cooperation among the ECOA members.

The ECOA defines an ethics and compliance officer as an individual tasked with integrating the organization's ethics and values initiatives, compliance activities, and business conduct practices into decision-making processes at all levels of the organization. In general, ethics and compliance officers assist employees at all levels of the organization to determine the right course of action in difficult situations.

Membership in the ECOA is open to those who are recognized by their organization as having the assigned role and responsibility for devising, implementing, or administering their organization's ethics, compliance, or business conduct programs. The ECOA offers two types of membership, sponsoring partner and basic member. The ECOA offers peer-to-peer networking the main goal of which is to create more awareness of ethics by discussion through conferences, education programs, a job-listing program, and networking events and seminars among a network of individuals from a wide variety of industries. The types of events held by the ECOA include (1) sponsoring partner forums, (2) the annual conference, (3) ECOA/U.S. Sentencing Commission forums, (4) training in "Managing Ethics in Organizations," (5) seminars on "Creating an Ethical Corporate Culture," and (6) Webcasts.

The ECOA engages in a number of other additional activities, including conducting research on corporate ethics and compliance, assisting in the provision of ethics administrative software, and providing members with an e-mail newsletter. In 2004, the ECOA's board of directors endorsed the "Standards of Conduct for Business Ethics and Compliance Professionals," which detail members' obligations to their organization as well as to the profession.

The ECOA has formed partnerships and alliances with the U.S. Sentencing Commission and leading ethics centers and subject matter experts. The ECOA has also entered into memoranda of understanding with other business ethics associations, including the Business Ethics Research Center (BERC) in Japan, the Cercle d'Éthique des Affaires–Cercle Européen des Déontologues (CEA-CED) in France, the Ethics and Compliance Custodian Organisation (ECCO) in South Africa, and the Institute of Business Ethics (IBE) in the United Kingdom. The ECOA collaborates with the BERC, CEA-CED, and ECCO in organizing meetings and conferences, developing surveys and research, and assisting in expanding each other's libraries and Web sites.

Recent U.S. regulatory initiatives such as the Sarbanes-Oxley Act of 2002 and amendments to the Federal Sentencing Guidelines for Organizations 2004 continue to reinforce the importance of having an ethics officer in an organization. Empirical evidence is also beginning to suggest that the existence of ethics officers, as part of a comprehensive ethics and compliance program, may help reduce the extent to which illegal and unethical behavior takes place in organizations.

—Mark S. Schwartz

See also Codes of Conduct, Ethical and Professional; Corporate Ethics and Compliance Programs; Corporate Governance; Ethics Training Programs; Federal Sentencing Guidelines; Global Codes of Conduct

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Ethics and the Tobacco Industry

Health advocates assert that tobacco is the first or second leading cause of preventable death among humans, contributing to cancer, lung disease, and coronary heart disease, among other ailments, and that the addictive properties of cigarette ingredients prevent smokers who desire to quit from doing so. While cigarettes are the primary culprit, other tobacco products, such as cigars and pipe tobacco, are potentially equally or even more dangerous, but because they are less prevalent, they do not pose public health risks on the same scale as cigarettes. Smokeless (chewing) tobacco is said to cause other health problems, such as mouth cancer. The risks of tobacco use are not limited to users of tobacco, since carcinogens, or cancer-causing agents, can be passed on to others through second-hand smoke and from a pregnant or nursing mother to her child; cigarette smoking contributes to an inordinate share of building and house fires, and the health care costs associated with tobacco are borne by the public at large. As a result of these health and economic risks, governments and nongovernmental organizations have increasingly treated tobacco as a public health hazard and have sought to economically impair the tobacco industry through aggressive regulation and litigation, thus reducing its harmful impact.

For decades, the big tobacco companies sought to downplay the health risks of tobacco products and categorically to deny claims that their products were addictive. In stark contrast to the health realities, various brands of cigarettes were associated through advertisements with social sophistication and glamour, friendship, rugged outdoorsmanship, recreation, and, generally, the good life. Historically, tobacco's place in society was more complex, a traditional pleasure among the native peoples of the Americas transported by explorers to Europe and then by commercial sailors to the Middle East and Asia. In these regions, tobacco took hold among the populace but received a mixed reception among political and religious leaders, who saw it as a pagan vice. As the global market for tobacco grew, however, its economic value became clear, and it became a key commodity grown and exported by European settlers in the southern United States as well as an exotic import from afar, hence the even contemporary references to "Turkish" and "Oriental" leaf and the famous Camel brand with images of the Near East. After industrialization, tobacco became an important enough commodity for political interests to coalesce to defend it from its detractors, for if big tobacco were suddenly to falter, the consequences for tobacco-dependent economic actors would be potentially catastrophic. At stake were the livelihoods of low-paid field laborers, high-paid executives, and those within the supply and distribution chains that linked them. Also at stake were an aesthetic view promoted by proponents of the smoking lifestyle and the search among researchers and developers for the perfect flavor. In recent years, faced with mounting regulatory pressure and litigation, big tobacco companies have become more transparent about the health risks and have been exploring new forms of innovation in product development and social responsibility to prop up their increasingly perilous economic reality. Fascinatingly, and possibly too late to flourish again, the tobacco industry has both been the target of the full range of ethical criticism that can be directed at business and demonstrated the potential for business to engage more constructively in the ethical debate on whether there is a place for dangerous products in the good life.

Ethical Criticism of the Tobacco Industry

The ethical criticism directed at the tobacco industry begins with the fact that its products are unhealthy, whether or not consumed in moderation. While other consumer goods pose risks to consumer well-being—for example, household cleaners may contain hazardous chemicals; prepared snacks may be high in sodium, fat, or sugar; and consumer electronics pose modest dangers to the laypersons who install them—the direct costs to individuals and the associated external costs to society of smoking cigarettes are perceived by critics to disproportionately outweigh any compensating benefits. Used as directed, cigarettes are high-probability, high-impact risks that are not only fundamentally unsafe but even more unsafe the more they are used.

In a free society, consumers generally are perceived to have the right to "choose their poison," but another ethical concern posed by cigarettes is that consumers may not have unfettered choice. Critics have charged that in the past decades, tobacco companies concealed evidence about the health risks of their products; manipulated studies to understate those risks; adjusted product formulae to increase the potency of nicotine, an addictive ingredient; and publicly denied that their products were addictive to fend off public concern and oversight by drug regulators. Not only were consumers making decisions about smoking based on incomplete information; those smokers who wished to quit were in effect incapable of free choice while battling addiction. The concern for consumer choice is even more pronounced with minors, who, even with complete information available to them, may make irrational choices when bombarded with advertisements that speak louder of the attractiveness of the smoking lifestyle than volumes of less accessible scientific data speak of the risks. Critics have further charged that advertising in sports venues inaccurately implies that cigarettes can be integral to a healthy lifestyle and that using cartoon characters as spokespersons specifically encourages youth to smoke. Until the early 1990s, tobacco representatives commonly took the position that restrictions on advertising restricted free speech, but this debate has for the most part been settled in favor of substantial restrictions as a matter of public interest.

Less unique to the tobacco industry but relevant nonetheless is the vulnerability of tobacco products to counterfeiting, in which inauthentic products bear name brand packaging, and the gray market, in which authentic products are purchased inexpensively in one market and subsequently diverted to be sold at below-market prices in a more expensive market. Cigarettes are vulnerable to these schemes in part because price gaps are significant from market to market due to varying regulatory practices and tax premiums and partly because the per unit price is reasonably high relative to the physical size and weight of the product. While tobacco manufacturers may not accept responsibility for these business practices, critics have charged them with complicity and with keeping suspect company. Another affair in which tobacco's role was too coincidental to ignore concerned the leveraged buyout of the tobacco giant RJR Nabisco in 1988, in which some company executives sought personal financial windfalls that would have entailed actions that were of dubious value to the company and the well-being of its employees. This episode occurred at the tail end of a decade in which investment bankers and junk bond traders rose and fell and prefigured the accounting scandals of the turn of the next century, in which executives benefited at the apparent expense of other stakeholders.

Constraints on Industry Growth

At the heart of the tobacco controversy is the question of whether the mere fact of consumer demand for cigarettes justifies the continued supply. This economic question has been answered in the affirmative to justify the market for firearms, pornography, violent entertainment, and other ironically labeled consumer "goods." The question includes consideration of manufacturers' and marketers' potential moral obligation to attempt to shape consumer perceptions regarding what will promote social well-being. While most free market theorists would contend that companies taking on such a moral obligation would smack of paternalism, tobacco companies have nevertheless, through marketing and advertising campaigns, shaped consumer perceptions regarding the place of cigarettes in the good life. Critics have suggested that in doing so they have kept the demand for cigarettes artificially high by allowing nicotine addiction to perpetuate consumer dependence on them and by withholding data that would allow consumers to make informed choices.

Because tobacco products have been part of the fabric of social relations and consumer habits since well before the health risks were documented, they bred cultural dependence among consumers, which led to economic dependence among suppliers. In the recent heyday of the industry's growth, spanning the third quarter of the 20th century, this economic dependence was rather a matter of economic flourishing, with Philip Morris, RJR Nabisco, British American Tobacco, and some of their lesser-known competitors among the United States' and the world's most financially successful corporations, enjoying brand visibility, strong margins, a solid consumer base in developed countries, and prospects for continued growth in untapped markets. The ubiquitous availability of cigarettes in large retail outlets, convenience stores, restaurants, and vending machines—anywhere the multipack-a-day consumer could obtain them to satisfy the need—required a complex supply, distribution, and sales network that could get the cigarette from the tobacco fields to the space between the smoker's second and third fingers. Consumers' smoking habits supported, among others, growers and harvesters, processors, truckers and shippers, paper suppliers and packagers, advertisers and marketers, warehousers, sales agents, and retailers—from grocers to gas station clerks to restaurateurs, who stood to pocket more when diners who smoked lingered at the table longer, ordering a few extra drinks.

An extension of the economic argument in support of the tobacco industry has thus been that any interference in this complex economic system would have unintended, harmful consequences for all these actors. To illustrate the complexity of this system, consider that tobacco farmers long benefited from governmental subsidies and that debate over the continuation of those subsidies was complicated by the fact that ending them might actually increase tobacco production (to compensate for lower margins with higher quantity) and lower prices (leading to increased consumption). However, in recent decades, regulation of the tobacco industry, especially in the United States, has accelerated, catching up with and finally surpassing the rate at which the tobacco companies envisioned their own expansion.

This regulation includes taxes and tariffs on tobacco products, which have grown to the point that as much as 80% of the cost of a pack of cigarettes in countries such as Denmark and Portugal and routinely more than half the retail price in many developed countries including the United States goes to government entities. The justification for such high taxes includes the argument that high product costs deter excessive smoking and the right of the government to recover costs that it will inevitably have to incur for the provision of health care. Also, the demand for cigarettes among young people has been demonstrated to diminish significantly with price increases. Historically, however, the tobacco industry has argued, to little sympathy, that these taxes were discriminatory since smokers are on average poorer than nonsmokers and thus spend a disproportionate amount of their income to support their habit. Notably, the percentage of the retail price that goes to taxes tends to be substantially lower in less prosperous countries.

As far back as 1954, personal injury litigation in the United States has cited adverse health effects caused by the tobacco industry, but until the 1990s, such litigation was largely unsuccessful given the relative inconclusiveness of scientific data and the imbalance of legal resources brought to the cases by the tobacco companies in comparison with what individual plaintiffs could afford. However, by the mid-1960s, the antitobacco movement took an important, if isolated, step forward when in the wake of a surgeon general's report on tobacco health risks, the Federal Trade Commission (FTC) instituted a new rule that finally resulted in warning labels appearing on cigarette packs and advertisements concisely affirming the risks posed by the product. The tobacco companies contended that if tobacco products posed any dangers, then they were no different from many other consumer goods that pose dangers to those who use them, but the FTC countered that there were no safe levels of cigarette consumption.

Tobacco companies continued with a united front to balk in the absence of conclusive clinical evidence in support of the surgeon general's claims, appealing to an age-old philosophical debate over whether any scientific evidence can ever properly be deemed conclusive, denying first the apparent link between tobacco and lung cancer and eventually the apparent link between nicotine and cigarette addiction. Despite this resistance, the report was seminal in opening the door to new regulatory strategies requiring tobacco companies to take actions, such as disclosure of risks, seemingly contrary to their own interests. Concern for the welfare of minors later resulted in regulatory proposals to restrict the placement and content of cigarette advertisements. Notwithstanding the written warnings on their products, tobacco companies continued to challenge their validity in other forums, but by the 1980s, the FTC had approved a rule requiring rotating written warnings on cigarette packages and ads that somewhat more explicitly depicted the direct and indirect risks of cigarettes to consumer, including fetal, health. In 1993, when the Environmental Protection Agency declared smoke to be a carcinogen, it was clear that the industry was increasingly subject to the scrutiny of multiple regulators. Nevertheless, as recently as 1994, tobacco executives summoned to testify before Congress uniformly denied that cigarette smoking was addictive and were successful, at least temporarily, in stonewalling the Food and Drug Administration's (FDA's) attempts at appropriate regulatory oversight of tobacco. But the increasing tide of public concern and class action personal injury litigation led finally to a breaking of the ranks among the leading producers of tobacco, so that in 1996, Liggett, then the smallest of the five major tobacco companies in the United States, settled health claims with several states and publicly admitted the deadly potential of tobacco use. These and other developments culminated in the historic Master Settlement Agreement of 1998 (MSA) between participating manufacturers and 46 state attorneys general and six U.S. territories (the other states were covered in separate agreements). Among other provisions, the MSA spelled out restrictions on the placement and content of advertisements, particularly restricting any venues and branding characters that would appeal to young people; lobbying activity; cigarette pack sizes; merchandising; and other activities that in effect seek to expand the consumer market for tobacco products. In addition, the MSA contained provisions for public access to information; the establishment of a national foundation for further coordinated public education and study on tobacco health risks; and payments for Medicaid reimbursement—the original focus of the MSA, thus illustrating the enhanced power of litigation to twist the arm of big tobacco. Once again, however, unintended consequences have caused an ironic intersection of interests, as state budgets for even non-health-related expenditures have benefited from the influx of tobacco industry funds, which would dissipate if the industry were to collapse.

The incentive for tobacco companies to enter into a settlement so evidently contrary to their interests was to reduce the litigation burden and potential share price volatility associated with fighting numerous similar cases, but the MSA has not led to a cessation in litigation against the tobacco industry within the United States. Internationally, there are few, if any, legal systems as conducive to class action and product liability litigation as that of the United States, so while the momentum for legal action against tobacco companies has not waned, there remain questions about the extent of the international threat to tobacco industry interests. The 2005 World Health Organization Framework Convention on Tobacco Control has sought to provide model instruments for its 168 signatory countries to enact legislation to reduce the demand for tobacco products through price and nonprice measures and also to reduce its supply by inhibiting illicit trade activities and sales of tobacco to minors.

Local interests have also sought action against tobacco, as demonstrated by the 2003 ban in New York City on tobacco use in all workplaces and most public venues, such as restaurants and bars, which as a sign of the times stimulated more copycat legislation than did a similar 1985 ban in Vail and Aspen, Colorado. Whereas bars were once a smoker's haven and restaurant space was long governed by an imaginary demarcation between smoking and nonsmoking sections, smoking is now increasingly a private activity, or when done in public, it is relegated to places such as sidewalks, where the space between smokers and nonsmokers is less simple to define. Well before the New York City legislation in bars and restaurants, smoking was banned from other public spaces, such as airplanes, and many workplaces.

Investors have further punished tobacco companies through nonlegal means by filtering tobacco stocks out of so-called socially responsible investment funds. Along with alcohol, defense contracting, gambling, and firearms, tobacco industry stocks are routinely classified as "sin" stocks, which are excluded from socially responsible investing (SRI) portfolios. While SRI capital continues to be a relatively minor proportion of the overall investment capital, that proportion is gradually increasing and represents yet another squeeze on tobacco companies' operating margins.

Preventing Asphyxiation

Far from eliciting sympathy for tobacco companies, the pressures from outside that seem to be contributing to the slow and painful asphyxiation of the tobacco industry—witness the 50% reduction in smoking rates among men in the United States, Canada, and the United Kingdom between 1960 and 2001—are increasingly being applied to other consumer goods. Increasing consumer consciousness of health and wellness has led to legislation demanding clearer labeling on the nutritional content of foods and beverages. Packaged consumer goods manufacturers have had to comply with good manufacturing practices to ensure product safety from food-borne disease and potential allergen contamination. Restaurants have come under formal and informal demands to use healthy ingredients or to disclose the presence of trans fats in meals. Such pressures have spawned self-regulation, such as voluntary action by soft drink manufacturers and marketers to restrict school sales and serving sizes of high-calorie, low-nutrition products.

These developments have their roots in the experience of the tobacco industry and its often innovative but ultimately futile attempts to resist adaptation to social norms regarding two fundamental ethical questions. First, to what extent do consumer goods manufacturers have moral obligations to support the well-being of consumers beyond the economic laws of supply and demand? For a long time, tobacco companies advanced a pure economic argument in defense of their product, while critics gradually restricted the applicability of that argument to adults who were free to choose, a dwindling population. Second, what should be the standard for truth telling and disclosure when scientific certainty about the effects of product consumption is unattainable? Again, tobacco companies' defense proved only temporarily effective as scientific certainty about tobacco-induced health risks drew ever closer.

As the ethical risks to the tobacco industry have increasingly become economic realities, tobacco companies have resorted to other forms of innovation to improve corporate performance. One step has been product innovation, which began with the introduction of filters in the early1950s, matured with the availability of so-called lite (low tar, low nicotine) product varieties, and more recently has manifested itself in the pursuit of the smokeless cigarette. While filters arguably made cigarettes marginally less unhealthy, lite cigarettes have been the target of litigation contending that companies essentially set forth deceiving claims about their relative safety for consumer health, and smokeless cigarettes struggle to provide the same satisfaction to consumers who choose to smoke. Another form of product and marketing innovation has been to develop cigarette varieties and advertising campaigns aimed at a specific consumer demographic, though this approach has been criticized for preying on less well-informed consumers. Likewise, producers have sought to prioritize international growth, since regulation on tobacco products outside the markets in developed countries is not typically as restrictive and consumers may be less well-informed. This has continued to spawn seemingly disingenuous advertising and marketing practices, in which tobacco companies have complied with restrictions in developed countries while handing out free cigarettes in promotions in less regulated markets. Pursuing such growth, however, has proved risky as real-time media coverage has increased the risk to the reputation of companies seeking to hawk their wares to unsuspecting consumers while disapproving investors look on. Meanwhile, the introduction of measures such as the 2005 World Health Organization Framework Convention on Tobacco Control has helped international regulators catch up. Another corporate strategy has seen cycles of diversification and disaggregation. With the introduction of other packaged consumer goods into their product portfolios, tobacco companies were able to reduce the risk of concentration and volatility to which they were vulnerable when they were exclusively dependent on tobacco, while leveraging economies of production and distribution scale since food products and tobacco products are often sold in the same retail venues. However, those economies have waned as tobacco has been perceived at times as dragging down the food side of the business, or vice versa, as tobacco purists have argued that tobacco companies would do best to focus on their core customers.

Perhaps even more interesting to watch has been the innovative transformation of some tobacco companies into odd paradigms of corporate social responsibility. It is no longer unusual for tobacco companies to promote and undermine their own interests simultaneously, making their products available to those who choose to use them while offering help and comprehensive information to customers who seek to quit and actively engaging in youth smoking prevention initiatives. Interested in preserving the stability of market share among a dwindling pool of smokers, in some cases tobacco companies have come to invite regulators such as the FDA in rather than continuing the fight to keep them out. Long engaged in active lobbying of politicians, big tobacco now manages its reputation through corporate support for the arts, education, and other community-building initiatives. Not wanting to shed the heritage of foreign royalty and American presidents, who were active in the tobacco business, and unable to deny a history of nonparticipation in constructive debate about health and the public interest, tobacco companies have increasingly sought to refresh their image with a balanced approach to perpetuating the industry. This approach recognizes that (addiction aside) there are still and may always be individuals who enjoy smoking and have a right to do so, while it appears to accept accountability for creating a framework for compliance and social responsibility that encourages open dialogue to put the decision to smoke in the hands of the consumer. While there continue to be skeptics regarding the sincerity of this approach, in theory it addresses the fundamental ethical questions challenging the tobacco industry and other consumer goods manufacturers and marketers. It remains to be seen whether the tobacco industry is sustainable in the broad sense of the term—socially, since its products are harmful to the health of its target consumer; environmentally, as its products originate from the soil and subsequently pollute the air with carcinogens; and economically, while the verdict on its financial performance remains in doubt.

What is beyond reasonable doubt is that there are many lessons to be learned by all industries from the experience of the tobacco industry: first, that economic questions cannot be wholly emptied of ethical content; second, that the accelerating pace of information availability and regulatory sophistication will inevitably catch up with attempts to restrict adequate disclosure; and third, and a consequence of the other lessons, that the decision about what consumer goods are good for social well-being is not exclusively up to the manufacturer or its business partners, government regulators, or the individual consumer. What is good is not a simple question of right or wrong but must rather emerge as an outcome of constructive debate and continuing dialogue among all parties in pursuit of an elusive, uncertain conclusion.

—Christopher Michaelson

See also Advertising Ethics; Commerce and the Arts; Consumer Goods; Consumer Rights; Disclosure; Enron Corporation; Product Liability; Public Interest; Reputation Management; Self-Regulation; Socially Responsible Investing (SRI); Sustainability; Truth Telling; WorldCom; World Health Organization (WHO)

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Ethics in Government Act of 1978

Why the Act Was Enacted

The 1970s was a decade of tumultuous social upheaval and political chicanery. Watergate precipitated the resignation of President Richard Nixon. The newspapers reported a litany of overseas bribery incidents. In response to what was perceived as prevalent, insidious corruption at the very highest level of government, Congress responded with a number of ethics-based legislative measures. Among the many acts and amendments were provisions for Independent Counsel (28 U.S.C. 591, *et seq.*) and the Ethics in Government Act of 1978 (5 U.S.C. App. 4 § 101, *et seq.*), hereinafter referred to as the Act.

The essential purpose of the Act was to require disclosure of the finances and financial interests of high-level federal employees, provide report formats and procedures, and give notice to all what the penalties would be for failing to make the requisite reports and disclosures. Congress's goal was to provide an objective means of determining possible areas of conflict of interest.

The General Provisions

The original Act consisted of five sections: Title I—Financial Disclosure Requirements of Federal Personnel, Title II—Executive Personnel Financial Disclosure, Title III—Judicial Personnel Financial Disclosure, Title IV—Office of Government Ethics, and Title V—Government-Wide Limitations on Outside Earned Income and Employment.

Section II, which related to executive personnel financial disclosure requirements, and Section III, relating to judicial personnel financial disclosure requirements, were repealed in 1989, effective January 1, 1991. The spirit of the prohibitions was generally incorporated in 18 U.S.C. § 203, coming under the heading of Crimes, Bribery, Graft, and Conflicts of Interest and titled "Compensation to Members of Congress, officers, and others in matters affecting the Government." The section is more general than the Act. It eliminates the detailed reporting procedures and substitutes an expansive scope of governmental investigative powers and prosecutorial powers. The portions of the Act that remain in force pertain to other federal government personnel who are not covered under Section 203.

Title I: Financial Disclosure

Sections 101 to 111 addressed financial disclosure by federal personnel. The goal of Congress was to discourage bribery and other acts of mischief associated with people in a governmental position of power by requiring them to disclose their sources of income.

Generally, the designated government officials and employees must file itemized reports within 30 days of assuming their new jobs. The Act requires the disclosure to include, but not be limited to, the source, type, and amount or value of income, honoraria, or payments made to a charity on behalf or in the name of the employee in lieu of an honorarium of more than $200 in value; the source and type of income from dividends, rents, interest, and capital gains in excess of $200, identifying the amounts involved within certain prescribed categories of value; the source, description, and category of value of all gifts of more than $250 received from nonrelatives; the source and description (including a travel itinerary, dates, and the nature of expenses provided) of reimbursements received from any source of more than $250; the identity and category of value of any interest in property in a trade or business or for investment or the production of income with a fair market value in excess of $1,000, excluding family members or savings of less than $5,000; the identity and category of value of liabilities owed to any nonrelative creditor, including revolving charge accounts, that exceeds $10,000, except for mortgages on personal residences, motor vehicles, and small household items; and the description, date, and category of value of any purchase, sale, or exchange in excess of $1,000 in real property (other than a personal residence) or stocks, bonds, and other securities (except for transactions with a spouse or dependent children). Although it is not exhaustive, this list gives a sense of the breadth of the report requirements. It also shows that the dollar amounts triggering the disclosure requirement, in some cases, is *de minimus* in comparison with the reporter's income or personal wealth.

An officer or employee covered by the Act who fails to make timely reports or files false reports (5 U.S.C. App. 4 § 104) will be reported to the attorney general of the United States. If the offender is charged, tried, and found liable, the sanction may be up to $10,000. In addition, the offender may be referred to the Judicial Council, a body of judicial officers and their appointees charged with disciplining persons within the federal court's jurisdiction. Although not specifically addressed in the Title, if an official misleads Congress, he or she can also be charged with contempt of Congress, perjury, or other criminal sanctions.

It was apparent with the destruction of Enron and Arthur Andersen that the problem of dishonesty and ethical lapses was not limited to the governmental sector. Regulation of the civilian sector is relegated to agencies such as the Securities and Exchange Commission and other industry regulatory bodies. The civil and criminal justice systems provide additional checks on civilian abuses.

Title IV: Office of Government Ethics

Title IV creates the Office of Government Ethics (OGE). The OGE director is appointed by the president and confirmed by the Senate for a term of 5 years. The director is responsible for providing the direction of executive branch policies relating to the prevention of conflicts of interest involving the officials and employees covered by Title I. In addition to whatever action or sanction the director may take, he or she can also recommend other governmental agencies for taking action. For example, the director might refer an offender to the Justice Department for prosecution on tax evasion charges. Title IV requires any action taken or any rule made by the director to be subject to judicial review.

In 2003, the OGE took the unusual position of petitioning Vice President Cheney, among others, before submitting their proposed legislation to Congress. Their goal was "to modernize the financial disclosure process for federal personnel, and for other purposes." Their proposal was titled the "Ethics in Government Act Amendments of 2003." The legislative stated purpose was to create a "single, Government wide system of public financial disclosure" that "preserves the equanimity of the current [governmental] system" (OGE's letter to Richard B. Cheney, July 16, 2003).

The hope was to streamline and simplify the public financial disclosure requirements applicable to the reporting persons. The OGE reported that the original Act, in place for 25 years, was working well. Their revisions were intended to encourage qualified persons to enter into government service but "not sacrifice the goal of public financial disclosure or deny necessary information to those responsible for determining whether a conflict of interests exists." They did not want to jeopardize public confidence in the disclosure process.

Title V: Limitations on Income and Employment

As a practical matter, many of the personnel serving at the highest level of government are independently wealthy and/or have outside income far exceeding their governmental pay. Title V addresses this situation. The Title uses a number of complicated formulae to address income, gifts, and honoraria.

Generally, members of Congress and senior officers and employees of the federal government are limited to an outside income in any calendar year not exceeding 15% of their annual government pay. Persons regulated by the Title may not personally receive an honorarium while a government official or employee. The idea is to thwart a miscreant from disguising an improper payment as an honorarium. All honoraria must be refused or directed to a charitable organization. No honorarium can exceed $2,000. No person regulated by this Title may accept a gift from an organization from which a close relative of a federal employee derives any financial benefit.

If a person within the regulated class violates any of the Title V provisions, the attorney general may bring a civil action in federal court. If found liable, the individual may be subject either to a civil penalty of not more than $10,000 or disgorgement of the compensation, whichever is greater.

Has the Ethics in Government Act Worked?

The question of whether the Act has worked as intended is difficult to evaluate objectively. Generally, the Act only addresses specific financial disclosures. In the ensuing postenactment years, we have seen a litany of prosecutions and convictions of elected officials, private individuals, and lobbyists for bribery, influence peddling, and tax evasion. Some of these convictions were a result of the Act. Some can be attributed to better investigation and prosecutorial competence.

Clearly the disclosure requirement has had some impact. It mandates transparency. The public and media can evaluate the disclosures for accuracy and for effect. We see the disclosures required by the Act all over the Internet. It seems that those required to make disclosures have, to some degree, taken the requirements of the Act seriously. However, we have no evidence as to the accuracy of any of the disclosures.

At best, we can speculate that the Act gave a reason to those who had nothing to hide to disclose their sources of income and, indirectly, their possible conflicts of interest with their public duty. The specter of sanctions may have scared some of those public officials who were ethically "on the line" to opt for honesty. However, it is fair to say the Act had little or no effect on those bent on mischief, as cases of conflict of interest have persisted in the years since the Act was established. These individuals took bribes and other income and failed to make the proper disclosures. This lapse does not indicate that the law is a failure, just that those who are going to be dishonest most likely will not be deterred by legislation.

Conclusion

Some regard the influence of money on politics to be inevitable. Others believe that the extensive revisions in our political system can substantially reduce the influence of money. A senior governmental official or employee prone to mischief will not be thwarted by legislated ethics. However, the hope, from its inception and throughout the various modifications and amendments, is that the Ethics in Government Act will give a potential miscreant cause to consider the ramifications and sanctions that will arise from his or her misbehavior. The Act also gives the attorney general's office numerous means to punish offenders. On balance, when a senior official fails the ethical test, the people have at least a soupçon of a possibility of holding him or her accountable.

Perhaps the more important issue, of which the Act is a small facet, is how we establish and then maintain a general trust by the public in our government. Requiring key, influential governmental employees and officials to disclose and publish their sources of income is important. However, until there is a more pervasive trust in those who work for and lead us, even the required disclosures will be looked on with mistrust.

—Michael B. Rainey and Linnea McCord

See also Accounting, Ethics of; Advertising Ethics; Amorality; Antitrust Laws; Arthur Andersen; Bankruptcy, Ethical Issues in; Christian Ethics; Communications Decency Act; Conflict of Interest; Corporate Moral Agency; Economics and Ethics; Ethics, Theories of; Legal Ethics; Marketing, Ethics of; Natural Law Ethical Theory; Neo-Kantian Ethics; Price-Fixing; Pricing, Ethical Issues in; Sarbanes-Oxley Act of 2002; Teaching Business Ethics; Virtue Ethics

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Ethics of Care

The term *ethics of care* refers to ideas concerning both the nature of morality and normative ethical theory. Over the past two decades or more, a discussion has arisen regarding these ideas. The caring perspective is distinctive in that it uses a relational and context-bound approach toward morality and decision making. In doing so, this perspective stands in stark contrast to ethical theories that rely on principles to highlight moral actions—such as Kantian deontology, utilitarianism, and justice theory. Importantly, such principles are meant to be absolute and incontrovertible.

Nel Noddings has provided one of the first comprehensive theories of care. Arguing that caring is the foundation of morality, she sees the dyadic relationship as ontologically basic to our very humanity. Identity is defined by the set of relationships individuals have with other humans, and as such without relationships we would not be human. In suggesting that caring is a universal human attribute, caring relation (a relationship in which people act in a caring manner) is seen to be ethically basic to humans. Since the impulse to care (in a specific way) is universal, caring ethics is freed from the charge of moral relativism to the same degree as is virtue theory.

The particularity of relations is fundamental to the ethics of care. Each relation consists of at least two people, the one-caring and the cared-for. Such a relation can certainly be more than merely dyadic as the one-caring and the cared-for come to exhibit reciprocal commitment to each other's well-being. However, what is distinctive in all such relations is that the one-caring acts in response to a perceived need on the part of the cared-for. The act is motivated by an apprehension of the cared-for's reality, a receiving of the cared-for into the one-caring such that the one-caring feels and senses what the cared-for is experiencing. The one-caring responds to the well-being of the cared-for by initiating a commitment to help the cared-for. Authentic care provides the motivation for such assistance. This does not mean that the one-caring does exactly what the cared-for desires in all situations. Rather, the one-caring considers the cared-for's point of view, assessment of need, and expectations of the one-caring in formulating a response that provides the best opportunity for helping the cared-for. This response might be irrational, since caring involves the commitment to do something, however remote the possibilities of success, to improve the cared-for's condition. In the ideal situation, however, the reason(s) the one-caring gives for his or her actions would be sufficient to convince a disinterested observer that he or she indeed acted in a way to promote the cared-for's well-being. Caring thus involves sentiment but is not necessarily emotional in nature.

Within the ethics of care the one-caring receives the cared-for without evaluation. However, in deciding how to respond, the one-caring works in what Nel Noddings calls a "problem-solving" mode—keeping in mind the particular relationship and context to avoid slipping into the abstract, impartial, impersonal reasoning of the deontologist, the utilitarian, or the justice theorist. Ultimately, there is a defining imperative to act that is a critical function of what it means to care.

These ideals apply to both natural caring, or caring born of inclination and love for those close to the one-caring, and ethical caring, which is the feeling response of "I must" to a person's predicament. Ethical caring is a natural outgrowth of natural caring, but unlike Kant's ranking of duty as primary and inclination as secondary, in the ethics of care the inclination to care is primary. Even with regard to those with whom one has no caring relationship—complete strangers—memories of natural caring arise, generating a feeling of "I must do something." This impulse is obligatory in anyone who aspires to what Noddings calls the "ethical ideal," the sense of self as a moral, caring person. However, within the ethics of care, this obligation to the stranger is limited. Two criteria must be met for such a duty to have force: (1) The relationship with the other person must exist (or have the potential to exist), and (2) the relationship must have the potential to grow into a mutually caring relationship. One does not have either the capacity or the duty to care for everyone; however, one does hold an obligation to be prepared to care at all times for particular others—for "the proximate stranger."

Ethics of Care and Feminism

It would be easy to confuse the ethics of care with feminist ethics. Feminist philosophers have argued that the deontological, utilitarian, and justice moral theories are grounded in the masculine experience. More specifically, these theories are seen to emerge in concert with the traditionally masculine forum of economic activity. Within this perspective, the values of competition and domination are seen to undergird both the activities of the marketplace and the rational moral theories. Virginia Held argues for adopting more compassionate bases for our human interaction(s).

Feminist moral theory at its heart has tended to mirror the differing gender experiences of women and men, particularly as these affect the development of understanding with respect to the ways the ethical life is conducted. However, it has been noted by Robbin Derry and others that *feminist* moral theory is not *feminine* moral theory, as feminist perspectives are not fully determined by gendered points of view. Nevertheless, the suggestion that gender matters, particularly as gender relates to one's ethical predispositions, calls into question the inherent "objectivity" of ethical theories, which are advanced in part due to their universal merit and application. Feminine moral theory thereby deals a blow to the exclusively rational systems of thought, which have as their grounding an inherent disregard for the inherently personal—and sometimes gender biased—nature of knowledge construction.

It was not necessary that feminine moral theory be aligned with the ethics of care. It so happens that those writing in the feminine tradition, such as Carol Gilligan, came to associate care and responsibility to others with a female-gendered approach to ethics and individual rights and justice with a male-gendered approach to ethics. Gilligan in particular made the argument that, historically, philosophers have seen women as morally inferior to men, when in fact they are simply different in emphasizing care over justice. However, central to the feminist perspective is not the content of the gender-specific approaches but rather the more fundamental observation that gender—and by extension a host of other demographic factors and interpersonal predispositions as well—contributes substantially to an individual's moral insight and development. This being the case, there is no reason to privilege masculine-rational approaches to ethics above feminine-caring approaches to ethics.

Ethics of Care Within the Business Context

The caring approach avoids the problem that many approaches to ethical management face: deciding whose rights, among people with roughly equal rights, will be respected. While all have the duty to treat others in a caring way, in cases of conflicts of duty, the responsibility of the one-caring includes deciding who is most appropriately the beneficiary of care and then acting on that judgment. It is the concrete, particular individual with whom one has a caring relationship whose well-being must take priority in each inherently unique circumstance.

If caring is regarded as a natural inclination that serves as the base for the development of specific character traits, then one can begin to understand what caring business praxis might mean. Gilligan discusses three levels of a caring morality—one where the self is cared for to the exclusion of the other, one where the other is cared for to the exclusion of the self, and a third where the needs of both self and other are understood. This third level is the one Gilligan sees as moral maturity. While stopping short of equating feminist ethics with virtue ethics, Brian Burton and Craig Dunn suggest that this portrayal sounds very much like the description of an Aristotelian virtue. Not opposed to a legitimate place for emotion in ethical discourse, Aristotle outlines the importance of feeling at the proper times, about important things, concerning the right people, and for good reasons. Aristotle further sees the moral person as possessing various character traits and describes a virtue as behavior regarding a particular trait that is a mean between two extremes of behavior, with one showing an excess of that trait and the other showing deficiency of the trait. Applying this depiction to caring, the virtue would be caring (understanding the needs of self and other), the vice of excess might be codependence (caring for others to the exclusion of self), and the vice of deficiency might be selfishness (caring for self to the exclusion of others).

To achieve the goal of the caring approach to management, the manager needs to understand what the mean of caring is, what this implies for different situations, and what specific virtues are associated with the base of caring. The manager can then care for the particular individuals involved in a specific situation by apprehending their reality, considering their well-being, and acting in a manner that is in their best interest(s) or explain, in cases of conflict, why the action taken might not readily be seen as in the best interest of the cared-for.

Ethics of Care and Stakeholder Theory

Much of the discussion regarding the relevance to management of the ethics of care has taken place within the bounds, or in attempting to expand the bounds, of stakeholder theory. Efforts have been made to use the language of stakeholder theory to describe the caring perspective or use the ethics of care to normatively justify stakeholder theory. In some instances, the ethics of care—or, more accurately, feminine ethics—have even been advanced as the grounding for a new theory of the firm.

Just as the most often discussed forms of moral theory focus on masculine principles, however, most discussions of stakeholder theory give decision rules for how to interact with stakeholders. In categorizing stakeholders and in giving generic principles for interacting with the stakeholder categories thus formed, theorists have moved away from the essence of the ethics of care—understanding the particular context and fashioning a response to that context. But caring cannot be captured in decision rules and universalizable principles. Rather, discussions of caring by their nature center on how we live or, in a business context, how we manage relationships (not contractual obligations), which, after all, form the whole of managerial behavior. Caring focuses on particular cases, with the understanding that each situation is unique. Caring elicits intuitive responses at first, with rational analysis coming later. Caring has an underlying context of moral sensitivity instead of detachment.

Numerous writers maintain that the ethics of care provide a better way of describing the environment in which a manager operates and the manager's response to that environment than principle-based approaches. The primary difficulty with stakeholder theory in the latter instance is that it imagines stakeholders not as individuals but rather as members of homogeneous groups. Although they are members of stakeholder groups, however, when approaching the manager, stakeholders do so as individuals. Each stakeholder naturally holds unique—and in some instances caring—relations to the manager. Each stakeholder holds perceived needs that he or she is trying to convince the manager to satisfy, and such needs will vary from context to context.

The moral impulse of managers is to respond to each stakeholder with understanding, concern, and the desire to do something to help the stakeholder. Such impulses cannot in all instances be explained through the perspectives of the more rational systems of ethical decision making. In fact, Noddings and Gilligan both argue that training in these systems may well extinguish the caring impulse. Furthermore, that impulse decreases as the relationship with the stakeholder becomes more distant—the “I must” response becomes less of an imperative because other stakeholders with closer relationships with the manager also bring forth the “I must” response and the manager can only react to a limited number of stakeholders.

Ethics of Care and Management Theory

There is a great opportunity to apply the ethics of care to organizational research and praxis. It is not too difficult to imagine how the crafting of an organization’s statement of purpose and mission might be informed by this perspective. Policies supporting work-family balance are easily seen as a matter of ethics of care. Recruiting and hiring practices might take into account the well-being of the cared-for—the prospective employee. A variety of employment practices, from job sharing to telecommuting to job rotation, could reflect caring impulses that not only explicitly acknowledge the particularity of intra-office relations but serve to honor interoffice relationships as well. Vacation and sick leave policies, termination guidelines, employee assistance programs, profit participation plans, performance appraisal, and so on—the litany of organizational practices that might prove to be natural extensions of the moral impulse to care seems limitless.

—Craig P. Dunn and Brian K. Burton

See also Aristotle; Empathy; Ethics, Theories of; Feminist Ethics; Feminist Theory; Impartiality; Justice, Theories of; Kantian Ethics; Kohlberg, Lawrence; Lesbian Ethics; Maternal Ethics; Rawls’s Theory of Justice; Relativism, Moral; Stakeholder Theory; Utilitarianism; Virtue Ethics

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Ethics of Dialogue

The ethics of dialogue has drawn increasing attention from scholars in the humanities and social sciences, as well as from policy makers and problem solvers in the realms of business, government, and civil society. Ethical dialogue is an approach for human discourse and reasoning directed toward improved problem understanding and possible problem resolution. Such discourse focuses on the enhancement of learning and relationship building by multiple stakeholders who are struggling to make better sense of complex, messy problems that are characterized by significant value or interest conflicts and contested knowledge claims. An ethics of dialogue can be examined by exploring dialogic modes of communication, tracing certain philosophical notions regarding dialogic ethics, and exploring possible risks and benefits for applications of dialogic ethics in organizational, business, and other contexts.

Defining Dialogue

A leading contemporary exponent of dialogue and dialogic learning, William Isaacs, breaks down the term to its etymological roots: *dia* and *logos*. *Dia* means "through" and *logos* is translated as "word" or "meaning." In this sense, dialogue is a "flow of meaning." An older derivation of *logos* is "to gather together," suggesting that meaning arises out of relationships. Thus, dialogue is an open-ended, interactive form of communicative learning that encourages those engaged in discourse to reflect on their own and others' preconceived values and ways of framing issues so that they can together move toward a common ground where joint problem solving via mutual discovery and cooperation becomes possible.

Often, the term *dialogue* is used loosely to cover a variety of modes of communication. Spoken and other forms of communication can occur solely or primarily for self-expression or for the construction of knowledge from an individual's existing cognitions and beliefs. Dialogue can be viewed as communication exchanges involving two or more individuals for purposes such as information sharing, persuasion and other instrumental outcomes, and empathetic relationship building. The learning theorist Peter Senge makes a distinction, though, between dialogue and other forms of discourse, such as discussions involving a group of individuals for instrumental or strategic purposes. These discussions usually seek a convergence of the perspectives of participants, by one point of view winning out over others, to reach some conclusion or course of action. Dialogue, instead, focuses much more on exploring and respecting the diverging perspectives and concerns of participants, seeks a richer grasp of complex issues, and fosters a unique, more trusting relationship among participants who so regularly interact.

The growth of interest in an ethics of dialogue has been associated with specific definitions of dialogue and the particular assumptions underlying these forms of communication. Recent conceptions of dialogue usually assume empowered and vocal participants and a search for "intersubjective" meanings as participants in a dialogue struggle to make sense of a shared problem from contrasting identity, interest, and value perspectives. The diverse applications suggested for dialogue include collaborative inquiry and learning, deliberation and negotiation of public policy in contested, problematic settings, and engagement for increased understanding of relationships and responsibilities among "selves" and "others." Such more recent assumptions and goals for dialogue contrast with forms of communication that are also referred to as dialogue. For example, traditional Socratic dialogue is not open-ended and exploratory since it has more strategic goals of persuasion and established roles for the master or teacher and novices or learners. Different conceptions of dialogue, thus, can have varying ontological (the nature of existence or reality), epistemological (the nature of knowledge or meaning), and ethical (the nature of the good life) assumptions.

Theoretical Contributions to the Evolving Conceptions of Dialogue

One of the more important philosophical trends of the last century has been a "dialogic turn" within philosophy in particular and in the social sciences and humanities generally. Dialogue attracted scholarly attention related to changing views about the nature of human agency or a sense of self. Premodern notions of self emphasized its place within a meaningful universal order. Enlightenment thinkers viewed the self as a rational, individualized, and very autonomous agent. A much more "decentered" conception of self is associated with postmodern thinking, where "objective truth" dissolves in a seething cauldron of competing language games. This sense of self is a fragmented construct, built from fleeting, semiconnected images of past relationships, and is subject to ongoing negotiation and self-promotion. The postmodern deconstruction of competing narratives does not offer much prospect for constructing a shared meaning from language games. In contrast, philosophers of hermeneutics and critical theory seek a more integrative, relational, dialogical understanding of meaning as constructed by expressions of self in relation to others. Hermeneutics is the branch of philosophy concerned with the discovery of human meanings by the interpretation of texts, including not only written documents but also spoken narratives, works of art, and even evocative events. Among the hermeneutic and other theorists seeking a new epistemological framework for better understanding of critical moral challenges and for generating more creative and integrative ethical responses were Martin Buber, Mikhail Bakhtin, Emmanuel Levinas, Hans-Georg Gadamer, Jurgen Habermas, and David Bohm. Criticizing the limitations of both Kantian universalism and Benthamite utilitarianism, this dialogic turn focused on identifying and developing the potential for improving awareness of the moral claims and obligations of stakeholders and for reducing self-deception, other perceptual biases, and a pervasive moral arrogance that arises from a natural psychological tendency to elevate one's own particular cognitions and interests. Cost-benefit studies of construction projects that emphasize the net positive economic values to one set of stakeholders while marginalizing the concerns about the social and environmental costs of the project voiced by other affected stakeholders are a case in point. Recent dialogic theorists, such as Habermas, have been particularly critical of excessively rationalistic and strategic modes of discourse as so dominating business and organizational life that these influences limit a broader exploration of the creative potential of self in relation to others. A relational or dialogic sense of self grounds its ethics less in terms of the discovery of universals of truth or justice or in the role of religion or science in establishing moral claims and much more in a dialogic process by which human beings create meanings and define their sense of identity through caring, social interactions with others. Advocates of dialogic learning as an approach to cooperative problem solving argue that an appreciation of reciprocal ethical obligations or relational responsibilities is more likely to arise from an interactive process of stakeholder engagement than from unilateral managerial applications of Kantian or utilitarian moral precepts.

Martin Buber characterized the essence of ethics as dialogue with genuine openness and appreciation of the other person. Instead of "I-It" relationships or "subject-object" thinking, dialogue can forge "I-Thou" relationships by viewing others as created in God's image. "I" is not the center of the universe in this perspective but a "gift" to be given to others. The focus on and respect for "Thou" or "You" through dialogue helps create a stronger sense of community and constructs a deeper sense of what "We" can accomplish and become. Between the extremes of subjectivism and absolutism and between egoism and purely altruistic concerns, Buber believed that dialogue offers resources for developing enhanced and caring interpersonal relationships. The precepts and practices of Alcoholics Anonymous (AA) are a highly effective example of a therapeutic dialogic encounter. Admitted addicts meet regularly to share stories, confess personal weaknesses, and celebrate advances within the interpersonal context of shared understanding and support. Committed AA members control their addiction by constructing an enhanced sense of self within a community of care.

Dialogic theorists with contrasting backgrounds, such as Mikhail Bakhtin and Emmanuel Levinas, regarded dialogue as an ethical imperative for better appreciating the complexity of cultures and contexts. Bakhtin stressed concepts such as the generation of meaning lying beyond the individual sphere of consciousness and "between" the texts of what is spoken (*intertextuality*). He advocated the prevalence of context over text (*heteroglossia*). Dialogue for Bakhtin and Levinas is an interactive alternative to ethical judgment arising from unilateral, or "monological," derivation of an abstract set of ethical rules. Dialogue responds, first and foremost, to a responsibility engendered by the presence and face of the Other. Dialogue goes beyond mere human exchange through words and becomes a form of virtue itself, as pure ethical (or relational) responsibility. These perspectives base an ethics of dialogue on genuine listening and the realization that the self can't be the central source of adequate moral meaning. The metaethical philosophy of Levinas did view the self as being responsible for ethical action, however, and, through dialogue, capable of transcending its own biases and limitations in order to respect and care for others. Levinas claimed that actual efforts to meet this pure sense of responsibility can never be truly complete or adequate.

Hans-Georg Gadamer commented on an ethics of dialogue from a hermeneutic tradition of textual analysis and interpretation. Gadamer believed that individual consciousness was historically effected or that individuals become so embedded in their culture and times that even their identities are shaped by these assumptions. Interpreting a text or the remarks of another person involves a fusion of horizons in which the individual tries to connect these realities, meanings, and identities. Gadamer viewed dialogue as a means to link the different mental maps of dialogic participants to achieve a broader perspective and common convictions concerning human well-being. Since understanding is shaped by the cultural and contextual influences on dialogue participants, Gadamer suggested that better understanding occurs through periodic efforts to dialogue or share and test diverse perspectives over changing times and circumstances.

These hermeneutic conceptions of dialogue were challenged by critical theorists such as Jurgen Habermas. Habermas claimed that the dialogic assumptions of Gadamer could not overcome the serious inequities of power among certain stakeholders and, therefore, could not discover certain ethical responsibilities or facilitate action with regard to these inequities. Habermas proposed an ideal speech situation or genuine conversation as a regulative ideal for dialogic intentions and processes. Such an ideal is intended to expose and help participants understand systematic distortions of communication by those with the power to dispose others to accept certain meanings and underlying values and interests. Two ethical principles underlie the normative procedural requirements of ideal speech. The first is a requirement that we recognize the right of all beings capable of speech and action to be participants in a moral conversation. The second requirement is that within such authentic dialogue, each participant has the right to initiate new topics and ask for reflection about the presuppositions that each brings to the conversation. In effect, this is a normative dialogic extension of a principle of fairness in engaging stakeholder relationships.

The conception of dialogue as an ethical ideal found in perspectives from Buber, Bakhtin, Levinas, Gadamer, and, particularly, Habermas offers an important counterbalance to human tendencies to rationalize decision-making processes as "ethical" when they merely serve instrumental purposes and outcomes.

Dialogic Alternatives, Assumptions, Risks, and Potentials

A huge tension exists between the notions of dialogic ideals proposed by philosophical theorists and recommendations for actual dialogues that would be more effective for improving human well-being. Scientific or empirical efforts to "capture" or appropriate the ethics of dialogue have some obvious limitations, according to Habermas and others. Such reservations have not impeded, and have sometimes informed, a number of recent theorists proposing dialogic alternatives. For example, the quantum physicist David Bohm advocated a particular form of dialogue to surface and change the tacit infrastructure of thought and overcome reductionist tendencies toward abstract categorization, which leads to fragmented thinking. Such forms of basic cognition become so familiar and embedded, according to Bohm, that individuals can conceive of these abstractions as actual reality and truth, and often the only or primary one. If beliefs and cognitions largely are shaped by previous communities of attachment, then more collective resources, such as dialogue, are needed to test these assumptions for new or complex challenges. For dialogue to be effective for these challenges, Bohm proposed certain basic requirements: (1) suspension of prior assumptions, (2) respect and appreciation for the contributions and assumptions of other participants, and (3) the key role of a facilitator to shape the dialogue process and context.

Building on the work of Bohm and earlier dialogic theorists, others recently have proposed related guidelines for more ethical dialogic processes and outcomes. Among such assumptions or guidelines are the following:

- A collaborative orientation and spirit of co-inquiry concerning the issues and concerns of participants
- Attempts to express viewpoints and positions with honesty and authenticity
- Appreciation of the mutual vulnerabilities and risks involved in such openness
- Reciprocity and caring reflected in the comments and responses shared with others
- Reduction of the impact of power differences among participants
- Awareness of the affective dissonance or discomfort, yet potential learning value, fostered by the unexpected consequences of dialogue
- Active, continuing critical reflection of evolving interpretations and judgments regarding the issues and moral claims of participants

Guidelines such as these have been suggested to create a safe space, or container, for tapping into the deeper learning potentials of dialogic processes. Embedded in certain forms of dialogue are powerful learning paradoxes that include concerns for self/others, interpersonal space/intimacy, and construction/deconstruction of metaphors and other linguistic structures to represent the cognitive tensions inherent in social realities and personal meanings.

Social scientists have also considered the stages of learning and relationship building in dialogic processes as well as what constitutes adequate facilitation to explore and move through these stages. Time is required for the unfolding of participants' knowledge claims, affective displays, and efforts to propose and consider possible actions in these dialogues. Preferences can differ among participants for more freedom or spontaneity versus more control or structure in undertaking the stages of dialogue. Aspects of dialogue such as allowing time for confrontation or challenge of ideas as well as for affirmation and empowerment of participants demand considerable facilitator skill and empathy.

Despite the promise of dialogue for learning and relationship building, there are obstacles and challenges in undertaking dialogue for such purposes. Patterns of human discourse are entrenched or conditioned such that suggestions for ethical forms of dialogue are in practice difficult to enact. Many individuals have poor listening skills or an addiction to conversational narcissism. Attitudes in some cultures devalue "talk" or dialogue in contrast to taking action. Frustration with dialogue, such as lack of opportunity for voice, discomfort when confronting conflicts, very lengthy or continuing time demands for dialogue, or preferences for a different dialogic process, can cause some participants to withdraw. Facilitating resources can help dialogue participants, particularly through the early stages of conflict, in expressing and listening to the diverse values and positions of participants. However, this facilitation can be perceived as biased or as less effective than possible. There are personal risks, too, in undertaking dialogue. Participants who are openly sharing, exploring, and constructing social realities or their identities are vulnerable and could be harmed by the responses of others. High levels of cognitive and affective strain can be experienced by individuals, even when such learning experiences are viewed quite positively in retrospect. The interplay of ideas and shifting relationships through dialogue can lead to perceptions of chaos, confusion, and ambiguity. More genuine dialogue can be a radical departure from the previous experiences of many potential participants, so considerable support for dialogue participants appears warranted when these communication and interaction alternatives are selected. Thus, dialogic exploration may not offer the appropriate benefit-risk profile for many social or organizational challenges. Much more research is needed to consider whether and when dialogic approaches are appropriate responses to contrasting social purposes or needs.

Stakeholder Dialogues for Business and Public Policy Applications

Given the potential for responding to learning and relationship building opportunities, ethical dialogues have been proposed as a means of negotiating, or at least generating alternatives for resolving, public and private policy problems. However, care must be taken to guard against a "strategic twist," where powerful interests can distort the direction of dialogic inquiry. Dialogue has limitations also for the actual stage of policy determination. More genuine and open forms of dialogue are oriented toward "keeping conversations going," thereby providing less guidance for any integration of viewpoints leading to particular decisions that participants might need to make. For this reason, inquiry processes developed in the social sciences, such as participative action research and action learning, have been suggested as being potentially useful in conjunction with implementation of ethical dialogic processes for policy analysis and determination. The relationship between ethical dialogues and other common organizational and institutional processes such as strategic planning and organizational development/change also presents both questions and possible opportunities.

Within the fields of business ethics, corporate social responsibility, and corporate citizenship, research on corporate stakeholder engagement has also suggested applications of dialogic ethics. The extent to which corporations are committed to and practice very high levels of stakeholder engagement, such that their key stakeholders are truly empowered and included in organizational decision-making processes, can certainly be questioned. Yet trends in corporate social performance assessment suggest that more firms are reporting more dialogues with their multiple stakeholders. Social audit consultants have proposed criteria for measuring the quality of stakeholder dialogues. These include measures of inclusiveness and responsiveness toward key stakeholders, as well as evaluation of the actual outcomes resulting from these dialogues. Concerns for the quality of inclusiveness and responsiveness toward stakeholders for purposes of social performance reporting might lead more business organizations to adopt the dialogic processes recommended by social scientists and business ethics consultants.

Multistakeholder dialogues are increasingly sponsored by nongovernmental organizations and governments grappling with complex regional or global issues such as environmental sustainability or technology assessment, in which businesses or corporations are just one of many participants. Agencies associated with the United Nations, for example, are among those sponsoring multistakeholder dialogues. Whether these dialogues can take advantage of the learning and relationship-building benefits while avoiding the obstacles and risks of more genuine forms of dialogue is an issue for continuing social science research. Private consulting firms and university research centers are already studying and recommending applications of dialogic ethics for multistakeholder dialogues. The potential for improved business and public policy practices as a result of the application of multistakeholder dialogues has been linked to concerns as diverse as providing a greater degree of workplace spirituality for employees, enhancing "moral imagination" for stakeholders in resolving complex social issues, and overcoming "paradigm wars" that block increased stakeholder understanding and empathy in cooperative problem-solving efforts.

—Stephen L. Payne and Jerry M. Calton

See also Corporate Citizenship; Corporate Social Responsibility (CSR) and Corporate Social Performance (CSP); Corporate Social Responsiveness; Ethics of Care; Postmodernism; Stakeholder Engagement; Stakeholder Theory

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Ethics of Persuasion

When we purposely use communication to influence others (their values, attitudes, emotions, beliefs, and actions), then we are engaging in persuasion for or against something. Adding media to the mix, so that we can extend our influence, makes us propagandists. This is not necessarily a bad thing. Without some level of persuasion, common agreements (or social contracts) about public policies would be impossible. Another reason is that although persuasion and propaganda are often negatively associated with falsehoods or half-truths, this is not necessarily the case. Much persuasion is in fact truthful, subject to review and critique. Ironically, democracies as well as dictatorships need such purposeful communication if society is to exist and progress.

Advertising and public relations, for example, have long been important persuasive communication strategies used by corporations. Without the ability to tell their stories and promote their products or services through advertising, public relations, and other forms of promotion, businesses would be unable to compete and grow.

From the point of view of self-interest, there is also compelling logic to an organization devoting resources to define problems, proactively track opinion, and be involved in shaping solutions. The process often involves linking one's self-interest to a broader public interest. This, in turn, presents unique problems since there is no such thing as a single "public interest" but rather the collective positioning of concerns in ways likely to be seen as socially desirable or undesirable. The contest usually devolves into a grab for power resources where various entities mobilize leverage for some sort of government involvement.

Of interest is the fact that a significant percentage of major corporate advertising budgets are now spent influencing various target audiences on image, ideological, and political issues in contrast to selling consumer goods. Some of this is conducted under the public service announcement banner of social causes approved by the Advertising Council, a nonprofit organization that grew out of corporate support for the war effort during World War II. Corporations and their trade associations also participate in public policy debates and referenda contests. By the mid-1980s they were already investing an estimated $1.8 billion per year, a figure that continues to grow.

These efforts are particularly controversial. Such spending on public communication by private groups raises concerns over the potential impact of more unfettered access by issue communicators, especially those with "deep pockets," or large capital resources in dominating lobbying and public policy debate. Without doubt, the deep pockets issue is very real. Driving such massive expenditures is the assumption that issues advertising informs and influences public opinion. For example, the Citizens for Better Medicare (CBM) positioned itself in the run-up to the 2000 presidential campaign as a broad-based bipartisan group concerned with the health of Americans and the future of Medicare. Actually, CBM was founded in 1999 by the Pharmaceutical Research and Manufacturers of America, a trade industry group representing more than 100 drug firms, along with some others. They were concerned after President Clinton announced his intention to request that a prescription drug benefit be added to the standard Medicare program. The resulting message of CBM, appearing in print ads and broadcast commercials starring "Flo" the senior citizen, was that they wanted a prescription drug benefit but without government intervention. Overall, they spent more than $7 million advocating Medicare proposals similar to those put forward by the Republican nominee George W. Bush in his 2000 campaign.

Criticisms from within are mostly concerned about whether or not such campaigns work. Scholars, as well as practitioners, are badly divided on whether or not the persuasive information contained in issue communication contributes to effective public policy making. While a number of studies on informational campaigns report that they can influence opinion and behavior (as was true in the CBM effort), other reputable scholars conclude the opposite.

One reason for this is inconsistency in execution. To be effective, issues communicators must demonstrate that their organizations not only seek to change others but also are prepared to reform internal policies and practices. This is often easier said than done, as Exxon discovered as a result of the *Valdez* oil spill crisis in Alaska. Contributing to the impediments caused by the natural human reluctance to admit error is the fact that those charged with issues management responsibilities generally lack a common ethical grounding in education, theory, or practice. This missing common ideological framework is one of the underlying reasons for the uncertain integration and application of issues management, a problem contributing to its overall acceptance within business. Factors such as the type of persuasion effort, the amount of information the audience already has, and how fixed opinions are prior to the campaign are also variables.

These concerns, however, do not directly address the challenges flagged by external critics who assert the perceived threat that implementation of issues management poses for fairness and equity. Some critics simply reflect the principled objection to corporate advocacy by opponents of the capitalist system. Others, while not necessarily antibusiness, raise ethical concerns when such messages use a "front group" strategy (as in the CBM campaign) to disguise who the real proponents are. If those exposed to the messages knew that they were emanating from self-interested elements, not an independent citizens group, then perhaps the audience might react differently.

Opponents also continue to argue that corporate spending, even when fully credited, allows companies to dominate public sentiment by literally overwhelming positions contrary to their own. This position is straightforward: Public opinion is not a function of even-handed debate but, instead, is significantly distorted by propagandistic corporate advocacy. In essence, business critics believe that the agenda is set for the elite media by corporate ownership and influence *prior* to newsrooms serving their gatekeeper function (the editorial selection of what makes the news and what doesn't).

Thus, the debate over the social utility of issues management remains a "hot-button" topic for a number of reasons. Private sector leaders have often been guilty of poor management communication about what they and their organizations stand for. Some businesses, for example, got on the environmental bandwagon in an attempt to look good. But without engaging in a real commitment to reform, such "greenwashing" often seemed false. The long-term erosion of public confidence in American business, a distrust now reemerging because of corporate accounting scandals and as domestic jobs disappear to globalization, is a reflection of this performance and perception failure. These concerns extend into the international arena, where corporate behavior is seen by critics to be pervasively indifferent not only to reasonable laws and regulations but even to minimum standards of human decency.

In addition to external persuasion, American businesses also exert a high level of control over internal information flow in the workplace. FedEx communicates regularly with its workforce so that they know the brand attributes of the company, including what the company's vision and values are. FedEx's leadership also listens and gets feedback from workers. This approach is generally considered a form of enlightened management. On the other hand, "employee relations" can prove a form of propagandistic control rather than simply an informational tool. Wal-Mart has successfully used employee relations to resist unionization and regulatory attempts to mandate greater benefits. So despite issues management's practical side, unless business more consistently articulates a clear-cut rationale for its own existence to a full range of publics, the future of issues management remains clouded.

Indeed, today almost any sustained effort by business to influence others raises some level of suspicion. Questions often asked about persuasive communication include the following:

- Is it unethical for issues managers in business and elsewhere to use persuasion to influence various publics and targeted decision makers?
- Is it unfair to mobilize resources to private ends, with corporate financial access contributing to this lack of balance?
- Does a capitalistic bias "defile" the public interest by propagating materialist values and overconsumption?
- Do issues management efforts push aside real issues, by stressing simpler, more manageable ones that obscure the role of business in causing social problems?
- Should communications be further regulated to ensure that people take a more active citizen-participatory role?

Some writers on the topic (only half-humorously) claim that American businesses should not be expected to do much in the way of ethics since so few corporate leaders have any expertise in it. While this is plausible, such concerns seem to be overrated, particularly when evidence shows that advocacy communication is perceived as valuable by consumers and is tempered by findings that show it to be most effective when seen as informative, nonthreatening, direct, and fair.

When then is persuasion ethical? Most ethicists turn to a utilitarian emphasis on factual information that evokes voluntary change as characterizing ethical persuasion. Voluntary participation is critical, since the recipient of such communication has the power of coparticipation in terms of accepting or rejecting the attempted persuasion.

Alternatively, when is persuasion unethical? Ethicists generally agree that it is unethical to falsify or fabricate, to distort so that the true intent is not conveyed, to make conscious use of specious reasoning, and to deceive the audience about the communicator's intent. While some forms of persuasion are unethical, this caveat is not universally applied to all mobilizing messages. Proponents further argue that propagandistic excess fortunately is generally self-correcting. When abuses occur, as they sometimes do, regulation usually follows. This generally occurs when businesses engage in questionable claims (regulation of automobile contracts) or when individuals cannot make an autonomous reasoned decision (e.g., in marketing to children, who may not be experienced enough to tune out of a dazzling ad campaign).

Today, the essential problem in information distribution involves cutting through the literally thousands of messages ("clutter") directed at individuals each day. There is very little option for larger institutions such as big business dependent on mass markets. Either they actively participate in events affecting them (through political as well as commercial speech) or they wait to respond after the fact (critical news reports, regulation). If the would-be persuader fails to offer something of interest or value, the message is unlikely to break through into consciousness, let alone the action stage.

While this tends to ameliorate the ill effects of partisan views, activists on the right and left are not satisfied. Both camps believe that the media (which after all in the United States are businesses) remain dominated by their ideological opponents, and so they look for government to intervene in guaranteeing that their views are given an airing. Similarly, those "moderates" opting for some form of social responsibility criteria tend to fall back on agencies such as the Federal Communications Commission and Federal Trade Commission for relief.

Certain regulations abroad are often pointed to as models that Americans should consider emulating. For example, Québec bans fast food marketing to youth, and Germany limits celebrity endorsements and other "fluff" in television ads, which are meant to be strictly informative of the nature of the product or service.

Current interpretations of First Amendment law focus on the right of the individual to *receive* information freely rather than on the right of the organization to communicate. Known as "the diversity principle," it serves as the moral linchpin for government intervention in the marketplace of ideas to encourage, in the words of the Supreme Court from *Associated Press v. United States* of 1945, "the widest possible dissemination of information from diverse and antagonistic sources." Issues communicators committed to two-way communication have no problem with the theory of diversity. Unfortunately, the practical aspect of government intervention through mechanisms such as the misnamed broadcast *Fairness Doctrine* (in force in the United States until the 1990s) has not proved particularly effective in policing fairness. All too commonly, the empirical result has chilled speech to the point that only those views most acceptable to regulatory authorities are actually given an airing.

There is some irony in this and a moral as well. Undoubtedly, conspiracies and evildoing *do* exist in the world. But given all we know about competition and human nature, it is particularly far-fetched to believe that there exist a series of monolithic interests in the large sector of the economy represented by business. For good or bad, social problems require real solutions and a level of independent resources only the corporate community can mobilize. This is the positive aspect of having deep pockets capable of underwriting a wide variety of organizations and activities. Indeed, as the source of disclosure for their organizations, communications practitioners contribute meaningfully to diversity. Despite the widespread use of persuasive doublespeak and George Orwell's warning of a memory hole, public communications do have a certain historical permanence that creates a traceable record. This makes for accountability. Even most nonlibertarians recognize that the more pristine corrective for unethical corporate behavior involves what happens to those who bring discredit to themselves, their organizations, and their profession.

—Richard Alan Nelson

See also Advertising Ethics; Capitalism; Cause-Related Marketing; Corporate Citizenship; Corporate Issues Management; Corporate Political Advocacy; Corporate Public Affairs; Corporate Rights and Personhood; Corporate Social Responsibility (CSR) and Corporate Social Performance (CSP); Corporate Social Responsiveness; Employee Monitoring and Surveillance; Employee Relations; Ethics of Dialogue; Fairness; Federal Communications Commission (FCC); Federal Trade Commission (FTC); Freedom and Liberty; Greenwashing; Libertarianism; Public Relations; Public Relations Ethics; Strategy and Ethics; Utilitarianism

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Ethics Training Programs

Organizations traditionally have conducted training programs to educate their employees. With the increased attention to ethical behavior, many organizations have created, or expanded, their ethics training programs. The result is that organizational ethics training has become a billion-dollar industry annually. There are many reasons why organizations offer ethics training programs:

- To further communicate and explain the organization's policy on business ethics conduct to current employees
- To introduce new employees to the numerous expectations regarding legal and ethical standards
- To establish or further reinforce the organization's ethical culture
- To communicate to employees the importance of senior management with regard to ethical behavior in the workplace
- To enhance employees' awareness of potential ethical challenges they may face at work
- To provide employees with an ethical decision-making framework to use at work when confronted with an ethical dilemma
- To avoid the potential for litigation against the organization due to employee wrongdoing
- To minimize the liability assigned to an organization by the courts guided by the U.S. Corporate Sentencing Guidelines

Extent of Ethics Training

Numerous surveys have been taken to assess the extent or frequency of ethics training programs. The survey results differ widely based on the size or type of the organization investigated or the frequency or depth of the ethics training.

According to one study, 95% of the Fortune 50, the world's largest companies, have ethics training programs. Another study found that 86% of the companies surveyed trained their managers in ethics, but only 35% of these companies offered ethics training to their hourly employees. A little more than half the local governments (58%) provide ethics training for their employees.

Other reports provide a much lower number. For example, a survey of the Fortune 1000 firms revealed only 25% of the firms having ethics programs. Another study, which included firms of all sizes, found that only 20% of the firms responding to the survey reported having ethics training programs. The authors of this research noted that the size of the organization is a significant determinant of the existence of an ethics training program.

A more in-depth study questions the relatively high percentages of ethics training. These researchers reported that less than 25% of the employees surveyed reported that they had received ethics training on an annual basis. Most of the inflated reports of ethics training may be due to ethics training being offered to employees only at orientation or infrequently or due to inconsistencies in what constitutes ethics training—whether it is legal compliance, such as sexual harassment training, or training that focuses on improving employees' ethical decision-making processes.

Reports of widespread ethics training also may need to be considered in terms of how in-depth it is. One study found that the typical ethics training program lasted only about 1 hour. Very few companies provide a half-day or full day for ethics training annually.

Many believe that the number of ethics training programs will increase with the ethics scandals uncovered at Enron, WorldCom, Adelphia, and other companies. Scholars believe that the incentives embedded in the U.S. Corporate Sentencing Guidelines and the Sarbanes-Oxley Act, to reduce criminal sentencing for those found guilty or the likelihood of prosecution for regulatory violations, will encourage organizations to communicate ethical standards through training programs.

There are an increasing number of resources to assist organizations in developing or enhancing their ethics training programs. Hundreds of ethics training consultants advertise on the Internet, and there is a cottage industry of ethics training resources available through many Internet-based companies. For example, LRN (The Legal Knowledge Company) offers more than 150 interactive ethics training courses on topics ranging from money laundering to conflicts of interest.

Types of Ethics Training

Ethics training programs, like other types of training, take many different forms. Ethics training can be live, where the trainer meets face-to-face with employees. Live ethics training enables the trainer to interact with the participants and immediately handle questions that arise from the training. Some organizations use videotapes or CDs containing ethics presentations or Web-based intranet ethics training for their employees. It may not be financially prudent for a global company to have ethics trainers visit every plant or office, so training videotapes or CDs or the company's intranet are used for ethics training. Intranet training also enables employees to take the training at their convenience, possibly in the evening after work hours or during weekends. The debate regarding the financial efficiency of offering ethics training through videotapes, CDs, or the company's intranet versus offering training live undoubtedly will continue for many organizations. Some organizations use a combination of live and prepared presentations, where the company's CEO, for example, presents a taped message, and the trainer engages the participants in a live case study session.

Information can be communicated through lecture presentation or discussions of hypothetical or real case studies, with the participants using ethical decision frameworks or cognitive reasoning processes to analyze and resolve the cases. Lecture presentations may be appropriate if the ethics trainer is seeking to instruct participants on new regulations or technical information. Researchers argue that, in general, engaging the participants in case study discussions based on real-work situations may be the most effective form of ethics training.

Ethics training can take the form of role-playing exercises, where employees assume the personae of actors involved in an ethical dilemma taking place at work. This type of training may enable the participants to grasp more deeply the ethical challenges embodied in a situation or come to understand how the other person may feel when affected by their actions when resolving an ethical dilemma.

Finally, some ethics training is achieved through the use of role models or socialization, drawing on individuals from the organization or targeting exemplary ethical individuals from history as examples of how people should decide or act in the workplace. If the organization has a former leader or founder who exemplifies ethical behavior, this individual may be a good role model for new employees in the company. Ethical leaders from history may be used as examples of how someone stood up to ethical challenges or used his or her strong moral character to act ethically despite the risks or costs. People often learn from examples, and ethics training can use ethical role models in this manner.

Approaches to Ethics Training

Other important considerations include when the training should be conducted, how often it should be offered, and who should lead the training program. Sometimes ethics training occurs at the employee orientation session for new employees or employees of an organization acquired through acquisition or merger. Researchers have found that ethics training at orientation is the most common form of ethics training, yet some question its effectiveness, as will be discussed later. Ethics training also can be conducted on an annual or periodic, as needed, basis. Some organizations set aside one training program a year or require employees to complete at least one ethics training session during a calendar year. Other organizations prefer to conduct training after a new set of legislation or regulations comes into effect or after an ethical breach has occurred at work.

Some ethics trainers are in-house personnel from the organization's human resources or legal department, while other organizations use outside ethics consultants, professional trainers, or academics. There is significant debate regarding who makes a better ethics trainer. Those preferring to use in-house personnel argue that these individuals are more familiar with the organization's culture and how things are done in the company. They may be better able to provide explanations of how the ethics guidelines best fit with the company's policies and procedures. Human resources or legal personnel may have a better grasp of other, related company policies that affect or appear to be in conflict with ethics expectations. The use of in-house staff, in most cases, is more cost-efficient because these individuals already are on the company's payroll. Employees may be more likely to "buy in" to the program if it is delivered by someone within the organization and particularly if senior management is involved in the ethics training delivery.

Others believe that having someone from outside the company enables the participants to be more open and honest about their concerns or to discuss questions of ethics with someone who does not have direct authority over them at work. Employees may be inhibited during an ethics training session if the employee's boss or supervisor, who evaluates the employee's performance, is conducting the training. In addition, managers may not be well versed in ethics or moral reasoning and, thus, may not be very effective in leading the discussion requiring ethical analysis or in a program that attempts to enhance employees' moral development. Trainers based at the company's headquarters may have difficulty in conducting training at remote company sites due to possible cultural or language barriers. Local employees may resent someone coming in from outside the culture to teach them ethics, whereas a local consultant or academic may be more effective in communicating with the employees at that location.

Effectiveness of Ethics Training Programs

Whether an ethics training program is effective or not is a difficult question to answer because the objectives of the training program often are unclear or multifaceted or one's ability to measure training outcomes may be complex. However, many researchers have tried to address this important question. Very promising results concerning the effectiveness of ethics training programs have been reported by scholars. Some researchers have found that employees who have taken ethics training reportedly are more likely to refuse to take an unethical action while at work. Others have found that ethics training negates in employees the feeling that they must be unethical to get ahead in the organization.

However, some findings do not support the effectiveness of ethics training. For example, one scholar reported that only 1% of those who received ethics training believed that it made a difference for them at work. This is a disheartening result for those who hope that ethical behavior at work can be improved through training.

Why do some ethics training programs fail while others succeed? Some scholars found that an emphasis on legal compliance in the training program (which is fairly common in ethics training programs) was less effective than a focus on improving the participants' moral judgment. As discussed above, some training programs simply present legal compliance information, while others focus on challenging the participants to use ethical decision-making frameworks or cognitive moral reasoning processes. It appears that using the latter is more likely to improve the effectiveness of ethics training.

Another study reported that the least effective training is that delivered by an outside consultant using a prepackaged or canned training program. This result argues for tailoring an ethics training program to the demographics or type of work performed by the employees of the department or organization being trained. One size apparently does not fit all.

It also is important to note that many organizational ethics training programs do not contain an evaluation or assessment process. One scholar reported that the lack of evaluation may be reflective of the organization's intention to create a window-dressing ethics training program rather than a program that seeks to improve the employees' ethical awareness or decision-making skills.

In terms of being effective, researchers have found that the method used in the training program is vital. The use of role-playing situations or case studies tends to improve the training program's effectiveness. It also is important to teach employees how to make good ethical decisions by focusing on their moral reasoning skills, which reportedly results in long-term benefits for an organization.

Another effectiveness element of ethics training consists of selecting a trainer who also is the direct report manager for the participants. This interaction is critical because the participants need to believe that the manager wants the employees to behave ethically and the employees need clear guidance regarding how the manager wants them to act at work. The manager also needs to engage the employees in discussions involving job-specific dilemmas to achieve a high level of training effectiveness. The training must be relevant to the daily work of the participants rather than involve the consideration of hypothetical situations that rarely, if ever, occur at work.

In conclusion, for an ethics training program to be effective, the program should contain the following elements: live instruction, small class size, significant group interaction, a minimum of 4 hours of instruction, the separation of ethics from legal expectations, participant assessment of the ethics training program, and follow-up communications with employees after the training session. The ethics training also needs to be linked to other ethics components in an organization's ethics program, such as the company's code of ethics. Training also should be coupled with mechanisms that assist employees in reporting unethical work conduct, such as through an "open-door policy" where employees can come to their supervisor with any concern or through a company-sponsored help or assist line where employees can call anonymously if they have a question or want to report a breach of ethical conduct. Finally, ethics training should be associated with a periodic review and revision of the company's ethics program by all employees, not just managers.

—*James Weber*

See also Cognitive Moral Development; Corporate Ethics and Compliance Programs; Dilemmas, Ethical; Ethical Culture and Climate; Ethical Decision Making; Legal Ethics

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European Union

The European Union (EU) is an economic and political coming together of European countries. It is not a federation like the United States of America, nor does it operate as an international organization for political or military cooperation, like the United Nations or the North Atlantic Treaty Organization (NATO). Instead, the (sovereign) member nations have decided to pool their sovereignty and delegate some of their decision-making powers to common EU institutions, which act in the interests of all member states. This way, the EU member countries have gained economic and political power that they would be unlikely to achieve individually. In 2004, approximately 380 million people lived in the EU. The EU's large size and the shift in decision-making power from the national level to more central EU institutions (see below) have also presented some obstacles to furthering European integration, most recently in the form of French and Dutch voters failing to approve of the proposed EU constitution.

Origins

The idea of European integration is more than a half-century old. After World War II, it was established in France in 1950 when the French Foreign Minister Robert Schuman encouraged economic integration, in the form of the European Coal and Steel Community. After initial successful cooperation, its six original founding countries (France, West Germany, Italy, Belgium, the Netherlands, and Luxembourg) decided to tighten their economic links by removing trade barriers between them and forming a "common market." For this purpose, the Treaty of Rome, signed in 1957 by the governments of the six member nations, created the European Economic Community (EC) and laid the foundation for further expansions of the EC.

The Treaty of the European Union, also known as the Treaty of Maastricht, signed on February 7, 1992, created the EU. This treaty comprises two major sets of provisions. The first set defined the steps for the establishment of an economic and monetary union. The second set described the steps toward the achievement of a political union, including common foreign and defense polices.

Member States

The EC expanded in 1973, when Denmark, Ireland, and the United Kingdom joined it. Greece followed in 1981, Portugal and Spain in 1986, and Austria, Finland, and Sweden in 1995. Ten other, mostly Eastern European, countries gained access in 2004. In May 2005, the EU consisted of the following 25 member states: Austria, Belgium, Cyprus, Czech Republic, Denmark, Estonia, Finland, France, Germany, Greece, Hungary, Ireland, Italy, Latvia, Lithuania, Luxembourg, Malta, the Netherlands, Poland, Portugal, Spain, Slovakia, Slovenia, Sweden, and the United Kingdom. Bulgaria, Croatia, Romania, and Turkey were candidate countries in May 2005.

Institutions of the European Union

The EU consists of three core institutions. The European Commission, the Council of the European Union, and the European Parliament (EP) form the institutional triangle that creates Europe-wide policies and laws. These institutions were originally established with the launch of the EC in 1957. These institutions are involved in decisions of joint interest at the European level. Three pillars circumscribe the institutions' activities. Fields of interest concerning member states' delegation of decision making to the EU institutions can be found in Pillar One of the EU. Pillar One includes institutional and legislative procedures, agricultural policy, the internal market, the environment, citizens' rights, economic and monetary union, and regional policy. Activities in areas that are not subject to the EU institutions are organized through intergovernmental cooperation. These areas are covered in Pillar Two, which contains provisions on a common foreign and security policy, and Pillar Three, which provides for cooperation on justice and member states' domestic policies. Pillars Two and Three play quite important roles as the EU operates under the principle of subsidiarity—that is, the intention to accomplish as much as possible at the level of the member states.

In addition to the three core institutions, there are a number of supportive EU institutions. Two judicial bodies monitor and check legal and budgetary compliance, namely, the European Court of Justice and the Court of Auditors, respectively. Furthermore, the EU has several advisory (e.g., the Economic and Social Committee), financial (e.g., the European Central Bank and the European Investment Bank), and cross-institutional bodies (e.g., the Office for Official Publications), as well as 16 decentralized agencies. However, the following discussion focuses on the three core institutions of the EU. Figure 1 depicts the institutional triangle of the EU as well as the main functions of these three institutions.

The European Commission

The European Commission is the executive body of the EU. It proposes legislation and policies and formulates legislative proposals for discussion at the Council of the EU. It is responsible for implementing the decisions of the EP and the Council. Furthermore, the Commission is responsible for managing the EU budget and various programs adopted by the EP and the Council. Finally, it negotiates international agreements on behalf of the EU and represents the EU internationally. These executive functions are one important administrative aspect of the Commission. Another important aspect is its character of a politically independent institution that embodies the European idea. Although nominated by their national governments, the members of the Commission have no obligation to them. They are (supposed to be) loyal to and act in the interest of the EU as a whole. As such, the Commission is the driving force within the EU's institutional system, initiating, implementing, and supervising common actions, programs, and policies.

Members of the Commission are known as *commissioners.* As the EU has increased its membership, the number of commissioners has risen from 20 to 30. For the Commission's activities to remain manageable, its size had to be limited. As of 2005, there were 25 commissioners (one from each member state). The Council decided that in the future, the number of commissioners

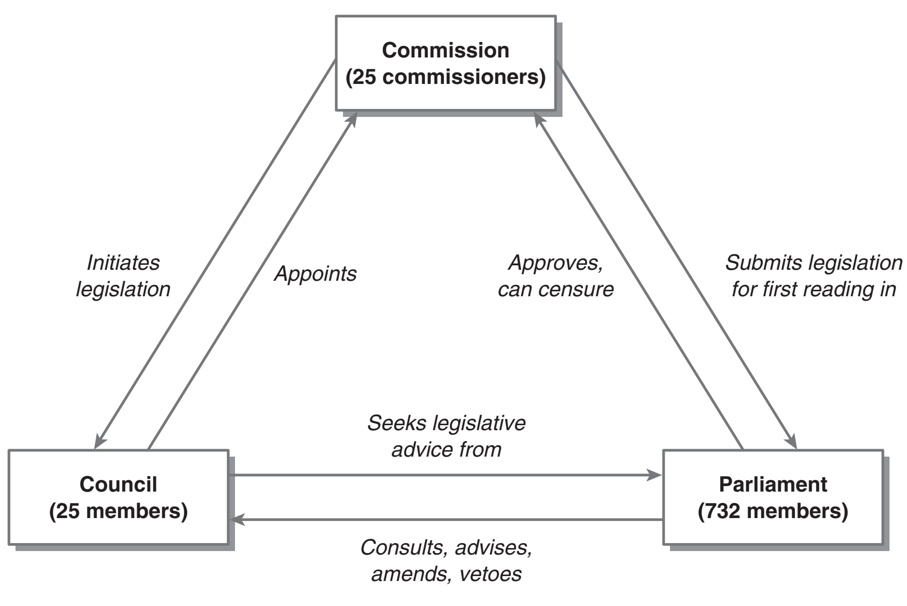

Figure 1 The Three Core Institutions of the European Union

should not exceed 27 and their nationality would be determined by a system of rotation. Commissioners are appointed for a 5-year term by the Council (see description below). The Commission is based in Brussels, Belgium, but has representations in all EU countries and delegations in many capital cities around the world.

The Council of the European Union

The Council of the European Union is the EU's main decision-making body. As the Council is made up of heads of government, it represents the particular interests of each member state. The Council has a dynamic membership; that is, one minister from each of the EU national governments attends the meetings, with different ministers attending different sessions, depending on the agenda topics of each meeting. Thus, the Council is not a permanent body but a series of committee meetings. Altogether, there are nine different Council responsibilities: general affairs and external relations; economic and financial affairs; justice and home affairs; employment, social policy health, and consumer affairs; competitiveness (internal market, industry, and research); transport, telecommunications, and energy; agriculture and fisheries; environment; and education, youth, and culture.

The most important role of the Council is its legislative role. In consultation with the EP, the Council decides on legislation proposed by the Commission. The Committee of Permanent Representatives (i.e., ambassadors to the EU) plays an important part in the EU legislation process. This committee considers proposals before passing them on to the Council. The presidency of the Council rotates every 6 months. The president is assisted by the general secretariat, which prepares the activities of the Council.

Decisions in the Council are usually (with few exceptions) made under a system of *qualified majority voting*. In this voting procedure, member states are allocated votes roughly in proportion to their population size. Since November 1, 2004, the total number of votes has been 321. Germany, France, Italy, and the United Kingdom have the largest number of votes, 29 each. A qualified majority on a proposal is reached when it is approved by the majority of member states *and* when a minimum amount of votes (72.3%) are cast in favor of the proposal. In some cases, such as the common foreign and security policy, taxation, and immigration policies, decisions have to be unanimous.

Three other important roles of the Council include (a) coordinating the broad economic policies of the member states, (b) negotiating international agreements between the EU and non-EU countries or international organizations, and (c) jointly with the EP, approving the EU annual budget. All these functions, including legislative functions, concern Pillar One of the EU, where the member states have decided to delegate decision-making powers to the EU institutions. In addition, the Council issues guidelines and coordinates cooperation on matters over which the member states have retained independent control but nevertheless decided to work together (i.e., Pillars One and Two). These are the areas of a common foreign and security policy, the police force, and judicial cooperation in criminal matters.

The European Parliament

The EP is elected by the citizens of the EU. Since 1979, parliamentary elections have been held every 5 years. The EU Parliament brings together all the main political groups operating in the EU member states. The EU ministers of Parliament sit in cross-national political groups (i.e., EU-wide parties), of which there have been seven since 1999.

The EP has three main roles: a legislative role, a supervisory role over the Commission and the Council, and a budgetary role. The legislative role is primarily an advisory role because to enact a law, the EU Council first needs to consult with the EP in a large number of areas. The EP is also invited to comment on any policy directives proposed by the Commission, a role that it shares with the Council. The EP's supervisory role, outlined in the Treaty of Rome, allows it to question and control the decisions made by the other EU institutions. It also includes the right to censure and dismiss the Commission as a body. The EP shares its budgetary role with the Council. No budget may be adopted without its agreement.

The powers of the EP have been significantly strengthened by the Maastricht Treaty of 1992. In the area of legislation, the EP is intensively involved in the process of consultation and *codecision*, which means that it shares legislative power with the Council. The EP can initiate actions of the Commission and has the right to veto certain legislation. In addition, it is authorized to appoint a European ombudsman, who acts as an intermediary between the EU citizens, business, and the EU authorities. The ombudsman is entitled to receive and investigate complaints of misadministration in the EU institutions. The EP's power also extends to approving the newly elected Commission and installing temporary committees of inquiry, which examine petitions from citizens.

Major Treaties

The treaties lay down the rules and procedures that the EU institutions must follow. They are entered into by the member states' presidents and prime ministers and ratified by national parliaments.

After the foundational 1957 Treaty of Rome, a number of other treaties, acts, and protocols have been signed by the member states over the years. The most important treaties include the following:

- Treaty of Brussels (signed in April 1965) defined the administrative structure of the EC by integrating the European Coal and Steel Community (ECSC) and the EC.
- Single European Act (signed in 1986) increased the legislative power of the EP, specified the realization of a common market, and adjusted voting procedures in the Council of the European Union (then the Council of Ministers).
- Treaty of Maastricht (1992) created the EU.
- Treaty of Amsterdam (signed in October 1997) clarified arrangements for common foreign and security policies and extended the powers of the EP. It instituted major human rights provisions, including free movement of persons, opening of internal borders, and social policy.
- Treaty of Nice (signed in February 2001) established the rules for the expansion of the EU. It created a new set of governing rules for the EU institutions and clarified the way they will work in the future.

Business Inside and Outside the EU

International business is affected by various EU features and institutions. First, its competition policy (mainly expressed in Articles 81 and 82 of the Treaty Establishing the European Community, that is, the Treaty of Rome of 1957) has the goal of balancing market integration with the precedent of U.S. antitrust law. Although European law allows defenses (e.g., economic consequences) barred under U.S. law, the consequences for business are often similar. For example, Microsoft had concurrent antitrust investigations and lawsuits in the United States and Europe. Second, like the United States in the late 1970s and throughout the 1980s, the EU has embarked on a course of market opening and privatization, leading to generally greater competition, which has benefited customers in various ways (e.g., in the form of drastic reductions in the prices of airline tickets). However, until very recently, the EU was more hesitant than the United States in abandoning agricultural subsidies and its bureaucratic social and labor market regulations. In fact, the current backlash among some EU citizens against greater European integration may be an expression of voter anguish over the importance of social-democratic welfare state features (and over the loss of member nations' cultural identity).

In its nonmarket strategizing, international business has often had to adapt to member states' corporatist structure, which means that national business associations often work with, but also co-opt, the agencies regulating organizational practices. Although the unionization rate in most EU countries tends to be higher than in the United States, business and union relations in Northern and Central Europe are often more cooperative and less adversarial than in Anglo-Saxon countries. One of the areas in which these business-government negotiations led to a compromise was the Kyoto Protocol and the EU's ecological leadership; the EU has now introduced a pollution credits trading system, which is, relative to a carbon tax, the solution preferred by industry for its economic efficiency.

Conclusion

During the past 50 years, the European Union has developed into a unique integration among European nations. It has established a single European market, launched a single European currency (the euro), developed common policies ranging from agriculture to defense, and developed a unified European voice in world economy and politics. From the initial economic cooperation among a few European countries, the EU has evolved toward a multilateral set of close economic, political, social, and environmental partnerships. However, in this and a few other areas (e.g., the debate about the candidature of Turkey), challenges remain. The upheaval brought on by the French and Dutch "No" votes on the new proposed EU Constitution in 2005 may considerably slow progress on further European integration. It has, at the very least, introduced a lot of uncertainty about the vision of a common European future, although several core member states (including Germany) had already ratified the new EU Constitution in their national parliaments.

—Marc Orlitzky and Ljiljana Erakovic

See also Agribusiness; Agriculture, Ethics of; Antitrust Laws; Capitalism; Deregulation; Kyoto Protocol; Market Socialism; Mergers, Acquisitions, and Takeovers; Monetary Policy; Multinational Corporations (MNCs); Privacy; Privatization; Regulation and Regulatory Agencies; Socialism; Subsidies; United Nations; Value-Added Tax (VAT)

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European Union Directive on Privacy and Electronic Communications

The 2002 European Union Directive on Privacy and Electronic Communications ("the Privacy Directive") and its predecessor, the 1995 Directive on the Protection of Individuals With Regard to the Processing of Personal Data ("the Personal Data Directive"), are legislative acts that work together to protect European citizens' and employees' e-commerce privacy. Since the first of the two directives became effective in 1998, they have affected U.S. companies attempting to do business with existing or potential customers and employees in the European Union (EU). Because of underlying philosophical differences between the United States and the EU concerning the scope and purpose of legislation and privacy interests, the EU directives' legal requirements do not mesh well with U.S. laws. A "Safe Harbor" for U.S. companies doing e-business in Europe has had mixed results, but according to an official EU study, U.S. companies are not fully complying with the Safe Harbor requirements.

Scope and Requirements of the European Privacy Directive

The directives' dual goals are (1) to ensure a high level of protection for individuals' privacy in all EU member states and (2) to enable the free movement of personal data within the EU. The directives protect four aspects of individuals' private data: (1) data quality, (2) legitimate processing of data, (3) rights of the individual whose data are being collected (the "data subject"), and (4) security of data. Data quality means that personal data must be processed fairly and lawfully; collected for explicit, legitimate, and specified purposes; relevant; accurate; and erased automatically when no longer needed. Legitimate processing means that personal data can be obtained only if the individual concerned has given his or her unambiguous consent. The data subject has a right of access to the information, the right to correct or block information that does not comply with the directive, and the right to object to the processing of data for compelling reasons. Finally, personal data must be secure. It must be protected from accidental or unlawful destruction or loss and against unauthorized alteration, disclosure, or access. Of concern to U.S. business interests is Article 25 of the 1995 Directive, which prohibits data transfers to any country that lacks an adequate level of personal data protection. In the EU's opinion, U.S. law does not provide the requisite level of protection.

Differences in Legal Philosophy

European Union

Both the United States and the EU strive to protect human rights, but they differ in terms of what type of entity is likely to present a threat to those rights: The

United States has typically viewed overgrown governmental power as the most likely threat to civil liberties. Thus, in the United States, laws protecting human rights usually focus on limiting governmental powers. In contrast, the EU focuses more on potential threats from private entities. The EU's historical foundation for this concern was the misuse of data collected by private industries in pre–World War II Germany, industries that subsequently aided the Nazi attempt to eliminate targeted groups. Thus, data protection laws in Europe are focused more on limiting the powers of private entities to collect and keep data, while limiting governmental power to do the same is of lesser importance than it is in the United States.

United States

In contrast, Americans historically have a fundamental distrust of governmental intervention into the private sphere: Much of the controversy over the ratification of the Constitution was based on a concern that the new U.S. Government would gain too much power over individuals. Thus, in the United States, the government's power to collect personal information is limited. Americans traditionally are less concerned about how private industry collects and treats personal information. Consequently, most existing legislation does not include privacy safeguards, or if it regulates such safeguards between business and consumer or citizen and government, it does not address employment relationships. Similarly, the common-law concept of invasion of privacy has rarely been applied in the context of private industry, as opposed to continued concern over governmental intrusion into the right of privacy read into the Fourth, Fifth, and Fourteenth Amendments by the Supreme Court. Nevertheless, there have been some changes due to a rising momentum with regard to general privacy issues in the United States. For example, health care providers are required under federal law to advise patients about exactly how and when they will release personal data.

The Safe Harbor and Its Effects

After the adoption of the EU Privacy Directive, the U.S. Government engaged in intense negotiations with the EU to resolve the discrepancies in privacy policies and facilitate e-commerce between the two entities, their citizens, and their industries. The product of the negotiations was the adoption of the Safe Harbor agreement in 2000. Under this agreement, a U.S. company soliciting personal data from a citizen or a company in the EU must voluntarily demonstrate that it will protect the data according to seven criteria: notice, choice, onward transfer, access, security, data integrity, and enforcement. Thus, it must (1) notify individuals about the purposes for which it is collecting and using personal information, (2) give individuals the choice of opting out and refusing to provide the information requested, (3) apply the "notice" and "choice" requirements before transferring information to a third party, (4) give individuals access to their personal information, (5) take reasonable precautions to protect the security of the information, (6) ensure that the data collected be reliable, accurate, complete, current, and relevant to the use for which it was collected, and (7) have a mechanism for enforcing Criteria 1 to 6. The Safe Harbor agreement is followed by U.S. companies on a voluntary basis. The expectation is that a company must first implement the seven Safe Harbor criteria and then notify the U.S. Department of Commerce of its compliance as well as declare its compliance on its Web site.

As of this writing, the effectiveness of the Safe Harbor has reportedly been dubious: U.S. companies have been reluctant to volunteer compliance, and the EU Commission of the European Communities found three major problems even among those that had so volunteered. The Commission found that voluntary statements of adherence were not always visible, and although some Web sites mentioned the privacy policy, they did not provide access to the self-certification. Less than half the privacy policies posted reflected all seven Safe Harbor criteria. Finally, in many cases, the policies did not provide clear instructions for individuals who wanted either to exercise their Safe Harbor rights or to obtain information on dispute resolution procedures.

The 1995 Directive and the EU-U.S. Safe Harbor, as well as antispam provisions in the 2002 Directive, create an additional layer of complication for U.S. companies wanting to do business in the EU. On the other side, U.S. legislation has made it more complicated for European companies who want to do business in the United States. Examples of U.S.-generated legislative complications are the Sarbanes-Oxley Act's whistle-blowing and other increased corporate compliance regulations, brought on by Enron and other corporate scandals of the early 2000s.

—Nadia E. Nedzel

See also Business Ethics; Corporate Ethics and Compliance Programs; Employee Monitoring and Surveillance; Enron Corporation; European Union; Global Codes of Conduct; Privacy; Sarbanes-Oxley Act of 2002; Whistle-Blowing

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Evolutionary Psychology

Evolutionary psychology is an approach to understanding any facet of the psychology field. It is concerned with how the mind is designed based on the assumptions and insights from evolutionary biology and evolutionary game theory. The purpose of evolutionary psychology research is to outline the blueprint of the mind and ultimately explain human nature. Evolutionary psychologists claim that the human brain was largely formed in primitive times, so to understand human cognition and behavior, it is necessary to evaluate the prehistoric conditions under which our ancestors lived.

The concepts and principles at the foundation of evolutionary theory can be applied to psychology based on the assumption that humans are a product of natural selection as a way of explaining behavior. This is a very different position from the one taken by most social science models of psychology. Standard models assume that human behavior is caused primarily by learned experiences and exposure to cultural influences. The standard social science model views the human brain as a tabula rasa, or blank slate, capable of unlimited flexibility. Contrary to that position, the evolutionary psychology field holds that human behavior is guided to a great degree by an interwoven set of psychological mechanisms that were formed by natural selection over time in response to various evolutionary pressures. Evolutionary psychology is a positivist approach to the design of the mind. It examines which adaptive problems the human mind is hardwired to solve and infers the structure of the brain in virtue of individuals' abilities to solve those problems.

Natural Selection and Evolutionary Biology

Driving evolutionary psychology is evolutionary theory. Critical to the theory of evolution is the fact that humans' primitive ancestors were faced with various selection pressures that compromised their survival. Charles Darwin described evolutionary theory as the progressive modification of species in which design features are altered over time to enable species to adapt to their environment. For improved designs to accumulate and be transferred to kin through genes, members of a species must be able to propagate. An adaptation is simply a successful design feature at a particular moment in time that aids the species to continue. Natural selection is the process by which successful features are passed down from one generation to the next and less successful features eventually are phased out. Over countless generations, the natural selection process designs organisms that are continuously better suited to coping with the current environment. Each design modification serves a particular purpose, or function, for coping with the surroundings. These new designs are transferred from one generation to the next through sexual reproduction. Traits useful to a species cannot be sustained by the species if its members do not reproduce.

Evolutionary biology is specifically concerned with the formation and perpetuation of physical traits in the development of a species. Traits such as humans' eyes, sense of smell, and hands all served a purpose for our ancestors and aided in their survival. These physical features enabled our ancestors to solve adaptive problems in the prehistoric environment, such as locating food and enemies and grasping objects. Researchers in the field of evolutionary biology induce the physical design features of organisms by discovering the adaptive problems those structures and traits solved in the Pleistocene environment.

Principles of Evolutionary Psychology

This same design logic is applied to evolutionary psychology in terms of the design of the mind. Some of the adaptive problems that faced primitive humans involved social exchanges (a mutually beneficial relationship between at least two cooperating parties). Hunter-gatherers often needed to cooperate with each other to accomplish tasks that could not be done alone (i.e., obtaining food, protecting kin). According to the evolutionary psychologists, natural selection favored programs in the mind that solved these problems with efficiency and precision. Each organ of the body, including the brain, solved a particular problem in ancestral environments. All human design features, both physical and mental, were formed and developed in these ancient environments. Evolution and the process that drives it, natural selection, operates in a slow and incremental manner. Any program or phenotype takes millennia to develop. Modern societal environments are very recent in evolutionary history and constitute a minuscule percentage of human existence. Evolutionary psychologists claim that our minds were formed during the Pleistocene period.

Due to the short amount of time the human species has been exposed to modern social environmental arrangements relative to the evolutionary historic timeline, the evolutionary psychologists posit that primitive environments had a profound and powerful influence on shaping the human mind. New physical features and cognitive programs have not had enough time to adapt to present conditions. Individuals' minds became hardwired to solve various tasks necessary for social exchange relationships. The brain slowly developed programs to solve particular survival problems. A common analogy is to compare the human brain with a computer in that it is designed to process information about the surrounding environment for directing behavior. Thousands of years were required to incrementally build the complex cognitive system capable of promoting survival behaviors. To understand the design of the mind, researchers essentially reverse engineer the brain by attempting to discover the conditions under which ancestral humans lived. Once the particular challenges facing our ancestors are identified, the evolutionary psychologists are able to induce the functional purpose of the circuits in the brain. The specific programs in the brain frame the way individuals perceive the world.

What is problematic for modern-day humans is that the circuits designed over time to regulate behavior and tackle certain primitive dilemmas may not be adapted to properly interpret contemporary cultures and conventions of society. This is particularly relevant to business ethicists. Leda Cosmides and John Tooby speculate that the context-specific programs that once solved prehistoric problems with precision and speed could even be responsible for shaping cultures among people.

Social Exchange

The relevance of the evolutionary psychology approach to business ethics rests on the premise that social exchange relationships are necessary for organizations to conduct business. From an evolutionary perspective, social exchange would only be selected if it aided in humans' ability to survive and propagate the species. For it to become an evolutionarily stable strategy, both parties to an exchange would have to elicit a cost in order to conditionally receive a benefit. Specifically, neural programs responsible for regulating conditional reasoning on social contracts are required for social exchange to take place. Using models from game theory to identify when social exchange would stabilize in a population, evolutionary psychologists were able to identify the specific skills necessary for reciprocal relationships. Individuals must have the ability to detect cheaters on particular social contract conditional rules and must also be able to direct future provisions to contracting partners who reciprocate. Cheaters are individuals who accept a benefit without paying the cost required by the conditional rule. It is posited that individuals' brains are hardwired with social contract circuits designed to serve the function of calculating the costs and benefits of a social exchange with a subfunction of detecting cheaters on social contract rules.

Empirical evidence exists that individuals are adept at detecting cheaters on conditional rules framed as a social contract but not on general permission-type conditionals or simple abstract logic. This lends additional support to the notion that the circuits in the brain are indeed specific to a certain problem. Since the violation of rules in business has ethical repercussions, the hypothesis that individuals are hardwired with the neural architecture designed to reason through social contracts is of interest to the business ethics field.

While these arguments are dyadic in context, in business, cooperation among three or more people is commonplace behavior. In nature, this kind of coalition forming is an anomaly except to the human species. In game theoretic terms, the impulse to free ride on a cooperative venture would become a stable strategy for dealing with relationships if it was evolutionarily advantageous. Rather, the evolutionary psychologists purport that since participation in nondyadic groups is the norm among individuals, cognitive machinery designed to punish free-riding behavior must have evolved for participation to have spread through the population. Punitive sentiments toward free-riding individuals (violators of social contracts rules) evolved over time as a moral device that served to eradicate the advantages of that behavior. Punitive sentiments are manifested in modern-day business in the form of lawsuits and the disintegration of relationships.

Critics

The alternate hypothesis to the evolutionary psychology approach is that the brain is highly malleable; that human experiences are a strong enough influence to shape the mechanics and structure of the mind. Critics of evolutionary psychology focus not only on creationist or intelligent design perspectives of human existence but also on the fact that the primary assumptions of the approach are dependent on mere hearsay. Predictions regarding the structure of the mind are proposed based on an inference about what prehistoric conditions were like. If the causal relationship between ancient conditions and physical and mental forms cannot be established, then the theory is invalid.

Other researchers have offered the possibility that the architecture in the brain is not context specific but context general. On the other side of this debate in the evolutionary psychology field is the proposition that logical reasoning comes from pragmatic reasoning schemas. This side argues that our ancestors had to consistently discover practical solutions to everyday problems and that the brain is structured according to the classes of goals that had to be attained for survival. How people practically interpret environmental situations or dilemmas forms the basis of reasoning rules in the brain.

—David M. Wasieleski

See also Darwinism and Ethics; Game Theory; Reciprocal Altruism; Social Contract Theory

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Executive Compensation

Executive compensation refers to the total reward provided by the firm to the top level of executives in a corporation, such as the chief executive officer (CEO), the chief operations officer, the chief financial officer, and a handful of other executives who occupy the very highest level of management. At this level in the firm, total compensation generally takes many forms, including any or all of the following: salaries, bonuses, incentive payments, deferred compensation plans, stock options, and the direct provision of goods and services. Unlike direct cash payments of salaries, bonuses, and the like, the other forms of compensation can be relatively large and less visible. For example, stock options granted to executives are not generally visible to the public, yet they may be worth more than the direct cash payments the executive receives. Similarly, many executives receive quite valuable packages of perquisites ("perks"), such as apartments, personal staff, personal transportation, and the payment by the firm of many other expenses that most employees would have to bear themselves.

Social and Ethical Issues

Many observers see the size and form of executive compensation as a pressing social and ethical issue. These concerns have become particularly poignant in recent years as the public has become aware of the absolute magnitude and generosity of some pay packages. Furthermore, public attention has focused on numerous instances in which executives were rewarded very handsomely even as the firms they were supposed to be leading had floundered. Public indignation has arisen at the picture of very handsomely rewarded executives coupled with a firm that is experiencing financial losses, closure of facilities, and employee dislocations in the form of cuts in pay and benefits and enforced layoffs.

One of the most emotional aspects of the executive compensation issue is the absolute magnitude of executive compensations. For large firms in the United States, compensation for top executives can run into many millions of dollars per year. Some celebrated situations have arisen in which compensation for a single year can push toward $100 million, particularly if stock options are granted in that year. To some observers, the very size of this compensation seems totally inappropriate and even obscene.

Criticism of executive compensation has focused most intensely on practices in the United States, and critics of the present executive compensation practices often point to both domestic and international comparisons with the present level and structure of executive compensation that prevails in U.S. firms. Within the United States, critics of executive compensation point to trends in executive compensation relative to the total pay packages received by rank-and-file employees in the same firm. Most studies suggest that the ratio of executive compensation to that of ordinary workers has increased dramatically in the past few decades. In other words, executive pay seems to be rising much more rapidly than worker pay, and these critics present these data as evidence of a system gone wrong.

Two types of international comparisons play a prominent role in the executive compensation debate. First, executive compensation in U.S. firms appears to be more generous than in comparable non-U.S. firms. Studies have examined the absolute magnitude of compensation internationally as well as the ratio of executive compensation to ordinary worker compensation across countries. In general, studies have found that top executives in U.S.-based companies receive a higher level of absolute compensation (i.e., the actual dollar worth of the entire pay package) than similarly placed executives in non-U.S. firms. As a second type of international comparison, researchers examine the ratio of executive compensation to the pay of ordinary workers in U.S. firms versus the same ratio in non-U.S. firms. Most studies find a large difference in this ratio, with the executives of U.S. firms receiving a much higher wage relative to that of ordinary workers than is the case in comparable non-U.S. firms. Again, critics take this disparity as evidence of a flaw in the system in the United States.

Defenders of the present arrangement of executive compensation generally acknowledge the overall accuracy of the empirical claims summarized above and grant that executive compensation in U.S. firms is higher than it is abroad and also that executive pay in the United States has been rising faster than that of workers. These defenders of the present level and system of compensation often argue that these trends by themselves constitute no evidence that the present level is wrong or that the trend is moving in the wrong direction. To make such an argument, they assert, merely assumes that the previous levels were correct and that recent departures are in error. However, what if the previous levels of absolute or relative compensation were too low? Then, the movement toward higher executive compensation would be a movement toward a more appropriate level of pay. Similarly, international comparisons might carry little weight by themselves. If U.S. pay levels are high compared with those that prevail in other countries, it might just mean that the other countries have it wrong.

These reflections suggest that the issue must be examined at a deeper level to make real progress in understanding the social and ethical aspects of executive compensation. In particular, a more sophisticated examination of the issue might attempt to answer questions such as the following. Do executives deserve the compensation they receive? Does the present system of executive compensation serve the interest of society as a whole? Does the present level of executive compensation lead to an unjust allocation of a society's resources? Is the present arrangement of executive compensation simply the result of individuals and firms that exercise freedoms and make decisions that rightly lie within their control? Finally, what are the effects on society as a whole of a system in which some receive relatively so much and others so little? The remainder of this entry considers these issues in turn.

Desert

Could it be that executives deserve the compensation they receive? Top executives of large corporations control the deployment of vast resources in the form of the firm's financial worth, the work of thousands of employees, and even the use of the land and natural resources to which the firm has access. These executives make decisions that have extremely important social consequences. Committing the firm to the wrong investments can waste billions of dollars of wealth, destroy the livelihood of thousands of employees, and even drive the entire firm into bankruptcy. Similarly, the value of correct decisions at this level is gigantic. For example, IBM's decision to create the IBM PC in 1981 spawned an industry that revolutionized work around the world, created any number of related industries and firms, and sowed the seeds of some of the greatest individual fortunes the world has ever seen.

A gifted executive who could make the right decisions at these levels would create value for society that would dwarf even the most lavish executive pay package. Does such an individual deserve very high compensation for exercising his or her talents in a manner that is so socially beneficial? Many think that the answer to this question is clearly affirmative, and they tend to see firms as perpetually engaged in a search for such talent. According to this analysis, it is extremely wise to pay $100 million annually to an executive who can make decisions that would create $100 billion in wealth. Surely such individuals are rare and difficult to identify, but perhaps the hunt for and competition for those with this kind of potential is justified?

Critics of this desert argument reply by pointing out that actual executives seldom display such genius, and it is in fact easy to identify very highly paid executives who seem much more adept at making wrong choices and destroying value than making brilliant decisions and creating benefits. Beyond pointing out situations in which the actual performance does not seem to deserve high compensation, critics of the desert argument often maintain that no one could merit such compensation no matter how brilliant one's decisions. They argue that it is wrong for any individual to take so much for himself or herself, no matter how much benefit that individual might create for others.

Freedom

Some view the level of executive compensation as essentially unproblematic no matter what the level, subject to the basic constraints that compensation be determined simply by economic actors exercising their freedom to arrive at a contract. Here, the argument goes as follows: An executive, like any other worker, seeks the best employment contract available. The firm seeks the best managers it can find, subject to its own ideas about its willingness to pay and the perceived qualities of the potential executive. Both sides of the bargain, firm and executive, merely exercise their basic freedoms as economic actors in a free market and reach an agreement on that basis. As a result, the process is fair and leads to employment compensation that is fair simply due to its being the result of a market process that is seen to be a fair process by its very nature.

Furthermore, those who emphasize the importance of freedom of contract point out that freedom of contract benefits society, because the capitalist economic system works by allowing firms to make their own choices and to compete. For the executive, the freedoms being exercised are even more basic than they are for the firm, because the executive sells his or her own labor, so the sphere of freedom being exercised is very basic indeed.

In rebuttal to this line of argument, critics of the present system of executive compensation assert that the model of two independent agents striking an arm's-length bargain does not describe the situation very well at all, so the emphasis on freedom is misplaced. These critics point out that executive compensation is typically determined by the compensation committee, which comprises members of the firm's board of directors. However, membership in many boards is conferred directly or indirectly by the CEO of the firm. As a result, the very people administering the compensation of a CEO may owe their directors' seats to the same CEO, whose compensation they are supposed to judge and control.

Furthermore, top executives and board members are often friends, sometimes old friends of close standing. In addition, many directors serve on the boards of several companies, and CEOs of one firm often serve on the boards of other firms. This arrangement creates a class of directors and CEOs who flourish in a club-like atmosphere. As a result, the employment contract with the firm's top executive may not be a fair bargain struck by two completely independent parties. Instead, these critics argue, it may well be an arrangement of mutual advantage reached among friends, or at least it may be a situation in which directors are naturally empathetic toward CEOs who are part of the same managerial class. The result of this intimacy is a set of employment contracts for top executives that is the result not of a pure and free market process, these critics charge, but of an impure process tainted by ties of friendship or mutual appreciation.

Utility Maximization and Social Goals

Some observers of executive compensation focus on the overall benefits, or overall utility, of the present policy of executive compensation. These thinkers believe that the best approach to such an issue turns on the question of what arrangement will create the highest total societal benefit. As such, they are less concerned with what an executive might receive or deserve and instead ask, What system of executive compensation will create the greatest overall benefit for society? For them, the best system of executive compensation is the one that achieves the goal of maximizing social utility, which we may restrict to the narrower range of social wealth for conceptual convenience.

Even though these thinkers approach the issue from within a framework that emphasizes utility, they can often differ in the solutions they favor, because they disagree on which policies will contribute to utility. One group of thinkers attempting to defend the basic structure of executive compensation arrangements approaches the issue from the point of view of designing contracts. These thinkers analyze the problem in the following terms. The top executives of a firm are agents of the shareholders, who are the principals. The executives choose how to deploy the assets of the firm. The perfect agent would allocate those funds just as the principals would desire were they themselves present and able to make decisions. However, executives are not only agents of the shareholders but also persons in their own right, and thus, in their decisions as executives, they are torn between the pursuit of their own desires and the fulfillment of their role as agents of the shareholders.

This conflicted loyalty suggests that shareholders might achieve the best result for the firm by designing contracts with the firm's executives that align the incentives of the executives with those of the firm. This is the approach of *incentive compatibility*—making the incentives that the executives are offered compatible with the goals of the firm. The well-designed employment contract allows the executive to prosper when, and only when, the firm prospers. One tool for aligning incentives is the granting of stock options to the firm's executives. The properly structured option in this case is worth very little or nothing when the firm does poorly, but it is worth a great deal when the firm performs well. For example, a stock option given to an executive might pay off handsomely if the stock price of the firm rises by 50% over the next 3 years, but it might be worth very little otherwise. Under this model, the level of executive compensation is of relatively little importance. Instead, the goal is to structure executive compensation so that the executive acts to create more wealth for the firm even when the executive acts selfishly.

Critics of this line of argument charge that these kinds of arrangements abound in *contracting defects*—the failure of the compensation scheme to align the incentives of the executive and the firm. These critics point to numerous and well-publicized cases in which executives have been rewarded very handsomely even when the firm suffered horribly. When this happens, these critics protest, the incentives have not been aligned, and the result is a failure from the point of view of maximizing utility or the interests of society. As a result, opponents of the present structure of executive compensation still believe that allowing executives to absorb so much wealth diminishes overall utility.

However, merely saying that the present structuring of executive compensation has failed, in fact, to achieve compatible incentives is only a technical argument. It does not yet attack the central idea of attempting to align incentives, and it is clear that these critics are not merely calling for a technical rearrangement of contract terms. They very much believe that the entire level and structure of compensation is deeply flawed or even evil. While these deeper disagreements over utility and contract design may not have been fully defined, the terms of debate seem to be moving toward clarification.

Distributive Justice

While utilitarian arguments about executive compensation generally concentrate on the total utility effect of compensation arrangements, other critics of executive compensation approach the problem in terms of the distribution of societal resources. For them, the issue is not merely the total amount of wealth but how that wealth is distributed across persons and groups in society. Some critics maintain that the present levels of executive compensation offend against the principles of distributive justice. They maintain that a just society is one in which the distribution of wealth, goods, privileges, and positions across society meets certain conditions. These critics maintain that concentrating so much wealth in the hands of these few executives constitutes an unjust distribution of society's wealth and that justice requires new social arrangements aimed at preventing that concentration.

There are many alternative conceptions of distributive justice, and different theorists arrive at different principles of a just distribution, with radically divergent prescriptions for the allocation of the goods in a society. Considering one sample position on the issue of distributive justice can make the charge against the present mode of executive compensation more concrete by considering *egalitarianism*—the view that a just distribution of goods in a society is one of perfect equality. Egalitarians see the vast gap in wealth between executives and others in society and conclude that such a distribution offends against justice because the distribution is not equal. The egalitarian view resembles that of many distributive justice theorists who believe that a just distribution is one that can be measured against a particular paradigm of a just distribution. Egalitarians take equality as their paradigm, but other theorists allow for much more inequality and much more flexibility. However, it is fair to say that most of those social observers who focus on issues of distributive justice would be highly critical of the present mode of executive compensation.

In contrast, some reject the very idea that justice might require some particular pattern of distribution. They often argue that any actual distribution that results from processes of exchange that are free from coercion and deception is by its very nature a just distribution. These theorists tend to emphasize freedom of individual action and economic freedom rather than being concerned about how wealth actually comes to be distributed. As such, they regard the very concept of distributive justice as bogus, at least as it is framed by those who wish to maintain that there is some standard of justice to which the distribution of goods in a just society must conform.

Communitarianism

Communitarian critics of executive compensation argue that the present system harms the community. They tend to see society as a community held together by social bonds in a way that allows citizens to form an organic whole. Extremely high levels of executive compensation place a gulf between a patrician class of executives and the citizenry of workers. As such, this gulf breaks down the bonds of community, weakens society, and works toward a fractured community that is resolved into persons as atoms, unconnected and out of touch with each other.

The remedy for this situation, as far as executive compensation goes, is a system that strengthens the community of executives and workers, a result that can only be achieved by reducing the gap in pay that alienates the two groups from each other. This criticism differs from a focus on utility or distributive justice because it tends to give greater weight to organic wholes—firms, communities, or entire societies—instead of placing so much emphasis on individual persons. In contrast, while those who emphasize utility and distributive justice may agree with the communitarians on policy prescriptions, their concern with utility and distributive justice is still highly compatible with an emphasis on the individual.

Philosophers who take freedom of the individual as a prime value are the natural opponents of communitarians. Against the communitarians, they argue that attempts to build stronger communities by interfering with free contracting of firms with executives tramples on individual rights in a way that is impermissible. Instead, they believe that the right of free action for individuals has a primacy that trumps the pursuit of any social goal, whether it be the maximization of utility, the achievement of some distribution that others might deem to be just, or the building of strong community ties.

Conclusion

Executive compensation continues to attract public attention and to generate a lively debate. The lifestyles of executives made possible by the compensation they receive cannot fail to generate interest and even envy. The admittedly large gap between executive pay and that of workers is bound to support the continuing view that something is amiss with the system and that some injustice must account for the difference. However, this entry has attempted to indicate some of the complexity of the issue. Finding a proper solution to the issue of executive compensation will involve the same concepts that arise in the criticism of almost all social arrangements: desert, freedom, utility maximization or wealth creation, the distribution of wealth in a society, and the effects of all social arrangements on the structure and health of communities.

—Robert W. Kolb

See also Agency, Theory of; Communitarianism; Consequentialist Ethical Systems; Freedom and Liberty; Grasso, Richard; Incentive Compatibility; Justice, Distributive

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EXISTENTIALISM

Existentialism, as a philosophical theory, practice, literary genre, and human tendency, makes individual experience and self-reflection the bases for truth, knowledge, and value. Human reasoning alone does not suffice in supplying individuals their own reasons for action and morals; human emotions and passions also have moral authority. As in daily life, so too in work and business, individuals must construct reasons, meaning, and morality, assessing worth and value for their existence. Jean-Paul Sartre defined existentialism as a new form of humanism for the 20th century. In its radical turn inward, esteeming subjectivity, existentialism breaks from past philosophical tradition and legacy. Philosophers from Plato to Hegel held up objective, universal, impersonal standards of truth and morality. Soren Kierkegaard (1813–1855) made a personal perspective on truth the foundational insight for existentialism. Disparate groups of thinkers and writers—novelists, playwrights, psychotherapists, and filmmakers, as much as philosophers, theologians, and business ethicists—have called themselves or have been called existentialists. Existentialism encompasses both religious and atheistic forms (Christian, Hindu, and humanist), which differ in the source, process, and purpose of morally productive and happy individuals.

Existentialism typifies the subjective awareness of being and acting human in a nonhuman world. Especially, this interactive loop between the impersonal world and the personal (human) world creates anxiety, fear, and dread. These emotions arise from the individual's awareness of being abandoned, alienated, or lost in a world separate from the human self and its subjectivity. Altogether, these feelings give rise to existential nausea over one's human condition. Because humans are or feel abandoned by the world and by God or any independent, nonhuman guarantor and source of goodness and truth, they must learn to live with significant entailments. Troubling negative assertions follow: There is no common human nature; no given essence for beings and objects; no divine or unchanging plan, meaning, or purpose for human life or the world; no objective rationality or fixed norms for knowledge or morality; and no human determinism, only freedom. Standards of right and wrong, benefit and harm are not there for the asking or for human discovery. They are not found simply in doing our jobs and following norms. Still, creative positive assertions likewise follow: Humans are unique beings, free to create themselves by their choices and activities; humans, unlike plants, insects, and stars, are left alone to use and develop their own devices and capacities for language, rationality, productivity, and creative work.

Specifically, the existential claim that human knowledge and morality are perspectival (hence, only interpretations) renders the business life open to imposing human will and design on an apparently amoral, material, and social world. For there is no logic, science, or universal set of rules in the economic sphere of existence (or in any other). Individual workers and corporate executives alike are free, yet they must make their judgments and also be judged based on unavoidable personal or partial perspectives, arising from changing contexts of time, place, and role. Due to this unpredictability of the existentialist business model, either a corporate leader and philanthropist or a corporate raider may emerge in the system.

Everything one does or does not do hangs on individual integrity and moral fiber. There is no fixed rationale or unchanging business ethic for the individual to employ in determining value and worth, profit and loss, no preexisting bottom line for individual or collective action and planning. Existentialist business ethics thus excludes utilitarianism and duty-based ethics alike. Nor can one resort to the pragmatic rationale—it must be true and good because it works effectively or efficiently gets the job done. One must evaluate how and why some means and ends, values and endeavors are better than others are. Even choosing and expertly executing a business enterprise cannot save anyone from a lost life, for the business and its workers may not be contributing much toward their greater fulfillment and the improvement of society.

As in existential philosophy, so too in economics and work life, with absolute human freedom comes absolute risk. The premier principle of existentialism is that one is nothing more than what one makes of oneself. The existential mode of personal, moral decision making diverges from the customary structures in place to guide choice and action—family, religion, government, law, culture, science, and common sense. Existentialism, however, depicts how the self becomes liberated through the enlightened understanding that this existential predicament is shared by all. One can attain a sense of solidarity with others through committed engagement with causes and projects, privately through relationships, and publicly in the workplace under the contractual terms of business and labor.

Before existentialism, philosophers, theologians, and scientists offered alternative comprehensive systems to explain and control the world, characterizing reality either as a divinely created and sustained whole or, conversely, as a mechanistic, material world governed by necessary physical laws and discrete processes. Regardless of the theory, meaningful knowledge and morals were presumed to be discoverable and knowable to humanity, making reality more or less capable of human control, even mastery. Yet mere chance and the unpredictability of certain forces of nature make reality unknowable, hence uncontrollable, because these aspects are irrational, nonrational, and perhaps even divine. Such unknowable external forces may be the impetus for the broad existential vision of "the absurd," coined by Albert Camus. Consequently, when challenged by the futility of life, living in an absurd world of unpredictable realities and daily occurrences, one must choose and act, commit and be held accountable for what one becomes and what results from one's choice and activities.

Humans are condemned to be free, equally participating in the common paradox of being humanly free. Ironically, both existentialism and the traditional Plato-Kant philosophies share this core tenet: Being a free, self-determining person is the keystone of being moral. Sartre believed that by one's actions one is not only responsible for oneself but also responsible for humanity. Paradoxically, Sartre and the 18th-century Enlightenment philosopher Immanuel Kant accept this intertwining of individual morality, freedom, and personal accountability with collective responsibilities and social repercussions. Like Kant, Sartre held that when one judges and chooses something or an action as right for oneself, then that person de facto deems it right for all. For as humans, we are equal, equally solitary as individuals, needy, flawed, and vulnerable. Humans are chancelike creatures, subject to misfortune and disability, as well as controllers and distributors of goods and burdens, wealth and poverty, misery and well-being. In being responsible for their fates, humans learn that they are nonetheless free from the same limitations that bind them. Individuals become increasingly free and responsible in making the self and society. They do this, choice by choice, in selecting the projects they undertake and by completing or not completing those projects. The saying that you are nothing other than your life, however, does not entail that an individual is judged only by accomplishments but rather that the individual is the sum total of his or her productions, relationships, and projects.

For existentialists, being is doing. Yet in doing so, humans compete with outside forces—impersonal, inhuman influences of nature, societal and workplace structures, institutions, machines, and technology. Edmund Husserl and Martin Heidegger exposed the errors of conceiving such mechanisms, technology, and the human sciences as value-free: These too are controlled by the dominant ideologies of sociopolitical orders of their times—Marxism, capitalism, and liberalism. The world, and the uneasy human feelings about it, can lead to bad faith and inauthenticity: These psychic conditions result from evading or deceiving oneself and others. Inauthentic individuals assimilate or adapt by donning personae and roles in doing their daily tasks and jobs. Either masking or numbing themselves through habits, rule following, rote understanding, and compliance, workers and businesspeople respond to external systems and institutions of law and order. Generally, these herdlike tendencies (identified by Friedrich Nietzsche) predominate when humans follow the leader, any impersonal or personal power of authority. Yet, according to existentialism, none of the goods of human existence are given or constructed for individuals as followers.

Particularly in business as in life, the individual faces similar challenges and pitfalls. On the job, one may choose to get by and even attain worldly success by going along with the group and subcultures of business or the corporation, finding therein one's identity, function, and purpose. On the one hand, the self follows the crowd, follows orders, relying on the system to provide the norms for what is expected and acceptable. Regardless of whether one conforms to, embraces, or simply accepts these standards, the individual becomes normalized through the systems in which the self operates daily. On the contrary, the business maverick, the risk-taking entrepreneur, the self-made tycoon, and the courageous union organizer and labor leader diversely typify the heroic existentialist. These rebels radically transform or overturn the system, newly designing it according to nobler human purposes. Within these different groupings, identities, and individual roles, the self must make its own moral choices, commitments to change or refrain from change, as the world or reality exists apart, indifferent to the customary confines of human loyalties and defections, whereby the self identifies with or breaks away from the group.

The businessperson and laborer may unconsciously know and live by the tenets of existentialism by virtue of his or her career training and conditioning. For to be oriented existentially is a commonplace reality, an everyday individual experience of interacting with the risk-ridden, often arbitrary arenas of business, the market, and the workplace. Individuals under contractual relations of trust and reciprocity must assume and accept the fluctuating risks regarding loss and harm as much as gain and benefit. The existentialist freely accepts the responsibility of either following or altering commitments and work projects as they unfold. The courage to design and redesign oneself and others through work remains dicey when unjustifiable by any external power or institution that could reliably regulate individual conduct and free choice.

Especially in terms of existentialism, legal regulation and intervention and the degree of governmental control of business, the marketplace, and labor cause continuing controversy. Might not regulatory measures make individual and collective business transactions and consequences more controllable, moral, and rational, by making individuals and corporations less free and hence individually irresponsible? From the existentialist perspective, the course of doing business, and economics itself, seems more irrational and unpredictable than classic economists have theorized. Though no sensible individual or business would advocate gambling or taking undue risks with people's retirement funds, pensions, stocks, health plans, and educational trusts, the existentialist business model would maintain that risky bargaining characterizes business as part of the general human predicament.

In the 21st century, philosophers and business ethicists (e.g., Robert Solomon) vow for existentialism. Humans as free decision makers are to be held responsible for their decisions in making meaning, morals, and purpose from their productive activities. Otherwise, humans would be self-pitying creatures, enslaved to work, subjects to the world as it is rather than workers, innovators, and entrepreneurs who choose their world as it could be and work to make it so.

—Mary Lenzi

See also Authenticity; Autonomy; Capitalism; Deontological Ethical Systems; Ethical Nihilism; Free Will; Individualism; Kant, Immanuel; Laissez-Faire; Leadership; Liberalism; Marxism; Pluralism; Roles and Role Morality; Self-Deception; Self-Realization; Self-Regulation; Utilitarianism

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Expected Utility

As part of rational choice theory, the concept of expected utility is used to elucidate decisions made under conditions of risk. The expected utility of an action is a function of both an agent's estimation of the utility of the various outcomes possible given that action and the likelihood of those outcomes occurring. The utility of an outcome refers to an agent's preference for that outcome. The probability of an outcome refers to the chance of that outcome occurring and can be represented by a number between 0 (no chance) and 1 (perfect certainty). The expected value of an action is calculated by multiplying the utility of each outcome by its probability of occurring and then summing those numbers. Thus, allowing $P(o)$ to refer to the probability of an outcome and $U(o)$ to the utility of an outcome, then for some action x, with a series of potential outcomes $o_1, \ldots, o_i$, the expected value of x, or $\mathrm{EU}(x)$, is calculated as

$$\mathrm{EU}(x) = \sum_i P(o_i)U(o_i).$$

For example, suppose an insurance company issues a theft policy on a piece of artwork for a year with a replacement value of $10,000 and a cost of $500, and there is a statistical probability of .02 that the artwork will be stolen in that year. The expected value of the act of insuring for the company would then be (.98)(500) + (.02)(500 − 10,000), or $300. According to standard decision theory, when comparing alternative courses of action, one should choose the action that has the greatest expected utility.

The concept of expected utility and the rule of maximizing expected utility have wide application to decisions in business contexts, including those involving insurance, capital expenditures, investment, marketing, and operations. The utility of the outcomes under consideration in such contexts can usually be specified in terms of potential monetary profits and losses. By using their estimation of the likelihoods of the outcomes of options open to them along with their associated monetary losses and gains, businesses can determine the expected utility of each option in terms of its expected monetary profits. The option with the greatest expected utility will then simply be that which has the largest expected profit associated with it, and this option, according to the rule of maximizing expected utility, will be the optimal choice.

While the concept of expected utility has played an important role in the study of economic behavior, criticisms have been raised concerning its application to contexts of choice in business and economics. For instance, some theorists from the social and behavioral sciences argue that the cognitive limitations of human beings make the concept of expected utility as a guide to choice too idealized for use in most significant decision contexts. Such critics thus advocate notions of bounded rationality that are more sensitive to these limitations and make use of evaluative concepts that do not depend on the precise sorts of assessments that are involved in determinations of expected utility. Other critics have argued that the application of expected utility to economic decisions, including policy decisions, has engendered inappropriate valuations, particularly in cases in which monetary units are used to scale the utility of nonmonetary outcomes, such as potential deaths or damage to the environment. Finally, many philosophers have questioned whether the rule of maximizing expected utility represents an adequate or complete guide to decisions, particularly with regard to decisions of an ethical nature. The rule of maximizing expected utility represents a consequentialist form of reasoning, in which actions are judged solely in terms of their potential outcomes. As such, philosophers of a deontological stripe question whether such reasoning can provide an adequate account of the role of rights and duties in practical reasoning. Such philosophers, for instance, argue that the moral rights of those affected by an action place constraints on the worthiness of a choice independent of the value of the consequences of that choice.

—Daniel E. Palmer

See also Bounded Rationality; Marginal Utility; Prisoner's Dilemma; Rational Choice Theory; Satisficing; Utility, Principle of; Von Neumann-Morgenstern Utility Function

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EXPLOITATION

Exploitation is a contested concept. In one sense of the term, to exploit means to effectively utilize the object of exploitation. It is in this sense of the term that one exploits sunlight to generate solar power. In another sense of the term, to exploit means to take unfair or illegitimate advantage of the object of exploitation. It is in the latter sense that the term is most often employed in relationship to business practices. For example, automobile salesmen are often accused of exploiting inexperienced or vulnerable customers by taking advantage of asymmetries in information. To assess such claims, it is necessary to have a coherent account of exploitation. There are two primary questions about the concept of exploitation that any account of the concept must answer. First, what constitutes exploitation? Second, when is exploitation morally objectionable?

Theories of Exploitation

Marx's well-known account of exploitation holds that capitalists exploit workers by expropriating worker productivity. Exploitation, in this account, is a fundamental feature of capitalism. Constant technological innovation results in labor-saving processes and ensures a large pool of unemployed workers. In Marx's analysis, workers must choose between accepting subsistence wages and few benefits and joining the ranks of the unemployed. This power imbalance allegedly coerces workers into compliance, resulting in the morally objectionable expropriation of surplus value from workers by capitalists. Critics of Marx argue that his account of exploitation ignores the risks involved in capital investment and fails to acknowledge the importance of managerial expertise. Furthermore, Marx did not develop his views with the clarity typical of the best contemporary philosophers and social theorists.

Largely as a result of these criticisms, the most influential contemporary accounts of exploitation are non-Marxist. Such accounts are typically divided into two categories: (1) moralized accounts that assume the wrongness of exploitation and (2) empirical accounts that do not. Alan Wertheimer defends an influential view of exploitation whereby a mutually advantageous exchange is exploitative when A takes unfair advantage of B relative to a specific baseline. Because a fairness baseline is a moral consideration, this account of exploitation is properly understood as moralized. Moralized theories of social concepts maintain that at least one of the truth conditions of the concept at issue is moral. Moralized theories also settle the question of the moral status of the act. In Wertheimer's account of exploitation, if A exploits B, then A acts wrongly. In contrast, empirical theories of social concepts maintain that all the truth conditions of the concept at issue are empirical and none moral. For example, Allen Wood argues that exploitation occurs when A takes advantage of B's weakness or vulnerability to derive some benefit from B. In his account, the question of whether or not exploitation takes place depends on certain factual matters, such as B's vulnerability or B's capacity to benefit A. In contrast to moralized theories, empirical theories do not settle the question of the moral status of the act. In Wood's account of exploitation, the fact that A exploits B does not by itself resolve the question of whether or not A acts wrongly. Indeed, the idea of justified exploitation is consistent with ordinary language use of *exploit*. For example, we do not normally criticize a coach who exploits the weakness of an opponent's team (within the rules of the game) of acting unjustly or unfairly.

The moral baseline Wertheimer defends is that of a hypothetical market price, or the price that would be generated in a competitive market. Such a price is to be differentiated from the price generated in a perfectly competitive market, a market in which there are many buyers and sellers and perfect information. A hypothetical market price does not correspond to desert. The market price for the services of a talented and well-trained public relations specialist may be greater than the market price of a talented and well-trained elementary school teacher, but this does not reflect a principle of desert. A similar point may be made with respect to moral luck. A hypothetical market price does not take into consideration the social and economic benefits of being born into poverty versus being born wealthy.

A common view of moralized accounts of social concepts is that because at least one of the truth conditions of the concept at issue is moral, such accounts render the need for subsequent moral analysis redundant. Thus, in Wertheimer's account of exploitation, statements such as "A's exploitation of B is wrong" will be true but redundant. This is because the moral wrongness of "exploitation" is built into the concept. After all, in Wertheimer's account, if one is exploited one has been treated unfairly. His account has the additional limitation of being unable to account for exploitation that occurs in nonmarket cases, such as in relationships. Wood's empirical account, on the other hand, has none of these deficiencies.

Are Workers in Global Factories Exploited?

It will be useful to illustrate the concept of exploitation with reference to an important contemporary debate. The question of whether or not sweatshop workers are exploited depends both on the wages and labor conditions of the factory in question and on one's definition of exploitation. Imagine a case in which a multinational corporation contractor (MNC) pays employees the equivalent of $2.00 per day, whereas the amount necessary to cover basic food, clothing, and shelter needs is approximately $4.00 per day. Imagine a second case in which an MNC factory required workers to work overtime and fired workers for their legally protected rights to collectively organize. In Wertheimer's account, the workers in the first case are not exploited because they benefit from their employment and the wages they receive are generated by a competitive market. As defenders of sweatshops argue, such workers freely choose to work in that factory because the wages they earn are better than those they could make elsewhere.

It is less clear what Wertheimer's account can tell us about whether or not the second case is one of exploitation. This is because his account of exploitation requires that the victim of exploitation must be at a disadvantage relative to a hypothetical market price for the good or service in question. However, in the second case, the question of whether or not the workers are exploited is tied primarily to the terms of employment rather than to wages. The most interesting question regarding exploitation in this case appears to be whether or not the relationship between the workers and their employer is exploitative, not whether a particular transaction is exploitative. However, it is arguable that as an element of employee compensation, the terms of employment are an element of the labor contract. Understood in this way, the workers in the second case are not exploited because they benefit from their employment and the conditions under which they work are the product of a competitive market.

Wood's empirical theory of exploitation suggests a different conclusion regarding these two cases. Recall that in Wood's account, exploitation occurs when A exploits a weakness or a vulnerability in B to derive a benefit from B. In this account, workers in both factories are exploited. This is because they take advantage of the workers' powerlessness to benefit from their cheap labor. In this sense, Wood concurs with Marx that owners nearly always exploit wage laborers.

It remains a separate question whether or not such exploitation is morally objectionable. Much can be said in defense of the right of individuals to engage in transactions involving their own property and labor, and efforts to interfere with capitalist exploitation may unduly restrict liberty or economic efficiency. At this point, one might conclude that no determinations regarding the moral status of capitalist exploitation can be made independently of an adequate theory of economic justice. However, there is another means for evaluating the moral legitimacy of the practices of employers. According to Wood, exploitation is morally objectionable when it is disrespectful of others.

Kant and his interpreters have provided the most sophisticated philosophical defense of the idea of respect for persons. In a Kantian analysis, persons are entitled to respect because they have dignity; they have dignity because they are free and rational beings capable of autonomous action and are subject to moral law. Kant famously argues that to respect someone, one must treat that person as an end and not merely as a means. To treat someone as a means only is to treat that person as a tool, as an object with mere instrumental value. Popular criticism of the labor and wage practices of MNCs is frequently grounded in the belief that the contract employees of these and other MNCs are treated merely as tools of production. So in the empirical account of exploitation discussed here, the exploitation of sweatshop workers is morally objectionable when it is disrespectful and unobjectionable when it is not.

Conclusion

Exploitation is a contested social concept about which there is little consensus among philosophers and social theorists. Nonetheless, an empirical view of the concept that allows for morally unobjectionable exploitation and that does not render phrases such as "wrongful exploitation" nonsensical has more plausibility than alternative concepts. Such a concept may be of considerable use in assessing market transactions that occur between parties with significantly different power.

—Denis G. Arnold

See also Coercion; Dignity; Kantian Ethics; Marxism; Sweatshops

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Export-Import Bank

The Export-Import Bank (Ex-Im Bank) was established on February 12, 1934, as the official export credit agency of the United States. The mission of the agency is to assist in financing the export of U.S. goods and services to international markets. The agency was originally incorporated as the Export-Import Bank of Washington until 1968, when the name was shortened to Ex-Im Bank. Services and products provided by the Ex-Im Bank include basically two categories of assistance: (1) financial products and support for U.S. companies exporting abroad and (2) financial products and support to foreign entities to establish and maintain markets for U.S. products.

The bank's programs come in the form of direct loans, export credit insurance, working capital guarantees, and financing for special projects such as environmental programs or small business initiatives. The Ex-Im Bank has supported the following specific programs in the recent past. In the environmental category, the bank has provided financing for the export of environmentally beneficial U.S. goods to foreign markets, including renewable energy exports such as wind turbines, photovoltaic panels, solar energy outdoor lighting, and geothermal plant services. The bank provides financial support for infrastructure that facilitates trade in foreign markets in the form of new airports, telecommunications projects, and transportation security programs.

Another initiative includes transportation products (aircraft, locomotives) and transportation security. Other areas of recent emphasis include electronics, telecommunications, mass transit, medical equipment, and the promotion and support of U.S. services in foreign markets, such as engineering, design, construction, oil drilling, training, and consulting. The Ex-Im Bank also provides support for markets of agricultural products from the United States including commodities, livestock, foodstuffs, equipment, chemicals, supplies, and services. In addition, the bank partners with the U.S. Small Business Administration (SBA) to assist small businesses seeking to sell their products or services in foreign markets. The Ex-Im Bank and the SBA can coguarantee loans up to $2 million. This partnership enables small businesses to obtain more capital than they could acquire under the SBA program alone. More than 80% of the bank's transactions benefit U.S. small businesses.

The Ex-Im Bank provides pre-export financing, financing for foreign buyers of U.S. products and services, and insurance to protect against buyer nonpayment. The bank can provide long-term credits to public or private entities, credits to foreign lending institutions for the purpose of lending funds to local businesses, and credits to countries with dollar shortages to maintain a consistent flow of trade of U.S. goods and services. Rather than compete with the private sector, the Ex-Im Bank offers financial products and services the private sector would normally not engage in.

The bank deals only with the export of U.S. goods and services; it does not finance imports. Governance of the bank includes a congressionally mandated advisory committee, 23 bank officers, and a board of five to seven directors appointed by the president of the United States. While the bank is headquartered in Washington, D.C., it operates out of six regional areas of the United States. In the past 5 years, the Ex-Im Bank has completed at least 11,000 total transactions involving $65.5.

Ethical issues concerning this institution lie mostly in the choices made about which ventures to support. Much like other industrial policy decisions, financing through the Ex-Im Bank has the potential to be influenced by politics.

—Jeanne Enders

See also Federal Trade Commission (FTC); Free Trade, Free Trade Agreements, Free Trade Zones; International Monetary Fund (IMF); International Trade; Trade Balance; World Bank; World Trade Organization (WTO)

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Export Trading Company Act of 1982

The Export Trading Company Act of 1982 was enacted to encourage U.S. exports of goods and services. The act was intended to facilitate the formation of export trading companies and export trade associations and to expand the provision of export trade services. Export trading companies are persons or organizations, whether operated for profit or as a nonprofit organization, principally involved in exporting, or facilitating the exports of, goods or services produced in the United States. The export trade services mentioned in the act are wide-ranging: They include consulting, international market research, advertising, marketing, insurance, product research and design, legal assistance, transportation (including trade documentation and freight forwarding), communication and processing, warehousing, foreign exchange, and finance services provided to facilitate the export of goods or services produced in the United States. A newly established office within the Department of Commerce would promote the creation of export trade associations and export trading companies.

The act sought to reduce restrictions on trade finance offered by financial institutions. To give exporting firms protection for joint activities, a provision of the act authorized the U.S. Department of Commerce to issue a certificate that entitles a holder to a limited antitrust exemption. Once issued, the certificate exempts the specified conduct from criminal and civil suits under both federal and state antitrust laws.

The act made it easier for exporters to secure loans, especially in cases where the private credit market failed to provide adequate financing for export transactions. The official export credit agency of the United States, the Export-Import Bank, was authorized and directed to establish a program to provide guarantees for loans extended by financial institutions or other public or private creditors to exporters. These loans had to be secured by export accounts receivable or inventories of exportable goods. The guarantees would facilitate expansion of exports that would not occur otherwise. The intended recipients of the loan guarantees were among the tens of thousands of small, medium-size, and minority businesses that produce exportable goods and services but do not engage in exporting.

The expansion of exports sought under the act was intended to boost manufacturing activity—at the time, U.S. exports accounted for one out of every nine manufacturing jobs in the United States—and counter the putative adverse effects of a growing trade deficit on the value of the dollar and the inflationary impact of a depreciating currency. In 1982, when the act came into effect, U.S. exports of goods and services amounted to $302 billion; in 2005, more than two decades later, they had quadrupled in inflation-adjusted terms to $1,195 billion. But the trade deficit has continued to rise inexorably, from $13 billion in 1982 to $633 billion in 2005 in real terms. During this period, the dollar has risen sharply against the yen, from 220 yen per dollar in January 1982 to 102 in January 2005. Manufacturing employment has declined steadily since reaching a peak of 19.5 million in 1979, falling to 14.2 million by the fourth quarter of 2005.

In a market-oriented economy, the government should play a minimal role in promoting exports. Trade policies designed to favor certain industries militate against the expansion of free trade sought by successive agreements of the World Trade Organization and in fact impose economic and political costs on the parties involved. Export promotion policies by the United States, for instance, will impose costs on the U.S. taxpayer and create tensions with trading partners. By encouraging production in certain sectors, these policies may also lead to a decline in world prices. In the case of agriculture, the increased production by farmers in developed countries will come at the expense of farmers in developing countries.

—*Sanjay Paul*

See also Export-Import Bank; Free Trade, Free Trade Agreements, Free Trade Zones; Managed Competition

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Externalities

An externality is a side effect generated as a result of consumption or production choices by one individual or entity and involuntarily received by another individual or entity. The decision maker's analysis or calculation deliberately or inadvertently ignores the consequence. The decision maker avoids "internalizing" a particular consequence and thus externalizes any cost or benefit. The recipient bears the burden of a negative (i.e., costly) externality and gains the value of a positive (i.e., beneficial) externality.

A negative externality imposes a burden elsewhere while benefiting the source through avoidance (i.e., externalization) of a cost. A classic example is air or water pollution. The polluter damages someone else and thereby avoids the cost of pollution control. Negative externalities particularly raise important issues for business ethics and law. Not generating, or at least compensating for, a negative externality comports with the ethical principle of avoiding unjustifiable harm to others when feasible to do so. A good citizen does not dump refuse on the road to avoid the inconvenience of finding a garbage can. Someone else pays the cost of that dumping.

A positive externality generates a benefit elsewhere at no direct cost or benefit to the source. A classic example is a beekeeper whose freely wandering bees pollinate the apple trees of a neighboring farmer. The farmer gains in the production of apples, while the beekeeper bears no immediate cost and cannot collect any part of the farmer's benefit. The beekeeper may gain of course in honey production, and if so, a second positive externality is at work in the reverse direction from farmer to beekeeper. Positive externalities can be interpreted as a form of violation of the opportunity cost principle of economics: The beneficiary does enjoy a "free lunch" in this instance. Beneficiaries may under some circumstances oppose acts to internalize the value of a positive externality. Positive externalities raise important issues for public policy formulation, particularly in the extreme forms of public goods and merit goods. A public good either occurs freely in nature (e.g., air) or cannot readily be produced for profit by a business (e.g., national defense). A merit good might be produced privately for profit (e.g., medical care) but ought in someone's judgment to be more broadly available (e.g., public education). The notion of a positive externality is akin to the ethical principle of discretionary altruism, where the producer cannot recapture the value of the beneficial side effect. A good citizen picks up at personal cost the refuse left by children at a public park.

An externality can be an example of Adam Smith's notion of unintended consequences. Discretionary corporate social responsibility might be predicted to create unintentionally more harm than good (i.e., negative consequences), while Smith's "invisible hand" market mechanism might unintentionally generate more good than harm (i.e., positive consequences).

Economic Theory of Externalities

Because side effects are commonplace phenomena resulting from consumption and production decisions, externalities are an important matter in welfare (i.e., normative) economics and public policy. Welfare economics concerns the conditions under which Adam Smith's invisible hand of free markets leads to the most efficient allocation of scarce resources so as to maximize national wealth. A resource allocation is Pareto optimal if no other resource allocation can make one person better off without making some other person worse off. So when resources are allocated in a Pareto-optimal manner, all possibilities for mutually beneficial voluntary exchange have been exhausted. In static conditions, workable competition reasonably achieves Pareto optimality. However, even a competitive market economy confronted with significant amounts of externalities and public goods will generally not achieve a Pareto-optimal allocation. Consumers will focus on private goods so that they can capture the full benefit of their expenditures. As a result of this focus on private goods, market economies typically underproduce positive externalities and public goods as measured by the condition of Pareto optimality. Market economies typically overproduce negative externalities as measured by that condition, raising the question of government regulation.

Positive and negative externalities are also termed external benefits and costs, external economies and diseconomies, or social benefits and costs, respectively. The language means simply, for example, that benefits and costs occur externally of the producer. Similarly, an economy is a side effect that increases someone else's benefits and a diseconomy is a side effect that increases someone else's costs. Externalities often create broad social rather than individualized side effects.

There are several ways of classifying externalities. They can be harmful (i.e., negative) or beneficial (i.e., positive), as illustrated earlier for pollution or a beekeeper and a farmer, respectively. They can be real (i.e., technological) or pecuniary (i.e., financial or monetary). A real or technological effect changes the total stock of assets. For example, water pollution adds something to the physical composition of water. Water as an asset has changed. A pecuniary or financial effect changes the prices of existing assets. A pecuniary externality is simply a working through of the market price mechanism. For example, air pollution may reduce the market value of affected housing. As a general rule, real externalities must be considered in a cost-benefit analysis, but pecuniary externalities should be ignored. In a voluntary exchange between a consumer and a firm, a product or service goes to the consumer, and money goes to the firm. An externality may occur in consumption (generated by the consumer) or in production (generated by the supplier). For example, a consumer mowing the lawn pollutes the environment. A producer dumping waste into a river pollutes the environment. Negative (i.e., costly) externalities can become depletion of a common pool or property resource in the tragedy of the commons. There is a continuing controversy over whether the broadcast spectrum (for radio and TV transmission) is properly a commons or a set of private property rights.

Where externalities exist, private benefits and/or costs diverge from social benefits and/or costs. Externalities result in a difference between a private decision maker's calculation of benefits or costs and society's valuation of benefits or costs. This difference can result in market failure or suboptimality. Suppose, for example, that the sale price of a good is \$10 per unit, reflecting consumer willingness to pay (i.e., demand). The producer bears a cost of \$8 and makes a profit of \$2. There is a production-generated negative externality of \$3 per unit and a production-generated positive externality of \$1 per unit—both ignored by the firm. The consumer generates an additional negative externality of \$1, ignored in throwing the unit away when economic lifetime is exhausted. The social valuation of this good is consumption benefit of \$10 plus the \$1 positive externality; from the sum of \$11 overall social benefit, one must now subtract the \$4 of negative externalities. The social valuation reduces to \$7 compared with the market price of \$10. Too much of this good is being produced and consumed. The firm cannot collect the value of the positive externality. If society compels the firm to internalize the negative externality of \$3 per unit, then the firm would lose money on each unit sold unless it can figure out a way to reduce its production cost.

The conventional diagrammatic illustration of externalities is to depict two demand or supply curves—depending on whether a consumption (demand) or production (supply) externality is involved. In the case of production externality, on the production side there is a social cost (i.e., supply) function positioned vertically above the private cost (i.e., supply) function (because supply embeds cost). At each point along these two cost functions, marginal private cost is less than marginal social cost by the amount of the external cost. A single demand curve (demand embeds consumer willingness to pay), in this instance, would mean that there are no external benefits offsetting the external costs: Social benefit and individual benefit are equal. In the case of consumption externality, on the demand side there is a social benefit function positioned vertically above the private benefit function. At each point along these two demand functions, marginal private benefit is less than marginal social benefit by the amount of the external benefit. A single supply curve, in this instance, means that there are no external costs offsetting the external benefits: Social cost and individual cost are equal.

Solutions for Externalities

Significant external impacts may have to be internalized in the decision maker's analysis or calculation in some way. How to do so is the vital policy issue, because the market mechanism no longer achieves optimal outcomes. Potential solutions include governmental regulation (e.g., ordering a ban on or reduction of an activity) or a Pigouvian tax (named after Arthur C. Pigou, 1877–1959) for negative externalities, or governmental subsidy for or even direct provision of beneficial externalities. Negative externalities—especially pollution, which can produce irreversible costly results in time—can be interpreted as a form of nuisance or of trespass on someone else's property fit for tort litigation. Ronald H. Coase presented the case for private self-regulation through a complete and enforceable system of property rights. Continuing deforestation of the Amazon basin occurs because no one owns the land or possesses sufficient resources and incentives to defend against loggers—in the absence of effective governmental action. The Brazilian government may argue that it requires substantial international financial transfers to address the problem.

Pigou, an English economist, pioneered welfare economics. Pigou drew the important distinction between private costs (or benefits) and social costs (or benefits). Pigou took the view that only governments—through taxes and subsidies—can feasibly "internalize" externalities in economic exchange or production. A Pigouvian tax is one intended to correct a negative externality. Pigou's position invokes the circumstance in which firms in competitive markets likely cannot address internalization of social costs. Any firm that moves first to internalize external costs would have higher costs than its competitors and be forced to exit the industry. As a result, a monopoly theoretically might be better able to address externalities. Given economic rent (profits above cost including a competitive return), a monopoly (where regulated by government) might be able to pay for the cost of the externality or restrict the quantity supplied so as to reduce the externality.

Coase—winner of the 1991 Nobel Prize in Economic Sciences—brought together the economic theory of externalities and the common-law tradition addressing nuisance and torts claims. The subsequently labeled "Coase theorem" expands solutions for externalities beyond government actions: Private losers and winners might in principle negotiate the internalization of externalities. Nongovernmental solutions also may evolve over time through community agreements and other approaches. It does not matter which party possesses rights of ownership over the cause of the externality: The initial assignment of property rights does not affect the efficiency of resource allocation where there is completely free trade of property rights. What can prevent negotiation are high transaction costs of bargaining. Coase had developed a theory that the firm (or any other economic organization or institution) exists as an entity in place of pure market exchange only when actors find a particular governance mechanism useful for minimizing transaction costs. The firm is a nexus of contracts intended to minimize transaction costs. Coase's insights have occasioned wide application in law and the social sciences—launching the field called the "new institutional economics."

The Coase theorem argues that government should facilitate private bargaining and enforce what amounts to private contracts concerning property rights. This theorem requires simultaneously (1) well-defined property rights, (2) a relatively small number of bargainers, and (3) relatively small bargaining (or transaction) costs. As the numbers increase, free riding may vitiate the bargaining efforts—as one encounters the difficulties attending attempted collective action. A class action lawsuit is a partial substitute for the numbers problem. Pigou's view can be interpreted as the necessity for governmental action when at least one of these conditions does not obtain in the real world. Litigation concerning asbestos or tobacco harms cannot meet Coase's conditions. Multiple-stakeholder forums for addressing business problems are a variant of the bargaining solution.

Environmental Economics

Environmental economics focuses on the negative externalities or side effects of consumption and production. The Kyoto Protocol for global climate protection is an example of the problem. Everyone generates negative externalities that in various ways likely contribute to global warming. These externalities damage the natural environment (a common resource pool) and are treated by the individual polluter as costless. These damages accumulate into conditions that warm the planet. The Kyoto Protocol—a negotiated arrangement—seeks to reduce pollution levels on a country-by-country basis. A difficulty in the arrangement is that the advanced economies agree to reduce pollution (in effect internalizing the cost of negative externalities), while the developing countries (including Brazil, China, and India, which are rapidly industrializing) are not parties to the commitment. As developing countries industrialize, their pollution levels—still driving global warming—will likely increase.

An illustrative pollution cost situation, adapted from John H. Dales, is as follows. Suppose that an isolated community living on the edge of a lake dumps all its water pollution into the lake, which is also the source of its drinking water and other water-related activities. Each person is contributing to the destruction of a common pool or common property resource. The cost of treating polluted lake water to obtain potable water is $1,000 per person annually. The only alternatives are to transport in bottled water at $1,200 per person annually or to divert waste water to a treatment plant rather than permitting runoff into the lake at $1,500 per person annually. Suppose further that diversion or cleaning is just sufficient to produce potable water but not to permit fishing or swimming in the lake. Each person would be willing to pay $50 a year for fishing and $50 a year for swimming. If the community decides on potable water only, fishing and swimming effects remain as noninternalized negative externalities. The decision output depends on citizen preferences in relationship to cost structure.

Spillover and Network Effects

Spillovers or neighborhood effects are externalities that affect the interests of a relatively broad number of people or of nature. This broad effect is in contrast to the simple beekeeper and farmer example used at the beginning of this entry. Spillover effects can be either real (i.e., technological) or pecuniary (i.e., financial). Complementary goods (e.g., purchase of cars increases purchase of gasoline) are a real spillover effect. The spillover notion permits the inclusion of pecuniary (or financial) externalities, which would be excluded from a cost-benefit analysis. A public park may raise the property values of all the houses in a neighborhood. This spillover effect is pecuniary. A spillover effect can occur across governmental jurisdictions, in the sense that provision of a public good in one jurisdiction could have impacts on another (generally neighboring) jurisdiction.

Public education of all the children in the neighborhood may create real spillovers. Education arguably is a merit good. The market economy can produce some limited quantity of education for profit. Someone's judgment is that education should be more broadly available through governments or nonprofit organizations, because having an educated citizenry generates broad positive externalities for everyone in the community or society.

The *Washington Post* reported research suggesting that an additional year of education is worth on average an estimated 8% to 10% more in pay to the individual educated. It was reported that, controlling for other factors affecting wages, a college education benefits the less educated through spillover effect: The proportion of college graduates in a city raises all wages. The largest gain is by those with the least education—high school dropouts. The specific estimate links a 1 percentage point increase in the proportion of college graduates living in a metropolitan area to a 1 percentage point increase in everyone else's pay. A cited reason is that as the relative supply of lower-wage labor declines (in proportion to college graduates), the wages of that labor rise; there may also be informal transfers of marketable skills among population groups.

Network externalities involve the progressive expansion of usage as more and more consumers purchase something. A network effect means that a good or service has value to a potential customer dependent on the number of customers already owning that good or using that service. The purchase of a good by one consumer indirectly benefits others who own the good: By purchasing a fax machine or using an e-mail service, a person makes fax machines and e-mail accounts more useful. A network effect is a network externality if either the participants in the market or the owner of a network do not internalize these side effects. A network effect is also an example of a positive feedback loop in which, initially, additional customers attract more customers sufficiently to pass some critical mass point; the feedback growth continues until congestion through overuse occurs (as on a crowded toll bridge). It may be the case that network effects are important in high-tech industries and are related to the dot-com phenomenon of the late 1990s. Firms may have thought that market share and volume growth were the most important strategic target in a new market. The largest firm arguably could set technical and marketing standards and dominate competition. Network effects occur on the demand side, scale and scope economies on the supply side.

Net-Harm Industries and Activities

Industries are socially net-gain or net-harm activities. A net-gain industry is one whose output causes greater benefits than harms. In consequence, hypothetical compensation of harms is feasible. In theory, beneficiaries could compensate losers and still have net benefits left over to enjoy. The net-gain condition characterizes most industries. There are net-harm industries, whose output causes greater harms than benefits; hypothetical compensation is not feasible. Net-harm industries produce socially undesirable goods (i.e., social or merit bads). A classic instance is tobacco production and consumption. Although there is consumer demand for tobacco products (which demand may reflect addiction), consumption is unavoidably harmful, and there are significant externalities including health harms from secondhand smoke. The net-harm notion can be extended to alcohol, child pornography, drug abuse, firearms, and gambling.

As reported in 2004 by the Associated Press, an estimate of lifetime costs of more than 60 years for a 24-year-old smoker suggests that smokers pay at least $33 a pack of cigarettes, while their families bear $5.44 and others in society about $1.44 net (not including higher cleaning bills and lower resale values). Part of the social cost is offset by earlier deaths, so that smokers do not draw as much on funds paid into retirement accounts. Smokers pay $0.76 a pack in taxes, as an offset to social costs of $2.20, thus reducing net to the $1.44 figure. External costs on families and society run (net) about one fifth (20.8%). Consumption is at least too much by that proportion—before addressing any judgment that tobacco is bad for the individual consumer.

—Duane Windsor

See also Coase, Ronald H.; Coase Theorem; Commons, The; Cost-Benefit Analysis; Economic Efficiency; Economies of Scale; Efficient Markets, Theory of; Kyoto Protocol; Pareto Efficiency; Perfect Markets and Market Imperfections; Pollution; Public Goods; Regulation and Regulatory Agencies; Smith, Adam; Social Costs; Torts; Tragedy of the Commons; Welfare Economics

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EXTORTION

Extortion (or solicitation) and bribery are among the main forms of corruption. Both may be defined as the act or effect of giving or receiving a thing of value, so that a person acts or does not act in violation of a formal or implicit rule about what that person ought or ought not to do, to the benefit of the person who gives the thing of value or a third party. In bribery, it is the beneficiary that takes the initiative—for example, when a company that wants to obtain a contract from a public authority makes a payment to the politician who has the power to decide who gets the contract. In extortion, it is the agent that takes the initiative.

Both extortion and bribery have the following features in common:

- A power or influence that someone (the agent: a public official, politician, manager, or employee) has in the exercise of a function, task, or responsibility in the service of a public office or company
- An element of discretion deriving from that power or influence
- Certain duties (established by law, contract, or code of conduct) associated with the agent's function in a public office or company
- An incorrect exercise of that power or influence, contrary to the duties associated with the agent's position or function
- A private benefit for a person or organization (the beneficiary): The benefit may be monetary or not (a cost reduction, or a job, license, or permit, or the mere expectation of it), and it may be positive or negative (e.g., avoiding reprisals)
- The delivery, or the promise of delivery, of something of value to the agent or another person (a relative, a political party, etc.) in exchange for the agent's exercising a power or influence in the beneficiary's favor

Extortion and bribery may take a wide variety of forms: The beneficiary may be entitled to the benefit obtained from the agent (e.g., a legitimate permit) or not entitled to it (an unjust sentence); the agent may be public or private (e.g., the manager of a company with which the beneficiary has contractual relations); the payment may be direct or indirect (e.g., a scholarship for the agent's son or daughter); and the payment may be made directly or through an intermediary. Facilitating payments are small payments made to help resolve a matter, expedite an administrative process, secure the issuance of a license, and so on, but not to obtain a major business advantage.

Ethical Problems of Extortion

In extortion and bribery, many ethical principles are violated: justice, impartiality, legality, professionalism, loyalty, good faith, solidarity, avoidance of harm, and so on. The moral core of extortion and bribery lies in the unfairness and disloyalty of those who execute these acts in the exercise of their duties to the company or public agency in which they work, when they use their position to obtain a benefit to which they are not entitled. There may also be injustice to the beneficiary, to the company or government department (because the agent's duty is not fulfilled or because the agent encourages others to act in a similar manner), to third parties (e.g., competitors), and to society (when an atmosphere of corruption is created). The moral responsibility of the beneficiaries derives mainly from their cooperation, as abettors or accomplices, in the agent's disloyal action.

The ethical rules for responding to extortion and bribery will depend on one's conception of ethics. The following views are shared, to a greater or lesser extent, by a broad range of theories:

- It is unethical to accept or offer a bribe or to demand a bribe (extortion).
- It is unethical to give in to extortion in order to obtain something to which one is not entitled.
- In certain cases, it is legitimate to give in to extortion in order to obtain something to which one is entitled. In such cases, the following rules should be observed: (a) Carefully consider all the options, to see whether it is possible to solve the problem without getting involved in extortion; (b) the extortion must be open—it is unethical to present what in fact is bribery as if it were a response to extortion; (c) act with the intention of obtaining a right; (d) try to avoid harm to third parties; (e) make sure that there are sufficient objective reasons for giving in to the extortion, in proportion to the damage caused; (f) take steps to minimize the bad example that may be set; and (g) take steps to prevent any recurrence of such collusion with corruption.

Other Consequences of Extortion

Extortion and bribery have many other harmful effects on the economy, society, and political life. For example, the following are the consequences with respect to the economy:

- Inefficient use of resources: higher costs and prices, lower output and quality, wasted time, slower growth, insufficient capital formation, reduced foreign investment, less efficient public spending, reduced tax revenues, and so on
- Unjust redistribution of income: illicit enrichment of certain groups, greater inequalities, growth of the underground economy, and so on
- Less competition, less transparency, laxity in the implementation of rules, obstacles to free trade, loss of legitimacy of institutions, distrust of the market system, and so on

In the sociopolitical arena, extortion distorts decision-making processes, restricts the scope of citizen rights, facilitates concealment, weakens controls, and, in the long run, undermines the government's legitimacy.

What ethics adds to the economic and sociopolitical arguments is recognition of the harm done to people: loss of virtues and weakening of the ability to act in a noncorrupt manner, on both a personal and a social level (corrupt people's behavior is imitated by others). Also, extortion tends to become endogenous: It becomes organized and institutionalized.

—Antonio Argandoña

See also Corruption; Foreign Corrupt Practices Act of 1977 (FCPA)

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Exxon Valdez

At 12:04 a.m. on March 23, 1988, the *Exxon Valdez* ran aground on Bligh Reef, near Valdez, Alaska. This was the 28th trip that the *Exxon Valdez* had made to this particular area. It was, and still remains, the largest oil spill in American history. More than 1,900 km of Alaskan coastline was affected. The actual size of the spill is still debated. Exxon initially reported the spill as 10.8 million gal, but others have challenged that figure and have estimated the spill at approximately 35 million gal. Other large oil spills include the *Ixtoc-1* blowout off the Mexican coast (1978: about 400 million gal); the tanker *Amoco Cadiz* off Brittany, France (1978: 69 million gal); and the tanker *Torrey Canyon* off the English coast (1967: 38 million gal); as spills go, the *Exxon Valdez* does not rank in the top oil spills worldwide. Yet the environmental impact of this spill was enormous. It is clear that thousands of animals died in a very short period of time after the spill, and the most reasonable estimates suggest 250,000 sea birds, 2,800 otters, 300 harbor seals, 250 bald eagles, up to 22 orcas, and billions of salmon and herring eggs.

The cleanup of the oil spill took more than 3 years and cost in excess of $2.1 billion. Several years later, the U.S. Congress passed the Oil Pollution Act of 1990, which authorized the Coast Guard to strengthen regulations on oil vessels, oil tanks, and owners and operators.

Despite extensive hearings, trials, and investigations, it is still not clear how or why this accident occurred. It has been alleged, but never proven, that the ship's captain, Captain Joseph Hazelwood, was operating under the influence of alcohol. A jury in Alaska found him not guilty of operating a vessel under the influence of alcohol, but he was seen in a bar prior to the ship leaving port. All parties agree that there was a well-qualified pilot on the ship, who left after the vessel cleared the Valdez narrows. The ship maneuvered to avoid icebergs in the channel (not an unusual occurrence). Captain Hazelwood left the bridge at this time, and it is not clear why the ship did not turn back into the shipping channel after avoiding the icebergs. The ship was taken to San Diego for repairs (estimated to have cost $30 million) and renamed the *SeaRiver Mediterranean* (still in service). It was barred from ever entering Alaskan waters again.

In 1991, Exxon settled several lawsuits (criminal and civil) and paid over $1 billion in fines and penalties as a result of the events in Valdez. An Anchorage, Alaska, jury awarded punitive damages to the tune of $5 billion in 1994. Exxon has fought this award, and as of July 2006, it is currently on appeal at the 9th U.S. Circuit Court of Appeals. Exxon Corporation's handling of the spill—both the cleanup and the communications as the event unfolded—has been subjected to deep criticism and scrutiny. The *Exxon Valdez* has entered into our vocabulary as an example of enormous environmental damage and poor corporate response to that damage.

—John F. Mahon

See also Corporate Issues Management; Corporate Public Affairs; Corporate Social Responsibility (CSR) and Corporate Social Performance (CSP); Crisis Management; Environmental Ethics; Reputation Management

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Factory Farming

Factory farming generally refers to confined animal-feeding operations (CAFOs), in which very large numbers of animals—especially cattle, pigs, and chickens—are crowded in a narrow space to gain weight, and therefore value, as rapidly as possible. In pursuit of optimum weight, motion is discouraged, and since animals tend to become sick in crowded and unhygienic conditions where exercise is impossible, their food is laced with antibiotics to keep them healthy as well as hormones and other nutritional supplements to speed their growth. Forty percent of the world's meat supply is raised in CAFOs.

At one point, CAFOs, and the agricultural practices associated with them, were restricted to Europe and North America, as the largest consumers of meat. With the new prosperity in China, Brazil, India, and other recent entrants to the global economy, the farms have spread worldwide, especially near the urban concentrations of Asia, Africa, and Latin America.

On the one hand, these practices have made fresh meat much more available to consumers in all parts of the world. Furthermore, the meat is not very expensive, largely because of the world overproduction of grain, which will fatten the animals much more quickly than will grass. Consumers have voted with their dollars to maintain these practices.

On the other hand, many objections to CAFOs have been raised, which may be summarized as follows:

First, there is widespread hunger in the world; the grain surpluses are artificial, fueled by developed world subsidies, and cry out for more equitable distribution. While people starve, critics have argued, it is wrong to feed the cereal grains that could save their lives to animals. (It takes about 10 pounds of plant protein to make 1 pound of animal protein.) Growing meat is not a good allocation of the food resources of the world.

Second, it is not clear that the addition of substantial amounts of animal protein is a good thing for the health of the developing world, or indeed for anyone. Most of the degenerative, chronic, and most dangerous conditions of the developed world are associated with animal protein and fat—heart disease, stroke, obesity, and several forms of cancer come to mind. Critics insist that there is no health imperative to maintain these facilities.

Third, the pollution that they generate is arguably an assault on the eyes, the nose, the neighborhood, and the natural environment. Where cattle, chickens, and pigs roam freely in small numbers over pastures, their widely distributed manure fertilizes the ground and enriches their food supply. But the CAFOs provide no room to spread and reabsorb the manure; it is stored in lined pits or lagoons in concentrations that would be toxic to any natural ecosystem. Discharge of the manure into the local waterways would kill all life for miles; spillage on the land makes the land unusable. Ironically, critics point out, this most organic of products, the manure of domestic farm animals, has become as threatening to its environment as any store of nuclear waste. And the amount continues to increase, exponentially.

Fourth, the concentration of work for the sake of maximizing profit changes the traditional work of the farmer and herdsman into an industrial job with traditionally unsafe conditions. When Upton Sinclair wrote *The Jungle* in 1906, the meatpacking industry was characterized by brutal and unsafe conditions in long hours of work. Since the 1970s, observers of the industry report, those conditions have largely returned, especially in those parts of the world without well-enforced worker safety provisions. In long rooms called disassembly plants, where the animals are butchered as rapidly as possible, not all the blood on the floor comes from the animals.

Fifth, critics argue that the nature of the industry leads to the choice of just the most profitable, that is the fastest growing, breeds to raise. Genetic engineering has made possible breeds of chickens, for instance, that have huge breasts and unworkable wings—in any disruption, not one would survive. Traditional breeds of cattle, pigs, and chickens, adapted to the climates in which they evolved, are in danger of disappearing altogether, taking with them the possibilities of reverting to them should climatic conditions become more extreme.

Sixth, the crowded conditions of the animals spread disease with terrible rapidity, the source of severe loss of profit unless countered with regimes of antibiotics that cure disease, prevent disease, and, independent of any disease, increase the rate of growth of the animals. Regular use of antibiotics, the critics point out, reliably produces antibiotic-resistant germs, and the result of that last is the spread, through the human population, of microbes that are resistant to all known antibiotics, and that is a very dangerous condition indeed.

Seventh, the suffering of the animals themselves in these crowded and toxic quarters is obvious, and heart wrenching to those who care for them.

For all those reasons, factory farms have become the target of activist nongovernmental organizations (NGOs) and restrictive legislation in many parts of the world, especially in the developed nations. While they are economically profitable, however, the practices adopted by them will continue.

—Lisa H. Newton and Keith Douglass Warner

See also Agribusiness; Agriculture, Ethics of

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Fact-Value Distinction

The fact-value distinction is generally summarized as the distinction between what is, or descriptive claims (the realm of facts), and what ought to be, or normative/prescriptive claims (the realm of values). Even though the issue of the fact-value distinction is closely intertwined with the is-ought distinction—and often the two are conflated in discussions, arguments, or positions—they are not identical. It can be held, for example, that values are natural facts or that normative propositions are factual or that normative claims assert nothing about real values.

The issue of the fact-value distinction came to the forefront, during the Enlightenment, with David Hume's argument that normative claims about values or what ought to be cannot be derived from descriptive claims about facts or what is. Hume argued that there is a gap between facts and values or between what is and what ought to be. For example, the fact that you promised to repay me the money you borrowed does not imply the conclusion that you ought to do so unless there is added the nonfactual, moral premise that one ought to keep one's promises or that one ought to repay one's debts. Hume argues that ethical philosophers make an imperceptible switch from the realm of facts to the realm of values, with no explanation offered. The switch to the value realm of obligation introduces a new relation or affirmation that needs to be clarified and justified. However, since he can find no justification, Hume suggests such a derivation cannot be made.

This problem was reinforced in the 20th century with G. E. Moore's attack on the view that moral terms are completely definable in nonmoral terms. The view he attacked, held by many philosophers who were ethical naturalists, claimed that moral judgments are a subspecies of empirical judgments and that moral terms stand for purely natural characteristics. They held, for example, that moral goodness can be defined in terms of one or more natural properties that we already understand. An instance of this would be the hedonist standpoint that good means pleasure. But, Moore points out, we can always ask if pleasure is always good; for it is not a contradiction to say that some pleasures are not good. Moreover, this lack of contradiction holds for any empirical property or set of properties that can be offered. These are significant questions regardless of what properties are substituted. But, if the naturalists are right, asking these questions should mean only that the questioner does not understand the terms being used. It would be like asking if all sons are male.

Moore argued that a naturalistic fallacy is committed when one identifies value properties with natural or empirical properties. He held that the property of moral goodness is simple, indefinable, nonnatural, or nonempirical and must be immediately grasped by a nonnatural moral intuition. This is analogous to an empirical quality such as yellow. The meaning of yellow cannot be understood by any definition, such as wavelengths, or by knowing that ripe lemons are yellow. Rather, yellow must be immediately experienced by a sensible or natural apprehension, a natural intuition. He calls the fallacy involved the naturalistic fallacy in ethics because it involves confusing a natural property, such as pleasure, with the nonnatural property of goodness.

The fact-value distinction has influenced the directions taken by the social sciences and business ethics. Scholars interested in business ethics seem, for the most part, to have split into two camps in delineating two kinds of business ethics, the normative and the empirical. The former is considered to be a prescriptive or value-laden approach and the latter an explanatory, descriptive, and/or predictive approach concerned with empirical facts.

The normative approach is rooted in philosophy and the liberal arts and focuses its attention on questions of what ought to be, how an individual or business ought to behave to be ethical. The empirical approach is rooted in management and the social sciences. This approach generally focuses on questions of what is, assuming that the organizational world is basically objective, awaiting impartial exploration and discovery. Empiricists answer questions of what is by attempting to describe, explain, and/or predict phenomena in the natural world, using the agreed-on methodologies of their social scientific training. Scholars who represent these different domains are said to be guided by different theories, assumptions, and norms that often result in misunderstanding or lack of appreciation for each other's endeavors.

The social scientist may devalue the philosopher's moral judgments because these judgments cannot be understood in empirical terms and cannot be verified by empirical testing or be used to predict or explain behavior. The social scientist's statements about morality, on the other hand, may be seen to be of little value to the philosopher because they do not address the essential questions of right and wrong. Normative ethical theories develop standards by which the propriety of certain practices in the business world can be evaluated. In contrast, the empirical approach focuses on identifying definable and measurable factors within the individual psyches and social contexts that influence individual and organizational ethical behavior.

In a broad sense, the fact-value split leads to the view that facts are not action guiding, for they do not indicate that something ought to be done. They are descriptions and causal explanations of human or natural phenomena. Value judgments, on the other hand, do have an action-guiding function and commend or condemn particular courses of action, whether this commendation or condemnation is held merely to evince subjective feeling or state an objective standard. Whether subjective or objective, such statements are usually understood as immune from scientific testing and hence are radically different from scientific claims and beyond factual refutation or verification.

While the two domains may be held to rely on each other in a practical relationship, they are two differently oriented conceptual sets with distinct methodologies. There are attempts to bring normative and empirical inquiry together under one big conceptual tent, but these are still usually understood in terms of the endeavor of trying to bring into a symbiotic relationship two distinct realms, facts, and values.

This split between the two approaches to business ethics is another manifestation of a problem that has existed between philosophy and science for several centuries. The fact-value gap as it developed and became entrenched in the way we think was grounded in what many think was a narrow empiricism rooted in the implicit acceptance of a scientific description of nature as exhaustive of what kinds of qualities can really exist in nature. It resulted in the view that empirical experience cannot include the experience of value, just as value cannot be a real irreducible quality unless it is nonnatural, to be experienced in a nonempirical way. What science finds is what and only what is truly real and truly knowable, and what we experience is reducible to the procedures and contents of math and science. Moore's attack on empiricism in ethics (because empiricism is unable to reduce normative claims to empirical claims) is based on the insight that value is not reducible to something other than itself. Along with this, however, he held deeply embedded assumptions, rampant in his time, regarding what can be experienced empirically and what kinds of qualities can exist in nature; if value is irreducible to the kinds of properties that can exist in nature and be experienced empirically, then value must be nonempirical.

A different approach may be taken that undercuts the fact-value distinction. This does not collapse the two fields of normative inquiry and empirical research. Rather, such an approach understands empirical and normative business ethics not as inquiries that focus on two different realms, facts and values, but as inquiries that focus on different dimensions of a concrete unified situation based on the two fields' differing contextual interests. In this way each area of business ethics can recognize that its particular perspective and approach not only cannot substitute for those of the other but also that in fact each approach gains its full significance only within the context of the other.

This way of viewing the two fields is found in a position known as holism. Holism understands the whole as having a significance that is on a level different from that of its parts. The meaning of the whole is greater than the aggregate meaning of its elementary parts, and things can have properties as a whole that are not explainable from the properties of their parts.

A dominant form of this position is called emergentism, the view that the properties of the more complex level are unique emergents that are lost when reduced back to parts whose interactions give rise to them. For example, for the reductionist, water is nothing but hydrogen and oxygen, while the emergentist holds that the unique qualities of wetness, thirst-quenching ability, buoyancy, and so forth, are emergent properties of the whole that are as real as, but on a level different from, those of the hydrogen and oxygen whose interaction gives rise to them, and these real emergent properties are lost when water is reduced to nothing more than the sum of its parts.

This position claims that nature is rich with contextually emergent qualities, including value as an emergent in the interactive context of natural organisms, just as wetness is an emergent property in the interactive context of hydrogen and oxygen. Value need not be, nor can it be, reduced to some experienced quality other than itself, for it is among the qualities that pervade our sensory experience. The occurrence of the immediate experience characterized by value is a qualitative dimension of a situation within nature, on an equal footing with the experiencing of other qualitative aspects of nature. Furthermore, any experienced fact within the world can have a value dimension, for the value dimension emerges as an aspect of the context within which the fact functions as value relevant. Indeed, the experience of value is itself a discriminable fact within our world.

According to this view, claims about the valuable, what ought to be, are about the enrichment of value, about creative ways of organizing the real but conflicting value qualities of experience to direct activity toward what works in enhancing value-relevant qualitative experiences in the long run for all those involved. This understanding of value-relevant qualities as contextually emergent natural properties, and the normative as about the enrichment and expansion of the value dimension of concrete human existence, undercuts the problematics of the fact-value issue as originally put forth.

In responding to the issue of the fact-value distinction, nonreductive naturalists in general agree that value concepts are special and sui generis but argue that value properties are natural properties. Emphasizing broad empiricism and holism, they claim that both facts and values are wedded dimensions of complex contexts that cannot be dissected into atomic bits. The entire fact-value problem as it has developed out of the past tradition of moral philosophy is wrongheaded from the start. The problem of how values can exist in a world composed of facts, or how one can get normative claims about what ought to be from descriptive statements of what is, is based on philosophical starting points that are alien to their way of thinking. For the nonreductive naturalist, the problem is not to figure out how to unite two ontological discretes, facts and values, but rather to figure out how to distinguish the two dimensions, for purposes of intellectual clarity and advancement of understanding, without viewing the resultant "products" in ways that distort both the qualitatively rich, unified concrete reality they are intended to clarify and the thought processes by which these products are obtained. Of course, there is a difference between normative and descriptive claims, but according to this view the distinction is not ontological but functional. Whether a statement is descriptive or normative depends on its situational function.

The rejection of the split between facts and values often leads to the view that normative judgments involve facts and causal relations relevant to the potential production of valuing experiences. Moreover, the rejection of this distinction is a strong impetus for the view that the empirical approach does not necessarily describe what actually occurs (objectively given facts) but rather describes what the researchers' conceptual nets are structured to catch and the values inherent in the very way the researchers structure their nets. Even the most scientific of disciplines are affected by the values of the people who direct the research and practices in that discipline and are thus value laden throughout. Some are led to oppose the fact-value distinction precisely because they accept the position that modes of factual inquiry presuppose values.

The separation of facts from values has led some to embrace either moral skepticism of some sort or various forms of noncognitivism or relativism. Noncognitivism holds that expressions such as "Lying is wrong" do not express factual claims or beliefs and therefore are neither true nor false, or that there are no objective facts to make them true or false. It may hold that such statements are either expressions of emotional approval or disapproval, prescriptions or commands, or nonfactual or nondeclarative speech acts that can work as if they were cognitive. Ethical relativism takes the position that that there are no universally valid moral principles. Morality is purely conventional, and moral claims are valid if they conform to the conventions of the particular culture (cultural relativism) or individual choice (individual relativism).

The issue of the fact-value relationship has a long history and, regardless of the stance one takes toward it, it continues as a driving force in our ways of thinking, shaping the developing course of the various disciplines, and structuring ongoing debates.

—Sandra B. Rosenthal

See also Cognitivism and Ethics; Hume, David; Is-Ought Problem; Naturalistic Fallacy; Normative Theory Versus Positive Theory

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Fair Labor Association (FLA)

The Fair Labor Association (FLA) is a nonprofit organization that represents the combined efforts of the apparel industry, various nongovernmental organizations (NGOs), and colleges and universities to improve the conditions of workers around the world. In 1996, at the initiation of the U.S. Department of Labor, 300 apparel company representatives participated in the Fashion Industry Forum. This workshop was intended to raise awareness of labor and human rights abuses against persons employed in manufacturing clothing. As a result of the success of that forum, under the auspices of the White House, the Apparel Industry Partnership (AIP) was formed. The partnership consisted of representatives of labor unions and consumer advocacy, human rights, and religious groups. The purpose of the AIP was to improve conditions and eliminate abuse of adults and children in the garment industry, regardless of location. Participation by companies is voluntary.

Formation of the FLA

The principal mechanism to achieve an improvement in the working conditions is a code of conduct supported by independent monitoring. The code applies to both company-owned operations and, importantly, contractors who manufacture garments for the companies. Key elements of the code cover working conditions, minimum wages, limits on forced overtime, and banning child labor. Principles for monitoring compliance with the code of conduct were also developed. To recruit additional companies for membership, monitor compliance, and publicize the compliance with the code of conduct, the FLA was formed by the AIP. Publicizing compliance by member companies includes labels on clothing and statements or logos in advertising and in stores that advise consumers that the factories where the garments were produced met the

FLA standards. Another branch of effort by the FLA is to monitor the activities of licensees for college-branded merchandise. Based in Washington, D.C., FLA has a board of directors that includes six company representatives, six representatives from NGOs, three university representatives, and its chairperson.

FLA Membership

Apparel manufacturers belong to FLA to seek accreditation of their compliance programs. FLA does not certify companies but the compliance programs themselves. Companies seeking accreditation must commit to conduct internal audits of their factories, permit the FLA to review internal audit records, communicate the workplace standards to its management, submit their suppliers' factories list to the FLA, and allow the audit results to be publicized by the FLA. Unannounced audits are part of the compliance procedure, and FLA represents that approximately 5% of covered factories are audited each year.

College licensees join by applying in one of four categories, A through D, generally based on the size of the company and location. The compliance standards are similar to the apparel manufacturer requirements above.

NGOs and trade unions also belong to FLA and participate through the FLA's NGO Network. These groups are encouraged to participate in the standards-setting process and to assist in the monitoring efforts of FLA factories.

Numerous brand-name companies belong to the FLA, including Adidas-Salomon, Eddie Bauer, Liz Claiborne, Nordstrom, and Nike. These companies have committed to compliance with the FLA Code of Conduct and the related monitoring efforts. Colleges and universities join the FLA to insure that goods bearing their logos are produced under humane conditions. More than 180 schools require their licensees to participate in the FLA college licensee program.

Code of Conduct

The FLA Code of Conduct covers a number of aspects of employment. Forced labor in any form is banned. Child labor is also banned. The FLA considers child labor as involving persons younger than age 15, subject to adjustment for the age at which compulsory education ends in the country where the factory is located. Harassment or abuse of any kind is also prohibited. Employees are not to be subjected to discrimination in any facet of employment based on gender, race, religion, age, disability, sexual orientation, nationality, politics, or ethnicity. Healthy and safe working conditions are required. Employees must be allowed to associate and bargain collectively.

The Code of Conduct also requires employers to provide the higher of the minimum wage required by law in the location of the factory and the prevailing industry wage. Benefits mandated by law must also be provided. Employers shall not require employees to work more than 48 hours in a week, or more than 12 hours overtime, except in extraordinary business circumstances. Employees must be provided at least one day off in every seven days. Overtime compensation must meet the legal requirements of the jurisdiction where the factory is located or be at least the normal hourly wage, where it is not legally defined. Application of the Code of Conduct also applies to licensees, contractors, and suppliers of the member organizations.

Monitoring

Monitoring compliance with the Code of Conduct is a key aspect of FLA membership. In addition to compliance with all applicable laws of the location of its factories and the FLA Code of Conduct, companies must submit to monitoring. The monitoring for compliance takes two forms, internal and external. Internal monitoring requires member companies to establish an internal system of monitoring their production facilities. This includes communicating to employees their rights under the Code of Conduct, establishing relationships with labor unions and human rights organizations, training company monitors, providing employees with a grievance procedure, conducting internal inspections of its facilities, and committing to correct situations that are not in compliance.

External monitoring involves inspection of member company facilities by independent monitors who are accredited by FLA. The results of these unannounced audits are reported to FLA and the company. Any deficiencies must be corrected by the company to maintain its accredited status with FLA.

Reporting

Member companies submit annual reports to FLA that report on compliance activities and any corrective actions that have been taken as the result of the monitoring activities. These member reports are reviewed by FLA and combined with the results of external monitoring activities to generate an annual report on each member company. These reports are publicly available on the FLA Web site.

Perspectives on FLA

Some human rights groups and union representatives have challenged the good faith of the participants in the FLA, characterizing their participation as motivated more by public relations than concern for their workers. One issue raised by critics is the FLA's establishment of a minimum wage in compliance with the laws of the country of manufacture or the prevailing industry wage. Critics have argued for what has been called a living wage. As various companies choose to join the FLA, this issue has become more contentious, with other monitoring organizations being touted by various public interest groups. The Worker Rights Consortium (WRC) was established by college students to monitor factories producing goods sold with college emblems. This group has lobbied for a living wage and mandatory disclosure of the factories where the goods are produced. Some manufacturers claim that identification of the factories is proprietary information. Duke University has joined both the FLA and WRC in an effort to meet student demands.

Regardless of the organization doing the monitoring, accurate information from the factories themselves is a key component. Recently, serious issues have been raised about the veracity of the reporting of work hours and overtime pay for factories in China. There have been reports that managers of Chinese factories have been coached on how to falsify work records to disguise unpaid overtime. Monitoring efforts may not result in improved working conditions in such cases.

Advocates of a free market approach have suggested that monitoring efforts may reduce employment opportunities in some countries to the detriment of the workers who most need the wages. In some cases, factories have lost large contracts when monitoring agencies reported unacceptable conditions. The resulting layoffs led to even more difficult economic conditions for the employees, who have little alternative employment. An issue of national sovereignty has been raised by some observers. When a monitoring agency from a developed nation enters a country and criticizes the way its citizens are being treated, there is an implicit criticism of the government of that country. Historians note that many countries used child labor as they developed, including the United States.

The voluntary nature of membership in the various monitoring organizations, including the FLA, introduces the issue of cost and production margins. In most cases, manufacturers that have joined FLA produce widely known major brands that sell for relatively high market prices and produce significant wholesale and retail margins. This is also true of college-branded merchandise. Notably missing from membership in FLA are major retailers such as Wal-Mart and Target, which produce large amounts of private-branded merchandise. This means that large amounts of goods produced throughout the world are made in factories where there is no independent monitoring that takes place, although the companies may undertake their own efforts.

Conclusion

As long as there are significant disparities in world economies, there will be controversy regarding appropriate working conditions, wages, overtime, and child labor. FLA functions as one of a handful of agencies that attempt to provide an independent view of working conditions in manufacturing facilities, primarily in less developed countries.

—David D. Schein

See also Child Labor; Sweatshops; Women in the Workplace; Worker Rights Consortium (WRC); Working Conditions

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FAIRNESS

Fairness is a term that is commonly employed. In respect of its everyday usage, it is commonly interpreted as meaning justice, the absence of bias, and being equitable or impartial in accordance with certain rules. As such, whenever claims of unfairness are considered, seemingly familiar and accepted principles are employed in determining the merits of the claim.

On reflection, whenever the notion of fairness is employed, many questions remain unanswered, not least the question of whether the notion of fairness can be an objective assessment. Its nature is also problematic. Whether justice, a lack of bias, and an equitable or impartial process or outcome are determinants that can be substituted for fairness or whether fairness is something more or less than any one of them is uncertain. The term justice is especially problematic: Some authors interchange the terms fairness and justice haphazardly, whereas others postulate fairness as being fundamental to justice, thereby suggesting that it is some form of subset.

The underlying basis for claiming fairness is also uncertain. The term carries moral overtones; it conveys something that is generally regarded as moral and ethical, and yet the foundations for whatever fairness is and what it conveys are unclear.

A decision or action may also be considered to be fair if it is in accordance with the relevant rules or standards or in accordance with a person's rights. But when viewed from another moral perspective, a decision or action may be fair only if it maximizes the well-being of individuals in society.

The complexity of fairness is revealed in the literature pertaining to moral philosophy; it is here that we appreciate fairness as a notion that lacks clarity or consistency in terms not only of its being identified as a moral concept but also its relevancy.

Fairness as a Moral Concept

The notion of fairness as a moral concept is often justified by reference to social norms that guide ordinary individuals in their everyday lives; it is also argued that notions of fairness are self-evident, in accord with instinct and intuition, and that there is no need for an explicit justification of what is fair. These arguments are appealing because notions of fairness such as keeping promises, holding wrongdoers accountable for their actions, and promoting well-being correspond to internalized, meaning-inculcated, and inborn social norms. But these arguments do not provide a satisfactory answer, and, given the extent to which fairness is employed, there is surely a need to further elaborate its moral basis.

That the notion of fairness is employed extensively can be evidenced by our understanding of a "fair game." Whether in the context of recreational games, house rules, professional codes, or laws, fairness is invariably intended in creating the so-called rules of the game. Thus, laws governing discrimination are intended to ensure fairness in the way people are treated, irrespective of, for example, their sex, race, age, or family status. That we create such rules suggests that we perceive a need to reinforce fairness as an internalized social norm or that we need to establish what is fair in a particular circumstance because otherwise there may be conflicting claims as to what is a fair game.

Arguably, we increasingly perceive a need to reinforce fairness as an internalized social norm not only to ensure fair game but also to overcome greed, and other unsociable behavior, and to bring about ordered societies. The notion of fairness is thus evident in theories relating to a social contract.

Fairness as a moral concept is, at best, vague. But if fairness is grounded in intentions, it may be that we can identify what we understand to be fair. A fair intent underlying a particular process or outcome will ensure that rules, codes, and laws endure. But intent is problematic in the event that a fair intention is thwarted by unfair processes or leads to an unjust outcome.

The Relevancy of Fairness

Here there are essentially two major concerns, the fairness of procedures and the fairness of outcomes.

The fairness of procedures is concerned with the absence of bias. If a decision or action is unbiased it means that it is made or done impartially, free from self–interest, and without preference or favoritism. Thus, in the event of several companies submitting tenders for a contract, if every company has an equal chance of success, the tender process can be described as being fair. But if the person determining the successful tender has an interest in one of the companies concerned, a conflict of interest arises and the procedures will appear to be unfair.

The fairness of procedures is also concerned with rights. The rights that are commonly claimed in relation to the fairness of procedures include the following: the right to be heard, the right to remain silent for fear of self-incrimination, and the right of presumed innocence until proven guilty. Such rights are regarded in Western societies as pertaining to Natural Justice. Others talk of rights more generally as human rights: the rights of free speech, freedom of the press, and privacy. These rights may also have an effect on procedures.

The process of negotiating business transactions raises complex issues concerning the fairness of procedures; while a fair game and a level playing field are accepted as the basis for certain laws governing the formation of contracts, such as misrepresentation and unconscionable bargains, the processes employed to agree on the terms of a contract, and the contract terms, are essentially for the parties themselves to determine. Negotiation is arguably morally justifiable if all persons importantly affected by a transaction are in agreement.

Aristotle took the view that trading, generally, and making a gain out of money, by usury in particular, are unnatural ways of gaining wealth. His notion of virtue requires habit of action in an intermediate state between the opposed vices of excess and deficiency. Thus, justice is the mean between doing injustice and suffering injustice. If the process of negotiation ensures that neither party gains more than the other from the transaction, it would be just. Thus, a price must be negotiated that equals the true value of the goods.

In practice, and given the nature of business today, this notion of fairness is arguably untenable. But Immanuel Kant would also condemn negotiations that do not abide by the golden rule of treating others the way you would like to be treated or, more precisely, acting in a way that would be accepted as a universal law. Fairness of procedures is also evidenced by the rules governing all forms of inquiry; in the event of an assessment for entitlement to social benefits or an investigation into an accident, there needs to be a fair process as a means of ensuring a fair outcome. The fairness of outcomes is a subject that has received a good deal of attention and that continues to provoke debate employing notions as diverse as equality, retribution, compensation, and need.

Equality as a principle of fairness has long been regarded as a social ideal. Egalitarians hold that there are no relevant differences among people that can justify unequal treatment, that all benefits and burdens should be distributed equally, that all human beings are equal, and that each person has an equal claim to society's goods. This argument is however heavily criticized on the grounds that (inter alia) human beings differ in their abilities in terms of their intelligence, virtues, needs, desires, and all other physical and mental attributes. The needs, abilities, and efforts of human beings will thereby be ignored.

The notions of retribution and compensation tend to be relevant to the outcome of criminal as well as negligent behavior. Retributive justice refers to the just imposition of fitting punishment and penalties on those who do wrong. Thus, it is fair that a person who has committed a serious crime is imprisoned for a certain period of time, whereas a person who has committed a minor offence is fined or required to perform some form of community service. Compensatory justice refers to the opportunity for obtaining compensation in the event of being wronged by others. Thus, it is fair that the victim of an accident has the opportunity to sue a negligent injurer (and that the negligent injurer pays). If such outcomes are just, it implies that conscience, ethics, and reason are employed as a means of ensuring fairness and that justice is being served.

Determining the fairness of outcomes is undoubtedly the most controversial and problematic aspect of fairness. In the event of competing claims of what would be a fair outcome, utilitarian theories offer a balance of social benefit over social cost. Thus, we need to identify the various courses of action that are available, and we need to ask who is affected by each action and what benefits or harms will be derived from each. We then choose the action that will provide the greatest benefits and the least harms. Utilitarianism thereby poses a number of difficulties relating to measurement and balancing one set of factors against anther. But, of greater difficulty is the fact that this outcome ignores not only the means but also other consequences, both of which may be grossly unfair.

While utilitarianism has been refined to accommodate some of its critics, Jeremy Bentham's notion of the greatest good for the greatest number (maximizing social utility) in his search for an objective basis for determining social policy and social legislation, which is regarded as traditional utilitarianism, is still respected. His concern was for making value judgments that would provide a common and publicly acceptable norm. But an evaluation that depends only on consequential benefit and ignores justice and fairness is arguably absurd.

The connection between justice and utility is a subject explored by John Stuart Mill. He discusses impartiality and inequality for the purpose of discerning the common attributes of justice by reviewing various actions that he argues are commonly regarded as unjust.

Mill concludes from his review that justice, as distinct from generosity or beneficence, constitutes a moral obligation or duty with a correlative moral right relying on the notions of punishing those who have done harm and knowing or believing that there is some definite person(s) to whom harm has been done. He concludes that nearly all cases of justice are also cases of expediency but that sentiments of justice have more definite commands and sterner sanctions. He illustrates this by reference to maxims of justice that are commonly appealed to: that it is unjust to condemn any person unheard and that the punishment ought to be proportionate to the offence. But Mill also acknowledged that in particular cases some other social duty may be so important that it overrules any one of the general maxims of justice. Thus, in some circumstances, stealing food may be justified to save a person's life.

In the course of this discussion Mill touches on the notion of distributive justice and benefits for all, as opposed to the majority. In his view, having an equal claim to happiness and to all the means of happiness, except insofar as the inevitable conditions of human life set limits, requires bending to every person's ideas of social expediency and ultimately leads to injustice and tyranny. He then reverts to utility and to utilitarianism.

John Rawls was deeply concerned with this apparent flaw, offering an egalitarian theory of justice that seeks to protect the least advantaged from the tyranny of the majority. Rawls advocates that ethical decisions or acts are those that lead to social justice in the form of an equitable distribution of goods and services. His approach is Kantian in that he attempts to arrive at a set of principles that are acceptable to all rational persons. These principles must be universal, must respect all persons, and must be rationally acceptable to all. To find such principles he suggests imagining that all people are behind a "veil of ignorance," meaning that behind the veil they would not know whether they were rich or poor, upper or lower class, talented or untalented, and so on. They would make rational choices and so determine principles that are just or fair and thus achieve a more objective and equitable method of distributing goods and services.

Rawls proposes two basic principles that, he argues, we should select if we were to use a fair method of choosing principles to resolve our social conflicts: first, the principle of equal liberty and, second, the principle of fair equality of opportunity. Together they ensure the greatest benefit to the least advantaged. But he does also permit economic inequalities if they do in fact benefit the least advantaged.

Karl Marx's criticisms of capitalism as being unfairly advantageous for the wealthy at the expense of the workers are extensive. He argues that capitalism necessarily produces inequality, promotes injustice, and undermines communal relationships. But ensuring fairness by reference to ability and need also produces difficulties.

Libertarian theories also appeal for fairness. They reject the conclusion that egalitarian patterns of distribution represent a normative ideal arguing that it would be a basic violation of justice to regard people as deserving of equal economic returns—that people have a fundamental right to own and dispense with the products of their labor as they choose, even if this leads to large inequalities of wealth in society.

Robert Nozick, a personal libertarian, argues that morality springs from the maximization of personal freedom and that individuals should be free from the interference of others. Justice and fairness, right and wrong should not be measured by equality of results (e.g., wealth) for all but from ensuring equal opportunity for all to engage in informed choices about their own welfare. Such negative natural rights justify the acquisition of wealth—wealth acquired without harming anyone else is fairly gained. Despite these enduring theoretical differences, common ground as to the relevancy of fairness can be found, especially in the relatively limited spectrum of business ethics.

Fairness Employed in Business Practices

The notion of fairness can be seen in a vast array of business practices but predominately in procedures and relationships between companies and their employees.

The procedures employed for selection, payment, and promotion of employees need to assure fairness. The short-listing of candidates, the interviewing, and the ultimate selection all need to be conducted fairly as a means of ensuring that the outcome is fair. The information in personnel files is critical in making decisions about wage increases and promotion and likewise needs to be fairly collated and accurate; otherwise the decision making will be unfair. The pay scales also need to be fair.

Determining what is fair, and setting up systems to ensure fairness, may meet with resistance simply because of a reluctance to change but especially if the new system requires greater disclosure of what is perceived to be a private matter. The notions of fairness explored in the foregoing may be employed to justify the proposed changes. The disclosure of the pay scales for executives, for example, can be justified by reference to both Marx and Nozick. They might agree that such information should be publicly available, but Marx would see it as a means of paying equity for the workers and Nozick would see it as accountability and transparency for investors.

Similar issues arise in relation to the directors of companies that look to the general public to raise funds. Fairness is employed to argue for greater transparency in matters such as nominating and appointing a director to the company's board of directors and disclosure of directors' remuneration packages.

Fairness is also employed extensively in matters relating to finance. In presenting and disclosing financial information, it is used as an evaluative principle, for example, auditors being required to report on whether a company's financial statements provide a "true and fair view" of its state of affairs.

In regulating markets, fairness serves as a means to the end of efficiency. While the main aim of financial markets regulation is to ensure efficiency, it is acknowledged that markets can be efficient only when people have confidence in their fairness and corresponding stability. Regulations concerning insider dealing and other forms of manipulation in the sale of securities are designed for this purpose. Trading off efficiency in recognition of the need to ensure fairness, the so-called equity/efficiency trade-off is commonly employed to justify further regulation of securities markets.

In relation to finance, that fairness may also be employed as an end in itself is clearly demonstrated by the notion of pro rata: that a company's dividends are paid in proportion to the amount paid up on the relevant share and that in insolvency, distributions to unsecured creditors are paid to all such creditors in the same proportion.

Societies are now demanding ethical business practices that go beyond the demands of their legal systems, and companies have responded by developing their own codes of practice. The development of in-house policies and rules dealing with ethical practices commonly relies on the notion of fairness. It may be that many of the broader theoretical disputes discussed in the foregoing are at least partially resolved when the notion of fairness is employed in a particular setting.

—Vanessa Stott

See also Accounting, Ethics of; Age Discrimination; Aristotle; Codes of Conduct, Ethical and Professional; Competition; Conflict of Interest; Consent; Disability Discrimination; Disclosure; Egalitarianism; Employee Protection and Workplace Safety Legislation; Employment Discrimination; Equal Opportunity; Gender Inequality and Discrimination; Glass Ceiling; Golden Rule, The; Human Nature; Impartiality; Informed Consent; Integrity; Justice, Distributive; Price-Fixing; Racial Discrimination; Rawls's Theory of Justice; Reasonable Person Standard; Religious Discrimination; Restraint of Trade; Sweatshops; Transparency; Unfair Competition

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Family-Friendly Corporation

A *family-friendly corporation* is a workplace that recognizes the family responsibilities of its employees and implements policies that allow them to sustain a work and family life balance. It can also be called a family-friendly company or family-friendly employer.

There are several reasons why organizations decide to become family friendly. Some of them adopt family-friendly programs in an effort to create a committed workforce. Other reasons are improving retention and productivity and providing an environment that allows employees to simultaneously accomplish work and family responsibilities.

Family-friendly corporations were initiated partly by the demographic changes in Western countries: Women entered the labor market in a massive way during the Industrial Revolution, the divorce rate increased, the number of single-parent families rose, and the birth rate decreased. The trend continues as Europe, for example, is currently experiencing a "demographic winter" (diminished birth rate in industrialized countries).

However, not all organizations consider these changes when they manage and organize their staff. The traditional work structure is still basically designed for male employees with timetables that are not compatible with other needs such as caring for dependents (children, the elderly, or persons with special needs) and being at home.

As a consequence of these sociodemographic changes, many people experience a big conflict among different life scenarios, especially between work and family. This is a reality not only for working mothers who are taking care of the family but also for working fathers, who are now more involved in family tasks.

Different Views About Family-Friendly Corporations

Reasons to become a family-friendly corporation may vary from one organization to another. Some companies implement family-friendly programs as a response for meeting the minimum requirements of the legislation and also as a response to the pressure and demands coming from their workforce. These organizations care about their image and use their family-friendly initiatives as a marketing strategy to attract more candidates and customers. Companies named "best employers" receive many more job applications per position compared with other firms.

Other organizations are on an alert status and do not want to risk losing valuable and efficient employees. They implement family-friendly programs to attract and retain people by creating favorable working conditions. Research suggests that giving employees flexibility, information, and financial assistance can improve the whole organization's performance and raise employees' satisfaction.

It is important to clarify to employees that not all family-friendly initiatives can apply to all of them at all times. One of the reasons is that not all employees have to take care of dependent persons. As a consequence, some employees may feel left out when compared with others and may have a negative attitude toward the organization. Therefore, it is advisable when implementing family-friendly programs to determine objective criteria and be consistent in the application process. Some organizations prefer to adopt a "work-life" program instead of a "work-family" one to include all employees, with or without family obligations.

All organizations should plan and evaluate the cultural change for implementation of family-friendly programs. There is no unique solution to achieving a family-friendly environment in a corporation. Nevertheless, changes are possible, and the specific design of a program would depend on the company's business model, size, geographic location, industry type, and the workforce needs. Experts recommend employers to calculate the inputs and projected outcomes of work-family arrangements in the short and long terms. In terms of inputs, the organization may have to spend money to set up home offices, part-time contracts, train supervisors in management by objectives, etc. These inputs should be weighed against the reduced cost of absenteeism and turnovers, workforce improvement, etc.

Some Family-Friendly Policies/Arrangements

Corporations may select from the different types of family-friendly policies that would most benefit the organization and the employees. There is not one widely accepted classification of family-friendly policies. Family-friendly arrangements can be grouped into five categories: (1) flexible work arrangements, (2) care provisions, (3) leave arrangements, (4) social benefits/salary perks, and (5) supportive arrangements.

The first group, flexible work arrangements, gives employees flexibility to adapt their work according to their needs. There is a general distinction between arrangements that create flexibility in time and flexibility in space.

The flexible working hours policy is the most popular measure and also the one that involves the least cost. Employees have a flexible work schedule where they can start and end work within a certain margin and are required to work a standard number of hours per day depending on each country's legislation. Another type of flexible arrangement is the part-time work where employees work fewer hours than the standard number of working hours. The job sharing policy allows two workers to share the same job and responsibilities of one full-time job.

On the other hand, flexibility in space refers to the workplace—it is also known as telework. It provides employees the choice of working at home or at the office. Employees have greater control over their timetable and workspace. To consider an employee with a flexible work arrangement in space, he or she must work at least some part of the week at home and not just occasionally or during business trips. It is also important to mention that some people adapt better than others to this type of arrangement. For certain individuals, a lack of physical barriers between work and family creates a higher level of stress and conflict.

The second policy group is the care provisions. Companies provide child and/or elder care referral to employees. Some organizations also offer on- or near-site child care centers. They can be owned by the firm or a third party. A less expensive option is to reimburse employees for child care expenses or negotiate discounts at care centers close to the organization. Other arrangements in this group include after-school care, summer programs or activities, and sick/emergency child care.

A third group of family-friendly policies is leave arrangements. In most countries, leave arrangements are regulated by legislation. They include maternity, paternity, and parental leaves that allow employees to take time off from work to care for an infant or a sick child or elderly member of the family.

The next group of arrangements is the social benefits and salary perks. They include health insurance for the employees and family members, life insurance, and retirement plans. Other forms are bonuses for childbirth, as well as gifts from the company and family trips as incentives for achieving objectives.

The last group, supportive arrangements, consists of the organization's support toward family-friendly policies and can include a work-family coordination unit, a work-family handbook, and an intranet Web page with the firm's family-friendly initiatives. Supportive arrangements also include training seminars on time and stress management as well as family seminars with a range of topics related to parenting, child development, and elderly care.

Some organizations may also include professional support: advice to expatriates seeking relocation services, legal and financial advice, psychological and career support. In all cases, the family situation is taken into account.

Several researchers have shown that formal work-family policies alone are not enough; to have a family-friendly workplace, employers need to create a supportive culture. This support is often needed in a more informal than formal way. Managers here are key players. Their attitude, example, and support are essential because they decide and implement policies on a daily basis. If managers, for example, do not follow the new culture and do not use any support policies, employees will not feel comfortable asking for a flexible timetable or leaving work on time.

One of the barriers to family-friendly programs is based on the assumption that there is a direct connection between presence and contribution at work. Consequently, employees might feel that if they use some family-friendly arrangements their careers can be put in danger as a result.

The success of a family-friendly program depends on a joint effort: Together with the corporate initiatives and the managers' support, the explicit will and commitment of the employees play an important role, but the achievement of a work and family life balance depends on each person.

—Nuria Chinchilla and Elizabeth Torres

See also Work-Life Balance

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Federal Communications Commission (FCC)

The Federal Communications Commission (FCC) is an agency of the U.S. government. Independent of the Executive Branch, it reports directly to the U.S. Congress. It was established by Congress in the Communications Act of 1934. Its purpose is to ensure that the nation's various communications systems work together and services and prices are in the best interest of the consumer, and it has the specific authority to regulate the broadcast of obscene, indecent, or profane language. Recent controversies include the "wardrobe malfunction," which enabled viewers of Super Bowl XXXVII to view pop singer Janet Jackson's breast for 19/32 of a second, about which the FCC received more than half a million complaints, causing it to move to a zero-tolerance response; and the $2.5 million in fines levied against radio shock-jock Howard Stern, prompting his move to satellite radio, which in 2005 remained unregulated.

The FCC is directed by five commissioners who are appointed by the president, with the advice and consent of the Senate. The President selects one of the commissioners to serve as chairperson. Commissioners serve five-year terms, except if they were appointed to fill an unexpired term. Only three commissioners can be of the same political party at any given time, and no commissioner can have a financial interest in any commission-related business.

The FCC's major charge is to regulate interstate and international communications by radio, television, wire, satellite, and cable. Present concerns include the deployment of broadband services, spectrum allocation through a fair and open competitive bidding process, media ownership, and strengthening the national communications infrastructure. The FCC has the authority to enforce provisions in the Communications Act. The FCC oversees compliance with international agreements about satellites and international telecommunications facilities and services.

In the technical arena, FCC policies influence the future directions of technology, such as high-definition television. All televisions sold in the United States since January 1, 2000, are equipped with a V-chip. The V-chip reads information encoded in programs, and it blocks programs from the set based on the rating selected by the parent. Since 1997, all television programming is labeled with a content rating. The original ratings system was voluntarily proposed by the industry. News and sports programming are exempt from these guidelines.

In the social arena, FCC regulations prohibit licensees from broadcasting obscene material at all times and from broadcasting indecent material during the safe harbor period between 6:00 a.m. and 10:00 p.m. Cable and satellite broadcasters are not subject to the indecency regulations because they are subscription services and because they allow subscribers to filter out channels showing indecent content.

An interesting ethical dilemma involves striking a balance between the government's concern for public interest and freedom of speech. Critics say the FCC's indecency standard for censoring expression on radio and broadcast television is vague and subjective. The recent imposition of fines threatens the free flow of ideas and hinders free speech. Other issues include the digital divide and the question of the coverage bias that might arise due to media consolidation and conglomeration.

—Donna Schaeffer

See also Adelphia Communications; Communications Decency Act; Internet and Computing Legislation; Telecommunications Act of 1996

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Federal Deposit Insurance Corporation (FDIC)

The Federal Deposit Insurance Corporation (FDIC) is an independent agency of the federal government. It was created by the Banking Act of 1933 to restore the public's confidence in banks after the numerous bank failures of the 1920s and early 1930s. The FDIC's mission is to maintain stability and the public's confidence in the nation's financial system. The FDIC has three main responsibilities: (1) to insure deposits, (2) to examine and supervise financial institutions, and (3) to manage receiverships for failed banks.

Virtually all the deposits in every bank and thrift in the United States are insured by the FDIC. If an insured banking institution fails, it is the FDIC's responsibility to ensure that customers have access to their insured deposits. Savings, checking, certificate of deposit, money market, IRA, and Keogh accounts are insured up to $100,000 per depositor. Since January 1, 1934, when the FDIC started insuring banks, no depositors have lost insured funds due to a bank failure.

The FDIC is funded through premiums that banks and thrift institutions pay for deposit insurance coverage and from earnings on investments in U.S. Treasury securities. The FDIC only insures the type of accounts listed in the foregoing and does not insure other types of financial investments such as securities, mutual funds, or other investments that banks and thrift institutions may offer.

There are approximately 9,200 banks in the United States today. Banks can be either state or nationally chartered. The FDIC has primary responsibility for examining and supervising all the FDIC-insured, state-chartered banks. It also serves as the backup supervisor of the banks that are members of the Federal Reserve System. As primary regulator, the FDIC conducts periodic examinations of the state-chartered banks to assess their overall financial condition, management policies and practices, and compliance with laws. The FDIC has authority to approve or deny applications by prospective banks for participation in federal deposit insurance. The receivership management program of the FDIC works proactively to identify troubled insured depository institutions before they fail and works with the institutions after failure to ensure that depositors and creditors are paid.

The FDIC is headquartered in Washington, D.C., and conducts business through six regional offices (Atlanta, Chicago, Dallas, Kansas City, New York, and San Francisco) and field offices around the country. It employs approximately 5,200 people. The FDIC is managed by a five-person board of directors who are appointed by the President and confirmed by the Senate.

While the FDIC has grown and modified operations in response to changing environmental and economic conditions (in particular the consolidation in the banking industry, in which the concentration of industry assets, deposits, and revenues with the top 10 organizations is more than 40% from 18% in the 1980s), the mission of the FDIC has remained unchanged.

—Patrice Luoma

See also Bankers' Trust; Barings Bank; Community Reinvestment Act of 1977 (CRA); Federal Reserve System; Individual Retirement Accounts (IRAs); Regulation and Regulatory Agencies; Savings and Loan Scandal

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FEDERAL ENERGY REGULATION

The U.S. federal government plays a pervasive role in the supply, delivery, and use of energy resources. Defining regulation as a set of governmental programs or activities intended to yield results that otherwise would not have occurred, as of 2002, other than military and national security operations, federal government energy regulation extended through 150 energy-related programs and 11 energy-related tax preferences. These programs and activities address a variety of energy concerns, including supply, environment and health effects, low-income assistance, basic research, delivery infrastructure, conservation, system reliability and physical security, market competition, and education. There are at least 18 major federal departments and agencies that have substantial energy-related responsibilities, including the Department of Energy (DOE), the Interior Department, the Department of Health and Human Services, the Nuclear Regulatory Commission, and the Federal Energy Regulatory Commission. In 2003, the federal government spent, directly or by tax preferences, $14.2 billion on energy programs and collected $44.7 billion in energy-related fees, taxes, royalties, and other program revenue.

Federal government energy regulation mechanisms include a variety of constraints, inducements, and development and support efforts. Examples of constraints are limits placed on energy prices, environmental pollution, and energy use efficiency. Examples of inducements include tax incentives and favorable access to federal lands for energy production. Development efforts range from supporting basic energy research to funding demonstration projects. Support activities include low-income energy use assistance and energy production subsidies. Energy policy has been used to pursue a variety of objectives including geopolitical standing, income distribution, and the promotion of ideologies.

Federal control of energy prices is most evident in the electricity and natural gas industries. The Federal Energy Regulatory Commission (FERC), the successor in name of the Federal Power Commission (FPC), has regulatory authority over electric and natural gas wholesale and transmission prices. The FPC was established in 1920 to license hydroelectric generation facilities on navigable streams and waterways. The FPC's authority was extended by the Federal Power Act (1935) and the Natural Gas Act (1938) to include the regulation of various electricity and natural gas prices. The FERC has regulatory authority over the construction of natural gas and petroleum pipelines though, at least historically, not over the construction of electric power transmission lines. In recent years the FERC has shifted its regulatory focus from cost-based regulation to the promotion of competition.

The FPC originally interpreted its price regulation authority under the Natural Gas Act to be limited to the control of interstate pipeline company wholesale prices. In 1954, the United States Supreme Court ruled in *Phillips v. Wisconsin,* 347 U.S. 672 (1954), that the FPC was required to regulate the prices that pipelines pay producers for the purchase of natural gas, effectively regulating natural gas wellhead prices. The FERC's regulation of production prices was phased out by the Natural Gas Policy Act (1978) and the Natural Gas Wellhead Decontrol Act (1989).

Prior to the 1990s, natural gas pipeline companies were merchant intermediaries. Pipeline companies purchased natural gas from producers and sold it to local distribution companies and various industrial customers. Local distribution companies and end-use consumers were effectively precluded from purchasing natural gas supplies directly from producers because they could not obtain transmission service from pipeline companies. Starting with FERC Order 436 (1985) and extending through FERC Order 636 (1992), FERC opened consumer access to the producer supply market by requiring natural gas pipelines to provide transmission service for natural gas purchased by local distribution companies and end use consumers from producers or brokers. Subsequently, interstate pipeline companies have transformed from wholesale supply merchants into the equivalent of transportation common carriers. In the past few years, most of the FERC's natural gas utility regulatory efforts have focused on pipeline transportation rates and service.

Historically, the FERC's electric power regulation focused on setting wholesale and transmission rates on a case-by-case, cost-of-service basis. Following the Public Utility Regulatory Policy Act (PURPA, 1978), however, non–public utility wholesale power supplies have accounted for a growing and substantial portion of bulk power sales. Prior to PURPA, virtually all electricity bulk power sales were made by regulated electric utilities subject to FERC price control. Following PURPA, a substantial portion of the wholesale market supply shifted to electricity suppliers whose prices are not regulated by the FERC. The nonregulated suppliers include independent producers and corporate affiliates of regulated electric utility companies. In the past few years, electric companies have increasingly transferred the ownership of their generation facilities from regulated utility companies to nonregulated corporate affiliates.

Though the FPC generally opposed competition, in the 1990s FERC moved toward supporting the development and expansion of competitive wholesale power markets. With Order 888 (1997), FERC opened access to the electric power transmission grid; open access is essential for the development of a competitive electric bulk power supply market. Over the past few years, FERC has sought to further wholesale competition by promoting regional transmission organizations and specifying market conditions under which negotiated prices could be held as just and reasonable. The purpose of the regional transmission organizations is to operate regional transmission grids and to establish and oversee market mechanisms for wholesale power sales. Though the FERC continues to have price control authority, it is moving in the direction of granting blanket approval for wholesale market prices when it appears that individual power producers lack appreciable market power.

Following the Arab oil embargo and subsequent substantial world market price increases in the early 1970s, the U.S. Congress imposed price controls on domestic oil. Concerned with the massive income redistribution that would occur if domestic oil supply prices rose to world market levels, Congress passed the Emergency Petroleum Allocation Act (1973), which established a two-price system for domestic oil. The price for pre-1972 production sources was limited to 1972 price levels, but the price for post-1972 supply sources was not regulated. Congress repealed oil price controls in 1981. Following the repeal of price controls, however, many oil companies were found to have perpetrated massive price control violations by selling pre-1972 oil resources at world market prices. The companies were fined several hundreds of millions of dollars, much of which went to support state-level energy programs.

Federal energy regulation has played a substantial role in the development of the nuclear power industry. The Atomic Energy Commission (AEC) was established in 1946 to both foster and control the development of peacetime uses of the atom. In 1975 Congress split the AEC into two separate organizations. The AEC's development activities were transferred to the newly created Energy Research Development Administration (ERDA), which was subsequently subsumed into the DOE. The AEC's control activities were transferred to the newly created Nuclear Regulatory Commission (NRC). The NRC is responsible for assuring the protection of public health, safety, and the quality of the environment from the adverse consequences of radiation associated with the commercial use and disposal of nuclear materials. The NRC controls the construction, operation, and decommissioning of commercial reactors, including those used for electric power production. Separate licenses are required for the construction and operation of nuclear power plants. The NRC oversees power plant operation operations on an ongoing basis. Should operation or facility integrity problems arise, the NRC can close a plant until all deficiencies have been rectified.

Federal energy regulation promoting nuclear power has taken many forms. Nuclear power research is substantially supported by the federal government, in particular by the DOE. The federal government has taken the lead in the development of uranium mining, milling, and fuel-rod fabrication. The federal government also bears substantial responsibility for nuclear waste disposal, including the development of a facility that can hold and protect high-level radioactive waste for thousands of years.

The development of the nuclear power industry was hampered by the limited availability of liability insurance. Nuclear power producers found it very difficult to obtain private insurance coverage. To address the problem, Congress passed the Price-Anderson Act (1975) to indemnify power producers against substantial liability for nuclear accidents. The Price-Anderson Act as amended and extended currently limits the industry's private insurance requirements to $200 million per nuclear generator. All nuclear power plant accident damages beyond $200 million are to be paid from a public fund that is limited to $9.5 billion for the entire industry.

The Department of Energy has substantial energy program and oversight responsibilities. The DOE was created in 1977 as a cabinet-level department that brought together oversight responsibilities for energy programs, nuclear weapons and waste cleanup, and various science and technology programs. The DOE's energy program areas include those associated with energy efficiency, fossil fuels, nuclear energy, renewable energy, nonmilitary radioactive waste management, and the collection and dissemination energy information. The DOE establishes minimum energy efficiency standards for numerous residential and commercial appliances and types of equipment such as air conditioners, clothes dryers, clothes washers, cooking equipment, dehumidifiers, dishwashers, furnaces and boilers, pool heaters, refrigerators, freezers, water heaters, and motors. The DOE requires energy efficiency and likely operating cost labeling for many appliances to facilitate appliance purchase decisions. The DOE has provided energy subsidy, and research and development support for various energy supply technologies. However, a variety of efforts have been far from successful; for example, the DOE provided several hundreds of millions of dollars of subsidies for the development of oil production from shale with little result.

The federal government has regulated motor vehicle fuel efficiency since the mid-1970s. In response to the 1973 Arab oil embargo, Congress mandated minimum fuel efficiency standards for automobiles and light trucks. The Corporate Average Fuel Economy (CAFE) standards establish minimum miles per gallon requirements for automobiles and trucks. Compliance is assessed on the basis of the weighted average fuel economy of a manufacturer's fleet of passenger cars or light trucks sales. The standards are established, amended, and administered by the National Highway Traffic Safety Administration of the Department of Transportation. The Environmental Protection Agency (EPA) tests and verifies vehicle fuel efficiency levels.

Early in the development of the domestic petroleum industry, production practices led to substantial wastes of natural gas and oil supplies. To conserve resources and avoid loss of reservoir production capability, the government limited natural gas flaring, unitized fields, required coordinated production, established reservoir-specific maximum efficient rates of production (MERs) and maximum allowable of production rates (MPRs). MERs are established so as to maintain reservoir integrity; MPRs are generally set at or below MERs. Originally administered by producer states, MPRs were used to maintain oil prices by limiting domestic oil production. Currently the responsibility for overseeing constraints on flaring, MERs, and MPRs is vested in the Department of the Interior.

A substantial portion of the oil and natural gas domestic production comes from onshore and offshore government lands. The Department of the Interior establishes royalty rates and leases federal lands for oil and natural gas production. In recent years the federal government expedited the rate of leasing and reduced royalty payments to promote increased domestic oil and natural gas production. A continuing debate centers on whether the United States Arctic National Wildlife Refuge lands should be opened for oil and natural gas exploration and production.

The EPA has a major impact on energy production and use. The National Environmental Policy Act (NEPA, 1969) was passed to promote harmony between humans and the environment, reduce harm to the biosphere, and enrich understandings of ecological systems. Much of the NEPA responsibility was passed to the subsequently established EPA. The EPA was established as an independent agency pursuant to a governmental reorganization plan submitted by President Richard Nixon to Congress in 1970. A variety of responsibilities were transferred to the EPA from other departments and agencies such as the Department of the Interior; the Department of Agriculture; the Department of Health, Education, and Welfare; the Council on Environmental Quality; the Atomic Energy Commission; and the Federal Radiation Council. Major regulatory responsibilities for the EPA are set forth in the Clean Air Act and its amendments (1970, 1977, 1990); the Federal Water Pollution Control Act Amendments (1972); and the Clean Water Act (1977) together with its various amendments. The EPA regulates vehicle emissions and gasoline additives; these regulations substantially affect vehicle production and oil refinery operations. EPA regulation of sulfur and nitrogen oxides, particulate matter, carbon monoxide, mercury, and other emissions has significantly affected generation technologies and the choice energy sources for electric power production.

The EPA traditionally used "command and control" methods to regulate pollution levels, specifying site-specific emission levels and requiring the use of the best available control technologies. More recently, EPA has adopted cap-and-trade methods to control overall pollution levels and improve economic efficiency in pollution reduction. With cap and trade, producers can trade "pollution permits" limited in amount to assure attainment of overall pollution constraints.

A variety of provisions in the federal tax code affect energy production and use. From the early 1900s, the federal tax code permitted the deduction of intangible drilling and dry hole costs and percentage depletion allowances for the stated purpose of increasing domestic oil and natural gas reserves and production. In the 1970s, oil and natural gas industry tax preferences were substantially reduced, new excise taxes were imposed on oil to capture windfall profits, and numerous tax preferences were established to encourage energy conservation and alternative fuels development and commercialization. During President Ronald Reagan's administration, oil windfall profit taxes were repealed and most energy tax preferences were phased out. During the presidential administrations of George H.W. Bush and William Jefferson Clinton, many tax preferences were again established to promote energy conservation and efficiency and the production of alternative fuels. Production incentives for fossil fuels were again adopted during the presidential administration of George W. Bush.

Though federal energy regulations extend back for more than a century, the federal government did not develop comprehensive energy policies until after the 1973 Arab oil embargo, when President Richard Nixon established Project Independence to end reliance on foreign oil by the 1980s. Every president since then has developed an energy plan that often led to comprehensive energy legislation. Energy independence has been a recurrent theme of federal energy policy. However, federal energy policies have not been effective in achieving the desired results. From 1975 to 2004, U.S. oil consumption increased from 16 million barrels per day to 20 million barrels per day. In 1975, oil imports accounted for one third of daily oil supply. By 2004, oil imports accounted for two thirds of daily oil supply.

—Rodney Stevenson

See also Acid Rain; Corporate Average Fuel Economy (CAFE) Standards; Environmental Protection Agency (EPA); Environmental Protection Legislation and Regulation; Greenhouse Effect; Market Failure; Natural Resources; Nuclear Power; Nuclear Regulatory Commission; Organization of Petroleum Exporting Countries (OPEC); Public Utilities and Their Regulation; Rural Electrification Administration

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Federal Reserve System

The purpose of the Federal Reserve System (The Fed) is to ensure stability in the banking system and to keep short-run political pressures out of monetary policy. The Federal Reserve System was created by the U.S. Congress and signed into law by President Woodrow Wilson on December 23, 1913, following a series of bank panics years earlier. In subsequent statutes, Congress refined The Fed's purpose to include enabling economic growth consistent with the U.S. economy's potential, a high level of national employment, stability in the purchasing power of the U.S. dollar, and moderate long-term interest rates.

The Federal Reserve System is composed of a seven-member board of governors and 12 regional Federal Reserve Banks with their 25 branches, which share the responsibilities mandated of the system. The Federal Reserve System is an independent entity within the government that is self-funded through its various operations. It is structured to have both public purposes and private aspects. The Federal Reserve System and its components are subject to several levels of review and audit, and its ultimate accountability is to the U.S. Congress, which can alter the responsibilities of the System by statute.

The seven presidential appointees to the board of governors are required to be representative of "the financial, agricultural, industrial and commercial interests and geographical divisions of the country." The members of the board of governors are appointed for 14-year terms with staggered appointments. A staff of about 1,700 in Washington, D.C., supports the board of governors.

Each of the 12 regional Federal Reserve Banks is designated a distinct letter and a number as an identifier. The regional Federal Reserve Banks supervise and regulate certain financial institutions and activities, they provide banking services to depository institutions and the federal government, and they ensure consumers receive adequate information and fair treatment in their transactions with the banking system.

A major component of the Federal Reserve System is the Federal Open Market Committee (FOMC). The FOMC oversees open market operations to influence money market conditions and the growth of the money supply and credit. The FOMC is a voting committee composed of the board of governors of the Federal Reserve, the president of the Federal Reserve Bank of New York, and presidents of four other Federal Reserve Banks who serve on the committee on a rotating basis. The rotating seats are filled from four groupings of the regional Federal Reserve banks. All the Federal Reserve Bank presidents attend the FOMC meetings and participate in the discussions. The FOMC normally meets for one day (the January-February and June-July meetings are two-day meetings) eight times each year in Washington, D.C., to discuss policy options related to the financial markets, the foreign exchange markets, and the trading desk activities of the New York Federal Reserve Bank. The FOMC deliberates monetary policy options at its meetings and then issues directives to the New York Fed's domestic trading desk on whether to tighten, maintain, or ease existing policy through the buying or selling of U.S. government securities. In addition to the open market operations, the Federal Reserve System conducts monetary policy through reserve requirements for depository institutions and through the discount rate paid by depository institutions when they borrow reserves from a regional Federal Reserve Bank.

Actions by the Federal Reserve have significant political and practical implications. The Fed has the ability to stimulate or restrain financial markets and broad economic activity by tightening or loosening the financial system with funds, by lowering or raising margin requirements, and by administratively changing other regulatory requirements. The Fed, through its FOMC actions on interest rates, has the ability to influence political activity regarding budget deficits, cumulative national debt, and tax policy. Changes in interest rates affect the rate of inflation, unemployment, and the flows of foreign investment. Changes in interest rates affect individual borrowing for homes, automobiles, durable goods, and credit card purchases. Changes in interest rates affect business expenditures and capital spending for plants, property, and equipment.

—Frank L. Winfrey

See also Gross Domestic Product (GDP); Gross National Product (GNP); Inflation

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Federal Sentencing Guidelines

In what was to have a profound effect on corporate America, unique legal standards were enacted in the United States in November 1991. The standards, referred to as the U.S. Federal Sentencing Guidelines for Organizations ("Guidelines"), used a carrot and stick approach to create incentives for thousands of corporations to report wrongdoing, to cooperate with authorities while accepting responsibility for misconduct, and to establish or enhance their compliance or ethics programs. As opposed to discussing the Federal Sentencing Guidelines for individuals convicted of federal crimes, this entry focuses on the Federal

Sentencing Guidelines for Organizations, their impact, their use by the courts, and their effectiveness with respect to improving legal and ethical behavior.

The Guidelines were developed by the United States Sentencing Commission, a governmental body that came into existence in 1984. The Commission was charged with the responsibility of creating uniformity in the sentencing of offenders of federal laws. Following the promulgation of the Guidelines in 1987 for sentencing *individuals* convicted of federal offenses (including crimes such as murder, assault, robbery, and drug trafficking as well as business crimes such as fraud, embezzlement, forgery, bribery, tax evasion, money laundering, racketeering, or extortion), the Commission proceeded to create the Guidelines specifically for *organizations* that went into effect in 1991. The Guidelines consist essentially of a manual for judges to apply when determining the appropriate sentence for organizations convicted of a federal crime. Judges were being required for the first time to consider whether the convicted firm had established an effective compliance and ethics program before the violation taking place—in other words, whether the firm had taken appropriate steps to prevent and detect violations of the law.

According to Win Swensen, the former Deputy General Counsel of the Sentencing Commission, one of the primary reasons for the enactment of the Guidelines was that the U.S. government lacked a clear corporate crime sentencing and enforcement policy. As a result, judges were having great difficulty in finding meaningful ways in which to sentence corporations. Empirical research conducted by the U.S. Sentencing Commission on corporate sentencing practices demonstrated that " . . . corporate sentencing was in disarray . . . nearly identical cases were treated differently." In addition, average fines were found by the Commission to be " . . . less than the cost corporations had to pay to obey the law."

To address these concerns, the Commission eventually came to accept the carrot and stick approach to corporate sentencing. This approach was based on three principal and related objectives: (1) to define a model for good corporate citizenship; (2) to use the model to make corporate sentencing fair by providing objective, defined criteria; and (3) to use the model to create incentives for companies to take crime-controlling actions. The final objective was designed to shift from the previous "speed trap" enforcement policy of the past (i.e., merely lie and wait for corporate offenders and then fine them) to a more interactive approach. By providing financial incentives, the government was inviting companies to undertake effective, crime-controlling actions that in turn would put less pressure on already limited government enforcement resources.

Numerous corporations have been prosecuted under the Guidelines since their enactment, some suffering fines and penalties in the tens and even hundreds of millions of dollars. Empirical evidence (discussed in the following sections) is now suggesting that the implementation of these programs is raising the level of legal and ethical behavior in corporations.

What Are the Guidelines?

According to the Guidelines, any organization is liable to payments of restitution, fines, and periods of probation if convicted for a federal offense connected with offenses such as price-fixing, bid rigging, copyright and trademark infringement, bribery, fraud, money laundering, extortion, embezzlement, conspiracy, and other types of misconduct. The preamble to the Guidelines states that the organization operates only through its agents, usually its managers, and is, therefore, liable for the offenses committed by them. Naturally, the managers are personally responsible and liable for their own behavior. The innovation of the Guidelines lies in the fact that the sentences imposed on the organization and its agents are designed to achieve the following objectives: (1) just punishment; (2) sufficient deterrence; and (3) encouragement of the development of internal mechanisms to prevent, identify, and report on criminal behavior in organizations (i.e., through a carrot and stick approach).

The Guidelines require judges to follow a specific formula in determining fines. The range of potential fines is based on two factors: (1) the seriousness of the federal offense (i.e., the "base fine"); and (2) the culpability of the organization (i.e., the "multiplier"). The base fine is the greater of the company's monetary gain, the victim's monetary loss, or a specified amount depending on the type of offense (ranging anywhere from $5,000 to $72,500,000). Once the base fine is determined, federal judges are required to multiply this amount by a "culpability score." The culpability score can lead to either a substantial increase or decrease of the base fine, depending on which of several factors are in existence. The culpability score will increase when (1) a larger sized organization is involved; (2) high-level employees are involved in the offense or have tolerated the offense; (3) the organization has a prior history of engaging in similar misconduct; (4) the organization has violated a court order; or (5) the organization has obstructed justice relative to the offense. As a result of these factors, a company could find itself facing up to hundreds of millions of dollars in fines (the "stick").

At the same time, the Guidelines provide organizations with an opportunity to take steps that can substantially mitigate the severity of the base fine (up to 95%). The Guidelines provide that the culpability score can be reduced (i.e., the "carrot") if the organization engages in (1) self reporting; (2) cooperation and acceptance of responsibility; and/or (3) establishing, prior to the offense occurring, an "effective compliance and ethics program" to prevent and detect violations of the law. In addition to potential fines, judges are required to place organizations with 50 or more employees on probation when they are deemed not to have an effective compliance program in place.

To assist corporations in knowing exactly what constitutes an appropriate internal detection and prevention mechanism (i.e., an "effective compliance and ethics program"), the Guidelines (which were recently bolstered through the 2004 amendments) list several minimum "due diligence" requirements: (1) standards and procedures to prevent and detect criminal conduct (e.g., a code of conduct or ethics); (2) responsibility at all levels supported by adequate resources and authority for the program (e.g., a compliance or ethics officer); (3) personnel screening related to program goals; (4) effective training at all levels; (5) auditing, monitoring, and evaluating program effectiveness as well as establishing and publicizing a nonretaliatory internal reporting system that allows anonymity or confidentiality (e.g., an employee helpline or hotline); (6) incentives and discipline to promote compliance; and (7) reasonable steps to respond to and prevent further similar offenses on detection of a violation. The Guidelines also indicate that the implementation and successful maintenance of an effective compliance and ethics program requires that organizations periodically assess the risk of criminal conduct. Guidance is also provided by the Guidelines on how small organizations may adapt the requirements to the particular constraints they may face (e.g., fewer resources). In addition, as a significant modification resulting from the 2004 amendments, the Guidelines now require organizations and their high-level personnel (i.e., directors and senior managers) to demonstrate that they have promoted "an organizational culture that encourages ethical conduct and a commitment to compliance with the law."

Impact of the Guidelines on Corporate Compliance and Ethics Programs

Although the Guidelines have been in existence for only over a decade, they have received significant attention from academia and the media. For example, one study found that, by 2001, nearly 500 law review articles and more than 300 newspaper articles had already addressed the Guidelines.

Part of the reason for the significant interest in the Guidelines may be due to the impact they have had on corporate America. For example, many companies have indicated that the Guidelines were one of the factors that influenced the enhancement of already existing compliance or ethics programs. According to a 1995 national study of compliance practices, 44% of the respondents stated that the Guidelines caused them to add vigor to their compliance programs, while 20% added compliance programs because of their awareness of the Guidelines. According to Andrew Apel, the author of the study, ". . . certainly, the guidelines are having a significant impact on what organizations are doing to prevent and detect violations of law." A 1997 survey by the Ethics Officer Association found that 47% of those firms responding indicated that the guidelines had ". . . a lot of influence on the organization's decision to adopt a compliance program."

Unfortunately, the studies do not break down the impact of the Guidelines on individual components of ethics programs. Despite this gap, one can assume that the Guidelines have had the greatest impact on four components: (1) ethics training; (2) ethics officers; (3) ethics offices; and (4) ethics hotlines. Each of these components can be related to one of the elements of an effective compliance program as stipulated by the Guidelines (corporate codes of conduct were already prevalent in most large companies by 1991). For example, the Ethics Officer Association was formed in 1992 shortly after the sentencing guidelines came into effect, with only 12 members. The membership has grown to more than 1,000 members, representing more than half of the Fortune 100 companies, doing business in more than 160 countries. Another organization, the Health Care Compliance Association (HCCA), was also established essentially as a result of the Guidelines. Its membership has grown to more than 3,000 members.

Use of the Guidelines

The Guidelines appear to have clearly had an impact on the establishment or enhancement of corporate compliance or ethics programs. One of the reasons for this achievement is that in the case of an offense, the size of the fine is conditional on the existence of a compliance or ethics program. But have U.S. courts actually used the Guidelines in sentencing corporations?

More than 2,000 organizations have been sentenced based on the Guidelines since they came into effect in 1991. According to the 2003 U.S. Sentencing Commission's Annual Report, 200 organizations were sentenced according to the Guidelines during 2003, with 134 organizations subject to the Guideline's fine provisions. Although this represented a decline in sentencing from 2002 (252 organizations were sentenced) and 2001 (238 organizations), the number of organizations sentenced steadily increased in almost every other year (2000 [304 organizations]; 1999 [255 organizations]; 1998 [218 organizations]; 1997 [220 organizations]; 1996 [157 organizations]; 1995 [111 organizations]; 1994 [86 organizations]). The major types of offenses in 2003 included the following: fraud (32%); environmental pollution (20%); food, drugs, agricultural, and consumer (7%); antitrust (7%); and money laundering (7%).

The Guidelines have had an even more significant impact on probation. Approximately 65% of companies sentenced from 1994 to 2003 were placed on probation, with approximately 12% to 20% of these being ordered to implement compliance programs. The Guidelines were to have less of an impact, however, on the courts' consideration of corporate compliance programs when assessing fines. Since 1994, only a handful of the prosecutions involved a direct consideration of the defendant's compliance program by the court. In 2003, none of the organizations received a reduced fine for having in place an "effective compliance program" to prevent and detect violations of the law, although one firm was recognized in 1999 for having such a program in place. Only two organizations in 2001 were found to have made an effort in the way of *compliance* or *ethics.* In 2003, 24 out of the 200 organizations that were sentenced (12%) were ordered to make some sort of *ethics*-related or *compliance*-related improvement.

Since the adoption of the Guidelines in 1991, we have already seen a number of examples of significant fines faced by firms that failed to implement effective compliance programs. For instance, in 1996, a Manhattan federal court sentenced Daiwa Bank to pay a fine of $340 million under the Guidelines. The case involved a bank employee who lost $1.1 billion in unauthorized trades. Two reasons for the fine were the bank's "lack of a meaningful compliance program" and its "consequent failure to report the employee's wrongdoing." In May 1998, in what was the largest criminal fine in U.S. history, Hoffman-LaRoche, a large Swiss pharmaceutical company, was fined $500 million under the Guidelines after being convicted of an antitrust conspiracy. The company, along with two other firms, attempted to control the prices and sales volume of a series of vitamins. In October 2001, TAP Pharmaceuticals was subject to a $290 million criminal fine for violating the Prescriptions Drug Marketing Act—the largest fine in any health care case under the Guidelines. The company engaged in a kickback scheme with doctors in marketing its cancer drug. All these cases appear to suggest that effective compliance programs are still not in place in many corporations.

Another development that has been noted due to the Guidelines is being referred to as the shadow effect. Essentially, the Guidelines are also being considered by courts and government agencies in criminal cases other than those brought under the Guidelines. For example, in the 1996 Delaware Chancery Court case *In Re Caremark International Inc.,* the judge essentially relied on the Guidelines in warning that directors themselves can be held personally liable if they have failed to institute an adequate compliance program to prevent illegal acts by employees. Other cases, such as *Dellastatious v. Williams* of 2001 and *McCall v. Scott* of 2001 have followed *Caremark* in requiring corporate directors to ensure that their companies have an effective compliance program in place, which has now been essentially legislated for public companies under the U.S. Sarbanes-Oxley Act of 2002.

In terms of government agencies, the Environmental Protection Agency (EPA) and the U.S. Department of Health and Human Services (HHS) have both issued standards for companies based on the Guidelines' compliance criteria. The EPA issued a policy providing in some circumstances for reduced civil penalties and no criminal sanctions for corporations with effective environmental compliance programs. The Department of HHS has set forth specific criteria for compliance programs as well as incentives for developing such programs.

The Guidelines also appear to be influencing the initial decision by government regulators on whether to prosecute companies. A 1999 memorandum from the U.S. Department of Justice includes a list of factors to consider in terms of prosecution, including the existence and adequacy of the corporation's compliance program and whether the corporation's remedial actions included any efforts to implement an effective corporate compliance program or to improve an existing one.

Effectiveness of the Guidelines

It can be seen from the above discussion that the Guidelines have had an impact on the creation and implementation of compliance or ethics programs and have actually been used by the courts (and by some U.S. government agencies as well) in assessing fines, in placing companies on probation, and even in deciding whether to prosecute. Despite this impact, one could ask a more fundamental question: Have the Guidelines helped to achieve their ultimate purpose, the reduction of corporate crime and an improvement in ethical behavior?

Unfortunately, there are no empirical data that measure organizational crime rates over time. As a result, as indicated by John Steer, the vice-chair of the U.S. Sentencing Commission, it is not possible to assess directly the success, or lack thereof, of the organizational guidelines in altering the rates at which organizations commit crimes. Thus, it may be some time before we can know the answer to this question with any degree of certainty. There is, however, a certain amount of indirect empirical information. Several studies released by the U.S.-based Ethics Resource Center (i.e., "Ethics in American Business: Policies, Programs and Perceptions" of 1994 and the "National Business Ethics Survey" of 2000 and 2003) found that comprehensive compliance or ethics programs (including codes, training, ethics offices, and reporting systems) appear to lead to several positive outcomes including a greater likelihood of misconduct being reported, higher perceptions that employees are held accountable for ethics violations, and lower pressure to compromise ethical standards. A 2003 study by the World Bank on the effectiveness of compliance programs in reducing corruption found that the 22 companies interviewed say they have no doubt that their ethics programs are succeeding in reducing the incidence of corruption.

In any event, the bulk of the evidence to date indicates that the Guidelines have had an influence on the development of compliance and ethics programs that appear to lead to improved ethical behavior in organizations. According to John Steer, "The past decade's experience with the organizational sentencing guidelines has provided positive evidence supporting the efficacy of this bold, novel means of influencing desirable organizational behavior." According to Judge Diana Murphy, former chair of the U.S. Sentencing Commission, "[The Guidelines] are a real success story for the United States Sentencing Commission in its work to deter crime and encourage compliance with the law." The Sentencing Commission, in reflecting on its first 10 years, states that " . . . the guidelines have had a tremendous impact on the implementation of compliance and business ethics programs over the past 10 years."

Future for the Guidelines?

More recently, the long-term future of the Guidelines may have been put into jeopardy. In a pair of 5-4 decisions issued in January 2005, the U.S. Supreme Court held that the Guidelines violate a defendant's Sixth Amendment right to be tried by a jury to the extent that they allow judges to engage in fact finding that can lead to a harsher sentence. As a result, the Court ruled that judges cannot increase sentences beyond the maximum that the jury's findings alone would support. The Court also held that the Guidelines should serve only as "advisory" rules as opposed to "mandatory" rules for judges. While some question whether this decision will lead to the downfall of the Guidelines, other commentators suggest that the Court's decisions should not affect organizations that are being sentenced (as opposed to individuals) as organizations do not appear to possess a constitutional right to be tried by a jury.

—Mark S. Schwartz

See also Codes of Conduct, Ethical and Professional; Corporate Ethics and Compliance Programs; Corporate Governance; Ethics Training Programs

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Federal Trade Commission (FTC)

The Federal Trade Commission (FTC) is an independent agency of the U.S. government that regulates markets and competition. Founded in 1915, the FTC is a successor to the Bureau of Corporations of the Department of Commerce, which was founded in 1903, making it one of the oldest regulatory agencies in the United States. The agency is known to consumers and businesspeople for its many functions, including consumer protection, product safety, enforcement of warranties, prohibition of price-fixing, and maintenance of competitive markets through review of mergers and restrictions on anticompetitive activities.

History

As the United States transitioned from an agricultural nation to an industrial power during the 19th century, many citizens and legislators became concerned about the concentration of economic power in the hands of only a few large corporations. The Sherman Antitrust Act was passed in 1890 in an effort to stem the tide of corporate consolidations. The objective was to protect competition and thereby benefit consumers by providing better products and services at competitive prices. However, United States Supreme Court rulings during this laissez-faire economic period, based on the belief that unrestricted competition would produce the best results for society, exempted mergers from the Sherman Act's coverage.

Following an unprecedented wave of merger activity from 1898 to 1902, the Bureau of Corporations was formed by President Theodore Roosevelt. The self-described trust-buster established the Bureau due to his concern about business combinations that reduced competition and in an effort to revitalize the Sherman Antitrust Act. The Bureau conducted investigations and published reports on interstate corporations. Such investigations were also in response to a growing consumerism movement early in the 20th century. This movement was aided by the publication in 1906 of *The Jungle* by Upton Sinclair. The resulting public outrage at the unsafe and unsanitary conditions in the Chicago meatpacking industry helped to give added momentum to the movement. Sinclair partially blamed the conditions he observed on the consolidation of businesses in the meatpacking industry, also known as the beef trust.

The 1912 presidential election featured a national debate on the necessity for controlling big business and business concentration. Democrat Woodrow Wilson was elected president by defeating William Howard Taft, the Republican challenger, and Theodore Roosevelt, then a third-party challenger. In 1914, Wilson signed into law the Federal Trade Commission Act, which created the FTC. Section 5 of the act prohibited unfair methods of competition. A short time later, the Clayton Act was signed into law, which strengthened and defined the limitations on business combinations.

The FTC assumed the role of the Bureau of Corporations, and its first chairperson was the former commissioner of the Bureau. Like the Bureau, the FTC could investigate and publish reports. However, unlike the Bureau, it could also bring enforcement actions, including enforcement of the Sherman and Clayton Acts. The FTC also had the informal duty to assist businesses in complying with the law.

The new FTC expanded its role by providing support to the federal government during World War I by establishing prices for goods sold to the government. Throughout the 20th century, the President and Congress expanded the role of the FTC as the leading source of protection for consumers and of protection of competition among businesses.

Due to amendments in 1938 and 1950, the FTC moved past, simply enforcing antitrust and price-discrimination laws on matters involving deception of consumers and unfair competition. It was also armed with the ability to assess civil penalties for violations of its orders. The Hart-Scott-Rodino Antitrust

Improvements Act of 1976 required that certain proposed mergers be filed with the FTC for approval before the mergers could proceed.

In more recent times, observers have commented on the various positions taken by the FTC depending on the political party in power and the general mood of the country regarding business conditions. The debate features arguments by advocates of minimal regulation of business, which would include allowing cooperation among businesses and most mergers, and advocates of a strong governmental regulatory approach that would as a matter of course restrict most mergers and business cooperation. The advocates for loose regulation argue that businesses in the United States are competing in a world market and that viewing businesses solely in the context of local or national competition is a myopic view of market realities. Advocates of strict regulation argue that with the power of major corporations, many with more revenue and assets than some countries in the world, controls are necessary to preserve some balance between the consumers and small businesses and the large, multinational corporations.

Major Functions

The FTC is governed by five commissioners appointed by the President and serving staggered seven-year terms. No more than three commissioners can be of the same political party. Headquartered in Washington, D.C., the FTC is composed of administrative, legislative, investigative, and legal functions. Its activities are supported by seven regional offices. It enforces laws passed by the U.S. Congress and also rules enacted by the FTC through its rule-making authority. The 21st-century FTC divides its focus across three bureaus: the Bureau of Consumer Protection, the Bureau of Competition, and the Bureau of Economics. Each bureau is described in more detail in the following sections.

Bureau of Consumer Protection

The Bureau of Consumer Protection (BCP) is charged with protecting consumers from deceptive or unfair trade practices. The BCP is composed of seven divisions, each with specific responsibilities. The Division of Advertising Practices has responsibility for protecting consumers from false advertising. Included in its broad authority are claims regarding tobacco, alcohol, food, over-the-counter drugs, energy-saving products, and products asserting environmental claims. The Division of Financial Practices enforces many of the laws related to consumer credit matters, including the Fair Debt Collection Practices Act and the Truth in Lending Act. The Division of Marketing Practices protects consumers from marketing schemes and possible scams by regulating franchise sales, telemarketing, and Internet sales.

The Division of Planning and Information develops reports to guide law enforcement and the FTC education efforts. The International Division of Consumer Protection works to increase international cooperation in combating consumer fraud. There is also a Division of Enforcement and an Office of Consumer and Business Education.

Bureau of Competition

The Bureau of Competition (BC) shares responsibility with the U.S. Department of Justice for enforcing antitrust laws. The Bureau works to insure that mergers and other business combinations and practices do not reduce competition in the marketplace. The Bureau concentrates its efforts on industries with the most potential impact on consumers, including energy, prescription drugs and health care, food, and technical products such as computers, cable services, and Internet access.

The BC enforces the following laws: Sections 1 and 2 of the Sherman Antitrust Act, Section 5 of the Federal Trade Commission Act, and Sections 7 and 7A of the Clayton Act. It is Section 7A of the Clayton Act, aided by the Hart-Scott-Rodino Act noted previously, that requires the submission of proposed mergers to the BC for evaluation before a merger can proceed. The main focus is on mergers between direct competitors, horizontal mergers. The BC also reviews mergers between companies in a supplier-buyer relationship, a vertical merger, and between companies where one of the parties might enter the market rather than purchase a potential competitor. The BC review is to determine the possible impact on consumers due to a reduction in competition if the merger is completed. Only a small percentage of mergers are actually disallowed by the BC.

The BC's authority is not limited to disallowing a merger. In some cases, divestiture of assets by one or both parties to a merger can correct the potential anticompetitive effects of the proposed merger. In the case of some oil company mergers, the divestiture of refineries and certain retail facilities allowed the mergers to go forward. In addition, the BC has the responsibility to investigate anticompetitive acts that do not involve merger activities. Other prohibited activity investigated by the BC includes price-fixing, tying product purchases to other products, and dividing markets or customers among competitors.

A more difficult area is the establishment of standards in certain industries. While standards, such as ones for DVDs and other technology-based products, can make life a great deal easier for consumers, they can also provide a windfall and perhaps control of the market for one or more competitors. This is especially true if patents are incorporated in the standards that are adopted.

Bureau of Economics

The Bureau of Economics (BE) provides economic reports on the impact of the FTC's activities and government regulation in general. Armed with the BE's detailed economic studies in cooperation with the BC, the enforcement arm of the FTC can proceed to make prosecution decisions in antitrust and other matters within the purview of the FTC. These studies are also used to direct the enforcement efforts of the BCP. The BE also assists the FTC in advocacy issues related to legal cases and legislation that affects businesses and consumers.

Agency Visibility in Daily Life

The FTC is one of the most visible agencies in the daily life of Americans, although few may realize it. FTC requirements include labels on clothing indicating fabric care and country of origin, energy labels on new appliances, product warranties, Truth in Lending notices, and the National Do Not Call List.

Businesses must be cautious when placing advertisements and marketing products and services to comply with the consumer protection regulations as well as the rules and laws governing antitrust and unfair competition. However, businesses benefit from a more level playing field and from protection from unfair competition by other businesses. Playing by the rules may be more confusing and difficult for small businesses due to the complexity of FTC regulations and the cost of compliance. The Fair Debt Collection Practices Act limits the measures businesses may take to collect debts. In addition, the Fair Credit Reporting Act may interfere with the investigation of the backgrounds of employees at the same time when business liability for hiring employees who cause thefts or injuries is increasing.

Conclusion

While the FTC has had an impact on the lives of most Americans and businesses, the benefits of the agency are still debated. Some consumers believe that when the local gasoline retailers raise their prices almost simultaneously, there must have been illegal collusion. The FTC has rarely found that to be the case as the retailers are allowed to meet competition. Businesses in many situations benefit from the protection of competition implicit in the enforcement of antitrust laws, but FTC enforcement of these laws could also prevent a business from being acquired by a competitor and, in turn, prevent the business from selling for its peak value.

—David D. Schein

See also Antitrust Laws; Consumer Fraud; Consumer Product Safety Commission; Consumer Protection Legislation; Laissez-Faire; Mergers, Acquisitions, and Takeovers

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Feminist Ethics

Feminist ethics is a diverse set of gender-focused approaches to ethical theory and practice. The primary aims of feminist ethics are (1) to examine the traits, virtues, and values that have been culturally tied to women worldwide, but particularly in the Western world; and (2) to determine whether they have been wrongly assessed and underused by much of traditional (Western) ethical thought. According to philosopher Alison M. Jaggar, many schools of traditional (Western) ethics fail women in five interrelated ways. First, they focus far more on men's issues, interests, and rights than on women's. Second, they approach problems that arise in the private or domestic realm as morally uninteresting or trivial. Third, they imply that for a variety of biological as well as social reasons, women are not as morally developed as men. Fourth, they privilege traits linked to masculinity (autonomy, separation, mind, culture, and transcendence) over traits linked to femininity (interdependence, community, connection, body, emotion, nature, and immanence) as if the latter traits were not just as essential for human beings to cultivate as the former. Fifth, they present masculine modes of moral reasoning that emphasize rules, universality, and impartiality as somehow better than feminine modes of moral reasoning that emphasize relationships, particularity, and partiality when, in point of fact, both these modes of moral reasoning are equally capable of yielding wise moral judgments.

Historical Background

Feminist ethics has its roots in 18th- and 19th-century debates about the nature and function of women's morality. Thinkers such as Mary Wollstonecraft, John Stuart Mill, Harriet Taylor Mill, Catherine Beecher, Charlotte Perkins Gilman, and Elizabeth Cady Stanton posed questions such as the following: Are women's feminine traits produced biologically and/or socially? Is there a nonbiased standard available to distinguish "good" feminine traits from "bad" ones? Is women's morality different from men's, and, if it is, why? Is ethics gender neutral or gender specific? Should women and men be held accountable to the same set of moral rules or to different ones?

Because 18th- and 19th-century feminist thinkers had different answers to the questions posed in the foregoing, it is not surprising that 20th-century feminist ethicists should have developed a variety of approaches to ethics. Despite their diversity, however, all feminist approaches to ethics use gender as their primary category of analysis and women's experiences as their primary source of empirical data. They can be divided into two basic types: care-focused feminist ethics and power-focused feminist ethics. Because these two fundamental approaches to feminist ethics stress different concepts, concerns, and controversies, they are able to check and balance as well as complement each other.

Care-Focused Feminist Ethics

Care-focused feminist ethics include a cluster of so-called feminine and maternal approaches to ethics that put a premium on those moral virtues that tend to strengthen people's felt commitments to each other. Whereas feminine approaches to ethics stress the value of human relationships in general, maternal approaches to ethics focus on the value of one type of human relationship in particular, namely the mother-child relationship. The strengths of feminine and maternal approaches to ethics are many, but they are offset by some significant weaknesses as discussed in the following.

Proponents of feminine approaches to ethics characteristically maintain that biological and/or social differences between men and women are the foundation of men's and women's, respectively, different moral identities, behaviors, and styles of moral reasoning. They also emphasize that, at least in the West, traditional moral theories generally ignore, trivialize, or demean virtues of character and traits of personality that are culturally associated with women.

Among the best-known ethicists who have developed a feminine approach to ethics is moral psychologist Carol Gilligan. In her classic, *In a Different Voice,* Gilligan claims that because women have traditionally focused on others' needs, they have developed an ethics of care that stresses the importance of creating and sustaining a strong network of human relationships. In contrast, because men have traditionally focused on competing in the public world, where people are sometimes tempted to advance their careers and causes by unfair means, they have developed a language of justice that emphasizes adherence to agreed-on rules or contracts. Moreover, there is a tendency to regard the language of justice as somehow ethically superior to the language of care because the former is associated with being objective and impartial, while the latter is associated with being subjective and partial. Supposedly, reason rules the ethics of justice, while emotion rules the ethics of care.

Gilligan criticized her university mentor, educational psychologist and moralist Lawrence Kohlberg, for devising a scale of moral development that presented men's morality in more favorable terms than women's. In his work, Kohlberg claimed that moral development is a six-stage process. Stage 1is the punishment and obedience orientation. To avoid the stick of punishment and/or to receive the carrot of a reward, children follow simple commands. Stage 2 is the instrumental relativist orientation. Based on a limited principle of reciprocity—"You scratch my back and I'll scratch yours"—young children meet the needs of someone only if that individual is meeting their needs. Stage 3 is the good boy–nice girl orientation. Adolescents conform to prevailing norms to secure others' approval and love. Stage 4 is the law and order orientation. As they move out of adolescence, young adults begin to do their duty, show respect for authority, and adhere to social standards to secure others' admiration and respect for them as honorable, law-abiding citizens. Stage 5 is the social contract legalistic orientation. Mature adults adopt an essentially utilitarian moral point of view, according to which individuals are permitted to do as they please, provided they refrain from harming other people in the process. Stage 6 is the universal ethical principle orientation. Exceptional adults adopt an essentially Kantian moral perspective that seeks to transcend and judge all conventional moralities. These fully morally developed individuals are ruled not by self-interest, the opinion of others, or the fear of legal punishment but by self-legislated and self-imposed universal principles such as justice, reciprocity, and respect for the dignity of human beings.

The more Gilligan reflected on Kohlberg's scale, the more she realized why speakers of the language of care (typically women) did not do nearly as well on it as speakers of the language of justice (typically men). Kohlberg's scale, alleged Gilligan, was constructed to recognize and validate the voice of justice but not the voice of care. There was little opportunity for people who justified their moral decisions in terms of their concrete personal relationships rather than in terms of adherence to a utilitarian calculus or an abstract set of universal principles to fare well on it. Gilligan's solution to this male-biased outcome was to conduct several empirical studies on women's (later also men's) styles of moral reasoning and propose a gender-neutral moral development scale. As a result of these early studies and subsequent later studies, Gilligan concluded that although many men and women can speak both the languages of justice and care, women tend to favor the vocabulary of care and men the vocabulary of justice. She also concluded that men are far less comfortable speaking the language of care than are women speaking the language of justice. Society views women who speak the language of justice as clear successes but men who speak the language of care as somehow failing.

Nel Noddings, another care-focused feminist ethicist, went further than Gilligan did in her defense of women's morality. Ethics, insists Noddings, is about particular relations. There are two parties in any relation: The first member is the one-caring and the second, the cared-for. The one-caring is motivationally engrossed or otherwise psychologically situated in the cared-for. She or he makes it a point to attend to the cared-for in deeds as well as in thoughts. When all goes well, the cared-for actively receives the caring deeds of the one-caring, spontaneously expressing his or her appreciation for the time, energy, and/or resources the one-caring is expending on him or her. Caring is not simply a matter of feeling favorably disposed toward humankind in general, of being concerned about people with whom we have no concrete connections. Rather, it is about two or more people being engaged in a face-to-face relationship. There is, after all, a fundamental difference between the kind of care a mother has for her child and the kind of care a woman has for an anonymous child to whom her charity of choice will give a measure of material support. Real care, insists Noddings, requires actual encounters with specific individuals; it cannot be accomplished through good intentions alone, let alone anonymously.

Noddings's ethics of care borrows from the moral sentiment theory that frames David Hume's ethics. Like Hume, Noddings believes both that the sentiments of sympathy are *innate* and that these sentiments must be *cultivated* lest they fail to guide one's everyday moral decisions and actions. In explaining the complex relationship between what she terms natural caring on the one hand and ethical caring on the other, Noddings notes that most people's initial experiences of care come easily, even unconsciously. Among the examples of *natural* caring that Noddings provides is that of a little boy who helps his mother fold the laundry because she does so many things for him. He wants to be connected to her and have her recognize him as her helper. Later, when he is a young man and would rather be around his friends than around his mother, he remembers all his mother has done for him throughout the years. Feelings of obligation flood over him. These feelings prompt the young man to forsake fun time with his friends so that he can assist her in what may be her days of greatest need. Through this kind of decision and action rooted in feelings, says Noddings, *ethical* caring comes into existence, a form of caring that is more deliberate and less spontaneous than *natural* caring.

Significantly, Noddings does not describe moral development as the process of replacing natural caring with ethical caring. As she sees it, our oughts build on our wants. Moreover, morality is not about serving others' interests through the process of disserving one's own interests. Rather, morality is about serving one's own and others' interests simultaneously. Supposedly, when we engage in ethical caring, we are not denying, negating, or renouncing ourselves to affirm, posit, or accept others. Rather, we are acting to fulfill our need to be related to other people.

As intuitively appealing as an ethics of care may be, it is in many ways an underdeveloped ethics subject to a variety of misunderstandings. In fact, the concept of care is susceptible to misinterpretation and may become a disempowering trap for women. More often than not, society has viewed women as bearing primary responsibility for the care of the young, the old, and the infirm. It has expected women to be the ones to sacrifice their careers and interests to serve family members' and friends' needs. Continuing to associate women with caring, as Gilligan and Noddings do, might have the effect of reinforcing the idea that because women can care and have cared so well for others, they should always care—regardless of the cost to themselves.

Closely related to feminine approaches to ethics are so-called maternal approaches to ethics. Maternal thinkers such as Sara Ruddick, Virginia Held, and Caroline Whitbeck affirm the feminine psychological traits and moral virtues that society associates with women. As they see it, a truly gender-equal ethics would not favor paradigms that speak much more to men's experience in the public world than to women's experience in the private world. Most of our relationships, say Ruddick, Held, and Whitbeck, are not between equals but between unequals. Women's relationships with their helpless infants, aging parents, ailing siblings, and distraught friends are not the same as the relationships that exist between equally informed and powerful adults. The way in which two businessmen negotiate a deal is not to be compared with the way in which a mother and her child agree to a bedtime. If any model fits relationships between unequals, says Held, it is the relationship between children and mothers—or more precisely—between children and *mothering persons.*

However appealing maternal ethics may be, nonfeminist critics of it doubt that any one human relationship either can, or should, serve as the paradigm for all human relationships. As they see it, no one type of human relationship is robust enough to serve as a general model for how all people should treat each other. In particular, relationships between unequals should not serve as the model for relationships between equals or vice versa. The same words that mothers use to comfort their children may strike an adult friend as condescending or demeaning.

Feminist critics of maternal ethics express similar reservations about it, adding the point that the mother/child relationship is a problematic choice for a feminist moral paradigm because it is burdened with enough patriarchal baggage to weigh down even the strongest of women. Although feminist critics concede that the mother-child relationship is a better model for fully human relationships than is the traditional two autonomous adults model, they believe that even better models are available. The mother-child relationship is not, they note, the only human relationship that is based more on need, love, and trust than on desire, duty, and fear. Nor is it the only kind of relationship that recognizes human beings' emotional connections as well as rational links. On the contrary, friendship relationships, especially ones based on shared goals and aspirations, can bind human beings in particularly strong ways. Held together by tears, laughter, and sweat rather than waivers, subpoenas, and depositions, goal-orientated and/or value-shared friendship relations hold out more possibilities for moral development than do contractual relations. They are also less imbalanced than mother/child relationships in that the parties to them are equals who can give as much as they take from each other, albeit in different sorts of ways.

Power-Focused Feminist Ethics

Unlike care-focused feminist approaches to ethics, power-focused feminist approaches to ethics ask questions about male domination and female subordination *before* they ask questions about good and evil, care and justice, or mothers and children. In an attempt to specify the kind of questions that feminist as opposed to nonfeminist ethicists typically ask, philosopher Alison M. Jaggar has claimed that to qualify as feminist, an approach to ethics, whether care-focused or power-focused, must assume that it is morally wrong to treat women as men's subordinates, as if women are somehow less deserving of respect and consideration than men. In her view, it is especially important that power-focused feminist ethics correct for the mistakes in some wrongly formulated care-focused feminist ethics. Among these mistakes is a tendency to overestimate the value of care and to underestimate the value of justice, thereby failing to see that equality is the proper aim of feminist ethics. Although power-focused feminist ethicists should attend first and foremost to patterns of *male* domination and *female* subordination, Jaggar believes that they should go on to address the immoralities caused by other patterns of human domination and subordination. Not only sexism but also classism, ethnocentrism, heterosexism, ableism, and so on are the enemies of feminist ethicists. Jaggar also stresses that any feminist ethics that merits allegiance must go beyond theory into practice. Feminist ethics is about making the present world a better world in which men and women equally thrive. It is not simply about imagining such a world.

Among the theorists who have followed Jaggar's admonitions is Susan Sherwin, a feminist bioethicist. Sherwin has written extensively on topics related to women's role in reproduction and women's overall health status in both developed and developing nations. Like Jaggar, she believes that a feminist approach to ethics differs from feminine and maternal approaches to ethics because it is more political than either of these two alternative approaches is. Although a *feminist* approach to ethics may affirm the same values and virtues a *feminine* or *maternal* approach does, it will not do so uncritically. Women must be wary of women's values and virtues to the degree that they are unliberating by-products of life in a sexist culture. Whatever positive features the virtue of care has, for example, it may still be a virtue that subordinates women to men, as it sometimes does in the field of health care. Vulnerable people such as patients and nursing home residents know they cannot afford to alienate the affections of those who have power over them such as physicians and nursing home administrators. The powerless are especially motivated to accommodate the powerful. Similarly, whatever the moral advantages of maternal thinking may be, it is still a mode of thought produced in a certain kind of family structure—namely, a Western, middle-class, heterosexual family. Insofar as this *structure* oppresses women, the maternal mode of thought produced within it is likely to oppress women. By choosing to specialize, as it were, in motherhood and caring, women tend to legitimate patriarchal attempts to make mothering women's prime duty. Women must win the right *not* to mother—the right for equality in public and private life—before they can safely develop a maternal or feminine ethics.

As mentioned previously, a feminist approach to ethics does not focus only on *women's* oppression. As Sherwin and many other feminists see it, because feminists are sensitive to patterns of male domination and female subordination, they are also attuned to patterns of domination and subordination that are classist and/or racist. Although a feminist approach to ethics usually begins with a question such as, "How does this policy, this state of affairs, oppress *women* in particular?" it often ends with a question such as, "How does this policy, this state of affairs, oppress vulnerable *people* in general?" Having posed the question, "How do current health care insurance schemes oppress women?" for example, many feminist ethicists tend to move on to the question, "How do current health care insurance schemes oppress the chronically ill, the elderly, people with serious disabilities, and the poor?" Often, it takes an oppressed group—in this instance, women—to recognize the oppression of other oppressed groups and to seek remedies for them. Clearly, the aim of feminist ethicists is not to prove that women's oppression is the worst form of oppression imaginable; rather, it is to identify and eliminate the *kind* of oppression that women have traditionally experienced.

Another feature of Sherwin's feminist approach to ethics, which is common to most other feminist approaches to ethics, is her refusal to envision it as a theory to end all theories. To the degree that feminist epistemology rejects universal truth as a desirable goal for human knowledge and that feminist ontology rejects the totally self-sufficient individual as a desirable model for selfhood, a feminist approach to ethics rejects absolute goodness as a desirable goal for human action. It does not aim to articulate an absolute and unchanging morality for all human beings, be they female or male, the oppressed or the oppressors. On the contrary, a feminist approach to ethics aims to provide oppressed women—and also other oppressed groups—with moral action guides and interpretive tools suited to their particular historical situation. These flexible norms aim to help people liberate themselves from those who would dominate them, for unless a person is free, she cannot dare to be fully moral.

Because liberation is not an overnight process, most feminist approaches to ethics tend to be incremental. To the degree that a woman, usually with the help of other women, frees herself from the constraints that limit her ability to help structure a world in which relationships of domination and subordination do not exist, to that same degree, she becomes a moral agent. Morality's imperatives are as different as the individual women to whom they speak in the sense that each woman must interpret morality's demands in terms of her social and historical context. Each woman is a Joan of Arc of sorts. She must decide whether the "voices" speaking to her are true or false, a source of liberation or further oppression.

As Sherwin sees it, however, it is not enough for a feminist approach to ethics to encourage women to assess the moral validity of the different voices that speak to them. On the contrary, a feminist approach to ethics must provide women with a rationale for determining whether a voice they hear is singing gibberish or articulating a meaningful message. Most feminists reject not only the kind of "moral absolutism" that cannot see beyond its own vested interests but also the kind of "moral relativism" that permits anything and everything, including the oppression of women or other oppressed groups. Only if feminists can say that some things are clearly wrong can they justifiably coalesce to try to make them right. If one person's decisions are as good as anyone else's, then there is no reason for either person to change their minds and/or course of action. Socially and politically speaking, moral relativism denies the possibility of moral progress.

Because feminist approaches to ethics focus on how power is used to oppress *women* in particular, critics have complained that these approaches are female biased. Ethics, insist the critics, cannot proceed from a specific standpoint—in this case, from the standpoint of women—and still be regarded as ethics. To this objection, feminist ethicists respond that traditional ethics proceed from a standpoint also. This standpoint is the standpoint of men presented as the standpoint of all human beings. Rather than hiding the fact that feminist ethics begins, though it does not end, with a discussion of women's moral experiences, feminist ethicists publicly celebrate their ethics' point of origin.

The fact that feminist approaches to ethics focus first, or even exclusively, on *women's* concerns makes them controversial, but it also makes them particularly empowering for women. Although it is difficult to make generalizations about specifically lesbian approaches to ethics, most of them seem to entail a thorough transvaluation of traditional moral values. Mary Daly, for example, insists that she whom the patriarch calls "evil" is in fact good, whereas she whom the patriarch calls "good" is in fact bad. If a woman is to escape the traps men have laid for her—if she is to assert her power, to be all that she can be—then she must realize that it is not good for her to sacrifice herself for the sake of the men and children in her life. What *is* actually good for women is precisely what patriarchy identifies as evil for women—that is, becoming their own persons.

Lesbian approaches to ethics also typically urge women to replace the question "Am I good?" with the question "Does this contribute to my self-creation, freedom, and liberation?" Just because lesbian ethicists emphasize the role of choice as opposed to duty in ethics, it does not mean that they are asking the wrong questions about human morality. As Marilyn Frye sees it, the need to ask the "right" questions tends to arise among people who have a vested interest in maintaining the socioeconomic and political status quo. For example, a white/Christian/middle-class/American male probably bases his conception of himself as an upright citizen on his conviction that he is in the right—that he knows what is best for himself and others. So long as women as well as men continue to accept this "male" conception of moral agency, reasons Frye, women will have but two choices: (1) to become men so that they can exert men's moral authority over others; or (2) to become female moral authorities who then make it their business to exert *women's* moral authority over others. Frye regards both these options as unacceptable for women. The first forces women to negate themselves; and the second sends women down the same moral blind alley men have gone. If ethics is about some people not only proclaiming to other people what is "good" for them but imposing that good on them, then Frye welcomes the criticism that lesbian approaches to ethics are not really about *ethics.* Only those who have a vested interest in the status quo—in the powerful remaining powerful—require certitude about their righteousness—about their warrant to direct and administer everything. But because lesbians supposedly do not want this kind of power—because their personal experiences have enabled them to appreciate the major immoralities it generates—they require neither proof of their "goodness" nor the "right" to impose it on anyone but themselves. Thus, it is doubtful that lesbians want or need ethics in the traditional sense of ethics.

Conclusion

Whether they are care-focused or power-focused, feminist approaches to ethics differ from nonfeminist approaches to ethics in that they are sensitive to women's moral concerns and to the ways in which being a member of a culturally disfavored gender—in this instance, the "feminine" or "female" gender—leads to women's disempowerment personally, politically, economically, and socially. In addition, they all agree with Alison Jaggar that their most important tasks are (1) to provide moral critiques of actions, practices, systems, structures, and ideologies that perpetuate women's subordination; (2) to devise morally justifiable ways (e.g., public policy initiatives, peaceful protests, boycotts) to resist the economic, social, and cultural causes of women's subordination; and (3) to envision morally desirable alternatives to the world as we know it: sexist, racist, ableist, heterosexist, ethnocentric, and colonialist.

Because feminist ethicists focus on women—or, more abstractly, on gender—some nonfeminist ethicists have dismissed their work as being just as "sexist" as traditional Western ethics supposedly is. These critics claim that if it is wrong to disguise men's preferences as human values, it is wrong to disguise women's preferences as human values. Either gender-free moral values exist or they do not. If they do exist, they belong equally to men and women. Finally, if it is wrong, for example, to keep women on the moral defensive by underscoring their low scores on Kohlberg's scale, it is just as wrong to keep men on the moral defensive by highlighting men's violence against women.

To the extent that feminist approaches to ethics are women-centered—that is, focused on female subordination and male domination—critics claim that they are not so much *ethical* approaches as *political* power plays. To say that feminist approaches to ethics are political in the modern sense of the term is to say something decidedly negative. It gives the impression that women are fighting against men to gain control over them—to have their own say, no matter what. But to say that feminist approaches to ethics are political in the classical sense of the term is to say something quite different. It is to say that feminists pay attention to issues of power because they want to liberate not only themselves but also others from oppressive structures, systems, and relationships. Politics is indispensable to ethics in the sense that only an empowered person has the capacity to *self-reflectively* make this a better world. Only free persons can be moral persons, and feminists want women (and men) to be free persons.

—Rosemarie Tong

See also Bioethics; Cognitive Moral Development; Empathy; Ethics, Theories of; Ethics of Care; Kohlberg, Lawrence; Lesbian Ethics; Maternal Ethics; Moral Agency; Moral Reasoning; Virtue Ethics

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FEMINIST THEORY

Feminist theory is a diverse body of thought based for the most part on one or more traditional or contemporary political, social, and cultural theories such as liberalism, socialism, and postmodernism. The difference between feminist theory and nonfeminist theory is that the former self-consciously reflects on the experience of women and deliberately uses the lens of gender as its preferred critical perspective. Sometimes nonfeminist theorists fault feminist theorists for not viewing reality through the single lens of the quintessential impartial and objective human being but instead through the multiple lenses of partial and subjective existing women. But feminist theorists are not flummoxed by this harsh critique. They respond that no one can simply be human. Among other feminist theorists, Susan Bordo emphasizes that reality is gendered. We cannot entirely escape the categories male/female, man/woman, and masculine/feminine, not even if we are transgendered, transsexual, multiply gendered, multiply sexed, or trying to be nongendered/nonsexed.

Throughout the 1960s and 1970s, liberal, radical, and Marxist-socialist feminisms were predominant, but they were complemented by several other modalities of feminist thought including psychoanalytic and gender feminism. By the 1980s and 1990s, these types of feminist thinking had been joined by multicultural, global, and postmodern feminism, all of which have been further supplemented by new millennial third-wave feminist thinking. Whatever their disagreements with each other may be, most feminist thinkers agree that to be classified as feminist, a theory must proceed on the assumption that traditional, largely patriarchal, modes of thinking, which support women's subordination to men, have to be replaced by modes of thinking that equally value both women's and men's intellectual, moral, and social contributions to the private, professional, and public domains.

Liberal, Radical, and Marxist-Socialist Feminist Theories

Liberal feminism is probably the most recognized and accepted form of feminist thought today. It is predicated on the view that women's subordination to men is rooted in a set of gender identities and roles that are used as justifications, first, for relegating women to the private realm, where they are expected to bear the brunt of most domestic work and care-giving activity, and, second, for limiting women's access to the public realm and the major professions (business, medicine, and law). As liberal feminists see it, the way to release women (and men) from this confining state of affairs is to open the public world to women and, as a correlative, the private world to men.

Liberal feminists are revisionists, not revolutionaries. Their goal is not to destroy existing systems and structures but to integrate women into them. Using legal and political remedies, liberal feminists have accomplished this goal to some degree over the past 35 years. Yet, the complete liberal feminist agenda, articulated in the 1967 National Organization for Women's (NOW's) Bill of Rights, remains far from being fully implemented. Circa 2000, the Equal Rights Amendment has yet to pass into U.S. law; the average American female worker earns only 56.0% as much as the average male worker; only 14 out of 100 members of the U.S. Senate are women; and just nine Fortune 500 chief executive officers are women. Moreover, U.S. women, like women throughout the world, remain heavily invested in the private realm, where they continue to do most of the family housework and a major proportion of dependency work (taking care of infants and children, the elderly, the infirm, and people with disabilities in home and institutional settings).

In contrast to liberal feminists, radical feminists focus not so much on social and economic issues as on women's sexual and reproductive concerns, seeing women's liberation in women's ability to control how their bodies are used. There are two major types of radical-feminist thinkers: radical-libertarian feminists and radical-cultural feminists. Their disagreements are several and somewhat profound.

Radical-libertarian feminists urge women to explore the pleasures of consensual sex, be it heterosexual or homosexual, autoerotic, sadomasochistic, or intergenerational. They seek to free women from the belief that good sex can be experienced only in a committed, long-term love relationship and that sex for sex's sake is somehow bad, promiscuous, or dirty. In addition, radical-libertarian feminists advise women to use reproduction-controlling and reproduction-assisting technologies as little or as much as they wish. For example, they encourage women to prevent or terminate unwanted pregnancies or, alternatively, to have children when they want them (premenopausally or postmenopausally), how they want them (naturally or artificially), and with whom they want them. The overall conviction of radical-libertarian feminists is that no matter how much educational, political, and economic equality women achieve, nothing fundamental will change for women so long as women's reproductive role remains the same. It does not matter whether a woman is a CEO or a file clerk. So long as her primary identity is that of a wife and/or mother, she will remain burdened with responsibilities from which men are free. For this reason, some radical-libertarian feminists look forward to the day when ectogenesis (extracorporeal gestation in an artificial placenta) entirely replaces the natural process of pregnancy, labor, delivery, birth, breast-feeding, and subsequent weaning.

Although radical-cultural feminists are just as focused on sexual and reproductive matters as radical-libertarian feminists are, they have serious reservations about women substituting reproductive technologies for their own birthing powers. Increasingly referred to as "essentialists" on account of their view that all women are fundamentally the same, radical-cultural feminists caution that sex, understood primarily as heterosexual sex, is usually more dangerous and compulsory than pleasurable and consensual for women. In their estimation, women are forced to serve men's sexual desires and reproductive needs to a greater or lesser degree. More often than not, men reject and/or ridicule women who are not attractive. Worse, some men physically abuse women for not satisfying them sexually or failing to produce children for them on demand. Radical-cultural feminists believe, therefore, that heterosexuality is not about men and women pleasing each other equally; rather, it is about men seeking to control and objectify women representatively through pornography and actually through the use of sex workers and the systematic sexual harassment, rape, and physical abuse of women. Therefore, radical-cultural feminists urge women to abandon heterosexual relations and to seek lesbian relations instead. Separate from men's gaze, control, and power, women can discover a woman-centered sexuality and gain strength to accomplish goals they value.

In addition to stressing the dangers of heterosexual relations and the advantages of lesbian alliances, radical-cultural feminists claim that artificial reproduction is more likely to disempower than empower women. They advise women to view physician-mediated donor insemination, in vitro fertilization, genetic testing, reproductive cloning, and plans for an artificial womb not as procreative options for women but as means for a male-dominated society to exercise greater control over women's procreative powers. In an unreflective rush toward the local assisted-reproduction center, women may unwittingly forsake their fundamental power—namely, their ability to bring new life into the world through their own bodies. Marxist-socialist feminists depart from both liberal and radical feminists in that they come close to replacing the category of gender with the category of class. They note that although it is true that women occupy a subordinate position relative to men for gender-related reasons, this fact does not mean all women are equally oppressed. For example, rich women are able to control poor men in ways that poor women cannot control poor men. In the United States, at least, money purchases women a measure of power that can offset their body-based vulnerabilities vis-à-vis men.

Marxist-socialist feminists insist women's oppression originated in the introduction of private property, an institution that they believe obliterated whatever equality of community humans had previously enjoyed. Private ownership of the means of production by relatively few persons, originally all male, inaugurated a class system whose contemporary manifestations are corporate capitalism and state imperialism. Reflection on this state of affairs suggests that capitalism per se, as well as the larger social rules that privilege men over women, is the cause of women's oppression. If all women—rather than just the "exceptional" ones—are ever to be liberated, the two-headed beast of capitalist patriarchy or partriarchal capitalism must be destroyed.

Marxist-socialist feminists are conflicted in ways that liberal and radical feminist are not precisely because they are not certain whether to use gender or class as their primary lens of analysis. According to Chris Beasley, Marxist-socialist feminists have developed three approaches to enable them to do what may be impossible, namely, blend class and gender into a seamless analytic tool. These three approaches are labeled the two-tier or dual-systems approach, the unified-system or capitalist-patriarchy approach, and the dynamic-duo approach.

The early work of Juliet Mitchell epitomized the two-tier or dual systems approach to class and gender. In her well-known work, *Women's Estate,* Mitchell abandoned the traditional Marxist feminist position according to which women's relatively low social status is fundamentally a function of their relation to capital, of whether or not they are part of the productive workforce. In place of this monocausal explanation for women's oppression, she suggested that women's condition is multiply determined by women's role not only in production but also in reproduction, the socialization of children, and sexual relationships. Yet Mitchell did not go so far as to say that women's role in production is no more important than her reproductive, maternal, and sexual role. Ultimately, her explanation for women's oppression is more class focused than gender focused.

In an effort not to privilege the category of class over that of gender, some of Mitchell's successors strove harder to develop a unified-system version of Marxist-socialist feminism. For example, Iris Young claimed that because class per se is a sex-blind category, it can never be an adequate basis for an analysis of women's specific oppression as women. She insisted that only a gender-aware category such as the sexual division of labor could explain why women in the productive workforce are more likely than men to take the orders, do the mundane jobs, get paid less, and work a "double day" (for example, 8 hours as a secretary in the "public" realm and then 8 hours or more as a housekeeper and child rearer in the "private" realm). Moreover, no matter how high up the professional ladder women climb, their work will be marked with the stamp of gender. For example, female physicians are more likely to specialize in pediatrics than in neurosurgery and women in business are more likely to head the human resources than the finance department.

Although a unified-system version of Marxist-socialist feminism blended class and gender analysis better than a dual-system version did, it turned out to be problematic precisely because it insisted there was no way to separate gender oppression from class oppression. Reasoning that capitalism could exist without patriarchy and vice versa, exponents of yet another version of Marxist-socialist feminism, the dynamic-duo version, stressed that despite capitalism's and patriarchy's common desire to control women, patriarchs sometimes want to use women in ways that do not serve capitalists' interests and vice versa. In the 19th century, for example, male workers wanted their wives and daughters to stay at home, where they could personally service them, whereas male employers wanted women (excluding their own wives and daughters) to work for low wages in the productive workforce so they could make higher profits for them. Only if male workers and male employers could find some mutually agreeable way to use women to meet their separate needs could both patriarchy and capitalism thrive. As it turned out, in this particular instance, a satisfactory deal was cut. Male employers offered male workers a "family wage" large enough to permit male workers to keep their wives and daughters at home but still small enough to keep male employers rich. But just because capitalists and patriarchs managed to answer the "woman question" successfully in this situation, it does not mean that they will always be able to answer it successfully. It is, in other words, possible for patriarchy to outlive capitalism or vice versa in the estimation of exponents of the dynamic duo version of Marxist-socialist feminism. One is not necessary for the other's survival.

Psychoanalytic and Gender Feminism

To the degree that liberal, radical, and Marxist-socialist feminists focus on the macrocosm (patriarchy or capitalism) in their respective explanations of women's oppression, psychoanalytic and gender feminists retreat to the microcosm of the individual, claiming that the roots of women's oppression are psychological—a matter of self-esteem, self-respect, and general self-understanding.

For psychoanalytic feminists, a focus on sexuality's role in the oppression of women stems from Freudian theory. In the so-called pre-oedipal stage, all infants are initially symbiotically attached to their mothers, whom they perceive as an omnipotent, unpredictable force in their lives. The mother, who can give so much, can also give too little. She can fail to nurse the infant on demand or to cradle him or her in the dead of night.

The primal pre-oedipal stage, which tethers the infant to the mother, ends for boys with the so-called Oedipus complex, the process by which boys give up their first love object, the mother, to escape castration at the hands of their fathers. As a result of submitting his id (desires) to the superego (collective social conscience), a boy is fully integrated into culture. Together with his father, he will rule over nature and women, seeking to control their irrational powers. In contrast to boys, girls, who have no penises to lose, separate slowly from their first love object, the mother. As a result of this slow individuation, a girl's integration into culture is incomplete. She exists at the periphery of culture as the one who does not rule but is ruled by men, to some degree because she fears her own power.

Because the Oedipus complex is the root of male rule, or patriarchy, some psychoanalytic feminists speculate it may be nothing more than a fiction created by men's imagination—a psychic trap that women in particular need to escape. Others object that human beings must accept some version of the Oedipus complex as the experience that integrates the individual into civilized society. In accepting some version of the Oedipus complex, however, human beings need not accept the Freudian version, according to which authority, autonomy, and universalism are labeled *male,* whereas love, dependence, and particularism are labeled *female.* These labels, meant to privilege men over women, are not essential to the Oedipus complex. Rather, they are simply the consequences of a child's actual experience with men and women. Over time, practices such as dual parenting and dual participation in the workforce might change the gender valences of the Oedipus complex substantially, so that authority, autonomy, universalism, love, dependence, and particularism become the equal property of both men and women.

Although gender feminism is related to psychoanalytic feminism, there are important differences between psychoanalytic feminists who focus on pre-oedipal and oedipal themes on the one hand and gender feminists who focus on the virtues and values associated with femininity or femaleness on the hand. Although care-focused feminists as well as psychoanalytic feminists probe women's psyches, care-focused feminists such as Carol Gilligan and Nel Noddings also pursue the relationship between women's psychology and morality, particularly their style of moral reasoning. In her groundbreaking work, *In a Different Voice,* Carol Gilligan claimed that on the average, and for a variety of cultural reasons, women in societies such as the United States tend to espouse an ethics of justice that stresses rules and rights. As Gilligan saw it, U.S. society seems to subscribe to a male model of moral development according to which a truly moral person is the kind of individual who is willing to forsake even family members and friends to uphold the law or to serve a cause he deems "noble." The kind of situation Gilligan has in mind is, for example, a father who rejects his homosexual son on the grounds that homosexuality is against God's law. Measured against this male model of moral development, many women fare poorly largely because abstractions such as the Law, Truth, and Faith are not nearly as important to them as the flesh-and-blood people in their lives. Gilligan insisted, however, that this fact about women does not mean that women are less morally developed than are men. Rather, it simply means that women are differently morally developed compared with men. For men, ethics is typically about being autonomous, taking a stand, self-identity, and achievement in work. For women, ethics is typically about being related to others, not hurting other people, intimacy, and success in love. But even though both men and women typically pursue their own kind of ethics, each gender is also capable of embracing the ethics of the other gender. In fact, in her later work Gilligan repeatedly stressed that the fully moral person is someone who is able to blend within his or her psyche the values of both women's and men's morality, expertly translating between the moral language of rights on the one hand and the moral language of responsibilities on the other.

Nel Noddings also drew a distinction between an ethics of justice and an ethics of care, identifying the former with men and the latter with women. She diverged from Gilligan, however, in her insistence that care is more fundamental than is justice. She also implied that, in U.S. society at least, men need to catch up with women morally.

Noddings contrasted the Greek myth of Ceres with the Old Testament account of Abraham and Isaac to underscore the limits of a morality she labels *male.* Recalling that Ceres was the Greek goddess responsible for the Earth's well-being, Noddings stressed that despite her sacred duties to nurture Earth, Ceres abandoned her post to search for her daughter Proserpine after she was abducted by Pluto, god of the underworld. Ceres refused to put her job, so to speak, above her daughter. In contrast to Ceres, observed Noddings, the Old Testament patriarch Abraham put abstract duty above concrete love. For him, doing one's duty—specified in his case as obeying God's will—was the ultimate moral imperative. When God commanded Abraham to sacrifice his son Isaac to him, Abraham prepared to kill his son even though he could not understand why God would command such an atrocious act. Distinctly unimpressed by Abraham's blind faith in God, Noddings claimed that Sarah, Abraham's wife, would have flatly refused to sacrifice her son Isaac to God. She would have reasoned that the command to kill Isaac was not really coming from God, or if it was coming from God, she wanted nothing to do with such a cruel deity.

In addition to Noddings, so-called maternal thinkers have used the mother-child relationship as a springboard for discussing the necessary and sufficient conditions for any and all moral human relationships. Maternal thinker Sara Ruddick argued that from the work mothers do for their children emerges a distinct mode of moral reasoning best termed maternal thinking. To meet the three fundamental goals of maternal practice—namely, the preservation, growth, and social acceptability of children—mothers must, said Ruddick, cultivate a multitude of very specific virtues, the most important of which is the metavirtue of attentive love. This metavirtue, which is at once cognitive and affective, enables mothers to really know their children in all their uniqueness. Recognizing that their children are capable of doing evil as well as doing good, good mothers try to help their children eliminate the vices and weaknesses peculiar to them, slowly replacing them with virtues and strengths.

Concerned that well-intentioned, goodwilled men might feel that, by virtue of their XY chromosome, they cannot think maternally, Ruddick noted that *all* human beings are capable of thinking in terms of preserving each other, helping each other grow, and making each other socially acceptable. To survive as a human species and to thrive as individual human beings, both genders need to think maternally in the public world as well as the private world. Ruddick opined that because nonmaternal thinking has dominated the public realm, U.S. society has been pushed in the direction of ecological disorder, social injustice, violence, and war. People who do not think like mothers, observed Ruddick, do not seem to see like mothers. For a nonmaternal thinker, war is about winning, defending one's way of life, and establishing one's position of power. In contrast, for a maternal thinker, war is about destroying the child whom one has spent years preserving, nurturing, and training—a unique human person who cannot be replaced. In other words, for a maternal thinker, war is about death—about canceling out the "product(s)" of maternal practice—and it is this realization that turns maternal thinkers in the direction of peace activities.

Multicultural and Global Feminism

Common to all the feminisms discussed in the foregoing is a desire to view women as somehow the same. There is a problem with stressing women's sisterhood and solidarity, however. Not only are women different from men, they are also different from each other. Women's class, race, ethnicity, nationality, sexual orientation, and so forth are not uniform. This point about women's differences, and not confusing one kind of woman (white, Western, middle-class) with all women or women in general, is the core conviction of both multicultural and global feminism.

In the late 1980s and early 1990s, the concept of "cultural diversity" captured the attention of major institutions in the United States, and multicultural feminism emerged as part of this celebration of diversity. Gender is neither the only nor necessarily the main cause of many women's oppression, according to multicultural feminists. As they see it, depending on her race, ethnicity, class, religion, sexual orientation, age, health status, and level of education, one woman's oppression may be another woman's liberation. Just because college-educated housewives in suburbia seek release from their domestic duties so they can get jobs in corporate America, it does not mean that female assembly-line workers do not yearn to be stay-at-home wives and mothers. More generally, just because many women find that matters related to their sexuality and reproductive capacities and responsibilities play the greatest role in their oppression, it does not mean that all women find this to be the case. For some women, not sexism, but racism, ethnocentrism, classism, heterosexism, ableism, and/or ageism are the major contributors to their low status.

Multicultural feminists replace discussions of sexism and androcentrism with discussions of interlocking systems of oppression (gender, race, and class) and women of color's and other marginalized women's multiple jeopardizes. Although a privileged white woman may hit her head against a glass ceiling or two in her lifetime, she will not have to face the kind of obstacles a Native American woman with limited education opportunities, severe diabetes, intermittent depression, and an alcoholic husband has to face. Nor will she have to contend with the kind of hardships that an undocumented Mexican woman in the United States accepts as her lot—as the price of admission to a better life for her children. As multicultural feminists see it, sexism, racism, classism, ableism, elitism—indeed all the "isms" that divide people—interlock and choke whomever they catch in their grip. Oppression is a many-headed beast capable of rearing any one of its heads depending on the situation. The whole body of the beast is the appropriate target for multicultural feminists who wish to end its reign of terror, and, depending on her situation, each woman must pick and choose her battles.

Global feminism differs from multicultural feminism because it focuses not on women in any one nation-state but on how the condition of women anywhere in the world affects the condition of women everywhere else in the world. Agreeing with multicultural feminists that feminism cannot ignore women's cultural differences, global feminists nonetheless strive to create alliances among women worldwide. They have two goals in common. The first is to convince all nations to honor women's right to make free choices about matters related to their reproductive and sexual capacities and responsibilities. Without the ability to control their own bodies, women cannot feel like full human persons. The second, coequal goal of global feminists is to bring women (and men) together to create a more just social and economic order at the international level as well as the national level. Global feminists are activists as well as theorists; they are bent on creating a world in which all people, no matter where they live, have enough food, shelter, clothing, health care, and education to live full human lives.

Global feminists claim that women must forge strong international networks to eliminate the disparities that exist between the world's wealthy people and the world's poor people. For them, universal sisterhood is not a natural state of affairs but an ideal to achieve. Because of their nations' condition, women in developing nations are often much more focused on economic, social, political issues than on the sexual and reproductive issues that have tended to preoccupy the interest of women in developed nations. As a result of women's different national priorities, however, women's conversations at international conferences have sometimes degenerated into shouting matches. In fact, at each of the three international women's conferences the United Nations (UN) sponsored during the International Decade for Women (1975–1985)—in Mexico City (1975), Copenhagen (1980), and Nairobi (1985)—problems emerged among women who were variously identified as First World, Western, Northern, or from developed nations on the one hand and women who were variously identified as Third World, Eastern, Southern, or from developing nations on the other. By the 1995 women's conference held in Beijing, however, global feminists had helped women resolve some of their cross-cultural differences and to appreciate some of their commonalities. This conference was pronounced a success by its participants, who forged a strong women's human rights document at it.

Global feminists are proud of women's international agreements, but they realize that women need to do more than talk about women's human rights to create a just and equitable social order. Privileged feminists must, they say, be prepared to forsake some of their material luxuries so that disadvantaged women can secure the food, clothing, and shelter they and their families need to survive. Emphasizing that material goods are not in infinite supply and that scarcity of goods and services is increasingly the order of the day, global feminists claim that feminists must take the lead in living more simply and frugally so that life on earth can continue through this millennium and beyond. Unless privileged feminists stop being part of the world's maldistribution system, they cannot in good conscience represent themselves as true opponents of the forces that coconspire to create and maintain systems of human domination and subordination.

Postmodern and Third-Wave Feminisms

Like multicultural and global feminists, so-called postmodern feminists emphasize women's differences, but in ways that shake some of feminism's basic assumptions. Inspired by a variety of antifoundationalists, especially the deconstructionist Jacques Derrida and the psychoanalyst Jacques Lacan, postmodern feminists faulted feminist thinking prior to their emergence on the scene to the degree that it sought to articulate *one, true feminist* story of reality. Postmodern feminists viewed this kind of feminist project as a variation on patriarchal phallocentric thought, which uses divisive language to maintain patterns of human subordination and domination. Wanting to overcome so-called oppositional thinking—that is, a mode of thinking that contributes to conceptual polarities and political divisions such as developed nation/developing nation, white/nonwhite, rich/poor, nature/culture, and male/female—postmodern feminists attempted to think nonoppositionally.

Among the early second-wave postmodern feminists who maintained that oppositional or binary thinking impeded the development of feminist thought was Hélène Cixous. She claimed that thinking in terms of oppositions not only limits thought but also generates real world power struggles by privileging one term in an oppositional dyad over the other. She also claimed that all conceptual dichotomies are grounded in the fundamental dichotomy—man/woman—in which man is associated with all that is active, cultural, light, high, or generally positive and woman with all that is passive, natural, dark, low, or generally negative. Cixous stressed that in the man/woman dichotomy, as in all dichotomies, the first term of the dichotomy is the term from which the second is said to depart or deviate. Man is the self, woman is the other; man leads, woman follows, and so on. Thus, said Cixous, woman exists in man's world on his terms. She is either the other for man, or she is nothing—the unthinkable, the unthought.

Cixous challenged women to liberate themselves by putting themselves into words and thinking the unthinkable. The type of writing that Cixous identified as woman's own—marking, scratching, scribbling, jotting down—evoked the image of Heraclitus's ever-changing river. In contrast, the type of writing that Cixous associated with man brought to mind Parmenides' changeless world in which what is has always been and will always be. As soon as a thought gains the official seal of patriarchal approval, said Cixous, it is no longer permitted to move or change. Thus, for Cixous, the way women write is not merely a new style of writing; it is the only way in which women can escape the power of men.

Third-Wave Feminism

Like postmodern feminists, so-called third-wave feminists are more than willing to accommodate diversity and change. They are particularly eager to understand the ways in which gender oppression and other kinds of human oppression reinforce each other. For third-wave feminists, difference is the way things are. Their world is the Heraclitean world, not the Parmedian world. Moreover, contradiction, including self-contradiction, is expected and even welcomed by third-wave feminists. So too is conflict. Leading third-wave feminists stress that they do not require women to subscribe to any one feminist dogma or party line. Their only goal is to help women, individually and collectively, lead happier, healthier, and fuller lives.

As part of their attempt to help women better understand each others' situations, third-wave feminists engage in research and writing that attends to the lives and problems of specific groups of women and, even more typically, individual women. Their work is based on the real lives and problems women face, and, even more than multicultural, global, and postmodern feminists, third-wave feminists stress that women come in many different colors, ethnicities, nationalities, religions, and cultural backgrounds. Thus, a typical third-wave feminist text will include articles about women who represent a wide variety of multicultural perspectives: Hispanic-American, African-American, Asian-American, Native American, and so on. Indeed, it is difficult to find an article authored by a third-wave feminist that is not heavily hyphenated and that does not emphasize that each woman is different from every other woman.

Third-wave feminists are not so much interested in getting women to want what all women should want, as in responding to what individual women say they want and not second guessing or judging whether their wants are authentic or inauthentic. They describe the context in which they do feminism as messy or partial and provisional in nature. According to third-wave feminists Leslie Heywood and Jennifer Drake, part of this messiness includes embracing women who refuse to identify themselves either as women or as men and who try on different ethnic identities as one might try on different styles of clothes. To put it mildly, third-wave feminists are very nonjudgmental.

Conclusion

By not only insisting that one feminist identity does not exist, but also celebrating its absence, third-wave feminists and postmodern feminists respond to the spirit of the 2000s. The strength of these forms of feminism is that they refuse to force women to think and act in the same way. But third-wave feminism and postmodern feminism also have faults of their own. Not only is the essentialist notion "Woman" gone, the category of gender has been seriously weakened. Whereas the challenge for past feminist thinkers was to overcome the idea that all women are necessarily victims or victims in the same sort of way, the challenge for feminists today is to recognize that to have feminism, one has to believe that women constitute some sort of class or social group and that just because some women feel empowered it does not mean all women feel this way. Women in the United States and other developed nations may be more equal and free than they were 50 or even 25 years ago. But women in many developing nations often live in conditions more oppressive to women than even the conditions that challenged U.S. feminists at the turn of the 19th century. Thus, women may have something to lose as well as to gain in their embrace of each other's many differences. They may, as Christine di Stephano cautions, lose themselves.

Gender still makes a difference, and men still remain more "equal" than women. Feminists are in no position to develop gender-blind theories as of yet. The only theories they dare create must remain focused on women and distinct from humanism.

—Rosemarie Tong

See also Egalitarianism; Empowerment; Gender Inequality and Discrimination; Mill, John Stuart; Multiculturalism; Patriarchy; Postmodernism; Women's Movement

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Ferguson, Adam (1723–1816)

Ferguson was a noted figure of the Scottish Enlightenment. His major work, *An Essay on the History of Civil Society,* offers a natural history of the development of society and examines the role of the citizen in the modern commercial state. Born near the Highlands of Scotland and educated at the University of St. Andrews and at Edinburgh, Ferguson was an ordained minister in the Church of Scotland (Presbyterian). He was later appointed to the chair of natural philosophy at the University of Edinburgh and subsequently was appointed to the chair of moral philosophy. His works include *Institutes of Moral Philosophy, The History of the Progress and Termination of the Roman Republic,* and *Principles of Moral and Political Science.*

Preeminently a moralist, and influenced by Aristotle and the Stoics, Ferguson maintains that the moral good lies in happiness, the perfection of character. Not reducible to pleasure, happiness requires activity and achievement, including benevolent action. There is no conflict between genuine self-interest and the well-being of society. Because this theoretical knowledge of moral goodness requires an awareness of human nature and social circumstances, these provide the subject matter of much of the *Essay on Civil Society.*

Ferguson opens this work declaring that human beings are forever found in groups. There is no state of nature out of which isolated individuals contract to form society. Nor can human motivation be reduced to egoism, as Thomas Hobbes or Bernard Mandeville seemed to believe. Blessed with multiple propensities, including a natural affection for society, humans also have an impulse to competition and opposition, seemingly negative tendencies that may, Ferguson maintains, contribute to social cohesion and the preservation of liberty. The human being also possesses an instinct to excel and seek improvement, and this operates at both the individual and the species level. Society progresses from savage and barbaric stages (with no or little property) to a refined state with landed property, government, and liberty under law. Notable in Ferguson's account is how institutions, including constitutional and social arrangements, develop and emerge in a slow and unintended fashion. What is attributed to rational foresight or conscious agreement is often the result of the myriad actions and adjustments of individuals responding to circumstances over time.

Although Ferguson prefers the prosperity and liberty of the modern commercial society, he worries that modern individualism puts at risk communal bonds and public spirit. The division of labor, an unintended development, is essential for prosperity, but overspecialization may leave the citizen distinct from the soldier and the soldier distinct from the statesman; it may also create inequalities between those in liberal and mechanical vocations. Ferguson warns that a fixation on material fortune, including luxury goods, may distract citizens from the public weal and sunder all social connections except those of trade and exchange. Such a corruption of the self, with its indifference, cowardice, and loss of vigor, leads to despotism.

Ferguson's thought manifests a sympathetic awareness of the risks that accrue to modern and commercial societies. He also discerns how social order emerges slowly and spontaneously, often from the interplay of agents in conflict. That unintended outcomes may also be beneficial is an important idea that also has a home in the work of Bernard Mandeville, Adam Smith, and, more recently, F. A. Hayek.

—F. Eugene Heath

See also Economics and Ethics; Egoism; Hayek, Friedrich A.; Hobbes, Thomas; Hume, David; Individualism; Invisible Hand; Liberalism; Mandeville, Bernard; Motives and Self-Interest; Public Interest; Smith, Adam; Spontaneous Order

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FIDELITY

Fidelity is a word that means being faithful to obligations, duties, or observances. It means being true to one's word and having the disposition to fulfill promises. It equates to trustworthiness and implies discretion, judgment, and conscientiousness. It can also mean having unswerving allegiance to a person, spouse, or cause.

Fidelity came into English usage in the 15th century. Initially it referred only to the quality of being faithful or loyal to a person. It has its origins in the ancient Greek word *peithesthai,* meaning to believe or trust in a thing. Homer (eighth century BCE), the Greek epic poet who wrote the *Iliad* and the *Odyssey,* used a form of the word that indicates that the notion of fidelity has been a key concept in Western thinking from earliest times.

Fidelity covers a wide range of meanings. It reflects words such as accuracy, veracity, loyalty, honesty, observance, and probity. In respect to accuracy, we talk about exactness and exactitude or precision and preciseness in reproduction. In the electronic world, we speak of high fidelity and low fidelity when referring to the reproduction of sound and the amount of distortion that is associated with it. In respect to veracity, we talk about truthfulness, and in respect to loyalty, we talk about constancy and faithfulness. Observance relates to reliability, good faith, and probity.

Probity is probably the most relevant of all these terms. It relates to qualities such as rectitude, uprightness, goodness, honesty, and integrity.

In today's business world, not all senior managers and executives have these qualities. Some of them appear in the media from time to time accused of breaching ethical guidelines or taking part in illegal activities such as fraud and embezzlement. If we interpret fidelity in a business sense to mean faithfulness to one's professional obligations, duties, or observances, then it seems there are some issues to address.

Fidelity in Business

Fidelity in a business sense, as opposed to fidelity in a general sense as described in the foregoing, is the quality that facilitates transactions that take place on the stock market or in real estate. Fidelity is the special quality that facilitates closure in a business situation where a handshake or verbal agreement is often all that is necessary to clinch a deal.

Fidelity in business refers specifically to three criteria, that is, keeping contracts; fiduciary duties and responsibilities; and maintaining confidences or giving assurances.

A contract is a mutual agreement between two or more parties that something shall be done or forborne by one or both. A contract can be agreed on within the context of an ethical approach to business and being responsible socially, but it can also be an agreement enforceable by law.

Fiduciary duties and responsibilities are more complicated. A fiduciary is someone who makes decisions on behalf of someone else: For example, a person who acts as a trustee in respect to an organization's retirement scheme is a fiduciary because she or he makes decisions on behalf of the plan participants. A fiduciary duty is a legal relationship between two or more parties where someone has agreed to act as a caretaker of someone else's assets or well-being.

Fiduciary duties require moral behavior and probity of a high standard, over and above that expected in a business environment. Fiduciary responsibility means that a financial adviser will always act in the client's best interests. In real estate or stock market dealings, agents have fiduciary duties and responsibilities in respect to their clients, which means that their basic duty is to act solely in the interest of their clients. People who want to buy or sell a house or who want to invest for their retirement would like to think that their assets are safe because the agent to whom they have entrusted their business can be trusted. Unfortunately, we see reports in the press where well-known corporations have fraudulently misled their staff and the investors who put their trust in them.

Fiduciary duties and relationships require a range of actions such as (1) acting with the utmost care, ensuring that maximum protection and information are provided to the client; (2) acting with integrity (integrity defined as soundness of moral principle and character); (3) acting honestly and fulfilling the duty of full disclosure of all material facts; (4) acting loyally, that is, refraining from acquiring any interest that could be adverse to that of the client; and (5) fulfilling the duty of good faith, which includes total truthfulness, absolute integrity, and total fidelity to the client's interest. There would be no conflicts of interest such as an adviser being compensated by a company for promoting their product(s).

In choosing an investment manager, trustees are charged with the responsibility of finding the best person in terms of qualifications and experience to carry out their duties. Investment managers must always act prudently, meaning they must act cautiously and wisely. Maintaining confidences or giving assurances also involve qualities such as trust, reliance, or faith.

The following may help explain the meaning of the term fiduciary. An acquaintance acquired $0.75 million from an associate who was also a mortgage broker. No one, it seemed, knew the exact terms of the deal. Was it a loan? A payoff? Something for services rendered? Or what? The money, we learned, was used to purchase an old warehouse that was in need of repair and renovation. Some years later, the associate who had provided the $0.75 million was surprised, perhaps shocked and angry would be more accurate, to see the warehouse being advertised. It was being transformed into inner-city, luxury apartments. The selling price started at $1.5 million and ranged upward. The acquaintance, that is, the beneficiary who had use of the money, took legal advice and became concerned when the word fiduciary was used by his lawyer to describe his dealings with the associate who had lent him the original $0.75 million. The acquaintance, we learned, was prepared to repay that sum but was having difficulty in coming to terms with the fact that he would probably have to repay considerably more if it was proved in court that the deal had been made on the basis of it being a fiduciary business arrangement.

The aggrieved associate who had provided the money felt he was entitled to a cut on his capital outlay if the apartments were sold at a substantial profit. He insisted that the two of them had entered into a fiduciary relationship. He wanted his $0.75 million back plus a substantial add-on for the increased value of the old warehouse that was being renovated with his original loan. The case reached the civil courts after a long-drawn-out process. The legal proceedings, which seemed to drag on for years, had a detrimental effect on the beneficiary's family, who were living with the possibility of bankruptcy and being made homeless if the case went against them. It transpired that the original transaction was a fiduciary business arrangement based on trust, a trust that had since broken down. The case was eventually settled out of court and at great cost.

—Michael W. Small

See also Accountability; Authenticity; Deceptive Practices; Trust

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Fiduciary Duty

A *fiduciary* is a person who has been entrusted with the care of another's property or other valuables and who has a responsibility to exercise discretionary judgment in this capacity solely in the interest of this other person's interest. Common examples of fiduciaries are trustees, guardians, executors, agents, and, in business, directors, officers, and executives of corporations. Fiduciaries provide a valuable service for individuals who are unable for some reason to exercise control over their own property or assets. Thus, a parent facing death might provide for a dependent child by creating a trust to be managed by a trustee.

A fiduciary is part of a *fiduciary relationship,* in which another person is the *beneficiary* of the fiduciary's service. Typically, the beneficiary is in a vulnerable or dependent status and must rely on the fiduciary to act on behalf of the beneficiary. A fiduciary, on the other hand, usually occupies a superior position of power and authority, which creates opportunities to advance the fiduciary's personal interests. For example, a trustee might (improperly) invest the assets of a trust in a personal business venture.

Anglo-American law has developed the principles of a legal duty to ensure that a fiduciary in a fiduciary relationship acts solely in the interest of a beneficiary and does not take improper advantage of the position of trust. A *fiduciary duty* may be defined, then, as the duty of a person in a position of trust (a fiduciary in a fiduciary relationship) to act solely in the interests of another (the beneficiary) without gaining any material benefit except with the knowledge and consent of that other person.

Who Is a Fiduciary?

The concept of a fiduciary originated in Anglo-American common law for cases in which one person entrusts property or other valuables to the care of another, and it remains a central concept in the law of trusts. The concept has evolved over time to cover other trustlike situations where one person has superior power and influence over another and that other person places confidence in or relies on that person. A fiduciary relationship, then, involves two elements: trust and confidence. Something is entrusted to the care of a person, and another has confidence that proper care will be taken.

That which is entrusted is most often property (land, for example) or assets (such as money or securities), but it can be anything of value, including information and power. Thus, a client may entrust valuable information to an attorney or an investment banker; or a person may entrust the power to make a certain decision to another, as when someone gives another person power of attorney. Indeed, guardians and agents are fiduciaries only in virtue of being delegated the authority to make decisions on behalf of another.

The concept of a fiduciary is of ancient origin. Certain positions of trust, such as trustee and guardian, were recognized in Roman law, and the word *fiduciary,* which derives from the Latin word for trust, dates from the 16th century. The position of agent, though, developed only in the 18th century, and a great expansion in the scope of fiduciaries occurred in the 19th and 20th centuries. This expansion occurred primarily in connection with the rise of a market economy and the modern corporation since they create a great need to rely on other individuals and on large institutions.

Anglo-American law holds that directors, officers, and executives of corporations have a fiduciary duty to serve the shareholders' interest. In addition, members of partnerships and joint enterprises are fiduciaries with respect to each other's interest, and majority shareholders are fiduciaries with responsibilities toward minority shareholder in some circumstances. Mutual and pension funds are fiduciaries for their investors, and investment advisers are fiduciaries for their clients. In recent years, fiduciary law has been extended to parties such as physicians and attorneys that have not been traditionally recognized as fiduciaries. Thus, the scope of fiduciary law is constantly expanding.

Although fiduciary duties can be created by contract between two parties and have a basis in legislation, they have been imposed largely by courts. Historically, fiduciary duty belongs to the law of equity, in which courts decide cases on the basis of justice or fairness instead of strictly formulated rules. The reason for this is that the duties of fiduciaries cannot easily be specified in rules, either in written contracts or in detailed legislation. These duties are concerned more with the proper exercise of broad discretion than with the observance of the terms of a contract or a legislative act. For this reason, courts rely on certain general principles to determine whether a fiduciary has acted appropriately.

The Duty of Fiduciaries

Broadly, the duty of a fiduciary is to act in the interest of the beneficiary. This duty, which requires the subordination of self-interest, contrasts with the market conduct, in which everyone is assumed to act out of self-interest. The main principles of fiduciary duty are candor, care, and loyalty. In general, these principles involve obligations that also apply to market actors but to a higher degree for those in fiduciary relationships.

Candor

In a market, everyone has an obligation of honesty or truth-telling. It is wrong to say something false or to make a material misrepresentation. However, market actors are not required to disclose all information that others might want to know. A fiduciary, on the other hand, has a duty of candor, that is, a more extensive obligation to disclose information that the beneficiary would consider relevant to the relationship. Thus, it would be violation of a fiduciary duty for an attorney or an investment banker to conceal important information from a client (unless doing so would violate a duty to another party). Similarly, the director of a company would fail in a fiduciary duty by remaining silent about matters that are critical to a decision under discussion.

Care

When property or assets are entrusted to a fiduciary—the trustee of a trust, for example—that person should manage what is entrusted with due care, which is the care that a reasonable, prudent person would exercise. Although an extraordinary level of care is not legally required, a fiduciary is expected not to act negligently. Although market actors also have a duty of due care with respect to certain matters, this obligation governs only how the party conducts a chosen activity and not the activities that are chosen. For example, a manufacturer should exercise due care in the design and assembly of its products, but it has no responsibility of due care in the products it chooses to manufacture. A fiduciary, in contrast, has a duty to act in all matters with a high level of care. Generally, a fiduciary has a great amount of discretion in choosing how to care for that which has been entrusted, and the principle of due care for a fiduciary includes how that discretion is exercised.

Loyalty

A duty of loyalty has two aspects: It requires a fiduciary to act in the interest of the beneficiary and to avoid taking any personal advantage of the relationship. In a market transaction, there is generally no obligation to serve the interests of another except to make good faith efforts to abide by the contracts made; and gaining some personal advantage is the whole point of entering into a market transaction. In general, acting in the interest of a beneficiary is acting as the beneficiary would if that person had the knowledge and skills of the fiduciary. Taking personal advantage, in contrast, is deriving any benefit from the relationship without the knowledge and consent of the beneficiary.

An example of personal advantage-taking in a fiduciary relationship is self-dealing, as when a director or executive buys some asset from the company or sells something to it, unless it can be shown that the transaction is fair and would have occurred at arm's length. Insider trading or other personal use of confidential information gained in a fiduciary relationship is also a violation of a duty. It is wrong for a fiduciary to gain some personal benefit, even if the beneficiary is not harmed, because the fiduciary would no longer have an undivided loyalty. To have such a divided loyalty is also a conflict of interest, and so the principle of loyalty entails that a fiduciary should avoid any conflict of interest.

Conflict of interest is difficult to avoid, however, and a requirement that conflict be avoided entirely might not be desirable. For example, directors are usually officers or executives of another company, and they often serve on other boards as well. To insist that directors avoid all conflict of interest would deprive companies of knowledgeable and experienced guidance. The principle of loyalty can still be honored, though, if directors act conscientiously to exercise unbiased judgment, disclose all conflicts, and refrain from participating in some decisions.

Remedies for Violations of Fiduciary Duty

For violations or breaches of fiduciary duty, the courts have generally imposed remedies that are more far-reaching than those for mere failures to fulfill contracts. The standard remedy for breach of contract is an award in the amount of a victim's loss. However, the remedy for violation of fiduciary duty takes account not only of the victim's loss but also the wrong done by the breach; that is, the breach of a fiduciary duty is a moral and legal wrong that ought to be punished regardless of the loss to a victim. The standard remedy for violation of a fiduciary duty, therefore, is the amount of the wrongful gain by the fiduciary. Thus, even if the beneficiary is not harmed or perhaps even benefited, any amount realized by the beneficiary in a violation of fiduciary duty is wrongfully gotten gain that ought to be forfeited. That a director's action benefited a company is no defense to a charge of self-dealing, for example.

The Justification of Fiduciary Duty

To the question of why a fiduciary has a particular duty—that is, why a fiduciary should act with candor, care, and loyalty—there is a simple answer: This is what a fiduciary has agreed to do. Fulfilling a fiduciary duty is merely abiding by the terms of a contract that one has made in becoming a fiduciary and entering into a fiduciary relationship. Fiduciary duty is thus founded on a contract, and the specific obligations of a fiduciary are whatever terms are contained in this contract. This simple answer requires some further explanation, however.

Although a fiduciary relationship is founded on a contract, the contract is incomplete in important ways. The obligations of a fiduciary, or what a fiduciary has agreed to do, cannot be fully specified in advance. For example, the creator of a trust (a grantor) could not write a contract with a trustee that details every act the trustee should perform. The situations that a trustee might encounter are too varied and unpredictable to allow the grantor to give precise instructions for each one. Indeed, the grantor may not know what instructions to give and may be relying on the knowledge and skill of the trustee to determine how to act in certain situations.

The main value of the fiduciary relationship is its use in situations where complete instructions are not possible, where it is impossible, in other words, to write contracts that specify every act to be undertaken. Indeed, if such contracts were possible, then there would be no need for fiduciaries. Fiduciary relationships exist primarily to enable individuals to give control of property, information, or power to other people without complete instructions, relying instead on trust.

Some of the obligations of fiduciaries may also be imposed by legislatures. The law of trusts prescribes some rules for trustees, for example, just as the law of wills similarly prescribes some rules for executors. However, the role of legislatures in connection with fiduciary duties is mainly to anticipate some of the situations a fiduciary might encounter and to enact legislation that approximates what the contracting parties might agree to. Such legislation provides, in effect, standard-form, "off-the-shelf" contracts that save contracting parties the trouble of addressing every matter. Thus, it would be burdensome for people creating trusts or wills to include all the necessary instructions for trustees or executors, and so legislatures provide rules that, in some instances, the parties involved can alter if they choose. Much of the law on fiduciary duty is default legislation that applies unless the parties contract differently.

However, in fiduciary relationships, neither contracts nor legislation can provide complete instructions and rules for all situations. In such cases, there is a role for courts to step in to "fill in the gaps" of incomplete contracts. Fiduciary duty can be understood, then, as gap-filling judicial interpretation. To some extent, the courts fill this role with all contracts, but in most cases, the need for such gap-filling is minor. In fiduciary relationships, in contrast, much of the contract is left open with only the general objective of serving the beneficiary's interest specified. Since a fiduciary has a great deal of discretion in the choice of means, the main task for the court is to determine whether the means are appropriate for the objective and whether any abuse has occurred. These matters can best be judged by applying the general standards of candor, care, and loyalty.

The Fiduciary Duty to Shareholders

The importance of fiduciary duty in business lies principally in the question, "For whom are corporate managers fiduciaries?" To whom do directors, officers, and executives of corporations owe a fiduciary duty? The standard answer is that managers have an exclusive fiduciary duty to shareholders, which is to say that they ought to serve shareholder interests alone and should seek to maximize shareholder wealth. This fiduciary duty to shareholders has been questioned on two related grounds. One ground is that management's fiduciary duty appears to place shareholders in a privileged position in comparison with employees, customers, suppliers, and other corporate constituencies. The second ground is that a fiduciary duty of exclusive loyalty to shareholders appears to bar corporations from being socially responsible inasmuch as this involves serving other interests as well. Both concerns may be largely explained away, however.

Why a Fiduciary Duty Is Owed to Shareholders

Although many rationales have been offered for making shareholders the beneficiary of management's fiduciary duty, the standard argument begins with the assumption that each corporate constituency—employees, customers, suppliers, and investors—contracts with a firm, providing inputs needed for production in return for some gain. The firm thus becomes a nexus of all the contracts with its various input providers. Most of these contracts are relatively unproblematic, but the situation of shareholders presents difficult contractual problems. Their return on the capital they have provided consists of a claim on the residual revenues or profits of a firm, which are the revenues that remain after all debt obligations are paid. This claim on residual revenues can be secured only if management operates the firm so as to maximize residual revenues or profits, and the best way of assuring this is for shareholders to have corporate control.

The right to residual revenue and the right of control constitute the contract that shareholders have with a corporation. If shareholders also manage a firm or are able to give complete instructions to the managers, then there is no need for fiduciary duty. However, when there is a separation of ownership and control, shareholders, like grantors with respect to trustees, are unable to write complete contracts; that is, the situations likely to be encountered by managers, who have effective de facto control of corporations, are so varied and unpredictable, that shareholders, who have de jure control, cannot provide detailed, comprehensive instructions. To compensate for this inability to write complete contracts, they rely instead on the protection offered by management's fiduciary duty.

Other constituencies, in contrast, are able to form relatively complete contracts with a firm and thus have little need to be the beneficiary of management's fiduciary duty. Employees, for example, would prefer that their wages be secured by fixed claims rather than residual claims, so that the payment of wages becomes a debt obligation rather than a part of the residual revenues. Similarly, the interests of customers, suppliers, and other kinds of investors, such as bondholders, are adequately protected by relatively complete contracts, and so they also prefer fixed claims that constitute debt obligations.

Fiduciary duties thus have value primarily for residual claimants, whose return on their investment in a firm cannot be easily secured by complete contracts. Far from privileging shareholders, management's fiduciary duty to them reflects their unique vulnerability inasmuch as fixed claims or debt obligations are much more secure than are the shareholders' claim on residual revenues or profits. Put another way, fiduciary duty is a corporate governance device that is uniquely suited to filling in the massive gap that exists in the open-ended contract between shareholders and corporate directors, officers, and executives. In some situations, other constituencies may benefit from the use of fiduciary duties; for example, in U.S. law, managers are fiduciaries with respect to employee pension plans. However, such exceptions are limited.

Fiduciary Duty and Corporate Social Responsibility

Management's fiduciary duty to exercise candor, care, and loyalty in pursuing the shareholders' interest serves in practice mainly to forbid self-dealing and gross negligence. However, short of such egregious violations or breaches of fiduciary duty, managers still have broad discretion. In particular, management has broad discretion in contracting with the corporation's main constituencies or stakeholder groups, and the business judgment rule protects managers from charges of violating their fiduciary duty as long as their actions are reasonably intended to promote the shareholders' interest. Since most acts of corporate social responsibility fall well within the appropriate exercise of management's discretionary authority, fiduciary duty is not a significant legal barrier to such conduct.

—John R. Boatright

See also Agency, Theory of; Berle-Dodd Debate; Business Judgment Rule; Conflict of Interest; Corporate Governance; Corporate Social Responsibility (CSR) and Corporate Social Performance (CSP); Due Care Theory; Due Diligence; Loyalty; Shareholder Model of Corporate Governance; Shareholder Wealth Maximization; Trust; Trustees; Trusts

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FIDUCIARY NORM

The fiduciary norm is a social norm that instructs the agent acting in his or her role of agency to act solely in the interest of his or her principal, without regard for any other interests, including the self-interest of the agent. The more highly dependent the principal on the agent's tasks of agency, the more likely is the norm to be triggered and to be more strongly prescribed.

As described in the following sections, the fiduciary norm requires the agent to make full use of the agent's skills; to expend all necessary effort to serve the principal; to exclude competing interests that could adversely affect the agent's actions for the principal, hence abiding scrupulously by the promise to serve the principal with perfect fidelity; to keep confidential information relevant to the relationship confidential; to make full disclosure to the principal regarding the agency, including the existence of any potentially competing interests;

and to ensure that the agent's actions feature good conduct, that is, are not disreputable in a way that will adversely reflect on the principal.

The notion that special expectations are placed on a social actor on whom others are dependent has a long history in the common law. Indeed, the counterpart of the fiduciary norm in the law is the *fiduciary principle,* which plays a prominent role in the laws of agency, contract, and trusts. As a social norm, however, the fiduciary norm is prescribed in certain quite general social contexts of dependency, described below, whether or not the relationship of agent and principal is formal. The fiduciary principle, on the other hand, is mandated in legal relationships of agency in which the agent is at least nominally under the orders of the principal (or has contracted with a third party to serve a beneficiary's interests and must act as if the agent's activity is mandated by the contract to serve). The modern law of agency, which incorporates the expectations of the fiduciary principle, is summarized in the *Restatement of the Law Third, Agency,* published by the American Law Institute in 2006.

The fiduciary principle presumes that the agent is acting under direction and must follow that direction. Thus, corporate directors are expected to serve shareholders under the fiduciary principle because they are actors who are in a legal agency relationship with the owners, that is, they must, at least technically, follow the orders of their principals, the stockholders. As a huge case law documents, this relationship, including the failure to follow the fiduciary principle, can be enforced—sanctioned—by the courts.

The fiduciary norm is also enforced, if with less certainty and formality. The fiduciary norm does not, of course, have a legal status, such that there exist governmental enforcement agents to ensure performance consistent with its provisions. But some definitions of *social norm* require that a social instruction does not even have the status of a norm unless behavior deviant from the norm's prescriptions is sanctioned by the community. In general, such sanctions are negative, though positive ones given on correct performance of the norm are also consistent with normative status.

As a social norm, however, the fiduciary norm is prescribed via socialization from the community in which the actor is embedded, and is actively maintained by that community. Hence, its essential character assumes that, whether or not the agent is in a formal relationship of agency, for example, within an employment relationship, the agent is acting with some discretion. Thus, the agent's discretionary choice of action is shaped by the community-supported norm; the agent *constructs* both the instruction of agency and the acts necessary to realize that agency. This is qualitatively different from the situation in which the question is whether or not to perform at a high level in response to a direction from the principal under a formal agreement with that principal, even though the level of response is discretionary, that is, the classic situation of the fiduciary principle.

In Stanley Milgram's famous experiments on obedience to authority, subjects follow experimenter directions to administer what they think are painful shocks to others. The issue is obedience, given knowledge of the consequences. This is not the same situation as the fiduciary norm, in which the question becomes how the agent will choose to fill in the discretion that she or he possesses to act for the principal. As noted and discussed at more length below, the agent's behavior under the fiduciary norm can be even more extreme because it can exceed the principal's initial request. In the Stanford Prison Experiment conducted by Philip Zimbardo, role-playing "guards"—agents—who had received only general instructions developed abusive behaviors toward the "prisoners." Their creative cruelty seems more consistent with the fiduciary norm than with what would have been generated by simple obedience to authority. Thus, ironically, both ethically best and worst behaviors under agency can follow from the operation of the norm.

The relationship between agent and principal under the fiduciary norm is at least abstractly one of contract, as it is in the case of the fiduciary principle and legal agency, but the contract may be informal in character so that there is mutual consent by principal and agent that the agent is to act for the principal. The situation may be distinguished from cases in which the consent by the principal is sequential, for example, that of the altruist or good Samaritan who rushes to the aid of a highly dependent principal who is unable to contract for the critical services voluntarily performed by the agent. Related social norms, including those of giving and helping, apply to such circumstances.

Some Examples

Examples of the fiduciary norm in operation are pervasive across many societal roles. They include situations as diverse as the following:

- A father agrees to bring back chocolate ice cream for his children for dessert. Finding the corner store out of chocolate, he drives five miles to buy it at a market certain to have chocolate, rather than trying another local store that may or may not have it. No one needs to ask him to drive the extra miles. If he were to come home with vanilla, his wife and children would tell him how much they were "depending" on him to bring chocolate and how disappointed they were in him because he did not put out the extra effort to try to get it elsewhere.

- A professor agrees to supervise an independent study course for a student who needs the credits to graduate. The professor creates a syllabus, discusses its content regularly with the student, and grades the student's paper. Teaching credit for independent studies is not given in the professor's department, but the department chair and the professor's colleagues make it known that they are aware and applaud the fact that the professor "went the extra mile" with the student.

- A doctor known for expertise in a particular developmental disability receives a phone call from parents of a newborn with the disability, born in another city. The phone call went to her office, but she takes the call, transferred from an assistant who answered the phone. The parents have specific questions about problems the child is having. After checking on some research, the physician calls the parents back in the evening of the same day. She does not get paid for this. Interns and residents in the doctor's specialty area are made aware that such behavior will be expected of them once their training is complete.

- Even while not under the direct supervision of their commanders, prison camp guards are observed to act with surprising cruelty when making discretionary choices about punishments or privileges to be given prisoners.

In each case, the agent chooses to go "above and beyond" in serving his or her dependent or vulnerable principal because it is uncertain whether ordinary levels of service will achieve the principal's goal, and, because of the norm and its sanctioning, it is unacceptable to the agent to fall below the principal's desired level of agent performance—*fiduciaries try to be "perfect" agents.* This assumes, of course, that provision of higher levels of service is indeed always preferred by the principal.

Such behavior illustrates a typical result of action by agents under the fiduciary norm: The use of the agent's skills with appropriate effort and without distracting, conflicting interests is not the only outcome from the norm. In addition, we get a tendency toward maximizing (or, at least, increasing) the level of service, given uncertainty, to ensure that the actual performance at least meets the principal's wishes. In an uncertain world, fiduciaries get us not only closer but sometimes beyond what was initially defined as *perfection.*

Note that because social norms are socially reinforced, the self-interest of the agent is not completely discarded, though it is not allowed to limit the agent's action for the principal. It enters as agents seek to avoid sanctioning for failing to serve the principal as a fiduciary. Thus, it acts as a spur to exceptional service for the principal.

Prescriptions of the Fiduciary Norm

The fiduciary norm was first identified as such—as a social norm, rather than only as a prescription in the common law—by Barry Mitnick in 1973. In 1975 (revised and published in a 1986 book), Arthur Stinchcombe independently discussed such a norm, placing it in the context of other norms of exchange, including norms of status and authority as well as the fiduciary norm. Other work on the fiduciary, both in its legal contexts and as a general social norm, has followed in the legal literature and elsewhere in social science. The discussion follows Mitnick's analysis of the norm.

The fiduciary norm is prescribed under the following conditions: (1) The norm applies to an actor, the agent, who *consents* to act for another actor, the principal. Thus, the norm occurs in mutually consensual, that is, contractual, relationships between agent and principal, though the contract may, but need not, be formal as in common business contracting. (2) The principal depends on the agent's actions. In other words, the principal is vulnerable to the agent's actions. (3) The agent is able to make *choices* of actions that affect the level of benefit received by the principal, that is, the agent has a degree of *discretion* over the return that the principal gets from the relationship. Thus, it is not just that what the agent does can affect the principal in different ways, depending on what the agent does; it is that the agent can *choose* acts that affect the principal differently. This is important because it permits aspects of the agent's preferences to shape his or her action for the principal.

The fiduciary norm instructs the following behaviors:

- The agent following the fiduciary norm (hereafter, *the fiduciary*) must act diligently for the principal's interests. This includes both the use of the agent's skills and the application of adequate levels of effort to the agency. Because the agent has discretion, she or he has by definition a range of actions that may be selected in the agency. Thus, lacking complete direction from the principal, the agent acting under the norm must diligently evaluate available actions and choose those actions that will result in better outcomes for the principal. The more that the principal depends on the agent, that is, the greater the discretion of the agent, the greater the prescription of the norm. Thus, agents for highly dependent principals, such as elderly or disabled principals, or principals unable to take any actions to oversee or correct the agent's work, must take extra care in acting for their principals.

- The fiduciary must allow only the principal's interests, as he or she sees them, to guide his or her actions. No other interests must be allowed to influence his or her decisions, including the self-interests of the fiduciary. Note that the agent had consented to act for the principal and that that consent may have been influenced by the provision of advance compensation to the agent. But once consent has been given, no self-interest must figure in the agent's actions. If the agent erred in calculating the benefits that the agent would receive in becoming agent, then the agent must live with his or her choice and choose the best actions for the principal. This component of the fiduciary norm is reinforced by another social norm, *valid agreements should be kept,* a norm described by Stewart Macaulay in his widely cited article on noncontractual relations in business. Thus, once the agreement is made to act for the principal, it constitutes a promise that must be kept.

The sensitivity of the charge given to a fiduciary, whether in the context of the legal principle or of the norm, is illustrated by the oft-cited remarks of Chief Judge Benjamin Cardozo in *Meinhard v. Salmon,* 249 N.Y. 458 (1928): "Many forms of conduct permissible in a workaday world for those acting at arm's length, are forbidden to those bound by fiduciary ties. A trustee is held to something stricter than the morals of the market place. Not honesty alone, but the punctilio of an honor the most sensitive, is then the standard of behavior. As to this there has developed a tradition that is unbending and inveterate."

The fiduciary norm incorporates such an instruction, but because it is a social norm there is an additional, sometimes subtle effect. The adoption and implementation of social norms are positively and/or negatively sanctioned by the community. Such sanction obviously bears on the agent's self-interest. No pure fiduciary should allow the possibility of community sanctions for performance (or for less-than-adequate performance) to influence the agency. But, as described below, real-world agents may logically perceive no conflict if they resolve the question of social sanctions by overperforming on behalf of the principal, while assuming that the principal will then be even better off.

- Several subnorms accompany the fiduciary norm. They tend to protect the principal and are prescribed at the same time as the fiduciary norm:
  - Confidentiality: The fiduciary must not reveal information that is confidential in his or her relationship with the principal.
  - Full disclosure: The fiduciary must reveal to the principal all information not received confidentially from other sources that bear on the agency actions. This includes revealing all interests of the agent that may conflict with the principal's interest.
  - Good conduct: The fiduciary's behavior must not draw criticisms or be disreputable, so that the principal's relationships with third parties are not compromised, and so that good relations between the agent and the principal may be maintained.

Consequences of the Fiduciary Norm

Several consequences follow from implementation of the fiduciary norm:

- Because the fiduciary norm is a true social norm, its implementation is monitored and sanctioned by the community. This monitoring can lead to requests for justification—to give accounts that support that the agency actions did in fact serve the principal with primacy, diligence, and lack of bias from conflicting interests. In addition, the norm carries with it the obligation to make full disclosure to the principal, so that a means of justification must be created to provide both to the principal and to external monitors. Thus, operation of the fiduciary norm typically generates a trail of account-giving and of defensive reporting.

- The fiduciary norm allows principals to economize on the costs of specifying actions to their agents and of policing them afterward to ensure adequate performance. This makes it possible for social systems to shift the burdens of action to agents, removing the need for principals to invest in training themselves in the expertise that would otherwise be necessary to either directly implement or evaluate the performance of agents. It is thus a way of dealing with problems of adverse selection, the condition that occurs when principals can observe their agents but cannot judge whether the agents' performance is optimal in reaching the principal's goals. In adverse selection, self-interested, perhaps lazy, agents conceal the fact that they are shirking in their agency task, knowing that the principal is unable to detect the difference. Thus, with the fiduciary norm instructing the behavior of their agents, social organizations can function more efficiently and effectively.

- When agency tasks are repetitive, the fiduciary may adopt prepared programs of action that improve his or her performance as agent. In addition, such programs may economize on the fiduciary's costs in service if the fiduciary is imperfect in adherence to the norm's prescriptions and wishes to keep the costs of agency low. Of course, the agent may have agreed to perform the agency with the programs in mind, so adoption of fiduciary programs may be completely consistent with the contracted agency and not be an imperfect action reflecting economizing during service for the principal. Such programs also isolate the fiduciary from pressure to make adaptations if the service to the principal is objectionable to third parties: The fiduciary can offer the excuse that, in following the prepared program, the fiduciary is "only following orders." The fiduciary can also disengage his or her own involvement in the agency; the actions of the program may be seen as not the result of active choice by the agent—it is the principal's program, not the agent's. Hence, we see agents acting with diligence in implementing prepared programs of action for the principal, with seeming disregard for the effects of such programs on others.

- In an imperfect world, with imperfect information, the fiduciary will often tend to maximize the return to the principal (at least to increase the return over the nominally set level). The maximization can go beyond that point at which the principal would stop, were he or she acting for himself or herself, fully informed, and could intervene, and beyond the point at which the fiduciary would stop if the principal's interest were his or her own. These behaviors may occur for the following reasons, taken together, though some may work by themselves to increase the return sought by the agent for the principal:
  - Because the norm prescribes action most strongly where discretion is greatest, yet that situation is one in which the principal is least able to convey his or her detailed preferences to the agent, the agent will err on the side of increasing returns to the principal.
  - The valid agreements norm reinforces the agent's contractual promise to act. With discretion and imperfect information about the principal's preferred stopping point, fiduciaries will err on the side of increasing returns to the principal.
  - The fiduciary has a task simpler than that of agent alone—he or she must serve only the principal; other agents may take account of more complex and/or competing interests. Hence, the agent will be less likely to be diverted from devoted service to the principal's interest.
  - Lacking complete information about the principal's preferences, the fiduciary will assume the most common forms for that preference, for example, making the assumption that, for the principal, "more is always better." With a simple goal, the fiduciary may construct a fiduciary program that generates returns to that goal, with no means of restraining its production of outcomes for the principal.
  - If the action for the principal is episodic or idiosyncratic, rather than repeated or continuous, there is less opportunity for the principal to intervene and instruct the fiduciary to keep returns to a lower level. Thus, the effect toward overreturn to the principal can occur both in the case of repeated actions (preparation of prepared programs) and with idiosyncratic cases (principal is unfamiliar with the actions taken by the agent and so cannot intervene).
  - Because it is a social norm, the fiduciary norm's implementation is sanctioned, positively or negatively, by the community. Thus, although the agent may not allow competing interests, such as the effects of community sanctions on the agent, to interfere with his or her agency for the principal, the sanctions may under uncertainty lead the agent to overproduce return to the principal. The agent reasons that by "going above and beyond" the principal will receive increased benefit at the same time that the agent escapes social condemnation or receives social approbation. In essence, both win. The agent's logic fails if his or her judgment of the structure of the principal's preferences is incorrect (i.e., more is not better to the principal) or if the agent's excesses are obnoxious to third parties (though still perhaps successful as agency).
  - The costs of supervision and policing by the principal may make it irrational for the principal to intervene and request a lower return from the agent's actions; that is, it does not pay the

principal to intervene—the costs of doing so can exceed the benefits that would follow. Hence, supranormal levels of service can be rationally tolerated.

It is evident that the use of fiduciaries can bias systems to overproduce returns to the principal. And thus a social mechanism implemented to provide quality of service can produce a service that goes beyond what is socially desirable. The ethical consequences of such extreme service are well described in accounts of discretionary responses to authority in social settings as diverse as those involving concentration camp guards, soldiers in wartime, and organizational/bureaucratic functionaries producing unsafe products.

—Barry M. Mitnick

See also Adverse Selection; Arrow, Kenneth; Asymmetric Information; Authority; Conflict of Interest; Corporate Moral Agency; Fiduciary Duty; Incentive Compatibility; Moral Agency; Moral Hazard; Transaction Costs

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Finance, Ethics of

Finance is concerned broadly with the generation, allocation, and management of monetary resources for any purpose. It includes *personal finance,* whereby individuals save, invest, and borrow money to conduct their lives; *corporate finance,* whereby business organizations raise capital, mainly through the issue of stocks and bonds, and manage it to engage in economic production; and *public finance,* whereby governments raise revenue by means of taxation and borrowing and spend it to provide services for their citizens. This financial activity is facilitated by *financial markets,* in which money and financial instruments are traded, and by *financial intermediaries,* such as banks and other financial service providers, which facilitate financial transactions.

Ethics in finance consists of the moral norms that apply to financial activity broadly conceived. That finance be conducted according to moral norms is of great importance, not only because of the crucial role that financial activity plays in the personal, economic, political, and social realms but also because of the opportunities for large financial gains that may tempt people to act unethically. Many of the ethical norms in finance are embodied in laws and government regulation and enforced by the courts and regulatory bodies. Ethics plays a vital role, however, first, by guiding the formation of laws and regulations and, second, by guiding conduct in areas not governed by laws and regulations. In general, moral norms reflect the conduct in financial activity that follows from fundamental ethical principles.

A Framework for Finance Ethics

Most financial activity takes the form of *financial contracting,* in which two parties come to some mutual agreement. For example, bank loans and stock trades are each kinds of contracts. Because so much financial activity consists of contracting, the ethical norms that apply in finance can be groups under two main heads: *fairness in making contracts* and the *observance of contractual obligations.* Virtually the whole of ethics in finance can be reduced to two simple rules: "Be fair (in making contracts)!" and "Keep your promises (made in contracts)!"

Although the ethical issues that arise in finance are numerous, they, too, can be grouped under a few main heads. These heads are as follows: financial markets, financial services, and financial management. The main ethical concern in financial markets, such as stock markets, is that they be *fair,* especially in cases of *asymmetry,* which occur when parties have unequal information or power. Ethical issues in the financial services industry and in the financial management of corporations mainly involve *agents,* who have an obligation to act in the interests of other parties, called *principals,* and *fiduciaries,* who have a *fiduciary duty* to act in the interest of *beneficiaries.* When agents and fiduciaries have a personal interest that interferes with their ability to serve others, they are said to have a *conflict of interest.*

Financial Markets

In financial markets, money and financial instruments, such as stocks, bonds, futures, options, and derivatives, are issued or traded. Generally, this activity is conducted in organized markets or exchanges, such as stock or bond markets or foreign exchange markets. However, many financial transactions, including the purchase of financial products, such as mutual funds or insurance policies, and private exchanges between two parties can be viewed as taking place in a market.

Market activity of any kind may be criticized as unfair. Unfairness in financial markets is commonly ascribed to unfair *trading practices* (most notably, fraud and manipulation), the *conditions* under which a trade is made (which are often described as an *unlevel playing field*), and difficulties in the *contracting process* (that is, in forming, interpreting, and enforcing contracts). Fairness or unfairness in financial markets may be further classified as *substantive* or *procedural*. A stock trade, for example, is fair in substance when the price reflects the actual value of the shares. It is fair in procedure when the trading parties have sufficient opportunity to accurately determine the value of the shares. Thus, "blue-sky laws," which require expert evaluation of securities offered for sale, aim at substantive fairness, whereas regulations that merely require disclosure of relevant information aims at procedural fairness.

Trading Practices

Fraud in a financial trade or transaction is committed when one party makes a material misstatement or omission that the other party reasonably relies on to his or her detriment. Fraud thus has three elements: a false statement about or the concealment of a significant fact; reliance by the victim of the fraud on the information provided; and some harm to the victim. Fraud is an unfair trading practice because the perpetrator uses dishonest means to induce the victim to make a trade that he or she would not otherwise make. Whereas fraud creates a false impression by means of a false statement (or an omission), manipulation deceives others by creating a false impression. In a so-called pump and dump scheme, for example, a trader buys a thinly traded stock to drive up the price (pumps) and then sells at the artificially created high price (dumps). Some large institutional investors have been accused of manipulating markets by creating volatility that they can exploit with sophisticated trading strategies.

Fair Conditions

A fair market, like a fair sports contest, requires a level playing field in which no one has an unfair advantage. A financial market may be unfair or unlevel because of inequalities in information, bargaining power, resources, and processing ability or because of special vulnerabilities. Unequal information, or *information asymmetry,* results when two parties either do not *possess* the same information or do not have the same *access* to information. Neither kind of information asymmetry is necessarily unfair; market participants inevitably differ in their possession of and access to information. However, it is wrong under some conditions to take advantage of another's ignorance or weakness. Thus, the law requires that issuers of securities (stocks and bonds) or financial products (a mutual fund, for example) provide a prospectus that offers sufficient information for buyers to make informed decisions. Insider trading—which is trading by a person inside a publicly held corporation on the basis of material, nonpublic information—is illegal, in part, because the parties on the other side of the transaction, being outsiders, cannot obtain the same information. The insider is thus taking unfair advantage of a privileged position.

In general, it is unfair to take advantage of different conditions when doing so violates some right or obligation. Thus, a prospectus is required for the issuance of securities because the buyers have a right to make an informed decision. In cases of insider trading, the insider is usually violating a fiduciary duty to the corporation not to use confidential information for personal gain. Laws that impose a "cooling off" period during which a buyer can cancel a large purchase or loan may be justified on the ground that it is wrong to take advantage of people's impulsiveness or inexperience. In other words, people have a right not to be taken advantage of in certain ways.

Financial Contracting

Contracts are often vague, ambiguous, and incomplete, with the result that disagreements arise about what is ethically and legally required. *Implied* contracts, which are unlike *express* contracts in that not every detail is put into writing, can usually be violated without any legal consequences. Most contracts are *imperfect* or incomplete either because it is not worthwhile to specify every detail or because it is impossible to do so given uncertainty about the situations that might arise. These "gaps" in imperfect contracts are commonly "filled" by relying on good faith efforts or fiduciary duties, both of which may be unreliable. Finally, contracts often fail to specify what constitutes a breach or how a breach should be remedied. In all such cases, ethical issues arise over the obligations of the parties to the contracts they have made. Because contracting by means of perfect, express contracts may be difficult, some parties rely instead on *relational contracting,* which involves building good working relationships.

Financial Services

Financial service firms—which include banks, brokerage firms, mutual and pension funds, and financial planners—act primarily as financial *intermediaries* by enabling their clients to consummate transactions rather than by engaging in transactions themselves. In acting as intermediaries, these firms become *agents* or *fiduciaries* with certain obligations or duties. In addition to the ethical issues that arise for agents and fiduciaries, financial service firms are engaged in selling various services and products to their customers or clients and thus encounter ethical issues in their sales practices and other operations.

Agents and Fiduciaries

In an agency relationship, one party (the agent) is engaged to act on behalf of another (the principal) and to serve that other party's interest. For example, a homeowner may hire a real estate agent to handle the sale of a house because the real estate has knowledge and skills that the homeowner lacks. In selling the house, the real estate agent is duty bound to act as the homeowner-principal would if that person possessed the agent's knowledge and skills. In this relationship, the agent has agreed—for a fee, of course—to forgo any personal interest and to act solely in the interest of the homeowner in all matters connected with the sale of the house. Thus, an agent owes a duty of *loyalty* to a principal in all matters within the scope of the engagement.

A fiduciary is a person who has been entrusted with the care of another's property or other valuables and who has a responsibility to exercise discretionary judgment in this capacity solely in the interest of the intended beneficiaries. Common examples of fiduciaries are trustees, guardians, executors, and, in business, directors and executives of corporations. Fiduciaries provide a valuable service for individuals who are unable for some reason to exercise control over their own property or assets. Thus, the pension funds of retirees are commonly controlled by trustees, who, like agents, have a duty of loyalty. Fiduciary duty is especially valuable in situations like those of directors and executives of corporations in which it would be difficult, if not impossible, for the intended beneficiaries—the stockholder, in this case—to specify precisely what should be done. As a result, considerable discretion must be allowed a fiduciary.

Although fiduciary relationships are similar to agency relationships, they are also characterized by a stronger duty to act in the interests of others as well as more latitude or discretion in serving the beneficiaries' interests. Whereas agents are generally engaged by a contract to perform specific tasks, fiduciaries assume positions of trust to exercise judgment about a broader range of matters. The duty of loyalty of a fiduciary is thus more open-ended and comprehensive than that of an agent. In addition, fiduciaries are specifically barred from gaining any material benefit from the relationship without the knowledge and consent of those the fiduciary serves.

Financial service professionals are almost always agents and frequently fiduciaries in their relations with customers and clients. For example, a stockbroker is an agent, but not a fiduciary, when he or she agrees to execute a stock trade for a client. Such a broker is acting merely as an intermediary in a particular transaction. However, a broker who manages a client's portfolio by offering financial advice and especially a broker who has the authority to trade on the client's behalf become a fiduciary as well. In contrast, a broker who merely recommends a stock to a client is acting as a salesperson and not as an agent or fiduciary, although the broker still has the moral obligations of any salesperson to avoid deception and offer only suitable products.

Opportunism

Agency and fiduciary relationships are subject to two well-known problems: *opportunism* and *conflict of interest.* Opportunism or shirking refers to the tendency of agents or fiduciaries to slack off and not expend the full amount of expected effort. This phenomenon, which is central to agency theory, occurs when principals are not able or willing to monitor the behavior of their agents. A client cannot easily monitor a stockbroker, for example, and the cost of doing so, even if it could be done, might exceed the benefit. As a result, the stockbroker might take advantage of the opportunity to increase his or her compensation by engaging in excessive trading of a client's portfolio, a practice known as *churning.* Similarly, a CEO might seek to acquire other companies, not because doing so benefits shareholders but because it expands the CEO's compensation and power, a practice called *empire building.*

Opportunism can be reduced by a number of measures besides closer monitoring. One of these involves changes in the incentives of the agent or fiduciary. For example, the self-interested incentives of brokers to churn client accounts can be countered by basing compensation on the performance of clients' portfolios rather than the volume of trades. Similarly, compensating CEOs with stock options aligns their interests more closely with those of shareholders and thus reduces the incentives to engage in empire building. Other means are to increase the sense of professionalism of agents and fiduciaries, which may involve the adoption of codes of ethics, and to use moral suasion to emphasize their ethical and legal responsibilities.

Conflict of Interest

A conflict of interest is a situation in which a person has an interest that interferes with that person's ability to act in the interest of another when that person has an obligation to act in that other person's interest. Agents and fiduciaries are called on to exercise judgment on behalf of others, and their judgment can be compromised if they stand to gain personally from a decision. Unlike opportunism, which involves merely the natural human tendency to act self-interestedly, conflict of interest arises when a person acquires an interest that competes with the interests an agent or fiduciary is pledged to serve.

A conflict of interest is created, for example, when brokers are offered a higher commission for selling a firm's own in-house mutual funds than for selling the funds of other firms. A conflict of interest is present in such cases because the broker, who has a duty to serve the clients' interests, has a countervailing incentive to sell a fund that may not represent the best value for clients. Mutual fund managers who also trade for their own account face a conflict of interest since they can direct especially attractive trades to their own account instead of the funds they manage. Analysts for an investment bank may also have a conflict of interest if they are involved in the bank's deals because the analysts' recommendations, which should be objective, might be influenced by a desire to attract and retain clients for the bank.

Conflict of interest can be managed by many means, including avoidance, that is, not acquiring any conflicting interests. Thus, a brokerage firm can avoid conflict of interest by not offering higher commissions for in-house mutual funds; a mutual fund can also avoid conflicts by not allowing fund managers to trade for their own account; and an investment bank can prohibit analysts from participating in its deal-making business. When avoidance is not practical, conflict of interest can also be managed by requiring disclosure on the assumption that when a conflicting interest is disclosed, other parties can take steps to protect themselves. A conflict of interest may also be managed by requiring a person with a conflict to recuse and not take part in a decision. Conflicts of interest can also be managed by fostering a greater sense of professionalism so that agents and fiduciaries appreciate the importance of exercising objective and independent judgment.

The Financial Services Industry

Financial services firms operate as businesses, and like any business, they have an obligation to observe the accepted standards of ethical business conduct. Thus, in their sales practices, firms should avoid deception and provide adequate information about products and services. Some advertising for mutual funds, for example, has been criticized for exaggerating a fund's past performance, omitting sales charges, and downplaying the level of risk. The generally accepted standard for disclosure is *materiality,* which refers to information that a reasonable or prudent investor would consider important in making a decision. Financial service professionals also have an obligation to recommend securities and products that are *suitable* for the client. This suitability requirement is violated by abusive practices such as *twisting* and *flipping.* Twisting occurs when an insurance agent persuades a client to replace an existing policy with a new one merely to generate a commission, and flipping is the practice in banking of inducing a customer to replace one loan with another to generate additional fees.

In the financial services industry, it is common for firms to require both customers and employees to sign a predispute arbitration agreement (PDAA) that commits them to submit all disputes to binding arbitration. Although arbitration has many benefits over litigation (that is, bringing suit in court), some critics consider mandatory arbitration to be unfair because it may deny customers and employees adequate protection. This is especially true if arbitration panels, as is sometimes alleged, have an industry bias. In addition, customers such as credit card and insurance policy holders generally have no choice when signing a PDAA as a condition for making an application. Mandatory arbitration for employees denies them the right that other employees have to sue in court over matters such as harassment or discrimination.

Bank lending practices have many impacts that raise ethical concerns. If banks refuse to issue mortgage loans for homes in distressed areas of a city, a practice known as *redlining,* then they contribute to further urban decay. Redlining has been addressed in the United States by the Community Reinvestment Act of 1977 and subsequent legislation that require banks to meet the credit needs of people in their service area. Large banks that finance massive infrastructure projects such as dams and pipelines in less developed countries have been criticized for failing to evaluate the impact of these projects on the local people. Cases in which banks have financed the fraudulent transactions of companies such as Enron raise questions about their responsibilities. Do banks have an obligation to act as "gatekeepers" when they have the ability to detect and prevent fraud by their clients?

Mutual and pension funds have an opportunity to enable investors to satisfy their desires to do good with their investments or at least to avoid profiting from businesses of which they disapprove. So-called ethical or socially responsible investment (SRI) funds use negative screens to avoid the stocks of companies with certain products, most commonly tobacco, alcohol, gambling, nuclear energy, and military weapons, or that have an objectionable record of social responsibility. In some cases, SRI funds also use positive screens to seek out companies that exhibit notable social responsibility. Some SRI investors hope, through their investments, to influence the behavior of corporations; others seek merely to avoid being complicit in certain kinds of activities. However, it is questionable whether SRI, in fact, has any impact on corporate behavior or whether profits from the makers of certain products really are morally tainted. In any event, it is morally permissible for investors to seek out SRI funds and for firms to offer such funds as long as there is full disclosure. Some critics contend, though, that the screening done by SRI funds is arbitrary, inconsistent, and largely ineffectual, with the result that SRI investors may be misled.

Financial Management

Financial managers, especially the chief financial officer (CFO) of a firm, have the task of raising capital for a corporation and determining how that capital is to be deployed. In a sense, a CFO is making investment decisions and developing a portfolio, but these decisions are not about which securities to hold but about what business opportunities to pursue. A corporation can be understood, then, as a portfolio of lines of business that can be bought and sold. Capital budgeting is making decisions about which businesses to invest in and how much to invest. Every firm must also have a financial structure in which its capital is divided between equity, debt, and other types of obligations. All these decisions are guided by a single corporate objective: to maximize shareholder wealth.

Ethical issues in financial management fall into two broad categories: the ethical obligations or duties of a financial manager of a corporation, and the ethics of organizing a corporation with shareholder control and the objective of shareholder wealth maximization. The former category bears on decisions made by financial managers, whereas the latter is a matter largely for government in establishing the laws of corporate governance.

Duties of Financial Managers

Financial managers are agents and fiduciaries who have a duty to manage the assets of a corporation prudently, avoiding the use of these assets for personal benefit and acting in all matters in the interest of the corporation and its shareholders. Specifically, this duty prohibits unauthorized self-dealing and conflict of interest, as well as fraud and manipulation in connection with a company's financial reporting and securities transactions.

It may be noted in this regard that the CFO of Enron allegedly committed all these offenses by personally benefiting from partnerships that he created to do business with Enron, serving as a principal of these partnerships while acting as CFO (although this conflict was approved by Enron's directors), hiding debts in these partnerships, which properly belonged on Enron's balance sheets, and preparing false reports that misrepresented Enron's financial condition. Although Enron is an exceptional case, the use of financial engineering through the use of off-balance-sheet partnerships and complex derivative transactions, not only to manipulate earnings but also to avoid government regulations, is a common practice that raises significant ethical and legal questions for financial managers. Even when accounting rules are satisfied, financial engineering may facilitate a lack of transparency that prevents investors from being fully aware of a firm's true financial condition.

To meet these possible failings in financial management, Section 406 of the Sarbanes-Oxley Act, passed in 2002 in response to the scandals at Enron and other companies, requires publicly held companies to adopt a code of ethics for senior financial officers that includes, among other elements, standards for honest and ethical conduct, including the ethical handling of conflicts of interest, full, fair, accurate, timely, and understandable disclosure, and compliance with applicable governmental rules and regulations.

In addition to a financial manager's duties as an agent and a fiduciary, there are other areas in which ethical judgment is called on, most notably in determining a level of risk, declaring bankruptcy, and responding to takeover offers. Although these matters involve financial management, the responsibility for decision making generally rests with the CEO and the board of directors.

Risk

Any business firm must determine an appropriate level of risk, and generally greater rewards require greater risk. Usually, shareholders, whose wealth is not tied closely to any one firm, prefer that corporations in their portfolio assume a higher level of risk than is favored by managers and employees, whose wealth is heavily dependent on one firm. Finance theory also suggests that for properly diversified shareholders, the level of risk for any given firm, called *unique risk,* is irrelevant and that only *market* or *systemic risk* is important. Shareholders might even support a strategy that courts bankruptcy if the returns are high enough. For these reasons, financial managers serving only shareholder interests might be led to pursue a very high-risk strategy. However, such a strategy poses dangers for employees and suppliers, as well as bondholders and managers themselves, who place a high value on the continued operation of the corporation as an ongoing entity. At issue, then, is the question, "Is it ethical for financial managers to increase risk in a firm so as to benefit shareholders at the expense of other parties?"

Bankruptcy

If a firm is truly insolvent, then bankruptcy may be forced on it, but entering bankruptcy can also be a means for achieving strategic ends. The bankruptcy code in the United States has been used by companies to avoid or reduce the payment of heavy legal judgments and to void or renegotiate collective bargaining agreements and other onerous contracts. Some solvent but unprofitable corporations enter bankruptcy to gain additional leverage with employees, creditors, and other groups as part of a reorganization. In such situations, bankruptcy is a strategic choice rather than an unavoidable condition. Although such strategic bankruptcy may save companies (think of some American airlines), critics have charged that such strategic bankruptcies are an abuse of the Bankruptcy Code.

Takeovers

Corporate takeovers often affect many groups, including employees who may lose jobs and local communities, their economic base. Bondholders often suffer when the debt incurred in the takeover, especially a highly leveraged buyout, lowers bond ratings. Some critics argue that directors, who generally have a fiduciary duty to act solely in the shareholders' interest, ought to be able to consider the interests of all affected parties. Some states have antitakeover laws and so-called other constituency statutes that permit consideration of a wider range of interests. Moreover, incumbent management has many defenses, including poison pills, golden parachutes, and greenmail, which may also be criticized on ethical grounds. Insofar as takeovers are conducted in a market through the buying and selling of shares, there is a market for corporate control. Broadly speaking, the rules for this market should be fair to all parties and provide a level playing field, but some critics of hostile takeovers question whether such important decisions as corporate control should be made in the marketplace.

The Corporate Objective

That a corporation should have the objective of maximizing shareholder wealth has been questioned by some critics, who hold that an exclusive pursuit of shareholder interests unjustly neglects the interests of other corporate constituencies. The argument for this objective of shareholder wealth maximization, as well as for the fiduciary duty of management to serve shareholder interests, is, in brief, that shareholders, who provide equity capital to a firm in return for the residual income or profits, ought to have control because this is the best means for securing their return. Other constituencies—employees who are compensated with wages, suppliers whose bills are paid, and bondholders, who receive principal and interest payments, to mention three of these constituencies—have little need for control. Shareholder control also benefits other constituencies automatically because only residual risk bearers have an incentive to operate the firm for maximum profitability and because their assumption of residual risk insures the return of all other stakeholder groups.

This argument is open to criticism, first, by those who reject the economic view of the firm that underlies it and adopt a communitarian view of the firm. Whereas the economic view considers the firm to be like a market, the communitarian position is that the firm is more like a community. Stakeholder theory, which maintains that a corporation ought to serve the interests of all those with a stake in the firm, also rejects the economic view. Second, the pursuit of shareholder wealth maximization may lead to social costs, such as pollution and urban blight, and also to an unequal distribution of wealth. Advocates of shareholder wealth maximization do not deny these consequences but hold that these problems are better addressed by means other than changes in the corporate objective.

—John R. Boatright

See also Agency, Theory of; Arbitrage; Asymmetric Information; Bankruptcy, Ethical Issues in; Blue Sky Laws; Chief Financial Officer (CFO); Churning; Community Reinvestment Act of 1977 (CRA); Conflict of Interest; Corporate Governance; Disclosure; Enron Corporation; Fiduciary Duty; Financial Derivatives; Fraud; Golden Parachutes; Insider Trading; Leveraged Buyouts; Manipulation, Financial; Market for Corporate Control; Mergers, Acquisitions, and Takeovers; Prudent Investor Rule; Sarbanes-Oxley Act of 2002; Securities and Exchange Commission (SEC); Securities Industry Association; Shareholder Model of Corporate Governance; Shareholder Wealth Maximization; Socially Responsible Investing (SRI); Soft Dollar Brokerage; Stakeholder Theory; Wealth Creation

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Financial Accounting Standards Board (FASB)

The Financial Accounting Standards Board (FASB) is a subsidiary of the Financial Accounting Foundation (FAF), an independent exempt organization. The FASB sets standards for financial accounting and reporting in the United States, a set of guidelines that constitutes an important component of generally accepted accounting principles (GAAPs). Although the Public Company Accounting Oversight Board (PCAOB) has superseded the FASB in formal standard-setting authority over the profession since the enactment of the Sarbanes-Oxley Act in 2002, the FASB continues to wield significant influence as a private-sector advisory body.

Historical Background

The Securities Act of 1933 provided for federal regulation of financial accounting and reporting for public companies and, by extension, for the practice of public accounting in the United States, and it invested this authority in the Federal Trade Commission. In the Securities Exchange Act of 1934, Congress created the Securities and Exchange Commission (SEC) and assigned it responsibility for this regulatory oversight. Between 1936 and 1938, the SEC moved to delegate this responsibility back to the private sector, on the premise that the accounting profession's decades of leadership in the development of the practice and theory of accounting enabled it to discharge this responsibility efficiently, effectively, and in the public interest.

A succession of private entities took up this regulatory task. The first was an agency of the American Institute of Certified Public Accountants (AICPA), the Committee on Accounting Procedure (CAP), which operated from 1936 through 1959. It issued more than 50 accounting research bulletins, but its modular, ad hoc approach to issues did not lend itself to developing a conceptual framework for financial reporting standards. The AICPA organized its successor, the Accounting Principles Board (APB), in 1959 to develop such a framework. Although the APB issued 31 opinions, it garnered little prestige, due, in part, to perceptions that it was not sufficiently proactive and productive, and it eventually ceased operating in 1973.

After review by the Study Group on the Establishment of Accounting Principles (the "Wheat Committee"), the accounting profession in 1973 established a new institutional apparatus to develop a conceptual framework and to promulgate standards for financial accounting and reporting, including a third private organization to assume this role, the FASB. Independence from other business organizations and professional associations was a distinctive feature of this apparatus from the beginning, and this helped the FASB gain early official recognition from the SEC and the AICPA as a standard setter. At the same time, to avoid disruptions for preparers, auditors, and users of financial reports, the FASB provided a bridge of continuity with the CAP and the APB by continuing to recognize the pronouncements of these entities, except where it amended or superseded them, for example, with its own statements of financial accounting standards.

Two parallel advisory and oversight bodies have helped to promote the FASB's independence, by informing its work with guidance from experienced leaders in the profession, while minimizing direct interference from the constituencies it regulates: (1) the Financial Accounting Standards Advisory Council (FASAC) and (2) the FAF, of which the FASB is a subsidiary.

The FASAC provides technical consulting services for the FASB, assists it in setting priorities, recommends issues for FASB consideration and action, and helps it to establish task forces to research questions for it and to attain its objectives. Its more than 30 members reflect a broad cross section of constituencies that prepare, audit, and use financial statements and collateral financial information, and this group forms an important source of experience and wisdom to inform the work of the FASB and to help it be accountable to those who depend on the profession.

The FAF is a tax-exempt organization, and it selects the members of the FASB and the FASAC. It also finances the operations of these organizations and supervises their activities, apart from the FASB's main technical work. The FAF performs these services for the Governmental Accounting Standards Board (GASB) as well, which it formed in 1984 to set parallel standards for financial accounting and reporting for state and local governmental entities.

Just as for the FASAC, the board of trustees for the FAF draws its membership from a cross section of constituencies with a concern for the efficiency and effectiveness of financial reporting in the public interest. In the case of the FAF, this representation comes mostly in the form of nominees whom prominent professional accounting organizations put forth for approval by existing trustees. These organizations consist of the American Accounting Association; the AICPA; the Chartered Financial Analyst (CFA) Institute; Financial Executives International (FEI); the Government Finance Officers Association; the Institute of Management Accountants (IMA); the National Association of State Auditors, Comptrollers, and Treasurers; and the Securities Industry Association. The existing trustees also choose a number of at-large members for the board.

In addition to the structural supports for the autonomous voice of the FASB, the members of the organization itself have worked diligently since 1973 to preserve its independence, through qualification and service rules to limit the effects of potential conflicts of interest on board members and by taking principled stands over accounting and financial reporting standards in the public interest, even when key constituencies from public accounting, industry, regulatory authorities, and other quarters have pressed for alternative treatments, for example, over accounting for stock options. Such conflicts have led to overt criticisms of the decisions of the FASB by members of these constituencies, and the resulting pressure on the FASB members and their staff occasionally has affected the willingness of some accounting professionals to accept service in these leadership roles.

Breakdowns in the Framework and the Reclamation of Federal Oversight

This framework for regulating standards and practices for financial accounting and reporting worked fairly well for many years, although problems occasionally arose over issues such as the thoroughness and diligence of audits in the face of financial fraud in the savings and loan crisis and ownership interests of accountants in their audit clients. When scandals arose, a common refrain among regulators, investors, and the public was "Where were the auditors?" The subsequent scrutiny of the profession by these constituencies led to widespread perceptions that, in many instances, accountants had failed to preserve their professional independence, in fact or in appearance.

The growing complexity of the practice of accounting and the ascent of nonaudit practices within accounting firms, especially advisory services, were prominent factors in accountants getting themselves into trouble, for example, as they became financially dependent on revenue from these alternative services and found themselves in the untenable position of issuing audit opinions on their firms' own work.

The seeds of many of these problems were apparent by the end of the 1980s. However, the combination of the robust growth in the U.S. economy and the dramatic expansion of the high-technology, telecommunications, and information services sectors in the 1990s diverted the attention of many inside and outside the accounting profession from the creeping structural dysfunctions in the framework, including government regulators, corporate leaders, stock exchange managers, and individual and institutional investors. One of the few voices to raise concerns during this period was SEC Chair Arthur Levitt, who supported tighter regulation of corporate governance and financial reporting. However, few in Congress believed his dire warnings, against the backdrop of record gains in financial markets and a booming economy. Instead, in response to pressure from the accounting profession, and over President Clinton's veto, Congress passed the Private Securities Litigation Reform Act of 1995, which raised barriers to litigation against auditing firms and others in cases of financial fraud, and diminished further the profession's incentives to mitigate risk (aggravating a condition that organizational theorists call *moral hazard*).

When the massive financial accounting frauds involving Enron, WorldCom, the accounting firm Andersen, and other organizations became public in 2001 and 2002, it was apparent that the integrity of the framework for financial accounting and reporting, and more generally for the accounting profession, was seriously deficient. Whatever progress the profession had made in regulating itself through institutions such as the FASB, it had become clear that the opportunistic behavior of multiple constituencies had led capital markets around the world to a state of crisis. There was a dramatic drop in confidence in the integrity of American accountants, corporate leaders, capital markets, and the economy, and the public's concern for the future mirrored the dramatic stories of the downfall of narcissistic and greedy corporate leaders and of millions of ordinary people who lost jobs and retirement savings as a result of these defalcations.

The early response from the accounting profession was to minimize the scope of the problems and to impute them to a small number of bad actors. The Bush administration also was slow to acknowledge the scope of the disaster. Comments by SEC Chair Harvey Pitt, a former general counsel for the SEC and external counsel for major accounting firms during his intervening years in the private sector, did little to allay people's fears and instead heightened anxiety among investors. The administration resisted calls to respond with substantive additional legislation or regulation through early 2002, when the number of scandals increased, including the problems at WorldCom.

By the spring of 2002, with the federal indictment of Andersen for obstruction of justice, and the rapid dissolution of that venerable firm as its audit clients departed in droves, it became clear that a federal response was necessary to begin the process of restoring confidence in corporate governance practices, the accounting profession, and capital markets. The profession was not eager to see tinkering with the regulatory framework in such an atmosphere, but the major accounting firms resigned themselves to legislative action in early 2002 and moved to influence the result, which became the Sarbanes-Oxley Act of 2002.

The passage of this act signaled the reversion to the federal government of substantive oversight of the accounting profession with regard to setting standards for financial accounting and reporting. This legislation created the Public Company Accounting Oversight Board (PCAOB), a tax-exempt organization with rule-making authority over corporations that issue and list securities in public capital markets ("issuers") and the accounting firms ("firms") that audit them. Although the PCAOB is not a government agency, its members are not federal officers under the Constitution, and it draws its funding principally from registration fees rather than from federal appropriations, it works under the oversight of the SEC (which also appoints its members). This reclamation of authority from the accounting profession marked the most dramatic change in the regulatory framework for the profession since the 1930s.

At the same time, the amendments to this framework evinced a subtle approach, especially in reserving a zone of authority for the private sector. In addition, the statutory requirement that three of the five members of the PCAOB *not* ever have been certified public accountants reflected the importance of sustaining a voice distinct from the perspective of the accounting profession, and in favor of the public interest. Despite the dramatic corporate scandals in the early 2000s that led to the disintegration of the accounting firm Andersen, turbulence in global capital markets, and passage of the Sarbanes-Oxley Act, Congress fashioned the legislative response with restraint, and it did not assign full regulatory authority to the federal government. This allowed a measure of continuity with those aspects of the regulatory framework that had been constructive, including the FASB. In fact, the Sarbanes-Oxley Act expressly permitted the SEC to designate reputable *private-sector standard setters* to provide authoritative guidance for the profession, and it moved quickly to affirm its confidence in the FASB for this role, on April 25, 2003.

The Structure of the FASB

The FASB consists of seven members who serve full time for five-year terms that are renewable once, and who, during their service, must discontinue their relationships with the accounting firms and other organizations and institutions that they have served. The FASB requires that board members possess "knowledge of accounting, finance and business, and a concern for the public interest in matters of financial accounting and reporting."

In addition, the FASB retains a staff of about 70 professionals from public accounting, industry, academe, and the public sector, plus their support staff. The professional staff directly assist the FASB and task force groups, perform research, contribute to roundtable meetings, analyze comments from the public, and draft recommendations and response documents for the FASB to evaluate. Among these professional researchers and technical specialists are the FASB Fellows, whom the FASB recruits for rotation assignments during leaves of absence from their firms, companies, and universities. This allows the FASB to benefit from their current experience, and it educates the fellows about the FASB's processes for setting accounting and financial reporting standards.

The Mission of the FASB

The FASB articulates its mission as a commitment "to establish and improve standards of financial accounting and reporting for the guidance and education of the public, including issuers, auditors and users of financial information." Foremost in the minds of the members of the board is a concern for the efficient and effective operations of capital markets, and the broader social effects of reliance on those markets by all types of investors whose financial, legal, and ethical interests the quality of financial reporting implicates. The availability of reliable and timely information is essential to the functioning of capital markets, but these institutions, the individual and institutional participants that animate them, the regulatory frameworks that oversee them, and the sources and uses of capital that they reflect and enable, all exist within a broader social context, and this enlarged sphere of moral concern for the work of the FASB is a legacy of the vocation of the accounting profession as a trustee for the public good that extends at least as far back as 18th-century Great Britain.

The FASB enumerates the following means for effecting its mission:

- Improve the usefulness of financial reporting by focusing on the primary characteristics of relevance and reliability and on the qualities of comparability and consistency.
- Keep standards current to reflect changes in methods of doing business and changes in the economic environment.
- Consider promptly significant areas of deficiency in financial reporting that could benefit from improvement through the standard-setting process.
- Promote the international convergence of accounting standards concurrent with improving the quality of financial reporting.
- Improve the common understanding of the nature and purposes of the information in financial reports.

To carry out this work, the FASB publishes five principal types of guideline pronouncements: (1) statements of financial accounting standards, (2) statements of financial accounting concepts, (3) interpretations, (4) technical bulletins, and (5) staff positions. The following sections summarize these processes.

The Process for Promulgating Statements of Financial Accounting Standards

The FASB continuously monitors professional and industry practices, significant litigation, and regulatory developments to note items for consideration for its standard-setting agenda. In addition, many recommendations and requests to develop and revise technical standards and advice come from public and private sources, including the SEC, industry, academe, professional associations, and other domestic and international regulatory bodies. Foremost among the FASB's advisory network are

- the AICPA's Accounting Standards Executive Committee (AcSEC) and the Auditing Standards Board;
- the PCAOB;
- the International Accounting Standards Board (IASB);
- the FASAC;
- the FASB User Advisory Council (representing investors, investment professionals, financial analysts, and rating agencies);
- the FASB Small Business Advisory Committee (SBAC); and
- relevant committees of the CFA Institute, FEI, and IMA.

The FASB often publicizes items that it proposes to include in its standard-setting agenda as a means for discerning public interest and soliciting public comment. It then uses the following criteria to decide which of these items to include in the agenda:

- The scope, frequency, likely duration, and diversity of treatment for an issue for preparers, auditors, and users of financial reports
- The likelihood that there will be alternative solutions to enhance the relevance, reliability, and comparability of financial reporting
- The practicability of developing a technically robust solution under current conditions
- The likelihood of acceptance and adoption, and the probable range of responses of other public and private regulatory entities
- The likelihood of developing a solution that will promote salutary convergence between domestic and international accounting standards, with improvements in the quality of the former
- The likelihood of cooperation or joint project management with one or more international standard-setting organizations
- The sufficiency of financial and professional resources from the FASB and other standard-setting organizations to manage and complete the project proficiently

To promulgate standards, the FASB has adopted "due process" rules that closely mirror the guidelines of the United States Administrative Procedure Act, including requirements that its processes remain open to the public, both in person and via Internet broadcasts, and that the public have the opportunity for comment on proposed standards. The FASB follows a majority written vote to determine whether to issue exposure drafts of these standards, and these drafts reflect and explain alternative positions among board members to foster open and honest dialogue. When the FASB receives comments on an exposure draft, the board members and their staff review and analyze them carefully for the substantiveness of their arguments and not merely for the number of responses in support of respective positions. Afterward, the board redeliberates over the proposed standard, also in public. It then issues a revised draft exposure for additional comments, or it votes to decide by simple majority whether to adopt the draft.

The document that the FASB issues as a result of this process is a "statement of financial accounting standards," and it bears a cardinal number for identification purposes, for example, Statement of Financial Accounting Standards No. 123, or FASB 123 for short. Each statement recites the content of the standard, the date it takes effect, the means for making the transition to the new method for reporting, supporting information regarding the factual and systematic issues the statement implicates, a summary of the FASB's research, the justification for the FASB's conclusions over alternative treatments, a roster of the vote by the FASB members, and explanations for dissenting votes.

The Process for Promulgating Statements of Financial Accounting Concepts

In addition to issuing statements of financial accounting standards, the FASB formulates "broad accounting concepts," and publishes guidance for accounting professionals to implement its standards. This conceptual framework helps the FASB and others analyze questions that arise regarding financial accounting and reporting, and it provides support for solutions that the FASB recommends. In this process, the FASB seeks to abide by guidelines and objectives that help protect the integrity of its work product, including

- objectivity in its decision making, and standards that promote "neutral" financial information and consistent treatment;
- reflective deliberation of the views of stakeholder constituencies, consistent with the FASB members' independent professional judgment;
- proportionality and commensurability between the articulable benefits and costs of accounting standards;
- a commitment to effect changes in financial standards and reporting through timing, treatment, and other means that create as little disruption as possible from existing practices; and
- a discipline to engage in an ongoing process of assessment, interpretation, and amendment of standards in a timely fashion.

The FASB's research draws on the resources of its own staff, as well as external contributions, including other national and international standard-setting organizations. The FASB has adopted "due process" rules for its thought leadership and conceptual development activities, which closely mirror the aforementioned procedures for formulating and promulgating statements of financial accounting standards, including openness to public observation.

The FASB's commitment to analytical transparency, reasoned justification for its positions, and participatory deliberation helps it to educate accounting professionals and users of financial information, to increase public confidence in the integrity and rational foundation of the financial reporting system, and to mitigate uncertainty and other risks that can raise the cost of capital. The FASB has continued these practices since the promulgation of the Sarbanes-Oxley Act, but the new reality of oversight by the PCAOB has made this a more challenging process. Even though the SEC has ratified the role of the FASB as a standard setter, the FASB has diminished in stature slightly, and its voice, though still venerable in the profession, now must compete for attention in a more crowded environment.

Additional Pronouncements From the FASB

In addition to statements of financial accounting standards and statements of financial accounting concepts, the FASB publishes "interpretations," "technical bulletins," and "staff positions," to aid practitioners in implementing its standards. The FASB also forms implementation issues resource groups to assist its staff in (1) gathering current information regarding its standards, (2) determining whether the relevant parties grasp the significance of new standards, and (3) assessing the effects of alternative interpretations of standards.

The FASB's technical bulletins include work from the Emerging Issues Task Force (EITF), an entity that it formed in 1984 to help improve the timeliness of financial reporting and to identity and preliminarily assess incipient issues facing preparers, auditors, and users of financial reports. The EITF has 14 voting members and principally consists of representatives from accounting firms, professional associations of financial statement preparers, and the chief accountant of the SEC. It meets at least quarterly in sessions that are open to the public, and it acts as an *early-warning system* for the FASB, analyzing issues and practices before they become widespread and providing an opportunity for an early assessment of the need for action by the FASB itself. When the EITF reaches "consensus" over an issue or practice (i.e., at least near unanimity), then the FASB typically ratifies the EITF's position, and it becomes part of GAAP. When consensus is not possible, then the FASB may undertake a direct and more formal review as a prelude to action with long-term effects.

This role in anticipating trends signals a distinctive ongoing contribution for the FASB in that it helps that body, and other constituencies, including the PCAOB, the SEC, and the investing public, think critically and imaginatively about the scope and likelihood of prospective risks. The lesson of the 1990s is that the appearance that the regulatory framework and capital markets remain healthy can be not only inaccurate but also dangerous because of the false sense of security that it can engender.

The fact that significant incidents of financial statement fraud occurred under the watch of the SEC, the FASB, the AICPA, the stock exchanges, and the state boards of accountancy in the early 2000s bespeaks a precautionary tale that one should retain a decorous skepticism about the efficacy of such institutions. They are necessary for the efficient and effective functioning of markets for governance, professional services, and capital, but they are not sufficient, particularly when human judgments remain essential for deciding whether to act on the risks they portend. A case in point is the 2006 scandal regarding the backdating of corporate stock options, which unfolded under the "improved" framework of the Sarbanes-Oxley Act and the PCAOB. The challenge in the future for the FASB, the EITF, the PCAOB, the SEC, the stock exchanges, and those who rely on them will be to avoid recurrences of such overconfidence and to anticipate the forms of fraud and misconduct that are not obvious to observers.

—Lester A. Myers

See also Accounting, Ethics of; American Institute of Certified Public Accountants (AICPA); Arthur Andersen; Certified Public Accountants (CPAs); Enron Corporation; Moral Hazard; Public Company Accounting Oversight Board; Regulation and Regulatory Agencies; Sarbanes-Oxley Act of 2002; Savings and Loan Scandal; Scandals, Corporate; Securities and Exchange Commission (SEC); Transparency; WorldCom

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Financial Derivatives

A *financial derivative* is a financial instrument whose value and profits depend on the value of some more basic underlying financial instrument. For example, a stock option is a financial derivative because the value and payoffs of a stock option depend on the value and price movements of the underlying stock. Similarly, an interest rate futures contract is a financial derivative because the value and payoffs of the futures contract depend on the value of an underlying debt instrument, such as a bank deposit or a bond. As a final example, a foreign currency forward contract is a financial derivative because its value and payoffs depend on the value of the underlying currency.

Strictly speaking, a financial derivative is a derivative that is built on an underlying financial instrument.

Different types of financial derivatives include primarily financial futures, options, forward contracts, and swap agreements. Financial derivatives are closely related to other types of derivatives, including agricultural, oil, and precious metal derivatives. The similarity extends to the structure of the instruments, the common economic understanding that links all the instruments, and the very similar pricing principles that unite all derivatives. Social and ethical issues surrounding financial derivatives arise because they are extremely powerful financial instruments that can generate very dramatic profits and losses, they are complex and difficult to understand, they are susceptible to misuse as gambling vehicles, and they at least seem to be far removed from economic realities.

Financial derivatives commonly embody very high leverage; that is, the price of a financial derivative is often very sensitive to the price of the underlying financial instrument, or equivalently, a small movement in the price of an underlying financial instrument can cause a very large percentage price movement in a financial derivative built on that instrument. For example, a 1% movement in the price of a stock could easily cause a 10% movement in the price of an option on that stock. This means that an apparently benign position in a financial derivative can suddenly generate very substantial profits or losses. This happens particularly when some sudden event causes a dramatic swing in financial markets. For example, a sudden interest rate rise can cause debt instruments themselves to have a sudden price drop, and debt derivatives will typically respond to the same interest rate shock with a much larger percentage price movement.

Because financial derivatives tend to be complex and difficult to understand, senior management in firms often lacks a full grasp of the financial implications of the derivatives positions the firm holds. Because of the complexity of financial derivatives, top management sometimes leaves oversight of these instruments to specialists. This lack of control has led to some spectacular business disasters involving financial derivatives that even include the ruin of entire firms, and they have often been used as vehicles for irresponsible speculation and gambling. In some spectacular instances, junior derivatives traders have used the firm's resources to place huge bets via financial derivatives, and the resulting losses have resulted in bankruptcy.

To many observers, the world of finance seems divorced from real economic concerns. For example, a share of stock is nothing other than a financial instrument that evidences an ownership interest in a firm. But a share of stock already stands at a considerable conceptual remove from the land, trucks, and equipment to which the share gives partial title. A financial derivative built on that share may seem completely divorced from economic reality. This perception has led some observers to see financial derivatives as being merely instruments of financial speculation and gambling. Perceived in these terms, it is not surprising that some have seen them as socially and ethically undesirable. Thus, some critics have even called for trading bans and for the dissolution of financial derivatives markets.

Since financial derivatives trading began to be a force in the United States in the early 1970s, the market for financial derivatives has grown to be a worldwide market trading many trillions of dollars of derivative instruments every year. This growth has been fueled primarily by the great usefulness of financial derivatives for legitimate business purposes. The three main uses of financial derivatives are as vehicles for investment, price discovery, and risk reduction and risk management.

Investment

Financial derivatives can be used as vehicles for investment and speculation. The difference between investment and speculation is obscure, but the distinction between the two turns principally on the level of perceived risk and legitimacy of purpose. Here investment may be taken to mean trading financial derivatives in a way that increases the investor's risk in pursuit of profit. As such it embraces the kinds of investment that many would choose to label as speculation. As a model to promote understanding, we may think of the investor as a person who trades stock index futures merely to profit if the stock market moves as the investor predicts. Such trading provides no new investable funds to the economy, and it produces no benefits for others, with the exception of its role in price discovery to be discussed below. Because of the lack of benefits for others, some observers see such trading as lacking social value. However, the millions of people who trade financial derivatives for investment or speculative purposes each day reveal that they find the markets useful for their own purposes. In this sense, even the most speculative use of the markets may be said to confer some benefits to those who choose to use the markets. However, if this minor and perhaps dubious benefit were the only social benefit of financial derivatives, they would be difficult to defend.

Price Discovery

Financial derivatives and derivatives trading confer significant benefits to society through their role in the process of price discovery. Price discovery might better be termed *price uncovering* or *price predicting.* The term *price discovery* refers to the process by which information about the future prices of goods is revealed and communicated to the public at large. Most financial derivatives have expiration dates at specific times in the future. As such, the prices of financial derivatives today embody information about the likely prices of underlying goods that will prevail at those future expiration dates. For example, today's futures price for corn for delivery in one year turns out to be one of the best available predictors of the price for corn that will actually prevail one year from now.

It is important to note that the price information is entirely a by-product of derivatives trading. This information about future prices is quite valuable to economic agents of all sorts. For example, information about future interest rates that financial derivatives markets reveal helps businesses to plan investment and financing. As an example, consider a home builder who contemplates a large project that will require considerable financing. Financial derivatives markets provide the home builder with some insight into the future direction of interest rates and the future financing costs the home builder is likely to face.

Traders in financial derivatives markets do not trade to generate price information for the benefit of the public, of course. They trade for their own purposes, either to seek profit or to manage risk as explained below. So the information about future prices that derivatives markets provide for the public is purely an unintended social benefit. Furthermore, it is also a benefit provided free of charge by derivatives markets to the public at large, who can simply observe prices that are reported from derivatives markets to gain insight into the future direction of prices.

Risk Reduction and Risk Management

In addition to pursuing profit, many participants in financial derivatives trade to reduce or manage preexisting risk that arises in the ordinary conduct of business. The classic example explains how both the farmer and a corresponding grain processor use the futures markets to reduce preexisting risk that they face in the conduct of their businesses. Consider a farmer who plants wheat today for harvest in six months. The farmer knows the cost of seed and can estimate production costs very accurately. But the price that will be received for wheat in six months is quite uncertain. The farmer, however, sells the anticipated crop in the futures market today for delivery in six months. This establishes the price per bushel that the farmer will receive when the crop comes to harvest. At the same time, a miller anticipates a need for wheat to mill into flour six months from now. Like the farmer, the miller can estimate operating costs but faces an uncertain future cost for wheat, a key raw input to the milling business. The miller buys wheat in the futures market for delivery in six months and thereby establishes the price that will be paid for that key input. Both parties use derivatives to eliminate the price risk that is inherent in their respective businesses.

While the mechanics of this transaction have been greatly simplified in this example, it reveals the key point about derivatives markets and risk reduction: Traders can use derivatives markets to reduce risks that they face in the ordinary conduct of business. Because the derivatives markets provide this possibility, they provide a very real benefit for society.

The example of the farmer and the miller does not use a financial derivative in the strict sense, but the basic risk reduction transactions of the farmer and miller find exact analogs in financial derivatives. For example, some businesses know they will need to borrow or lend at a future date, such as home builders or savings institutions, respectively. Both parties can use interest rate futures markets to reduce the uncertainty about interest rates that they face in the ordinary conduct of business. Businesses find similar uses for all existing financial derivatives.

In addition to purely reducing existing business risk, more sophisticated users of financial derivatives use these markets to manage risk rather than attempting to avoid it all together. For example, pension funds are charged with managing a pool of assets for beneficiaries who will need pension payments at distant future dates. As such, pension funds are in the business of managing the risk-return trade-off of their investments. For such an investor, the goal is not to avoid all risk but to limit the risk to certain acceptable levels and to manage that risk in the best possible way. Financial derivatives markets provide tools of great power and flexibility for achieving that desirable social outcome.

As this discussion of risk reduction and risk management shows, financial derivatives provide considerable social benefits that are difficult for the uninitiated to discern. A great deal of the bad press that financial derivatives receive is due to the fact that their misuse and their admitted susceptibility to misuse is much more visible and dramatic than the obscure and vital services that they provide to businesses that use these powerful tools in a prudent business manner.

—Robert W. Kolb

See also Bank of Credit and Commerce International (BCCI); Barings Bank; Commodity Futures Trading Commission; Contingent Valuation; Metallgesellschaft

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Financial Services Industry

Ethics in the financial services industry refers to ethics in banking, securities, and insurance. This is a broad field in that it covers an array of somewhat dissimilar products and services, connected by their link to the financial interests of customers. In spite of heavy regulation of the industry, ethical challenges persist. The reliance of customers on the responsibility of members of this industry to care for their financial well-being leaves customers feeling particularly vulnerable. Furthermore, the complexity of many available products and/or services places the industry under additional scrutiny.

Financial Services as a Profession

Providing financial services is often considered a profession. This is clearly linked to the increasing complexity of financial planning and the vital role that planners, agents, and so on play in assisting individuals and companies identify and meet their complex financial needs. Unlike other professions, there is no specific code. There are, however, norms that reflect understood principles and responsibilities that guide behavior within the industry.

Professionalism enjoys a long history in the financial services industry, which dates back at least a century when, in 1915, Solomon S. Huebner articulated his dream of turning the life insurance salesperson into a professional. In 1927, Huebner founded The American College to educate insurance salespeople. Since that day, The American College has established a strong presence in the financial services industry through distance education and the award of respected industrywide designations.

As professionals, members of the financial services industry are both involved in the industry (not merely in the periphery) and knowledgeable as new financial instruments are introduced and older products evolve. Furthermore, they remain committed to serving customers, particularly where customers need guidance in differentiating among products and services and understanding their implications. As is characteristic of professionals, members of the financial services industry take ownership of and responsibility for their industry through self-regulation.

Industry Background

Before the past decade or so, as a result of legislation passed during the Great Depression of the 1930s, financial services were divided among separate industries. Banks were not permitted to sell insurance, and insurance companies were limited to the distribution of insurance products and services. This began to change with the introduction of new financial instruments, such as mutual funds and retirement funds. This, coupled with increasing longevity, which has enhanced the importance of long-term care and access to retirement funds, led to the passage of the Financial Services Modernization Act (known as the Gramm-Leach-Bliley Act) on November 12, 1999, which created the financial services industry, which now encompasses banking, securities, and insurance.

The Gramm-Leach-Bliley Act was significant in that it paved the way for common entities to offer one-stop shopping for financial products and services. On the one hand, many argue that this step, of bringing these sorts of operations together, was natural, particularly since most other countries either never recognized the distinctions removed by the Gramm-Leach-Bliley Act or removed them before the 1990s. At the same time, however, there is still concern that the industry needs to be mindful of problems that could arise, such as those linked to conflicts of interest and/or monopolization.

Marketplace Changes

The changing legal landscape has been accompanied by significant marketplace influences that influence the roles and responsibilities of financial services professionals. For example, the passage of the Gramm-Leach-Bliley Act has not only changed the nature of the industry but also augmented the requisite knowledge and responsibilities of members of the industry. Financial planners, insurance agents, and so on can no longer limit their knowledge to the select group of products and services with which they are familiar; they have to understand the industry to give customers the appropriate guidance and advice.

Technological advancements have also complicated the role of the financial services professional. The Internet increases the knowledge that the consumer has available to him. This leads to more educated consumers but also, often, more confused consumers (whether they realize it or not). Many products and services are complex so that publicly available information, such as that accessible via the Internet, is not always sufficient to guide responsible decision making. It thus becomes incumbent on planners and other professionals to anticipate these sorts of difficulties and to account for them.

The trend is toward self-service, and the Internet makes this possible without discriminating among customers. The lack of discrimination also translates into the failure to recognize particularized needs of vulnerable groups of customers, such as the elderly. While the Internet makes self-service possible, it is the responsibility of professionals nevertheless to provide oversight where he or she recognizes the expertise that he or she inherently brings to bear on the situation.

Products, Services, and Customers

Responsible behavior in the financial services industry is an increasing concern, not only because of the amount of money at stake but also because of the complexity of products. There are many products, particularly related to insurance, that even producers do not understand fully. Equity-indexed annuities, for example, are currently creating considerable controversy such that some firms are choosing to stay out of that market entirely. A number of common themes characterize ethical concerns in the financial services industry.

Conflicts of Interest

Of significant concern is the elimination of conflicts of interest and the removal of any sort of presence of these sorts of conflicts. Conflicts exist where there is a presence of perceived or actual competing interests. Conflicts of interest are said to arise where the professional's separate relationships with clients intersect such that the advice to one client can affect the financial situation of another client.

This sort of conflict can exist, for example, where a planner advises a husband and a wife who subsequently enter into a divorce. On the other hand, a conflict could also exist between two seeming strangers who, as it turns out, are engaged in a business partnership or some other relationship. It is not necessarily the case that these sorts of conflicts cannot be overcome, but most professionals recognize that they have to be recognized and handled in a responsible fashion.

Conflicts also exist where a professional is connected to other stakeholders (i.e., suppliers). For example, it is considered a conflict for a professional to advise a client to invest in a company in which the professional is a major stockholder. It is generally expected that professionals will avoid these sorts of conflicts or even the perception thereof.

A potential perceived conflict exists in that the adviser is paid by commission—that is, according to what he or she sells. While this does not create an absolute conflict, perceptions often exist that advisers are influenced by the lure of compensation.

Disclosure

One way in which professionals handle conflicts of interest, or the appearance thereof, is through disclosure.

Disclosure refers to open acknowledgment of these sorts of potential biases. It entails informing the customer so that he or she is aware and can make a meaningful choice. This choice can involve how to evaluate the professional's advice, or even whether or not to continue the relationship with this professional.

Disclosure also comes up as an important issue with regard to compensation practices. Insurance agents are often paid by commission, and some of the commissions paid are distributed in lump sums. Oftentimes agents choose not to discuss their payment arrangements with consumers because it creates a perception that financial services professionals consider distorted. To many, it appears that agents receive a windfall, and this can jeopardize sales. An increasing number of customers are moving toward Internet-based options that seem to involve lower commissions.

In fact, the perceived windfall is not entirely accurate, in that it reflects the timing of the recognition of payment, not necessarily the extent of the professional's efforts on the client's behalf. The trend, nevertheless, appears to be toward increased disclosure. The emphasis lies on educating consumers so that compensation practices become less controversial.

Suitability

Suitability also remains a significant concern. Suitability refers to the consideration of various strategies to meet the client's needs. It is considered important for financial services professionals to evaluate opportunity within the context of investment risk and the risk tolerance of the consumer.

Particularly in recent years, suitability is becoming an increasing issue. A number of professionals and companies have been faulted for selling products too aggressively, without adequate consideration of clients' needs. In fact, this sort of situation can happen through intentional neglect, but it can also occur, through no conscious fault of the professional, as a result of his or her inability to navigate through all the information appropriately. The industry continues to wrestle with suitability as a priority for enhancing responsible decision making in the financials services industry.

Conclusion

One of the leading tensions in the financial services industry remains the perceived conflict between ethics and compliance. In fact, many people argue that the increasing emphasis on compliance is detracting from sufficient attention being paid to ethics. Compliance refers to adhering to rules; ethics, on the other hand, guides decision making in the absence of clear rules. It is therefore deeply troubling that ethics could possibly be lost in the morass of regulations.

At the intersection of ethics and compliance, however, lies attention to and concern for the customer. This is a pervasive theme that has existed as long as the financial services industry has been operating. While lapses in judgment do occur, the professionals within the industry continue to take responsibility for their industry and the customers for whom they care.

—Tara J. Radin, Ronald F. Duska, and Julie Anne Ragatz

See also Bankers' Trust; CFA Institute; Conflict of Interest; Disclosure; Federal Deposit Insurance Corporation (FDIC); Fiduciary Duty; Finance, Ethics of; Individual Retirement Accounts (IRAs); Life Settlements; Profits; Regulation and Regulatory Agencies; Securities and Exchange Commission (SEC)

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Firestone Tires

Firestone has faced significant scrutiny for the production of tires that matched poorly with Ford Explorer and Mercury Mountaineer sport utility vehicles. This mismatch, or ultimately poor tire performance, resulted in many highway accidents wherein consumers were injured and in extreme cases killed when Firestone tires experienced tread separation. Firestone has suffered significant brand, reputation, and financial repercussions as a result of the faulty performance and ensuing recalls.

Bridgestone/Firestone, Inc., based in Nashville, Tennessee, has been in the business of making tires since 1900, when Harvey Firestone founded the Firestone Tire & Rubber Company in Akron, Ohio. Firestone was acquired by Bridgestone USA, Inc., a subsidiary of Tokyo-based Bridgestone Corporation, in 1990 for $2.6 billion. Today, the company markets 8,000 different types and sizes of tires and a host of other products. The company has also enjoyed a long and prosperous relationship with Ford Motor Company that began in 1906 when Henry Ford purchased 2,000 sets of tires from Harvey Firestone.

In July 1998, a State Farm Insurance researcher advised the National Highway Traffic Safety Administration (NHTSA) that he had found 20 cases of tread failure associated with Firestone tires dating back to 1992. He was politely thanked, but no action resulted. In January 2000, Houston television station KHOU aired a 9-minute story on tread-separation accidents in Texas. After the story aired, many people called the station to relate their own stories of Firestone tire failures, most on them on Ford Explorer sport-utility vehicles. These were relayed to Joan Claybrook, former chief of the NHTSA. Finally, Sean Kane, a former employee of the Center for Auto Safety and the founder of Strategic Safety, a research organization, also tried to alert the NHTSA about problems with tread separations on Firestone tires. After learning about similar problems in Venezuela, Strategic Safety, together with Public Citizen, another consumer watchdog group, issued a press release on August 1 asking Ford for a vehicle recall.

Despite the evidence compiled by these sources, the NHTSA was slow to respond. In March 2000, investigators Steve Beretzky and Rob Wahl found 22 tread-separation complaints that they marked for "initial evaluation." The number of complaints skyrocketed between March and May, and by May 2, the NHTSA had elevated their status to "preliminary investigation." Days later, the NHTSA requested that Bridgestone/Firestone supply production data and complaint files, which it produced on July 27.

On obtaining a copy of the report, Ford immediately began analyzing the data. Of the 2,498 complaints logged by that time, 81% involved P235/75R15 Firestone tires. Of the 1,699 complaints involving tread separation, 84% involved Ford's Explorer and Bronco SUVs and Ranger and F-150 trucks. On August 5, agents of Ford and Bridgestone/Firestone met in Dearborn, Michigan, to discuss the issue. By this time, the NHTSA was investigating 21 possible deaths related to tread separation of Firestone tires. Within days, the investigation had grown to include 46 possible deaths, and Ford and Bridgestone/Firestone met with NHTSA officials to discuss a plan of action. On August 9, the companies issued a recall of 6.5 million tires.

After continued investigations, the NHTSA encouraged Bridgestone/Firestone to expand the recall to include other sizes and models of tires, but the company refused. On September 1, the NHTSA issued a consumer advisory warning of potential problems with other sizes of Firestone tires.

Since the recall announcement, both companies' stock prices have declined, and Bridgestone/Firestone suffered a $750 million loss in 2000. Opinion polls suggested that the public had lost faith in both Bridgestone/Firestone and Ford and that consumers were quite worried about the safety of Ford Explorers with Firestone tires. Moreover, both companies face hundreds of lawsuits stemming from deaths and injuries resulting from tire-separation incidents—these still continue five years later. The first of these, which went to trial in Texas in August 2001, was settled out of court for $7.85 million. Ford, which also was named in the suit, settled for $6 million before the trial began. Ford Motor Co. filed a lawsuit against Bridgestone/Firestone relating to the 2000 recall of defective tires. Bridgestone/Firestone recalled 6.5 million tires and in 2001 Ford had to cover the costs of the tire-replacement program. More than 270 people were reportedly killed and more than 700 more were injured in accidents involving Firestone ATX and AT tires, mostly on Ford Explorer vehicles. In late 2005, Bridgestone agreed to pay Ford a $240 million settlement.

In July of 2006, Bridgestone-Firestone announced a recovery rate of recalled tires that exceeded 95%. The company declared it was not satisfied with this recall rate and attempted to reach out to consumers who were still in possession of the potentially faulty tires. The renewed effort to communicate with consumers included sending letters to current registered owners of Ford Explorers, Mercury Mountaineers, and Mazda Navajos. In addition, the company sent letters to every Firestone company-owned store and participating, authorized Firestone dealer reminding them to look for the recalled tires and to check the spare. Firestone reiterated their offer to replace, mount, and balance new, replacement tires, at no cost to consumers.

The ultimate question is not where this crisis will leave Ford and Bridgestone/Firestone but how it will affect the ethical and legal responsibilities of the government, regulatory agencies, and businesses. Consumers can now research all aspects of vehicle quality except for tires, so one suggestion has been to create consumer reports on tire durability, traction, strength, and other important traits. It is up to consumers to determine whether Ford, Bridgestone/Firestone, and the NHTSA acted ethically and responsibly based on the information available. Did they try to hide information? Did they act quickly enough? Will the public forgive and forget? Only time will tell.

Public Citizen, along with Bridgestone, three other tire companies, and a trade group representing the tire industry, took regulators at the NHTSA to court asking for a tougher tire-pressure monitoring rule. The resulting rule is mandated under the Transportation Recall Enhancement, Accountability, and Documentation Act (TREAD), which was passed by Congress following the Firestone incident. This act calls for stricter reporting of vehicle and tire problems with NHTSA and requires vehicle manufacturers to install a system on vehicles' tires to warn when they become 25% or more below the recommended tire pressure. This new technology must be present in all new vehicles manufactured after August 31, 2007.

—O. C. Ferrell and Linda Ferrell

See also Accountability; Business Ethics; Business Law; Consumer Fraud; Corporate Ethics and Compliance Programs; Crisis Management; Deceptive Advertising; Deceptive Practices; Honesty; Integrity; National Highway Traffic Safety Administration (NHTSA); National Traffic and Motor Vehicle Safety Act

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FLAT TAX

The flat tax is a proposal to replace the current federal income tax code with a simple one-rate tax on all earned income. Instead of a system of progressive rates in which the percentage of tax taken increases as income rises, all income would be taxed at the same rate, 17% in some proposals, and the only deduction allowed would be a personal deduction.

Proponents of the flat tax cite several advantages over the present system. Complexity would be reduced, making it possible for all individuals to fill out their own tax forms. The present tax code fills more than 60,000 pages, and most income tax returns are prepared by professionals. Complying with the tax code costs as much as $194 billion a year according to some estimates. The flat tax would eliminate virtually all compliance costs.

A second advantage claimed by proponents of the flat tax is more ethical government. Under the present system with its thousands of exemptions, deductions, credits, and special treatments, there is an incentive for special interest groups to lobby legislators for favorable treatment. A flat tax, it is claimed, would eliminate the rewards for manipulating the tax code and thereby reduce the temptations of government officials to be influenced by favors.

A third advantage cited by flat tax supporters is economic stimulus. Removal of the highest income tax rates would motivate people to work more, earn more, save more, and invest more, resulting in economic growth that benefits everyone. Some flat tax proposals include elimination of any taxes on dividends, interest, and other unearned income for further economic stimulus, although this is not necessary for a flat tax system.

A flat tax has been enacted in nine nations of Central and Eastern Europe, the major one being Russia, which has a flat rate of 13% on personal income. Supporters point to the growing economies of this region as evidence of the beneficial effects of the flat tax.

Criticisms of the Flat Tax

The main criticism levied by those who oppose the flat tax is that it is unfair. This system, they say, would result in a windfall for the rich and a higher burden for the poor and middle class. The flat tax would abandon the progressive tax system, which places a greater burden on those more able to pay, and increase taxes on those less able to afford them. Defenders of the flat tax say a progressive tax system would be maintained through a generous personal exemption, which is as high as $30,000 for a family of four under some proposals.

A second criticism is that the flat tax would increase the federal government deficit by lowering the taxes paid by the wealthy. Flat tax supporters counter with the argument that the economic growth stimulated by the flat tax would more than make up for the revenue lost from lower tax rates. While the 17% flat tax depends on economic growth to make up for lost revenue, the flat tax rate could be set at any level to produce desired government revenue.

Among the most vocal opponents of the flat tax are home buyers and builders since the interest on a home mortgage is the main income tax deduction for most people. The mortgage interest deduction, they say, has encouraged home ownership and brought the social benefits that come with a larger number of homeowners. Other groups generally opposed to a flat tax are nonprofit organizations. Since the flat tax would eliminate deductions for charitable contributions, there would be less incentive for people to donate to these organizations. Defenders of the flat tax answer concerns of both these groups counter these arguments by citing the economic growth they say their plan will generate. People who have more income, they say, will contribute more to charity even without tax deductions. Economic growth will enable more people to buy homes also, even without the mortgage interest deduction. Furthermore, they say, the increased savings will drive down interest rates, making home mortgages more affordable than they are under the present system.

As for the economic growth in Russia and other European nations that instituted flat tax systems, critics say that economic growth in these nations had begun well before the flat tax was instituted. The growth, they say, was due to other structural changes in the economies.

Ethical Issues

Debates over the flat tax involve both utilitarian arguments and issues of justice. Proponents of the flat tax rely mainly on utilitarian arguments to defend their proposals. Although they admit a flat tax would further enrich the wealthiest citizens, they argue that the resulting economic growth would bring greater prosperity for everyone. Furthermore, the simplification of the tax system and elimination of the necessity for professional tax preparers would lessen the burden on all tax payers and free the tax professionals for more socially useful work. Economic justice is often a secondary argument for the flat tax. The same rate for everyone is said to be a fairer system than one that discriminates against the wealthy.

Opponents of the flat tax tend to be skeptical of the economic growth predicted by flat tax proponents. They often appeal to ideas of justice and fairness in opposition to a plan that could result in a greater disparity between the wealthiest and the poorest segments of the population. Those opposed to the flat tax are often political liberals who believe in the ability of the government to accomplish desirable social objectives through the incentives available with the present system of tax deductions. For example, a flat tax would eliminate the tax incentives that encourage the use of alternative energy sources such as wind and solar power as well as hybrid automobiles and other products desired by environmentalists. These types of tax deductions are often cited by flat tax supporters as examples of the wasteful allocation of resources that their plan would eliminate.

—*Allen Hall*

See also Consumption Taxes; Tax Ethics; Tax Incentives; Utilitarianism

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Food and Drug Safety Legislation

Major Federal Food and Drug Laws

In the United States, food and drug safety is regulated through a variety of federal, state, and local laws and government organizations. This complex web of enforcement agencies and regulations works to cover all aspects of food and drug safety, from drug approvals to food labeling to restaurant sanitation. With regard to food safety, continual monitoring is provided by food inspectors, microbiologists, epidemiologists, and other food scientists working for city and county health departments, state public health agencies, and various federal departments and agencies. Some monitor only one kind of food, such as milk or seafood. Others work within a specified geographic area. Others are responsible for only one type of food establishment, such as restaurants or meatpacking plants. The Clinton administration's Food Safety Initiative of 1997 was created to strengthen the efforts of all the members of the food safety team.

The primary federal law covering food and drug safety is the Food, Drug, and Cosmetic Act of 1938. This law, which has been amended multiple times over the years, requires safety and effectiveness testing of new drugs for humans and animals, prohibits adulteration of food products, requires labeling of food products, and monitors devices that emit radiation such as microwave ovens and medical equipment. The U.S. Food and Drug Administration (FDA) is responsible for enforcement of this law. The FDA is charged with protecting the public health by assuring the safety, efficacy, and security of human and veterinary drugs, biological products, medical devices, our nation's food supply, cosmetics, and products that emit radiation. The U.S. Department of Agriculture is responsible specifically for the safety of meat, poultry, and egg products and serves to uphold the Federal Meat Inspection Act, Poultry Products Inspection Act, and Egg Products Inspection Act.

All states have laws that regulate some aspects of food and/or drug safety. Most state laws model the Federal Food, Drug, and Cosmetic Act and adopt the food safety standards found in the Code of Federal Regulations. The states serve as important first responders to inspect, monitor, and detect problems in food safety. A Government Accounting Office (GAO) report in 2001 indicated that state programs provided more than $300 million in resources to food safety programs in 1999. These resources accounted for almost 2 million food safety inspections, of which 44% were at the processor level. The FDA's budget for field activities provided $145 million in resources that same year. These numbers show the valuable contributions made by both the federal and state governments, just in the area of food inspections and field activities.

Some of the agencies involved in food safety include the FDA, Centers for Disease Control and Prevention, U.S. Department of Agriculture, Cooperative State Research, Education and Extension Services, U.S. Environmental Protection Agency (EPA), National Oceanic and Atmospheric Administration, Bureau of Alcohol, Tobacco, and Firearms, U.S. Customs Service, U.S. Department of Justice, Federal Trade Commission, and state and local governments.

History of Food and Drug Legislation in the United States

The United States was slow to recognize the need for a national food and drug law. Great Britain's first national food law was passed in 1860, while the first food and drug law was passed in the United States in 1906.

The conditions in the U.S. food and drug industries during the 1800s and early 1900s can hardly be imagined today. Changes from an agricultural to an industrial economy had made it necessary to feed the increasing city population with food from distant areas. But sanitation was primitive and ice was the principal means of refrigeration. Milk was still unpasteurized, and cows were not tested for tuberculosis. The use of chemical preservatives and toxic colors was virtually uncontrolled.

In the same era, thousands of so-called patent medicines, produced by patent medicine companies, reflected the limited medical capability of the period.

Medicines containing such drugs as opium, morphine, heroin, and cocaine were sold without restriction. Labels did not list ingredients, and there were no warnings against misuse.

Yet there were many firms producing reliable and wholesome products. Ethical companies were concerned with competitors who used fake ingredients and adulterated foods to save money. At the same time, scientific developments led to the ability to detect impurities and fake ingredients.

The Pure Food Movement, a grassroots phenomenon that began in the 1870s, was the original and principal source of political support for the Food and Drugs Act of 1906. Members of the food industry began to advocate for a federal law against adulteration as a result of trade interests. They were concerned about competition from a new breed of food products (glucose as a replacement for sugar and oleomargarine as a threat to butter were just two examples). Another issue was that variations in the laws between the states made it difficult for food manufacturers to comply with the requirements for their products according to differing state laws. In 1879, Peter Collier, the fifth head of the Division of Chemistry, urged federal legislation to make food adulteration a crime.

President Abraham Lincoln appointed Charles M. Wetherill as the first chemist of the New Department of Agriculture. Wetherill set up a laboratory and began to analyze samples of food, soils, fertilizers, and other agricultural substances. Wetherill was a chemist and physician. He organized a wide array of groups into a coalition that would be powerful enough to get Congress to act. Members included agricultural chemists, state food and drug officials, women's club members, the medical profession, sympathetic journalists, the reform wing of business, and favorably disposed members of Congress.

In 1883, Dr. Harvey W. Wiley became chief chemist and came to be leader of the pure food crusade. Dr. Wiley conducted research with human volunteers to study the effects of food preservatives on digestion and health beginning in 1902. The voluntary "poison squad," as they came to be known, ingested such chemicals as borax, formaldehyde, and salicylic, sulfurous, and benzoic acids. These experiments went on for five years.

Opposition to Wiley's campaign for a federal law came from whiskey distillers and the patent medicine firms, who were then the largest advertisers in the country. Many of these men thought they would be put out of business by federal regulation. Pressure for a law ultimately came from President Theodore Roosevelt in December 1905 after he had read about filthy conditions in Chicago's packing plants from the news media and the Upton Sinclair novel *The Jungle*. The news of the conditions cut meat sales in half and angered President Roosevelt. When it appeared that the House leadership seemed determined to give the food bill the silent treatment, Roosevelt called the Speaker in and insisted that the bill be brought to the floor. The Meat Inspection Act was passed the same day as the Food and Drugs Act.

The 1906 Food and Drugs Act

The 1906 law forbade interstate and foreign commerce in adulterated and misbranded food and drugs. The assumption of the law was that the average consumer was prudent enough to plot his or her own course and would avoid risks if labeling made him or her aware of them. The law required that drugs abide by standards of purity and quality, set forth in the United States Pharmacopeia and the National Formulary, or meet individual standards chosen by their manufacturers and stated on their labels.

The law prohibited the adulteration of food by the removal of valuable constituents, the substitution of ingredients so as to reduce quality, the addition of harmful or toxic ingredients, and the use of spoiled animal and vegetable products. Making false or misleading label statements constituted misbranding.

The Bureau of Chemistry enforced the 1906 law until 1927, when it was reorganized. The Food, Drug and Insecticide Administration was formed and renamed in 1931 as the Food and Drug Administration.

In 1937, a public health disaster drove home the need for a stronger federal drug safety law. One hundred and seven people (mostly children) died from the liquid formulation of a drug. This highlighted a weakness with the 1906 law that did not require the drug manufacturers to test the formulation for safety before it was sold.

The Federal Food, Drug, and Cosmetic Act of 1938

Congress corrected the prior law's weakness with the passage of the Federal Food, Drug, and Cosmetic Act in 1938. Now companies were required to prove the safety of new drugs before putting them on the market, including different formulations of previously approved drugs. The new law also covered the regulation of cosmetics and therapeutic devices and updated the old law to improve consumer protection. Drugs and medical devices must be proven effective as well as safe before they can be sold. The Food, Drug, and Cosmetic Act of 1938 has been amended multiple times since it was passed. The following are some examples of the types of amendments that have been made.

The Kefauver-Harris Drug Amendments of 1962 were passed to improve drug safety and ensure greater drug efficacy. For the first time, drug manufacturers were required to prove to the FDA the effectiveness of their products before marketing them.

After several deaths from cyanide placed in Tylenol capsules, the FDA issued Tamper-Resistant Packaging Regulations in 1982 to prevent further poisonings. The Federal Anti-Tampering Act of 1983 made it a crime to tamper with packaged consumer products. In 1990, the Nutritional Labeling and Education Act required all packaged foods to have nutrition labeling. The act further required that all health claims for foods be consistent with terms defined by the Secretary of Health and Human Services. Some health claims were allowed for foods and the food ingredient panel and serving sizes, and terms such as *low fat* and *light* were standardized.

Regulatory changes arising from the implementation of a 2004 Food Allergen Labeling Law and food companies' own desire to court health-conscious consumers drove new requirements in food labeling by the FDA in 2004. As a result of the food allergen law, food makers were required to label in plain language the presence of the eight allergen groups: tree nuts, milk, eggs, fish, crustacean shellfish, peanuts, soybeans, and wheat. The FDA required that food makers list the amount of trans fat on the label. Trans fat is found naturally in animal-based foods and in processed foods like vegetable shortening. In response, some food makers changed the formulations of their products to remove trans fat and/or updated their product labels.

California's Proposition 65 passed in 1986 created a controversy in food labeling. Proposition 65 requires that businesses disclose the presence of chemicals that the state believes cause cancer, birth defects, or other reproductive harm. For example, fish counters in California display state-mandated warnings about mercury and related compounds. Like the drug labeling policy above, recently introduced legislation in Congress would prohibit many state and local laws, such as California's Proposition 65, unless the states obtain FDA approval to keep them. The food industry argues that it is difficult to comply with requirements that vary state by state because it adds uncertainty, confusion, and extra costs to interstate commerce. The state attorneys general and food-safety officials are concerned with protecting the rights of the citizens and their governments in passing laws.

There are a few key federal laws pertaining to food and drug safety, and there are numerous state and local laws regulating the same areas. Many federal, state, and local government agencies work together every day to ensure the safety of the U.S. food supply and the safety and efficacy of drugs.

Social and Ethical Issues in Food and Drug Safety

The social and ethical issues surrounding the food and drug industries are significant, and questions of corporate obligations beyond specific legal requirements abound. One very pertinent issue, not specific to the food and drug industry but certainly looming large within that realm, is the problem all corporations face of balancing profit with public welfare. The public expects that corporations will, at a minimum, comply with the law. It is the government's responsibility at all levels to work to provide the legal and regulatory environment for insuring that the food we consume and drugs we use are safe. Prior to the first food and drug laws in the United States, some unethical companies violated the public's trust by producing products with fake or adulterated ingredients or sold dangerous "patent medicines" containing ingredients such as cocaine or heroin. Governmental regulation was required to ensure punishment for such unethical behavior and to reassure consumers about the food and drugs they use. Most corporations, to protect their reputation and their market share, abide by the food and drug laws and may even go beyond what is required by law, being aware that it is in their best interest to maintain the public's trust beyond the scope of simple legal compliance. Examples of corporations taking actions above and beyond legal compliance are common. Johnson & Johnson is cited as an exemplary case of corporate responsibility in the face of a product tampering in which several people died. Johnson & Johnson pulled all their Tylenol products from retailers and took the time to reformulate the product and create tamper-resistant packaging. When the company reintroduced the product, it was met with much support and enthusiasm by consumers. In some cases pressure from nonstatutory entities, such as environmental groups encourage companies to go above and beyond what is required by law. Dolphin-safe tuna is an example of pressure put on companies that started at the grassroots level and resulted in some companies changing their fishing methods to minimize or eliminate the number of dolphin accidentally caught in tuna nets.

Some ethical issues in the drug industry have raised the question of what society condones or supports based on what is accepted as right and wrong. An example of this is the work that has been done by pharmaceutical companies and researchers regarding stem cell research and products. The issues in the case of stem cell research center not so much on the safety of the public as they do around the values that society as a whole professes to hold. Another ethical question relevant to the drug industry is whether or not some laws are overly restrictive. A case in point would be FDA laws that keep certain drugs off the market that could be beneficial to many people but that have proven to have very adverse, in some cases fatal, effects for a small percentage of the population. Merck Pharmaceutical's Vioxx is one such example. While some individuals were harmed by taking Vioxx, others lobbied the FDA to keep the product on the market because the improved quality of life they experienced while taking the drug more than made up for any risks of the drug. Pharmaceutical products are often a trade-off. While the drug may cure or control a medical condition, there are side effects experienced by some individuals. The ethical issue is whether drugs that harm some individuals, even though they help others, should be completely pulled from the market. Some people feel that consumers should be able to make an informed choice, as long as the risks and benefits are clearly outlined.

Keeping up-to-date with food and drug safety requires continual monitoring of situations and events that can affect these areas. As new food safety risks arise, or we gain better knowledge about nutrition, new medical conditions, epidemics, or new technologies, updates to the food and drug laws and policies are necessary. As a result, Congress or the states may amend the existing food and drug laws or create new laws. Food and drug agencies such as the FDA may create new policies to deal with amended or new laws.

Technological developments and medical research has resulted in the ability to create new types of drugs and will continue to result in new drugs and products. The FDA can grant "fast track" clearance to a company to expedite development of a drug under certain circumstances. Over the years, more and more medicines and related products have been and are being created with biotechnology techniques. Medical research over the past several decades has made significant discoveries pertaining to the human genome that, in turn, have resulted in the creation of numerous biological drugs, many of them reengineered human proteins. Biotechnology has resulted in significant advances against cancer and age-related blindness, among other diseases. New medical research and discoveries have and will lead to innovative and novel products and cures for diseases. How these are handled by the FDA and the companies involved will be an important issue in maintaining drug safety.

The question of who bears the primary responsibility for public safety, the government or the corporations, is a question that goes well beyond the food and drug industry. It is a question that is as old as free market society itself and one that we will be struggling with more and more as populations and technologies increase and resources decrease.

—Patrice Luoma

See also Consumer Protection Legislation; Food and Drug Safety Legislation; Regulation and Regulatory Agencies

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Ford Pinto

One of the best-known and infamous cases in corporate ethics and social responsibility involves the Ford

Pinto. The case involved the decision by the Ford Motor Company during the 1970s not to recall its Pinto model, despite knowledge of a dangerous fuel tank design flaw and the potential loss of life that would result. It also involved, for the first time, charges that were brought against a corporation not just for negligence but for murder.

In 1976, Ford was the second largest manufacturer of automobiles, with revenues of $30 billion a year and net income of almost $1 billion. Due to concern over competition over subcompact vehicles from Germany and Japan, Ford President Lee Iacocca was determined to manufacture a car at or below £2,000 and for less than $2,000. Whereas normal development and production of an automobile takes more than three and a half years from start to finish, the Pinto was a rush project, beginning in 1968 and taking just over two years to reach the showrooms. As a result, engineering design decisions came after style decisions to a greater degree than normal. The Pinto's style required that the fuel tank be located behind the rear axle, leaving only 9 or 10 inches of "crush space" between the rear bumper and rear axle. In addition, bolt heads were exposed that were capable of puncturing a fuel tank on rear impact.

Crash tests revealed that when the Pinto was struck from behind at even slow speeds the fuel tank could be punctured, causing fuel leakage. Any stray sparks could then ignite the spilling gasoline, causing the car to become engulfed in flames. If the fuel tank design was to be modified however, or a rubber bladder installed, the vehicle could pass the rear impact test. The crash test information was forwarded to the highest levels of Ford management.

Despite being fully aware of this information, the company continued with the production of the Pinto and was able to justify the decision on the basis of several reasons. First, the company met all applicable federal safety standards. Second, the car was comparable in safety with other cars then being produced. Third, in the early 1970s consumers were more concerned with price than safety, leaving little incentive for firms to spend money promoting the safety of their vehicles. Fourth, changing the design would lead to little trunk space, an important selling feature for cars.

The fifth and most controversial reason for sticking with the design was based on a cost-benefit analysis conducted by Ford. An internal study suggested that it would be more cost effective to continue with the same fuel tank design rather than change it. The study indicated the cost to improve the design of all Ford vehicles using the flawed fuel tank to be $137 million ($11 per vehicle × 12.5 million vehicles), which was much greater than the cost to society of just over $49 million. Ford's estimate of the cost to society was based on a 1972 study by the U.S. National Highway Traffic Safety Administration, which estimated the cost of a human life to be approximately $200,000, with the cost of a serious burn injury being approximately $67,000. These amounts included categories such as future productivity losses, medical costs, property damage, legal costs, and employer losses. The amount of $49 million was based on the estimated cost to society of the expected 180 burn deaths (180 × $200,000), 180 serious burn injuries (180 × $67,000), and 2,100 burned vehicles (2,100 × $700).

Despite reported incidents of burning vehicles, Ford still decided not to recall the Pinto. In addition, the company managed to successfully lobby the U.S. government for 8 years not to implement a key government safety standard that would have required Ford to modify its fire-prone gas tank or even warn the public of the danger. Several high-profile deaths were reported in the media, and a civil suit was settled in 1978 when a jury awarded $125 million, later reduced to $6 million, for what the judge called Ford's callous indifference to human life. Following the death of three teenage girls in 1978, Ford went on trial in 1980 with the charge of criminal conduct, the first time a company experienced such a charge. It was only after the law became effective in 1977 that the Pinto was made with a rupture-proof fuel tank design. In 1978, Ford finally recalled all Pintos made between 1970 and 1976 and replaced the Pinto with the Ford Escort after 1980. Some estimate that more than 500 people died in burn deaths related to the Ford Pinto.

It's not clear whether Ford learned anything from the Pinto experience, based on its actions (or inaction) during the Ford Explorer versus Bridgestone/Firestone scandal in 2000 when many drivers and passengers died or were seriously injured due to rollovers and/or tire blowouts. Ford appears to have known of rollover problems for some time before taking any action and continued to blame Bridgestone/Firestone. On May 25, 2001, Ford placed advertisements in several newspapers such as *USA Today* signed by its CEO Jacques Nasser and Chairman Bill Ford stating that customer safety has always been and always will be their first priority. Based on the Ford Pinto case, however, many might suggest that Ford provided an example of a company that disregarded the safety of its customers out of concern for their bottom line.

—*Mark S. Schwartz*

See also Consumer Rights; Cost-Benefit Analysis; Utilitarianism

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Foreign Corrupt Practices Act of 1977 (FCPA)

The Foreign Corrupt Practices Act (FCPA) is a U.S. law that prohibits companies from gaining business or any improper competitive advantage through bribes paid to foreign officials. Passed by Congress in 1977, the FCPA's enactment made the United States the first industrial nation to criminalize transnational bribery. Congress further amended the law in 1988 and 1998.

The FCPA applies to companies organized under U.S. law, as well as foreign companies that issue securities within the United States. These organizations and their agents may be held liable under the FCPA for acts performed either within or outside U.S. borders. A 1998 amendment also extends the law's reach to include citizens of other countries who support or engage in foreign bribery while physically present within the United States.

The FCPA addresses bribery through two avenues. First, it proscribes companies from making payments to foreign officials that are intended to induce the recipient to misuse his or her official position to help the firm obtain, retain, or direct business or secure any improper advantage—for example, by encouraging the recipient to take or omit some action or to use his or her influence to affect a foreign government's decision. The law's definition of *foreign official* includes officials of foreign governments, officials of foreign political parties, candidates for foreign political office, and officials of public international organizations, such as the International Monetary Fund or the World Bank. The FCPA prohibits both direct payments to these individuals and payments made through intermediaries. The law is violated once a payment is offered, even if it is subsequently refused. Companies convicted under the FCPA's antibribery provision are subject to a criminal fine of up to $2 million. Willful violation of the law by individual officers, directors, employees, and other company agents can result in a maximum fine of $100,000 and up to five years' imprisonment.

The FCPA's antibribery provision is notable not just for what it prohibits but also for the kinds of payments it allows. It does not outlaw bribes aimed at private companies or individuals, so long as these payments are not channeled to the government. Furthermore, it permits so-called facilitating or grease payments. This is a sum paid to induce a government official to provide a service he or she is obliged to perform and to which the payer is entitled. Facilitating payments typically are differentiated from bribes on the basis of two features: (1) they usually involve small amounts of money, and (2) they are not intended to secure a competitive advantage. In many poorer nations, such payments function as "tips" that supplement inadequate wages. The original 1977 legislation exempted payments of this type directed at foreign government employees whose positions were "essentially ministerial or clerical." The 1988 amendments modified this definition, permitting payments to public employees for "routine government action." Examples of such activities provided within the statute include visa processing, mail delivery, the scheduling of inspections, and utility hookups (phone, power, water, etc.). The list is not exhaustive: a subsequent qualification makes clear that other government services may qualify under this exemption.

The second avenue through which the FCPA addresses bribery is a set of accounting and control requirements. The law obliges companies to maintain records and file financial statements that accurately reflect the firm's transactions. It also requires the implementation of internal controls adequate to reasonably assure that a company's assets are used only for purposes that are legal and appropriately authorized. The FCPA's accounting provisions are designed to enhance corporate transparency, prevent the creation of slush funds, and forestall the disguising of bribes as legitimate commercial transactions.

The FCPA is a product of the heightened sensitivity to political corruption that prevailed during the years immediately following Watergate. Investigations during the mid-1970s revealed that numerous U.S. corporations had offered or given bribes to political figures in foreign countries. Perhaps most notoriously, Lockheed Corporation paid senior officials in Japan and the Netherlands for preferential consideration of its aircraft. The resulting scandals led to the fall of the Japanese government and implicated a member of the Dutch royal family. A voluntary disclosure program conducted by the Securities & Exchange Commission demonstrated that Lockheed's activities were by no means unique: More than 400 corporations, including 117 of the Fortune 500, admitted to paying more than $300 million to foreign officials.

Through the years, commentators from government, business, and the academy have raised numerous questions and concerns about the FCPA. These critiques center on three issues. First, the FCPA is alleged to place U.S. companies at a competitive disadvantage relative to firms unhindered by similar legal constraints. Some assessments of the FCPA's financial impact estimate the value of the business opportunities lost by U.S. companies at tens of billions of dollars annually, not counting related economic consequences (lost wages, diminished tax revenues, decreased shareholder returns, etc.). Other studies conclude that the law has a smaller economic effect on U.S. exports, but one that is statistically significant. Still, some U.S. business leaders underscore the benefits their organizations enjoy under the FCPA. For example, the law provides a public standard to which U.S. firms can appeal when confronted by bribe solicitations; thus, it helps shield them from the direct and indirect costs that surround such demands. The refusal to pay bribes also can provide companies with a reputational advantage.

A second line of criticism questions the law's moral soundness. The FCPA has been cited as an example of a law that imposes Western values on other cultures. Respondents to this charge of ethical imperialism emphasize two indicators that suggest bribery is broadly acknowledged as morally improper: the ubiquity of legislation outlawing domestic bribery, and the clandestine and secretive conduct that universally attends these payments. Others argue that the FCPA categorically imposes a moral standard that is only conditionally binding, and there may be occasions when a corporation's responsibilities to its stakeholders—for example, providing a fair return to shareholders—should take precedence over its obligation to avoid bribes. One reply to this argument is that it does not actually oppose two moral duties. Rather, it places stakeholder *interests* in opposition to the moral obligation to abstain from bribery, and it is uncertain whether these interests ever could carry sufficient weight to override that duty.

A third criticism of the FCPA is that it is an ineffective deterrent to bribery. Advocates of this view highlight trends and data that suggest the law's impact has been limited at best. The evidence cited includes the following: the relatively small number of cases prosecuted under the FCPA; economic analyses showing that during the 1980s U.S. exports grew faster in product markets traditionally susceptible to corruption—for example, defense equipment and oil and gas field machinery—than in sectors customarily less plagued by bribery; and the relatively poor showing of the United States on Transparency International's Bribe Payer's Index, a ranking of bribe sources first instituted in 1999. Defenders of the law point to the positive developments that have followed in its wake. The FCPA has served as the basis for several highly publicized prosecutions, resulting in substantial fines for guilty companies. It has also spurred companies within its purview to implement internal policies and practices aimed at preventing bribery.

The FCPA has played a critical role in catalyzing multilateral responses to the problem of transnational bribery. Concerns about the law's impact on the competitiveness of U.S. companies created political pressure to extend antibribery legislation through international agreements. In 1988, the FCPA was amended with a proviso that directed the President of the United States to work with the country's trading partners to staunch cross-border bribery. Aided by a growing global awareness of corruption's deleterious effects on both countries and companies, these and similar diplomatic efforts began to bear fruit during the late 1990s, when numerous multilateral conventions addressing international bribery began to appear.

The multilateral initiative most closely linked with the FCPA is the Convention on Combating Bribery of Foreign Public Officials in International Business Transactions, adopted in 1997 by the Organisation for Economic Co-operation and Development (OECD), a worldwide association of advanced economy nations. Modeled largely on the FCPA, the OECD Convention is directed toward the supply side of the bribery equation. Signatories to the Convention must establish laws criminalizing the bribery of foreign government officials by businesses. Furthermore, they are called to cooperate with other signatory countries in identifying and fighting bribery. Importantly, the OECD Convention contains a provision for compliance monitoring and reporting, to promote its full and effective implementation. A related initiative also calls on those OECD member countries whose tax codes permit the deductibility of foreign bribes to eliminate this practice.

As of 2004, all 36 countries party to the Convention had passed implementing legislation. For example, the 1998 amendments to the FCPA were introduced specifically to align U.S. law fully with the Convention's stipulations. Some of the national legislation spawned in response to the OECD Convention is noteworthy for its innovation. In particular, the bribery and corruption section of the United Kingdom's Anti-terrorism, Crime, and Security Act of 2001 does not distinguish between facilitating payments and larger bribes, making both types of payments illegal. The UK law thereby moves beyond the Convention's requirements and arguably sets a new benchmark for corporate conduct in this arena.

The OECD Convention is reinforced by other important antibribery initiatives, including the European Union's Convention on Corruption, the Council of Europe's Criminal Law Convention, and efforts sponsored by the United Nations, the World Bank, and the International Monetary Fund. Its goals also are broadly supported by the civil society organizations now working to combat corruption, most important the country-specific and transnational projects of Transparency International. Assiduously and consistently implemented, the OECD Convention could help both to deter bribery and level the playing field for multinational enterprises headquartered in the world's leading economic nations.

In summary, then, the significance of the FCPA is threefold. As the first national law to criminalize foreign bribery by domestic enterprises, the FCPA stands as a milestone in the history of efforts to eradicate transnational bribery. The statute also serves as a continuing test case for laws that seek to raise standards of corporate conduct in global markets: The concerns raised about the FCPA's economic consequences, moral soundness, and effectiveness illustrate the challenges faced by such legal initiatives. Finally, although the FCPA has been widely criticized, it has become, through the OECD Convention, a model for international legislation. Thus, it has helped to stimulate some important first steps toward the development of a comprehensive, global antibribery regime.

—*T. Dean Maines*

See also Corruption; Disclosure; Ethical Imperialism; Extortion; International Business Ethics; International Trade; Organisation for Economic Co-operation and Development (OECD); Reciprocity; Side Payments; Transparency International; Unfair Competition

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Foreign Direct Investment (FDI)

Foreign direct investment (FDI) is the investment in an entity in one economy by an investor in another economy. Unlike foreign portfolio investment (FPI), in which the investment is in foreign financial instruments, FDI provides the investor with control over the acquired asset. Control of an asset has been defined (OECD Benchmark) as owning 10% or more of the ordinary shares or voting stock in an incorporated enterprise or the equivalent in an unincorporated enterprise. FDI can occur in various forms: greenfield investments in which there is an investment in a new facility; mergers in which the assets and operations of firms from two different countries are combined to form a new entity; and acquisitions in which there is a transfer of existing assets from a local entity to a foreign investor. There are also nonequity forms of FDI, which include types such as subcontracting, management contracts, turnkey arrangements, franchising, licensing, and product sharing. The amount of FDI is generally defined by two measures: the flow of FDI and the stock of FDI. The flow of FDI refers to the amount of investment over a given time period (typically one year), and it is made up of three components: equity capital (purchase of shares of the enterprise), reinvestment of retained earnings of the entity, and intracompany loans or transactions between the parent enterprises and its foreign affiliates. It is commonly tracked both inwardly (FDI recipient or host country) and outwardly (FDI source or home country). The stock of FDI refers to the total accumulated value of foreign-owned assets at a given time. Individuals or business entities may undertake FDI. Firms that source FDI are known as multinational or transnational corporations (MNCs or TNCs) or enterprises (MNEs or TNEs). These firms are generally large and have budgets that exceed those of many countries.

An investor's motivation for acquiring or establishing foreign assets fall into three primary categories: FDI may be an effective way of gaining access to a foreign market or to valuable foreign resources, or it may be an effective way of reducing the cost of operations. But these incentives may be mitigated by potential risks due to uncertainty in the political and economic environment of the host country or the openness of the country to FDI.

Worldwide FDI has grown tremendously since the late 1980s as the institutional structures have encouraged economic liberalization and globalization. FDI inflows peaked in 2000 at $1.4 trillion but have since fallen to $560 billion in 2003 as a result of a worldwide economic downturn and the events of September 11, 2001, in the United States.

Historically, the developed countries have accounted for the majority of FDI. In 2003, they were responsible for 90% of the FDI outflow and were the recipients of 66% of the inflow. That being said, FDI is a major source of external capital for developing countries and is thought to be a major contributor to economic growth and development. In 2003, FDI inflows accounted for 72% of all resource flows to developing countries.

With economic globalization, the demand for FDI dollars far exceeds the supply, allowing foreign investors to be choosier when deciding where to invest and, in turn, creating an environment of fierce competition among developing countries for the scarce FDI dollars. Developing countries have responded by instituting liberal FDI policies, providing tax breaks, and relaxing environmental and worker health and safety standards to attract foreign investors. This has created a situation where the developing countries are increasingly more vulnerable to foreign investors' actions, which in turn has raised the level of awareness and the debate concerning the social responsibility of foreign investors in developing countries.

History of FDI

During the two decades following World War II, FDI rapidly increased in Western Europe and some developing countries. The United States undertook new international expansion efforts, first in the reconstruction of war-torn Europe and then during the period of rapid economic growth in many countries during the 1960s. To a great extent this was a honeymoon period for FDI and MNEs. There was not much concern about regulating MNEs. Host countries welcomed private foreign capital in the form of inward FDI, and home countries were not too worried about the effects of outward FDI on trade, employment, or technology. FDI regulation was primarily defined through bilateral investment treaties, which prevailed over multilateralism after the unsuccessful attempt to create an international trade organization at Bretton Woods. The UN Conference on Trade and Development (UNCTAD), which was established in 1964, initially focused on increasing the flow of foreign capital, and thus it recommended that governments of capital-exporting developed countries should take steps to encourage the flow of private investment to developing countries and those of private-capital-importing countries should provide favorable conditions for FDI. By the end of the 1960s, the total FDI stock value was approximately $160 billion, four fifths of which was sourced from only five countries (United

States, United Kingdom, Germany, France, and Switzerland), and 50% of that was sourced by the United States.

By the late 1960s and early 1970s, the honeymoon period was over for MNEs. The focus shifted from the flow of FDI to the activities of MNEs. There were allegations of U.S. MNEs interferring in policital matters in developing countries. In a speech to the UN General Assembly in 1972, Chile's President Allende made a virulent attack on MNEs, as a result of the International Telephone and Telegraph Company (ITT) devising a plan to overthrow the Chilean government and another company, Kennecott Copper Corporation, attempting to control its natural resources. And thus, while only a third of the MNE activity was located in developing countries, it attracted the most attention because of MNEs' power and bold actions.

The developing countries used the UN system to try to protect their national sovereignty and control their natural resources. In 1974, two General Assembly resolutions were sponsored by developing countries that affirmed the principle of permanent national sovereignty over natural resources and called for the industrialzed world to assist in financing third world economic development. While the resolutions had no force in international law, they did highlight the developing countries' position.

Also in 1974, the UN Economic and Social Council (ECOSOC) established the Commission and the Center on Transnational Corporations, in which the developing countries held a majority of the 48 member seats. The objective of the Commission was to enhance the understanding and nature of MNE activities, to obtain arrangements for MNE operations that promoted national goals, and to strengthen the negotiating capacity of host governments in dealing with MNEs.

In 1976 and 1977, the Organisation for Economic Co-operation and Development (OECD) created guidelines that were promoted by the United States but counteracted the moves of the developing countries. These guidelines protected U.S. investments overseas, promoted a liberal investment climate, and accepted that all OECD governments had a responsibility to treat foreign enterprises no less favorably than their own national enterprises.

The economic situation in the late 1970s and early 1980s was one of high oil prices and worldwide recession conditions, which quickly reduced the bargaining power of developing countries as the international direct capital flow slowed down. Developing countries were in a state of debt crisis, and sources of external financing other than FDI were drying up. The debt-ridden developing countries that did seek help from international financial institutions, such as the IMF and the World Bank, were required or encouraged to institute austere fiscal policies. Structural adjustment programs became the prescription and the Washington consensus idealogy was an important basis for this prescription. The recommendation to developing countries was to give a larger role to the market forces and to reduce the role of the state, which in turn gave FDI a bigger role in the economy. This shifted the focus from how to control FDI to that of how to attract FDI. Hence, this period saw a proliferation of national liberalization programs, bilateral investment treaties, regional trade agreements that included significant investment policy liberalization measures, and General Agreement on Tariffs and Trade/World Trade Organization (GATT/WTO) agenda items that focused on investment issues.

As a result of economic liberalization, FDI increased rapidly in the 1980s, with the United States and the European Community together making up nearly 80% of the total world's outward FDI stock. By the end of this decade, Japan became a major source as the outward flow of the United States declined, and the triad (United States, European Union, and Japan) sourced 80% of the world's FDI stock. The triad also dominated the inward FDI flow and stock, accounting for 65% and 50% of the world total FDI flow and stock, respectively. Only 17% of FDI inflows went to developing countries, and 0.1% of it went to the least developed countries. Overall, FDI outflows tripled between 1984 and 1987, and they increased another 20% in both 1988 and 1989.

The focus in the 1990s continued along the path of economic liberalization. During the period from 1990 to 2002, of the 1,641 changes that were introduced by 165 countries in their FDI laws, 95% were in the direction of greater liberalization. Many countries had established investment promotion agencies to attract inflows of FDI, and the World Association of Investment Promotion Agencies (WAIPA) was established in 1995. In 1991, UNCTAD started to publish an annual World Investment Report that provides data and trends relating to FDI.

As FDI increased, MNEs' voluntary behavior came under more scrutiny since there was no international regulation to constrain them. In 1999, UN Secretary General Kofi Annan offered a challenge to MNEs to form a "Global Compact" with society, adhering to a set of principles that would protect especially the environment, and human and labor rights. Increasingly, more studies were conducted to understand the impact of FDI on economic development. It became increasingly clear that the benefits of FDI were not automatic and were dependent on the proper behavior of MNEs.

Impact of FDI in Developing Countries

While intratriad investment dominates international capital movement, FDI continues to be an important source of external capital for developing countries. FDI has the potential to affect nearly every aspect of the host country's environment, including the following: the market structure and performance; technological development; human capital development, employment and wage structure; quality of the physical environment; and economic growth. While FDI provides immediate direct benefits to the host country in that it is a source of capital, tax revenue, and employment, it is difficult to determine the exact impact FDI has on other aspects of the host country's environment.

The impact of FDI on the host country's market structure and performance is not easily understood. Some argue that the competitive pressures of FDI will force the local enterprises to be more efficient if they are to survive, resulting in higher productivity and lower prices. Conversely, a foreign enterprise may be significantly superior to domestic enterprises and may either buy or drive out local firms, leading to a concentration of power in the industry.

FDI will also affect the diffusion of technology in the host country. This will occur, some argue, through vertical linkages (local suppliers and distributors) because the foreign investor's success depends on a domestic firm's ability to perform. But this can transpire only to the degree that foreign investors use local suppliers and distributors. Diffusion occurs in the horizontal direction (competing or complimentary enterprises) because the presence of FDI forces local firms to use more efficient techniques to survive. But this requires that local enterprises have the capability to imitate, which means that the level of technology is within their grasp.

FDI can also have an impact on human capital enhancement. Some argue that the skills and knowledge from the foreign enterprise will transfer to its employees, suppliers, and distributors by way of interaction and training. Foreign investors can also affect human capital through workplace standards and labor practices. Some argue that foreign investors will manage the workplace as they do at home and create an atmosphere where employees are empowered and treated with a high level of self-respect and dignity. In addition, there is a long-term impact whereby foreign investors' demand for more skilled workers directs educational policy in the country. This reasoning supports a "race to the top" hypothesis; that is, foreign investors are interested in locations where workers are trained and protected. On the other hand, some argue that a "race to the bottom" hypothesis is more likely; that is, foreign investors will go where labor is cheapest and costly standards are lax, to reduce their overall transaction costs. This in turn imposes downward pressures on wages and working conditions in the more developed investing countries. As the race to the bottom hypothesis has gained support, pressure has been applied on MNEs from developed countries to improve the working conditions in developing countries where they invest or subcontract, as exemplified by criticisms of Nike, Disney, and Wal-Mart. In addition, nonprofit organizations such as the Fair Labor Association and the Worker Rights Consortium keep a watchful eye on the activities of MNEs by assisting in the monitoring and the verification of workplace standards worldwide.

FDI can also affect the physical environment. Even when the latest technology is used, industrialization negatively affects the environment, and hence, as FDI increases the industrialization and urbanization of a developing country, it can have a detrimental effect on the environment. But not all the environmental consequences associated with FDI are necessarily negative. Foreign investors may bring technological solutions that are environmentally superior to those currently in use in the developing country. On the other hand, they may use the developing country as a dumping ground for inferior or obsolete technology. And host countries may be tempted to relax environmental standards to attract FDI.

FDI will also have an impact on economic growth. While there is little argument about the idea that FDI is a source of capital and tax revenues and thus provides benefits in the short term, what is of even greater concern for long-term development is domestic investment. Some argue that FDI will crowd out local enterprises and actually be detrimental to economic development in the long run. While there is some evidence of crowding out, especially in countries where mergers and acquisitions figure prominently in FDI inflow, another view is that FDI "crowds in" domestic investment by creating complimentary activities, and thus spurring local investment.

There has been an abundance of empirical studies to evaluate the true impact of FDI on developing countries. The overall prognosis is that the indirect benefits of FDI are not automatic. Developing countries are extremely heterogeneous, and the exact nature of the impact varies between industries and between countries. The country's characteristics and policies are important determinants of the net benefits.

—S. L. Reiter

See also Bretton Woods Institutions; Development Economics; Double Taxation; Economic Growth; Fair Labor Association (FLA); Free Trade, Free Trade Agreements, Free Trade Zones; Global Business Citizenship; Global Codes of Conduct; Globalization; International Monetary Fund (IMF); International Trade; Mergers, Acquisitions, and Takeovers; Multinational Corporations (MNCs); North American Free Trade Agreement (NAFTA); Organisation for Economic Co-operation and Development (OECD); United Nations; United Nations Global Compact; Worker Rights Consortium (WRC); World Bank; World Trade Organization (WTO)

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Fraud

Fraud is a generic term that encompasses the multifarious and often ingenious means by which one individual can gain an advantage over another through deliberate false suggestion, concealment, or misrepresentation of the truth. Fraudulent acts include the forging of documents, tampering with scales and measures, false bookkeeping, and intentionally lying in contractual negotiations. In ethical terms, fraud combines deliberate falsehoods with a conscious willingness to prey on the trusting nature and reliance needs of others; hence, fraudulent acts carry strong moral disapprobation. In the law, fraud constitutes a defense to a breach of contract action, an affirmative cause of action in tort, and a crime.

Although the scope and scale of fraudulent practices in America are difficult to assess and measure, a significant amount of fraud seemingly touches every industry and commercial endeavor. The U.S. Attorney General's Office estimates that fraud in the health care industry alone, including Medicare fraud, illegal kickbacks, and the prescription of unneeded medical procedures, costs society in excess of $100 billion each year. Tax evasion costs the government $250 billion a year. The costs associated with Internet fraud, including fraud through online auctions, identity theft, and electronic embezzlements of various sorts similarly have been estimated at over $100 billion annually. The recent wave of managerial misconduct epitomized in the Enron and WorldCom scandals has brought accounting and securities fraud in its various forms to the center stage of the public consciousness. These scandals eroded investor confidence and contributed to a $1.5 trillion decline in the New York Stock Exchange in the year following the public disclosures. Of course, there also is good old-fashioned common-law fraud, including the schemes and scams of the unscrupulous huckster and confidence man.

This entry begins with a general discussion of the legal elements of fraud. It then examines economic and sociological explanations for various types of fraud in American society.

Legal Elements

Depending on the context, the law of fraud can be criminal or civil, state or federal, common law or statutory. Hence, there is not one law of fraud but many. Historically, the law of fraud, criminal and civil, developed in the state courts through common-law interpretation. Today, most states have enacted criminal codes that replace the various common-law crimes, including criminal fraud, with specific statutory provisions. Congress also has enacted several antifraud statutes, many of which provide for both criminal penalties and civil remedies. The common law of fraud retains its relevance, however, supplementing the various federal and state statutes by providing a civil action for fraud when no statute applies.

The elements of criminal fraud are specified by statute. Some criminal statutes address the *means* through which fraud is perpetrated; others are limited by the *substantive context* in which the fraud occurs. For example, the federal Wire Fraud Act addresses means, making it a crime to engage in fraud over the radio or television. The Sarbanes-Oxley Act and Lanham Act differ by substantive context, with the former pertaining to managerial fraud and the latter defining fraudulent advertising. State statutes also differ by substantive context, with one statute addressing nursing home fraud, a second statute covering bank forgery, and yet another statute addressing insurance frauds. Criminal fraud at both the state and federal levels typically constitutes a felony, and sanctions generally include significant fines and imprisonment. As in any criminal case, the prosecutor must prove each element of criminal fraud beyond a reasonable doubt.

The common law specifies the elements of civil fraud. The *Restatement (Second) of Contract* defines civil fraud as (1) an intentional (2) misrepresentation (3) of material fact (4) that is reasonably relied on, causing an injury. Pursuant to the common law, whenever one party fraudulently induces another party to enter a contract, the defrauded party can rescind that contract and get a full refund. The defrauded party can also sue for civil damages in tort law, receiving both compensatory damages and often a punitive damage as well. A punitive damage goes beyond compensation, seeking to punish the wrongdoer rather than simply compensate the victim.

The *Restatement* provides a good working definition of fraud. Although the *Restatement* addresses civil law, not criminal, the statutory elements of most criminal frauds mirror those of common law. Hence, the elements of criminal and civil fraud are essentially similar. On first look, the four elements enumerated in the *Restatement* may seem deceptively simple; yet, each is open to interpretation and has its own vagaries and dynamics. To get a fuller understanding of the social, ethical, and legal issues associated with fraud, it is useful to look at each of these four elements in more depth.

Intent to Deceive

The common law distinguishes between fraudulent misrepresentations and innocent misrepresentations. The former arises when an assertion of fact is consciously false and the falsity is intended to mislead the other party. An innocent misrepresentation, in contrast, arises when the asserting party does not know and has no reason to know that the assertion he or she is making is false; that is, there is no intent to deceive. If a party enters a contract induced by an innocent misrepresentation, then contract law will often allow that party to rescind the contract and get a refund. An innocent misrepresentation, however, does not constitute a tort or crime.

Fraud involves *scienter,* or intentional deception. Sometimes the deception is premeditated, with steps taken to conceal the fraud. For example, suppose a used car salesperson rolls back an odometer with the intent to mislead the buyer into thinking the car is worth more than it is. Knowing that this act is both unethical and illegal, the salesperson forges mileage documents to conceal the deception. The salesperson's purposeful and premeditated state of mind constitutes the highest form of culpability and blameworthiness and accounts for fraud being treated as a crime and may justify the implication of a punitive damage as well.

Reckless misrepresentations may also be fraudulent. The common law defines recklessness as the "unreasonable taking of a known risk." To illustrate a reckless intent, suppose a businessperson is selling a business and has provided the latest cash flow information pertinent to the sale. Before the deal is finalized, new data come in. If the businessperson purposely avoids seeing the new data so as to avoid any duty to provide bad news, he or she is behaving recklessly and could potentially be liable for fraud.

The purposeful avoidance of negative information may have been at work in the Enron case. Ken Lay, former CEO at Enron, has claimed that he did not know of the fraudulent schemes undertaken by other members of his organization. He has argued that this lack of knowledge negates any criminal intent. Most courts, however, hold that reckless disregard for the truth or, alternatively, willful ignorance, is sufficient to establish criminal intent. In this light, simply saying that one did not know that financial records were false would not disprove scienter so long as the former CEO had reason to know that there was a significant risk that the records were false and intentionally disregarded that risk.

Misrepresentations

To establish fraud, one party must prove that the other party made a misrepresentation. Most commonly, the misrepresentation is expressed in spoken or written words. For example, when the confidence man claims that the forged painting is an original Rembrandt, or the tax fraud submits a false tax claim, each has made a misrepresentation in words. Misrepresentations can also be made through actions: For instance, when a real estate vendor constructs a false wall that conceals structural damage to the home, the act of concealment constitutes a misrepresentation that the structure is sound. The acts of forging a signature or tampering with scales similarly constitute misrepresentations even though no words are used.

Sometimes failing to either act or speak can be interpreted as a misrepresentation. This occurs whenever a person has a legal duty to take action or to speak but does or says nothing. For example, a person who sells a product with a latent and dangerous defect has a legal duty to warn the buyer of the danger, and failure to warn may be interpreted by the buyer as an assertion that the product is safe and sound. In such a setting, intentionally omitting to mention that danger can be both unethical and illegal.

Exactly when a party has a legal duty to speak up in contract negotiations and other business settings varies from state to state, and the law is constantly evolving. Nonetheless, some aspects of the law seem fairly clear. As a general rule, sellers must warn buyers of product defects that pose potential dangers to human health and safety. Sellers also have a duty to fully respond to reasonable questions posed by buyers and to clear up half statements that may be misleading. For example, suppose a buyer in a real estate transaction asks the seller about the annual taxes on the property. The seller provides truthful information about taxes in previous years but intentionally fails to mention that higher tax rates now apply and that the county assessor has recently raised the appraisal on the home. resulting in a significant net increase in the property's tax burden. Responding with misleading half statements in response to reasonable questions posed by the buyer is not only unethical, but it is potentially criminal fraud as well.

The common law also recognizes a heightened duty to speak in fiduciary relationships. A fiduciary is a trusted person. Classic fiduciary relationships include trustee/beneficiary, doctor/patient, corporate executive/shareholder, and attorney/client. In each case the trusted party has undertaken a duty to act primarily for the benefit of another. In such settings, if the stronger party seeks advantage over the weaker party, an act of fraud may occur. Consider, for example, the fraud of insider trading. An executive who uses inside information to trade on the executive's own account takes unfair advantage of shareholders who are unaware of the information the executive is trading on. Such trades are deemed fraudulent even if the executive makes no direct misrepresentations. Similarly, physicians who prescribe questionable procedures without explaining other options to the patient may be violating a fiduciary pledge to avoid the excesses of self-serving behavior.

Material Fact

To be fraudulent, the misrepresentation must concern a material fact. The common law distinguishes facts from opinions. Facts typically can be proven or disproved; opinions cannot. For example, if a salesperson states that a toothpaste tastes great, this is an opinion; claiming that in an experiment 7 out of 10 people rate the taste as great is a statement of fact. Facts also concern things of the past or of the present rather than predictions of the future. For instance, projecting that a business is likely to earn increased cash flows in the future is most likely an opinion. Stating that over the past decade the business has witnessed a steady increase in cash flows constitutes a statement of fact.

The distinction between fact and opinion may become blurred when an expert expresses the opinion. For example, stockbrokers and investment bankers routinely offer expert opinions on which stocks to buy. Presumptively these opinions are based on hard facts, independent judgment, and applied expertise. Suppose, however, that the expert has a conflict of interest so that the expert has a financial incentive to encourage the buying of particular stocks. This was a common scenario in the recent wave of financial scandals that struck Wall Street. It appeared that certain opinion letters were skewed to favor the hidden agendas of the advising companies. In such contexts, expert opinions can be sufficiently factual to support a legal claim for fraud, including criminal fraud.

A fact is material when it is of significance and importance to the defrauded party. Immaterial matters are of relatively little or no importance. For example, suppose a seller of a used car states that the car used to be owned by a famous country-Western singer. To most buyers, such a statement would be immaterial; they would base the decision to buy or to not buy the car on other criteria. On the other hand, if the transaction depends on the veracity of such information, then the assertion is material, and if it is knowingly false, then the seller may have committed fraud.

Reasonable Reliance Causing an Injury

The final elements of fraud are reasonable reliance and injury. Ultimately, fraud involves predatory behavior. The defrauding party makes a misrepresentation fully intending that the other party will trust that the misrepresentation is true. When the assertion proves false, the trusting party gets hurt. If the lie was intentional and the innocent party's reliance was reasonable, then fraud, both civil and criminal, has been committed.

The question arises as to when it is reasonable to rely on the representations of one's trading partner. Traditionally, the law has required business actors to be fairly self-sufficient and to take reasonable steps to inform themselves with regard to the material aspects of any business transaction. In other words, parties cannot always reasonably believe the representations made by their trading partners. Such a rule may reflect an economic logic by encouraging people to take cost-effective precautions and by rewarding self-industry. If one can easily check the veracity of the assertions made by one's trading partner, then it may be unreasonable not to do so.

The common-law rule of caution and self-sufficiency may also reflect traditional marketplace ethics. In the absence of a fiduciary relationship, a reasonable person should generally assume that his or her trading partner is primarily self-interested. Given an assumption of self-interest, words of inducement during a business negotiation must be taken with a grain of salt. For example, it is customary for salespeople to emphasize the positive aspects of a transaction and potentially to engage in a little puffery, framing their wares in the best possible light. Both marketplace ethics and the law distinguish between legitimate and acceptable sales puffery and material misrepresentations, with only the latter potentially constituting fraud. Buyers are expected to exercise both caution and common sense.

Sometimes, however, salesmanship can go too far, and increasingly courts are using the law of fraud to discourage overly aggressive sales tactics. This is particularly true whenever there is a high degree of expertise involved in the transaction and unequal access to information. In an increasingly specialized society, asymmetric information has become the norm rather than the exception. Specialization is the key to a bountiful society, but it also creates dependency and places a premium on trust. In highly specialized settings, relying on one's trading partner seems reasonable, and abuses of confidence appear unconscionable.

Causes of Fraud

Fraudulent behavior may be at an all time high. On any given day, the business pages of the *Wall Street Journal, New York Times,* and *Washington Post* are likely to report some sort of high-profile fraud. Consider for example recent scandals in defense contracting. Headlines announce that a major defense contractor has admitted to overbilling the U.S. Navy by tens of millions of dollars, another contractor has agreed to pay $37 million in a cost-inflation scam, and a third contractor may have been overcharging for fuel in Iraq. Of course, fraud is not limited to defense contracting or even to traditional business contexts. For example, commentators estimate that half of major league baseball players use performance-enhancing steroids. Studies report that 80% of "A" students admit to having cheated on an exam and suggest that nearly half of all résumés contain lies. Overall, employee theft totals $600 billion annually, or 6% of GDP.

What then accounts for fraud? Perhaps one explanation derives from simple economics. According to economic theory, people respond to pecuniary incentives. Apparently too many people in too many settings conclude that fraud pays. Given the difficulty in detecting and proving fraud, it is far from clear that they are wrong. Certain forms of white collar crime such as insider trading or tax fraud are notoriously difficult to detect and prove, and even if the crime is detected and proven, prison sentences may be light. Economic theory predicts that the rational businessperson will calculate the potential gains from the illegal behavior and compare those gains with the potential costs associated with criminal and civil sanctions and loss of business reputation. The perception, and likely reality, that fraud pays may explain the widespread instances of consumer fraud, tax fraud, Medicare fraud, and the like.

Of course people do not always commit fraud just because it is in their financial interest to do so. First, people value things other than money, and a person may feel a sense of shame from blatant criminal activity such as tax fraud, securities fraud, or insider trading even if their guilt goes completely undetected. This suggests that for many people, it is in their non-pecuniary self-interests to obey the law, even when fraud pays. Second, people often act out of a sense of public duty. If a person has sufficient respect for the rule of law in general or respect for the law in question, then they may restrain themselves even if they calculate that crime pays. Third, people are not always so calculating. Most commonly, people obey the law simply from habit without calculating anything.

Ultimately, there seems to be a trade-off at the core of fraud. Fraud occurs in part because society commits too few resources to detecting fraud and provides penalties that are too light. But fraud also occurs because people fail to restrain themselves. To be willing to obey a law of fraud that is not effectively enforced, people must recognize that fraud in its various forms is inherently wrongful and embrace a duty to act accordingly.

—Daniel T. Ostas

See also Bluffing and Deception in Negotiations; Consumer Fraud; Deceptive Practices; Ethics of Persuasion; Identity Theft; Insider Trading; Negotiation and Bargaining; Ponzi Scheme; Sarbanes-Oxley Act of 2002; Scandals, Corporate

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Freedom and Liberty

The idea of liberty is closely associated with the concept of freedom, although *freedom* may be slightly broader in its meaning. Compared with *freedom, liberty* carries clearer associations with the social and political world, and this entry addresses that social and political meaning of freedom and liberty.

Thus, we are not concerned with the issue of free will versus determinism. If we lack free will in the sense that we have no choices and that all human behavior is causally determined by the laws of physics since the beginning of time, then our discussion of liberty and freedom lacks significance. Nor does this entry consider restrictions on behavior and choices that result from the laws of nature in the ordinary sense of the term. No human is free to fly under his or her own power, but that is not a restriction on his or her liberty in the current sense of the term.

Positive and Negative Liberty

Contemporary discussions of liberty typically take their starting point from a famous article by Isaiah Berlin, "Two Concepts of Liberty," which was published in the middle of the 20th century. Berlin distinguishes between "negative" and "positive" liberty. Negative liberty is concerned with freedom from certain external restraints, while positive liberty is concerned with the agent's internal freedom to act in certain ways. Negative liberty addresses restrictions on the scope of control that a person faces, while positive liberty focuses on the source of control. Negative liberty emphasizes external constraints, while positive liberty gives weight to internal factors, such as psychological ability or inability to act in certain ways. Doctrines of negative liberty emphasize the importance of freedom from interference by others, while theories of positive liberty are concerned with one's ability to control and shape one's own life. As most commentators would agree, it is extremely difficult to draw a sharp line between negative and positive liberty, yet the two ideas represent different general outlooks about the factors that are important in assessing human freedom and liberty.

Negative Liberty

In the most minimal sense of liberty, one is free if one is not physically restrained. Thomas Hobbes emphasized this conception in his *Leviathan,* while recently Hillel Steiner has argued that one is free unless some other individual makes an action impossible. An armed robber may threaten death, but in this very limited sense, one is still free to refuse to surrender her wallet. The robber's gun makes the surrender of the wallet less desirable, but one is free, in some sense, to refuse. But virtually all theorists of freedom would agree that physical restraint limits freedom. We may take absolute physical restraint as one end point in what it means to be free. In a way, this minimalist conception of freedom lacks interest—we all hope for a richer freedom for ourselves.

A slightly more robust sense of liberty asserts that one is free unless one is "subject to the arbitrary will of another." For many authors in the libertarian tradition, the direct coercion of one person by another is the paradigmatic violation of one's freedom. The master, for example, can dispose of the slave, so the slave is subject to the arbitrary will of his master. This slightly broader conception of freedom would regard the victim of a robbery as lacking freedom. In this view, the key criterion of freedom is absence of coercion, the paradigmatic case of which arises when one person directly forces another to perform a certain action or prevents a person from acting in a certain way. The coercion can also be by a group of people against another person.

But what is to count as coercion is often somewhat unclear. Expanding our robbery example somewhat, would a gang of teenage toughs in a dark street verbally demanding a wallet, be coercive? In contrast with the armed robber or gang, an aggressive panhandler may make it desirable to surrender a donation, but is this an example of coercion? More broadly, some even speak of "coercive wage offers"—an offer that one feels compelled to accept merely due to an absence of better choices. In contrast, if we take an offer as an overture that may be rejected without changing the position one had before the offer, some deny that any offer can be coercive. When we compare the view of freedom as the absence of absolute physical restraint with the slightly broader idea of coercion, we begin to see that there is a continuum of actions by others that can be seen to limit our freedom differentially. This idea of a range of possible restrictions on liberty reveals the motivation for maintaining that only absolute physical restraint restricts freedom. Otherwise one may be embarked on a "slippery slope" toward an ever more expansive idea of freedom.

So far, we have considered obstacles to freedom that are placed on one person by another person or group of persons. These views we have been considering would not count laws and regulations as limits on freedom. However, when we turn to liberty in a social or political context, many thinkers maintain that laws and regulations limit individual freedom. Legal speed limits deploy the coercive power of the state with the intention of restricting behavior, for example. If such laws do not intend to restrict our freedom to drive as rapidly as we wish, what point could they possibly have?

As we consider the relationship between individual liberty and the power of the state, we reach the core concern for the theory of negative liberty. Thus, when we consider the issue of political freedom, we reach a very practical level of concern. If we value individual freedom as consisting of the absence of constraints, what laws should we have that limit some freedoms, and what effect do these limitations on freedom have for the freedom of others?

Advocates of political freedom typically maintain that there must be a region of activity and concern that lies within the province of the individual alone and that the state must not infringe on this personal space. This way of thinking about political liberty developed most intensely from the Enlightenment to the present day and takes political liberty as its touchstone. Thus, we find theorists such as John Locke maintaining that the state should not infringe on one's "life, liberty, and property," just as the United States Declaration of Independence insists that one must be free to enjoy "life, liberty, and the pursuit of happiness." In the same spirit, John Stuart Mill asserts that *liberty* simply means "protection against the tyranny of the political rulers."

The tradition of thought that insists on protecting an individual's private sphere of action against state intrusion is known as *classical liberalism.* Liberalism in this sense is the ancestor of, but quite different from, the doctrines of current-day liberals in U.S. politics, which generally countenance considerable state intrusion in some areas of human life but not in others. Classical liberalism is much closer to the political philosophy of libertarianism. Classical liberalism maintained that the state's regulation of individual conduct should be held within very strict bounds to ensure a wide-ranging individual freedom. To a considerable extent, this tradition views a key function of the state as placing minimal restrictions on the freedom of some only to maximize the extent of freedom that can be enjoyed by all.

Among many thinkers of the early modern period, the goal was to promote freedom across all citizens. In their conception, this required placing the minimal constraints on the liberty of some that would expand the freedom of others. Thus, laws against theft aim to restrict the freedom of would-be thieves to expand overall societal freedom.

Classical Republicanism

In these different versions of negative freedom, the emphasis has been on actual palpable restrictions of the freedom of one person or group of persons by another person, persons, or the law. But what if the restrictions are not actual but only potential? For example, consider a state ruled by an absolute dictator, who happens to be benevolent toward her citizens. People in that state might have a great deal of freedom that they can exercise from day to day, but they live under the shadow of a government that is not of their own devising. Similarly, consider a state that exists under the hegemony of a much more powerful neighbor. The weaker state's existence and the freedom of its people are not secure.

Some theorists of freedom maintain that the residents of the autocratic state or the dominated state would lack freedom. In recent years, thinkers such as Pettit and Skinner have striven to revive what they identify as the classical republican theory of freedom. Under this view, people are free only if they live in a state in which the actions of the body politic are determined by the community as a whole. This would not be the case, they maintain, in our examples of either an autocratic state or the dominated state. More specifically, the theory of classical republicanism maintains that freedom requires the unconstrained enjoyment of a wide range of civil rights, including the right to participate in the making of laws. In short, if a person or people are within the power of others, even potentially, that person or people lack freedom.

If the classical republican view is correct, it implies that restrictions on negative freedom need not always be intentional. The benevolent autocratic, for example, does not aim to restrict the freedom of her citizens. This situation differs significantly from the narrow view that we considered at the outset, in which one person physically constrains another or in which one person intentionally coerces another.

Must Restraints on Negative Freedom Be Intentional?

Theorists of negative freedom are divided on the question of whether negative freedom is diminished only by intentional restrictions. Consider for example a situation in which a clerk locks a store's stockroom at the end of the day. Unknown to the clerk and contrary to all custom, a colleague was sleeping there. Later, the sleeper awakes to find that he cannot exit. Clearly, a person in this situation would feel a lack of freedom quite acutely. Whether we should think of this kind of example as illustrating an unintentional reduction in negative freedom or as an instance in which one's free movement is constrained by physical circumstances instead of the actions of a person is not clear, and there is much debate on this topic.

But we can shed more light on this issue by thinking again of the autocratic state ruled by a benevolent despot who really wants what is best for the people of that state. In such a case, it is easy to see that many people in the state might readily feel they have less freedom than they would in a democratic state, and they may even act in a way consistent with an absence of freedom. In this case, the lived experiences of citizens in the autocratic state can be ones in which freedom is reduced and actions that might be undertaken under circumstances of more robust freedom are foregone.

This survey of curtailments of negative freedom began by considering the brute force of physical restraint and then went on to consider milder forms of a loss of liberty, such as direct coercion of various sorts and the coercive effect of the law. But we ended by analyzing a state in which there is no specific restraint on liberty but where the feeling of freedom is curtailed and actions of a free person are sacrificed under the specter of power outside oneself. This brings us to the positive theory of freedom, which emphasizes one's ability to experience life as free and to be able to implement a life plan that one chooses.

Positive Liberty

While negative liberty focuses on the obstacles that limit one's actions, the concept of positive liberty concerns a person's freedom to carry out a plan of action. Negative liberty addresses the external obstacles to one's free action, while positive freedom focuses on the internal psychic obstacles to a plan of action. But not just any plan of action is at stake but the very ability to carry out a plan of life. Thus, positive freedom is concerned with issues of self-realization, self-determination, and self-mastery.

Imagine you observe someone moving freely around his or her house, looking in this cupboard, opening that drawer. No external impediments block the person's path. Eventually, this person finds a pack of cigarettes, nervously lights up, and takes a long draw. Those actions now seem to take on a different meaning. It becomes plausible to say that the person was not acting in a manner that was fully free but rather was driven by a strong habit or even an addiction. Such impediments are internal and lead to considerations of limits on positive freedom. Without meaningful control over oneself, it is impossible to implement a life plan, and those who emphasize the concept of positive freedom want to focus on these issues of self-control and self-direction.

But factors other than a drug addiction can limit our positive freedom. For instance, a lack of self-respect and self-confidence can impair a person's ability to undertake a course of action that they would have good prospects of being able to complete if they would merely try. A lack of these internal psychic resources may limit one's freedom to act and achieve. To addiction, we might add irrational desires, illusions, compulsions, and phobias as other types of freedom-limiting psychological states.

Against this line of argument, one might say that our concern here is with freedom in the social and political sphere, not limitations on freedoms that arise from our neuroses or psychological limitations. Yet theorists of positive freedom—Rousseau and Marx for example—emphasize the social and political factors that can be internalized and come to limit positive freedom just as a lack of self-confidence might. Thinkers in this tradition tend to maintain that social and political factors do affect the consciousness of individuals and can incapacitate them for developing life plans they otherwise might be able to undertake. They would maintain that social and political circumstances can lead to just the lack of psychic resources that limit positive freedom.

Think, for example, of a slave who through long captivity becomes inured to his state. While this person might once have had ambitious plans, a long history of servitude has slowly compressed the scope of his desires such that he now feels quite content with his station in life. This sequence of events has led to psychological changes that limit the slave's capacity for action and thwart his positive freedom. He no longer considers or even desires to undertake certain actions that are inconsistent with his slavery.

A society structured in a way that frustrates the realization of life plans of its citizens may be subject to serious criticism for limiting positive freedom—especially if these factors become internalized. For example, a society that engages in ideological manipulation of its subjects may lead to the internalization of freedom-limiting attitudes. Furthermore, a society may be structured in such a way that a large segment of its citizens come to see its opportunities as considerably diminished. This is, in briefest terms, one of the criticisms that Marx levels against capitalist society. The bourgeois world, according to Marx, has abused the workers to such an extent that they no longer understand their capacity and have come to accept their diminished place in a corrupt society. In short, for such people positive freedom is limited by internalized factors, but social and political arrangements might be responsible for engendering those limitations. Finally, it is important to note that those who emphasize positive freedom also acknowledge that people suffer from various restrictions on their negative freedom. Thus, positive freedom theorists expand the concept of freedom beyond merely negative freedom.

Resource Constraints and Disincentives as Impediments to Freedom

While negative and positive concepts of freedom focus on external blocks and internal disabilities, respectively, some find yet another class of freedom-limiting structures in the social and political sphere. Implementing virtually any plan of life requires some resources. At the most elemental level, if one lacks food, one lacks freedom to implement many life plans that would be within the ordinary scope of human endeavor. For example, in his "capability approach," Amartya Sen argues that one must have resources to be free to act in a fully human way. Focusing largely on emerging nations, he addresses the necessity for economic development in creating the conditions of freedom.

Similarly, a society may be structured in a way that makes human achievements difficult. A structure of cumbersome disincentives might arguably limit the scope of one's freedom. For example, a society could be organized with a system of economic regulations, religious prohibitions, and social expectations that would limit the life choices of its people. Resource constraints and a social structure that reduce one's choices do not seem to be instances of constraints on negative or positive freedom. Yet there can be no doubt that such factors can limit life prospects and that circumstances in such a society can be felt as freedom limiting.

Freedom, Rights, and Distributive Justice

While this entry concentrates on freedom and liberty, it is important to realize that freedom and liberty are generally regarded as a special case of a broader class of rights. In the modern world, we tend to regard freedom as a right. We may think of freedom as a human right that obtains independent of all social organization, or we may think of liberty as a right guaranteed by the political structure of a nation. For example, this second way of thinking of liberty as a right has been an intellectual cornerstone of the United States since the American Revolution.

But freedom, like almost all rights, is seldom absolute. This certainly proves true in practice, and rights are generally not regarded as absolute and inviolable in theory either. This is necessarily the case because one right can often conflict with another, and one right can also conflict with other important values.

Not only can freedom conflict with other rights, but one person's freedom often conflicts with another's also. My negative freedom to park my car in a particular spot may conflict with your negative freedom to park in the same location, at least on some interpretations of negative freedom that we considered above. Also, one form of freedom can conflict with another. For example, some assert that we possess a negative right to engage in commerce as we wish without governmental interference. Critics of unrestricted commerce maintain that the rapacity of the economically successful will impoverish some members of society and leave them in dire circumstances. As discussed earlier, the positive freedom to implement a plan of life requires a resource base. If these critics of unfettered commerce are correct, the result of this process would be the diminishment of the positive rights of economic losers. Thus, one version of freedom can conflict with another.

Freedom, like many other rights, can conflict with other values that are not considered rights. For example, many believe that freedom can conflict with the values of equality and a just distribution of society's resources. If the critics of unfettered commerce are correct, and the pursuit of profit by the able leads to the impoverishment of others, equality of resources in a society will be grossly affected, and the resulting distribution of resources may be unjust.

Freedom and the World of Commerce

Freedom is a key concept of all dimensions of human life, including business, and the different ways in which freedom and liberty can be exercised and denied in commerce are numerous. This section uses the concepts of freedom outlined above to explore a sample of business issues that illustrate issues of freedom and liberty.

Economic Liberty

The idea of economic liberty emerged with the advent of market society and developed into a key principle of economic thought from the 17th through 19th centuries. The idea that one should be able to enter contracts freely, to dispose of one's property as one wishes, and to engage in commerce without government interference was a core belief of classical liberalism during this era. As such, the idea of economic liberty is essentially a species of negative liberty because economic liberty enshrines *freedom from* interference with business operations.

Of course, government regulation does restrict economic liberty. In part, these restrictions limit the economic freedom of some persons to expand the economic freedom of others and perhaps to enhance freedom across society. It also seems that some restrictions on economic liberty attempt to foster values other than negative liberty. For example, rent control policies directly interfere with the economic liberty of the landlord in the interest of benefiting the tenant in a way that has no necessary association with the economic liberty of the tenant.

Minimum wage laws, working condition regulation, and restriction on working hours are all examples of ways in which government restricts economic liberty in the pursuit of other values. Similarly, legal prohibitions on deceptive advertising and consumer fraud also intentionally limit economic freedom and have the aim of promoting the public good. Under the doctrine of "employment at will," both the employer and the employee are free to terminate the employment contract at any time without notice and without cause. In a way, such an arrangement seems to epitomize economic freedom for both parties. While employment at will continues to be a widespread doctrine of employment law, governments constrain the employer side of this relationship to a considerable, and perhaps growing, degree.

Contemporary, highly developed, industrial countries generally support economic freedom, at least in concept, but they all place limits on economic freedom as well. The argument for such policies is that, while economic freedom is to be valued, it must be restricted to some extent to prevent rapacious behavior. While most observers of economic life would support the idea that there must be some restrictions on economic freedom, the nature and extent of those limitations continue to be hotly debated.

Sweatshops

Other business practices bring issues of both negative and positive freedom to the fore. Consider, for example, the controversy over sweatshops and a living wage. *Sweatshop* is a pejorative term that usually refers to a manufacturing facility located in a developing country with market-determined wages that are very low and working conditions that are extremely harsh. Usually the term refers to a facility that makes some good for the industrialized West.

The economic arrangement of sweatshops seems to emerge from the exercise of economic liberty on the part of the employer, but some observers contest that the workers who have accepted these wages and conditions have the opportunity to exercise their full freedom. For example, some activists insist that it is morally required that working conditions be improved and that workers in these facilities receive a "living wage"—a wage that will sustain a reasonable standard of living in the local economy. Here, a living wage contrasts with the market wage, with the presumption that the living wage is higher than the market wage.

Critics of sweatshops often maintain that employment at such low wages and in such bad working conditions results from a lack of negative freedom on the part of the workers. They regard the terms of employment as being the result of a "coercive wage offer"—an offer of employment on such unfavorable terms that only a person with no meaningful freedom of choice would accept. On this account, the workers lack negative freedom and are being coerced by the employer. (Traditional defenders of classical liberalism would deny that any offer that one can refuse without altering circumstances that prevailed before the offer can be coercive.)

Living wage proponents also typically maintain that the terms of employment in sweatshops interfere with the positive freedom that all people should enjoy. As we have seen, many thinkers believe that a person enjoys positive freedom only when she can implement a meaningful life plan. On this account, the employment bargain characteristic of sweatshops frustrates the positive freedom of workers because the wage contract restricts the resources necessary for anyone to implement such a life plan.

Globalization

In a similar spirit, many critics reject the movement toward globalization on the grounds that this economic movement interferes with the positive freedom of people in poorer economies. More specifically, they charge that the invasion of developing countries by multinationals reorganizes economic life in those countries, dominates and perverts the local culture, and frustrates the positive freedom of the local inhabitants to choose their own life plans.

Right to Work

As another example of positive freedom in the context of business, Article 23 of the Universal Declaration of Human Rights promulgated by the United Nations includes the following provision: "Everyone has the right to work, to free choice of employment, to just and favorable conditions of work, and to protection against unemployment." Exercise of this right to work is essentially an instance of a positive freedom. It is a *freedom* to have employment, the income from which is regarded as essential to the implementation of a meaningful plan of life.

Personnel Issues

Finally, personnel issues for individual employees can interfere with one's negative and positive freedoms. For example, sexual harassment on the job is a violation of a worker's negative freedom. Similarly, surveillance makes one behave differently than one otherwise would. So, inappropriate surveillance of employees violates their negative freedom by violating their zone of privacy. Various forms of discrimination in employment can violate both negative and positive freedom. Racial and sexual discrimination violate one's negative freedom from unjust interference, but both forms of discrimination also interfere with the positive freedom to pursue a meaningful life plan. Similarly, illegitimate hiring and advancement policies interfere with one's positive freedom to pursue a meaningful career as part of a plan of life.

—Robert W. Kolb

See also Capabilities Approach; Coercion; Employment Contracts; Empowerment; Free Market; Friedman, Milton; Globalization; Hayek, Friedrich A.; Justice, Distributive; Laissez-Faire; Liberalism; Libertarianism; Market Socialism; Marxism; Paternalism; Racial Discrimination; Regulation and Regulatory Agencies; Rent Control; Rights, Theories of; Right to Work; Sexual Harassment; Slavery; Sweatshops; Wage-and-Price Controls; Workplace Privacy

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Freedom of Contract

There are three basic institutions that provide the framework for all economic transactions in contemporary society, namely, market, governmental regulation, and contract. The economic analysis of their performance and function reveals that contracting is an especially effective legal institution in coordinating private economic transactions if the following requirements are satisfied in the process of contract formation and contract performance: freedom of contract, fairness and social utility, bargaining power parities, symmetric information and transparency of intentions, third-party exemption, possibility of adjustment, and legal forum for settlement and enforceability.

Freedom of contract is sometimes explained as deriving from the prepolitical notions of freedom and autonomy, which assign rights to the individuals to plan, consider, and pursue their welfare. Other contract theorists originate freedom of contract within democratic self-government and the division of responsibility between the citizens and the state for promoting just society, and individual and social welfare. One of the basic duties of the liberal state is to recognize its citizens' rights to freedom of contract and to protect their voluntary, rational, and lawful consent from coercion or interference in their private transactions. Therefore, governmental and judicial intervention in private contractual relationships by means of legislation and court rulings must be limited to equal protection of citizens' rights, their rightful expectations, and the legal enforcement of their obligations. Briefly, freedom of contract is constitutionally protected in a liberal society. Besides moral and political claims for freedom, autonomy, and responsibility, freedom of contract is also justified by the fact that it provides the most efficient welfare-enhancing institution for coordinating the transfer and exchange of property, rights, and entitlements among the members of society. Therefore, considerations as to whether private contractual arrangements enhance individual and social welfare do not fall outside the purview of legislation and jurisdiction. Jurisprudence and the law based on these philosophical, economic, and political theories have attributed central importance to freedom of contract—and ownership rights—since the last decades of the 19th century.

Nevertheless, the proponents of legal realism and critical legal studies, to mention a few influential legal schools, discuss critically the notion of freedom of contract and regard it as an ideological doctrine of jurisprudence, which is rooted in 19th-century laissez-faire capitalism. One of the most persuasive arguments against classical contract theory comes from the plain fact that standard form contracts created and used by business enterprises in transactions with their clients and customers are predominant in the economy today. In the case of standard form contracts, bargaining—whereby the contracting parties attempt to draft a contract, determine its contents, and agree on contract terms and conditions of performance—virtually never takes place. Price frequently comes under the nonnegotiable terms of contract as well. These types of contracts do not depend on *aggregatio mentium* or *consensus ad idem,* namely, the meeting of the minds of the parties. Standard form contracts are deliberately drafted on a take it or leave it basis. *Freedom of contract* rarely means freedom of contract from the point of view of the nondrafting party. We have to conclude standard form contracts on a daily basis without following the steps of contract formation prescribed in contract law textbooks. Bargaining inefficiencies, high transaction costs of contract formation, asymmetric information, and other market imperfections give business enterprises opportunity to create their own private ordering and to impose less favorable or even unfair terms and conditions on their nondrafting parties. While it is necessary to choose the law of the jurisdiction to avoid choice-of-law conflicts in private contractual arrangements, business enterprises can also capitalize on the global commercial environment, especially in the case of online transactions. Mutual acceptance of governing law, forum, arbitration, and judgments on the part of the contracting parties are also absent in standard form contracts. Business enterprises choose the exclusive jurisdiction and venue of the courts on whose territory they are incorporated, even if the place of performance is in another hemisphere. They also endeavor to opt out of the legal jurisdiction that prescribes high and strict standards for contractual liability and contains detailed regulations on the protection of consumer rights. As a result, a legal forum for settlement is practically inaccessible to the nondrafting parties—most often, clients and customers—when contract disputes arise. The geographical distance of courts located far away from the place of performance, high transaction costs, and the imperfect knowledge of contract terms and governing law provide disincentives for the other party to seek remedies for unconscionability, undue influence, harm, or contract breach. Nondrafting parties typically take the option of rational ignorance and do not educate themselves about terms and conditions of contract to become informed and rational decision makers. In doing so, they seek to avoid incurring the high transaction costs of obtaining information, negotiation, and contract formation. Therefore, the well-established concepts of classical contract theory—such as offer, acceptance, and consent between equally situated and rational economic actors—lose their original meaning in the context of standard form contracts. To sum up, commercial and consumer sales contracts—boilerplate contracts, preprinted contracts, one-sided contracts, mass-market uniform adhesion contracts, take it or leave it contracts, rolling contracts, shrink-wrap and click-wrap contracts, and so on—usually do not satisfy the above-mentioned requirements for contract formation.

It does not follow from these objections that the nonnegotiated terms and conditions of contracts are inevitably unfair or surely inefficient for the nondrafting parties. However, the ritual recitation of freedom of contract in the legal literature cannot conceal the core of the problems of contract theory: There are fundamental discrepancies between the notion of freedom of contract and actual contracting practices in the economy and society. While freedom of contract is justified on the ground of the priority of individual rights and autonomy over any other considerations in contract theories, it is frequently traded off against economic efficiency. The classical model of contract theory, which focuses on atomistic individuals' discrete (one-time, clearly specified) contractual relationships, can be hardly applied to the real-world situation, where contracts are usually relational (open-ended and evolving) agreements between individuals, large economic organizations, and legal entities. Isolated, discrete, and person-to-person contracts are quite marginal in the economy today. Critical legal scholars point out that bargaining power disparities, asymmetric information, bounded rationality, opportunism, and monopolistic or oligopolistic markets can seriously undermine the ethos of freedom, self-reliance, and autonomy in private contractual relationships. These problems of private contractual arrangements lead us to constitutional dilemmas, which necessitate equitable regulatory solutions in contract law, especially when the choices of business enterprises encroach on freedom and welfare of individuals. Therefore, the state should not be a neutral and reserved observer of the economic and social consequences of unequal distribution of rights and obligations in its citizens' private contractual arrangements. Indeed, the state should play a proactive role in placing freedom, self-reliance, and autonomy in the focal point of public policy. As a matter of fact, contract law in most countries explicitly prohibits contractual terms and conditions that are contrary to the requirements of reasonableness and good faith and that cause significant imbalance in the rights and obligations of the parties. According to critical legal scholars, contract law rules are aimed not only at providing the parties with value-neutral and technical nonmandatory default rules to facilitate communication in the process of contract formation but also at implementing fairness and distributive and corrective justice in their contractual relationships. Only a binding and effective contract law regime can deter the parties from using contract terms opportunistically and can contribute to creating fair contractual relationships between individuals, economic organizations, and legal entities. They also tend to hold the view that contract adjudication should enforce individual rights and implement public policy, respectively.

The claim for more active legislative and judicial interventions and more mandatory rules in private domains is not devoid of paradox. Insisting on a clear demarcation between public and private domains, libertarian theorists think that the state must take the position of distributive neutrality in enacting contract law and private law rules in general. Paternalistic legislation in contract law and judicial activism in private contractual arrangements result in less freedom of contract and finally in less freedom in society. Despite these well-known libertarian arguments against state and judicial interference in the private domain, contemporary states prescribe substantive and procedural rules to be observed when entering into contract in almost all fields of economic and social activities. They also administer sophisticated systems of institutional and legal constraints on private contractual arrangements.

Law and economics scholars are quite skeptical about promoting fairness and justice through the coercive and distributive mechanism of the law and legal institutions in private contractual relationships. Moreover, they call into question the assumption that an omnipotent state and a coercive regime of private law could master the contractual problems by means of codifying equitable regulatory solutions, more compulsory and binding rules in contract law, and interventionist and policy-oriented adjudication. Economic analysis of contracting practices provides the best policy guideline for legislatures that seek enacting of contract law rules, completing contracts between parties, interpreting contract provisions, and applying default rules in the absence of precise or explicit wording at court. At any rate, the prevalence of standard form contracts in the economy demonstrates that they are cost effective and a rather fair alternative to active governmental and legal regulations for both parties. There is no reason to believe that mandatory and binding legal rules and more judicial interventions to prevent bargaining power disparities, information asymmetries, and cognitive biases between parties could yield more efficient and more equitable contractual outcomes. Because competitive markets punish opportunistic behavior of business enterprises in the short term, this circumstance creates incentives for them to offer fairly advantageous terms and conditions for the nondrafting parties. If they offer suboptimal contracts, the nondrafting party can quite easily choose optimal contracts in competitive markets without incurring high transaction costs of information and negotiation. Competitive markets are believed to steer all parties' decisions into a welfare-enhancing direction and to solve their contractual conflicts with or without emphasizing the importance of freedom of contract. On the face of it, this argument is convincing from an economic perspective. However, it does not rely on the rights of individuals, freedom of contract, or the proper system of contract law but rather on the priority of pricing and the market mechanism. If this assumption about market mechanism were correct, contractual disputes over performance, entitlements, and the rights and obligations of parties would never occur.

Law and economics scholars usually refer to the Coase theorem, which is thought to buttress their strong arguments against imposing legal and judicial restrictions on freedom of contract. According to the Coase theorem, in a bilateral contractual situation when the parties are free, rational, and symmetrically informed, their rights are initially well-defined, and transaction costs are zero, the allocation of resources will be efficient and invariant regardless of the underlying rule of law or alternative assignments of rights. Nevertheless, there is no general consensus of what the Coase theorem precisely proves in the context of practical contractual problems originating from bargaining power disparities, information asymmetries, undue influence, cognitive biases, and other market imperfections. The Coaseans tend to draw a conclusion from the theorem that the operation of a paternalistic legal regime and the imposition of legal and judicial constraints on private contractual transactions use up all the expected benefits of balancing bargaining power disparities and information asymmetries or setting cognitive biases and "irrational" choices of parties right. In case of proactive legal and judicial interventions in freedom of contract, the parties will privately bargain over contracting out the rules, which they assume to be inefficient. In a world of market imperfections and positive transaction costs, the strict regime of governmental and judicial regulations on freedom of contract could not provide a better resolution for contractual conflicts.

Fair and efficient outcomes of private contractual agreements will rarely emerge spontaneously from economic transactions if the initial rights of the parties are not well-defined. Government and legal institutions play the central roles in the assignment, protection, and enforcement of these rights, which give the opportunity and set a limitation for private contractual transactions. The extent of freedom and restriction allowed by law in private contractual arrangements varies from time to time since the issue is subject to endless debate.

—László Fekete

See also Bounded Rationality; Coase Theorem; Consumer Rights; Contracts; Economic Efficiency; Externalities; Fairness; Justice, Distributive; Libertarianism; Market Failure; Opportunism; Paternalism; Regulation and Regulatory Agencies; Rights, Theories of

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Freedom of Information Act of 1966 (FOIA)

The Freedom of Information Act (FOIA) is a law intended to give citizens and organizations access to government information with minimal restrictions and hindrance. The original act was signed into law by President Lyndon Johnson on July 4, 1967. It was subsequently amended to specifically include in its scope all electronically stored and transmitted information, which resulted in the Electronic Freedom of Information Act (EFOIA), signed by President Bill Clinton on October 2, 1996. The law provides a process for requesting government information, a timeline for government response, and judicial channels for forcing government compliance.

The FOIA and EFOIA laws are meant to ensure a citizen's "right to know." While usually framed in the context of national security, the FOIA has been valuable in accessing information as diverse as consumer product safety data, workplace condition reports, government-business contracting practices, environmental data, and public policy implementation and effectiveness.

In theory, democracy works best with an informed citizenry; governments are believed to best respond to the interests of their citizens when their actions are open to public scrutiny. However, in the wake of World War II and through the beginnings of the Red Scare and the Cold War, the U.S. government showed a greater reluctance to share information with the public, either directly or through news and educational organizations. Eventually, the Department of Defense adopted a policy of only releasing information that would directly contribute to its national security efforts, institutionalizing a governmental "right to withhold" and creating de facto censorship of the news media. Pressure from news organizations and growing concerns in Congress resulted in a series of congressional hearings through the 1950s and early 1960s and eventually led to the passage of the FOIA in 1966.

The cornerstone of the FOIA is its bias toward public access to government information and away from a governmental right to withhold. The law requires that the government release information unless it can prove that it should not make the requested information public rather than force the public to prove that the information is needed. Just as critically, the law also attempts to specify what constitutes "secret" information, putting in place some boundaries to the government's ability to withhold information on the basis of national security concerns.

Although the FOIA most often is applied to government information, this can also include information about individual businesses or entire industries provided to the government by lobbyists, industry associations, and the businesses themselves. Through both routine interactions (e.g., regulatory reporting, permit applications, responses to RFPs) and other more specialized activities (e.g., lobbying efforts, task force participation, informal discussion with government officials, congressional fact-finding efforts), information that businesses provide to the government in many cases becomes subject to discovery through FOIA requests. Information that businesses would prefer remain closely held may eventually become public in this way.

The law has proven to be effective in improving the flow of information between the government and the public, but it has not eliminated all problems. While the law sets a time period in which the government must respond to requests, agencies often fail to meet those requirements, either due to the volume of requests received or through intentional delays. Forcing government agencies into court over delays is costly and time-consuming, so many requests either expire due to government or public neglect or are litigated indefinitely. Especially in requests involving the FBI and CIA, requests from as far back as the 1980s and 1990s are yet to be handled, and as backlogs on all agencies grow, delay has become an effective tool for the government to withhold information.

The FOIA is not perfect, but it has become a model for similar laws around the world. In the United States, requests have increased to more than 3,000,000 per year, and the FOIA is considered by many to be an indispensable tool for the public's monitoring of government activities.

—Tom Bugnitz

See also Consumer's Bill of Rights; Ethics in Government Act of 1978; Government Accountability Office (GAO); U.S. Department of Justice

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Free Market

The free market represents an unregulated system of economic exchange. *Unregulated* in this context means that taxes, governmental quality controls, quotas, tariffs, and other forms of centralized economic interventions by government either do not exist or are at least minimal. From this definition, it is clear that the free market represents an ideal type that does not actually exist. In reality, modern societies can only approach or approximate this ideal of efficient resource allocation. In other words, real markets can be described along a spectrum ranging from low to high amounts of regulation. Many economists (such as

Adam Smith, the father of economics) consider resource allocation in a free market to be efficient. According to Vilfredo Pareto, who elaborated on this concept of market efficiency, a free market is efficient if no one can be made better off without making anyone else worse off. Moreover, according to this theory, through the invisible-hand mechanism, society benefits by having self-interested actors make free (but also virtuous) economic decisions that benefit them. Some ethicists have argued that the efficiency of free markets depends on several moral parameters as scope conditions, such as fair play, prudence (or self-restraint), competition among equal parties, and cooperation.

Critics of the free market system tend to argue that certain market failures require government intervention. First, prices may not fully reflect the costs or benefits of certain goods or services. Because of these externalities, public goods are underinvested or exploited to the detriment of others or future generations, unless such exploitation is prohibited through government regulation. Second, a free market may tempt competitors to collude, which makes antitrust legislation necessary. Antitrust and similar regulations are especially necessary in cases where certain market actors (for example, companies) have acquired enormous market power. Third, transaction costs may mean that some exchanges are best performed in a hierarchy rather than spot markets. Most important, Pareto-optimal resource allocation in a free market may violate principles of distributive justice and fairness, which again may necessitate some government action, according to the critics of the free market concept.

In reply to, or preempting, several of these critiques, Ronald Coase, Milton Friedman, Tibor Machan, Ludwig von Mises, Friedrich Hayek, and many others have argued for the robustness of markets because they can adjust to or internalize supposed market failures in many situations. For instance, many goods that have traditionally been conceptualized as public goods and, thus, have been presumed to require government provision have been shown to be open to free market contracting as well, ranging from lighthouses to beekeeping. Today, libertarians are strong defenders of the idea that a system of free markets provides the best economic system.

—Marc Orlitzky

See also Austrian School of Economics; Cato Institute; Coase, Ronald H.; Efficient Markets, Theory of; Externalities; Freedom and Liberty; Freedom of Contract; Friedman, Milton; Hayek, Friedrich A.; Invisible Hand; Libertarianism; Nozick, Robert; Nozick's Theory of Justice; Pareto, Vilfredo; Pareto Efficiency; Public Goods; Regulation and Regulatory Agencies; Smith, Adam; Transaction Costs

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Free Riders

A free rider can be defined as a person who, being a member of a group, decides to take advantage of the consumption of a good, or use of a service, that is generated as a result of the common efforts by the group members, without bearing a proportionate (or, in *pure* free riding, any) share of its cost of production or without contributing to its direct realization. One simple way of representing free riding is to think of a member of a rowing team who fails to do his or her share by faking the rowing effort—consequently getting a "free ride" on the boat.

The possibility of free riding is not an exceptional case: On the contrary, according to economic and rational choice theory (as we will discuss in the next paragraphs), it is a rather natural condition of human interaction within groups. This is because rational, self-interested individuals will naturally tend to minimize their costs of participation in a group if they can still benefit from the outcomes of cooperation.

In the business world there are many examples of situations where individuals have a positive incentive to free ride. For instance, consider being a member of a sales team. You know that your company will reward each member of the team with an annual bonus if a predetermined goal—say, an increase of 5% in total sales—is reached by the end of the year. You also know by the beginning of December that your team is very likely to meet the target due to the good work done by everyone so far, you included. At this point, you will have an incentive not to contribute to the collective effort anymore and still will enjoy the benefits of the collective good. Similar manifestations of the free rider problem can be found within many other team working situations, such as in R&D (e.g., an individual can free ride the intellectual property generated by others), in production (e.g., lack of or less effort from some team members, as in the example of the rower), or in services, in a tax or legal consulting team (e.g., weak or no contribution in performing a team brainstorming task).

The free riding tendency can be extended from the provision of collective goods and services to, more generally, a wide range of situations concerning participation in collective action—for example, teamwork within organizations, local community activities, pressure groups, social activism, etc. A well-known example of its manifestation concerns the tendency to not participate in political elections—when an individual enjoys the benefits resulting from collective action (elections produce a government, which ensures the provision of public goods such as roads and infrastructure, a legal system, and national protection) without bearing the cost of participating in the activity itself. Another manifestation of the free rider problem that creates social concerns refers to the preservation of natural resources and to issues such as pollution and environmental degradation: Everybody in society benefits from actions that preserve air and water quality, but since the relative impact of any individual's behavior on overall pollution is hardly noticeable, no one has an adequate incentive to contribute with her or his effort to preserve natural resources.

The key problematic aspect of free riding is that if every individual followed the same logic, there would be scarce or no public good produced or service delivered at all, and the entire society (including the free rider) would ultimately end up being worse off—a situation described as the tragedy of the commons. This is, in a nutshell, what constitutes the free rider problem, also known in economic theory as "the problem of collective action."

The Sources of Free Riding

What makes free riding possible and influences the probability of its occurrence is the combination of three main elements characterizing collective action: (1) the *indivisibility* of the collective good produced by the group cooperation; (2) the *noticeability* of individual efforts; and (3) the *perceptibility* of individual contributions. The first element refers to the fact that the benefits produced by cooperation are equally distributed among the group members—in other words, it is not possible to exclude anyone from enjoying them. For instance, if a football team wins its league, all the team members enjoy the same benefit of being the league champions, and no one can be excluded. Therefore, free riders will seek to avoid—or, at least, minimize—their share of effort.

The remaining two elements—noticeability and perceptibility—are directly influenced by the size of the group. In large groups, it is easier for the free riding behavior of an individual member to pass unnoticed as the relative contribution of any individual member is very modest. On the contrary, in small groups it is more likely that group members are able to detect a free ride as the lack of any single individual contribution has more significant impacts on the production of the common good. With regard to perceptibility, as the size of the group increases, members' perception of their individual contribution will decrease, therefore making it less attractive to pay their share, while in small groups individuals perceive a higher importance of their own contribution, and therefore the benefits of membership are more likely to exceed the cost of participation.

The Analysis of Free Riding Across Different Disciplines

The early formulation of the concept of free riding can be traced back to the origin of economic theory, particularly in the work of Adam Smith. In describing the benign mechanism of the "invisible hand," Smith recognized the importance of individual *self-interest* in guiding individual behaviors toward socially desirable outcomes. However, at the same time Smith also clearly emphasized—what, unfortunately, has been neglected by generations of economists—the crucial role of *moral sentiments* for the existence and well functioning of the market itself as they provide the underpinning rules of conduct without which no transaction could take place (in the absence of trust among the parties) and no contract signed (by fear of poor or unfair enforcement). These moral rules, Smith wrote, can in many situations correct the "misleading" tendencies originated by narrow self-interest—that is, as economists would say today, help limit the negative effects that opportunism and free riding produce on society.

More recently, since the 1950s the free riding problem has been formally analyzed and empirically studied by economists, rational choice theorists, political scientists, social psychologists, and moral philosophers, who have pointed out the puzzling questions it raises in many different situations of human interaction in economic, social, and political contexts. "Why should I pay my share, if I can enjoy the benefits of public goods without doing so?" is the question that has embarrassed economists over the decades. Similarly, "Why should I cooperate, if by defecting I can gain a larger outcome?" is the problem that rational choice theorists have to face—that is, the solution of the "prisoner's dilemma." Another free riding manifestation can be formulated in the question, "Why should I care to vote, if my participation in elections is almost certainly irrelevant to decide the outcome?" also known as the *voting paradox,* which kept busy generations of political theorists. Finally, the implications of free riding also matter from the perspective of ethical theory, which looks in normative terms at the rightness or wrongness of people's choices. Within ethics, the relevant question we should ask is therefore, "Is free riding a morally wrong behavior?" The following sections explore in greater depth some of these questions.

Free Riding and Economic Theory

In economics, the free rider problem has initially been addressed as the problem of inefficient production (i.e., too scarce) or the lack of production of public goods—a situation configuring a market failure and generating nondesirable, Pareto-inefficient social outcomes. Public goods are defined as goods whose consumption has the characteristics of being *nonexclusive* (or *nonrivalrous*), meaning that any individual consumption of that good does not affect the ability of any other member of the community to consume the same good. Traditional examples of public goods include national defense, public radio, or a lighthouse. Assuming that everyone enjoys the consumption of public goods, and that individuals maximize their utility function, economic analysis of public goods concludes that rational people will not be willing to pay a price for the consumption of public goods and therefore public goods will not be supplied, or will be undersupplied, if the contribution to them is left voluntary. To counterbalance free riding effects on the provision of public goods, economic analysis concludes, it is necessary to supplement the market system with some form of political decision, such as taxation.

Free Riding and Rational Choice Theory

The focus of rational choice theory is the study of rational decision making in situations of strategic interaction and in the presence of uncertainty. The problem of free riding emerges within this field of study as the problem of how to promote human *cooperation* when the tendency to take advantage of each other's cooperation leads to mutually disadvantageous effects—as represented in the prisoner's dilemma situation. This represents a paradox for rational choice as the noncooperative strategy *is* the best choice (it is a *dominant strategy* in the terminology of game theory) for each individual rational actor—yet, it generates socially inefficient results. Cooperation, according to standard rational choice theory, is therefore an *anomaly,* as rational behavior predicts—and as a normative decision theory, prescribes—free riding is sometimes the best choice to pursue the actor's interests (i.e., maximizing the actor's utility function).

However, the empirical evidence contradicts this prediction: There are many examples of human cooperation, where free riding is possible. Many passengers do pay the ticket on the bus; people clean up after a picnic in a public park; and public radios are able to broadcast thanks to voluntary contributions. The interesting question therefore becomes "What factors influence the degree of cooperation versus free riding?" Recent developments within rational choice theory have suggested that factors such as *ideology* (i.e., a sense of membership within a group), *expressive choice* (i.e., the benefits people receive from the act of participation itself, rather than from the outcomes of cooperation), and *self-commitment* (i.e., the idea that in the prisoner's dilemma one player will respect a self-commitment to cooperate in response to the other player's cooperation) can significantly change an individual's tendency to free ride and promote the emergence of cooperative behaviors. These studies demonstrate that the traditional assumption of selfish rationality of the economic man—what Amartya Sen incisively described as "rational fools"—is inadequate to understand the complexity of human motivation. Their conclusions suggest a revision toward a richer concept of rationality, able to encompass "sensible cooperators"—people who have good reasons to cooperate (and not to free ride).

Free Riding and Ethical Theory

From the point of view of ethics, free riding behavior raises a number of issues. The fundamental issue concerns its moral legitimacy: What are the *fair* rules that members of any group should be bound to respect? Is free riding simply "unfair playing" and therefore morally condemnable behavior, or can it be, at least in some instances, morally acceptable? Other ethical issues are generated by the fact that in any group *individual interests* coexist—and sometimes conflict—with the *common interest* of the group. One implication of this duality of interests is, for instance, that even if individual members of the group may agree that their cooperation produces desirable benefits, their self-interest may make them prefer not to cooperate (i.e., free ride) to save costs/effort. The relationship between individual freedom of choice and group/society's goals becomes critical: To what extent can the achievement of a (socially desirable) collective outcome interfere with individual freedom? Where is the line between voluntary cooperation and coercion? What is the role of persuasion, and the risk of manipulation, by the group leaders?

Within ethical theory, the libertarian approach of the theory of rights emphasizes the importance of individual rights and interests versus the common interest of the group. Robert Nozick, one of its most famous representatives, illustrated the issues at stake with a simple, brilliant example: If each day a different person on your street sweeps the entire street, must you do so when your time comes? Even if you don't care that much about a clean street? Must you imagine dirt as you traverse the street, so as not to benefit as a free rider? In the libertarian approach, allocating to the group (e.g., the State) a right to enforce an individual obligation to cooperate would be in many instances objectionable and unacceptable: It would violate most fundamental natural rights of every human being—for example, the right to have your own system of values and preferences. After all, in some cases, people might not desire to be free riders; they may just not care about the ride (the clean street) at all.

An opposite answer to this dispute can be found in the social contract approach to ethics, which is based on the idea that rational and autonomous individuals can agree on impartial principles of justice on which their life in society can be regulated. In particular, the problem of free riding is addressed by the "principle of fairness" formulated by John Rawls, one of the most prominent philosophers of this approach. According to the principle of fairness, any person who has voluntarily accepted to be a member of a cooperative scheme, in light of sharing the benefits produced by cooperation, is bound by a duty of fair play to do his or her part and not to take advantage of the free benefit by not cooperating. In other words, according to the principle of fairness free riding is a morally unacceptable behavior.

—Simone de Colle

See also Collective Choice; Economics, Behavioral; Economics and Ethics; Egoism; Game Theory; Moral Hazard; Nozick, Robert; Opportunism; Pollution Externalities, Socially Efficient Regulation of; Prisoner's Dilemma; Public Goods; Rational Choice Theory; Rawls, John; Reciprocal Altruism; Smith, Adam; Social Contract Theory; Tragedy of the Commons

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Free Speech in the Workplace

Free speech refers to the First Amendment rights of individuals to express themselves, such as through religion, association, and the press. An individual's free speech rights exist solely to prevent action by the government to silence speech. In fact, there is no constitutional right to free speech in the private workplace; any right to free speech of an employee at a private place of employment exists, if it all, solely as the result of state and federal legislation passed specifically to protect rights associated with free speech.

Freedom of speech, or freedom of expression, is often recognized in the context of free press. One of the hallmarks of American society is the guarantee of freedom of the press. This is considered vital to a free society, in that it enables people to speak out against the government without fear of recriminations. One of the conditions on which the founding fathers based their eventual decision to accept a federal government was that fundamental rights, such as free speech, be protected.

Freedom of Association

Closely tied to the freedom of expression is the freedom of association. A citizen of the United States has a constitutional right to associate freely—or to choose not to associate with—anyone else. This right has not always been protected as vigorously as it is today, with anti-Communist laws and oath of office requirements in the 1950s as perhaps the most recent example. The right to associate is closely tied to the right to free expression, as often like-minded individuals are drawn to organize on behalf of whatever position or platform they might wish to advance.

The analysis of free association rights for employees is largely the same as that for free speech. In the absence of other state or federal prescriptions to the contrary, a private employer may not base employment decisions on many outside affiliations—in other words, employers are prohibited from choosing to hire (or retain) or terminate employees who associate with most other groups. While this is constitutional, there are a number of other restrictions that constrain an employer in this regard. First, an employer who terminates or takes any other negative employment action against an employee on the basis of speech or association protected by the Civil Rights Act can face stiff penalties in the form of damages from lawsuits brought by aggrieved employees (often with the assistance of the Equal Employment Opportunity Commission). Second, some states or localities have laws that protect employees from termination without cause. Finally, association with organized labor is further controlled and protected under federal law.

Global Perspective

The First Amendment is not unique when compared with other declarations of free speech rights, though the breadth of free speech rights afforded to American citizens is broader than that in most other countries. Article 19 of the Universal Declaration of Human Rights, promulgated by the United Nations, recognizes the importance of free speech and guarantees to everyone the freedom of expression, which specifically encompasses freedom of the press. While some countries have adopted similar language, many others have not. Even in those countries that have adopted similar rights, the enforcement and interpretation of the right of free speech is often less vigorous than it is in the United States.

Free Speech in the Private Workplace

The right to free speech is guaranteed by the First Amendment to the Constitution of the United States. The First Amendment bars Congress from making any laws that interfere with religion, speech, association, or the press. The critical, and often overlooked or misunderstood, word is *Congress*. A private employer is not constitutionally required to permit free speech by its employees. To reiterate, although other state and federal legislation does exist that imposes civil liability on employers for permitting, or failing to control, certain forms of speech within the workplace, employees in private workplaces do not have protected First Amendment rights in those workplaces. The protection of any speech in private workplaces is the result of other state or federal legislation.

As technology has advanced, so too has the opportunity for employers to monitor its employees' expressions in the workplace. Before the advent of computers, an employee who held certain opinions could avoid scrutiny by simply refraining from mentioning them in the presence of the employer. With the rapid increase in electronic communications, the temptation for employees to express their personal opinions in "private" electronic transmissions to personal friends, either within or outside the workplace, has increased. The employer is often watching, however. A substantial number of employers save, and have the capability to review, an employee's e-mail and/or instant messages. A large percentage of employers monitor the Web surfing of employees, and some employers employ software capable of capturing screen shots of an employee's computer or recording every keystroke. Put simply, an employee's speech, if performed at the workplace, is often capable of being reviewed by the employer, a fact that is often disclosed in company policy manuals or sign-on screens.

Whether or not an employer should be capable of such oversight is a matter of political debate. Many argue that the long hours required of employees underpin arguments that they should be afforded some privacy for clearly private communications, even if the communication is made using an employer's time and equipment. Employers defend the oversight on several fronts, arguing that it permits them to identify employees spending inordinate amounts of time on personal matters while being paid and further permits employers to identify improper communications that might otherwise lead to civil liability against the employer (e.g., harassing content transmitted to fellow employees). While the matter is one of debate, what is clear is that private employees often do not have reasonable expectations of free speech or privacy in their workplace communications.

Free Speech and the Government Employee

Far more complicated a subject is the right of a government employee to free speech within the workplace. Where the government is the employer, the First Amendment prohibits actions undertaken by the employer to restrict an employee's speech. The result has been a substantial body of litigation, still ongoing and seemingly never ending, in which government employees continue to challenge restrictions on their workplace speech.

Court decisions interpreting the speech of government employees have made it clear that a government employee does not lose his or her constitutional protections by entering the government workplace. A government employee can, for example, choose a political party, support a political or social issue, or speak out in favor or against legislation, without fear of retribution. Far more problematic is when, where, and in what manner, the government employee can do so. Put another way, courts have attempted to address, on an ad hoc basis, what a government employer can do to restrict speech within the workplace. The decisions are fact specific and often tied to the specific duties of the government employee. In general, however, a government employer can restrict an employee's speech under certain circumstances.

For example, a government employer may not forbid an employee from holding certain religions or political beliefs or from expressing them in letters to the editor or in speeches made on personal time. The same government employer often can, however, generally control the content of an employee's speech if the speech can be fairly construed as that of the government. After all, the government does get to decide what speech it wishes to make on its own behalf and thus can exercise some control over employees when they are speaking for the government itself.

Conclusion

Mindful of the roles played by those political leaders who risked their wealth, employment, and even lives to rally the colonists against the government of England, the founders of the United States treated the right to free speech, and the closely related right to free association, as fundamental, and thereby gave free speech a place of honor as the First Amendment to the U.S. Constitution. The right is not as broad, however, as many people might think. The right is generally a prohibition of government repression of speech, and private employers are often at liberty to control employee speech within the private workplace. Even government employers can, under certain circumstances, exercise some control over a government employee's speech, especially if it is made within the workplace.

It is worth noting that the right to free expression is also a right not to be forced to give an audience to the expression of others—a right that is often forgotten in the shuffle. While the government may not generally prohibit a person from speaking in support of an issue, there is no requirement that any private citizen or corporate entity must listen and provide the speaker with a forum or audience. Speakers may thus speak on nearly any topic in the town square free from interference by the government but may find local media unwilling to cover the event and passersby uninterested in listening.

—Tara J. Radin and Steven R. Zahn

See also Employee Monitoring and Surveillance; Employee Rights Movement; Genetic Information in the Workplace; Privacy

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Free Trade, Free Trade Agreements, Free Trade Zones

Free Trade

Free trade is the trade of goods, services, or intellectual property across national borders, substantially unencumbered by governmental policies. Free trade is driven by market forces: domestic buyers desiring to purchase foreign products or services and foreign sellers willing to sell to those domestic customers. Free trade emphasizes the limited role of government through restrictions on international trade such as tariffs and nontariff barriers.

Comparative Advantage

Free trade is related to international trade. International trade is based on what the economist David Ricardo originally called the "law of comparative advantage." At its simplest, the law states that a country's wealth will be maximized if it produces only what it is best at producing and trades that output for all other goods and services. Economists derive what is best in a backward kind of way: You are best at what costs you the least to give up. This is called *opportunity costs.* Sometimes opportunity costs seem obvious: It would be quite costly to grow bananas in the northern reaches of Canada—one would need a hothouse and considerable energy for example—while it might be difficult for a fisherman in a warm-water country such as Honduras to raise cold-water fish such as cod. In this case, trading Honduran bananas for Canadian cod seems to be a no-brainer. This is a case in which each country has an absolute advantage over the other in terms of producing one of the goods and free trade can ensue.

But comparative advantage states that trade can be beneficial even when one partner is superior to the other in producing both (or all) the products. In a world of free trade, a country will specialize in the production of what it is relatively best at doing and trade for other products. In doing so, free trade forces manufacturers to specialize only in what they can do best in that particular location, forcing economic efficiency and, in turn, driving down the costs of production.

Ideologies of Free Trade

There are three distinct ideologies of political economy for analyzing free trade: (1) the liberal view;

(2) the nationalist view; and (3) the Marxist-Leninist view.

Liberal View of Free Trade

This view of comparative advantage finds itself embedded within the liberal position on trade. The liberal position on trade places the individual consumer as the most important stakeholder in international economic relations. The liberal view emphasizes the economic advantages of efficient production driven by free trade that ultimately benefits consumers in terms of more variety, higher quality, and lower prices. Efficiencies come from the technological, labor, or geographic advantages that one country's producers have over others. Free trade becomes a positive sum game where both parties are better off specializing and trading across borders than producing and selling all their output domestically.

The liberal position on trade does not require a heavy-handed government. Government exists mainly to define and defend the property rights of merchants and consumers, to provide or facilitate some of the public goods for commerce such as public ports and power and telecommunications systems, to open the economy to foreign goods and services, and to eliminate trade protection. The liberal view also emphasizes the positive international relations aspect of free trade; that is, liberals believe that free trade promotes cooperation and peace between nations because they rely on each other for goods and services that benefit their respective consumer-citizens. Therefore, countries that trade with each other are less likely to have wars and other conflicts than those without such economic relationships.

Nationalist View of Free Trade

Other perspectives, however, do not give such a rosy review of free trade. Political economist Robert Gilpin of Princeton University says that the nationalist perspective and the Marxist-Leninist perspective stand alongside the aforementioned liberal perspective on international trade and investment. The nationalist view focuses on how economic activities serve the "primacy of the state." The goal of nationalists is to promote the power and wealth of the state. The question is, How well does free trade serve this goal? As the liberal perspective shows, free trade forces efficiency and thus economizes on the use of resources—this can bring wealth. But in doing so, one might rely on the goods and services from other countries. For example, in information technology outsourcing, a U.S. company might rely on an Indian company for that function. What happens, for example, if the government of India decided to prohibit Indian companies from having U.S.-based clients unless the government of the United States changes its diplomatic position toward Pakistan? Since U.S. companies rely on Indian companies for these services, they will want the U.S. government to acquiesce to this political request. But the request may contravene the best national interests of the United States. This demonstrates that free trade can place a country in a vulnerable political position. So according to the nationalists, free trade should only be pursued when it creates relative advantages in wealth and power for the country: Otherwise it should be prohibited. Because of this fear, nationalists often support economic self-sufficiency, often through subsidies, particularly in the industrial and military-technology sectors, and advocate erecting trade barriers against foreign products and services in these areas.

The Marxist-Leninist View of Free Trade

The Marxist-Leninist view of political economy also does not fully support free trade. The Marxist-Leninist position looks at the inequality of economic relations. For trade, Lenin focuses on the relations between countries with capital and those without. The basic argument is that countries with capital have leverage over those without so that the terms of trade and international investment are always skewed toward those capital-rich countries. Furthermore, with each transaction, the terms become less desirable for the poor country. Lenin saw a world where the capital-rich countries would divide the rest of the world, the capital-poor countries, into economic spheres for their own gain. But he foresaw that eventually even the rich countries would be in dire straits as they fought over each other's possessions. Thus, the Marxist-Leninist view of free trade is one of inequality between capital-rich and capital-deficient states and one where conflict is likely to occur between rich and poor nations and eventually between rich states. In sum, international capitalism is conflict ridden and unstable over the long run.

Free Trade Agreements

Free trade agreements (FTAs) are agreements between two (bilateral), three (trilateral), or more (multilateral) nations that specify the terms of trade. Generally, FTAs seek to lower the barriers to the flow of goods and services between the countries and to facilitate greater investment by companies in each other's territory. FTAs have become a popular trade policy for many countries to pursue parallel to their participation in the multilateral World Trade Organization (WTO). Many countries have found it considerably easier and faster to achieve satisfactory trade arrangements with a few other countries via FTAs than working with the nearly 150 countries in the multilateral WTO.

Free Trade Zones

Free trade zones, also known as preferential trade areas, are the formalized arrangements between nations for free trade and investment. The WTO permits free trade zones when they cover substantially all the trade between nations and do not worsen the conditions of trade for third parties. The WTO's General Agreement on Tariffs and Trade (GATT) Article XXIV gives member countries permission to pursue free trade zones under certain conditions. The two types of free trade zones are (1) customs unions and (2) free trade areas.

Customs Union

A customs union is a free trade zone between nations that sets a common tariff for members of the customs union (sometimes called the "internal tariff") to zero or very low levels and a common tariff (the "external tariff") for countries outside the customs union at a higher rate. These tariffs cover substantially all the goods and services traded between the nations. The European Union and Mercosur in South America are examples of customs unions. Oftentimes, customs unions involve deeper political commitments than for free trade areas.

Free Trade Area

A free trade area (FTA) is a free trade zone between nations that sets a common internal tariff, typically zero or very low, but unlike the customs union does not set a common external tariff—that is, for a country that is a member of a FTA, it can maintain whatever tariff schedule it chooses for countries that lie outside the FTA. Like a customs union, the countries in an FTA set tariffs for substantially all goods and services that are traded as well as other trade rules such as over investments. Modern examples of FTAs are the North American Free Trade Agreement (NAFTA) between Canada, Mexico, and the United States; the Central European Free Trade Agreement (CEFTA) between Poland, the Czech Republic, Slovakia, Hungary, Slovenia, Romania, Bulgaria, and Croatia; and the Andean Community between Bolivia, Colombia, Ecuador, Peru, and Venezuela. There are hundreds of bilateral FTAs.

The creation of free trade zones is not without controversy. Advocates support their creation for several reasons. First, they worry that countries may engage in stalling tactics, sometimes called *foot dragging,* during the multilateral WTO negotiations. Foot dragging slows the speed and limits the scope of negotiations within the WTO. For example, agricultural subsidies have been discussed for many years with few substantive changes in the rules. In a smaller forum such as in a preferential trade arrangement, the parties may move swiftly on such topics. In addition, in a smaller setting, parties may address some new trade topics neglected by the WTO. For example, the NAFTA placed investment rules centrally and was ahead of the WTO in handling this area of international commerce. In this way, the free trade zones often experiment with particular trade issues before the WTO subsumes them.

Discrimination and Trade Diversion

Critics, however, have several complaints about free trade zones. First, since these free trade zones give advantage to members relative to nonmembers, they seem to be contrary to the most favoured nation clause of the WTO's rules. Expressed otherwise, free trade zones discriminate against nonmembers. Second, one of the effects is that free trade zones may result in trade diversion. Trade diversion is when a trading partner switches its source of supply from a supplier located outside the free trade zone to a member of the free trade zone that would have been a higher cost supplier than the outside supplier if not for the tariff advantage conferred by the free trade zone. For example, the World Bank conducted a study in the mid-1990s that showed that after the formation of Mercosur many Argentine companies switched their source of supply from cheaper suppliers outside Mercosur to more expensive Brazilian suppliers, only because of the tariff advantages bestowed to Brazilian producers through the free trade zone. If this is so, free trade zones distort production and do not result in maximum benefits for consumers.

Rules of Origin

A third problem is specific to FTAs and concerns something called the *rules of origin.* Since FTAs do not set a common external tariff, a country outside the FTA that wishes to ship something to a customer inside the FTA should choose the lowest tariff country to make this transaction and then transship within the FTA to the customer. For example, if a supplier of computer printers from Singapore wishes to reach customers in the United States, but the United States had set a tariff of 20% on such printers, the Singapore firm might first ship to Canada, where there is only a 5% tariff, and then ship from Canada to the United States duty-free. Since more often than not political pressure from domestic printer manufacturers is what led the U.S. government to set the tariff at 20% to protect the domestic industry, transshipment defeats such a policy goal. Therefore, in FTAs, procedures called rules of origin must be written to identify the origin of goods subject to tariff treatment. Rules of origin are often very complex and are often crafted to protect various domestic producers. Rules of origin are particularly elaborate for products that contain many components from different countries. For example, a typical desktop computer has parts that were made in China, Singapore, Malaysia, South Korea, Japan, and the United States and was assembled in China, Taiwan, or Malaysia. So if Malaysia has an FTA with Australia that lowers Australia's tariffs on laptop computers that were "made in Malaysia," would this computer qualify for this favorable treatment? The answer is derived through the rules of origin that specify what value of the product needs to originate within the FTA zone. The difficulty is that to some extent the rules of origin are arbitrary. For example, should the value be based on the costs of production such as the materials and labor used and an allocation of overheads or the price that the product is sold? Which currency should be used, and what should be the conversion exchange rate? Should a value-added system be used?

An example of the rules of origin comes from NAFTA, between Canada, Mexico, and the United States. Article 401 defines *originating* in four ways: (1) goods wholly obtained or produced in the NAFTA region, such as silver mined in Mexico and exported to the United States; (2) goods produced in the NAFTA region wholly from originating material, such as silver rings made in the United States from Mexican silver and exported to Mexico and Canada; (3) goods meeting the Annex 401 originating rule; and (4) unassembled goods that do not meet the Annex 401 rule or origin but contain 60% regional value content using the transaction method or 50% using the net cost method. The Annex 401 originating rule refers to a change in tariff classification, a regional value-content requirement, or both. From the NAFTA Guide to Customs Procedures, a change in tariff classification would be frozen pork meat imported into the United States from Hungary and combined with spices from the Dominican Republic and grains from the United States to make pork sausage. This finished product, the sausage, represents a changed tariff classification from its meat and spice inputs and is considered by the rules to be a NAFTA-originating product. The other criterion used is the regional value content, meaning the percentage of the value of the goods must be from one of the NAFTA countries. There are two methods used to calculate this: the transaction value method, which uses prices with certain adjustments, and the net cost method, which takes into account the costs of the goods used to produce the items. Finally, there are rules to confer origin on certain unassembled goods.

The WTO stipulates that the rules of origin in FTAs be transparent, that they do not restrict or inhibit international trade, that they are consistently administered, and that they specify what confers origin rather than what does not. The WTO has a Committee on Rules of Origin to promulgate guidance for these trade rules.

In spite of the problems, it is likely that FTAs will multiply in the coming years. FTAs are quite attractive to governments as they attempt to position themselves favorably toward important trading partners. For example, South Korea is moving ahead toward an FTA with the United States, even with much domestic opposition, because it sees the FTA as a way of securing an economic advantage for Korean producers in the United States against Chinese and Japanese rivals. Second, FTAs seem to breed more FTAs. For example, in the wake of NAFTA, many countries in Central America and the Caribbean saw that their producers were at a disadvantage against Mexican producers for access to the lucrative U.S. and Canadian markets. The recently consummated Central American Free Trade Agreement (CAFTA), a regional FTA that includes the United States, is aimed at reducing this gap with Mexico. For companies, the implications are that while FTAs generally reduce barriers toward conducting business, they also create these pockets of policy-created cost advantages that must be constantly monitored. For example, many apparel manufacturers relocated from Central America to Mexico because of NAFTA; a company that did not do so was at a cost disadvantage. So FTAs make international business increasingly complicated for companies.

—Doug Schuler

See also Comparative Advantage; Developing World; Exploitation; Globalization; International Trade; Justice, Distributive; Liberalism; Marxism; North American Free Trade Agreement (NAFTA); Opportunity Cost; Political Economy; Utilitarianism; World Trade Organization (WTO)

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Free Will

Free will is the capacity to make choices and to act on those choices. Most of us are convinced that we have this capacity because we know, or think we know, that when faced with a choice between one action and another, it is up to us to decide. We decide what to do, and we act on that decision. Had we decided otherwise, we would have done otherwise. Thus, we have free will. Or so it certainly seems.

The problem is that our conviction that we have free will does not fit together with other things we think we know. For instance, either everything that happens—every event—is a necessary consequence of previous events and the laws of nature, or not everything that happens is a necessary consequence of previous events and the laws of nature. Call the first possibility "determinism" and the second "indeterminism." We know that one of these two must be true; there are no other alternatives. If the first is true, then everything we do, including every decision we make, is a necessary consequence of previous events and the laws of nature. If so, we do not have free will after all because we cannot do anything other than what we actually do. On the other hand, if not everything is a necessary consequence of previous events, then some of the things we do might have no antecedents—they just happen for no reason at all. Yet if a decision we make or an act we perform just happens for no reason, then there is no reason to say that it is our decision or our action. It is not up to us in the sense required for free will. Again, we do not have free will. Since one of these alternatives must be true, and since we do not have free will on either alternative, the only conclusion we can draw is that we are not free. We may fervently believe that we are, but if we do, we are sadly mistaken.

A response might be that as long as we believe that we have free will, then it does not really matter that at some "deeper" level we suspect that we are not free. Our commonsense belief in free will works well enough for everyday purposes, so why not leave it at that?

This sounds like a good way to sidestep the problem, but it immediately collides with another commonsense idea, that is, that moral responsibility implies free choice. We all believe that we are morally responsible for what we do only if we could have done otherwise had we chosen to do so. But if we cannot do otherwise, if we are not, in a deep sense, free to choose and free to act on our decisions, then in what sense are we morally responsible? And if we are not morally responsible, how can we be properly blamed or praised for what we do? Without freedom, the notion of moral responsibility and all that goes with it seems pointless. So it looks like we are in a tight spot. On one hand, we believe that we have free will, we believe that we are morally responsible, and we believe that either determinism or indeterminism is true. On the other hand, it seems impossible that all three of these beliefs are correct. We have to give up something. What should it be?

Compatibilism

Maybe we do not have to give up anything. This is the position of compatibilists, who argue that we can both be free in a sense required for moral responsibility and accept determinism. All we need to do to show that free will and determinism are compatible, the argument goes, is be clear about what is ordinarily meant when we say an action is free. In the ordinary sense an action is free when we have the ability to do it and nothing prevents us from doing it. For example, you are free to walk to the store provided you have the ability to walk and nothing is stopping you from doing it. You are not free to walk to the store only if you lack the ability to walk or you have the ability but are, for example, tied to your chair. In short, a free act is one you can physically perform and to prevent doing which there are no impediments.

Someone might object that this sort of freedom is no better than that of a thermostat. A thermostat has the ability to control temperature if not prevented and so would be free in the compatibilist understanding of freedom given so far. What the thermostat lacks is the ability to choose to do otherwise, to choose not to control the temperature if the mood strikes. People, however, do have the ability to choose otherwise. A person can take a walk or choose not to. What people do is up to them in a way that it is not up to the thermostat. All this is missing from the compatibilist account of freedom.

A compatibilist would reply that to say that you could have chosen otherwise is just to say that you would have chosen otherwise had you wanted to choose otherwise. You decide to take a walk, but you could have stayed home to shoot a little pool. Had you chosen to shoot pool, you would have, but you thought some exercise would do you good. Thus, compatibilists claim, once we understand what it means to say that someone could choose otherwise, we see that there is no real problem here. If you had wanted to choose otherwise, you would have, and if nothing prevented it, you would have acted on that choice.

Still, the objection might continue, something crucial is missing in compatibilism. If determinism is true, then your deciding to take a walk instead of shooting pool is a necessary consequence of previous events and the laws of nature. You could not have done otherwise; deciding to take a walk is the only thing you could do given past events and the laws of nature. The only way you could have chosen and done otherwise is if the past had been different, if you could reach back and alter something that has already happened. But this is impossible. The past cannot be changed. Thus, when compatibilists say that *you could have done otherwise* means *you would have done otherwise had you chosen to do so,* what they are really saying is that had the past been different, you would have chosen and acted differently. That may well be true, but it does not capture the sense of "could have done otherwise" necessary for moral responsibility. To be morally responsible it must be true that at the moment of choice you could decide differently given the past that you actually have, not merely that you would choose differently had the past been different. Thus, compatibilist freedom is only a flimsy facade, not the robust structure needed for moral responsibility.

Compatibilists have responded to this argument in two main ways. The first is to deny that moral responsibility implies that at the moment of choice we have the ability to choose otherwise. The second is to develop new and finer-grained understandings of freedom and moral responsibility that are consistent with determinism. Whether these arguments are successful is a matter of ongoing controversy.

Incompatibilism

Suppose that free will and determinism are incompatible, that is, that they cannot both be true. Then there are three possibilities. One is that we have free will and determinism is not true. This is called *libertarianism.* The second is that determinism is true and we do not have free will. This is *hard determinism.* The third is that neither is true; we do not have free will, and determinism is not true. This is sometimes called *hard incompatibilism.*

Libertarianism

Libertarians argue that when you make a free choice you could have chosen otherwise given the same past events and laws of nature. For example, on Tuesday at one o'clock you decide to take a walk instead of shooting pool. Libertarians assert that because determinism is not true, you could have decided otherwise even if the laws of nature and everything in your past remained exactly the same. At the moment of choice on Tuesday it was literally up to you and was based entirely on your deliberations. You make the choice, and you bear the responsibility for it.

An objection to libertarianism is that if some of our decisions and actions are undetermined, that is, if they could have been otherwise given the same past and laws of nature, then they are arbitrary and inexplicable. They are not under our control in the way needed for moral responsibility. For instance, if libertarians are correct, then given precisely the same circumstances and precisely the same deliberations, you might have decided to shoot pool instead of taking a walk. Thus, your actual choice "just happened" because your deliberations made no difference. You might have made a different choice given exactly the same deliberations. If so, then there is no clear sense in which you are responsible for the choice because nothing you did had any effect on the action you eventually performed. This is not free choice; it is mere chance.

In response, libertarians have proposed what might be called "hidden aspect" accounts of free will. The idea is that if free acts cannot be entirely explained by past events and the laws of nature, and if such acts are not to be arbitrary or inexplicable, then there must be some other aspect of action, some "agent" or "act of will" or "purpose" that is the source or cause of free action. Whatever this is, it is not itself determined by previous events and the laws of nature. Moreover, since these things in a sense stand outside the normal chain of cause and effect, they are hidden from ordinary view and can only be discerned by introspection or by analysis and argument. For example, philosophers such as Roderick Chisholm argue that free acts are caused by agents, which are not events or laws of nature, but enduring substances that cause free acts and are not themselves causally determined. Hence, according to Chisholm, when you decide to take a walk instead of shoot pool, it is true that your action is not determined by previous events and the laws of nature, but it is not true that what you do is totally uncaused. It is caused by an agent—you—and you are the sort of thing that causes things to happen, but nothing causes you to cause those things. You are a *causa sui,* an unmoved mover.

Many writers reject Chisholm's argument on the grounds that it posits mysterious entities that really explain nothing. Even assuming there are agents, either what they decide to do is based on past events and the laws of nature or not. If the former, then agents are no different from ordinary things. They are no more free at the moment of choice than anything else. If the latter, that is, if what they decide to do is not determined by past events and the laws of nature, then what they do just happens for no reason at all. It is inexplicable and not under the agent's control or will. Hence, positing agents does not solve the problem. Moreover, positing agents is ad hoc; there is no reason to suppose there are agents except to solve a problem about free will. If we cannot explain freedom without agents, we cannot explain freedom with them either.

One response to this argument appeals to modern science, especially quantum physics and chaos theory. Writers such as Robert Kane note that quantum theory postulates undetermined quantum events and that these events might occur in the brain. Furthermore, according to chaos theory, small alterations in initial circumstances can eventually cause large and unpredictable changes. Kane then argues that moments of stress and uncertainty in our lives could make our brain sensitive to quantum changes and that these changes could lead to actions on our part that are not strictly determined but are up to us because we willed them to happen "then and there," at the moment of choice.

The complete version of Kane's attempt to reconcile modern science, indeterminism, and free will is far beyond the scope of this entry. His argument has generated a number of objections and considerable discussion. In this respect, at least, it is no different from any other argument in the debate over free will.

Hard Determinism

Hard determinists argue that free will and determinism are incompatible. The argument is simple. If determinism is true, we do not have free will. Determinism is true; hence we do not have free will. Consider the second premise. As mentioned earlier, quantum theory seems to show that determinism is not true. Some events at the quantum level are undetermined. Thus it appears that the second premise of the argument is false, and so hard determinists cannot use it to show that we do not have free will.

Hard determinists have replied in two ways. The first is that quantum indeterminism is irrelevant to free will. Subatomic particles may behave in strange ways, but human behavior is not influenced by random quantum events because in larger physical systems like the human body quantum indeterminism is negligible. However, whether it is negligible is, of course, just what Kane and others like him dispute.

Hard Incompatibilism

The second reply, hard incompatibilism, is closely related to hard determinism. However, hard incompatibilists abandon the commitment to determinism and argue that nevertheless we have no free will. The argument is roughly this. Compatibilism fails as an account of free will because it implies determinism, and modern science has shown that determinism is not true. Libertarianism fails as an account of free will because there are and could be no agents, no "unmoved movers," of the sort required by libertarianism. One reason, as Galen Strawson argues, is that for us to be responsible for what we do now, we must be responsible for our nature or character, from which our actions flow. But for us to be responsible for who we are now, at this moment, we must have done something in the past to make us as we are now. Furthermore, to be responsible for who we are now, we must have been responsible for who we were then, at that moment in the past. And to be responsible for who we were then, at that moment in the past, we must have done something even further back in the past, and so on. This regress continues all the way back to our birth, when we clearly are not responsible for anything. Thus, Strawson argues, there can be no free will, and this is true regardless of whether determinism is true or not.

If Strawson is right, or if some version of hard determinism is correct, then free will is no more than a persistent illusion. We all believe that we have free will, but we are all wrong. This has disturbing implications. For example, we admire and praise acts of generosity, kindness, and courage in no small part because we believe that they are undertaken freely by people who could have chosen otherwise. Yet if we have no free will, these acts and others like them are not free, and the people who do them could not have done otherwise. If so, our admiration and praise feels empty, valueless. On the other side of the coin, we condemn and punish those who transgress the laws, but if they are not free to choose what they do, condemnation and punishment are inappropriate. A prison might be used to deter crime or to rehabilitate offenders but not because we think it just to imprison the guilty. Finally, if we do not have free will, then we are not in control of our lives in the way we think we are. We cannot be credited with our achievements or reproached for our failures. Our lives may go on as before, but if we know we are not free, surely the spice of living must lose some of its flavor.

Ethics, Free Will, and Business

Free will is one of the most difficult problems in philosophy. All the alternatives discussed above, and others not discussed, face weighty objections. It is also one of the most important problems, since how it is answered has deep implications for how we see ourselves in the world. However, outside philosophy it goes largely unnoticed. In everyday life, almost everyone believes in free will. So, leaving philosophical worries aside, consider for a moment exactly how free we really are. In business, for example, managers and workers are buffeted by a myriad forces beyond their control. On a small scale, markets, customers, suppliers, fellow workers, bosses and subordinates, and government and corporate rules and regulations all have their say over what businesspeople do and become. On a larger scale, globalization, terrorism, and even global warming play a big part in controlling the possibilities open to them. Freedom in business, if we have it at all, is for most businesspeople not the freedom to do what they want, when they want, for the reasons they find compelling. It is only the freedom to respond imaginatively to what the forces in business require or to what other people want or expect. It is a limited freedom, constrained in almost every respect.

For example, suppose Jones is a skilled software engineer with many years' experience. He has a family, house, and deep roots in the community. One morning he is notified that within a month all software engineering in the corporation he works for will be outsourced to another country. When the move is made, his employment contract will be terminated. He will receive three months' severance pay, three months' medical insurance, and nothing else. What does he do?

The obvious answer is to look for another job. But think of the constraints he faces. He is limited by the global trend toward outsourcing, about which he can do nothing. He is limited by his commitments to his family and by their commitments to their friends, school, and community. Not least, he is limited by his own specific expertise and experience. Thus, he is not free to accept just any job or to move to just any location. He is not a candidate for retraining for an entry-level job in another field. His best option is to find something suitable in the local area. But, again because of outsourcing and his own experience and expertise, suitable jobs may be hard to find or even nonexistent. Maybe he will be lucky enough to find another decent job or will be able to cobble together enough consulting work to keep going. But Jones is not really free to do whatever he wants. He is tied down in a hundred different ways.

Not, however, in every way. There is one way, a very important way, in which we are still free in business in spite of everything. It is how we treat the people we work with and work for. We are free to treat them with the respect and dignity they deserve, and we are free not to so treat them. This is the heart of ethics, and it is up to us to decide.

—Robert Frederick

See also Autonomy; Darwinism and Ethics; Ethical Decision Making; Freedom and Liberty; Human Nature; Moral Agency

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Friedman, Milton (1912–2006)

Milton Friedman, born in New York City in 1912, was one of the 20th century's most famous and influential economists, renowned for his depth of analysis, his innovative capacity, his practical outlook, and his simple, persuasive style. However, he is probably best known for the political repercussion of his ideas. The son of an immigrant, he studied at Rutgers (B.A. 1932), Chicago University (M.A. 1933), and Columbia (Ph.D. 1946). Married to Rose Director, he spent most of his professional life at Chicago University and was awarded the Nobel Prize for Economics in 1976.

Friedman conceived economics as a positive science. Value judgments are consigned to private life and must not interfere with scientific proposals: There is no place for moral criteria in economics. The economists' task is to provide theoretical arguments that enable predictions to be made about reality but not to give opinions about the results of their predictions.

Friedman's methodology is drawn from John Dewey's pragmatism. The role of theory is to provide a framework for the formulation of explanations and predictions. Theory is not validated by the realism of its assumptions but by its ability to generate predictions that are not refuted by facts.

Liberalism (or classical liberalism) is perhaps the trait that best defines his economic policy proposals. Friedman upheld freedom (conceived as an indivisible whole) as a basic moral principle in the shaping of society and maintained that the market is the system of economic organization demanded by that freedom. His liberalism was individualistic: There are no reference values outside of the individual; ethics is strictly private. The role of the State is to create the framework in which the individuals perform their free activities. This led to some of his best-known proposals, including those against price controls, in favor of the education voucher and negative income tax, etc.

Friedman's content and method helped define the Chicago School, characterized by a solid grounding in the principles of neoclassic economics, strict logic in the development of these principles, and emphasis on empirical verification. For example, his statement that the firm's sole purpose is to maximize profits was a logical consequence of neoclassical economics in the pursuit of maximum economic efficiency.

In macroeconomics, Friedman is known as a key figure in monetarism: Money influences output and employment in the short term (money matters), but this effect is not lasting; in the long term, money only influences prices. Monetary policy is powerful. However, it should not be practiced discretionally but in accordance with simple rules (a constant growth rate of the money supply). The capitalist economy is basically stable, and therefore it is not desirable to implement active stabilizing policies, which may be dangerous (monetary policy) or ineffective (fiscal policy).

—Antonio Argandoña

See also Business, Purpose of; Capitalism; Chicago School of Economics; Freedom and Liberty; Free Market; Liberalism; Positive Economics; Pragmatism; Profit Maximization, Corporate Social Responsibility as

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Gaia Hypothesis

The Gaia hypothesis holds that the earth itself is a living organism. Associated most closely with the work of atmospheric chemist James Lovelock and microbiologist Lynn Margulis, the Gaia hypothesis is interpreted by some as a metaphor for how we should think about the earth and by others as a literally true description of the earth.

The Gaia hypothesis can be best understood in contrast to the alternative, which views the earth's biological and abiotic processes as independent of one another. From that perspective, the planet's geophysical processes, from plate tectonics and climate to atmospheric and oceanographic conditions, simply provide the physical context in which life evolves and exists. In contrast, the Gaia hypothesis emphasizes the effects that biological processes have in creating and maintaining geophysical conditions.

In one version, often referred to as the weak Gaia hypothesis, the hypothesis suggests only that living organisms alter the abiotic conditions in which they live in ways that result in a more hospitable environment. A more radical version, often called the strong Gaia hypothesis, postulates the earth as a living superorganism, which, by design or conscious intent, maintains the balance of abiotic conditions necessary to support its own life.

Lovelock's initial hypothesis was stimulated in the 1960s by his study of the striking contrast between the atmospheres of Venus, Mars, and Earth. The atmospheres of both Venus and Mars are in equilibrium that is chemically inert, consisting of more than 95% CO_2. In contrast, Earth's atmosphere is also in equilibrium but is composed of a gaseous mixture (77% nitrogen, 21% oxygen) that should be chemically reactive and unstable. Lovelock sought a hypothesis to explain this anomaly and was struck by the parallel with biological homeostasis. In simple terms, the atmospheric equilibrium was maintained through a complex and dynamic interrelationship between the biotic and abiotic processes on earth.

Biological homeostasis is the property of living systems to maintain the internal equilibrium necessary for life. For example, the human body must maintain such features as temperature, salinity, nutrients, blood pressure, wastes, water, and oxygen within certain levels in order to remain alive. Biological systems maintain homeostasis through a variety of processes, including respiration, metabolism, sweating, shivering, excretion, and food ingestion. A series of physical, chemical, and biological processes work together in a complex system of feedback loops to produce and maintain the conditions necessary for life. Some might even say that this very interaction of physical and chemical processes of working together to maintain equilibrium is life itself.

Lovelock's initial hypothesis was that the earth is itself a living system. The earth can be understood as existing in a state of homeostasis in which physical, chemical, and biological processes work together to maintain a systemic equilibrium necessary for life. Photosynthesis is a paradigmatic example of such interaction. Life (in this case plants) creates, through a physical (solar energy) and chemical (water and carbon dioxide) process, the conditions (oxygen and carbohydrates) by which life can be maintained. Lovelock named this self-regulating living system after the Greek earth goddess Gaia.

The Gaia hypothesis was immediately challenged by a wide range of critics. The fact that it had been adopted by a diverse collection of New Age religions, mystics, and many environmentalists only added to its scientific disparagement. Scientific critics tended to focus on the stronger versions of the hypothesis in which purposive, intentional, and teleological categories were attributed to the Earth. Scientific criticisms especially rejected the teleological aspects of the hypothesis and denied that it was testable.

Revised and less teleological versions of the Gaia hypothesis have entered the scientific mainstream. Least controversial are versions of the hypothesis that simply acknowledge that living beings influence, and are influenced by, their physical environment. This conclusion enjoys universal scientific assent.

A somewhat more controversial version is defended by Lynn Margulis, whose initial work with Lovelock in the mid-1970s did seem to attribute purposive designs to the living earth. More recently, she defends a version that diverts from the homeostatic hypothesis. Instead, Margulis suggests that the earth should be understood as a "homeorhetic" system, a system in which a variety of dynamic processes interact but which do not tend toward any single state of equilibrium. Rather than operating in concert to maintain a single equilibrium, the earth's biotic and abiotic elements operate to remain in a relative, yet evolving, equilibrium. As a result, the biotic and abiotic elements of the earth are understood to be on a trajectory of coevolution. By implication, there is no guarantee that any particular biophysical equilibrium, including the one necessary to support human life, will continue into the future.

The Gaia hypothesis has given rise to a wide variety of ecological, social, and ethical conclusions. Even the more modest and metaphorical interpretations can reinforce ecological conclusions about the interdependency of life and its natural environment. Normative implications suggest caution when taking physical or chemical resources from, or putting waste into, the natural environment. Given the interdependencies of biological life and its abiotic environment, discretion and caution would be the prudent social and business policy. Strong versions of the Gaia hypothesis in which the earth itself is a living being suggest the possibility of recognizing moral standing for the earth.

The Gaia hypothesis can also provide a broader perspective on the concept of sustainability that is in much use within business and economic contexts. Sustainability is often characterized in terms of economic and business activity that provides for present needs without jeopardizing the opportunity for future generations to meet their own needs. The Gaian concept of homeostasis can be understood as the biological conditions necessary for economic sustainability. The Gaia hypothesis, therefore, can also provide a link between economic sustainability and the ecological sciences.

—Joseph R. DesJardins

See also Biocentrism; Deep Ecology; Environmental Ethics; Environmentalism; Global Business Environments; Greenhouse Effect; Kyoto Protocol; Moral Standing; Ozone Depletion; Pollution; Pollution Externalities, Socially Efficient Regulation of; Sustainability

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Gambling

Gambling, also often referred to as gaming or betting, has been defined as any behavior involving the risk of money or valuables on the outcome of a game, contest, or other event in which the outcome of that activity is partially or totally dependent on chance or on one's ability to do something. Gambling occurs in many forms and is now widespread throughout the world, whether as a legalized or illegal activity. For example, lotteries are publicly operated on almost every continent, in at least 100 countries. Lottery tickets are sold at more than 240,000 locations in North America, most of which are retail outlets such as convenience stores, gas stations, and supermarkets. Worldwide lottery sales were almost $160 billion in 2003. Legalized casinos (e.g., slot machines and table games) operate throughout North America, as well as in Europe, Asia, and Australia. Worldwide, revenue from legalized casino gambling alone is expected to exceed $100 billion in 2009, up from $68 billion in 2004. In the United States, casino gambling revenue will top $64 billion in 2009, compared with $47 billion in 2004. The Asia/Pacific region (and in particular the Chinese gaming enclave of Macau) is expected to be the world's second largest casino market, with revenues reaching $18 billion by 2009, up from $9 billion in 2004. Worldwide pari-mutuel wagering (e.g., horse racing, dog racing, Jai Alai) is estimated at $116 billion. Online gambling via the Internet has enhanced one's opportunity to gamble from the comfort of one's home. Revenues from online gambling (e.g., lotteries, sports betting, slots, blackjack, roulette, bingo, poker) reached almost $6 billion in 2003 and is expected to reach $17 billion by 2009.

Over time, a continuing debate over the morality of gambling has taken place. Society is now potentially at a pivotal point in time in the history of gambling, as many are wondering in particular whether the proliferation of gambling opportunities will continue to be a "financial pearl" or ultimately result in "social peril." To better address the nature of the debate, the following will outline the principal arguments for and against gambling. Other related ethical issues, such as whether or not governments should be involved in owning or operating various gambling ventures (i.e., whether governments are "addicted" to the tax revenues), whether advertising of gambling should take place or be limited, or the possible ethical or social responsibilities of gambling operators, while important, are outside the scope of this discussion.

Arguments in Favor of Gambling

Society's Acceptance of Gambling

One of the primary arguments in support of gambling is simply due to the fact that society now seems to accept it as a legitimate activity. In determining society's acceptance of gambling, one can look to various indicators such as polls regarding its moral acceptability, current legislation and its historical development, legal decisions, increased licensing of gambling activities, direct government involvement and promotion of such activities, and the large number of individuals who participate in games of chance.

All the evidence indicates that society's views have shifted dramatically with respect to gambling around the world, particularly over the last few decades. For example, although casinos were legalized in Nevada in 1931, until 1969 most forms of gambling remained illegal in the United States as well as elsewhere around the world. Eventually, however, amendments in criminal legislation began to legalize a wider range of gambling activities, such as lotteries and charitable gaming. Eventually, legislation was again amended providing various governments with exclusive jurisdiction over lotteries, slot machines, and video devices.

Several have documented the history of casino gambling in the United States and its transformation from an immoral practice into an acceptable activity. Even by 1993, casino visits made by U.S. households were 92 million, ranking ahead of other forms of popular entertainment such as major league baseball games and arena concerts. By 2004, the number of casino visits had increased to 319 million. Research from the American Gaming Association in 2005 indicates that approximately 54% of U.S. adults believe that casino entertainment is "perfectly acceptable," while an additional 27% believe that casino entertainment is "acceptable for others, but not for me." Only 15% feel that the activity is not acceptable. While certain governments in the world still prohibit various types of gambling activities (e.g., casinos), the vast majority now permit it.

From the above, it becomes extremely difficult to argue that gambling is unethical on the basis of society's conventions. Current legislation, the current level of gambling activity, and national surveys all indicate that a majority find gambling acceptable.

Gambling as a Source of Revenue and Employment

Gambling, from a consequentialist perspective, has certainly provided a tremendous source of revenue for governments (i.e., taxes) and gambling operators. Almost $5 billion in gaming tax revenues paid in 2004 by the industry to government bodies where casinos operated provided funding for needed services and programs for various communities. In addition, gambling activities have provided enormous opportunities for employment. The American Gaming Association found that in 2004 there were more than 350,000 individuals employed by the U.S. casino industry alone earning more than $12 billion in wages (including benefits and tips). Spending by the industry and its employees created approximately 500,000 more jobs nationwide.

Gambling as Entertainment

In addition to direct and indirect revenues, gambling arguably provides an additional form of entertainment that would have some degree of value for society. Many consider gambling a social activity and derive personal enjoyment from the "risk" involved. For some, the attraction of gambling is not the money, thrills, or addictive compulsion but the social rewards of regular participation.

Gamblers Possess the Moral Right to Gamble

According to moral rights theory, individuals should have the right to engage in gambling if they freely choose to do so, and governments should be prevented from limiting this right by deciding which activities their citizens can engage in. For example, a rights principle would suggest that a person is entitled to dispose of his or her own property in any manner they wish. The loss of money from gambling could be compared with other misguided voluntary actions such as making a bad investment in the stock market, whereby no claims of injury would arise.

Religious Arguments in Favor of Gambling

Each world religion takes a slightly different position on the moral acceptability of gambling. For example, Judeo-Christian doctrine does not directly forbid gambling. There is no mention of it in the Ten Commandments or in the Sermon on the Mount. On the contrary, one can find several biblical references to gambling. In the Book of Numbers, lots were taken to decide how to distribute the Promised Land. God placed the first wager in recorded biblical history to see whether Job's belief in God would falter if he were tested severely enough. In fact, many churches throughout the years have used bingo as a means of fund raising suggesting a level of moral acceptability.

Arguments Opposed to Gambling

Social Costs of Gambling

The benefits of gambling have to be contrasted with the costs. For example, in addition to the cost felt by gamblers (and their families) in losing their bets, arguably the most serious social costs of gambling are the contributions to gambling addiction that ensue. The central argument is that a certain number of individuals are prone to gambling addiction, that gambling addiction is a disease with severe societal costs, and that the existence of gambling opportunities only exacerbates the potential for individuals to become addicted.

As early as 1980, pathological gambling (as opposed to casual social gambling) was recognized by the American Psychiatric Association as an official disorder or illness in the *Diagnostic and Statistical Manual of Mental Disorders* (*DSM-IV*). Although the studies on the number of problem gamblers differ, most studies appear to place the prevalence rate at between 1% and 6% of the adult population. For those individuals who are problem gamblers, there are reports of serious social consequences such as throwing away savings and careers, abuse of families, lies and deception, illegal acts, divorce, depression, and even suicide. One study suggests that each problem gambler affects between 10 and 17 individuals, including one's spouse, children, extended family, employer, employees, clients, consumers, creditors, and insurance agencies. It has been estimated that the total social cost of a problem gambler is approximately U.S.$30,000 per year in lost productivity, social services, theft, and jails.

Gambling Exploits Gamblers

Others argue that gambling is wrong because as a potentially addictive activity it infringes on the mental health rights of problem gamblers. Gambling has also been viewed as exploiting the weaker elements of society (e.g., the poor) by creating unrealistic hopes of "winning it big."

Religious Arguments Against Gambling

Others use religious arguments in opposition to gambling in terms of stewardship; gamblers ignore their duty of ownership of property or their responsibility to properly use the property of God. While Judaism does not explicitly forbid gambling, the Talmud makes it clear that a professional gambler (i.e., one who makes money only from gambling) is not to be trusted as a witness during court proceedings. As opposed to Judeo-Christianity, Mohammed (the founder of Islam) considered gambling a forbidden pleasure in the Koran, and Confucius believed that gambling represents a significant human weakness.

Gambling as an Unfair Form of Taxation

The moral standard of distributive justice would ask the question, "Does gambling improve the lot of the least advantaged?" One view is that gambling is unjust as it takes disproportionately from the poor and almost none from the wealthy. This argument may be more related to lotteries whereby there is evidence that low-income families pay a higher proportion of their income on lottery tickets than high-income families.

No Net Benefit to Society

Other arguments suggest that there is not net economic gain in gambling (i.e., it is a nonproductive activity) if the benefits and costs for the entire world are taken into account, as opposed to a specific jurisdiction. For example, some research studies suggest that a particular state jurisdiction will not derive a net benefit unless gamblers are coming in from other jurisdictions, with the corresponding social costs left for other state governments to deal with. In a similar vein, one might argue that there is no net benefit to society from gambling, but rather, it simply leads to a reshuffling of assets from the "losers" (e.g., the gamblers and their families) to the "winners" (e.g., governments, casino operators, and their employees).

Response to Above Arguments

Due to the inability to translate many of the benefits and costs of gambling into monetary figures, a clear assessment of the overall impact of gambling on society is extremely difficult. Overall, gambling might be argued to benefit society, but only when the social costs due to problem gamblers are minimized.

While a rights approach does not provide a clear determination of the morality of casino gambling, most of the moral criticism based on a moral rights approach might be countered if gambling can take place in a manner that leads to a fair, informed transaction without deception or exploitation of gamblers, and with measures to protect problem gamblers. In terms of gambling representing an unfair form of taxation, as long as there is evidence that the disadvantaged are much happier for the opportunity to gamble and that the hope of winning is worth something and is not irrational, then it may not represent an unfair form of taxation.

—Mark S. Schwartz

See also Cost-Benefit Analysis; Justice, Distributive; Relativism, Cultural; Rights, Theories of; Socially Responsible Investing (SRI); Utilitarianism

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Game Theory

Game theory uses mathematics to model the interaction between two or more parties when they make decisions that will affect their outcomes. It sets up rules that determine each player's possible moves, the available information, and the various payoffs. Their actions are strategic in the sense that the actions of all parties are not fixed. The players have to make their best assessment of what to do in the face of actions of the other party and other variables to achieve an optimal outcome. Game theory has been used extensively in various fields, including economics, business, politics, social sciences, psychology, military planning, and more recently, biology.

Game theory originated shortly after World War II from work done by the mathematicians John von Neumann and Oskar Morgenstern for the RAND Corporation. It was further developed by John Nash and John Harsanyi in the 1950s.

The standard terminology calls the strategic interaction a *game*, and the participants are *players.* The best strategy is known as the *solution*, and the outcome is the *value* of the game. Games in this sense need not be trivial; for example, they have been used to work out nuclear strategy, where quite literally the payoffs involve life and death.

The game will specify who the players are, what moves are allowed, and the payoffs for each. A very simple example of a game used by von Neumann had two players who simultaneously present a coin face up or face down. If they are the same, then Player 1 wins by taking both coins; if they are different the coins go to Player 2. Games may be represented either by decision trees known as the *extensive* form that plot all the available information or more typically as a simple matrix (see Table 1).

Table 1 A Zero-Sum Game

	Heads	*Tails*
Heads	+1, −1	−1, +1
Tails	−1, +1	+1, −1

Source: Adapted from Neumann, J. v., & Morgenstern, O. (1953). *The theory of games and economic behavior* (3rd ed.). Princeton, NJ: Princeton University Press.

The rows typically correspond to the strategic possibilities for the first player, and the payoffs are typically rendered with the row player's result, followed by those for the column player. Thus in this case, if both play heads, the top left cell, then the row player will win the coin at Player 2's expense. This is a *zero-sum* game since a win for one side represents a loss for the other: +1, −1 = 0. We assume the players to be self-interested, and so they will seek to maximize their gains and minimize their losses.

Either before they begin or after a few rounds, players will develop a *strategy.* If a strategy were written down it would provide a set of directions that specify how to act and react to various payoff options. Here, the first player recognizes that if she is consistent in showing heads, then the other player will work out what is going on and play to his advantage by always selecting tails. Both sides impute similar rational thinking to the other and develop a strategy that denies any advantage to the opponent. In this case, the first player is best off choosing randomly and the best response by the second will be to play randomly as well. Thus in this game, and in fact for any similar game, the sides will come to a point where they have achieved the best possible response given the constraints and payoffs involved.

Maximin

In a one-time, two-party, zero-sum game no cooperation is possible. We can imagine that two hungry children have to divide a pizza, where one cuts once and the other chooses whichever half she wants (see Table 2).

Table 2 A Maximin Game

	Choose Bigger	*Choose Smaller*
Cut evenly	Little difference +	Little difference −
Cut unevenly	Disproportionately large	Disproportionately small

Source: Adapted from Poundstone, W. (1992). *Prisoner's dilemma* (p. 43). New York: Bantam Doubleday.

If we put ourselves in the place of the cutter, the clear strategy is to cut as evenly as possible, because we believe the chooser will take the largest slice offered. It is plausible that she will irrationally take the smaller, but we impute our own motives onto her and, therefore, expect that if we cut unevenly we will lose out by doing so. The cutter is attempting to maximize the possibility of an outcome that provides the chooser the minimum possible. Here, that will be the top left cell, and the strategy is known as the *maximin.* In a similar vein, John Rawls says in his book *A Theory of Justice* that behind the veil of ignorance, and not knowing exactly our place in society, a rational, risk-averse person would choose the maximin strategy by spreading almost equal opportunities as widely as possible so that they are available to everyone.

Equilibrium

Equilibrium represents an optimal strategy for a player. In the following game, we can imagine that a business, Widget Inc., is trying to decide whether to spend money on a new advertising campaign (see Table 3). The advertisements promise to be cost effective by bringing in more revenue. If its rival also launches a campaign at the same time, however, the effects will be considerably dampened.

Table 3 A Strategy for Equilibrium

	Launch	*Do Not Launch*
Launch	+1, +1	+5, 0
Do not launch	0, +5	0, 0

Source: Adapted from Davis, M. (1997). *Game theory: A non-technical introduction* (p. 34). New York: Dover.

Looking at the various options, the row player will be better off by launching the campaign whatever the other company does. The game is not zero-sum, since a gain for one side is not made at a cost to the other. Widget might hit the jackpot if the rival does nothing, but nevertheless advertising will always bring a gain. However, if both sides are aware of what the other is doing and each other's payoffs, then they are likely to act the same way, with the result that both will end up advertising. In technical terms, Widget will be better off choosing to advertise in every case, that is, its *dominant* strategy. Thus, in this game the sides will come to the equilibrium point where they select the best possible response available in the circumstances.

Table 4 represents a game called "battle of the sexes" (sometimes, battle of wills). In this case, a couple, Martha and George, want to go out together, but it is a one-time date, and hence they cannot alternate preferences. Martha, the row player, prefers the opera (which she rates as worth 2) to boxing (rated 1), whereas George would rather watch boxing (2) than the opera (1). They both want to go out together instead of going alone (0). There is no dominant strategy, and hence no obvious solution. The outcomes depend on the parties communicating and accommodating the desires of the other, lest they be left alone. Hence, this kind of choice set is called a *coordination game.*

In games without a dominant strategy, each side will opt for strategies that have the result that any alteration will make them worse off. This is the case with the battle of the sexes: They can both go to the opera or both to the boxing match, and any other choice has a less attractive outcome. These optimal points are known as the *Nash equilibrium.* Some games will have multiple equilibriums, but nevertheless the set will be limited and can be portrayed mathematically.

Mixed Strategies

In cases where there are multiple equilibriums, game theory has worked to establish decision processes for choosing the right strategy. The game of tennis gives us a nice example of how mixed strategies operate. Imagine that there are two players who have a weekly game. Although fairly evenly matched, one is better at serving the ball to land near the net rather than at the back of the court. However, if she plays to her strength all the time, then the opponent will realize what is going on and adapt his play accordingly. Thus, in a repeated game it may be worth altering strategies from time to time. We assume that both sides think the same way and are aware of what the other side is doing but find an advantage in keeping them guessing. Furthermore, game theory asserts that expected payoffs are treated the same as certain payoffs; in other words, a player will be risk neutral between receiving $15 and a 15% chance of earning $100 (and the associated 85% chance of getting nothing). Once we incorporate this assumption, we can then use probabilities in working out the optimal strategy for any game.

So, for example, one of the tennis players may have a 90% chance of winning a point by positioning herself at the back of the court because the other player routinely places himself near the net (see Table 5). Rationally, she ought to do that for every serve. However, as the other player learns what she is doing, he

Table 4 The Battle of the Sexes

	Opera	*Boxing*
Opera	2, 1	0, 0
Boxing	0, 0	1, 2

Source: Adapted from Battle of the sexes. (2005). In *Dictionary of game theory terms.* Retrieved December 21, 2005, from www.gametheory.net/dictionary/Games/BattleoftheSexes.html

Table 5 A Mixed Strategy

	Front	*Back*
Front	50, 50	80, 20
Back	90, 10	20, 80

Source: Adapted from Duffy, J. (2003, December). *Introduction to game theory.* Retrieved from www.pitt.edu/~jduffy/econ1200/Lectures.htm may well change his position and the likelihood of her success would diminish. Next, we integrate the second player's response (for ease, limited to two options in this case). The players can play front or back. However, rather than getting direct payoff, we put in the percentage of success; recall that a 90% success rate over 10 serves will be equivalent to a payoff of 9.

If the column player alternated front and back randomly over a series of games, then the row player is better off constantly playing back; the winnings will offset the losses over time. The situation is more fluid, though, because the column player is making exactly the same sort of calculation. Mathematically, we can plot the point where the payoff for the opponent is the same whatever strategy they employ. That will tell us their ideal mix of strategies in the face of our behavior and is termed a *best response function.* (Here, it turns out if the row player plays front 60% of the time, her opponent will be indifferent to front or back.) Combining the probability of the other side making a particular choice and the payoffs they will receive from it with our own allows us to derive what we can expect over repeated encounters. In business as well as tennis, plotting out the equilibrium point with mixed strategies enables us to minimize any exploitation that could arise from constant predictable behavior. As an interesting correlate, some chess grand masters playing challengers they have met several times before have benefited from making deliberately poor opening moves to throw their opponents off guard.

Nash acknowledged that his formulation relied on the assumption of complete information about the choices and payoffs facing the other side and fully realized that if it is relaxed, then the outcomes are far less predictable. In typical bargaining, for example, the parties often deliberately try to mislead the other side about their goals and alternatives. This will confound the predictions somewhat, and a lot of research has gone into marrying the cleanliness of laboratory testing with the messiness of the real world.

Variables

Game theory deals with a number of variables. Games may be zero-sum, or may have outcomes that depend on cooperation. The payoffs may not be symmetrical, and the players may have mixed motives. For example, in cases such as the famous prisoner's dilemma it is mutually beneficial to cooperate, but rational to go it alone if there is reason to suspect that the other side may defect from the enterprise. In the coin game above, the sides had to take action simultaneously, whereas in dividing the pizza the parties took turns and could clearly see what the other side had done. Some games are single play, whereas others have many rounds where players are faced with similar choices. Consider, for instance, that the tactics a buyer uses at a yard sale may be significantly different from those at a weekly market.

Another key factor is the number of players involved. In the so-called *n*-player games, players have the opportunity to form coalitions. Thus, there may be three companies bidding on a contract; the client says that the payments will be the same whether two companies or three share the work. This leaves each manager with the decision of whether it is better to join an alliance of three and get less reward or try for a two-party coalition's higher amount with the consequent risk of being frozen out of the deal altogether by the other two. There are sophisticated mathematical means of working out the best course of action for coalitions working under uncertainty as long as there are rational players and sufficient information, again based on calculating the probability of achieving the optimal payoff from all the various possible permutations.

Confounds

Humans tend not to be perfectly rational in their decision making. A series of recent experiments have set up games where participants have to guess a number, and then divide it by a fraction they decide on, and the one closest to the mean of the group wins. Thus, if ten participants decide on the numbers 10, 20, and so on to 100, and the fraction they choose is one half, the total will be 550, the mean 55, and the answer half of that, 27.5: The winner would be the one who chose 30. Once participants realize that the number has to be low, they would modify their choice if they could for the next round; for example, the person choosing 100 would make a far more conservative guess nearer 30. But, of course, the people who chose 90 and 80 would also act the same way and so the final number would keep going down. The Nash equilibrium for this game is to choose 0, but it takes forethought to work this out. The number someone chooses reflects their ability to think in the abstract about future choices and make judgments about their fellow players' ability to do the same. Research shows that the majority of people only think one or two steps ahead. This goes against Nash's assumption about perfect rationality over iterated plays. If we apply game theory to real-life applications such as negotiation, then we would do well to assume that most people are only thinking one or two steps in advance, either because they are incapable or unaware of repeated strategic play.

Utility

Utility is a measure of personal welfare. Individuals place different values on resources and events. There are signs, for example, on casinos in Las Vegas that declare they return 98 cents on the dollar. The clear message is that the house will win, and thus it is economically irrational. On the other hand, we realize that players are paying for the thrill of betting, and hence they find it a worthwhile expense.

A game that is totally zero sum, where the options are essentially "take it or leave it," often demonstrates how our decisions are not purely economic. One form has a pair of negotiators given the chance to have $100 if they can decide on a division against a deadline. Typically, participants will come up with an even split, but one strategy is to hold out for a $99 to $1 division; rationally, it makes sense that someone should take a dollar rather than nothing, but it is very common for people to walk away from the deal because of the perceived inequity. The effects of the deadline and perceptions of the future relationship come into play, too. Individuals have psychological needs to be respected and treated fairly, and game theory does not incorporate these values very well.

Utility also varies with wealth in the sense that a rich person can afford to forsake a gain much more readily than a poor one. In addition, experience shows that people are conservative when faced with risk; contrary to economic supposition, most people would prefer a certain million dollars than a 50% chance on 2 million if faced with the real choice.

A lot of recent work has been done in the area of trust. For example, one game gives the first player (P), say, $10. P then divides the money and sends some amount to a receiver (R). The amount that R gets is doubled or tripled, and then R is asked to do another allocation back to P. Under Nash's assumptions, no money would be sent either way because of the conjecture that the players are selfish and untrusting. Instead it turns out that the average amount allocated to each is about half the total. This implies that people are inclined to put themselves in the other party's shoes and treat them accordingly. Furthermore, the perception of intentions appears to have a significant effect on play. In prisoner's dilemma games where cooperation had been established, and one side defects to its own benefit, expressions of regret were tremendously effective in reestablishing cooperation, although they are regarded in economic terms as *cheap talk*. Although all these effects can be modeled with proxy valuations in games, they are highly subjective and vary widely in different situations.

The fact that we favor some people more than others is known as *social preference*, and the effect is that we develop networks and alliances to facilitate our dealings. Here again, this mirrors common experience that has only been recently incorporated into game theory and shows us that individuals do not always act as selfish atomistic entities. Despite some of these limitations, game theory has been profoundly effective and influential over the past 50 years in bringing intellectual rigor into discussions about decision making.

—Kevin Gibson

See also Auction Market; Decision-Making Models; Equilibrium; Free Riders; Nash Equilibrium; Negotiation and Bargaining; Prisoner's Dilemma; Tragedy of the Commons

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Gay Rights

Historically, the term *gay rights* has encompassed areas as diverse as free speech, employment, religion, and cultural expression. Proponents of gay rights argue that the ability to inherit property from their partners without paying inheritance taxes, to have legal standing in matters involving a partner's health and legal guardianship, the right to marry, and the right to adopt children are basic civil rights that belong to all individuals, including gays, lesbians, and transgender individuals. Critics of gay rights argue that homosexuality is contrary to human nature, generally from a moral or religious perspective.

Because there are so many interest groups with widely diverging perspectives, there can be no single definition for the term *gay rights*, but in a broad sense it refers to a movement that supports nondiscrimination against lesbians, gay men, transgender individuals, and other sexual minorities identified by sexual orientation. From a business perspective, such support would include access to equal employment opportunities, provision of domestic partnership benefits, gay-inclusive diversity training, the protection of employees against violence and other forms of harassment in the workplace, and nonbiased representations of gays and lesbians in television, newspapers, and all other forms of media. Critics of such corporate policies contend that promotion of a gay or lesbian lifestyle undermines family values. Groups such as Focus on the Family and The Christian Coalition argue that gay rights advocates are seeking special treatment. In response, these groups conduct protests, create picket lines, and boycott products and services to make their opposition known.

Taking a position either for or against gay rights must first assume that all individuals are entitled to *rights*. From a philosophical point of view, a presupposition to rights can be disputed. Rights theorists have examined this question from a variety of perspectives, taking into consideration the fact that an individual's actions may be governed by self-interest or preservation of a culture or community, or that one might shift the discussion from a matter of rights to one that focuses on *responsibilities*. If an employee, for example, claims a right to spousal health insurance, does that employee have a corresponding obligation to claim that right for others in the same firm? In addition, one might argue that such benefits are not natural but acquired rights, and as such do not extend to all members of the community. Such arguments have broad implications. Nevertheless, organizations, whether countries or corporations, have created constitutions, laws, policies, and regulations based on the assumption that certain fundamental rights do exist. Whether or not these rights can be extended to specific interests groups such as gays and lesbians is a matter of historical debate.

The Global Perspective

From an international point of view, the response to equal rights for gays and lesbians varies widely; however, the legal problems faced by same-sex partners are similar around the world. One of the earliest movements to petition for gay rights formed in Germany in the 1890s. Magnus Hirschfeld, Max Spohr, and Erick Oberg founded the Wissenschaftlich-Humanitäres Komitee (the Scientific-Humanitarian Committee) in Berlin in 1897. The committee provided assistance for defendants in criminal cases and labored to achieve social recognition of homosexuals. Their major goal was to lead a program to repeal Paragraph 175 in the Imperial Penal Code of the German Constitution that contained a provision against homosexual behavior. Such behavior was considered immoral and many medical professionals concluded that it was a form of mental illness. Although the provision was repealed in 1929, the rise of the Nazi party led to additional anti-homosexual measures and the Wissenschaftlich-Humanitäres Komitee eventually disbanded.

Today, the position of gays and lesbians in many societies is largely governed by religious and traditional cultural beliefs. In many Asian countries, where family relationships are highly prized and individual rights are sometimes subservient to the rights of groups, social acceptance of gays and lesbians would undermine such values and is, therefore, strongly discouraged. Religion has a persevering influence on politics in Middle Eastern countries and in traditionally Catholic countries such as Italy and Spain; however, in July 2005, Spain officially published a law legalizing same-sex marriage. Other western European countries and Australia are considered more liberal with regard to gay and lesbian issues, and in Britain and Europe many gays and lesbians have formed political alliances with the left, whose members often promote social policy reforms that benefit minority communities.

In North America, Canada's federal government indicated that it would extend spousal benefits to the gay and lesbian partners of federal employees in 1999. The plan covers more than 300,000 federal employees and pays the same survivor pension benefits to spouses of gay and lesbian employees as are currently paid to spouses of heterosexual couples. In Latin America, there have been several proposed initiatives. In 1996, the Statutory Convention of Buenos Aires, Argentina, approved a measure forbidding workplace discrimination on the basis of gender, age, race, religion, political ideology, or sexual orientation. According to a study by the International Gay and Lesbian Association (ILGA), this measure made Buenos Aires the first Spanish-speaking city in Latin America to address all these issues. In March 2003, Brazil presented a resolution on sexual orientation at the UN Commission on Human Rights in Geneva. The text states that sexual diversity is an integral part of Universal Human Rights. Under the pressure of the Organization of Islamic Conferences and the Vatican, a solid block of countries opposed the voting of the text in 2003. In 2004, Brazil, realizing that the resolution still did not have sufficient support to ensure passage, decided to postpone discussion to 2005, but the commission again delayed the vote during that session.

Scandanavian countries and the Netherlands have been more liberal in supporting gay and lesbian rights. On June 21, 1979, the Netherlands passed Article 1623h of the Civil Code, a law granting a succession right to a same-sex cohabitant of a deceased tenant. In June 1989, Denmark passed the Law on Registered Partnership, which allowed same-sex partners to register, and in December 2000, Article 30(1), Book 1 of the Civil Code of the Netherlands was amended by the *Act on the Opening up of Marriage*, which allows marriage by two persons of the same sex.

Currently, there are 48 countries that have publicly supported sexual orientation as an issue at the UN Commission on Human Rights between 2003 and 2005. In addition to recent laws passed in the United States, legislation recognizing some form of same-sex partnership has been passed in at least 18 of the 189 countries that are members of the United Nations, including Australia, Austria, Belgium, Canada, Denmark, France, Germany, Hungary, Iceland, the Netherlands, New Zealand, Norway, Portugal, Scotland, South Africa, Spain, Sweden, and Switzerland. Some of these laws allow registration for partners and offer an official legal recognition. Many include antidiscrimination laws that prohibit discrimination in employment, housing, and other areas.

Today, gay rights activists are working to create a global agenda, and groups such as the ILGA attempt to bring these issues up for consideration by larger bodies such as the United Nations. In 1994, one year after ILGA had been granted consultative status at the United Nations, the Economic and Social Council suspended it, based on concerns that the association promoted pedophilia. Subsequently, ILGA requested reinstatement of its status, but a number of delegations repeated their concerns and the Economic and Social Council voted again in 2002 to deny the association consultative status.

Gay Rights in the United States

Although many scholars mark the beginning of the modern American gay rights movement with the Stonewall Rebellion of 1969, the struggle for gay rights in the United States has a long history. One early activist group, the Society for Human Rights, was founded in Chicago in 1924. The organization published two issues of a newsletter called *Friendship and Freedom*, but the members disbanded after only a few months. For many years, division between private and public life was an accepted part of homosexual society. Police frequently raided gay bars and cruising areas such as parks and public restrooms, publishing the names of those arrested in newspapers. Such publicity often meant losing a job.

It was generally regarded that homosexuals were vulnerable to blackmail and easily convinced to divulge sensitive information to political adversaries. After World War II and the Cold War, gays and lesbians were linked to Communist organizations and were denied employment as civil servants because they were considered security risks. Such restrictions on civil rights led to the rise of several "homophile" movements, including the Mattachine Society, a men's group established by Harry Hay in Los Angeles in 1950, and the Daughters of Bilitis, a women's group formed in San Francisco in 1955 by Del Martin and Phyllis Lyon. These organizations sought to create change through existing institutions without challenging the values of mainstream society. They sought legal and legislative ways to secure basic rights for gays and lesbians.

To some extent, these early groups protested antigay employment practices, particularly in government employment, but for the most part they served as social outlets, educational forums, and support groups. But by 1964, gay men and lesbians were picketing government offices, demanding civil rights and calling for an end to discriminatory employment practices. Even then, the federal government prohibited lesbians and gay men from civil service employment until 1975. Opposition to the war in Vietnam, and persistent discriminatory practices in employment, housing, and education, sparked resistance efforts for many groups seeking freedom from oppression. This period, inspired by the black civil rights movement and Women's Liberation, was marked by public protests. Between 1968 and 1973, the years of "gay liberation" sparked by the anti-Vietnam war activism, such rebellion was characterized by a much more vocal style of protests and an emphasis on "coming out."

The Stonewall Riots began on the evening of Friday, June 27, 1969, when New York City police raided the Stonewall, a popular gay bar in Greenwich Village. Many of the patrons fought back, locking the police in the bar and setting it on fire. The street riots continued between the police and angry residents for another day and night, and *Stonewall* became a symbol for the modern gay rights movement. In many ways, this protest divided the generations—unlike their earlier counterparts, the activists involved in the Stonewall riots sought to work against the system rather than inside it. But all those who supported gay and lesbian causes benefited from the publicity generated by their outcry, and by the mid-1970s most major U.S. cities hosted gay pride marches attended by individuals from all generations who marched enthusiastically side by side.

Much of this activism was in response to specific state and federal legislation. Until 1961, when Illinois decriminalized sodomy, all 50 states in the United States had laws against it. Other states followed Illinois in repealing these laws, but in 1976 the Supreme Court upheld Virginia's sodomy law, which made it a felony for individuals of any orientation, punishable up to 20 years in prison. Another Supreme Court decision in 1986, *Bowers v. Hardwick*, upheld Georgia's right to make and enforce sodomy laws. A series of state decisions overturned sodomy laws, in Louisiana in 1994, Michigan in 1990, and Georgia in 1998.

As these laws were repealed, gay activists began to push for inclusion of new laws recognizing same-sex partnerships. By 1997, more than two dozen cities had domestic partner registries. State courts witnessed a wide variety of cases, and today many cities and states allow same-sex couples to register for domestic partnership. In 2003, the Vermont Supreme Court found that same-sex couples had the same rights to benefits as married couples, and the state legislature created a category of partnership called "civil union." In May 2004, Massachusetts became the first state to legalize marriage for same-sex couples; however, the state's governor Mitt Romney, a staunch supporter of exclusively heterosexual families, has backed a campaign to reverse the court's decision. On a national level, the Defense of Marriage Act, enacted by the U.S. Congress in 1996, prohibits federal recognition of same-sex marriages.

From a business perspective, equal employment is a focal point for discussion about gay and lesbian rights. In 1980, the Office of Personnel Management prohibited employment discrimination based on sexual orientation in all federal civil service jobs. In 1994, the Employment Non-Discrimination Act was introduced in Congress, offering gay men and lesbians protection against antigay discrimination in the federal workplace. The act prohibited discrimination based on sexual orientation, but it was voted down in 1996 by the Senate by a 50 to 49 vote and never made it to the House.

Defenders of gay rights also argued for benefits from corporations and some complied, in part because of growing protests from consumers. One of the first gay and lesbian protests against a major corporation began in the spring of 1970, when gay liberationists in San Francisco, New York, and Los Angeles picketed ABC after one of its affiliate stations fired an employee because he participated in a militant gay movement. When Anita Bryant led an effort to repeal a Dade County Florida gay rights ordinance and the measure was repealed in 1977, gays and lesbians led a nationwide orange juice boycott. In the 1980s, activists challenged the price of pharmaceutical companies for AIDS treatment drugs, with protests by such groups as ACT UP that convinced Burroughs Wellcome to reduce the price of AZT. Other early protests included action against AT&T, which then added "sexual orientation" to its nondiscrimination policy in 1974.

Groups such as the Human Rights Campaign and the Investor Responsibility Research Center periodically survey corporations to gather data regarding equal employment policies, and such surveys indicate that there is a growing trend to incorporate "sexual orientation" into nondiscrimination policies. A report on equal employment opportunity issued by the Investor Responsibility Research Center in 2003 examined gay and lesbian rights as part of the larger issue of equal opportunity for women and minorities. The report found that although there has been significant demand for public disclosure of workforce data by race and sex, only a small percentage of U.S. companies comply with such requests. The report also noted that there is no federal legislation to protect gays and lesbians in private employment from discrimination based on sexual orientation and that only 13 states have made it illegal to fire someone based on sexual orientation.

Those 13 states have amended their civil rights statutes to include sexual orientation in the private sector and 9 have executive orders barring such discrimination. At least 130 cities and counties have employment nondiscrimination laws that include sexual orientation. Many of these municipalities have adopted ordinances requiring extension of same-sex employee benefits as a prerequisite to eligibility to contract for goods or services. On the opposing side, equivalent measures were enacted to facilitate continued employment discrimination against gays and lesbians. In January 2000, the governor of Ohio, Bob Taft, deleted the words "sexual orientation" from a state government policy banning employment bias. In November of that year, Maine voters rejected a ballot initiative banning discrimination based on sexual orientation, and in December of that same year, a judge overturned an executive order in Iowa that prohibited the state from employment discrimination based on sexual orientation or gender identity.

Corporate Policy

More than 60% of the Fortune 500 corporations have nondiscrimination policies that bar discrimination based on sexual orientation. In 1984, IBM became the first corporation to adopt a written nondiscrimination policy that included sexual orientation. By 1997, more than half the Fortune 1000 companies offered domestic partner health and other benefits. In June 2000, the Big Three automakers announced that they would offer domestic partner benefits to same-sex partners of more than half a million gay and lesbian employees. These benefits included coverage of medical, dental, and prescription-drug costs to same-sex domestic partners of all eligible U.S. employees. Workers are required to attest that their domestic-partner relationship meets eligibility guidelines, including being of the same sex and having shared a committed relationship with each other for no less than 6 months. Although there are no studies to indicate that such policies have had a negative effect in the workplace, critics might argue that such benefits undermine the meaning of marriage or divert funds that might instead benefit the entire workforce.

To date the only studies that evaluate corporate behavior have been conducted by defenders of gay rights. The Human Rights Campaign Foundation (HRC) launched the Corporate Equality Index in 2002 as a way to evaluate how major U.S. corporations treat their gay, lesbian, bisexual, and transgender employees, consumers, and investors. The Foundation surveys the Fortune 500 companies, companies on *Forbes*'s list of the 200 largest privately held firms, and any other company with 500 or more employees that requested a rating or for which HRC had sufficient data to derive a score.

The criteria used in creating the Corporate Equality Index requires a written nondiscrimination policy that includes the words "sexual orientation" or "gender identity" or "gender identity and/or expression" in a corporation's primary written nondiscrimination policy. The index also measures health insurance coverage to employees' same-sex domestic partners firmwide or cash compensation offered to employees to purchase health insurance for a domestic partner on their own. Other criteria include recognition and support of a gay, lesbian, bisexual, and transgender employee resource group; diversity training that includes sexual orientation and/or gender identity and expression in the workplace; respectful and appropriate marketing to the gay, lesbian, bisexual, and transgender (GLBT) community; and financial support for GLBT health, educational, political, or community organizations or events. In 2004, a total of 56 companies met all the criteria, resulting in a score of 100%. This was more than four times the number of perfect scores awarded in 2002, the first year the index was released. No company that received 100% in 2002 or 2003 has seen its score decrease.

Corporations must also take into account the values of customers who oppose such nondiscrimination policies. Campaigns against "gay-friendly" corporations include boycotts and letter-writing campaigns.

Conservative organizations such as the American Family Association, the Family Research Council, the Moral Majority, Anita Bryant's Save Our Children, and the Southern Baptist Convention have opposed corporations offering benefits to same-sex domestic partners on moral and religious grounds. In 1996, the Southern Baptist Convention issued a statement opposing Walt Disney Company for offering benefits to same-sex partners. The Convention encouraged its members to boycott Disney's theme parks and store. Similar groups have also contacted Cracker Barrel to protest adding "sexual orientation" to its nondiscrimination policy.

Conclusion

On a global scale the response to defenders of gay and lesbian rights varies widely. Although there have been many changes, particularly in the area of employment, not all gays and lesbians feel they have job security. Employment discrimination continues, particularly at the federal level. The armed forces, one of the largest employers in the United States, refuse to accept avowed gays and lesbians among its ranks. A September 2002 survey released by Witech-Combs communications and Harris Interactive(R) found that almost 1 in 10 gay and lesbian adults had been fired, dismissed, or pressured to quit a job because of their sexual orientation.

Corporations provide support for gays and lesbians in a variety of ways. Many major companies advertise in gay and lesbian publications and provide financial support through foundations and community giving programs. Proponents for gay rights contend that these corporations benefit by recruiting talented employees and by addressing the needs of gay and lesbian consumers and investors. At the same time, these corporations risk alienating conservative groups that seek to prevent such policies. Those who defend gay rights base their arguments on the fact that gays and lesbians are members of a larger community and that corporations that provide benefits to that community should also address their needs. This is a basic tenet of rights theory. Those with opposing viewpoints generally do not make an argument based on equality, or entitlement, or human need, but instead base their opposition on convictions that stem from scripture or morality.

As more corporate executives make the decision to recognize or dismiss sexual orientation as part of a larger human resources agenda, they must weigh the effects of such changes on the entire organization. These effects will vary from one organization to the next. From a practical perspective, it may not be a question of morality or human rights, but a question of how such policy changes will influence the bottom line. However, as is evident by the history of boycotts on both sides of this issue, consumers' moral values and principles can dramatically affect corporate profits. On an international scale, as more multinational corporations adopt workforce diversity, these policies will have a significant impact on global perception of sexual minorities. Conservative and religious opposition will continue to resist broader acceptance of gay rights, and the array of issues relevant to gay rights will remain in flux for the foreseeable future.

—Eugene H. Hayworth

See also American Civil Liberties Union (ACLU); Benefits, Employee; Civil Rights; Diversity in the Workplace; Employee Relations; Employee Rights Movement; Employment Discrimination; Equal Employment Opportunity; Equality; Human Rights; Lesbian Ethics; Minorities; Multiculturalism; Sexual Harassment

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Gender Inequality and Discrimination

Gender inequality can be defined as allowing people different opportunities due to perceived differences based solely on issues of gender. Gender discrimination is the prejudicial treatment of an individual or group due to gender. Gender inequality and discrimination are generally discussed as pertaining to women, but anyone can experience gender-based inequality or discrimination.

In order for these definitions to have meaning, we must first define "gender." The terms *gender* and *sex* are sometimes used interchangeably, but social scientists and medical personnel are beginning to recognize them as different. Sex refers to one's biological identity as defined by physical and/or chromosomal makeup. Generally, people are categorized as either male or female depending on their chromosomes and/or genitalia. Gender is commonly defined as the social identity of the sexes. It is determined by socialization and social values, not biology, and includes social markers such as behavior and appearance. Usually, people who identify as transgender believe they are different in sex and/or gender than what society has labeled them. For example, a person may believe himself to be a man despite genitalia that is defined as female by society. Transgender issues have helped bring to light the spectrum of sex and gender possibilities that is denied by the male or female binary and the use of sex and gender interchangeably.

This entry will begin by exploring the broader issue of gender inequality and will then discuss gender discrimination as it relates to business.

Gender Inequality

Gender inequality is rampant in most societies. In some countries, women continue to be denied access to financial resources such as bank loans to start a business, scholarships for education, and legal recourse against wrongful termination. American popular culture illustrates more subtle examples of gender inequality. In general, women are portrayed in the media as weaker and less intelligent than men. Magazines marketed to women tend to define women in terms of their being sexually attractive and available to men. On television and in movies, women tend to be younger than their male counterparts and cast in roles that are supportive to a male and less serious. Women are held to a more rigid standard of beauty and are depicted as more sociable, nurturing, and caring. In popular culture, men are generally portrayed as more aggressive, assertive, and violent as well as less expressive and emotional than their female counterparts. While male characters are more likely to initiate violence, female characters are more likely to be the victim of male violence. These stereotypes of gender hold each sex to an impossible standard. Gender inequality is perpetuated not only by a person's views of others based on gender, but also her or his view of her or his own abilities and opportunities based on her or his gender. Gender inequality can manifest itself in obviously discriminatory ways—such as not hiring a male candidate for a child care position because of the stereotype that women are naturally better at child care—and in more subtle ways—such as a male not ever considering a career in child care because he has internalized the stereotype that desiring such a position proves he is feminine.

Gender inequality is a major concern of feminist theorists. While some have fought for the equitable treatment of women in society, others have celebrated the difference between the sexes. Feminist theories on gender can be split into three major categories: essentialist, constructivist, and performative. Essentialists believe that something innate within people determines their gender. Essentialist feminists tend to celebrate what they define as the "feminine" and believe that embracing the "feminine" will allow women to better understand their difference from men. Carol Gilligan, Nancy Chodorow, and Luce Irigaray are examples of essentialist thinkers. Constructivists believe that gender is not innate or natural but constructed through interactions with society. Constructivists believe that one's sense of his or her gender does not come from something essential but rather is created. Constructivist thinkers include Gloria Anzaldua, Donna Haraway, and Juliet Mitchell. Performative theories describe gender and all gendered behaviors as performative, meaning that one behaves in a particular way to perform the gender roles he or she believes society requires. Judith Butler wrote the most well-known performative theory, which can be categorized as a constructivist theory. Eve Kosofsky Sedgwick also proposed a performative theory of gender, one that focuses on sexual orientation. Sedgwick theorizes that while there are performative aspects of gender, there must also be something innate. Her theory attempts to combine essentialism and constructivism. Debates regarding gender inequality continue within feminism, and inequality remains a central issue for most feminist theorists.

Differences between the sexes—either real or perceived—have caused differences in the ways individuals are perceived and valued in society. These differences in treatment have caused inequalities between the sexes. Gender inequality differs between nations and within nations. While generalizations about gender inequality can be made based on recent research, individual experiences may differ greatly depending on the time and place, as well as the perceptions of those involved.

Causes of Gender Inequality

There are many, often competing, ideas about the causes of gender inequality. Theories regarding the causes of gender inequality can be grouped into five main categories: biological, psychological, sociological, materialist, and religious.

The biological argument for gender inequality states that women are physically weaker than men and made more physically vulnerable by their ability to have children. Therefore, women need to be protected by men. This argument had more support when the majority of work needing to be done was physical in nature. Now that the majority of jobs do not involve physical labor, this argument has lost much of its appeal. Women's menstruation has also been used to argue that they are less emotionally stable than men and, therefore, should not be allowed positions of power, such as political office. By unfairly denying women access to the workplace, a society is not using all its resources.

Sigmund Freud and other psychological thinkers have proposed various psychological theories to explain gender differences and, therefore, gender inequality. To compliment the "Oedipus Complex," Freud developed the "Electra Complex" through which a young girl supposedly realizes that she and all women do not have penises, which causes her to feel inferior to men and, therefore, develop "penis envy." Freud defines a woman's gender identity through the lack of male genitalia. This use of the male as the norm persisted in psychology through much of the 20th century until Carol Gilligan began to explore female identity and developed her theory regarding the ethics of care. Defining women as the other (i.e., not men) may explain why "women's work" (generally thought of as the nurturing and caring of others) has been devalued by most cultures.

The socialization of children is believed by many anthropologists and sociologists to be the main cause of gender inequality. From the moment a child is born, his or her gender is the deciding factor in how the child will be treated by both the family and the society at large. Children learn appropriate behaviors for their gender. In most cases, this means that boys are socialized to be "masculine" (typically defined as more independent and aggressive), while girls are taught to be "feminine" (more dependent on others and nurturing). Gender socialization is a cycle that perpetuates itself through generation after generation.

Materialist theories point to the lack of access to valued resources as the cause of gender inequality. Due to their position either in the home or in lower-valued jobs, women do not have personal access to the most valued resources in their society. While a mother's work in the home is vital to a society, it is devalued, goes unpaid, and is not acknowledged as work. Women also have less access to financial resources due to lower paid or unpaid work. Historically, women have received a lower level of education than their male counterparts. This lack of educational resources limits women's ability to improve their material status. Recently, this educational trend has begun to reverse in some nations.

Finally, religious beliefs have also affected gender equality. Most of the major religious texts imply that men are superior to women, causing those that follow these teachings to maintain the conditions that cause gender inequality in their culture. For Christianity and

Judaism, the Old Testament of the Bible is that text. In the Old Testament, women are often absent and, when present, have a subservient role to men. One portion of text that is often cited as the source of gender inequality is in Genesis: Eve is created out of one of Adam's ribs. Many read this as an illustration of female inferiority. The role of women in Muslim culture is currently being debated. Many Muslims believe that the Quran mandates women's subservience to men. They argue that their religious laws are based on the understanding of gender by the divine. The role of women has evolved in religions over time and will continue to do so.

Reinforcement of Gender Inequality

Gender inequality is reinforced through various social structures, most prominently social, familial, religious, and materialist structures. Language also perpetuates gender inequality by reinforcing the idea that men are the dominant gender and women are subordinate. Until recently, "he" was universally accepted as the generic pronoun in English for a person of an unspecified gender. Many languages continue to be more "gendered" than English. For example, in many Romance languages plural groups of people with just one male use the male version of the plural noun for "they" or "them." Women also tend to be referred to in sexually derogatory or trivializing ways more frequently than men.

Gender Discrimination

Gender inequality is also reinforced within the workplace. One major way this occurs is through gender discrimination. Gender discrimination is treating individuals differently specifically because of an individual's gender. In many developed countries, discrimination is illegal regardless of whether it is based on sex or gender or both sex and gender. The ways in which gender discrimination occurs tend to be subtle and complex. Gender discrimination is often difficult to prove. Gender discrimination in the workplace is the most widely discussed form of gender discrimination and will be the focus of the remainder of this entry. While gender discrimination is generally thought of in terms of female workers being discriminated against, men are also vulnerable to gender discrimination. For example, a male who wishes to become a nurse may be discriminated against because men are generally not considered nurturing and caring.

Types of Gender Discrimination

There are four major ways in which people are discriminated against in the workplace based on gender: hiring, pay and benefits, promotion, and firing.

Hiring

During the hiring process, gender discrimination can occur because of the employer's preconceived notions regarding the work ethic and style of a gender. For example, a woman may not be hired because the employer is concerned she will have or already has children and will need to take time off from work to care for them. Proving discrimination during the hiring process is extremely difficult because the sexist reasons given for or against a hire are generally not revealed in an obvious manner.

Pay and Benefits

In the United States, on average, women make 76 cents to every dollar made by men. While the exact statistic is debated and has improved in recent years, it still reflects the basic pay inequity experienced by female workers. Also, this gender gap increases substantially for women of color. Differences in pay are also difficult to prove because of the differences in skill sets and employment histories between individuals. Women may also face a "glass ceiling" in their pay level. This occurs when a women finds she is no longer able to advance in her company while her male counterparts continue to advance. Many people debate the existence of glass ceilings. Benefits are another aspect of compensation in which gender discrimination is possible. Concerns about job security due to taking maternity leave, needing to take breaks to collect breast milk while at work, and needing health insurance coverage for medically prescribed birth control are common examples.

Promotions

Women can also feel the effect of the glass ceiling in terms of promotions within the company. Women with families may be looked over for promotions because the employer believes that she will not be as committed to the position as someone without a family. As with other forms of discrimination, proving that one was overlooked for a promotion based on her gender can be very difficult.

Firing

Most gender discrimination cases tend to be regarding wrongful termination. If a person believes that she or he has been discriminated against while employed at a company, being fired from her or his position causes her or him to no longer be fearful of losing her or his job; therefore, she or he feels free to seek legal recourse.

Legal Aspects of Sex Discrimination

Discrimination based on sex is illegal in most developed nations. In the United States, the federal law Title VII of the Civil Rights Act of 1964 protects individuals from discrimination based on sex. This law makes it illegal for an employer to discriminate against individuals because of their sex in hiring, firing, and other terms and conditions of employment, such as promotions and other job opportunities. Title VII covers all private employers, state and local governments, and educational institutions that employ 15 or more individuals. Most states also have their own sex discrimination laws in place.

Concerns regarding sex discrimination have resulted in other federal laws, including the Equal Pay Act (EPA) and the Pregnancy Discrimination Act (PDA). Under the EPA, employers are prohibited from paying unequal wages to men and women who perform jobs that require substantially equal skill, effort, and responsibility, and that are performed under similar working conditions within the same establishment. The PDA amended Title VII to clarify that discrimination based on pregnancy is a form of sex discrimination. Under the law, pregnancy is considered a temporary disability. Title VII prohibits employers from treating pregnant women different from other temporarily sick, injured, or disabled employees. The Equal Employment Opportunity Commission (EEOC) enforces the federal laws regarding equal opportunity. Federal law does not currently prohibit parental status discrimination, meaning that a parent can be denied employment opportunities based solely on her or his status as a parent. However, several states have laws making it illegal to discriminate on the basis of parental status and many companies have rules against such discrimination.

In many developing nations, employees have little or no legal recourse for sex or gender discrimination.

Gender Identity Discrimination

As discussed earlier, there are some people for whom their biological sex and their chosen gender identity do not match in a socially accepted manner. The term *transgender* is generally used to describe such a person. A person whose outward appearance and self-identified gender do not match is an example of a potentially transgender person, meaning that one may have the physical markers of a female but identify oneself as a male. Currently, gender identity is not an issue protected against discrimination in federal laws. Six states—California, Minnesota, Illinois, Maine, New Mexico, and Rhode Island—have established antidiscrimination laws that make it illegal to discriminate on the basis of gender. Many cities and counties across the United States have local ordinances that make gender identity discrimination illegal. Numerous large corporations have also instituted rules against gender identity discrimination, including American Airlines, Apple Computers, JP Morgan, and Xerox. The laws in this area are under constant change.

—Amy Parziale

See also Affirmative Action; African Business Ethics; Age Discrimination; American Civil Liberties Union (ACLU); Americans with Disabilities Act of 1990 (ADA); Barriers to Entry and Exit; Benefits, Employee; Birth Control; Buddhist Ethics; Business Ethics and Health Care; Christian Ethics; Civil Rights; Comparable Worth; Comparative Advantage; Competition; Developing Countries, Business Ethics in; Disability Discrimination; Diversity in the Workplace; Employee Protection and Workplace; Employee Relations; Employment Discrimination; Empowerment; Equal Employment Opportunity; Equality; Equal Opportunity; Equal Pay Act of 1963; Ethics of Care; Family-Friendly Corporation; Feminist Ethics; Feminist Theory; Gay Rights; Glass Ceiling; Human Rights; Intergenerational Equity; International Business Ethics; Islamic Ethics; Jainist Ethics; Jewish Ethics; Just Wage; Lesbian Ethics; Maternal Ethics; Media and Violence; Minimum Wage; Minorities; National Origin Discrimination; Other-Regardingness; Paternalism; Patriarchy; Poverty; Preferential Treatment; Price Discrimination; Privacy; Racial Discrimination; Religious Discrimination; Reverse Discrimination; Right to Work; Roles and Role Morality; Self-Interest; Self-Regardingness; Sexual Harassment; Slavery; Social Ethics; Stress, Job; Taoist Ethics; Unfair Competition; Values, Personal; Violence in the Workplace; Wages for Housework; Women in the Workplace; Women's Movement; Work and Family; Work-Life Balance

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Genetic Engineering

Genetic engineering is a catchall term for the development of substantially novel living organisms and marks a breakthrough from selective breeding or conventional hybridization that has gone on without controversy for centuries. In its most common form, genetic engineering describes the direct transfer of genetic material across or within an organism's genome, which is then described as a "transgenic organism," "genetically engineered" (GE) organism, or a "genetically modified organism" (GMO). GMOs breed true, while hybrids do not; the entire germ line of the modified organisms are permanently reconfigured. Scientists and private industry embrace transgenic modification because this allows the more precise insertion of genes carrying desired traits into target organisms. Genetic engineering is used in a variety of contexts. It has been relatively uncontroversial in medical applications such as human insulin and far more controversial as an agricultural technology.

To date, commercially grown genetically engineered organisms in agriculture have been limited to a few major grain and legume crops that function as industrial inputs for the modern food system and less effort into the manipulation of animals. The first wave of crop biotechnology emphasized traits to increase the economic efficiencies of large-scale farming. The two most common traits engineered into seeds are naturally occurring insecticides and tolerance to herbicides. The second wave is poised to deliver traits desirable for consumers, such as nutritional or health benefits. The third wave will bring factories to the fields in the form of crops that produce pharmaceuticals or industrial chemicals. From one perspective, it is merely the technological improvement on conventional plant breeding. But from another vantage, it poses the threat of serious ecological and social disruption. Genetic engineering is a highly controversial practice among some producers and consumers in industrialized nations, more so in Europe and Japan than in the United States. Its proponents regard it as a panacea for the world's food and environmental problems. But its critics charge that it will maintain worrying trends in industrial agriculture.

Its Endless Promise

Before any controversy started, growers of our most basic crops—corn, soybeans, cotton, canola—adopted GMOs, and for good reasons. Monsanto's Roundup Ready soybeans, corn, and canola (rapeseed), for instance, are engineered to be tolerant to Roundup, the most popular broad-spectrum herbicide on the market. These crops are planted extensively, in blocks of thousands of acres, allowing growers to spray herbicides directly over the crop—without affecting it—to kill weeds. Roundup Ready seeds simplify weed control. However, the technology user fees that accompany the patented seeds incur additional expenses that must be weighed against purported benefits. The potential for increased herbicide usage or the evolution of herbicide resistance in weeds also figure into the logic of adoption.

Corn (maize) and cotton genetically engineered with *Bacillus thuringiensis* (Bt), a naturally occurring soil bacterium that is lethal to the larvae of lepidopteran insects (butterfly and moth family, some of the most common agricultural pests), have other advantages. Bt is not toxic to humans or other animals, with the exception of this specific order of insects. Private industry has engineered Bt into crops to reduce reliance on insecticides, and GE crop has this naturally occurring pesticide in every cell. In small, targeted amounts, Bt has proven relatively environmentally safe; it has been used by organic gardeners and farmers for years, as a natural alternative to petroleum-based, chlorine-laced pesticides. However, Bt breaks down in the sun's ultraviolet rays, and GE crops with the Bt trait have been shown to accumulate Bt in the soil beyond the sun's rays.

Across the globe, genetic engineering has been suggested as a plant breeding strategy to end one of the most severe forms of childhood malnutrition in Southeast Asia. A Swedish scientist, Ingo Potrykus, has developed a strain of rice that can produce provitamin A (from daffodils!) in the endosperm. The vitamin in the rice grain turns it yellow, so Potrykus dubbed it golden rice. It promises to end the eyesight failures and other effects of vitamin A deficiency among people who subsist mainly on rice.

In the developing world, genetic engineering may be able to help small farmers cultivate marginal lands, where water and nutrients are in short supply or conventional plant breeding techniques have proven ineffective. Perhaps scientists could engineer sweet potatoes for Africa that would resist the plague of witchweed that ruins harvest after harvest. In an era of global warming and climatic variability, conventional breeding may proceed too slowly to give us crops better adapted to heat and drought. Could we genetically engineer crops to grow in hotter and drier weather?

Meanwhile, a genetically engineered hormone, bovine somatotropin (BST), is able to increase milk production in cows; further experiments seem likely to develop a genetic modification to goats that will allow them to produce tough fibers in their milk; the research continues and is not limited to food. The future is exciting but filled with ethical dilemmas. Is it humane to genetically engineer animals with traits that affect their welfare?

Its Intractable Problems

Genetic engineering has its critics, and the points they make have to be taken seriously. In some cases, for instance, engineering only postpones problems, and biological rules will trip up this strategy. As soon as insect pests become resistant to Bt, just as they did to DDT, we will be back where we started, except that now the organic gardeners will not have any natural pesticide to fall back on. The chemical treadmill will give way to the genetic treadmill. Researchers point to preliminary evidence of the development of "superweeds" resistant to herbicides. After all, we have not trumped the laws of natural selection.

There are persistent questions about threats to human health in the consumption of GMOs, although no evidence of harm has been demonstrated. It is particularly difficult to apply the "precautionary principle," which suggests strict regulation of GMOs if there are doubts about their safety. Almost all GMOs end up as animal feed, textiles, or oils; and does the modification survive the conversion of grain into meat? The rest of it turns up unlabeled in processed food; after so much processing, is the "transgene" still present?

Beyond the possible danger to human health, there is the possibility that transgenic material may spread to native plants in the field margins. We occasionally forget that wild relatives and landraces, the origin plants of the crops we grow for food and trade, are essential reservoirs of genetic material to tap whenever new plagues or pests bedevil our crops.

Last, the possibility has been raised that GMOs may be harmful to nontarget species; it was plausibly argued, for instance, that Bt corn pollen are toxic to the larvae of monarch butterflies. A study at Cornell in 1999, currently discounted for absence of controls, demonstrated that corn with high levels of Bt expressed in the pollen was toxic to monarch larvae.

The environmental and health risks of GMOs, while widely circulated, are largely speculative. More clear and immediate are the problems of economic justice. At the global scale, agricultural germplasm had been viewed as the common heritage of humankind until just a few decades ago, but the biotechnology revolution and economic globalization are accelerating a trend away from traditional common property regimes. The development of GMOs has revolutionized the seed industry, transforming it from a series of regional commercial enterprises into highly concentrated transnational corporations, eager to sell seeds as the foundation for an integrated agrotechnological package of herbicides and seeds.

Most companies manufacturing GMOs claim to regulators that their product has "substantial equivalence" with natural seeds, but claim to patent courts that they are novel inventions among competitors. Critics insist that society's best interest cannot be pursued when private corporations control the research trajectory. The economic concentration of something so fundamental to life as seeds raises profound ethical questions of access and justice.

Widespread cultivation of GMOs bears heavily on the small farmer and especially on the poor farmer, especially in the less developed world. Many of them are the poorest people on the planet. The problem is economic scale; given the large expense of the seed, all of which is covered by the Europe- and U.S.-oriented patent regime under our current conventions on Intellectual Property Rights, only very large, and very well-capitalized, farms can use GMOs and make a profit.

In Europe, where small farms have more state support, GMOs are not widely accepted. A February 2006 ruling from the WTO found that their precautionary moratorium on the cultivation of GMOs was not based on "sound science." It remains to be seen whether this will change the amount of GMOs brought to Europe; the EU has strict labeling requirements and major European food retailers refuse to purchase GMOs.

Small farmers generally want nothing to do with GMOs because they will be put out of business by the large farms required to grow them profitably. In their resistance, they are supported by Greenpeace, the environmental nongovernmental organization (NGO), because of worries about the potential environmental effects of GMOs; European governments back up Greenpeace because they need the votes of the farmers and are tangling with a powerful environmental political presence; moral authorities weigh in on the side of maintaining the integrity of creation; and only on this point do the agendas of those diverse parties converge. Experience suggests that a more diplomatic approach on the part of the industry will be required to obtain widespread acceptance of this new technology.

Some farmers in the developing world perceive corporations from the advanced industrial organizations to be exploiting their genetic resources. In India, for example, farmers have stormed and burned facilities owned by the Monsanto Corporation. Disagreements about GMOs among member countries of the World Trade Organization, especially between the United States and small, developing countries, have contributed to blocking progress in trading regimes. Widespread use of GMOs across the world could have dire consequences for small farmers. To the extent that the cultures of many countries are built on the small farm, GMOs might cause irreparable cultural damage. To the transnational corporations that manufacture GMOs, however, these seeds merely represent scientific and economic progress.

The State of the Conflict

The future status of GMOs is uncertain and ambiguous. Investors have grown uneasy about the amount of time their capital is tied up in the development of these technologies, and they are queasy about public resistance. Despite their volatility, nonagricultural biotechnology investments have outperformed GMO-oriented companies. Original patent laws were expanded by the U.S. Supreme court to include life forms in 1980, which was a key development making the GMO economically practical. But the application of patent law to these cases must leave some people feeling somewhat odd, posing questions such as the following: Does God have some right to be concerned about these new life forms, born of the laboratory, possibly creating havoc? Few people realize that it is now legal to patent living organisms. Why was there no genuine debate about this? Religious leaders, including John Paul II, have speculated that genetic engineering may be "playing God," claiming the right, with God, to create life, insufferably arrogant and inherently wrong. Even if they were to make definitive pronouncements that this were so, civil authorities would not be likely to ban the technology itself. Because they raise genuine political, economic, environmental, ethical, and scientific questions, GMOs are likely to remain controversial, at least in some sectors of the globe.

—Keith Douglass Warner,
Lisa H. Newton, and Dustin Mulvaney

See also Agribusiness; Agriculture, Ethics of; Archer Daniels Midland; Biodiversity; Factory Farming; Intellectual Property; World Trade Organization (WTO)

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Genetic Information in the Workplace

Although genomic information is not yet widely applied in the business world, rapidly growing knowledge about the workings of our genes has the potential to give businesses fuller information about the future, as well as the current, health of the individuals with whom they deal. People's genetic condition—acquired either through inheritance or mutation—affects whether they are disposed to manifest symptoms of various kinds of illnesses. Genomics already has shown that humans are less able to control what illnesses they will suffer from than advocates of healthy lifestyles and preventative care may hope.

Genetic testing could help make what is not controllable at least more predictable for businesses. For example, information from genetic testing could enable businesses to reduce risks arising from people susceptible to certain adverse health conditions being included in their employee or customer pools. Genetic testing, therefore, could offer useful information to businesses that are affected by the health of individuals with which they deal, and genetic testing may become more common as more, and more economical, tests become available.

Ethical Issues

That such information could be used to advance organizational interests at the expense of individuals raises several crucial ethical issues, however. For example, businesses could use people's genetic information to separate individuals who carry risks of ill health from employment or to defend against victims' claims for compensation by claiming that the harm is traceable to their genes. Conversely, individuals could use knowledge of their own genetic inheritance to gain advantage over an organization, for instance, by not revealing having inherited an allele associated with the early onset of a degenerative disease to an organization that relies on the individual's remaining well. These and similar possible uses raise concrete ethical questions are about who owns such genetic information and in what circumstances it may or must be revealed, or instead must be considered confidential. Prior to these, however, there are theoretical ethical questions centering on the degree to which individuals should bear social accountability for biological outcomes they cannot control, such as health risks resulting from their having certain configurations of genes.

We cannot be fully free to take advantage of one another's bad luck. For if we were, fear of falling prey to other people when luck deserts us could deter us from productive engagement with one another. So protective constraints that regulate our interactions with one another are basic to cultivating the cooperative climate on which commerce depends. Whether such protections should extend to protecting people against the medical and social consequences of inherited bad health is a matter of conscience as well as of moral, legal, and political debate. The proposition that risk should be distributed beyond the individuals whose health is made problematic by their genetic inheritance raises related questions. Should government, employers, health care providers, or others share the risks and accept the costs?

Reducing Health-Related Business Risks

In principle, relating to individuals—whether as customers or employees—carries risks as well as benefits for businesses. Ideally, risks can be revealed, assessed, and thereby reduced. But it has been hard to know in practice what the future holds in store for particular individuals. In practice, businesses with an interest in the future good health of employees or customers have adopted two approaches to reduce their risks.

Sometimes businesses preclude involvement with individuals whose health is already compromised or who have a biological condition that increases the likelihood of their being so in future. To illustrate, employers sometimes make preemployment medical examinations a condition for being hired. The Americans with Disabilities Act (ADA) permits job-related preemployment medical examinations after an offer of employment has been made. In *Chevron USA, Inc, v. Echazabal*, the U.S. Supreme Court held that a business could withdraw an employment offer if a risk of serious illness was found, even if the individual might never become symptomatic, as long as the business would encounter hardship should the person become ill. In a similarly risk-aversive practice, health care insurers often will not cover individuals who manifest or disclose conditions that might dispose them to or are associated with illnesses.

Businesses also sometimes promote protective practice to preserve the health of individuals with whom they are involved. To illustrate, employers can require abstention from smoking as a condition of employees being retained, and health care insurers can require their service providers to encourage patients' participation in preventative care. In sum, businesses have relied most heavily on retrospective and preventative measures to reduce risks occasioned by employees or customers with poor health.

Risk Management Through Genetic Testing

Genetic testing promises to improve on both these risk-reducing strategies. The application of genetic testing in business could shift the emphasis in risk reduction to a prediction-based mode. Tests that examine genes for mutations, analyze gene products, or identify the structure of chromosomes are commonly viewed as genetic tests. There are now approximately 1,000 genetic tests. These detect many but by no means all the genetic variances that dispose people to single gene, multigene, and mutifactorial illnesses. Undoubtedly, more genetic tests will be available in the future. Subjects are usually tested directly, but tests of a subject's family members that are positive for variations or markers associated with genetic anomalies may also indicate the subject's disposition to manifest an inherited disease. Of course, the predictive value of information gained from genetic testing is affected by variances in gene expression, false positives and negatives, and by genetic recombination causing the genetic marker or markers to separate from the disease genes.

Applications of genetic testing might effect enormous risk reductions for businesses that are disadvantaged by involvement with individuals of compromised health. Conversely, some businesses, among which insurers come prominently to mind, could experience increased risk if prospective customers could weigh information about their own genetic makeup in making decisions, when that same information that is denied to the businesses with which they deal. Insurers fear the prospect of "adverse selection," where people who know their inherited risk characteristics to be great purchase insurance but where the premium charged is based on underwriting that is denied information about these characteristics, while people who know their risk characteristics to be low do not contribute premiums to the insurance pool at all. Of course, this scenario is plausible only if predictive genetic testing is sufficiently comprehensive and clear to reliably determine those who will be unusually unhealthy from those for whom insurance is unnecessary.

Presymptomatic genetic testing discovers genetic conditions that are associated with a higher than usual disposition to future illness. As is the case in families with Huntington's disease, a negative result may provide reassurance. Where prophylactic measures to delay or prevent the onset of dysfunction are available, a positive test result can lead to precautions or to treatment that staves off the symptoms of disease. Individuals identified as genetically susceptible to berylliosis can be kept from work sites where beryllium is machined, individuals identified as susceptible to early onset breast cancer can be approved for more frequent monitoring, and individuals disposed to Wilson's disease can be treated to address copper buildup.

Carrier testing identifies individuals who do not have genetic impairments but whose offspring are at risk of inheriting such genetically associated diseases as cystic fibrosis, Tay-Sachs, and sickle cell from them. Carrier testing is usually used to enable informed family planning and to help prospective parents avoid, or at least prepare for, having children whose medical conditions could affect their parents' employment status or increase costs for their parents' health care provider.

Diagnostic genetic testing confirms a suspected diagnosis or else eliminates the possibility of a genetic condition as the cause of symptoms, thereby facilitating appropriate medical intervention and deterring incorrect or unnecessary treatment. Once identified as possessing one of the mutations associated with cystic fibrosis, for instance, patients receive the specialized antibiotic and pulmonary treatments that can preserve their functionality and prolong their lives.

Risk Management Through Personal Information

Even without genetic testing, some businesses have used predictive information to reduce risks. For example, some businesses have required applicants to divulge any family history of Huntington's disease. Huntington's disease is a degenerative neurological disease with symptoms that usually onset in early or late middle age. It is associated with the presence of a single allele and has the rare property of 100% penetrance. Penetrance is the proportion of individuals of a particular genotype that express its phenotypical effect. Individuals with the genetic configuration associated with Huntington's disease invariably develop the symptoms.

A person whose parent has manifested Huntington's symptoms has a 50% chance of developing the disease, and a person whose grandparent did so has a 25% chance. Such a family history has been enough to disqualify applicants in the United Kingdom from obtaining mortgages needed to purchase homes and to disqualify applicants in the United States from obtaining disability insurance (although in the latter case insurers sometimes simply have excluded work disability arising from Huntington's disease from coverage or else raised the price of insurance to reflect the applicant's odds of developing the disease). Now, however, a genetic test can reveal whether an individual has inherited the Huntington's allele and, therefore, can free those who have not from being penalized by suspicion. Nevertheless, very few disease-related alleles share the highly deterministic 100% penetrance of Huntington's disease.

Genetic Discrimination

Most disease-related alleles constitute a much less reliable basis for supposing that individuals who test positive for them will become symptomatic. The history of the association of the alleles BRCA1 and BRCA2 with the onset of breast cancer is illustrative. When the link between these mutations and the disease was first made, the rate of disease manifestation in women who tested positive was thought to be about 90%. In addition to the fear of developing cancer, women in this group also experienced threats of loss of employment and of health insurance.

The data available at that time were drawn from initial studies that had discovered that women with certain histories of cancer very often also had one or the other of these variants of the gene. Concerned about having to bear the costs of this illness, employers and insurers considered testing young women of the highest risk European heritages. In response, legislatures in states where ethnic groups with such medical history had political influence imposed bans on basing negative employment or insurance decisions on medical information about BRCA1 and BRCA2. Subsequently, studies of asymptomatic subjects with these genetic variations have shown the incidence of breast cancer to be less than 50%, although the risk is still higher for this group than for species typical cohorts.

Public Concerns

The story of legislation developed to protect individuals with certain kinds of genetic configurations is not unique to breast cancer. The earliest state prohibition against disadvantaging individuals because of an inheritable trait was Georgia's ban on the use of information about sickle trait for such purposes. Sickle trait is not deterministically predictive of severe symptoms. Some individuals who inherit the trait from both parents develop anemia, impaired immune systems, organ damage, stroke, vision problems, reproductive difficulties, episodic profound pain, and delayed growth, while others never experience more than mild symptoms or are virtually symptom free. Both physical and social environments appear to influence the severity of symptoms but the mechanisms that differentiate cases are not fully known.

In this case, as in the case of genetically heightened risk of breast cancer, concerns about the ethical and political propriety of disadvantaging individuals with a greater than species-typical disposition to illness are particularly acute. Breast cancer patients are usually women (although males with breast cancer are not unknown). Approximately 1 in every 500 African American babies is diagnosed with sickle cell anemia. Impelled by these groups' histories of unfairly truncated opportunity, current U.S. law requires at least heightened scrutiny of practices that subject these groups to special disadvantage. In a culture that has stigmatized these groups as being defective competitors and contributors, is it fair to penalize a subcategory of the group for biological anomalies even though most individuals in the category will never become symptomatic?

Business Applications of Genetic Testing

In general, businesses might apply genetic testing to screen out prospective or current employees whose genetic dispositions invite illnesses in themselves or in family members that could reduce the worker's productivity and/or increase the employer's health care insurance costs. Individuals believed likely to take sick leave, resign, or retire early for health reasons, file workers' compensation claims, or be eligible for expensive health care benefits could encounter special difficulty in finding or remaining at work. Such screening could have a disproportionate impact on members of historically stigmatized or disadvantaged groups.

Businesses might also screen out prospective employees with a higher than typical risk of being made ill by worksite conditions or deny compensation for work-related illnesses and injuries by proposing that the harm would not have occurred but for the worker's own anomalous genetic state. Insurance providers might screen out, curtail coverage, or charge higher rates to higher risk customers. And businesses might defend against charges of harmful negligence by arguing that damaged individuals were genetically more likely to be injured than the ordinary population reasonably is expected to be.

Informed Consent and Autonomy

To adopt such practices, businesses must have access to medical information about the individuals with whom they are involved. Two basic and closely related ethical values are relevant here. People own their own bodies, and they should be free to make autonomous decisions about what medical tests and treatment they receive. Businesses must obtain informed free consent if they want to do genetic testing.

To illustrate, in 2002 the Burlington Northern and Santa Fe Railway Company settled a complaint about genetic testing filed with the U.S. Equal Employment Opportunity Commission (EEOC) for more than $2 million with 36 employees who were required to provide blood samples after reporting work-related carpal tunnel injuries. Associating a genetic anomaly with carpal tunnel syndrome, the company proposed to defend against worker compensation claims by describing the injured workers as genetically disposed to injury from tasks harmless to other people. The EEOC intervened, citing the company's coercion of employees in obtaining the samples and its failure to disclose the intention to submit the samples to genetic testing without specific consent from the sample donors.

Legal Protection

The Americans with Disabilities Act

The Burlington Northern workers pursued their complaint under the Americans with Disabilities Act of 1990, claiming their employer mistakenly regarded them as having disabilities and on that basis subjected them to medical testing not imposed on other employees. In the context of this case, the EEOC made a general determination that entities that discriminate on the basis of genetic predisposition are regarding the individuals as having impairments, and such individuals are covered by the ADA. But unaffected carriers of recessive and X-linked disorders, and individuals with late-onset genetic disorders who may be identified through genetic testing or family history as being at high risk of developing the disease, would not be protected under this standard unless they are treated as already having disabilities. Furthermore, whether the EEOC determination in the Burlington Northern case extrapolates to other cases, or whether courts ultimately will find that the ADA protects against genetic discrimination in any sense at all, remains unclear.

Other Federal Protection

An executive order issued during the Clinton administration protects federal workers against coerced genetic testing, imposes strict privacy, and bans depriving federal employees of assignment or advancement opportunities because of a genetic predisposition for certain illnesses. The third main federal protection against genetic discrimination is found in the privacy and antidiscrimination provisions of the Health Insurance Portability and Accountability Act of 1996 (HIPPA), which limits exclusions for preexisting conditions and prohibits discrimination in covered plans against individuals based on health status, including their genetic information. While HIPPA extends coverage to people who have genes that predispose them to a disability or disease, or who have genes for a late onset disorder, it may not protect carriers of genetic disorders who do not yet manifest symptoms. More than 30 U.S. states have statutes pertaining to genetic discrimination, almost all states limit employer access to genetic information about employees, and most states have enacted higher standards of privacy for genetic than for other health-related information.

Acceptable and Problematic Uses of Genetic Information

Almost all statutes that regulate business uses of genetic information enable employers to access genetic information in the service of workplace safety. Indeed, employers may have a positive ethical obligation to do regular genetic testing for the purpose of monitoring the genetic normality of employees exposed to mutagens. Furthermore, employers have at least a moral duty to warn employees about environments that can injure genetically susceptible individuals, and their duty might extend to paying for employees' testing. Under the ADA, employers may deny work to at-risk individuals, because this law does not prohibit adverse employment action if a person's biological anomaly makes a work environment dangerous for that person.

Nor does the ADA prohibit banning anomalous persons if their presence in the workplace is dangerous to other people. The question becomes more difficult when the choice is between denying genetically anomalous individuals equal employment opportunity or eliminating the possibility of future harm that anomalous individuals might visit on others in case they become unable to execute a job's essential tasks. To illustrate, existing genetic tests can identify some individuals who are at risk of the early onset of Alzheimer's disease, but their predictive reliability is not established. Workers such as air traffic controllers, whose assignments demand accurate perceptual judgment, might endanger the public if they continued working after Alzheimer's symptoms set in. There is an ethical problem about what degree of threat would justify overriding autonomy and privacy to mandate nondispositive genetic testing for such workers.

Even if regulations sequestering genetic information are strengthened, complete privacy may prove impossible to guarantee. Clues to a person's genetic inheritance are to be found in family members' records as well as the person's own. And unless genetic testing becomes routine, the very fact of having been tested could stigmatize the patient.

If businesses subscribe to genetic discrimination, genetic test results could make some individuals uninsurable or unemployable, regardless of whether they ever manifest symptoms of inherited disease. Fear that genetic information might be used against them could induce people to forego the health benefits that better understanding of their genetic dispositions can bring and consequently could reduce the pharmaceutical industry's potential for bringing about a healthier population. Widespread discrimination based on genetic information could lead to the formation of a genetic underclass in a society where hard work and talent are less deserving of opportunity than the random luck of inherited genes. Such eventualities are unlikely to serve either civic or commercial interests and so are problematic for a fair and productive society.

—Anita Silvers

See also Adverse Selection; Age Discrimination; Americans with Disabilities Act of 1990 (ADA); Bioethics; Business Ethics and Health Care; Genetics and Ethics; Health Insurance Portability and Accountability Act; Human Genome Project

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Genetics and Ethics

Genetics is the study of heredity. The basic unit of heredity is the *gene*, which passes traits from one generation to another. Genes are sequences of DNA (deoxyribonucleic acid) located in *chromosomes* (of which humans have 23 pairs). The total DNA in an organism is called the *genome.* The genes that are part of the genome make up the *genotype.* The expression of the genotype in the physical characteristics and functions of an organism is known as the *phenotype.*

A number of technologies have been developed in the course of genetics research. *Recombinant DNA technology* involves splicing a gene from one source into another. Using a genetically modified virus as a vector, which introduces a gene into a cell, often does this. This technology is used in agricultural technology involving genetic alternations in plants and animals, and in *gene therapy*, in which normal DNA replaces defective DNA to treat genetic diseases. Both nonhuman and human genetic technology have raised a host of ethical issues, including issues surrounding genetic modification of plants and animals, human genetic engineering and gene therapy, genetic testing, and cloning.

Genetically Modified Crops

There has been considerable controversy over the use in agriculture of crops whose genetic code has been modified. *Transgenic crops* are those developed when a gene from another species has been inserted into a plant such as corn or tobacco. The gene could come from another plant, an animal, or a bacterium. Plants resistant to drought and disease (such as plant viruses), plants with an ability to produce their own pesticides, and plants with a higher crop yield have been developed. Companies that make these products argue that they both increase crop yields and decrease crop loss from drought, disease, and insects. In a difficult agricultural market, genetically modified crops can help make farming more economically viable. But more important, higher crop yields can increase the world's food supply, especially in developing countries. Agribusiness companies also argue that genetic modification of crops is only an extension of what farmers have been doing with selective breeding for centuries and that such crops are as safe as their non-genetically engineered counterparts.

Opponents of genetically modified crops (which many label as *frankenfoods*) argue that agribusiness companies have put profit first, ignoring potential safety concerns. They argue against inserting of genes from different species into crops, claiming that this practice is not safe. If someone is allergic to particular plant products such as peanuts and peanut genes are inserted into another crop such as corn, then eating that corn might cause an allergic reaction. Another potential problem is that pest-resistant crops may lead to "super pests," which are pesticide resistant. In the case of disease-resistant crops, new varieties of viruses could develop, which are even more destructive of crops. A 1999 study of Bt corn (corn with a gene from a bacterium that causes the corn to produce an insecticide) involved monarch butterfly caterpillars eating milkweed leaves dusted with pollen from Bt corn. Half the caterpillars died. This fueled opponents of transgenic crops, who also pointed out that it may be difficult to localize such crops within a particular area—Bt corn pollen, for example, might spread to other corn. Proponents replied that most transgenic corn did not use the gene correlated with caterpillar deaths. Opponents said that more testing should be done before transgenic crops are placed on the market, since we do not know all the effects genetic modification may have on the plant—there may be health hazards (such as carcinogens) created, which may not be detected for a long time. Pressure was also put on the Food and Drug Administration to require labeling of genetically modified foods.

Another concern is the potential loss of biodiversity due to the increasing cultivation of monoculture crops (in which only one variety of a crop, for example, corn or wheat, is grown on a farm). There is concern that growing only one variety of crop will deplete the soil of key nutrients as well as reduce the diversity of plants needed for a healthy environment. These critics argue that traditional methods of farming in developing nations, in which several varieties of crop are grown, preserve such biodiversity. In addition, if only one genetically engineered variety of a particular crop, such as corn, is grown, it will not have the necessary genetic diversity to respond to any new environmental challenges. Opponents also claim that biotechnology firms have pressured governments and farmers to become dependent on genetically modified crops, which have not only harmed the environment, but have hurt farmers economically because of their dependence on one cash crop. Biotechnology firms reply that their crops help reduce starvation in developing nations due to high yields and fewer problems with pests.

Genetically Modified Animals

Animals used in agriculture may have their genetic code modified to make them more disease resistant or to make the meat more tender or favorable. Similar issues arise as those stemming from the discussion of genetically modified crops. Transgenic animals have also been used in medical research, particularly in transplantation research. Human genes have been inserted into pigs; the hope is that this will allow pig organs, which are similar in size to human organs, to be transplanted into human beings without being destroyed by hyperrejection. The hope is that the extent of the organ recipient's rejection reaction will not go beyond the reaction of patients receiving human organs. The advantage is that pigs are plentiful, and if pig organs could be transplanted into humans, the shortage of human organs could be wiped out.

Most opponents of pig to human transplantation are not as concerned with human genes being injected into pigs as the danger of potentially dangerous pig viruses being transferred to recipients of pig organs. The concern is that viruses that have little effect on pigs could cause sickness or death in human beings. Although defenders of research on pig organ transplantation say the risk is minimal, concerns about viral transmission have slowed research in the field. Another concern of opponents is that of proponents of animal rights, who believe that killing pigs for organs is unwarranted exploitation and unjustified killing of a sentient creature.

Human Genetic Engineering

The same techniques used to modify the genetic code of organisms from bacteria to dogs can also be used on human beings. Recombinant DNA technology can be used to transfer DNA into human genes. The DNA could come from another human being or from a member of another species. In gene therapy, a normal gene is injected into a cell, and if all goes well and it expresses itself by making a protein, a genetic disease could be permanently corrected. If gene therapy is focused on the individual person's organs and tissues to correct a genetic disease for that individual alone, this is *somatic gene therapy.* If the target is one of the germ cells (egg or sperm) so that the results of gene therapy are passed on to the offspring of the affected person, this is *germ line gene therapy.* Both forms of gene therapy raise moral issues.

Ethical Problems in Somatic Gene Therapy

Somatic gene therapy, if successful, could cure an individual of a genetic disease such as cystic fibrosis. Although this is a worthy goal, there are problems with somatic gene therapy. There are technical problems with accurately inserting a gene into the right location. With today's technology, the final location to which the gene attaches cannot be precisely pinpointed. Not only is there a risk that such inaccuracy will not eliminate the disease, with interaction between genes important to the expression of phenotype, there could be unintended negative effects on the body. This raises the issue of whether human subjects research with gene therapy is safe enough to move forward at this time. The 1999 death of an 18-year-old patient in a gene therapy trial has exacerbated such concerns. Critics of research in gene therapy believe that it should be banned until technical and safety problems have been resolved. Such a ban has been in place since January 2003 in the United States due to Food and Drug Administration concerns about patient complication in a French gene therapy project. When such research is approved, subjects should be informed of the risks in order to give adequate informed consent.

Another concern is the safety of the vector (usually a virus) used to introduce the gene into the cell. Has the virus been sufficiently deactivated so that there is virtually no risk of disease? The subject could also have an allergic reaction to the vector.

There are also business ethics issues, one of which is related to the fact that most gene therapy research focuses on treating malignant diseases (cancers) rather than single-gene disorders. This is due to the larger market of cancer patients, and a larger market means a larger profit. But, some argue, gene therapy would be most effective in treating monogenetic disorders such as Huntington's disease, which results in its victims suffering irreversible progressive brain damage, usually beginning in their 30s or 40s. The issue is one of whether it is fair that the large market diseases are the focus of almost all gene therapy.

Germ Line Gene Therapy: Additional Ethical Issues

In addition to the previous concerns, germ line therapy muddies the moral waters with concerns about genetic changes that are passed on to an individual's offspring. The advantage is that it may be possible to totally eliminate a genetic disease (cystic fibrosis, Huntington's disease) from the human germ line. Some writers have also argued that human capacities might be improved and these improvements passed on through the germ line.

On the other side of the issue, given present technological limitations on the accuracy of gene targets, there is considerable risk that negative traits could result that will be passed on to offspring. Since phenotypic traits are due more to the interaction of genes than one specific gene, concerns have been expressed about how the inserted gene will interact with other genes and which phenotypic traits would result. Critics of germ line therapy also note that the same gene that causes sickle-cell anemia also causes the body to protect itself against malaria. If that gene is wiped out of the human genome, and a major malaria outbreak occurs, will people regret that a protective trait has disappeared for good?

Genetic Testing

Sophisticated tests are being developed that reveal with high accuracy whether a person has a genetic disease or whether a person has a greater risk for cancer or heart disease. With the success of the Human Genome Project in mapping the genes in the human body, more tests for more conditions will be developed. Some tests may be given to embryos used in in vitro fertilization before they are implanted; others may test the fetus in the womb. If a test for, say, cystic fibrosis were positive, a prospective parent might decide to abort the fetus. If a preimplantation embryo were to test positive, it might be discarded. At this point, the debate over abortion intersects genetic testing. Those who believe that the embryo or fetus is a human person oppose abortion and the destruction of the embryo, even if it has a genetic disease. Those who deny such personhood may believe that the embryo and fetus deserve some respect but not to the point that these entities have the moral right not to be killed. They also argue on utilitarian grounds that a parent should not be required to bring a child into the world that will suffer greatly and create a significant burden for the parents. Defenders of the rights of people with disabilities, who may not oppose abortion, in general, have argued that abortion of those with genetic diseases contributes to negative attitudes toward the sick and individuals with disabilities in society.

Issues also arise concerning genetic profiling. If an employer knows an individual's genetic profile showing either that the person has a genetic disease (such as Huntington's disease) or a high probability of heart disease, then the employer may either refuse to hire the individual or, if the individual is already an employee, lay the person off. Insurance companies may also deny an individual coverage based on the person's genetic profile. Opponents of such profiling by employers and insurance companies consider it to be discrimination. Laws have been passed in several states protecting the privacy of genetic information, though critics say that an employer or insurance company can find loopholes in the laws. On the other side, insurance companies, in particular, have argued that the increased risk of disease of those with high-risk profiles justifies their denying or charging more for insuring them.

Cloning

A *clone* is a cell or an organism genetically identical to another organism; examples include two bacteria that result from the division of one bacterium and human identical twins. Artificial cloning involves a variety of methods, many of which involve cloning embryos or cells derived from embryos. But the most famous clone, "Dolly the sheep," was created in 1996 using a mammary gland cell from an adult sheep. The genetic material was removed from an egg cell, the material from the mammary gland cell inserted. This material was then reprogrammed to divide and form an embryo, which was inserted into the mother. Dolly was the first mammal cloned from an adult somatic (bodily) cell.

Artificial cloning could be used in agriculture, for example, to clone high-yield milk-producing dairy cows. Proponents of such cloning argue that cloning superior animals can increase agricultural production; opponents argue that reducing the diversity of the gene pool may result in animals more vulnerable to disease. Cats have also been cloned, and pet cloning may become an industry in itself.

It is human cloning that fuels the most intense debate. Although there is little opposition to cloning individual human cells, tissues, or organs, cloning the human being as a whole is much more controversial. Human embryos have been cloned to harvest embryonic stem cells (cells that can divide to form any type of bodily cell), and in theory a cloned embryo could be implanted in a mother who gives birth to a clone. Cloning to harvest embryonic stem cells is controversial because the embryo is destroyed in the process, and those who believe the embryo is a person believe that such destruction is unjustified killing. Proponents deny that the embryo is a person.

Advocates of cloning to produce a complete human being have claimed a variety of reasons a person would want someone cloned. These include parents cloning a dead child or infertile couples cloning a child genetically related to one of the parents. Defenders of cloning for such reasons often appeal to personal autonomy and reproductive rights. They argue that these rights should be respected, even in a case in which a parent wishes to clone a dead child, not realizing that the child born would be a younger identical twin of the dead child, with its own individual personality. Opponents argue against cloning for a number of reasons. First, they argue that human cloning amounts to unauthorized experimentation on human subjects who cannot give permission for research. In addition, they point out safety concerns; more than 90% of cloning attempts fail, and cloned animals often have severe deformities such as organs too large for their bodies. Human clones may suffer similar deformities. Other criticisms include a concern about cloning involving humans becoming manufactured objects, leading to the devaluation of human reproduction and human life. Controversy over cloning has led to attempts to ban human cloning in the United States and elsewhere. But proponents of cloning argue that opponents do not distinguish mainstream cloning research, involving cloning human tissues, organs, and embryos for uses such as harvesting stem cells, and extreme research involving the implantation of a human embryo into a woman so that she could give birth to a clone.

—Michael Potts

See also Agribusiness; Genetic Engineering; Human Genome Project; Informed Consent; Stem Cell Research

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George, Henry (1839–1897)

At one time, the third most famous American (after Thomas Edison and Mark Twain), George was an influential practical philosopher, social critic, and reform proponent of the "single tax" during the progressive error. Despite George's limited education, he was praised for his logic and originality by many prominent intellectuals ranging from Leo Tolstoy to John Dewey.

In his book *Progress and Poverty* (first published in 1879), George asserted that the ownership of property created poverty by only enriching the owner at the expense of the community. In essence, George believed that land and its wealth belong to all. In this he was akin to the 18th-century physiocrats and their *impôt unique*, as well as philosophers such as James Mill, John Stuart Mill, and David Ricardo.

As a political economist, George argued that "economic rent" on land going to its owners served to create resource inequity (through commerce on urban properties, through agriculture on farm lands, and the value of natural materials extracted from mineral leases, minus the cost of property improvements that increase land's value).

To rectify misdistribution, George said that governments at every level should abolish all taxes except those on beneficiaries of economic rent. Because land is a fixed resource, the income it yields is a product of the economy's growth and not individual effort. The remedy was to impose a "single tax" on the unimproved value of that land if it remained in its natural state without buildings or other improvements. George believed that the government's annual income from this single tax would be fair and prove so significant that resulting surpluses could underwrite necessary beneficial public works. On the other hand, opponents have argued that there is no correlation between land ownership and total income or wealth. Furthermore, they protest that the lack of graduation under a single tax system fails to take into account an individual's ability to pay.

George's first book sold in the millions and appeared overseas in numerous translations. In 1880, he moved to New York to continue writing and lecturing. His popularity grew and this encouraged George to try to put his ideas into practice. He challenged the "politics as usual" system in a reform platform campaign for mayor of New York in 1886. Although George outpolled Theodore Roosevelt in a three-person race, he narrowly lost to the Tammany Hall–endorsed Democrat. Later, he again campaigned for the office, but died before the election.

Ethics form a central focus of *Progress and Poverty* and George's subsequent books, especially on the dominant question of right and wrong. For George, each person's labor belongs to himself or herself and should be free of arbitrary government taking. George, thus, sees a natural right or justification for private property in products created by one's own hands. On the other hand, land is not produced by man and is to be held in common. The value of land exists only as the community exists. It grows as the community expands and decreases as the population declines. Thus, unfettered private property in land, according to George, is unjust because it allows landowners to erect a toll for its use (a form of robbery) or even refuse all access to property (thereby injuring one's livelihood and threatening life itself).

The single tax plan actually gained considerable support in subsequent decades but was never fully implemented. Nevertheless, a number of single tax mayors and legislators have been elected to office, and the continuing interest in his ideas has influenced tax legislation in some U.S. states, as well as across the globe in western Canada, Australia, Britain, and Western Europe. Interestingly, the origin of the popular board game "Monopoly" has been traced to Henry George's followers by the Public Television program *History Detectives.*

Even today, for George's adherents the single tax is not merely a proposed fiscal reform. Rather, they argue that it remains a basic necessity if human progress is to occur, because without fundamental realignment in wealth and ownership no other meaningful social restructuring will prove lasting.

—Richard Alan Nelson

See also Absolutism, Ethical; Accountability; Agriculture, Ethics of; Authority; Capitalism; Ethics of Dialogue; Fairness; Freedom and Liberty; Free Trade, Free Trade Agreements, Free Trade Zones; Income Distribution; Industrial Policy; Labor Unions; Land Ethic; Liberalism; Libertarianism; Loyalty; Mill, John Stuart; Morality, Public and Private; Moral Principle; Political Economy; Poverty; Property and Property Rights; Public Interest; Social Costs; Social Ethics; Socialism; Speculation and Speculator; Surplus, Consumer and Producer; Sweatshops; Tariffs and Quotas; Tragedy of the Commons; Utilitarianism; Utility; Utility, Principle of; Wealth; Wealth Creation

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Glass Ceiling

The term *glass ceiling* was first used by Carol Hymowitz and Timothy Schellhardt in their 1986 *Wall Street Journal* article to describe the invisible barriers that keep women from upper management positions in American corporations. It has also been used to refer to the exclusion of racial and ethnic minorities from upper management, both women and men. The glass ceiling phenomenon was studied extensively during the 1990s and, although Carly Fiorina denied its existence when she was appointed CEO of Hewlett Packard in 1999, there is evidence that it still exists. There are currently many more women in upper management and executive positions, but parity has certainly not been reached, particularly in the highest positions.

Exclusion of women and racial and ethnic minorities from the possibility of promotion to senior management positions in business has a long history. In the United States, the problem of entry-level positions was aided by the passage of the Civil Rights Act of 1964, Title VIII, and later, the Equal Opportunity Act of 1972. In 1968, women were not even accepted in management training programs, thus preventing them from beginning their climb up the corporate ladder. During the 1980s, women began to obtain college degrees in business administration and continue on for their MBAs. By 1990, however, there were still only three women CEOs in Fortune 1000 companies: Katherine Graham, Linda Wachner, and Marion Sandler. That year, 97% of all senior managers were male, although progressively more women and minorities filled entry level and middle management positions.

In 1991, President George H. W. Bush appointed the Glass Ceiling Commission to study and prepare recommendations for eliminating the glass ceiling. The 21-member commission was chaired by Robert Reich, the secretary of labor, and consisted of 16 women, 3 of whom were senators, and 5 men. Many members were minorities. The commission defined the glass ceiling as the unseen, yet unbreachable, barrier that keeps minorities from rising to the upper rungs of the corporate ladder, regardless of their qualifications or achievement. They issued two reports in 1995: *Good for Business: Making Full Use of the Nation's Capital: The Environmental Scan: A Fact-Finding Report of the Federal Class Ceiling Commission* and *A Solid Investment: Making Full Use of the Nation's Capital: Recommendations of the Federal Glass Ceiling Commission.* After soliciting research from a number of organizations, their findings showed that the glass ceiling did indeed exist and that it excluded women and minorities from leadership positions. The commission was also convinced that this exclusion was not good for business and that there was a need to address the issues.

The findings reported three sets of barriers to true parity. Societal barriers were caused by stereotypes and prejudice, while structural barriers were perceived as the corporations' failure to recruit women and minorities and a hostile corporate culture. Governmental barriers included inadequate monitoring of cases as well as inadequate law enforcement. Various explanations have been forwarded for the existence of the glass ceiling. Corporations have traditionally blamed a woman's lack of experience, low motivation to succeed, having not enough or the wrong kind of education, and a lack of training. They also suggest that a woman has less interest in promotion due to a focus on family and household responsibilities. Other explanations focus on built-in organizational structure: bias in selection and promotion decisions, gender-typed jobs leading to lower expectations of the employee, a lack of developmental opportunities, few available mentors, problems with work-life balance, and lower compensation for the same job a male is performing.

The second report, *A Solid Investment*, detailed recommendations for alleviating the problem, one set aimed at corporations and another set for the government. Corporations were urged to demonstrate visible commitment to diversity from the board of directors and the CEO down through all management levels. It was also suggested that diversity be included in the strategic plan, that line managers be held accountable for diversity initiatives, and that affirmative action be used as a tool to ensure equal access and opportunity to compete. Imagination was suggested in the recruitment process through seeking out candidates from unusual backgrounds and experiences. And, once hired, minorities and women needed to have access to developmental experiences, mentoring, and career guidance in preparation for senior positions. Changing the corporate culture was addressed through sensitivity training and workplace practices emphasizing participation and partnership. The commission also suggested work/life and family friendly benefits and practices. The federal government was urged to lead by example and increase all efforts to erase the glass ceiling. Other recommendations focused on strengthening enforcement of and updating antidiscrimination laws, improving the complaint process, and deepening data collection.

By 2005, 10 years after the publication of the Glass Ceiling Commission reports, progress remains very slow. Catalyst, a consulting organization that takes a biennial census of women CEOs, suggested that it would take 40 years at the present rate to achieve parity with men in senior leadership positions in large corporations in the United States. In their 2005 census, findings showed that, while both men and women aspire to top positions and use the same strategies for business success, the numbers did not reflect equality of position. Only 16.4% of the corporate officers in Fortune 500 companies were women and 1.7% were women of color. Only 6.4% of the top earner positions were held by women, and more than half of the Fortune companies had fewer than three female corporate officers. In 2006, with the appointment of Indra Nooyi as the CEO of Pepsico, there were 11 women leading Fortune companies.

The glass ceiling is not unique to the United States. While there are a few women leading corporations in other countries, they stand out because there are so few. Despite all the research and recommendations, and all the women and minorities in middle management, progress has been very slow and it will take many years to attain true equality in promotional decisions between men and women in management, particularly at the senior management levels.

—Carol H. Krismann

See also Barriers to Entry and Exit; Civil Rights; Diversity in the Workplace; Employment Discrimination; Gender Inequality and Discrimination; Women in the Workplace

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Global Business Citizenship

Global business citizenship (GBC) is an emerging theoretical framework that extends the concept of corporate social responsibility into a globalized environment. It is an alternative to prevailing frameworks in finance and economics in that it accepts the validity of stakeholder claims on firms. The GBC framework offers a process that multinational managers can use to consistently implement social responsibility and ethics within and across nations and cultures.

Concept History

The GBC framework was developed to address several problems with predecessor concepts and to offer an alternative to views of the firm as merely a nexus of contracts or a tool of capital owners' interests. GBC's principal conceptual ancestor is corporate social responsibility (CSR), the obligation of corporations to use their power wisely and to respond to societal needs. Developed in the United States from the 1960s onward, CSR was built on an assumed moral base that was never adequately articulated. The dimensions and processes of CSR were never well-defined, so businesses had little guidance in identifying or exercising social responsibilities. Furthermore, CSR was typically defined in terms of a business's responsiveness to social demands, or responsibility to particular societies, with little attention paid to a company's own core values or to real cultural differences in ethics.

GBC is also a conceptual replacement for corporate citizenship (CC). Although some scholars have attempted to define corporate citizenship as a broad-based enactment of a business organization's social and ethical obligations, the term is much more commonly used to narrowly indicate firms' voluntary participation in philanthropy and community affairs.

GBC does not view the firm as consisting solely of contracts or as a single-purpose tool for shareholder value. The GBC concept is counterposed to these perspectives in several ways: (1) GBC accepts the view from traditional organization theory that firms are entities, not fictions; (2) GBC recognizes a broad range of relationships, rights, and duties between a firm and its stakeholders; and (3) GBC requires an explicit, principled, comprehensive moral foundation for firm policies and practices.

Businesses as Citizens

Citizenship ordinarily defines the relationship of persons and political units. Citizenship typically involves certain protections based on rights guaranteed by the polity's legal infrastructure, often including rights to liberty and rights to protection and welfare. Citizens may also have duties; Aristotle's observation that citizens participate in taxation, governance, and defense is still largely true in modern democracies.

On three counts, nation-state citizenship for persons does not provide an adequate metaphor for companies: Can businesses be citizens in the same way that persons are? If so, what is the polity of which businesses are "global" citizens? Finally, what kinds of citizens can businesses be? GBC, thus, requires attention to and expansion of the citizenship metaphor.

First, there is considerable debate over the question of whether organizations can be citizens as humans are. The issues concern who should have what rights and duties, how organizations should participate in government, and whether businesses should be thought of as citizens in any manner, given the presumed special moral standing of human beings and the overwhelming power and influence of large organizations. The GBC framework does not assume that businesses are equal to humans in moral status or that businesses should be accorded equivalent rights. Instead, businesses are thought of as secondary citizens—a convenient status for accomplishing certain human goals.

Second, in the absence of world government, to what polity do firms owe allegiance as citizens? Globalization has made nation-states increasingly irrelevant to economic activity, so older notions of firm allegiance to the "home" country no longer offer a basis for a business citizenship metaphor. To answer the question, the GBC framework relies on the idea of universal citizenship, as in the works of Rousseau and other "natural law" thinkers. To be a "citizen of the world" means to hold allegiance to the human race rather than to any particular subgroup. "Global citizen" reflects a perspective, not a legal status.

With respect to the third question, political theory—a branch of philosophy that attempts in part to answer the question, "How can we live well together?"—can be used to categorize the ways in which businesses can be citizens.

Minimalist theories, such as libertarianism, public choice theory, and agency theory, view the firm as a nexus of contracts with no independent substance and no loyalties other than those specified in its contracts. In this view, the firm can be a citizen only in the minimal sense of being law-abiding; it has no justification for considering the common good or the interests of noncontract holders, and its executives are not likely to see it as a citizen. Minimalist firms may indeed behave ethically within and beyond the demands of law, but their guiding perspective does not require that they do so.

Communitarian theories, with a focus on boundary maintenance and group identity, view the firm as an important player in the local environment, and so the firm can be a "corporate citizen" in the usual sense of a business that voluntarily "gives back" to local communities. Communitarian firms are likely to abide by the ethical principles governing their communities of allegiance, and they may or may not apply those principles when dealing with "outsiders."

Universalist theories, whether deontological or teleological, emphasize the rational consideration of others' interests as well as the interests of the whole, in addition to self-interest. In these views, firms accept responsibilities to a broader range of stakeholders as well as a general responsibility to act in ways that are consistent with universal ethical principles and that advance, or at least do not harm, human well-being.

Only from the lens of universalist political theories can firms be viewed as global business citizens. This does not imply that other lenses produce unethical, irresponsible firms. A minimalist firm may be law-abiding and ethical, but its focus is on generating wealth for capital owners and it will not hold an image of itself as a citizen. A communitarian firm is likely to be law-abiding and ethical at home, but may not extend these behaviors elsewhere. A universalist firm will attempt to consistently and responsibly exercise its rights and implement its duties to individuals, stakeholders, and societies within and across national and cultural borders.

The Global Business Citizenship Framework

The GBC framework is developed by considering relationships between a company's choices of global *strategy* and the degree of *ethical certainty* with respect to particular issues and environments. The framework is shown in Table 1 and explained below.

Table 1 The Process of Implementing Global Business Citizenship: Ethical Certainty and Strategic Approaches

Degree of Ethical Certainty	*Multidomestic Strategy*	*Globally Integrated Strategy*
High certainty: Principles—a limited number of basic, universal ethical rules	(Ethical relativism)	Step 1: Code of conduct
Moderate certainty: Consistent norms—variations in practice consistent with principles	Step 2: Local implementation	(Ethical imperialism)
Low certainty: Incompatible norms—variations in practice inconsistent or in conflict with principles	Step 3: Problem analysis and experimentation	Step 4: Organizational and systemic learning

Source: Adapted from Wood, D. J., Logsdon, J. M., Lewellyn, P. G., & Davenport, K. (2006). *Global business citizenship: A transformative framework for ethics and sustainable capitalism.* Armonk, NY: M. E. Sharpe.

The Strategy Dimension

In international business, companies use a multidomestic strategy that tailors its operations to local conditions, or a globally integrated strategy that strives to achieve a unified approach across all units, or a hybrid model combining elements of the two.

The Ethical Certainty Dimension

The GBC framework acknowledges varying degrees of ethical certainty about what is right. A GBC firm has high certainty about its principles, such as, "It is wrong to harm innocent persons." However, there are situations where local custom demands variations in implementing principles without violating them. And there are situations where local norms are in conflict with principles, application of the principles will cause unintended negative consequences, or where local managers cannot tell whether local customs conform to or conflict with company norms. In such cases, the degree of ethical certainty is much lower.

GBC'S Hybrid Approach

Table 1 shows the nature of the hybrid approach that best allows companies to consistently and responsibly exercise rights and implement duties within and across national and cultural borders. Two cells are eliminated from the model and the remaining four cells form a process for implementing GBC.

The two eliminated cells are ethical relativism and ethical imperialism. First, a multidomestic strategic approach cannot be applied by GBC companies in situations of high ethical certainty, because once one accepts universal ethical principles, they must by definition be operative everywhere. Ethical relativism allows companies to violate those few big principles by which they aspire to operate. Second, ethical imperialism is also eliminated, because a globally integrated approach requires that identical practices occur everywhere a company does business. This can be dysfunctional because it fails to recognize and respect legitimate differences in practice that do not violate principles, and it, therefore, creates stresses and hostilities where none are necessary. The four remaining cells constitute rational steps in the hybrid process of implementing GBC.

Steps in the GBC Process

Step 1: Development of a Code of Conduct

To implement GBC, companies first accept a small, reasonably comprehensive set of ethical principles that are near-universal and easily justifiable. Principles of liberty and welfare contained in the Universal Declaration of Human Rights, or the 10 principles of the United Nations Global Compact, are examples. Principles serve as the basis for the company's code of conduct, developed from a comprehensive inventory of the company's exposures, liabilities, and stakeholder challenges.

Step 2: Local Implementation

Sometimes a company's code and policies can be implemented straightforwardly. Sometimes, however, modifications will be demanded to conform to local law or custom. An acceptance of *cultural* relativism does not necessarily imply acceptance of *ethical* relativism. Companies can often implement policies in culturally sensitive ways without violating basic principles. Doing so may involve a measure of stakeholder engagement and concentrated effort to listen and learn, but it need not involve conflict or compromises in basic values.

For example, child labor prohibition is a near-universal principle. But there are legitimately different ideas about what the age limits and constraints should be. UN guidelines say that children less than 14 years should not be employed full time. This can be construed as a minimum, with some nations having 16 years or older as the age of compulsory education. And, in some less developed cultures, a child of 12 years might legitimately be employed in a family enterprise as long as schooling continues and the child is not exploited.

Step 3: Problem Analysis and Experimentation

When the company is faced with high ethical uncertainty, managers at Step 3 of the GBC process respond with analysis and experimentation to situations in which their company's principles cannot readily be implemented, or are violated by, seem to conflict with, or do not cover observed local practices. Experimentation involves testing various ways of satisfying the demands of universal principles and the constraints of local cultures. Outcomes may range from discovering that there is no conflict after all to deciding that the company must exit the region because its principles cannot be applied.

Step 4: Organizational and Systemic Learning

In the final step in GBC implementation, the company engages in a continuous process of *systematic* learning from its experiences and making the results accessible to all company decision makers. In addition, the company engages in *systemic* learning. GBC is aimed at sustainable capitalism, not merely competitive advantage for particular firms; so GBC companies will share what they learn with other companies so that overall harms are lessened and benefits are enhanced for people, social institutions, and the earth itself. Systemic learning can happen through trade and industry associations, conferences, scholarly research and publications, and increasingly through the posting of data on the World Wide Web.

Examples

Companies that have adopted universal principles as their guiding values (Step 1) include export contractor W. E. Connor & Associates, in their role in supplier certification of child labor–free production, and computer giant Hewlett-Packard, which spearheaded industrywide supplier codes of conduct. Local implementation examples (Step 2) are plentiful on the UN Global Compact Web site (www.unglobalcompact.org). Experimentation (Step 3) can be seen in Bouygues Telecom's employee experiments to find the most satisfactory way to recycle office paper and in the partnering of gold mining company AngloGold Ashanti with several global nongovernmental organizations to address the HIV/AIDS crisis among its African workforce by delivering both basic health care and HIV/AIDS drugs to employees and their families. Organizational learning (Step 4) is illustrated by clothing retailer The Gap's response to stakeholder criticisms with an extensive regional reporting of sweatshop conditions in its supply chain and a process for follow-up and improvement. Systemic learning (also Step 4) is seen in Interface Inc.'s transparency about and advocacy of its ongoing efforts to create and market environmentally friendly carpets and to reduce the company's overall "environmental footprint" or impact.

—*Donna J. Wood*

See also Business Ethics; Corporate Citizenship; Corporate Social Responsibility(CSR) and Corporate Social Performance (CSP); Global Business Environments; Global Codes of Conduct; Globalization; Human Rights; International Business Ethics; Political Theory; Stakeholder Theory; United Nations Global Compact

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Global Business Environments

Global business environments encompass internal and external stakeholders that affect the operations of multinational companies (hereafter referred to as "multinationals"). Multinationals are firms that make investments to produce and/or market products and services in foreign countries.

Several theorists such as Jagdish Bhagwati and Steven Hymer have identified the reasons for the rise of multinationals and the benefits and costs that they bring to global environments. Generally, the theories of multinationals have identified multinationals as possessing intangible assets, including brand names, investments in research and development, ability to engage in financial arbitrage, managerial expertise, and control over logistics and distribution channels; these intangible assets, theorists have argued, give multinationals advantages over local companies' knowledge of local markets and conditions. Theories of multinationals can focus on either internal or external stakeholders in the global environment. For example, theories dealing with market imperfections, internalization, and strategic management delineate the interests of internal stakeholders, specifically multinationals' owners and managers. A second set of theories dealing with manufacturing processes, oligopolistic markets, political economy, international relations, dependent development, and global networks specify multinationals' abilities to affect labor, governments, states, societies, and the world. As argued in *Multinational Corporations in Political Environments: Ethics, Values and Strategies*, the second set of theories has portrayed multinationals as catalysts or change agents: Theorists have assumed that because of their control over intangible assets, powerful multinationals bring about major changes, beneficial to some stakeholders but detrimental to others in global environments. In this entry, we do not deal with the net benefits or losses of globalization and global production, but rather review the effects that global production through multinationals have on various stakeholders in global environments.

Theoretical Rationales for Relations With Stakeholders

Owners and Managers

Economists beginning with Stephen Hymer have portrayed multinationals as arising from market imperfections that allow them to exploit their intangible assets and give them advantages, over local companies' knowledge of local markets. They have also argued that multinationals internalize markets—that is, they bring external markets for goods and services under internal control. These theorists have portrayed multinationals as entrepreneurial firms that strive to maximize profits and efficiencies and have granted owners' (stockholders' and investors') interests paramount importance. Many of the theories also deal with how managers recoup transaction benefits by common governance of separate but interrelated global activities—that is, the theories explain why managers control and coordinate operations. Many of the theorists have assumed that subsidiaries are miniature versions of headquarters. Consequently, subsidiaries' and headquarters' managers are portrayed as having similar interests and views.

Strategic-management theories have also focused on how headquarters' managers may control subsidiaries to maximize profits. When the theories have explained labor's or governments' behaviors, they have concentrated on the circumstances under which these stakeholders hinder or help managerial control. Many theories have focused on multinationals' needs to integrate subsidiaries' managers into global operations and the most efficient types of management controls. For example, Yves Doz and C. K. Prahalad concluded that various organizational mechanisms enhance the abilities of headquarters' managers to elicit valid, reliable information from subsidiaries' managers. These include data management mechanisms such as information systems, managerial mechanisms such as reward-and-punishment systems, and conflict-resolution mechanisms such as task forces and business teams.

Labor

Theories that analyze manufacturing processes have related multinationals' growth and expansion to technological developments in their home countries. The theorists have generally assumed that technological developments occur in developed countries with high labor costs, which encourage the multinationals to use laborsaving, capital-intensive technologies. When multinationals eventually move production to less developed states, the theorists have posited that they continue to use the same factor proportions in production—to the detriment of labor-rich, host states. For the most part, theorists have ignored the possibilities that by initiating labor-intensive innovations of their own, host states could make multinationals less competitive.

Raymond Vernon and other theorists extrapolated on how multinationals' manufacturing processes hurt domestic labor. As multinationals' technologies evolve, their operations may use foreign rather than domestic labor. Efficiency and profit considerations may prompt multinationals to export labor-intensive jobs from home to less developed states. In effect, multinationals may snatch jobs from home states' labor. Thus, theorists explained social phenomena, such as the antagonistic behaviors of home states' labor toward multinationals.

Governments

Multinationals often operate in oligipolistic markets, where a few companies control the bulk of the markets. Theorists concentrating on multinationals' strategies in oligopolistic markets have argued that they may prevent the growth of domestic firms. Their observations have implications for governmental roles in industries and the regulation of multinationals' activities.

In many of these models, multinationals adopt defensive strategies in response to their major competitors' price cuts and maneuvers. Edward Graham referred to the relations between these oligopolistic multinationals as exchange-of-threat motivations. Oligopoly theorists have often concluded that as multinationals increase their potential responses, they concurrently reduce domestic and global competition and stabilize markets. Oligopoly theories imply that multinationals' comparative advantages and global strategies often preclude domestic firms from competing successfully in the same markets. Their implied conclusion is that governments should intervene to maintain competitive markets, and to promote social welfare, by correcting the imbalances perpetuated by multinationals.

Early political economists used bilateral-monopoly models to analyze the relations between multinationals and governments: Multinationals control capital, technology, management, and marketing skills to launch economic projects; governments control access to states before multinationals invest, and control conditions for operation afterward. Multinationals and governments were generally represented as struggling over the distributions of benefits from economic projects. For example, Edith Penrose argued that at first, multinationals receive just enough benefits to induce them to commit investments; later, they receive just enough to prevent them from withdrawing.

Raymond Vernon introduced the dynamic concept of the obsolescing bargain to the static, bilateral-monopoly models. Risks and uncertainty formed central tenets of this concept. Before multinationals invest in foreign states, production costs and markets determine their perceptions of risks and uncertainties. To induce foreign investments, governments structure contracts to reward multinationals handsomely for successful projects, and initial contracts tilt heavily in favor of multinationals. However, if projects prove successful, risks and uncertainties dissipate. Hostage effects also take place, because multinationals cannot credibly threaten to exit once they have invested heavily in states. Besides host states may move up learning curves of bargaining and managerial skills, drive harder bargains with multinationals, and threaten to replace them if they fail to renegotiate contracts. Whatever the causes, the obsolescing bargain predicts that initial agreements favoring multinationals are likely to be renegotiated in favor of host governments.

Political-economy theories have generally depicted subsidiaries' behaviors as strategies to exploit intangible assets and to extend parent firms' abilities to extract oligopoly rents. For the most part, the theories have concentrated on just a few ways in which governments influence multinationals: by creating or heightening market imperfections through tariffs and trade barriers, restricting financial and factor markets, restricting know-how, containing sellers' markets, and widening international tax differentials.

Generally, the theories have focused on how multinationals influence governments. Theorists have argued that multinationals cause efficiency and equity effects in states. Efficiency effects deal with multinationals' abilities to increase states' outputs: As multinationals move resources such as capital from places where returns are low to places where returns are high, they bid up the prices of abundant resources, such as labor, in host countries. By their more efficient uses of global resources, multinationals may increase global outputs. By increasing market competition, multinationals may also boost domestic firms' efficiencies. Equity effects deal with the distribution of the incremental outputs between governments and multinationals. Equity effects generally take place through host states' taxes, lower prices for consumers, and increased profits for multinationals. Political-economy theorists often viewed governments and multinationals as antagonists, arguing over allocations of incremental outputs through taxes or repatriated profits. Generally, labor forces lose in these theories: Multinationals' strivings for increased efficiency, together with their flexibility, cause labor forces to lose their bargaining powers.

States

Many international relations theorists have assumed that from the early 1900s until World War II, the United States constituted the world's dominant military and economic power, contributing greatly to creating and to maintaining the international economy through institutions such as multinationals. After World War II, the United States, Western Europe, and Japan formed the dominant powers. Today, this triad, and the economic order it maintained, is in disarray. The theorists have offered at least two contradictory explanations for multinationals' roles in the aftermath of this hegemonic collapse.

Raymond Vernon initially proposed one explanation in his influential book *Sovereignty at Bay.* He argued that economic interdependence and technological advances in communication have undermined the traditional, economic rationales for states. World efficiencies and domestic, economic welfares will continue to decrease states' powers vis-à-vis multinationals and other international institutions. Sovereignty-at-bay differentiates between the United States' creation of a world economy and the subsequent dynamics of its maintenance. Theorists subscribing to this view have argued that rather than hegemonic powers, interdependent, international, economic interests, and the benefits from the interdependencies, now bind international orders together. States have joined in economic relations with multinationals and other states from which they cannot easily escape and from which they derive great benefits. States' citizens would not tolerate the sacrifices in economic well-being that would follow if states hamper multinationals' operations. Governments, therefore, dare not forego employment and regional-development opportunities by sanctioning multinationals.

Sovereignty-at-bay deduces that the flexibility and vast resources of multinationals grant them advantages in confrontations with states. If multinationals move production facilities elsewhere, states lose employment, corporate resources, and access to world markets. Thus, the theorists have argued that multinationals often escape states' controls and emerge as powers to change international, political relations. Conversely, states often face the possibility of losing control over economic affairs to multinationals. States may not be able to retain traditional sovereignty and to meet their citizens' rising economic demands. Therefore, the sovereignty-at-bay model views states' efforts to enhance security and power as incompatible with an interdependent world economy that generates absolute gains. The theorists have contended that economic forces will eventually contribute to the end of nationality as we know it. The sovereignty-at-bay world consists of interdependent economies with voluntary cooperative relations that accelerate everyone's economic growth and welfare. In this world, multinationals, freed from nation states, form critical transmission belts of capital, ideas, and growth.

Another explanation revolves around the mercantilist theories that have painted the interplay of states' interests as the primary determinants of the international economic order's future. These theories relegate multinationals to peripheral places or regard them as states' instruments. According to these theorists, the interdependent world economy that provided an extremely favorable environment for multinationals has come to an end. In the wake of the relative decline of the United States' power, and of the growing conflict among capitalist economies, a new international order, less favorable to multinationals, is coming into existence. This emergent world order is characterized by intense, international, economic competition for markets, for investment outlets, and for sources of raw materials. In the new order, states manipulate economic arrangements to maximize their own interests, even at the expense of their stakeholders. States' interests concern domestic matters (such as employment and price stabilities), as well as foreign-policy matters (such as security and independence). Thus, mercantilist theories have granted priority to states' economic and political objectives over global economic efficiencies. In pursuit of economic objectives and national interests, states attempt to control actors within their realms, including multinationals.

Mercantilist theorists have argued that international competition has intensified because the United States has lost its technological lead in products and manufacturing processes. U.S. multinationals must now increasingly compete on the basis of prices and a devalued dollar. Thus, the United States can no longer draw on the technological rents associated with its industrial supremacy, and the supremacy of U.S. multinationals in the economic order has come to an end. Consequently, U.S. multinationals play greatly diminished roles in maintaining the United States' hegemonic rule. States will now increasingly form regional, trade, and monetary alliances to advance their own interests. This regionalization will replace the United States' emphases on multilateral free trade, the dollar's international role, and the U.S. multinationals' supremacy.

Societies

Multinationals' effects on societies are largely depicted in sociological studies dominated by the Marxist, dependency school. A variety of contentions, some contradictory, have emerged from the dependency theorists. The theorists have argued that multinationals distort economic development in less developed states by forcing them into associated or "dependent development" relationships. They have charged multinationals with creating branch-plant economies of small, inefficient firms that are incapable of propelling overall development. They have argued that foreign subsidiaries exist as appendages of their home firms, and as enclaves in states' economies, rather than as engines of self-reliant growth. They have accused multinationals of introducing inappropriate, technological developments and of employing capital-intensive, production techniques that cause unemployment and prevent the emergence of domestic technologies. They have asserted that multinationals skew income distributions among classes in less developed states. And, because of their repatriation of profits and their superior access to local capital, they have contended that multinationals prevent the rise of indigenous companies.

Dependency theorists have also concluded that multinationals wreak negative, political consequences in less developed states. For example, theorists have asserted that multinationals require stable, host governments that are sympathetic to capitalism; therefore, dependent development encourages authoritarian regimes in host states and creates alliances between multinationals and domestic, reactionary elites. They have contended that multinationals' home governments sustain these exploitative alliances by intervening in the internal affairs of less developed states. In this fashion, multinationals tend to make host states politically dependent on home, industrialized states.

Some dependency studies have concentrated on trying to show that social and economic equalities are caused by multinationals distorting employment opportunities and labor-force structures. The studies generally have drawn on Marxists' beliefs that capitalist systems increase inequalities. Other studies have concentrated on multinationals' negative effects on societies and cultures. Dependency theorists have concluded that states may lose control over their culture and social development. Therefore, multinationals may contribute to cultural imperialism or CocaColaization of less developed societies. Dependency theorists have proposed that multinationals undermine societies' traditional values by introducing new values and tastes through advertising and business practices. These new values often create demands for goods that do not meet the masses' true needs.

The World

Anthropological theories have analyzed multinationals' attempts to control and to coordinate their operations by managing global environments. Changes in political and economic systems threaten multinationals' abilities to predict, to plan, to manage, and to economize. To help control their destinies, multinationals generate large-scale regularities and interdependencies through means other than centralization. Anthropological theories show how political and economic networks develop as multinationals, create branch offices, merge, and cooperate with other firms, political groups, and governmental agencies. Thus, multinationals develop political-control networks that serve as socially integrating mechanisms for them. The networks bind multinationals, states, and families into supranational structures with ambiguous boundaries. But as multinationals extend their spheres of influence through participating in the networks, and as they increasingly adopt policies that slow growth, they also de-emphasize their market-exchange functions, and increasingly emphasize redistributive functions with respect to states and societies.

George Haley documented how the overseas Chinese companies form global networks to enhance the distribution of information while not necessarily maximizing profits or efficiencies. Alvin Wolfe also described how multinationals bind together in global networks that channel reciprocities. He isolated two types of decision rules that multinationals use: maximization rules in which behaviors are contingent on anticipated returns and reciprocity rules in which behaviors are contingent on assessing others' needs and wants. He argued that often multinationals follow reciprocity rules just to keep some stakeholders in the system. For example, a multinational may sell another a raw material that is in such short supply as to be unavailable to firms unaffiliated with the system. In this fashion, multinationals may control and coordinate their operations at global levels, while not necessarily maximizing profits or efficiencies.

Ethical Implications in the New Economy

In recent decades, substantial changes have occurred in multinationals' competitive environments. Traditionally, the industrialized democracies of Western Europe, North America, and Japan (the Triad) had spawned multinationals. This prevalence of culturally and economically related home countries created an environment of similar ethical standards for multinationals' managers: Japan served as the only significant, non-Western source of ethical conflict for multinationals. Today, emerging markets such as India and China, culturally and economically different from the Triad, are also giving birth to multinationals. The ethical standards of multinationals from these emerging markets can differ substantially from their Western counterparts. Ethical differences often emerge starkly in China and Southeast Asia, where ethics have Confucian roots independent of the West's Judeo-Christian roots. Differing perceptions of intellectual property (IP) provide an example of the difficulties that can arise. In Confucian societies, IP did not exist—entrepreneurs were supposed to copy their employers' and/or competitors' technologies. Thus, people raised in traditional Confucian societies tend to view the Western multinationals that seek compensation for IP theft as the transgressors.

Consumerism and relations with customers also pose ethical dilemmas in the new global environment. Whereas the industrialized societies generally have active consumer movements, most of the newly emerging economies do not. Consumer movements are rapidly developing in many of the more advanced emerging economies, but in the poorer economies and in some of the transitional, formerly communist, economies, multinationals' managers must be cautious: In the former, because failure in consumer issues can elicit charges of ethical callousness in the Triad markets; in the latter, because the emerging markets' governments, frequently still totalitarian, can use consumerist charges to attack foreign multinationals.

Ethical and policy implications arise in business practices, such as relations with clients in global environments. For example, advertising ethics in the United States vary widely from those in Asia. In the United States, an advertising agency that represents two competing companies would commit a breach of ethics; in Japan, advertising agencies tend to specialize so that the same agency represents several companies in the same industry; in Europe, the standards are subject to interpretation.

The relative role of the media also differs between countries. In most Triad economies, the media enjoys relative freedom. In some Triad countries, such as the United Kingdom, the state owns substantial portions of the media, but the media retains its independence. In contrast, in many emerging markets the governments own and control the media. Even when media ownership rests in private hands, substantial ties often exist between the media and the local governments. In these instances, multinationals must deal with situations where the media serves governmental rather than public or private interests.

—Usha C. V. Haley and George T. Haley

See also Globalization; *Guanxi*; International Trade

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Global Codes of Conduct

A global code of conduct may be defined as a set of guidelines or principles for business practice that establish ethical standards for business and employee conduct, especially for those firms operating in the international business environment. Global codes of conduct have grown in importance as we have witnessed the rise of global business as a critical element in the world economy. This rise is one of the most significant developments in business during the past 50 years. This period has been characterized by the rapid growth of direct investment in foreign lands by the United States, Western Europe, Japan, and increasingly other Asian countries. Global business has grown by leaps and bounds as technology, communications, and competitive forces have pressured firms to seek new markets.

In recent years, there has been evidence of a backlash against global capitalism. One reason for this is the complexity of the transnational economy and the opportunity for ethical issues to arise as companies increasingly do business across cultures. It is inevitable that as the clash of cultures and ethics increases, the need for business to take more affirmative action to head off these problems also occurs.

Protests in recent years have been led by environmentalists, who are concerned about the degradation of natural resources, and by human rights activists, who are concerned about treatment of human rights and fair treatment of the world's workers. Many protestors are today being referred to as antiglobalists because they believe global capitalism has gone too far and has been creating more disadvantages than advantages. These antiglobalists argue that multinational corporations have created ethical problems with respect to consumers, employees, human rights, developing nations, and the natural environment.

It is against this backdrop that the issue of global codes of conduct have arisen and become more important in recent years. It should also be observed that global codes of conduct are just an extension of traditional codes of conduct that have been used by companies for decades before international business and global competition became a widespread and integral part of the business world.

As global ethical issues have become more of a serious concern, there has been a growing need for effective responses on the part of business to these issues. Companies have taken many different steps to help restore confidence and trust in business. Consequently, global extensions of corporate social responsibility, corporate citizenship, and business ethics initiatives have become commonplace in the past two decades. Thus, global codes of conduct have typically been embedded in broader programs aimed at improving corporate conduct around the world, especially in developing countries. In this context, global codes of conduct may be seen as just one element in business's overall global corporate social responsibility initiatives.

Global Codes of Conduct Defined

A global code of conduct may be defined as a set of guidelines or principles for business practice that establish ethical standards for business and employee conduct. These global codes are established at a variety of different levels. Corporations may create a global code applicable to just the firm in question. Industry-wide codes of conduct may also be established. For example, industries such as shoes, apparel, forest products, mining, and paper have established industry-level codes of conduct. In addition, global codes of conduct have been established by international organizations. Some of these international organizations may be government based, nongovernmental organizations (NGOs), or other nonprofit, special-interest organizations interested in improving business ethics internationally.

Code Formats

Most global corporate codes of conduct are voluntary in nature. That is, there is no legal enforcement mechanism governing their implementation. Such codes may be expressed in a variety of different formats. In a major study of corporate codes, The Conference Board, a nonprofit, business advocacy association, has found that these codes may be formulated and distributed in several different formats. Codes may be stated as *compliance codes.* These are usually a set of directives that give guidance to managers as to what to do or not to do with respect to various business practices. Another form used is that of the *corporate credo.* These are composed of broad, general statements of business commitment to various constituencies, or stakeholders, and may embrace value statements and strategic objectives. Finally, *management philosophy statements* may be the format used. These are similar to corporate credos but may just explicitly summarize the company's or the CEO's approach to doing business.

In its own study, the U.S. Labor Department has differentiated among the following different kinds of code formats. *Special documents* include written codes of conduct that summarize company standards, principles, or guidelines in a number of different arenas. These special documents communicate standards to the public and to affected stakeholder groups such as suppliers, customers, competitors, and shareholders. *Circulated letters* are another format. Such letters expressly state company policies on a specific issue to affected stakeholders. *Compliance certificates*, another format, are documents that require suppliers, agents, or other contractors to agree in writing that they will comply with the company's stated standards. Finally, *purchase orders or letters of credit* are written documents that make compliance with a company's policy part of a contractual obligation on the part of suppliers or other contractors.

Three Types of Global Corporate Codes of Conduct

Previously, it was stated that global corporate codes may be established by individual companies, industry groups, and international organizations. A more careful exploration of these three types of codes reflects details clarifying how each type is developed and used.

Corporate Global Codes of Conduct

Corporate codes of conduct are typically just one element in a company's overall ethics program. Today, many companies have ethics programs that are often managed by ethics officers. These ethics programs typically include codes of conduct, ethics training, whistle-blowing mechanisms (e.g., ethics "hotlines"), ethics audits, and responsibility for a variety of different ethics-related aspects of the business such as ethical decision-making processes, discipline of violators, board of director's oversight, corporate transparency efforts, and effective communication of company standards.

Since the creation in 1991 of the Federal Sentencing Guidelines, which reduce penalties for companies with ethics programs, most large corporations today have embraced the idea of ethics programs and codes of conduct. According to these U.S. Sentencing Guidelines, a key feature in an ethics program needs to be a statement of *compliance standards*, and this is what is typically reflected in a company's global code of conduct.

Regarding these compliance standards, companies are expected to have established a set of standards that then serve as the basis for detecting and preventing legal violations. The code of conduct states these standards. Beyond this, a set of ethical principles or guidelines are also helpful to extend beyond what is required by law or to address topics that may not be covered by the law. Other U.S. Sentencing Guidelines requirements state aspects of the code of conduct's implementation that make a difference in its effectiveness. For example, it is expected that the code of conduct's implementation will entail high-level personnel in the company (such as ethics officers); will prevent the undue delegation of inappropriate discretionary authority; will be effectively communicated; will contain systems for monitoring, auditing, and reporting; and will embrace effective enforcement. Furthermore, companies are expected to take action when offenses have been detected, thus preventing future offenses, and to keep up with industry standards. This means that companies are expected to carefully monitor industry standards and practices and make sure that it is at least keeping up with industry standards.

Beyond the fact that companies may suffer less severe penalties if they have ethics programs and codes of conduct in place, what other benefits do companies receive from global codes of conduct? Various studies have shown that companies believe that they get some of the following benefits from codes of conduct:

- Legal protection for the company
- Increased company pride and loyalty
- Increased consumer and public goodwill
- Improved loss prevention
- Reduced bribery and kickbacks

The literature on corporate codes identifies that companies create such codes for both normative and instrumental reasons. From a *normative* point of view, the corporate codes serve as principles intended to guide corporate behavior in the most ethical directions. These have been referred to as "aspirational strategies," the purpose of which has been to describe how employees and agents of the firm *ought* to behave. From an *instrumental* point of view, corporate codes have been motivated by a variety of justifications. According to Krista Bondy, Dirk Matten, and Jeremy Moon in 2004, some of these motivations are their being a part of an internal control system, their being a part of a strategy of differentiation in the marketplace, their being a signal to stakeholders concerning a company's quality and reputation, reduced insurance premiums, peer pressure within an industry, improvement of customer relations, maintenance of standards within a supply chain, and preemption of boycotts and formal accusations.

As to what subjects or topics global codes of conduct address, the following represent some of the most frequently addressed topics found in these corporate codes:

- Conflicts of interest
- Receipt of gifts, gratuities, and entertainment
- Protection of company's proprietary information
- Giving gifts, gratuities, and entertainment
- Employee discrimination
- Sexual harassment
- Kickbacks
- Bribes
- Employee conduct
- Employee theft
- Proper use of company assets
- General conduct

To make sure that corporate codes are more than platitudinous statements of aspiration, S. Prakash Sethi, an expert on this topic, believes that companies need to create codes of conduct for their multinational operations, but that it should not stop there. Sethi recommends that companies should permit their activities and practices to be monitored by external and independent sources. An example of this model would be the Mattel toy company, which Sethi has worked with, in setting up a code, standards, and monitoring procedures. In the case of Mattel, the independent reviews of the company's practices are posted on a Web site, where they may be viewed by others. The company would have the opportunity to correct any factual errors, but beyond this they may not alter the monitor's report. They may write their own report disputing the findings or reporting on how the company would be responding to the findings. Sethi argues that the best global codes are those voluntarily written by companies because such a code may be carefully scrutinized and evaluated by outside parties and only the company itself can be held responsible for its actions. Some corporations have taken their global codes a step further by stipulating that their business partners and suppliers also adhere to their codes. For example, on the subject of global outsourcing, some companies such as Nike, adidas-Salomon (formerly adidas), Levi Strauss & Co. (LS&Co.), and the Gap have striven to monitor not only their own companies but also those with which they do business.

Specific Corporate Examples

As reported by Tara Radin in 2003 and 2004, two different companies in different industries serve as modern exemplars of the use of global codes of conduct: Chiquita Brands International and LS&Co. Chiquita, operating primarily in Latin America, employs a values-based approach to management and monitors its global conduct through the umbrella of a corporate responsibility officer. Chiquita monitors its performance through both internal and external means. Chiquita issues annual corporate responsibility reports in which it presents and evaluates both the strengths and weaknesses of its social and ethical performance.

In contrast, LS&Co. operates almost exclusively through sourcing partners scattered throughout the world, including Latin America. LS&Co.'s initiatives have served as a model for others in developing outsourcing standards and guidelines as many companies operate throughout the world in a similar manner. LS&Co.'s *Global Sourcing Guidelines* include both regular country assessments as well as analyses of the extent to which its sourcing partners are adhering to the company's "Terms of Engagement," which were established in 1991. These Terms of Engagement represent the actual standards by which the company expects its global partners to comply. LS&Co. implements its initiatives through a corporate level director and regional compliance officers. The company conducts widespread monitoring of its suppliers, and is increasingly seeking to employ external monitors. In many respects, LS&Co.'s program is more difficult to implement because it operates through private contractors, while Chiquita, in contrast, operates as a direct employer. Both these companies have served as exemplars for other firms seeking to employ global codes of conduct. The experience of both these companies points to the critical importance of internal and external monitoring to give their codes of conduct integrity.

As it will become apparent with both industry-based corporate codes and international groups' codes, the issue of monitoring is crucial to the effectiveness of global codes, whatever the level of their implementation. Internal monitoring may occur by special teams or consultants and represent a necessary first step in developing effective code implementation. External monitoring, often made possible through a strategy and practice of corporate transparency, allows external groups to conduct their own analyses of the codes' effectiveness. External monitoring sets the stage for higher levels of accountability as NGOs and other stakeholder groups are able to independently evaluate the firms' progress and achievements.

Industry-Based Corporate Codes

Beyond the individual company level, some industries have begun initiatives to create global codes of conduct for the companies competing in that industry. This makes a lot of sense because often the firms in a given industry are identified as a group and the actions of one affect the reputations of others. Furthermore, if firms operating in an industry can agree on ethical standards, this places the member firms on a level playing field in terms of treatment of stakeholders and issues affecting the industry.

As suggested earlier, one of the first industries to recognize the common interests of those in the industry was the defense industry in the United States. Due to corporate scandals surfacing in the 1980s, companies in the defense industry saw that one way to promote common interests was through some form of self-regulation that might deter further government regulatory strictures. The various initiatives in the industry included codes of conduct and the creation of ethics programs, ethics officers, and ethics training. These efforts eventually led to the Defense Industry Initiative on Business Ethics and Conduct, which would be classified as an industry-based set of guidelines or corporate code.

Over the years, other industries have developed global corporate codes as their commercial activities became more internationalized. Industries that have moved in this direction by creating various forms of corporate codes include apparel/garments, lumber, paper, mining, banking, and manufacturing, in general. Thomas Hemphill has termed such initiatives as attempts at industry self-regulation.

In recent years, the controversy surrounding "sweatshops" and some of the questionable practices associated with them have spurred the creation of a number of different industry groups determined to set standards for the firms participating in the apparel industry. In many instances, these different associations have come into competition with each other, as each is striving to become the standard-setter for the industry. Two industry-level groups trying to regulate industry behavior with respect to sweatshops include the Fair Labor Association (FLA) and Social Accountability International (SAI).

According to its Web page, the FLA is a nonprofit organization that coordinates the work of industry, NGOs, and colleges and universities to promote adherence to international labor standards and improve working conditions worldwide. The FLA conducts independent monitoring and verification to ensure that the FLA's workplace standards are upheld where FLA company products are produced. Through public reporting, the FLA provides consumers and shareholders with trustworthy information to make responsible buying decisions. The FLA "workplace code of conduct" includes ethics standards for such categories as forced labor, child labor, harassment or abuse, nondiscrimination, health and safety, freedom of association and collective bargaining, wages/benefits, work hours, and compensation for overtime work. The FLA takes these standards one step further by expecting that signees to these standards also require its licensees and contractors, or suppliers, to abide by local laws in the country in which they are operating and with the standards set forth in the FLA code.

According to its Web page, SAI has the mission of promoting human rights for workers around the world as a standards organization, ethical supply chain resource, and programs developer. SAI promotes workers' rights primarily through its voluntary SA8000 system, which is based on the International Labour Organization (ILO) standards and UN Human Rights Conventions. SAI argues that SA8000 is widely accepted as the most viable and comprehensive international ethical workplace management system available. What is interesting about SAI and to some extent the FLA is that they both originate in specific industries that compete globally but have drawn other organizations, including governments and other nonprofits, into their networks. Thus, although they began as industry-based initiatives, they evolved to be more comprehensive in scope, membership, and affiliation.

Another example of industry-level global corporate codes is the banking industry that has developed its Equator Principles, which are a set of guidelines developed by the banking sector for dealing with social and environmental issues with respect to the financing of economic development projects. The Equator Principles truly represent a global industry set of standards for financial institutions as member banks currently come from most of the major countries of the world.

International Organizations' Global Codes

Over the years, a number of different international organizations have sought to develop global codes of conduct that would serve as overarching guidelines for multinational companies doing business across country lines. These international organizations have included faith-based groups, NGOs, and even some political entities that have sought to set standards for companies operating globally or in particular countries. Their standards have been dubbed "group based." Examples of these group-based global codes of conduct that have been developed by various international groups include, but are not limited to, the Sullivan Principles for South Africa, later renamed the Global Sullivan Principles, the Caux Principles for Business, Principles for Global Corporate Responsibility, the Global Reporting Initiative, and the UN Global Compact. A brief statement of several of these is illustrative of the types of groups putting them together.

Caux Principles

The Caux Principles were issued in 1994 by a group known as the Caux Round Table. The Round Table was composed of senior business leaders from Japan, Europe, and North America. The Caux Principles are an aspirational set of recommendations and guidelines for corporate behavior that seeks to communicate a worldwide set of standards for ethical and responsible business conduct. The Principles address the social impact of company operations on the local communities.

Principles for Global Corporate Responsibility: Benchmarks

These principles were developed by the Interfaith Center for Corporate Responsibility (United States), Taskforce on the Churches and Corporate Responsibility (Canada), and the Ecumenical Council for Corporate Responsibility (United Kingdom) in 1998. These principles are intended to provide a model framework through which stakeholders can assess corporate codes of conduct, policies, and practices related to Corporate Social Responsibility expectations. The standards include 60 principles and benchmarks that can be used to assess corporate social and ethical performance.

UN Global Compact

The Global Compact was issued by the United Nations in 1999. It includes a set of 9, later expanded to 10 principles, that endorsing companies would agree to abide by. According to its Web page, the UN Global Compact asks companies to embrace, support, and enact, within their sphere of influence, a set of core values in the areas of human rights, labor standards, the environment, and anticorruption.

Global Reporting Initiative (GRI)

A revision of the GRI was issued in 2000 by the Coalition of Environmentally Responsible Economies.

GRI is an international reporting standard for voluntary use by organizations reporting on the social, environmental, and economic aspects of their products, services, and activities.

Global codes of conduct at this level have typically been created by a variety of different groups, often working in conjunction with governments and NGOs, to create standards that serve as guidelines for companies doing business in the international sphere. Many different companies have become signatories to these codes and some companies have agreed to comply with multiple codes.

Conclusion

Global codes of conduct are an important way by which companies and industries may strive to conduct their activities on a legal and ethical plane in the international sphere. Most codes began as domestic focused, only later to become globally focused in keeping with the increasing globalization of commerce worldwide. Such codes have been created primarily on three different levels—the level of the firm itself, the level of industry associations, and the global level at which international organizations have created principles and standards for all firms doing business in the world or a particular part of the world.

To some extent, the idea of global codes of conduct has been controversial and not supported by everyone. It is difficult enough to implement conduct codes at the domestic level but extremely difficult at the global level. Some commentators have thus been critical of the idea, thinking they represent more of an ideal than a realistic possibility. In spite of this, the trajectory of global codes continues to grow.

Global corporate codes seem to have a bright future. It is axiomatic that increased ethical conduct and practice can only follow from standards that have been expressly established, communicated, adopted, and monitored. As the trend toward corporate transparency continues, the monitoring activities that have begun will continue. It is expected that all three levels of corporate codes will continue to flourish in the future as companies, industries, and the business community strive to build and retain trust and credibility with customers, employees, countries, and other stakeholders. To date, the use of global codes of conduct has had a positive impact on international labor practices, and thus, they are expected to continue.

—Archie B. Carroll

See also Caux Principles; Codes of Conduct, Ethical and Professional; Corporate Accountability; Corporate Social Responsibility (CSR) and Corporate Social Performance (CSP); Fair Labor Association (FLA); Federal Sentencing Guidelines; Global Reporting Initiative; Transparency; United Nations Global Compact

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GLOBAL CROSSING

Global Crossing was founded in 1997 and became the fourth-largest bankruptcy in U.S. history just 5 years later in 2002. Specifically, Global Crossing was swapping network capacity with other carriers to artificially inflate earnings and make the company look more profitable than it was. The road to that bankruptcy is a story of revenues inflated by what appears to be fraudulent accounting, in which senior executives enriched themselves while Arthur Andersen served as auditor. Global Crossing employees and shareholders seem to have been left holding the bag, much as in the Enron bankruptcy filed just 2 months earlier.

Global Crossing was the brainchild of Gary Winnick. Winnick was a former junk bond financier who worked with Michael Milken at Drexel Burnham Lambert but escaped untarnished from a 1990s scandal at that firm. Together with a group of financial gurus and chief executive officers, he envisioned a global broadband network that would link continents with undersea fiber-optic cables. This was a risky proposition in 1997 because no such network existed, and no one knew exactly how profitable, or unprofitable, such a network would be. It has always been extremely difficult to forecast the profitability of new services or new technologies, and the Global Crossing proposal was no exception.

Global Crossing faced one, not so small obstacle to executing its business plan: It effectively had no assets, and building such a high-tech, undersea network would be tremendously expensive, of the order of $2.7 billion. Fortunately, *Wall Street* investors valued the Global Crossing concept highly and offered Winnick and his management team about $40 billion in equity financing and $10 billion in debt financing. Investment analysts gave the stock a "strong buy" rating.

The Global Crossing situation was complicated due to the fact that stock analysts were consistently bullish after the company went public in August, 1998. For example, during the time that Jack Grubman, employed by Salomon Smith Barney, was pushing the stock, Global Crossing executives were selling company stock. The result was millions of dollars of personal income for executives at a time when the business model was falling apart. Chairman Gary Winnick is reported to have sold stock valued at $123 million on May 23, 2001, despite a witness telling a congressional committee investigating Global Crossing that Winnick had seen an April 2001 forecast projecting a drop in revenue of $300 million.

Global Crossing founder and chairman Gary Winnick resigned from the board on December 31, 2002, under pressure from investor groups. Altogether, it appears that Winnick profited by about $734 million from his sales of Global Crossing stock before the company filed bankruptcy. However, he and more than 20 Global Crossing executives and directors face a lawsuit filed in the Federal District Court in Manhattan that consolidates several class-action complaints on behalf of investors who lost billions of dollars on Global Crossing stocks and bonds. Arthur Andersen settled with Global Crossing investors for $25 million for its role in the company's financial failure.

Global Crossing had a market valuation of more than $50 billion, larger than General Motors on paper, and its fiber-optic telecommunications network connected 200 cities in 27 countries. However, it amassed about $12.4 billion in debt establishing its global fiber-optic telecommunications network. Global Crossing's revenues dropped to $2.4 billion in the first three quarters of 2001, down from about $3.8 billion for the same period in 2000. Global Crossing was forced to declare bankruptcy on January 28, 2002.

The Securities and Exchange Commission (SEC) claimed that Gary Winnick didn't have enough involvement with day-to-day operations to warrant civil securities charges. Winnick agreed to pay $1 million to settle charges that he failed to fully disclose the terms of several deals to swap fiber-optic network capacity. Global Crossing has emerged from bankruptcy as a global Internet protocol (IP)-based telecommunication carrier whose customers include more than 40% of the Fortune 500.

Today, Global Crossing has reemerged through a strategy of "invest and grow." The company now provides sophisticated IP products to multinational corporations. Just less than 80% of the company's traffic is now VoIP (Voice over Internet Protocol) and the company operates between 130 and 140 softswitches worldwide. In addition, Global Crossing has been able to improve their gross margin from 7% to nearly 13% over the past 2 years (2004–2006). Customers include more than 35% of the Fortune 500, as well as 700 carriers, mobile operators, and Internet service providers.

—O. C. Ferrell and Linda Ferrell

See also Accounting, Ethics of; Business Ethics; Consumer Fraud; Corporate Accountability; Corporate Ethics and Compliance Programs; Corporate Governance; Corruption; Shareholder Resolutions; Shareholders

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Globalization

Globalization refers to the increasing interconnectedness of the world. In stark contrast with prior times, when countries frequently found themselves in competition with one another (and often at war), globalization reflects their coming together to pursue common goals. This phenomenon is manifest most prominently, though not exclusively, through business. At the same time, however, the development of a world economy and global workplace has been accompanied by a general shift in thinking about social, economic, cultural, and political issues as well.

While globalization has arguably been taking place for centuries, the term was not coined until 1983, in a *Harvard Business Review* article by marketing scholar Theodore Levitt. In "The Globalization of Markets," he argued that the world was moving toward a single "global" market and that success would be dictated by the ability of companies to integrate global thinking into their strategic thinking and planning. According to Levitt, "Companies that do not adapt to the new global realities will become victims of those that do."

Globalization allows for the international transfer of goods, services, and ideas through a global marketplace. Although the 1980s and 1990s witnessed a large degree of globalization, its pace has quickened in recent years, particularly as a result of changing technology and the rise of the Internet. Enhanced communication has enabled people to overcome geographic obstacles through real-time interaction. Exchanges take place through local vendors, distributors, and via the Internet. People around the world now have access to many of the same products, no matter where they are. People are also connected through shared media—including, but not limited to, the Internet. CNN, for example, is available on most cable networks across the globe.

A critical factor is that these technological changes have substantially brought down the cost of the spread of information. Even some of the poorest people around the world have cell phones and can get access to the Internet. This has opened the door to innumerable business opportunities that have, in effect, changed the face of the globe.

Historical Context

Scholars and historians tend to differ with regard to how they categorize the various eras of globalization. Some distinguish merely between the pre– and post–World War I periods, while others draw additional distinctions.

Globalization begins with curiosity—the desire to know, understand, and interact with others. It actually dates back at least to the discovery that navigation and travel could connect various peoples around the world. This curiosity led Marco Polo to head east in 1295 and prompted Christopher Columbus to set sail for the West in 1492. At this point in time, what today is called *globalization* translated into exploration and the quest for new trade opportunities.

It can be argued that the period of time until the 17th century represented the first era of globalization: mercantilism. Mercantilism involves trading goods for profit. It was during this time that European countries set out in search of new resources and new trading partners and thereby established new trade routes and trading companies. Entities such as the East India companies were established to champion international trade and to mitigate its inherent riskiness—for instance, through the issuance of stock.

Exploration quickly turned from exploitation of trade opportunities to pursuit of ownership (of resources) as Europe spent centuries methodically colonizing land around the world. In a sense, this unified the globe in joining distant lands under common ownership. This can be called the second era of globalization—colonialism—as empires were created, maintained, and eventually torn apart. This was not the only period of time during which empires existed, but it was during this time that they reached their heyday.

European colonialism dates back to at least the 15th century; it was not until the 17th century, however, that England, France, and the Netherlands extended their empires overseas. Colonialism therefore dominated most of the 18th and 19th centuries. Although it was during this time that some colonies fought and won their independence and the right to self-determination, it was also during this time that the pace of colonization quickened in other areas of the world, such as Africa.

The 20th century can therefore be said to have heralded the third era of globalization: global conflict. It was during this time that colonies, one by one, were beginning to assert themselves. At the same time, imperialist countries were both resisting and finding themselves drawn into global warfare, including two world wars, which represented the fight for resources, territory, and, most of all, power.

Deterioration of colonialism during this era of global conflict began with World War I, as empires collided in a military clash that spanned much of the globe. This was then exacerbated by the pressures of the gold standard, which served as the operative monetary system at that time.

In many ways, World War II represented a continuation of World War I, in that Germany never really accepted the resolution of the first war. When Germany regrouped and reasserted itself, countries around the globe again found themselves in conflict through the same sort of entangled alliances and power struggles that characterized the prior war. This time, the resolution was certain.

World War II was a wake-up call: Its end signaled the beginning of global accountability. The message was sent that countries needed to work together to prevent such atrocities from reoccurring. This led to enhanced emphasis on self-determination for all peoples, which could be said to have laid the groundwork, at least in part, for the subsequent thrust toward the liberation of the remaining colonies and territories of the world.

The next era was that of decolonization, which took place in Africa, Asia, and the Middle East. The result of decolonization was the creation of a fractured globe, composed of disparate entities. In the wake of rampant imperialism, many countries began questioning and challenging one country's involvement in another country's affairs. As states struggled to establish their own identities, the emphasis lay on independence, not interdependence.

During this time, the United States and its allies entered into an era of unspoken discord with the Soviet Union and other Eastern European countries. As many have said, this Cold War was anything but "cold." It was a heated controversy between conflicting ideologies and revealed itself on multiple fronts. It was arguably more universal and widespread than any of the World Wars, encompassing everything from small skirmishes to full-blown conflicts. It spanned continents, with the Korean War (1950–1953), the Bay of Pigs (1961), the Cuban Missile Crisis (1962), the Vietnam War (1964–1975), and the Soviet-Afghan War (1979–1989).

Battles also took place without violence, such as the competition in science and technology, as each of the two superpowers struggled to better the other in exploring outer space. This was accompanied by significant investments in defense spending and a massive nuclear arms race. Even the Internet was born out of this conflict as the former Soviet Union's launch of *Sputnik* prompted the development of a special research organization, the Advanced Research Projects Agency (ARPA, which later evolved into the Defense Advanced Research Projects Agency, or DARPA). It was this entity that created an electronic network for military purposes that was subsequently commercialized as the Internet as it is known today.

Political tension and military sensitivity had a significant impact not only on governmental affairs but also on interaction between and among peoples around the world. Travel—particularly tourism in Eastern Europe—was severely limited and accompanied by little economic and/or business cooperation. Then, in 1989, the Berlin Wall came down, physically and metaphorically, and as it fell, so did the economic, social, and cultural separatism. By the early 1990s, Eastern Europe was transformed from a closed door into a new land of opportunity. This was coupled with a renewed interest in globalization as former enemies turned into cautious acquaintances. Businesses quickly identified partnership and/or joint venture prospects along with other avenues through which they could carve out opportunities in these newly liberalized economies.

As Eastern Europe opened up, most of Western Europe steadily became integrated into a single supranational and intergovernmental entity, the European Union, through the Treaty of Maastricht in 1992. As of 2007, there are 27 member states, including countries from Eastern, Western, and Central Europe. This has led to the removal of additional barriers to trade, travel, and communication. The overall effect of this has been to enhance globalization.

The late 1990s heralded the Information Age, which has advanced globalization arguably to yet another era. This has led to even more rapid globalization in the 21st century. Not only is the economic market for goods and services viewed as a global market, but the labor market is now viewed as a global workplace as well.

It appears that global awareness lies among the current challenges in this era of globalization. Although technology and the Internet have enhanced communication and technology, some people suggest that there is now so much information that it is difficult to filter out extraneous and/or erroneous information in order to identify that which is pertinent.

Global awareness is of particular importance because of the increasing role that companies are playing in global politics through their role in multinational supply chains. Thomas Friedman, author of *The Lexus and the Olive Tree* and *The World Is Flat*, argues that the current era of globalization is characterized most significantly by the "flattening" of the world. Countries are no longer defined by their core competencies so much as they have been integrated into worldwide corporate supply chains—of parts, products, processes, services, systems, or labor—where national origin is no longer relevant.

Joseph Stiglitz, winner of the 2001 Nobel Prize in Economics and former senior vice president and chief economist of the World Bank, challenges the impact of globalization. In both *Globalization and Its Discontents* and *Making Globalization Work*, he contends that it is essential to consider not only those benefited by globalization but also those made worse off. Although critical, he remains optimistic, though, as he asserts that a global society is ultimately best suited to address shared problems such as sustainability and poverty.

Globalization and Trade

It is important to keep in mind that globalization prior to this century was limited in large part by the cost and difficulty of travel and communication. Ships—which, prior to the mid- to late 20 century, represented the predominant method of travel—were costly and slow. This created a significant impediment to more rapid globalization. Advances in technology have enabled faster, cheaper, and more reliable travel and communication, and this has clearly paved the way for the rapid globalization we see today, particularly through enhanced trade opportunities.

Trade is essential to globalization. In a sense, it is the currency through which countries communicate with one another. In fact, globalization of politics, culture, and so on cannot exist without trade.

Trade occurs throughout the world because people desire different goods and services—people appreciate variety and choice. Through trade, countries are able to acquire increased availability of goods and services and more numerous and diverse consumption possibilities.

Low trade barriers are necessary for trade to occur. Early global barriers to trade included the limitations imposed by the barter system, transportation, and technology, which existed in addition to those erected by countries themselves, such as tariffs, duties, licenses, and quotas. Globalization has been significantly influenced by the imposition and removal of trade barriers over time.

An early influence on trade was the introduction of monetary systems. Prior to that, trade possibilities were severely limited by the barter system. For an exchange to occur, at least two parties had to have an interest in what each had to offer the other. With the introduction of currency, a wider range of transactions was made possible.

Trade has also been facilitated by advances in transportation. Initially restricted by land travel, trade benefited significantly from improvements in sea travel and, more recently, air travel. Furthermore, technology now tears down geographical barriers almost entirely by enabling virtual transactions to take place around the globe in real time without any sort of physical travel.

During the late 18th century, countries became aware of the steadily increasing amount of trade that was occurring throughout the world. The Industrial Revolution provided the world with record amounts of goods and supplies. Although industry in Europe and the United States grew significantly, it could not keep pace with the appetite of the domestic markets. Global trade therefore picked up the slack with regard to product surpluses. Certain countries with absolute or comparative advantages over other countries began to trade, or simply export and import goods, in order to maintain higher profits and get rid of the surpluses that they produced. Some domestic companies even began to cater to these international markets in the hope of tapping into the distant though large markets that appeared ripe for exploitation. This increase in trade resulted in the fostering of strong economic and political ties between various nation-states.

The early 19th century witnessed the effect of the growing interconnectedness of the world's countries as entangled alliances led to World War I. Even the United States, separated by an ocean, was dragged into the conflict. This war, directly involving seven countries and causing the deaths of millions of soldiers and civilians, was the first war in which so many countries were involved on so many fronts. Some people argue that World War I was the direct result of conflict caused by increased economic and political competitiveness. As interaction and/or integration escalated between countries through heightened levels of trade, these countries also experienced more opportunities for tension to arise.

Similarly, when the stock market crashed in the United States in 1929, the ripple effects were felt around the world. International trade fell sharply during the Great Depression that followed, and construction came almost to a halt in many countries.

The United States government responded by increasing trade restrictions through the Smoot-Hawley Tariff Act passed in 1930. In raising tariffs, this act arguably exacerbated the depression as other countries retaliated by restricting imports from the United States.

Although the Smoot-Hawley Tariff Act was short-lived, its effects have been long-lasting. It was, at least in part, responsible for the Bretton Woods Agreement in 1944, which established a set of principles to guide commercial and financial dealings among the world's major industrialized countries. These changes in foreign policies have had a major impact on trade. The lessening of self-interested, protectionist thought and easement of trade restrictions made transactions more viable and more desirable.

Bretton Woods also led to the creation of the International Monetary Fund (IMF) and the International Bank for Reconstruction and Development, one of the five institutions that now constitute the World Bank. The Bretton Woods system remained in effect until the early 1970s.

The establishment of the General Agreement on Tariffs and Trade (GATT) in the 1950s can also be traced back to the experiences of the United States with the Smoot-Hawley Tariff Act. GATT was initially set up through Bretton Woods to help provide for post–World War II economic recovery. Its primary role lay in decreasing barriers to international trade. It is important to keep in mind that, unlike the IMF and the World Bank, GATT was an agreement, not an organization.

The final round of GATT negotiations between 1986 and 1994 led to the eventual creation of an organization, the World Trade Organization (WTO), established for the purpose of liberalizing trade around the globe. The WTO handles a range of responsibilities, including negotiation, implementation, and policing of trade agreements.

Efforts are also taking place regionally. The North American Free Trade Area (NAFTA) represents one such effort aimed at managing multinational trade. This agreement removed trade restrictions between the United States, Canada, and Mexico. Similarly, though on a much larger scale, the formation of the European Union removed internal trade barriers and, at the same time, facilitates external trade as well.

Global Organizations

Reflective of the world's recognition of countries' growing interconnectedness and interdependence, numerous agreements and organizations have emerged and continue to influence multinational political, economic, cultural, and social interaction in varying degrees.

Governmental Organizations

The first and foremost of these organizations is the United Nations (UN). Established in 1945, the UN is an international organization comprising 200 member states that endeavors to promote cooperation with regard to international law, international security, economic development, social progress, and human rights. Although the effectiveness of the UN is frequently challenged, it remains in existence more than 60 years after its founding.

The Global Compact is one of the UN's more recent initiatives. Officially launched in 2000, the Compact brings companies together with UN agencies, nongovernmental organizations (NGOs), and civil society in a voluntary effort to promote sustainable and socially responsible business. The Global Compact boasts more than 3,000 member companies from around the world as of 2007.

Organizations such as these are important in that they bring countries together as they confront similar and shared challenges. Again, the reality is that countries are interconnected. Sustainability, for example, is a global problem—not one created by or to be solved by a single country alone. These kinds of organizations bridge the gaps created by political strife.

Nongovernmental Organizations

In addition to those organizations linked to governmental efforts, NGOs endeavor to bridge the gaps created by commercial endeavors. Perceiving global business as a potential threat to local communities and fundamental human rights, NGOs—small and large—strive to offset the harm that businesses can and do commit.

Although the term *nongovernmental organization* was not coined until 1945, with the creation of the UN Charter, voluntary associations formed for humanitarian purposes actually date back more than a century. The International Committee of the Red Cross, for example, founded in 1863, was an early NGO (even though not labeled as such at the time). This was only the first of many. There are approximately 40,000 international NGOs in existence as of 2007, with an estimated 2 million domestic NGOs in the United States, many of which emerged within the past 30 years.

NGOs tend to perform two primary functions: advocacy and operations. They continue to influence multinational corporations (MNCs) and contribute to local and regional working environments both directly and indirectly. The Rainforest Alliance, for example, has had a significant impact on Chiquita and on how that company does business throughout Latin America. The Rainforest Alliance contacted Chiquita several years ago as part of the Better Banana Project, aimed at enhancing environmental awareness and sustainability. After agreeing to participate in the endeavor, Chiquita worked closely with the Rainforest Alliance and ended by drastically revamping systems and processes. The result is that not only is Chiquita more environmentally conscious today, but it is also generally more socially responsible.

In spite of the invaluable role that many NGOs have played and continue to play, there is still considerable controversy surrounding NGOs more generally. While their influence is often for the benefit of marginalized or vulnerable groups, many NGOs have their own agendas. What they are able to accomplish is limited in that they rely on the voluntary assistance and cooperation of others—NGOs do not enjoy any sort of legal mandate or special authority over those they endeavor to influence and/or protect. Furthermore, while many take seriously their responsibility to those they serve, this is a choice they make—their only real accountability is to those who fund them.

Regardless, they do play a vital role in the fabric of global society. In general, they do not affiliate themselves with a national entity but with a cause that can span geographic borders. Their goals tend toward alleviating some sort of pain or suffering or wrong. In this way, in spite of their alleged shortcomings, their presence is becoming increasingly significant, in terms of both their numbers and the magnitude of their impact.

Business Organizations/ Multinational Corporations

Increased globalization has led to the rapid proliferation of MNCs—organizations whose business operations and/or dealings span at least two countries. In fact, many MNCs do business throughout the world.

Although the presence of MNCs has increased in recent years, the MNC as an entity is not new. The Dutch East India Company, established in 1602, was one of the early MNCs, whose purpose was to fund trade and sponsor the importing of exotic goods to Europe. For nearly two centuries, it represented a powerful force in trade and politics. Not only was it a major player in business, but it also represented the Dutch government in relations with other countries.

Although MNCs today are not generally granted diplomatic privileges, their political importance can similarly rival that of small countries through their ability to influence economic, political, social, and cultural affairs. Whereas in the past, there were a relatively small number of MNCs, globalization has led to the emergence of an increasing number.

MNCs have played an important role in developing business around the globe. MNCs both build and serve international markets. In addition, in many developing and emerging countries, they have also contributed to the development of vital infrastructure, and they have identified and addressed needs where local governments were not situated to do so.

The operation of MNCs is not, however, without controversy. Not all have acted responsibly. In fact, the American public was so embarrassed by a wave of incidents in which American businesses failed to exercise proper discretion that, in the 1970s, the United States responded by enacting the Foreign Corrupt Practices Act (FCPA). This monumental legislation severely restricted the behavior of American businesspeople overseas by preventing them from engaging in explicit bribery, even when failure to do so would place American businesses at a competitive disadvantage. Although the FCPA was initially criticized heavily, it has more recently become the model legislation for the anticorruption movement around the globe.

MNCs continue to confront challenges as they operate across, between, and among national borders—often in uncharted territory. Local laws—particularly in developing or emerging countries—are frequently nonexistent or insufficient and fail to protect the interests of local communities or the MNCs themselves. In addition, the absence of proper regulation leaves them vulnerable to media backlash if their behavior is subsequently questioned.

Even countries in which MNCs operate have been known to resent the presence of these MNCs. MNCs are sometimes viewed as imperialistic as they move in, often without showing adequate respect for local customs and traditions. Their motives are arguably self-serving, and they address only those needs that interest them. As in the United States, where communities often suffer as companies relocate manufacturing facilities away from those communities, this sort of situation can be even more severe when an MNC moves out of a developing or emerging country. In addition, the continued operation of MNCs in poorer countries such as Bangladesh perpetuates poor government practices by creating a false sense of economic security.

Role of Business

As globalization has increased, businesses have taken on new and expanding roles. While business is often viewed as limited to profit generation, new opportunities are being identified for MNCs to generate additional profits as they make other significant contributions to society as well.

Relationship Between Business and Poverty

Globalization makes people more aware of poverty and their ability to help alleviate it. Globalization also enables businesses to contribute to improving the standard of living by creating new markets. In fact, new business opportunities linked to developing and emerging countries often lead to new potential buyers and new categories of products.

There are those who argue, however, that the problem with businesses is that they have traditionally been too focused on the top of the pyramid. If society is viewed as a pyramid, the smallest group at the top comprises the wealthy, while the largest group at the bottom comprises the poor. The University of Michigan scholar C. K. Prahalad argues that there is tremendous opportunity at the bottom of the pyramid—that businesses can both serve social ends and, at the same time, increase profits by targeting the poor.

Many MNCs nevertheless remain resistant to this line of thinking. Many of these companies, such as Levi Strauss and Company, endeavor to contribute to developing and emerging countries, not by changing their business models but by indirectly assisting local populations through their general contributions to local economies. For example, MNCs make valuable contributions by implementing educational initiatives, providing health care, offering job training, developing local infrastructure, and so on.

Despite the perceived potential of globalization, there is also a belief that globalization actually runs counter to improving economic conditions. Joseph Stiglitz argues that globalization has actually exacerbated the disparity between the rich and the poor around the world. In fact, he contends, globalization gives powerful countries the means with which to exploit less powerful countries.

There is also the argument that poverty is not being reduced through globalization at a level commensurate with the degree to which the rich are being made more prosperous. The poverty reduction rates are simply not keeping pace with the growth rates. This is problematic in that it reveals how the apparent positive consequences of globalization mask the underlying shortcomings that should be addressed and not ignored.

It is important to recognize these disparities because it is the only way they can be tackled effectively. The unequal distribution of wealth and resources deprives many of the poor of the means with which they could lift themselves out of poverty. Globalization alone does not solve their problems of lack of access to resources, illiteracy, poor health, and so on, which contribute to their inability to make meaningful contributions to their societies.

Contrary to this is the reality that many countries have emerged from poverty during the past 50 years only because of globalization and the enhanced roles that MNCs and NGOs have taken on. The same is true for China in recent years, as it is becoming a dominant force in the global marketplace.

China is where globalization is now. The same companies that withdrew and/or refused to do business in China in the 1990s as a result of the rampant human rights violations were among the first to reenter the country in the early years of the 21st century. Although there is a view that China has changed its social practices, a more compelling argument is the pragmatic one—that is, that MNCs today simply cannot afford not to be in China; China holds too much of a stake in the global marketplace and workplace as a result of its huge and growing population. In addition, the MNCs in China today tend to assert that the best way they can influence responsible social practices is by being there.

Levi Strauss and Company, for example, has therefore partnered with the Asia Foundation to reenter China. In addition to finding responsible outsourcing partners, through collaboration with the Asia Foundation, the company helps educate and inform workers throughout China.

Global Markeplace

The effect of having China in the global marketplace is proving increasingly profound in that it is changing how companies view their role in the market. Ferrari, for example, is confronting a significant challenge to its business model. The company previously stated that it would never increase its level of production, in spite of increasing demand, to protect the exclusivity of its cars. Demand for Ferrari cars, however, has recently spiked far beyond anticipation. This is in large part due to the increasing affluence in China, which is creating a new, large class of wealthy Chinese businesspeople who are placing orders. This problem of supply and demand is further exacerbated by the steadily growing Chinese population. The challenge Ferrari confronts, along with many others, is how to handle this explosive growth of the global market.

Global Workplace

In addition, the high cost of labor (and benefits) in the United States has arguably forced many companies—such as manufacturers in the apparel industry—to go overseas for labor. Since roughly the 1990s, there has been a trend toward increased offshoring and outsourcing. Offshoring occurs when companies relocate facilities and processes from one country to another—often from the United States or other Western democracies to a developing or emerging country. Outsourcing, on the other hand, is somewhat different in that it involves transferring responsibility for business processes to third parties.

Outsourcing has become particularly controversial during the past decade as media exposés uncovered the questionable, "sweatshop," labor practices endorsed by leading companies such as Walt Disney, Nike, and Wal-Mart. It was argued that these companies violated fundamental human rights by supporting practices such as child labor, excessive working hours, and unsafe conditions.

At the same time, globalization has enabled job creation and specialization. The presence of a global workplace enables businesses to shift their processes to locations where they can find the least expensive, most talented labor pool for the appropriate job functions. As more and more companies take advantage of the global workplace, however, increasing concerns are emerging regarding the loss of jobs in the United States and other Western democracies.

Peace Through Commerce

Increased globalization is also leading to a growing recognition of the connections between business, poverty, and political stability. While people disagree as to whether this correlation is primarily positive or primarily negative, few people deny that the interconnectedness exists.

One view is that business interferes with peace and can lead to political instability. The influx of strong multicultural influences can cause local peoples to lose touch with their own identities. In addition, as the economic landscape changes, this can lead to increased corruption and other negative behaviors. Development of business can exacerbate the economic gaps between the wealthy and the poor and, in some instances, drive the impoverished into greater despair. In the former Soviet Union, for example, there were no beggars until after the economy began liberalizing in the late 1980s and early 1990s. In addition, businesses can also contribute to instability and increased bloodshed by profiting from war. Some companies, for example, are in business to trade in weapons and arm warring states.

These are but a few examples of how increased commerce can have a negative impact on peace. There is also a strong argument that the development of business can help promote stability both by increasing the reliance of countries on one another through global trade and by contributing to local development and the reduction of poverty. Countries that need one another financially are arguably less likely to declare war on one another.

Economic development in the former Yugoslavia offers examples of this. Since the end of the civil war that led to the breaking up of Yugoslavia into separate republics, numerous business relationships have been developed among and between Bosnia, Serbia, Croatia, and Slovenia, for example. People who fought violently against one another just over a decade ago are now sitting down together to move their economies forward.

Korea is also recognizing that although peace has been attained, the situation is delicate. Commercial ties are therefore being developed, arguably in an effort to help cement that peace. An unprecedented event took place in Korea in May 2007. For the first time in more than 50 years, trains traveled across the demilitarized zone from the top of North Korea to the bottom of South Korea—one from north to south, the other from south to north. This signifies potential commercial activity that could cement the established peace. South Korea, in particular, is anxious to create travel and trade opportunities through North Korea into China and Russia to connect with the Trans-Siberian Railway.

The impact of commerce on peace and stability is thus complex and multifaceted and involves both negative and positive potential consequences.

New Business Opportunities

Businesses have quickly seized the opportunity to enter—and exploit when possible—this global marketplace. The Berlin Wall coming down signaled the presence of new markets to which they finally had access. Since the door opened, there has been no stopping the integration of business around the world.

This has also created a more heated business environment, for Western businesses now face the challenge of new competitors that are able to provide the same, or similar, goods and services for lower prices and, sometimes, higher quality. It is inevitable, however, that to remain profitable, more and more businesses are finding it necessary to acquire a global presence.

A problem is that globalization has also exposed businesses to new threats. Facilitation of information exchange has also opened a Pandora's box of intellectual property challenges. It has enabled business rivals in other countries to replicate leading brands and to sell their products at low prices—often without regard for quality. This has arguably caused brand dilution and created a significant threat to new product development.

Globalization has changed the business environment significantly. In many instances, it has lowered costs for the consumer by forcing companies to streamline processes and cost structures in order to remain competitive in a wider marketplace. At the same time, it has opened up new markets for companies to target; even though these companies are now faced with fiercer competition, they are able to reach a larger audience.

In fact, few businesses today—no matter where they are located—enjoy the luxury of being able to compete only locally, particularly as a result of the presence of the Internet and the ease of travel. Globalization has implicitly forced businesses to start thinking on an international scale.

Globalization Controversy

Not everyone agrees, however, that the effects of globalization are entirely positive. Although many people applaud globalization for its numerous positive contributions, there are significant concerns that cannot—and should not—be ignored.

Proglobalization

The argument in favor of globalization is intuitive and largely based on common sense and experience. The positive benefits of globalization are visible: increased communication, lower travel costs, increased product availability and diversity, to name a few. Generally speaking, globalization breaks down the geographic barriers between communities and countries to allow for unfettered trade.

Globalization increases the options available to people around the world. This applies to products and services as well as to ways of life and ideas. It can be argued that globalization is breaking down the barriers between cultures. This translates into a huge benefit for companies, who now have access to much larger markets.

In addition, through globalization, companies around the world are held to a higher degree of scrutiny. This is leading to a greater degree of accountability—for instance, with regard to the responsible treatment of global workers. There is an increasing push around the world today toward standardization of working conditions and responsible labor practices.

Countries are also becoming increasingly accountable for their political choices and legislative policies. As a result of globalization and increased multinational trade, countries are becoming more cognizant of and concerned about what is going on. Iraq, for example, although geographically removed from most of the world's superpowers, has nevertheless become a focal point of contention in recent years.

In fact, globalization can be said to contribute to peace between otherwise warring countries. This is true, for example, with regard to the relationship between India and Pakistan. In spite of their history of tension, ongoing business ties have created de facto sustainable peace between them.

Thomas Friedman, an advocate of globalization, argues that there are still problems but those problems are not insurmountable. For example, in *The Lexus and the Olive Tree*, he points out that it is inevitable that countries relinquish some of their sovereignty to global institutions to contribute to global economic prosperity.

Out of globalization has emerged an implicit, if not explicit, recognition of the interconnectedness of the world and countries' inherent interdependence. This is particularly visible with regard to the sustainability movement, which emphasizes ongoing change with regard to shared resources. Globalization is responsible for bringing diverse people together in common endeavors.

Antiglobalization

Opponents to globalization contend that globalization is, in fact, more destructive than constructive. Whereas many people choose to focus on the new opportunities that globalization affords the wealthy, they seem to overlook the intended and unintended consequences to everyone else. Among others, Joseph Stiglitz, in *Civilization and Its Discontents*, has criticized globalization for not delivering on its promise of economic development. According to Stiglitz, globalization can potentially perpetuate poverty around the world.

The problem—or point of contention—is that certain large companies act as gatekeepers and are able to exert considerable influence even in the absence of explicit political authority. This was true in centuries past for the East India Companies and remains true today for companies such as Wal-Mart. Today, Wal-Mart is criticized for the degree of pressure the company allegedly puts on suppliers. It has been suggested that Wal-Mart exercises de facto control over what products are imported for distribution to its customers.

Cultural imperialism and the homogenization of the world are also major concerns as the presence of MNCs becomes more widespread, particularly in developing and emerging countries. MNCs often fill in the gaps for local governments. In doing so, they are not always respectful of local customs and traditions, which can potentially become undermined as the presence of MNCs becomes increasingly overwhelming.

Interestingly, this also creates dependencies that can leave countries vulnerable. The situation pertaining to oil in the Middle East, for example, is effectively holding the rest of the world hostage. This could also happen with regard to other scarce resources.

Conclusion

The bottom line is that globalization exists. It is here today and will inevitably be there tomorrow. Now that the barriers have been broken down, they will be difficult to re-erect in the foreseeable future. Technology makes this virtually impossible.

Globalization has changed the lens through which many businesses view their identity. Increasingly, many are viewing themselves not just as independent operators or MNCs but as global corporate citizens, and they are voluntarily accepting the social responsibilities of global citizenship as they operate within global workplaces and serve global markets. While not every business views itself in this way, more and more of them are following suit.

—Nadan Sehic and Tara J. Radin

See also Bottom of the Pyramid; Colonialism; Cultural Imperialism; Developing World; European Union; Fair Labor Association (FLA); Foreign Direct Investment (FDI); Free Trade, Free Trade Agreements, Free Trade Zones; Global Business Citizenship; Global Codes of Conduct; Human Rights; International Business Ethics; International Labour Organization (ILO); International Monetary Fund (IMF); International Trade; Living Wage; Maquiladoras; Monetary Policy; Most Favoured Nation Status; Multiculturalism; Multinational Corporations (MNCs); Multinational Marketing; Nongovernmental Organizations (NGOs); North American Free Trade Agreement (NAFTA); Organisation for Economic Co-operation and Development (OECD); Outsourcing; Poverty; Restraint of Trade; Sweatshops; Transparency International; United Nations; United Nations Global Compact; Worker Rights Consortium (WRC); World Bank; World Health Organization (WHO); World Trade Organization (WTO)

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Global Reporting Initiative

The Global Reporting Initiative (GRI) is a project formed in 1997 by U.S.-based Coalition for Environmentally Responsible Economies and the United Nations Environment Program to develop guidelines for sustainability or triple-bottom-line reporting. Sustainability reporting is based on the value of *sustainability*, defined as supporting the continued existence and welfare of oneself and identified others, and *transparency*, that is, being accountable to stakeholders who have a legitimate interest in organizational performance related to sustainable behaviors. The sustainability reporting framework is an expansion of the financial reporting framework that includes an organization's broader economic, social, and environmental impacts.

The GRI's framework for reporting organizational performance is intended to bring greater uniformity and comprehensiveness to sustainability reports. Without a common reporting framework and standards, it is difficult to compare reports from different companies. The GRI is regarded as the most widely known, supported, and comprehensive set of voluntary reporting standards. The process for creating the GRI guidelines involves extensive comment and feedback from representatives of business, accounting groups, investor organizations, activist groups, and other stakeholder representatives.

Over time, it has created a multistakeholder consensus process to develop and pilot test standards before publishing a draft to seek broader input interested groups.

The initial set of GRI guidelines was developed in 2000, and 50 organizations used the guidelines for reporting 2000 performance. Feedback from reporting organizations and users of the initial reports led to the second set of guidelines issued in 2002, and more than 150 organizations used them to report 2002 performance. In that year the GRI became a separate nonprofit organization with headquarters in Amsterdam, the Netherlands. Over the next 3 years, sector-specific supplements were developed for several large industries, including mining and metals, financial services, logistics and transportation, and telecommunications. The number of reporting organizations increased to 325 in 2003, 500 in 2004, 750 in 2005, and at least 950 in November 2006. The third version of GRI guidelines was released in October 2006 after an extensive comment and review period.

Most of the organizations that use the GRI guidelines for sustainability reporting are large multinational corporations that are highly visible global competitors, such as BP, Chevron, Exxon, PEMEX, PetroBras, Shell, Statoil, and Total in the petroleum industry and BMW, Daimler-Chrysler, Ford, General Motors, Nissan, Toyota, and Volkswagen in the automotive industry. A small number of public sector organizations also use GRI guidelines in their sustainability reports, such as Australia's Department of Environment and Heritage, New Zealand's Department of Corrections, and the United Kingdom's Ministry of Defence.

A sustainability report according to GRI guidelines includes information on the organization's strategy, operating profile, and governance and management systems in addition to data on 50 performance indicators related to economic activity, environmental impacts, and social impacts. The social impact category includes human rights, community impact, and product responsibility. In addition to the three categories of performance indicators, two types of integrated metrics are encouraged. One relates to systematic indicators that demonstrate how an organization's activities contribute to the economic, environmental, and social systems in which it operates. For example, a company might report on net job creation as a proportion of total new jobs in a region in which it has operations. The second integrated metric is a cross-cutting indicator, which directly relates two or more dimensions of economic, environmental, and social performance as a ratio. For example, an ecoefficiency measure related to a new technology may indicate the change in air pollutant emissions per increase in production level.

GRI supporters believe that organizations should be motivated to provide sustainability reports to improve relations with their stakeholders. Access to accurate and comprehensive information about its impacts on the economy, the environment, and society should increase the organization's reputation and level of trust that stakeholders have in it. These reports inform decisions beyond those supported by traditional financial reports. For example, a potential investor who is concerned about environmental preservation can more easily ascertain whether the organization is committed to that goal if it uses GRI reporting guidelines. Potential employees can decide whether they want to work for a firm, based on more complete information about employee benefits beyond legal minimums, equal opportunity policies and monitoring systems, and health and safety records. Communities can either welcome or resist an organization seeking to locate a new facility in their midst, based on GRI-provided descriptions of significant environmental impacts of principal products, services, and manufacturing processes.

An unresolved issue related to the GRI guidelines is credibility because few sustainability reports are audited by independent assurance providers. Questions have been raised about the appropriate qualifications and certification of assurance providers because experts in financial auditing are unlikely to have expertise in all facets of triple-bottom-line reporting.

Application of GRI guidelines is likely to expand to include a larger number of reporting companies in the future. These guidelines became linked to the United Nations Global Compact in October 2006 when the two organizations proposed an approach to the 3,000 companies participating in the Global Compact to use GRI guidelines when reporting their performance on the 10 Global Compact principles.

—Jeanne M. Logsdon and Patsy G. Lewellyn

See also Accountability; Coalition for Environmentally Responsible Economies (CERES); Social Audits; Sustainability; Triple Bottom Line; United Nations Global Compact

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Golden Parachutes

A golden parachute is a provision in an employment contract that grants lucrative severance benefits to an executive if control of the company changes hands, as by a merger. Most definitions offered by legal authorities stress three elements: (1) a lucrative or attractive severance package, (2) available to a few selected senior executives, (3) in a change of control situation for the company. Some also define it as compensation to a chief executive officer or other C-level executive for losing his or her job. Others do not so restrict its availability to those who actually lose their jobs, but extend it as well to those who lose job status in the event of a change in control.

In common usage, the term *golden parachute* refers to large severance payments made when a change of control results in job termination. However, for tax purposes, the crucial element is change in corporate control, and the payment need not be to compensate for termination, but could be any type of compensation. It is also useful to distinguish a golden parachute from a normal severance payment. Usually, an employee dismissed for cause does not receive a severance payment, and the same is true when that employee leaves voluntarily. However, even a C-level executive who is fired for cause or simply resigns may receive a golden parachute, depending on the terms of the employment contract.

As a way to further distinguish golden parachutes from severance payments, the amount of a severance payment is based on years of service to the company, while a golden parachute will be based on the individual negotiation between the executive and the company. Even a CEO who serves for a short time period may wind up with a substantial golden parachute.

Scope of Coverage

Golden parachutes are usually included in the contracts for C-level executives (chief executive officer, chief operating officer, chief financial officer, and chief legal officer), but they sometimes appear in the contracts for executive vice presidents and other top officers as well. After the merger between Coors and Molson Companies, 11 top executives at Coors resigned, since they had change-of-control payment provisions in their contracts. None of the Molson top executives resigned, though, as they were not covered by such provisions.

Components

The pay components of a golden parachute may vary widely. It may include not only a cash payout, along with restricted stock or stock options, but also an annual pension, a departure bonus, medical benefits, and administrative and secretarial support. It may also include other imaginative perks, including payment of charitable donations in the executive's name or use of an executive jet.

Amounts

In their golden parachutes, CEOs typically receive two or three times the value of the base salary and bonus, as well as benefits, stock options, and pension payments. Presidents, COOs, CFOs, and other C-level executives typically receive one to two times the base salary, plus bonus, benefits, stock options, and pensions.

Some CEOs have negotiated golden parachutes that have allowed stock options to vest immediately, and thereafter payouts skyrocketed, according to one compensation expert. Some golden parachutes have had a platinum lining. For instance, Michael Ovitz received a severance payment exceeding $100 million from Disney; Phillip Purcell had an exit package of $114 million after his ouster as CEO of Morgan Stanley; and Jim Kilts, CEO of Gillette, received a golden parachute of $165 million after Procter & Gamble acquired his company. Those amounts raise questions of distributive justice, especially since a merger may trigger uncompensated layoffs of lower-level employees.

When a CEO receives a huge golden parachute after the company's stock value has plummeted, that offends shareholders and critics the most and raises questions of deservedness. Henry McKinnell of Pfizer, for instance, was granted a pension package of $83 million before his resignation and after the company had lost 46% of its stock value during his term of office.

Purposes

The original and key purpose of the golden parachute, dating back to the 1970s and 1980s, was to protect CEOs and other top officers in the event of takeovers that might lead to their ouster. They would then enjoy security in a market where other CEO positions might not be readily available and be more willing to take the job initially. Second, a golden parachute might better align the interests of CEOs with those of shareholders. Given the security that golden parachutes provide to CEOs and the compensation for future lost expected earnings, they would have no self-interest in resisting a merger or takeover that might enhance the value of shares, at least on a short-term basis. Top management would not have the incentive to interfere with the market for corporate control that includes potential takeover bids. In fact, some CEOs might view the sale of a company as a crowning event to their careers, and with golden parachutes, the CEOs would benefit both economically and from any positive publicity attending the sale of the company.

Another purpose of golden parachutes might be to deter an unwanted or hostile takeover, since the raider then absorbs the burden of making substantial payouts to the CEO and other senior executives. In that sense, golden parachutes might serve as poison pills and defenses to takeovers. In fact, a company might institute golden parachutes as events triggered by a takeover offer. Furthermore, golden parachutes might serve as recruitment and retention incentives, attracting senior executives to a firm where they might expect a substantial payout some years down the road and causing them to stick with a firm until that eventuality. When other companies have adopted golden parachutes, its defenders argue that an employer must adopt generous packages to keep pace and remain competitive.

Criticisms of Golden Parachutes

A major criticism of golden parachutes is that they entrench existing managers in their jobs by deterring takeovers. In that sense, they subsidize existing management at the expense of shareholders. When the golden parachute is eventually paid, it subsidizes the then departing managers at the expense of shareholders once again. A golden parachute might also constitute a reward for failure when management hastens to sell the company in the wake of a plummeting stock value.

To the extent that adoption of golden parachutes might signal future takeover bids, stock values might increase, benefiting shareholders. However, negative market reaction is even more likely, as golden parachutes often signal to shareholders that additional antitakeover measures will follow to prevent the eventual sale of the company.

Defenders of golden parachutes maintain that they guard the objectivity of management and allow it to best serve shareholder interests by providing an incentive to get top dollar in a sale or auction of the company, rather than protecting their own jobs. To that argument, critics respond that management has a preexisting fiduciary duty to serve shareholder interests and should not require an artificial incentive to live up to their obligations.

Critics also cite instances of "golden bungees," where golden parachutes are abused. Rather than executives simply redeeming their golden parachutes when a change of control occurs, they also jump back into the company in a different position. For instance, when Washington Mutual acquired Providian Financial, its CEO returned as head of Washington Mutual's credit card division, while also receiving his golden parachute. Shareholders oppose this type of abuse and have urged a "double trigger" to control payouts, requiring termination of an executive's employment to trigger the golden parachute.

Legal Controls

In normal circumstances, golden parachutes are completely legal. In abnormal circumstances, however, there could be legal constraints. In a bankruptcy situation, for instance, judges have disallowed golden parachutes as legitimate administrative expenses, while allowing retention pay for a broader base of employees based on years of service.

Directors, especially members of board compensation committees, might be found liable for violating their duties of due care and good faith to shareholders if they exercise insufficient scrutiny of exorbitant severance pay or golden parachutes. Although Delaware Judge Chandler ruled that the Disney board did not violate its fiduciary duty in approving a severance package of over $100 million for Michael Ovitz, who had been fired without cause, the case may have raised the bar for future board conduct. That the court even decided to hear the case indicated growing judicial concern over such pay packages. In his ruling, Judge Chandler acknowledged that the Disney board's approval "fell significantly short of the best practices of ideal corporate governance."

The Sarbanes-Oxley Act reformed accounting controls and oversight, while also mandating other changes in corporate governance, but it had no direct impact on golden parachutes or severance packages. In fact, by prohibiting loans to C-level executives, it might have indirectly created more pressure for lucrative severance packages.

Tax Aspects

There are three components of the internal revenue code that relate to golden parachutes. Section 4999 imposes a 20% excise tax, above and beyond the normal income tax, on "excess parachute payments," while section 280G makes such payments nondeductible to the corporation. Congress passed these provisions as part of the Budget Deficit Reduction Act of 1984. Denying deductibility to the corporation provides an incentive not to provide golden parachutes, and the imposition of an excise tax provides an incentive to the individual executive not to receive them. These provisions apply to the top 250 employees of the corporation, not just to the top executives. Finally, section 162(a) of the internal revenue code denies deductibility of any compensation in excess of $1 million unless it is performance based. Rewarding an underperforming executive with a lucrative golden parachute would trigger that provision.

While the goal of these provisions was to limit the use and amount of golden parachutes, that goal has not been realized. The impulse to both provide and receive golden parachutes persists. Corporations have even used tax gross-ups to circumvent Sections 4999 and 280G and to pay all the taxes of recipient executives, thereby preserving their incentive to receive golden parachutes. Tax gross-ups are very costly to corporations, but they remain willing to pay them in order to provide the incentives of a golden parachute.

Corporate Governance Aspects

Corporate governance relates to golden parachutes similar to the way in which it relates to other executive compensation issues and in the same way it relates to the various components of golden parachutes. The composition and practices of the board compensation committee are important, as are the roles of shareholders in pressing for reforms of executive compensation. Regulations surrounding stock options and restricted stock, often components of golden parachutes, are also important.

Even when CEOs or former CEOs who sit on the compensation committee of another CEO are considered independent, they often approve excessive severance packages and golden parachutes for their fellow CEOs. Hence, boards dominated by outside directors have adopted golden parachutes even more frequently than insider-dominated boards. Studies of social networking also reveal that CEOs with some connection to members of the compensation committee receive larger packages than those lacking such connections.

Where compensation committees do exercise some restraint on pay packages, they do so partly by hiring a pay consultant rather than leaving that up to the CEO. More than half of the top Fortune 100 corporations follow that practice.

Although board directors may adopt golden parachute provisions without shareholder approval, shareholders are exercising downward pressure on golden parachutes in three ways. First, statutory stock options, often a component of such parachutes, require shareholder approval within 12 months of action by the board of directors. Second, shareholder activists sponsor resolutions that call for acceptable levels of benefits. For example, the California Public Employees Retirement System has sponsored proposals calling for shareholder approval of severance packages in excess of 2.99 times the sum of the base salary and bonus. Shareholder resolutions on golden parachutes are among the issues that have garnered the highest percentage of majority shareholder votes, and golden parachutes are among the business practices that correlate most heavily to negative shareholder value. Third, shareholders have withheld votes for directors who sit on compensation committees that grant large severance packages, pensions, or golden parachutes. At Pfizer, for instance, some pension funds and other institutional investors withheld votes for the four directors in 2006 who sat on the compensation committee that approved of the CEO's pension. Such shareholder activism, over time, may reduce the scope and incidence of golden parachute payouts to top corporate executives.

—John M. Holcomb

See also Corporate Governance; Executive Compensation; Market for Corporate Control; Shareholder Activism

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Golden Rule, The

Do unto others as you would have others do unto you. Often referred to as the Golden Rule or the Ethic of Reciprocity, this ecumenical moral principle implores adherents to contemplate the feelings and preferences of fellow human beings before acting. Although the rule finds its prominence in Christian theology through the teachings of Jesus, its origin can be traced back to the Hindu tradition and a pronouncement circa 3000 BCE.

The Golden Rule is contained within the ethical systems of many of the world's most prominent religions such as Buddhism, Christianity, Confucianism, Hinduism, Islam, Jainism, Judaism, Sikhism, Taoism, and Zoroastrianism. Alongside these world religions, many prominent thinkers also incorporate the Golden Rule into their philosophies, including Plato and Socrates. The philosopher Immanuel Kant's categorical imperative disallows personal exceptions unless the same exception can be made for all others in similar situations without an irrational result. Similar to the Golden Rule, this Kantian categorical imperative requires people to think of others as ends instead of a means to an end and also about the consequences stemming from actions. Finally, from a purely secular viewpoint, both anthropology and psychology can claim a nonreligiously motivated origination of the concept of the Golden Rule. An anthropologist may argue that the rule is a cultural variation of the underlying human relationship principle of social reciprocity and that this principle has defined human organizations and human interaction for centuries. Correspondingly, a psychologist may argue that the reciprocity urged by the rule merely reflects the behavioral-cognitive trait of empathy.

But why is the Golden Rule compelling as a moral principle? The morality or immorality underlying a proposed action is not always apparent, and such unanalyzed uncertainty often leads people to act without moral clarity. The Golden Rule is compelling as a moral principle because it requires an actor to undertake a comprehensive ethical analysis *before acting.* First, the actor must analyze the potential consequences of the contemplated action on the primary recipient and assess how the actor would feel if the roles of actor and recipient were reversed. Second, the actor must look beyond the immediate recipient to others who may be remotely affected and assess how the actor would feel if the roles were again reversed. Because the Golden Rule is a moral principle and not a comprehensive ethical system, this sequential thought process will not result in a determination as to whether any particular action is moral or immoral. Such contemplation of consequences will, however, allow people to monitor their actions to determine whether they are acting in a manner consistent with their morals and, theoretically, lead them toward taking moral actions. The application of the rule also allows adherents to more clearly see the commonalities between themselves and others.

The Golden Rule has two common formulations—a positive formulation and a negative formulation. The positive formulation requires people to do unto others as you would have others do unto you. In other words, this formulation tells people what they should do. The negative formulation of the rule—often referred to as the Silver Rule—is do not do unto others as you would not have them do unto you. In other words, this formulation tells people what they should not do. While certain adherents claim that each formulation captures a different moral principle, other adherents claim that the Golden and Silver Rules encompass the same moral principle and need not be separated.

Analyzing the Golden Rule

The Golden Rule is deceivingly simplistic. Literally, the rule requires an actor to treat others in the same way that the actor would want to be treated in a similar situation. Such a literal reading of the rule raises two key interpretative questions. First, who are the "others"? Are they composed only of members of a specific faith community or members of humanity in general? Second, must an adherent strive only *to do good* or must the same person also *strive to avoid evil* although such avoidance of evil is not specifically mentioned in the rule? To address these issues, the Golden Rule has been subjected to the following distinctions: (1) the Complete versus Partial Distinction and (2) the Inclusive versus Selective Distinction.

The Complete Distinction requires adherents to abide by both the positive and the negative formulations of the rule. In other words, an actor must strive to both do good and avoid evil when acting. The Partial Distinction, on the other hand, only requires adherents to abide by the negative formulation of the rule. Therefore, actors must avoid hurting others through their actions but have no obligation to affirmatively help others. This distinction requires adherence to the Silver Rule and not the Golden Rule in its positive formulation.

The Inclusive Distinction of the Golden Rule requires adherents to treat all humanity—not merely members of a specific faith community—in accordance with the rule. This inclusive interpretation can be accompanied by adherence to either the Complete or Partial Distinction of the rule. The Selective Distinction, on the other hand, interprets the rule in such a way that it only applies to a select class of people and not to humanity in general. For example, a Christian adhering to the selective version of the rule need only treat other Christians—or possibly only members of a particular Christian denomination—in accordance with the Golden Rule. The Selective Distinction can be accompanied by adherence to either the Complete or Partial Distinction of the rule.

Criticism of the Golden Rule

The Golden Rule—despite its broad theological, philosophical, and secular acceptance—faces two prominent criticisms: (1) the Social Norms problem and (2) the Social Rules problem. The Social Norms problem results when an action violates a social norm but is nevertheless acceptable under the rule because the actor would not object to the same action if the roles were reversed. For example, an employee enjoying situations where other employees start frivolous arguments—completely unrelated to an employment relationship—acts in compliance with the rule by starting non-work-related frivolous arguments with other employees. Such argument starting violates the generally accepted social norm that it is impolite to start frivolous arguments with others in the workplace while at the same time apparently complying with the Golden Rule.

The Social Rules problem results when a person commits any act that violates an established social rule—such as a state or federal statute—and would not object to a similar violation if roles were reversed. For example, assume that an actor offers nonpublic investment information to a friend in the form of a stock tip and that the offeror would want, or even expect, the friend to reciprocate if roles were reversed. At this point, the offeror is acting in accordance with the Golden Rule but in violation of state and federal law.

Rule adherents argue that the critics' interpretations of the rule violate its spirit—a spirit requiring an actor to consider two aspects neglected by the two problematic actors above: (1) the dignity and consent of all recipients and (2) the secondary recipients as represented by societal segments and not just individuals. Therefore, in the argumentative employee example above, the actor would not adhere to the spirit of the rule by starting frivolous arguments because this action does not take into account the dignity and consent of the recipient—an individual who would not likely endorse this social norm violation. Just as a rational actor would not tolerate invasions of personal dignity and consent, such an actor should not treat others in an undignified and nonconsensual manner. As for the insider trading example, actors must consider that company stockholders are also indirectly affected by this insider stock tip. Therefore, assuming a role reversal, the actor must ponder a reaction as a stockholder harmed by insider trading and not just as the recipient of inside information. With this in mind, proponents argue that both the Social Norms problem and the Social Rules problem would be eliminated if actors complied with the spirit and not merely the literal interpretation of the Golden Rule.

—Corey A. Ciocchetti

See also Christian Ethics; Divine Command Theory; Equality; Jewish Ethics; Moral Rules

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Goodwill

Goodwill as a Disposition

"Goodwill" is a central concept in Western moral thinking. It has several meanings, even already in daily discourse. Common to the various meanings is that the concept refers to something internal to a person and that something is considered to be of moral value. Goodwill deserves moral esteem.

In common discourse, goodwill can first refer to a specific *disposition* of a person. As such, goodwill can be defined as the virtue of being prepared to accept the fair share of a burden, in the context of a situation in which a group of people wants to realize a goal that involves costs of some sort that must be borne by the members. Put briefly, a person of goodwill does not take advantage of others. Thus, we can say that a local library initiative is based on goodwill if people share their books on a voluntary basis without a judicially full proof return system in place.

In its most general meaning, the shared goal may only be deemed good subjectively by the members. A somewhat more qualified employment of the concept differs in this respect. Here, goodwill is necessarily linked to an objectively good moral cause, for which a person is willing to make a sacrifice. The sacrifice may even involve more than his or her fair share. An example of this employment would be to say that "All people of goodwill strive for world peace."

It is in this specific interpretation of goodwill as a disposition that the concept is relevant for the business context. Corporations (or market agents in general) are often called on to show their goodwill in this sense. Objectively good moral causes often mentioned nowadays are, for example, sustainability, nature protection, or the fight against poverty. Thus, oil companies are prompted by nongovernmental organizations to show their goodwill by investing in fuel efficiency, the development of alternative energy sources, wildlife protection, and so forth.

Goodwill as a Motive

The second and arguably the dominant interpretation of goodwill in common discourse employs the concept as referring to the *motive* a person has when performing an act. A person of goodwill in this sense has a "good heart" or "good intentions," morally speaking, when performing a particular act. This means that in acting, this person is actually motivated by morally true or morally proper motives, feelings, inclinations, or reasons. Within common discourse, this concept of properness must be interpreted rather broadly and includes, for example, feelings of sympathy, love, benevolence, a concern for the happiness of all, or a sense of duty. So when a person who is already busy decides to help a friend in need for the sake of (this particular) friendship, we may say that he or she acts out of goodwill. An example of a motivation that typically falls outside the reach of goodwill is self-interest. A person who acts out of self-interest does not act out of goodwill. This is not to say that self-interest must therefore be condemned as bad. In many instances, self-interest is an acceptable motive, morally speaking, but acting out of self-interest is not particularly good or valuable. So when a person who is already busy decides to help another person in need because she expects that this action to pay off in the long run, she is not acting out of goodwill.

Distinguishing Moral Value and Moral Rightness

In understanding goodwill as a concept and why it is so central to Western moral thinking, we must clearly distinguish the moral *value* of an action and its moral *rightness.*

From both a moral and a prudent perspective, society considers it very important that people act in accordance with all moral rules and moral principles. Moral rules and principles have a function in upholding society. A (general) disregard of moral rules and principles will threaten the possibility of society. If people act in accordance with all moral rules and principles, we call their actions morally *right.* Moral *value* is attached to conduct that is morally outstanding or good in the sense that the reasons behind this conduct are contributive to the realization of a society in which all people uphold all moral rules and principles for their own sake or autonomously. Motivations oriented toward this moral goal are true or proper moral motivations.

Crucial to understanding goodwill is to see that a society in which all people act *rightly* does not necessarily—or not even typically—coincide with a society in which people's conduct is morally valuable. People may have a lot of reasons to act morally right—in the sense of acting in accordance with moral rules and principles. They may, for example, worry about their reputation, fear legal punishment (if a moral rule also is a legal rule), or figure that some benefit will emerge from the act, such as a reward or the admiration of a person one wants to impress. Moral rightness—in the sense specified—therefore is not directly or necessarily morally valuable. Moral value arises only if a person is moved by a true moral motivation.

Taken the other way around, it also holds that the moral valuableness of an act does not imply that the action also is morally right. Sometimes action done out of goodwill is based on poor judgment or has terrible consequences. Still, the implications of moral value for moral rightness are more complex. Or perhaps it is better to say that there is some reasonable moral disagreement as to this issue within Western moral thinking. Some people maintain that the moral value of an action has no implications whatsoever for its moral rightness (e.g., because they hold that only the principle is relevant here that says that only consequences count). Others maintain that goodwill does affect the rightness of an action, even if its origin in goodwill cannot be a sufficient reason to determine an action right.

Good Intentions in the Business Context

The issue of goodwill and the related distinction between moral rightness and moral value is vital for understanding the complexities of contemporary discussions in business ethics, especially in relation to a phenomenon such as corporate social responsibility (CSR). CSR can be understood as the appeal to corporations to act out of goodwill. It can also be understood—or at least is often understood—as the appeal to corporations to act morally right. These two conceptions do not amount to the same thing. That is why sometimes corporations that make quite an effort in terms of advancing sustainability as a goal are still accused of window dressing or are treated with great suspicion by the public. Acting right does not imply acting in ways that are morally valuable and the public may think that this particular company is only acting the way it does out of self-interest.

Kantian Interpretation

Goodwill is not only part of the Western common discourse on morality. It is also the subject of philosophical investigation. A specialized philosophical account of goodwill has been worked out most notably by Immanuel Kant (1724–1804). His account has been very influential, even for our common understanding of goodwill.

Kant defined goodwill in terms of a pure motive for action. Persons of goodwill thus do not just act in conformity with rules and principles. They act out of a sense of duty in every situation in which it is necessary. This means that they are rationally committed to upholding moral rules and principles out of respect for morality.

Comparing the Kantian conceptualization with the common usages of the concept as motive shows that Kant's interpretation of what constitutes an appropriate motive is much more confined than common discourse on the subject. In common discourse, feelings such as benevolence and love can be considered to be included in goodwill. Within the Kantian account only the rational commitment to morality is accepted as goodwill. Still, Kantian goodwill is not something elitist. According to Kant, any person can acquire goodwill.

Kant was not very articulate on the issue of how goodwill relates to the moral rightness of an action. He seemed to believe that a person of goodwill also acts morally right, except perhaps in exceptional cases. This rather astonishing view is often explained by pointing out that Kant lived in a morally speaking homogeneous society. He was not bothered by the problem of moral pluralism that troubles even the persons of goodwill in our day and age.

—Wim Dubbink

See also Autonomy; Corporate Social Responsibility (CSR) and Corporate Social Performance (CSP); Duty;

Free Will; Kantian Ethics; Neo-Kantian Ethics; Pluralism; Self-Interest; Virtue

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Government Accountability Office (GAO)

The Government Accountability Office (GAO) is an agency of the U.S. federal government that reports to Congress and bills itself as independent and nonpartisan. Founded in 1921 as the General Accounting Office, its was renamed the Government Accountability Office (GAO) in 2004.

The GAO is assigned to monitor various governmental agencies and their expenses. It studies the effectiveness of governmental expenditures, focusing primarily on the executive branch. The GAO seeks to make government more accountable and effective in managing programs and spending tax dollars. The current budget for the GAO is approximately $500 million per year, and the office has a staff of slightly more than 3,000 people.

Because the GAO principally monitors the programs of the executive branch, it is specifically removed from the purview of the executive. The comptroller general of the United States heads the GAO. A special congressional committee recommends candidates for controller, the president nominates the controller, and the Senate confirms the controller for a single term of 15 years. The professional staff of the GAO is organized into teams such as “health care,” “defense capabilities,” and “acquisition and sourcing management.” The GAO is headquartered in Washington, D.C., and has 11 other offices in major cities across the United States.

As examples of its work, the GAO has recently issued reports on federal farm programs, crop insurance, the food stamp program, bankruptcy reform, Hispanic representation in the federal workforce, nuclear security, human trafficking, and intercollegiate athletics. All of the GAO’s reports appear on its Web site, and the public may request free printed copies of the reports as well.

The creation and dissemination of such a wide range of studies requires a variety of professional staff members, and the GAO offers career paths for analysts, information technology specialists, financial auditors, economists, attorneys, and communication analysts. It is not at all unusual for the GAO to issue a report on some highly technical practice of government; maintaining such a capability requires the GAO to have a staff of experts in many fields.

In spite of a long and generally well-maintained reputation for objectivity, the GAO does come under repeated criticism. Critics generally object to findings in specific reports rather than to the overall quality or objectivity of the agency. Nonetheless, conflict with Congress did lead to a significant reduction in the budget and staffing of the GAO; 2007 budget and staffing levels were about 27% lower than the peak levels of 1995.

—Robert W. Kolb

See also Campaign Finance Laws; Certified Public Accountants (CPAs); Cost-Benefit Analysis; Environmental Protection Agency (EPA); U.S. Bureau of Economic Analysis; U.S. Department of Justice; U.S. Food and Drug Administration (FDA); Whistle-Blowing

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Grasso, Richard (1946–)

Richard A. (Dick) Grasso, born in 1946, is well-known as the former chairman and chief executive of the New York Stock Exchange (NYSE) from 1995 through 2003 before being asked by the NYSE board of directors to resign in a high-profile compensation controversy.

Grasso overcame an improbable background to rise to one of the most powerful positions in the financial world. After dropping out of college and spending 2 years in the U.S. Army, Grasso was hired by the NYSE in 1968 as a floor clerk making $82.50 per week. Working primarily in customer service and marketing, Grasso (who first became interested in the stock market as a teenager and purchased his first shares of stock with money earned working in a pharmacy) immersed himself in the history, operations, and traditions of the NYSE, gaining a reputation of a quick study, hard worker, and outstanding marketer in spite of his modest education. After spending 27 years rising through the ranks, the NYSE named Grasso chairman and chief executive of the NYSE on June 1, 1995. Grasso became the first staff member in the NYSE's more than 200-year history to rise to the top position, a feat made even more surprising with Grasso's lack of a college degree.

During Grasso's tenure at the NYSE, the stock market experienced a period of unprecedented growth that dramatically enhanced the relevance of the NYSE in American business society. As chairman and CEO, Grasso pushed relentlessly to improve and expand the NYSE. He focused on bringing state-of-the-art technology to the NYSE trading, regulatory, and administrative operations and increased the visibility of the NYSE by increasing the number of the companies (especially international companies) whose shares were listed on the "Big Board" at the NYSE. In 2001, in the aftermath of the September 11, 2001, terrorist attacks, Grasso became a reassuring public face for the American stock market and successfully led the restart operations of the NYSE.

Despite his personal success story and recognized strong leadership of the NYSE, Grasso is best known for a scandal involving his compensation. In September 2003, it was revealed that Grasso had been given a deferred compensation package worth reportedly between $140 and $187.5 million by the board of directors of the NYSE. This compensation package caused immediate controversy because the handpicked members on the compensation committee came from NYSE-listed companies over which Grasso had regulatory authority as head of the NYSE. After criticism of the deal by the chairman of the Securities and Exchange Commission and several pension funds, the NYSE board voted to ask for Grasso's resignation, which he submitted on September 17, 2003.

Subsequently, on May 24, 2004, Elliot Spitzer, the New York attorney general, sued Grasso (along with the NYSE and one of its directors) citing violations of New York's Not-for-Profit Corporation Law in awarding Grasso an excessive compensation package. The suit asked a state court judge to rescind the pay package and to determine a "reasonable" level of compensation for Mr. Grasso. The suit alleged that (1) the NYSE board of directors was misled on various aspects of the Grasso's compensation package; (2) the compensation formula that resulted in the $187.5 million compensation package was flawed and under Grasso's control; (3) the compensation was not reasonable under New York state law for a nonprofit organization; and (4) Grasso's dual role as a regulator and NYSE employee raised an impermissible conflict of interest. On May 26, 2004, Grasso, in turn, sued the NYSE and its Chairman John Reed seeking payment of unpaid portions of his pay package, as well as damages for "besmirching his name." Both these cases are still pending.

—Stephen R. Martin II

See also Corporate Governance; Executive Compensation

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Great Depression

The Great Depression was an economic downturn of unprecedented proportions. The stock market crashed, unemployment soared, banks closed their doors, spending on goods and services plummeted, and industrial production went into a tailspin. It is still looked on as a watershed event in our society that ushered in new philosophies and programs relative to the role of government in a market economy. To even begin to understand the depth of this economic downturn, it must be seen against the prosperity that existed just prior to the depression itself.

The period between World War I and the Great Depression was one of unprecedented prosperity. Many people became new millionaires, the stock market soared, and production of goods and services increased dramatically. The United States emerged from World War I economically and physically undamaged, giving it an advantage in world markets. Mass production methods were employed in many industries increasing production of goods and services. Several major new products, such as automobiles and electric power, created many new jobs and markets. Installment buying became popular and, coupled with the widespread use of advertising and new sales techniques, stimulated consumption of these products. Enormous profits could be made in stock market speculation, and low margin requirements made it possible for many people to participate. There were thus many reasons for this prosperity.

All this ended, however, when the bottom dropped out of the economy in 1929 with the start of the Great Depression. Statistics tell only part of the story. Unemployment soared to almost 25% of the workforce, affecting more than 12 million of 52 million workers in a nation of almost 122 million. Consumption spending slid by one fifth, and investment collapsed entirely. Waves of panic struck the banking system from 1930 through 1933, forcing more than 9,000 banks with deposits of $7 billion to close their doors. More than 9 million savings accounts were lost, and thousands of businesses went bankrupt. Panic selling hit the stock market and paper fortunes were lost overnight when the crash began.

There is still debate over the causes of such a drastic change in the fortunes of the country, but several emerge as major reasons for the collapse. The soaring stock market, for instance, was more the result of speculation than of increases in real physical wealth, and low margin requirements encouraged such speculation. People borrowed heavily to buy stocks and participate in the rise of the market. When the psychology of the market changed and investors sensed it had reached a peak, they began selling to get their money out of the market. Panic quickly set in, and the whole speculative structure collapsed rapidly.

The prosperity of the late 1920s was not shared by society's agricultural sector and working classes. Farm purchasing power steadily deteriorated throughout this period, aggravated by the inelastic demand for farm products. Coupled with this problem was a bad and worsening distribution of income. Most of the money in the 1920s went to those who were already wealthy rather than to workers with lower incomes. Smaller proportions of total income went toward wages and salaries. Much of the money received by the wealthy was reinvested in new productive facilities, causing an overextension of factory capacity. People simply could not buy all that the economy was producing.

The Smoot-Hawley tariff, passed by Congress in 1930, further aggravated the situation. Its very restrictive provisions caused other countries to pass retaliatory tariffs. This action curbed our exports to foreign countries when such markets were badly needed. With the decline of both domestic and foreign markets, business investment was sharply curtailed, and layoffs of workers increased. Finally, the Federal Reserve System adopted a restrictive monetary policy during the late 1920s, which some scholars believe was the major cause of the depression. This action cut off credit to business and resulted in lagging business investment through the end of the period immediately before the crash, further aggravating an already deteriorating situation.

Whatever the real causes of the depression, the long-term effects are quite clear. Franklin Delano Roosevelt won the election of 1932 by promising a new deal for the American people. This New Deal consisted of a series of public policy measures that was unprecedented in American history. The federal government assumed responsibility for stimulating business activity to escape the depression and correct abuses in the economy. It sought to relieve the distress being felt by business, farmers, workers, homeowners, consumers, investors, and other groups. In the famous 100 days following Roosevelt's inauguration, an unprecedented amount of emergency legislation was passed that plunged the federal government deeply and unalterably into the affairs of society and the economy. In all, during Roosevelt's first 2 years in office, 93 major pieces of legislation were passed that directly affected banking, business, agriculture, labor, and social welfare.

The depression was such a shock to the self-confidence of the nation and the distress it caused was so widespread that people were not willing to wait for the market to correct itself. The traditional view of an inherently self-correcting market system proved bankrupt to deal with the problems of the depression. People, including business leaders, wanted action, and they wanted it immediately. Many believe that Roosevelt, instead of being an enemy of the free market, actually saved the system and prevented a radical reform movement from gaining headway in moving the country toward some form of socialism. Roosevelt himself saw the New Deal as a set of programs to save the free-enterprise system by fusing welfare benefits and market reforms to a capitalist foundation.

Whether all this New Deal legislation actually pulled the economy out of the depression is a matter for debate. Unemployment never recovered from its 1929 low and gross national product in 1939 had barely attained its 1929 high. Some historians believe that the depression actually lasted until World War II when the war production period began. Although Roosevelt managed to restore confidence in democratic institutions and the American market by installing a more regulatory and welfarist federal presence, it appears that spending for rearmament before and during World War II was instrumental in bringing the Great Depression to an end.

—Rogene A. Buchholz

See also Capitalism; Economic Growth; Federal Deposit Insurance Corporation (FDIC); Federal Reserve System; Laissez-Faire; Market Failure; Monetary Policy; Unemployment

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Greenhouse Effect

The *greenhouse effect* is a term used to describe the trapping of heat in the earth's atmosphere that would otherwise escape into space. A naturally occurring greenhouse effect is essential to support life on earth because some heat is needed to maintain temperatures conducive to plant and animal survival. However, too much heat that is kept within the atmosphere because it is absorbed by the so-called greenhouse gases can lead to global warming. It is this problem of escalating concentrations of greenhouses gases that is typically linked to the greenhouse effect.

Most climate scientists now believe that increasing concentrations of greenhouse gases are a significant cause of climate change and global warming, and that these increases are due in large part to human activity rather than resulting from natural climate cycles. Assessment reports of thousands of climate research studies were issued by the Intergovernmental Panel on Climate Change (IPCC) in 1990, 1995, and 2001 and indicated that greenhouse gases are increasing in concentration, that climate changes are actually occurring, and that human activity is linked conclusively with increases in carbon dioxide, the most significant greenhouse gas. Based on a growing consensus within the scientific community and growing alarm by the general public, governments have begun to institute policies and programs to reduce the growth of greenhouse gases and meet the goals found in the Kyoto Protocol.

At the same time, controversies have continued since the late 1970s about the nature of the scientific phenomenon itself and its potential environmental, social, and economic impacts. A small group of scientists and other skeptics believe that what is labeled as the greenhouse effect is part of long-term natural climate cycles or that a warming climate will not have the dire consequences that supporters of the greenhouse theory predict. They point out evidence that climate changes have occurred regularly in the past without any suspected human cause, and that adaptation by plants and animals, including humans, has accounted for much of human history. The critics caution that some recommendations to address perceived climate change are unnecessary and economically inefficient because the costs of reducing greenhouse gases are high relative to the benefits achieved.

The Scientific Evidence

Concerns about the greenhouse effect began to be raised in the scientific community in the mid-1970s when measurements of carbon dioxide concentrations over a relatively short time period, 1958 to 1975, indicated an increase of 7%. Potential consequences of such increases were hypothesized, and a flurry of research studies and conferences sponsored by the U.S. Department of Energy, the National Academy of Sciences, and the World Meteorological Organization brought attention to the possibility of global warming to the environmental community and policy makers. It is important to note that life on earth exists because of the balance between the amount of solar radiation coming in to warm the atmosphere and the planet and the amount of infrared heat that leaves the atmosphere. The presence of some amount of naturally occurring greenhouse gases (water vapor, carbon dioxide, methane, nitrous oxide, and ozone) is essential to absorb part of the infrared heat and redirect it back toward earth. This is the naturally occurring greenhouse effect, and accounts for why earth can sustain life while the moon and other planets cannot. However, increasing amounts of greenhouse gases are believed to disturb the balance by absorbing even higher amounts of infrared radiation, thereby leading to higher temperatures and potentially devastating environmental and social impacts.

The role of human activity in increasing concentrations of greenhouse gases has been the subject of scientific study and debate for several decades. The now-conventional theory is that prior to the Industrial Revolution, human activity added very little to greenhouse gas concentrations, but with technological advances and industrialization came an escalation of energy use and population growth. Evidence in support of this theory comes from scientific studies reported by the IPCC in its 2001 assessment report on greenhouse concentrations. The IPCC supported the research findings that between 1750, just before the beginning of the industrial period, and 2000, carbon dioxide had increased in the atmosphere by 35%, methane by 143%, and nitrous oxide by 18%. Furthermore, it stated that human activity was conclusively linked to these increased concentrations.

The greatest contributor to higher greenhouse gas emissions is carbon dioxide from the use of fossil fuels for energy (about 85% of U.S. greenhouse gas emissions). Coal and petroleum release the highest amounts of carbon dioxide and somewhat lower amounts of natural gas. Electricity generation, transportation, and industrial processes are the heaviest users of fossil fuels. Population growth and increasing population density play a role not just because of the increase in demand for energy but also because of the destruction of forests that absorb billions of tons of carbon annually.

The consequences of the greenhouse effect are uncertain in terms of timing and magnitude because climate is extremely complex to model. It is expected that higher average temperatures will cause more precipitation as glaciers melt but some areas will experience severe drought. Growing seasons are likely to be affected as weather patterns shift. Sea levels will rise and existing coral reefs will die as ocean temperatures increase. Some species will benefit, while others will not. Best-case and worst-case scenarios continue to be refined but it is too soon to know how severe the environmental impacts of the greenhouse effect will be.

A substantial consensus about the nature of the greenhouse effect exists within the scientific community. For example, in 2005 the national science academies of 11 countries (Brazil, Canada, China, France, Germany, India, Italy, Japan, Russia, the United Kingdom, and the United States) issued a joint statement declaring that significant climate change is occurring, that greenhouse gases are a major cause of climate changes, and that immediate actions should occur to reduce greenhouse gas concentrations.

Criticisms of the nature or the dangers posed by a greenhouse effect continue to be expressed by a few scientists, policy makers, and free-market-oriented analysts. For example, the MIT meteorologist Richard Lindzer accepts some of the scientific evidence related to the greenhouse effect, such as that carbon dioxide concentrations and temperatures are rising, but he disputes the connection between the two and does not believe that human activity has much impact on these increases. Think-tank analyst S. Fred Singer is skeptical of the temperature and chemical concentration data collected in climate studies. He views some global warming as beneficial rather than detrimental to human populations. Both are highly critical of the alarmist rhetoric of environmental interest groups and the media.

Business Responses

Business responses to the potential for climate change have been mixed. Most companies in the fossil fuel and automobile industries have been reluctant to publicly accept the scientific consensus, but the companies that have done so have enhanced their reputations for being environmentally responsible. Many firms in other industries are investing heavily in energy conservation and converting to alternative sources of energy. The insurance industry has indicated its support for the greenhouse effect by incorporating the potential for climate change and more volatile weather patterns into risk assessment models.

Voluntary U.S. business responses have had some impact on reducing greenhouse gases. While the nation's gross domestic product rose by 51% between 1990 and 2004, the total U.S. greenhouse gas emissions increased 15.8%. This far exceeds the U.S. Kyoto goal of a 7% decrease from 1990 greenhouse gas emissions, but it is much less than would have occurred in the absence of voluntary business actions. The U.S. Environmental Protection Agency coordinates a number of energy efficiency programs, including Energy Star to promote energy-efficient products and buildings and the Climate Leaders program of about 100 U.S. corporations and nonprofit organizations that have committed to substantial reductions in greenhouse gas emissions. For example, chipmaker Intel Corporation has committed to a 30% reduction in greenhouse gas emissions per production unit between 2004 and 2010. Raytheon has pledged a 33% reduction per dollar of revenue between 2002 and 2009.

While uncertainties continue about the magnitude and timing of the impacts of climate change, the precautionary principle recommends that risk of serious harm be minimized. Based on the scientific evidence gathered to date, greenhouse gas reduction strategies are likely to grow in importance over the next decade.

—Jeanne M. Logsdon

See also Commons, The; Emissions Trading; Environmental Protection Agency (EPA); Externalities; Global Business Citizenship; Green Marketing; Kyoto Protocol; Pollution

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Green Marketing

Green marketing refers to a broad range of activities designed to generate and facilitate any exchanges intended to satisfy human needs or wants, with minimal detrimental impact on the natural environment. It involves adopting resource conserving and environmental friendly strategies in all stages of the value chain. Other synonymous terms such as *sustainable marketing* and *environmental marketing* have also been used to denote this term. They are perceived as cost-efficient, effective, and just tools of handling problems related to the impact of economic activity on the environment and are often a means of sustainable competitive advantage.

Several companies have proactively implemented green marketing programs to improve their business offerings in several different ways. Some recent notable examples follow:

- British Petroleum has committed to spending $350 million on energy-efficient products over several years and is aggressively promoting its environmental awareness programs.
- General Electric is spending $1.5 billion on its *Ecoimagination* in researching for less polluting technologies and promoting them as well.
- Starbucks recently announced the donation of $10 million over the next 5 years for clean drinking water around the world through the sale of its Ethos bottled water. The company already offers coffees that offer fair pay for growers and environmentally sound cultivation.
- 3M encourages employees to participate in its Pollution Prevention Pays program. Since 1974, the program has eliminated over $2 billion pounds of air, water, and solid waste pollutants from the environment.
- The largest home and garden center chain, Home Depot, has discontinued the sale of wood products from endangered forests since 2002.

In addition to firms, major global bodies such as the United Nations have urged better "green" planning by asking cities to hold tree plantings and cleanups throughout the world. Even buildings, such as the presidential library for Bill Clinton, offer a "green" focus and feature environmentally friendly construction. Industry-based associations are actively encouraging green marketing programs—the U.S. Green Building Council is responsible for certifying and promoting environmentally responsible and high-performance buildings, while the Green Seal organization awards green seals to products that meet rigorous environmental standards, which in turn helps consumers identify products that are environmentally safe.

History of Green Marketing

Although a major focus on green marketing began in the last three to four decades after the publication of Rachel Carson's *Silent Spring*, the history of green marketing in the modern era can be traced back to the 18th century when Benjamin Franklin urged France and Germany to follow England's practice of switching from wood to coal, which had saved what remained of their forests. Franklin also attempted to regulate waste disposal and water pollution in Philadelphia. He also left money in a widely publicized codicil to his will to build fresh water pipeline to Philadelphia due to links between bad water and disease, which ultimately led to the city's water department to be the first (in 1801) in America to supply drinking water to all its inhabitants.

The American Marketing Association held its first conference on ecological marketing in 1975 that attempted to bring together academics, practitioners, and public policy makers to examine marketing's impact on the natural environment. Concern for green marketing has escalated since the 1980s and 1990s after the growth of environmental ills such as ozone layer depletion, oil spills, and overflowing landfills. Since then, the U.S. Federal Trade Commission and the National Association of Attorneys General have been very active in monitoring green marketing claims as well as developing extensive documents examining green marketing issues.

Motivations for Green Marketing

There are several motivations for companies going green. Michael Jay Polonsky identifies five major reasons for firms' increased use of green marketing. They are as follows:

Lower Costs or Higher Profitability

Disposing of harmful by-products has resulted in substantial cost savings in many firms. In trying to minimize waste, firms often stumble across more efficient production processes that eliminate the need for some raw materials, thereby reducing costs. In other cases, instead of minimizing waste, these materials serve as another firm's input to production processes. Finally, developing more efficient new industries, for example, using oxygen instead of air in making steel, can enhance cost or profitability.

Competitive Parity

To keep up with the benchmarks set by the competitors, firms may try to emulate their environmental marketing position; for example, a manufacturer may stop deforestation in a sensitive area in response to a major competitor's similar action or a tuna manufacturer may stop using driftnets by following others.

Commitment to Social Responsibility

Many firms are beginning to realize that they are members of a broader global community and, therefore, must meet environmental objectives in addition to their profit-based objectives. As such, they take a proactive approach to embracing a philosophy of environmental social responsibility in their overall firm's culture. Some, such as the Body Shop and Ben and Jerry's, heavily promote their involvement in green marketing initiatives, while others such as Coke and Walt Disney World practice this philosophy and yet choose not to publicize it as much.

Consumer Demand

Several surveys have shown that both individual and organizational customers in most countries are becoming more concerned about their natural environment and are demanding firms to be responsive to these concerns. Photocopier companies such as Xerox, for example, introduced a "high-quality" recycled photocopier paper in an attempt to fulfill demands for less environmentally harmful products.

Governmental Pressure

Finally, governmental pressures are also being designed to "protect" consumers by reducing production of harmful products or by-products, modifying consumer and industry's use and/or consumption of harmful goods, or ensuring that consumers have the required information in evaluating the environmental composition of goods. Governments regulate the control of hazardous wastes, while most by-products are controlled through the issue of appropriate licenses. They modify consumer behavior by "inducing" consumers to participate in voluntary curb side recycling programs, or in other cases taxing them for irresponsible behavior. In the United States, agencies such as the Federal Trade Commission protect consumers by regulating misleading claims, thereby enabling them to make better-informed decisions.

Profiling Green Consumers

There are many ways of segmenting green consumers. For example, J. Ottman Consulting identifies three types of green consumers: "planet passionates," "health fanatics," and "animal lovers." Planet passionates are committed to maintaining a healthy environment and avoid waste and products with poor environmental records. Health fanatics, on the other hand, try to maintain a healthy diet and lifestyle by taking precautions against toxic waste, pesticides, sun exposure, and other environmental problems that might affect their health. Finally, animal lovers protect the rights of animals through vegetarianism, buying products labeled as "cruelty free" and "not tested on animals," and boycotting products such as fur and tuna.

Marketing research firm Roper ASW on the other hand divides the total population into five segments, out of which two segments are likely to buy green. "True blue greens" (9% of the population) are wealthy and educated and include environmental activists and leaders; "greenback greeners" (6% of the population) also share the same characteristics, yet are not always likely to sacrifice the comfort and convenience for the sake of the environment. Roper ASW publishes the Green Gauge Report about consumers' willingness to pay for green products, thus helping companies target their marketing strategies.

Finally, Ginsberg and Bloom have suggested that companies should follow one of four green marketing strategies depending on market and competitive conditions, that is, from the relatively passive and silent "lean green" approach to the more aggressive and visible "extreme green" approach—with "defensive green" and "shaded green" in between to be better prepared in helping their companies choose the most appropriate environmentally friendly approach to marketing.

Greening the Supply Chain

Greening the supply chain refers to firms integrating environmental issues within the new product development process, which include predevelopment activities, supplier's business practices, and product design and development. Environmental responsive companies take proactive posture in requiring a significant level of environmental responsibility in core business practices of their suppliers and vendors. Many companies have even begun taking a more proactive stance in ensuring compliance of their suppliers at the second- and third-tier levels. General Motors (GM) in a recent media release perhaps articulated it best, when they said that working with their suppliers, they can accomplish much more to improve the environment than GM could alone. Empirically, there is demonstrated evidence of a proactive supply chain management role in corporate greening and environmental strategies.

Suppliers too benefit by seeing greater operational efficiencies, cost savings, enhanced value to customers, increased sales, positive media attention, and positive ratings from socially responsible investment groups.

A recent report on the suppliers' perspectives on effective supply chain management strategies prepared by Business for Social Responsibility Education Fund talked with representatives from 25 suppliers in four industry sectors, that is, automotive, business services, electronics, and forest products, and found that an increasing number of companies are seeking to influence their suppliers' environmental practices. The types of environmental issues that firms are seeking to address with their suppliers varied by sector. Firms in the automotive and electronics sector received the most environmental requests from suppliers, while those in the forestry sector had mainly received requests to explain their environmental practices. The service sector had received the fewest environmental requests—most such requests came from the larger firms. Greening the supply chain themes include environmental responsiveness of top management, environmental policy, early product development activities, design for environment and life cycle assessment, cross-functional environmental coordination, supplier involvement, environmental database, specialist environmental knowledge, and environmental benchmarking.

Research Findings, Caveats, and Conclusion

The impact of green marketing on both marketing performance and consumer behavior has been thoroughly investigated. For example, research has shown that the market value of a firm declines slightly when green marketing initiatives are broadcasted. Announcements related to green products, recycling efforts, and appointments of environmental policy managers had insignificant effect on stock price reactions, while promoting green marketing produces significantly negative stock price reactions.

Consumers who have a positive attitude toward ecologically conscious living and negative attitude toward pollution are likely to buy green products. Further findings substantiate what is known as the "4/40" gap: Roughly 40% of consumers say they are willing to buy green products, but only 4% actually do. Environmentally conscious behaviors are most likely to occur when consumers perceive that their actions are likely to make a difference.

One must also be wary of "greenwashing" practices, which involves disinformation disseminated by firms so as to present an environmentally responsible public image. Such practices are usually promoted through the use of image ads, misleading product labels such as "all natural," "biodegradable," "organic," and so on, as well as public relations tactics such as having hollow mission statements and codes of conduct, sustainability reports offering only partial disclosure, hiring scientists who vouch for industry-funded research, feigning public support for hidden anti-environmental agendas as some major examples. Industry ombudsmen such as the Green Business Network and Green Life attempt to monitor and expose such practices and keep the public informed about what is legitimate and what is not. Green marketing can be a very useful and successful strategy for firms as long as they comprehend the underlying motivations of customers in choosing environmentally friendly products.

—Abhijit Roy

See also Agribusiness; Agriculture, Ethics of; Biodiversity; Environmental Ethics; Environmentalism; Environmental Protection Agency (EPA); Environmental Protection Legislation and Regulation; Global Business Environments; Greenhouse Effect; Green Revolution; Green Values; Pollution Externalities, Socially Efficient Regulation of; Sustainability; World Wildlife Fund

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Green Revolution

The *green revolution* can refer to any major and innovative change in agricultural productivity, but more commonly the term is used to identify the radical changes in agricultural productivity that occurred in the middle and late decades of the 20th century. Historians sometimes speak of three agricultural revolutions. The first was prehistoric and occurred when humans first established relatively permanent settlements in which domesticated animals and farming replaced hunting and gathering as the primary food production. The second, beginning in the late 18th century, was fueled by advances in mechanical technology, land reform, as well as better understanding of animal breeding and crop rotation. The resulting revolutionary increase in productivity provided food for the exploding urban centers of the Industrial Revolution. In each of these first two agricultural revolutions, the growth in food production was caused primarily by a growth in the amount of land under cultivation.

The third revolution, what is more typically identified as the green revolution, occurred in the latter half of the 20th century when advances in plant genetics created higher-yielding varieties of crops, chemical fertilizers increased fertility, pesticides decreased losses, and industrial production methods and technology increased efficiency. The resultant increase in agricultural productivity was indeed revolutionary. Unlike the first two agricultural revolutions, the green revolution was fueled by increasing productivity from land already under cultivation rather than an increase in cultivated land area itself.

By the middle of the 20th century, population growth, especially within the world's poorest countries in Latin America, Asia, and Africa, threatened to overwhelm agricultural production. At mid-century, Mexico, with support from the Rockefeller Foundation, embarked on a program designed to increase agricultural production of grains such as wheat and rice. Through a combination of innovative plant breeding and improved farm technologies, Mexico went from a wheat importer to a wheat exporter within a decade. American scientist Norman Borlaug was credited with much of this work, and for this he received the Nobel Peace Prize in 1970.

This green revolution relied heavily on the creation of hybrid varieties that produced significantly improved yields per plant. Hybrids were developed that were better able to absorb fertilizers and nutrients, better adapted to local climate conditions, better able to resist pests, and were easier to grow, harvest, and transport.

Advances in agricultural and mechanical technologies contributed significantly to this revolution as well. While mechanized cultivation and harvesting had existed for several decades, by the middle of the 20th century this technology provided major and unprecedented improvements in cultivating, planting, weeding, fertilizing, and harvesting crops. New chemical fertilizers increased crop yields significantly, and new pesticides and herbicides reduced crop loss proportionately. Improved irrigation techniques contributed much to this revolution as well.

These technological advances resulted in an increase in agricultural productivity that was truly revolutionary. Yet these scientific and technological changes created social and ethical challenges that, if anything, have only increased over time. These present controversies have an historical precedent.

In 1798, early enough in the midst of the second agricultural revolution that its effects were not yet understood, economist Thomas Malthus published *An Essay on the Principle of Population, as it Affects the Future Improvement of Society.* Malthus famously predicted that population, advancing geometrically, was fast outpacing the food production, which advances arithmetically. Malthus predicted that poverty, famine, disease, and conflict would inevitably result unless humans consciously took steps to control population. Malthus failed to realize that he was living in the midst of the very agricultural revolution that would falsify his predictions.

Similarly, in 1972 the well-known Club of Rome report, *Limits to Growth,* predicted dire consequences if trends in resource use, population, pollution, and industrialization continued unchanged. Yet food and materials production over the following decades not only kept pace with population but made some real and significant gains. Some contemporary observers claim that those predictions of environmental disaster suffered from the same mistake that Malthus made. The *Limits to Growth* analysis, like Malthus, failed to appreciate an agricultural revolution that was occurring within its midst. The green revolution capitalized on the ability of human creativity, in the form of science, technology, and entrepreneurial skills, to keep food production in line with population growth. According to these observers, there is no reason to doubt that increases in productivity cannot continue indefinitely.

Critical Challenges

Yet several important challenges remain. First, many observers point out that increased productivity has not always translated into direct benefits to those people most in need. Famine and hunger remain major problems throughout the world. Factors ranging from war, political corruption, and simple market forces have prevented the benefits of this revolution from getting to those most in need.

A wide range of environmental problems has also been associated with the green revolution. The increased reliance on chemical fertilizers, pesticides, and herbicides has increased air, soil, and water pollution. Reliance on hybrids has translated into a loss of biodiversity, especially a loss of native plant species. Monoculture crops used to increase production face greater risks from disease and pests. Land degradation and desertification have accompanied many intensive farming techniques. Furthermore, some observers point out that the green revolution has created a greater dependence on fossil fuels. The increase in fossil fuels, used in everything from fertilizers and planting to harvesting and transportation, has created adverse environmental consequences.

Various social and political aspects of the green revolution have also drawn criticism. Plant and animal breeding technology has given way to genetically modified plants and animals, which, according to some critics, create greater and perhaps unknown risks. The green revolution has also resulted in the concentration of agricultural power and wealth. The technological resources that fed the green revolution are very expensive and the need for increased efficiencies has driven many smaller family farms out of business. Transnational corporations have gained ownership of specialized plant and animal hybrids and, more recently, of patents for genetically modified crops. As a result, they can exert economic and political control over farmers throughout the world. The concentration of agricultural power has also created giant industrial and factory farms that have been criticized for both their inhumane treatment of animals and the pollution created by animal wastes.

Thus, the green revolution provides an intriguing case study in business and environmental ethics. Significant social and economic benefits followed from the revolution in agricultural productivity that occurred in the later decades of the 20th century. Yet the challenges of this revolution, most of which were unimagined by the well-intentioned people who led the change, will remain for decades to come.

—Joseph R. DesJardins

See also Agribusiness; Agriculture, Ethics of; Animal Rights Movement; Archer Daniels Midland

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Green Values

Green values are the wide range of values appealed to in defense of environmental policy prescriptions. Environmental policies can be defended by reasons of prudence, morality, social justice to present generations, social justice to future generations, aesthetics, spirituality and religious conviction, historical significance, symbolic meaning, and economics. Green values also involve giving greater normative consideration to nonhuman interests and concerns, including the status of animals and other nonhuman natural objects; to the preservation of biological diversity; to the protection of ecosystems; and to the aesthetic impacts of human operations on the environment.

Environmental philosophers debate the possibility of reconciling this diversity of environmental values. Monists argue that unless a single unifying principle ultimately holds sway, environmental policy will remain relativistic and inconclusive. Value pluralists maintain that there can be a plurality of independent values that cannot and need not be reduced to a single unified theory.

Extending Moral Values

In general, values are what incline us to act in one way, or to choose one thing, rather than another. Thus, values are the perceived goods that provide us with a reason for action. The value that a person places on education leads him or her to study rather than play video games, and it provides him or her with a reason to study.

Philosophers have long distinguished the value of prudence (self-interest) from moral value. Prudence is the value of protecting one's own self-interest. A prudent person does not spray pesticides on the garden one is about to harvest. Moral values expand the range of this to include the impartial consideration of the interests of others. Moral values would, for example, prohibit dumping toxic wastes into a stream that flows onto one's neighbor's land.

Much work within environmental philosophy can be understood in terms of extending the range of moral value. As societies confronted a variety of new environmental challenges, philosophers began to consider the possibility that the domain of moral value was being too narrowly drawn. Disposal of nuclear wastes, for example, forces us to consider the value of human beings not yet living. A variety of other issues, from species extinction to the destruction of ecosystems, raised the possibility that moral value ought to be extended to nonhuman living beings as well. Animal welfare advocates extend moral standing to at least some animals on the basis of sentience or consciousness. Biocentrists argue that only life itself can provide a nonquestion begging ground for moral consideration and extend moral value to all living beings.

The shift to more holistic and ecological approaches to environmentalism suggests that moral value might be overextended when applied to nonhuman natural objects. While some might argue for the moral value of ecosystems and species, others prefer to explain green values in nonmoral terms. We might seek to preserve natural and wild spaces, for example, because they are beautiful, awe-inspiring, and majestic. Preserving biological diversity might be sought as an expression of religious or spiritual values. Protecting an endangered species is defended as symbolically valuable. Wilderness areas get preserved not because they are moral beings but for their historical and cultural meaning.

Instrumental and Intrinsic Values

A distinction between instrumental and intrinsic value can help explain the nature of such aesthetic, religious, spiritual, historic, and symbolic values. Philosophers have sometimes spoken as if the value domain is exhausted by the categories of moral value and instrumental value. Perhaps influenced by Kantian language of ends and means, subjects and objects, some philosophers suggest that if something is not an end in itself, not a moral subject, then it is a mere means and has only instrumental value. Since only autonomous beings are ends in themselves, the nonhuman natural world is reduced to having only instrumental value. But many environmental values cannot be reduced either to questions of moral standing or to mere usefulness.

Instrumental value is a function of how something is used and this value can be replaced by another object with equal or more efficient usefulness. For example, the instrumental value of having a garden might be replaced by a local grocery store. An object is intrinsically valuable, valued in itself, when its value depends on the unique object itself. Intrinsic value cannot be replaced with the substitution of another object, no matter how similar or useful. Accordingly, a garden might also have intrinsic value as the product of one's own creativity. This symbolic and aesthetic value is irreplaceable by a grocery store. This value inheres in, or is intrinsic to, this particular garden itself.

There are many environmental issues that do not involve intrinsic moral value. The concept of moral standing is stretched beyond recognition in claiming, for example, that a prairie, a wetland, or the Grand Canyon is a moral subject. But it is equally misguided to conclude that such things are to be valued simply for their usefulness. Many nonhuman natural objects possess intrinsic value and human beings would be doing a harm, not a moral harm but a harm nonetheless, in destroying them or in using them as mere instruments for human satisfaction.

Green Values and Business

What are the implications of these reflections for the social responsibility of business? According to a standard understanding of corporate social responsibility, business fulfills its social responsibilities when it responds to the demands of the marketplace while obeying the law and respecting minimum moral duties. Business may choose, as a matter of supererogation, to promote environmental values, but it is otherwise free to pursue profits by responding to the demands of the economic marketplace without any particular regard to environmental responsibilities. Insofar as society values environmental goods, for example, lowering pollution by increasing the fuel efficiency of automobiles, it is free to express those values through legislation or within the marketplace. Absent those demands, business has no special environmental responsibilities.

The problem with this approach is that it excludes any ethical responsibilities for individuals or business that emerge from those nonmoral intrinsic values found in nature. This standard would leave us with a very impoverished environmentalism. Perhaps some animals could be brought in under moral values, but the rest of the natural world could be valued only instrumentally, and we would be left with what is, at best, a conservationist ethic. A richer understanding of green values and practical reason, one with roots in Plato and Aristotle rather than in Kant, can support a more robust environmentalism. In this view, the *point* of ethics is to provide an answer to the (Socratic) question: How ought we to live? That is, ethics seeks to provide good reasons for doing one thing rather than another, for being one type of person rather than another. Individuals or institutions have ethical responsibilities (not categorical obligations in the Kantian sense) when doing one thing rather than another will produce or preserve something of value. To the degree that these values are more than mere subjective preferences, our reasons for acting are more than merely instrumental, hypothetical imperatives. In this sense, the range of environmental values previously described provide many good reasons for acting in ways that minimize harm to the natural environment. Some, but not all, of our environmental responsibilities involve moral responsibilities to other human beings. Some, but not all, are morally obligatory. In general, reasonable humans have ethical responsibilities to, and have good reasons to act in ways which, promote or preserve intrinsic value.

Of course, by claiming that green values should receive greater attention from the business community, one risks the possibility that such values will be co-opted by businesses' financial interests. Examples of greenwashing are a case in point. Some companies have learned that they can hide objectionable practices, or gain a marketing advantage, by appropriating the language of green values. Terms such as all-natural, recyclable, biodegradable, organic, and earth-friendly are often little more than a marketing ploy that uses the language of green values to promote products that have little if any environmental value.

—Joseph R. DesJardins

See also Animal Rights; Animal Rights Movement; Anthropocentricism; Biocentrism; Deep Ecology; Environmental Ethics; Environmentalism; Land Ethic; Sustainability; Wilderness

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Greenwashing

Greenwashing, a pejorative term derived from the term *whitewashing*, was coined by environmental activists to describe efforts by corporations to portray themselves as environmentally responsible in order to mask environmental wrongdoings. While the term has been used within activist circles since the late 1980s, it was not until 1999 that it was added to the *Concise Oxford English Dictionary* and officially recognized as part of the language. Consequently, some of the literature relating to greenwashing uses more neutral terms to describe this and related activities, including "environmental advertising," "environmental public relations," "green marketing," and "green communications."

The History of Greenwashing

The first instances of what environmentalists now call greenwashing appeared in the late 1960s as part of a corporate response to the modern environmental movement that was catalyzed by Rachel Carson's book *Silent Spring*. During the 1980s, the environmental movement gained momentum as a result of the Bhopal, Chernobyl, and Exxon Valdez disasters. By the early 1990s, polls suggested that consumers were more likely to buy products from a company that had a sound environmental reputation; corporations responded by portraying themselves, and more of their products, as environmentally friendly. By the mid-1990s, firms were spending millions of dollars on public relations activities aimed at "greening" their images and managing environmental opposition.

The term greenwashing was originally confined to describing misleading instances of environmental advertising, but as corporations' efforts to portray themselves as environmentally virtuous have diversified and proliferated, so have charges of greenwashing. The term is now used to refer to a wider range of corporate activities, including, but not limited to, certain instances of environmental reporting, event sponsorship, the distribution of educational materials, and the creation of "front groups." (Front groups, such as the International Climate Change Partnership and the National Wetlands Coalition, are organizations that pose as independent advocacy groups, but which in fact are funded by and promote the interests of a particular corporation or group of corporations.)

It is important to note that not all environmental advertisements or public relations campaigns can fairly be labeled greenwashing, as there are genuinely environmentally conscious companies that use advertisements and other means to promote themselves as such. The clearest cases of greenwashing occur when these media are employed by firms to proclaim (or in some cases merely imply) a deep-seated devotion to sound environmental practice (usually by pointing out some specific accomplishments in that field) in an attempt to distract from its otherwise lackluster environmental performance. For example, a company that advertises its sole laudable environmental initiative to distract from its more environmentally deleterious activities, or a company that, despite being a recalcitrant polluter, boasts about a marginal reduction in emissions at one of its factories, would be clear targets for a charge of greenwashing. Similar suspicions arise when corporations within environmentally problematic industries sponsor grassroots environmental events such as Earth Day, or when corporations with poor environmental track records distribute environmental education videos to schools.

Why Is Greenwashing Problematic?

The characteristics that render greenwashing subject to ethical criticism are related to, but differ somewhat from, those of other problematic types of promotional activities. Although a range of advertising and public relations techniques have been criticized for their potential to manipulate or coerce consumers, to manufacture desires, and generally to deceive the public, a certain degree of "puffery" or exaggeration has come to be expected, and in some cases considered acceptable, in the marketing of products or services. However, the use of similar tactics to publicize good corporate conduct—and in particular, corporate environmental achievements—has been deemed more problematic. One possible explanation for this is that companies guilty of greenwashing are not just *exaggerating* their environmental accomplishments or contributions: They are claiming to be environmental champions when they are in fact environmental villains. Thus, the charge of greenwashing seems especially apt in instances where corporate environmental communications are not just exaggerated, but tastelessly ironic.

Ethical worries about greenwashing extend far beyond the general unseemliness of the practice. One of the key concerns expressed by environmental activists is that greenwashing could result in unwarranted consumer and regulator complacency. Corporations that make exaggerated claims regarding their commitment to the environment might give consumers and government regulators false hope that corporations themselves are making great strides toward protecting the environment, leading consumers and policy makers to believe that current levels of mass consumption are sustainable and that further government regulation is unnecessary. Moreover, there is the fear that if one corporation in a particular industry gets away with greenwashing, other corporations will follow suit, thereby creating an industrywide illusion of environmental sustainability, rather than sustainability itself. A final worry is that greenwashing may engender cynicism: If consumers come to expect self-congratulatory ads from even the most environmentally backward corporations, this could render consumers skeptical of even sincere portrayals of legitimate corporate environmental successes. This could result in a failure to justly recognize the achievements of genuinely progressive corporations, thus eliminating one significant incentive for improving corporate environmental performance.

Conclusion

The concept of greenwashing should be of interest to a range of parties. First and foremost, greenwashing should be of interest to consumers. While many instances of corporate environmental communication are well-intentioned and truthful, not all are, and consumers who wish to "vote with their dollars" need to be aware of various kinds of corporate deception and spin. Second, environmentalists and corporate watchdogs, such as the Green Life and CorpWatch, are of course interested to spot, and point out, cases of serious greenwashing. The charge of greenwashing constitutes a significant and poignant piece of critical rhetoric (in the nonpejorative sense of "rhetoric"). Finally, students and scholars of business ethics should be interested in the concept of greenwashing, too. There has thus far been a regrettable shortage of academic attention to the concept, despite the term's prevalence and its normative richness. The charge of greenwashing represents a savvy, typically nonacademic criticism of corporate environmental communications. Academics ought to be attending to the significance of such lay evaluations: The growing prevalence of greenwashing as a practice, and as an accusation, signals a new complexity in the evaluation of corporate environmental performance.

—Melissa Whellams and Chris MacDonald

See also Advertising, Subliminal; Advertising Ethics; Deceptive Practices; Environmental Ethics; Marketing, Ethics of; Public Relations

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Gross Domestic Product (GDP)

The gross domestic product (GDP) is the market value of all the final goods and services produced in a country in a given period. As early as the 19th century, the need to compile information on the evolution of an economy over time prompted economists to develop aggregate calculations of a country's total production. In 1942, the U.S. Department of Commerce published the first official set of national accounts: a set of statistics that measure the country's economic variables, the most important measures being GDP and gross national product (GNP).

The Economic Dimension of the Gross Domestic Product

In the GDP, all the goods and services produced are aggregated in terms of value, that is, in terms of the prices paid by the buyers. Because some goods are used to produce other goods (e.g., the steel used in the production of automobiles), adding up the value of all the products would lead to "double counting" (the steel would be counted twice, once as a product of the steel industry and again as part of the value of the automobiles). To avoid that, only "final" goods are taken into account, that is, goods that are not used in the production of other goods (in our example, the automobiles, but not the steel). Alternatively, we can add up the "value added" by each production unit (the value the steel company adds to the raw materials, supplies, and energy purchased from other companies; and the value the auto maker adds to the value of the raw materials and supplies obtained from other industries, etc.).

The GDP is calculated, as we said, using the selling prices in the period in question. Therefore, to compare the GDPs of two different periods we need to separate the change in physical output from any mere change in prices. To do that, we calculate the GDP in real terms, that is, in the prices of a given year (known as the base year, which tends to be the previous year). That effectively eliminates any change due solely to changes in prices. And as the size of a country's GDP will depend on the amount of production factors available, it is useful to calculate GDP per capita (total GDP divided by the country's population) as a measure of the volume of the income generated by one person in the country.

As we have seen, the GDP contains information about the scale and composition of a country's production, the income it generates, the size and makeup of its citizens' spending (in other words, the standard of living of its population), employment creation, and how these variables have changed over time. It also allows us to compare the economies of different countries, although this raises at least two further problems. One is what common currency to use for the comparison, because any changes in the exchange rate of the chosen currency may give rise to spurious changes in our comparisons of the GDP. The other is the fact that the purchasing power of the same monetary unit may be very different in different countries: Although one dollar is one dollar, whether in the United States or in India, you can buy a lot more with one dollar in New Delhi than you can in New York. For that reason, international comparisons tend to be made in terms of what one could purchase in each country with a certain amount of money, which corrects that effect.

Limitations of the GDP

The GDP is a very useful economic concept, but it is important to be aware of its meaning and its limitations, in economic, social, and ethical terms:

- The GDP includes the goods and services that are the object of exchange in the market, for which there are set prices, and certain other goods and services, such as the services of owner-occupied housing or the consumption of farm produce by farm producers, for which prices are imputed. But it excludes many goods and services that are not the object of exchange in the market, such as housework, child care and elder care (when not carried out as paid work), voluntary work, and so on. In other words, its scope is limited.
- It does not include illegal productive activities (drug trafficking) or undeclared activities (underground economy).
- It does not include activities entailing mere transfers of assets between people, such as the sale of a house (whereas the construction of the house is part of GDP), the sale of a company's shares, the increase in value of a work of art, donations, or thefts.
- GDP does not measure the value of a country's wealth, only the value of the goods and services produced. If, for example, a natural disaster destroys part of the country's productive capital or resources, which will not be directly reflected in the country's GDP, although it will be reflected indirectly if final production is reduced as a result of the destruction.
- It does not include the value of leisure—though it is assumed that the market wage should reflect it, at least ideally. Nor does it include spiritual, moral, or cultural values, unless they are reflected in the production of goods and services.
- Market prices do not reflect all the opportunity costs of production, nor the harm (and benefits) caused by economic activity outside the market, such as environmental damage or traffic congestion. Paradoxically, the GDP may not reflect the environmental damage caused by production or the insecurity resulting from crime, and yet it will reflect the value of the goods and services produced to combat those ills.

For all the above reasons, GDP is a useful concept, but it needs to be used and interpreted with care, especially when its growth is adopted as a policy objective. It may be legitimate to promote faster GDP growth, particularly in developing countries, in order to create better opportunities for the population. But that policy must meet certain conditions. It must (1) be sustainable, (2) be fair (problems of inequality and poverty), (3) be efficient, and (4) foster (or at least not obstruct) values such as social cohesion, quality of life, or moral values. (For a discussion on the use of other indices designed to overcome at least some of the limitations of the GDP, see the entry "Gross National Product.")

In any case, it is important not to confuse GDP with well-being or welfare. The GDP refers only to the production of goods and services, in other words, the material component of well-being. Giving absolute priority to that component may lead to ethically questionable postures, such as the predominance of "having" over "being," or the subordination of other human values to the attainment of material well-being.

—Antonio Argandoña

See also Economic Growth; Environmental Ethics; Gross National Product (GNP); Underground Economy

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Gross National Product (GNP)

The gross national product (GNP) is the market value of the goods and services produced in a given period by the domestically owned factors of production of a country. It is an alternative to the gross domestic product (GDP): Both share the same accounting principles, qualities, and limitations.

The difference between the two indicators has to do with the scope of the calculation. The GDP refers to goods and services produced within the country by factors of production owned by residents and nonresidents alike. In contrast, GNP refers to goods and services produced by factors of production owned by residents, whether the production takes place within the country or abroad. For example, the salary of a U.S. national who works in Belgium without being resident in this country will be included in Belgium's GDP but not in its GNP. Conversely, it will be included in U.S. GNP but not in U.S. GDP. Formally, GNP is equal to GDP plus any income (from labor and capital) earned abroad by domestic factors, less income earned within the country by foreign factors.

Ireland is an interesting case: In 2003, its GNP was equal to 79% of its GDP. The difference was due to the high volume of foreign investment in the country, the return on foreign investment being included in GDP, but not in GNP. In 2003, Ireland ranked 4th among OECD countries by per capita GDP (in purchasing power parity terms), and 17th by per capita GNP. That may reflect an ethical problem: the possible manipulation of transfer prices by multinational companies to generate most of their profits in Ireland, whose tax policy is particularly favorable.

Like GDP, GNP may be seen from three equivalent points of view:

1. *Expenditure based*: The value of domestic final expenditure on goods and services at market prices (which includes purchases of consumer goods and services by households; gross private domestic investment in structures, equipment, and software; residential investment and change in inventories; and government consumption expenditures and investment), plus the value of exports, less the value of imports.
2. *Income based*: All payments made in production, such as wages and other labor costs, interest, rental, depreciation, profit, and taxes paid by companies (less subsidies).
3. *Output based*: The sum of the value added by all the production units plus net taxes paid.

The Alternatives

To overcome the limitations of GNP and GDP as measures of well-being, various alternatives have been proposed. William Nordhaus and James Tobin, for example, proposed the Measure of Economic Welfare (MEW): an adjusted measure of total national output, including only the consumption and investment items that contribute directly to economic well-being. The calculation includes deductions for capital consumption, disamenities (e.g., pollution), regrettable activities (which do not contribute to well-being), and intermediate activities (whose contribution is already included in other items), such as the cost of national security and diplomacy and some personal business and travel expenses, and additions to account for the well-being derived from leisure and nonmarket activities and some capital services.

Another is the Index of Sustainable Economic Welfare (ISEW). It is calculated in much the same way as the MEW, based on the consumption component of GDP, with additions to take account of factors such as unpaid household labor and the net formation of man-made capital, and deductions to reflect resource depletion, income inequality, and environmental damage. It has been reformulated as the Genuine Progress Indicator (GPI), to include factors such as the value of volunteer work, the cost of crime and family breakdown, the cost of underemployment, ozone depletion, and so on. Generally speaking, these indicators yield a much lower rate of growth than GDP or GNP, particularly since the 1970s, and often enough a declining trend. With different goals in mind, the United Nations prepared the Human Development Index (HDI), which combines indicators of life expectancy, educational attainment, and adjusted real income.

Recently, economists have used international surveys to compare happiness indicators with GNP or GDP. Easterlin posed the paradox that rising levels of per capita GNP did not contribute to greater happiness. However, more recent studies have found a positive correlation between happiness and personal income, the generosity of the welfare state and life expectancy, and a negative correlation with factors such as average hours worked, environmental degradation, crime, inflation, and unemployment.

—Antonio Argandoña

See also Environmental Ethics; Foreign Direct Investment (FDI); Gross Domestic Product (GDP); Underground Economy; U.S. Bureau of Economic Analysis

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Guanxi

No literal translation exists for the Mandarin term *guanxi,* but it incorporates aspects of relationship building and the rights and duties that two or more parties have toward each other.

Confucianism, practiced in Mainland China, Greater China, and Southeast Asia, considers people as a part of the social network in which a person plays different roles. Confucius originally listed five relationships of unequal, bipolar contexts that defined Chinese society. As George Haley and colleagues identified, these relationships include

- Ruler–Minister
- Father–Son
- Husband–Wife
- Elder Brother–Younger Brother
- Friends

The five relationships have attendant, though unequal, ethical expectations and duties. For example, those relationships on the left side of the above list (ruler, father, husband, etc.) can extract more duties and obligations than those on the right (minister, son, wife, etc.). Outside these five relationships, individuals have no ethical obligations, except to maintain social harmony. Because of China's weak legal system, and the traditional and historical administrative bias against the Chinese merchant classes, Confucian relationships including *guanxi*, with their emphasis on trust and uprightness, defined Chinese business relations for centuries. The importance of *guanxi* in business environments was emphasized by the Confucian bias against the merchant class and the concept of profit. Book 4, paragraph 16 of *The Analects* states, "A gentleman understands what is moral. The Small man understands what is profitable." A full discussion of the sociology of Chinese relationships and their effects on the evolution of Chinese culture and society, including businesses, can be found in *From the Soil: The Foundations of Chinese Society*, by Fei Xiaotong (the founder of Chinese sociology and whose works the Chinese Communist Party banned until the 1980s; the People's Republic of China banned sociology itself as a discipline until 1976). Confucian expectations on *guanxi* and ethical conduct continue to affect interpersonal business behaviors and business environments in China.

The inequality of *guanxi* molds interpersonal ethics in Chinese business; different levels and intensities of *guanxi* receive different levels of treatments. Several researchers have provided empirical evidence of how *guanxi* affects diverse relationships in business and social environments. For example, A. K. M. Au and D. S. N. Wong in 2001 used auditors in Hong Kong and Chinese companies to show that *guanxi* correlates with moral reasoning. Au and Wong explored the effect of ethical reasoning on the relationships between *guanxi* and auditors' behaviors in an audit-conflict situation. Their research showed that auditors' behaviors in an audit-conflict situation were influenced by the existence of *guanxi* and the level of cognitive moral development of the auditors; *guanxi* influenced decisions in conflicts, and even auditors with high professional ethics were influenced by it. In 2002, D. Tan and R. S. Snell derived five Chinese moral principles from their research on work ethics in Chinese society. Tan and Snell's theory specifically addressed the Chinese habitual emphasis on interpersonal relationships. Earlier, H. K. Ma had also proposed relational hierarchy from the perspective of utilitarianism and classified interpersonal relations into relatives, friends, strangers, and enemies. Relatives refer to blood relations, while friends include close friends and confidants. Strangers span ordinary strangers and extraordinary strangers. The latter consists of the socially vulnerable (e.g., people with disabilities), children, and the social elite (e.g., Nobel laureates). The amounts of utilitarian acts vary with the types of the interpersonal relations, with relatives receiving the most attention and enemies the least.

In broader social and political contexts, corporate political strategy often distinguishes between transactional and relational approaches to political behavior. Amy Hillman and Michael Hitt have proposed that companies with higher perceived or actual dependence on government policy will likely use relational approaches to political action. Chinese Confucian culture strengthens relational approaches. *Guanxi* networks permeate Chinese society. To influence government decision making, companies attempt to build and to lock in long-term *guanxi* with government officials or departments. Transactional approaches to political action may lead to the break of government *guanxi*, which could result in subsequent, unbearable transaction costs.

Indeed, research conducted by George Haley and colleagues has shown that *guanxi* provides a core competence for Chinese and overseas Chinese companies giving them privileged access to Chinese and Southeast Asian markets and relevant strategic information that foreign companies do not have. The research identified that in China's modern business environments, companies had to maintain *guanxi* among three separate, though overlapping networks—business, government, and ethnic networks. Relationships or *guanxi* with the government assumed particular importance for business success in China. In her testimony before the U.S. congressionally mandated commission, the U.S. China Economic and Security Review Commission, Usha Haley elaborated on how *guanxi* moulds off the book subsidies from the Chinese governments to Chinese businesses and prevents effective implementation of the Word Trade Organization principles.

—*Usha C. V. Haley*

See also International Business Ethics; Relativism, Moral

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H

HAYEK, FRIEDRICH A. (1899–1992)

One of the most significant thinkers of the 20th century, Hayek is renowned for his critique of socialist economic planning and for a defense of classical liberalism that employs a theory of social evolution and spontaneous order. A recipient of the Nobel Prize in Economics in 1974, he made important contributions to political philosophy, the history of ideas, psychology, and the method of the social sciences. The fundamental problem of society is, for Hayek, not the allocation of resources but the coordination and utilization of the knowledge that is dispersed among millions of anonymous individuals. To meet this problem, Hayek argues for a rule of law to establish conditions of liberty, thereby allowing the emergence of a spontaneous social order of greater complexity than could be attained by planning.

Hayek served in World War I and subsequently enrolled in the University of Vienna, majoring first in law and then in economics. In 1931, he accepted a position at the London School of Economics (LSE), becoming a British national in 1938. Focusing on monetary theory and the business cycle, his early work also includes robust criticism of Keynes, whose theory, Hayek argues, neglects the temporal elements of economic production. During this same period, Hayek turns to the topic of "socialist calculation." In his contribution to his edited collection, *Collectivist Economic Planning: Critical Studies on the Possibilities of Socialism* of 1935, Hayek extends the theory of Ludwig von Mises, one of the great economists of the Austrian School, by arguing that without freely determined prices, socialist planners will not know what to produce, in what quantities, or by what methods. In *Economics and Knowledge* of 1937, Hayek takes up the problem of the utilization of knowledge. Given the subjectivity of individual perception, along with the dispersed and fragmentary nature of knowledge, the theoretical construct of economic equilibrium (the mutual compatibility of expectations) must be explained rather than assumed. Hayek suggests that under the right conditions, the knowledge of individuals would coordinate spontaneously, tending toward an order analogous to that which a designing mind might have wrought. With the publication of *The Road to Serfdom* of 1944, Hayek extends his critique of socialism, warning that well-meaning attempts to plan the economy would have deleterious effects not just on economic affairs but on the political, moral, and attitudinal character of individuals.

Hayek remained at the LSE until 1950, when he joined the University of Chicago; he also taught at Freiburg (1962–1967) and was an honorary professor at Salzburg (1968–1977). During the decade of the 1950s, he published, among other works, *The Sensory Order* (1952), a treatise on psychology (a draft of which he had composed three decades earlier) and *The Counter-Revolution of Science* of 1952. In this work, he defends methodological individualism and argues that the relevant facts of the social sciences are the beliefs and intentions of agents, not empirical data.

By the end of the 1950s, Hayek completed *The Constitution of Liberty* of 1960. This important work restates the ideals of classical liberalism and critiques both socialism and the welfare state. His political philosophy is grounded in an understanding of society that he traces to 18th-century philosophers such as Mandeville, Ferguson, Hume, and Smith. Social norms and patterns of conduct emerge over time in an unintended and evolutionary manner. Liberty, established through general and impartial law (and not through specific or particular commands), is essential to the emergence of spontaneous and beneficial patterns and institutions. These ideas are developed further in the three volumes of *Law, Legislation, and Liberty* (published in 1973, 1976, and 1979). Hayek focuses on the "abstract" and purpose-free rules necessary for generating a spontaneous order (explaining how such rules may run counter to deeply felt emotions). He also contends that "social justice" has no coherent application in a free society, and he elaborates the legal institutions required to preserve freedom.

Hayek's thought has relevance to several areas of business ethics. He is often noted for his rejoinder to John Kenneth Galbraith's contention that consumer preferences are the dependent creations of corporations and are therefore not urgent. Hayek counters that most desires (including those for art and music) have been produced by organizations or institutions of society, but this fact does not show these desires to be insignificant. More important yet, the demise of socialist regimes may vindicate the thesis that economic planning cannot surpass the productivity of markets. And the idea of society as a spontaneous order should prove fruitful for developing a business ethic attuned to the ongoing processes of markets. Finally, Hayek's contention that the basic economic problem of society is one of coordination raises an unrecognized implication for the stakeholder theory of management. If freely determined prices provide information that helps to coordinate multivarious plans and intentions, then is the manager who responds to stakeholders, rather than to prices, a disruptive force whose actions forestall the productivity that would otherwise be achieved?

—*F. Eugene Heath*

See also Austrian School of Economics; Ferguson, Adam; Hume, David; Invisible Hand; Methodological Individualism; Smith, Adam; Spontaneous Order; Stakeholder Theory

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Hazardous Waste

A hazard, in a technical sense rather than in day-to-day meaning, is the source of a potential harm, while a risk is the combination of the frequency of the hazard and the consequences of its occurrence. Hazardous wastes are broadly defined as those waste products that have a negative impact on human health and the environment when they are emitted or discharged into air, water, soil, food, and tissues. They are defined more specifically in the Basel Convention and in OECD Regulations for the Control of Transboundary Movement of Wastes Destined for Recovery Operations, agreed to by the OECD Council in 2002. According to the Basel Convention, the intergovernmental agreement administered by United Nations Environment Program, such wastes fall into the following categories: explosive, flammable liquids/solids, poisonous, toxic, ecotoxic, infectious substances. Other regulatory lists also act as national classificatory systems. For example, in the United States, the Resource Conservation and Recovery Act (RCRA), passed in 1976 and amended in 1984, 1992, and 1996, established the authority for the U.S. Environmental Protection Agency to control hazardous waste from "cradle-to-grave." This includes the generation, transportation, treatment, storage, and disposal of hazardous waste.

Risks Associated With Hazardous Waste

As global population grows, our economic development continues, and communication systems expand, environmental hazards have greater socioeconomic and biophysical impacts. Public opinion polls in the 1990s and early 2000s have shown that hazardous wastes are the most worrying of all environmental risks and hazards. They arouse most public controversy and challenge policy makers and the business and scientific communities alike to develop new ways of decision making to manage their storage, transport, and disposal. Researchers have found major differences between how the public, on one hand, and the scientific community, on the other, assess the risks associated with hazardous waste. Studies show that risks borne involuntarily, caused industrially, or that are difficult to pick up through our senses, such as nuclear irradiation, are perceived as higher. The question of acceptability of the risk goes back to trust in the organizations that produce, manage, and regulate the hazards.

The publication of Rachel Carson's *Silent Spring* in 1962 marks public recognition of the persistent effects of hazardous or toxic substances on the biosphere. It was not until 1975, however, prompted by the notorious episode of Love Canal, a small canal near Niagara Falls in New York State, where the Hooker Chemical Company had dumped toxic chemical waste for a decade, that the impact hazardous waste can have on human health emerged as a specific policy issue and a political phenomenon, with potential impact on government credibility as well as corporate performance. In the decades since, environmental justice movements concerned with hazardous waste have both proliferated and diversified. These often intractable disputes represent the failure of traditional forms of authority and organization in dealing with these problems. In this way, hazardous wastes are emblematic of many of the environmental problems facing society and reflect the new environmental, social, and economic pressures facing organizations of all types.

Implications for Business

Proponents of the business case for corporate social responsibility argue that apart from reducing costs associated with compliance, there are business benefits in reducing the generation of hazardous waste. They include more efficient resource use, improved quality, higher reputation, increased innovation, and new niche markets. As a result, some voluntary business efforts are under way, often led by industry associations, such as the American Hospital Association's agreement that member organizations would eliminate hazardous wastes such as mercury.

Investors and consumers can also react negatively to the risks associated with the creation of hazardous waste, such as high penalties and cleanup costs. This is more the case since regulators are increasingly releasing information on polluters to the markets (investors and consumers) as a means of pressuring companies to reduce their environmental impacts. On the other hand, there are also economic incentives for developed nations with more stringent environmental legislation to export their wastes to the developing world. Hence capital markets may act both as an incentive and a disincentive for firms to control their production of hazardous wastes.

In terms of government regulation, hazardous waste is controlled using three regulatory principles: the proximity principle, the polluter pays principle, and the precautionary principle. These principles are enshrined in much of the legislation and regulations concerning sustainable development in general and waste management in particular. The first two of these guidelines in decision making are relatively straightforward in their implications for business and government regulators. The proximity principle holds that the best place to deal with a problem is as close to it as possible. Polluter pays describes a wide gamut of financial incentives for firms to make preventative decisions but basically puts the responsibility for costs of any damage on those engaging in potentially hazardous activities. The precautionary principle holds that if there is scientific uncertainty associated with the disposal of potentially hazardous waste, then other options for the disposal or storage of the waste must be considered.

Applying this principle to the management of hazardous substances raises major difficulties for companies. Their effects on human health are often uncertain because their chemical composition and the specific source of the hazard are frequently unknown. Low-level hazardous waste may have cumulative effects, and different chemicals composing the waste may interact synergistically in unknown ways. Waste streams may be reclassified as hazardous as we develop more understanding of the impact of certain chemicals. Hence, for many companies, the hazardous nature of their industrial legacies may not emerge until long in the future, making their long-term risk profile and shareholder investment a cause for concern.

The Control of Hazardous Waste

The major international treaty dealing with hazardous waste is the Basel Convention of 1989, which by May 2006 was ratified by 164 countries and has been emulated in other intergovernmental arrangements. Its immediate purpose was to prevent developed countries, as their own governments tightened environmental legislation, from dumping their hazardous wastes in developing countries. However, it is also concerned with lessening the generation of hazardous wastes by taking an integrated life cycle approach that involves controls from the generation of a hazardous waste to its storage, transport, treatment, reuse, recycling, recovery, and final disposal. Signature nations are required to report annually on the generation and movement of hazardous waste. The convention allows for trade in wastes between signatory countries that have signed bilateral agreements concerning waste transfer.

Various regulatory regimes have attempted to set controls on hazardous waste, albeit in different ways. For instance, in the United States, RCRA addresses responsibility for activities related to generating, handling, and disposing of hazardous waste. The effect on business of the increasing controls on transboundary waste transfer and tightening national legislation is a shift to waste reduction to reduce or eliminate compliance issues. This is particularly evident in the electronics industry because of rapid obsolescence of products such as computers and cell phones, many containing toxic materials. The European Union is implementing strict new take back and recycling legislation for electronic waste products through various directives such as Waste Electronic & Electrical Equipment and End-of-Life Vehicles Directives. In Japan, the Law for Promotion of Effective Utilization of Resources embraces the principle of extended producer responsibility by requiring manufacturers to establish collection and recycling systems for used computers. This law now also addresses the recycling of small batteries containing toxic materials.

Ethical Issues Surrounding Hazardous Waste

A first ethical issue concerning hazardous waste arises from its longevity. This leads to the question of intergenerational justice—that is, whether risks to present generations should be decreased by transferring them to future generations. Such considerations are sometimes backed by the argument that future generations are likely to have a larger range of technological know-how and hence would be better able to deal with our problems. However, such a position is subject to both factual and ethical objections. Problems resulting from hazardous waste may actually get worse over time and hence become more costly to tackle. On ethical grounds, it has to be noted that just because A is better able to deal with B's problem, it does not follow that A has an obligation to actually do so. An attempt to address intergenerational justice is the neutrality criterion in nuclear waste management, which stipulates that risks to future generations should not be higher than those they would face without the interference by the present generation. In terms of nuclear waste, future generations should thus not be subjected to risks that are higher than naturally occurring background radiation.

Another intergenerational issue is linked to the notion of consent. Who would be eligible to grant consent as proxy of future generations and under what conditions? In practice, it can often be observed that present-generation stakeholders, such as host communities of proposed storage sites for hazardous wastes, do not consent to the siting of the facility. Consent by the present generation to the imposition of a risk would, however, be an important precondition for the consent of future generations, as one cannot assume that future generations would accept a condition that the present one does not.

Hazardous waste also creates a number of intragenerational issues, which center on the distribution of risks, such as living near a hazardous waste storage facility, and benefits, such as having access to cheap nuclear energy. There is indeed evidence in industrialized countries that underprivileged sections of the population have a greater likelihood of living next to hazardous sites and therefore bear a higher burden of the risk. Another issue of justice concerns the imposition of transport routes for hazardous waste on local governments, whether to dispose of waste on site or at some remote location.

Further intragenerational issues concern trade in hazardous waste. Although most such trade is between industrialized countries, an undefined proportion is exported, legally or illegally, from industrialized to developing countries. This export becomes a source of ethical concern where the importing country lacks the administrative expertise and technical resources to adequately deal with such waste. Burying hazardous waste in landfill facilities that are not properly managed or only partially controlled can lead to the contamination of ground water or agricultural land. Another concern regarding the externalization of risk from the

North to the South are the conditions under which workers in developing countries dismantle electronic components or decommissioned ships to recover recyclable materials: They may work unprotected from toxic fumes and other hazards. Such impacts are particularly problematic as developing countries have only scant economic resources they can devote to public health issues. Hence, coping with more urgent short-term problems, such as infectious diseases or infant mortality, diverts attention from the more long-term public health impact of hazardous waste.

Hazardous waste not only has a negative impact on the quality of air, water, and agricultural soil but by evaporating and turning into toxic rain, some forms of it can also reappear in areas far removed from the original location. This raises the question of whether decisions on modern manufacturing methods and the risks arising from these can be left to scientific experts and corporate executives. If public opinion is not sought and taken account of as valid—rather than dismissed as unscientific lay view—then ultimately the public may end up becoming disenfranchised. From an ethical point of view, the controversy surrounding hazardous waste concerns a clash between welfare gains and rights, in particular the right not to be harmed or put at risk. There seems to be general agreement among moral philosophers that protecting a person from serious harm is more important than any enhancement of societal welfare, whether accruing to that person or not. Such a conclusion is also backed up by reference to the social contract that binds human society. By virtue of being members of the same species, members of all generations, whether present or future, deserve equal treatment. This anthropocentric argument can, of course, be enlarged to encompass other species.

—Lutz Preuss and Suzanne Benn

See also Consent; Justice, Distributive; Love Canal; Market Failure; Market Power; Pollution; Rights, Theories of; Social Contract Theory; Sustainability; Toxic Waste

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Health Insurance Portability and Accountability Act

The Health Insurance Portability and Accountability Act (HIPAA) was passed by the U.S. Congress and signed into law by President Clinton in 1996. There were two main concerns behind the law. The first is related to employees fearing to switch jobs due to the potential of losing medical insurance coverage for preexisting health problems such as diabetes or hypertension. HIPAA provides increased protection to employees in that situation.

The second concern behind the law was the increasing use of electronic storage of medical records. Such storage eases communications between, for example, the patient's health care provider and insurance company. However, it also increases the risk of sensitive health care information about a particular patient being shared with the wrong parties. Often, private medical records must pass through a number of hands during activities such as the processing of insurance claims. Even more hands are involved with the complex decision-making processes and auditing that take place in HMOs and hospitals. In addition, medical records stored on computer hard drives and portable storage devices such as CD-ROMs are vulnerable to hacking attacks and/or theft. The age of the Internet, in which sensitive personal information could potentially be shared worldwide, has heightened privacy and security concerns. HIPAA requires that both government agencies and private firms that have access to personal health information address such concerns.

Provisions Related to Protection of Employee Health Insurance

HIPAA regulates group health insurance plans in relation to their decision to offer or not offer coverage to patients with health problems. "Health problems" are broadly defined, and include illness (physical and/or mental), disability, and a poor genetic profile. The law allows benefit limitations on these conditions, but only if they are applied uniformly to all individuals with similar conditions. With the same caveat, a similar regulation allows group health plans to limit lifetime benefits.

The second set of provisions related to protecting employee health insurance concerns insurance coverage of patients with preexisting medical conditions. A "preexisting condition" is defined as one from which a patient suffers at least 6 months prior to the patient's enrollment in an insurance program. While excluding such conditions from coverage is allowed, there is a time limit for exclusion: 12 months for most individuals and 18 for those who enroll late. The next provision is designed to avoid the problem of patients fearing to take a new job due to loss of coverage for preexisting conditions. Previous insurance coverage counts toward meeting the 12-month exclusion, provided the break in coverage is less than 63 days. Thus, if an employee had more than 12 months of coverage in a prior job, he or she cannot lose coverage over the preexisting condition when accepting a new job with a new health plan.

The moral issues surrounding these health insurance regulations involve whether it is fair for a provider of health care coverage to deny such coverage to a patient with a previously existing medical condition. This issue has expanded to whether an insurance company can deny an individual coverage for a poor outcome on genetic testing, even if that individual does not yet have a disease. The insurance industry has argued that to make a profit, it is necessary to deny coverage to those with known serious medical conditions or poor genetic profiles. Critics argue that such policies only result in the healthy being covered by medical insurance, with the result that those who need health care insurance the most—namely, the sick—are the ones who are denied coverage. These concerns are extensions of a larger debate over the treatment of patients by insurance companies. These companies can freely contract with individuals and businesses and charge what they wish for coverage, something that hurts smaller businesses in negotiations for insurance coverage for their employees. In addition, the insurance industry's notion of "actuarial fairness" claims that it is morally acceptable to charge people different rates based on their likely burden on the insurance system. These issues play into more, even broader, debates over rights language ("is there a right to health care?") and justice ("is it really fair to deny the sick the coverage they need?").

Privacy Provisions

The major impact of HIPAA, and the major focus of discussion surrounding HIPAA regulations, has been on privacy provisions. These provisions apply to "covered entities," including health care professionals, health care facilities, such as hospitals and nursing homes, providers of health plans, such as insurance companies and HMOs, and Medicare and Medicaid—any entity having access to patient medical records.

It is not only information in an individual's medical records that is protected. Conversations among health care staff concerning a patient's treatment, information about an individual's medical bill at a health care facility, or personal information held by an insurance company is also protected. It is irrelevant whether such information is found in hard copy or stored on a computer hard drive or any other electronic storage device.

The HIPAA regulations give certain rights to patients regarding their own access and limiting others' access to health related information (e.g., requesting that a physician call the patient's office phone rather than home phone). If any patient requests a copy of their medical record, the health care provider has 30 days to provide it, although it can delay for an additional 30 days if it gives the patient a reason for the delay. Patients also have the right to correct their medical records if they are in error. They have the right to a notice detailing how their health information will be used and with whom it will be shared. If a provider wishes to use patient information for nonhealth reasons such as marketing, the patient must give prior permission. The patient also has the right to receive a report on when health care information was shared and the reasons for that sharing. The patient can get this report free once a year, and the health care entity is required to provide the report within 60 days of request, but it can take up to 90 days if it provides a reason. Although a patient may request that health information not be shared with others, such as other physicians at a clinic, the clinic is not required to agree to the patient's request. If a patient has a privacy-related complaint, that patient can file a formal complaint with the Department of Health and Human Services Office for Civil Rights.

Covered entities have responsibilities regarding the use and release of medical records. Most sharing of health information unrelated to a patient's health care, such as disclosures of health information to employers or potential employers of the patient, are forbidden unless the patient gives prior permission. Information shared must be the minimum necessary to make adequate disclosure given the purpose of disclosing such information. Health care providers and other entities covered under HIPAA are required to have a written privacy policy detailing who can see and use protected information and when it can be released to others. Normally, the patient will receive a copy of the privacy policy on the first visit to the health care facility. Covered entities must train employees in privacy procedures as well as appoint a privacy officer to enforce privacy regulations. Policies and procedures manuals must specify privacy provisions as well as include a list of those classes of employees having access to health care information. Companies that outsource business involving patient information to third parties must ensure that the third party will ensure the same protections for patient information as the outsourcing company. A contingency plan is required for emergencies, including data backup of patient information. Encryption of some computer data of medical records may also be required. Notes concerning mental health care are not meant to be shared and thus are held to a higher standard of protection. Covered entities may release health care information for certain public responsibilities, such as emergency situations, identifying a body, or determining the cause of death, public health needs (e.g., stopping an epidemic), medical research approved by an Institutional Review Board, regulation of health care entities, judicial and law enforcement activities, and national security. If a state law has privacy regulations that are stricter than HIPAA, a covered entity located in that state must follow the more stringent state regulations. Both private and public sector health care and insurance entities must follow HIPAA, and there are civil and criminal penalties (up to a $250,000 fine or 10 years in prison) for those who knowingly violate the privacy provisions.

Is HIPAA a Good Thing?

While consumer and privacy advocates have, for the most part, applauded HIPAA, some privacy advocates, along with health care providers and other covered entities, have concerns. On one hand, there is the danger of patient information being released to the wrong parties. This concern helped move HIPAA easily through Congress. If a patient's health care records, for example, are released to a potential employer, and it turns out that patient had cancer 8 years before, that company may not hire that individual. Or a man might not want his wife to know that he had a bout of gonorrhea 5 years before they were married; release of such information could be embarrassing and damage his marriage. Insurance companies might use the results of genetic testing to discriminate against patients if they gain access to that information. With one fundamental principle in medicine being nonmaleficence, "do no harm," it is important that health care providers not release sensitive information that could harm their patients. Privacy laws, such as HIPAA, are a result of that concern not to harm patients by releasing private, potentially sensitive information. In an age of greater ease in information sharing due to computers, many consumer advocates argue that HIPAA is a good start in protecting patients from unauthorized or unjustified release of their personal health information.

Critics, including some privacy advocates, have argued that the protections of HIPAA are too weak; some have further argued that *no* laws and regulations can adequately protect privacy. One example is a person filling out an application for health insurance. The application will ask health questions that the applicant is required to answer truthfully. Some of these questions may concern sensitive information such as the results of genetic testing. The application may request release of the patient's medical records to the insurance company. If the company argues that the entire record is relevant to its making an informed decision about coverage, then, these critics claim, HIPAA offers no meaningful privacy protection for the applicant.

Another source of criticism has come from covered entities such as doctors' offices and hospitals. They have complained of difficulty in understanding government regulations on enforcing privacy. There are concerns that overzealous hospital employees, fearful of being fined for HIPAA violations, may refuse to give information concerning a sick patient to the patient's close family members. In addition, increased regulation means increased costs. Larger companies may wish to hire a privacy officer rather than add those duties to one of the existing employees. Revamping computer programs and generating more paperwork also increase costs. It is estimated that implementation costs will be more than $17 billion over the first 10 years of the initiation of HIPAA privacy regulations. However, it is also estimated that covered entities could save up to $30 billion through administrative simplification (such as standardization of financial transaction formats and code sets). Whether HIPAA will increase the cost of health care or result in cost savings remains an open question. Whatever its merits as law, the passage of HIPAA has stimulated debate over the proper scope of privacy and confidentiality regarding health care records.

—Michael Potts

See also Business Ethics and Health Care; Confidentiality Agreements; Consumer Rights; Privacy

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Health Maintenance Organizations (HMOs)

Health Maintenance Organizations (HMOs) are the primary vehicle for managed health care in the United States. An HMO is an organizational structure that insures participating members for health-care-related expenses through its coordination of the financing elements of medical care with the care provision aspects. In their role as insurer, provider, and administrator for health care coverage, HMOs attempt to fulfill three often conflicting agendas: the provision of high quality health services; the reduction of inefficiencies, both operational and economic, in such services; and the generation of financial profits for the owners of care provider systems.

The underlying philosophy behind the development and implementation of health maintenance organizations is the concept of managed care. Managed care is an approach to the provision of health care services that attempts to balance concerns for the application of effective medical treatment with administrative concerns for economic efficiency, as represented by cost control measures. A critical element in this balance between treatment and cost containment is an emphasis on preventive care—the effort to prevent serious disease through periodic preventive treatments such as annual physical examinations. Preventive care attempts to identify potential health problems before they grow both in severity and in treatment cost.

HMOs form a unique element of the U.S. health care system by offering a means to "manage" health care costs through the provision of prepaid health coverage for future services; in this fashion HMOs serve as both health insurers and health care providers. They operate largely as private, for-profit organizations within the U.S. health care system, which itself is a predominantly private (nongovernmental) medical services delivery system. Prior to the emergence of HMOs, most medical services in the United States were performed on a fee-for-services basis, with traditional health insurance offering posttreatment payments. Under this structure, the risk of excessive health care costs that would not be covered in full by these existing insurance plans tended to discourage some individuals from obtaining necessary medical treatment. Moreover, the cost of traditional insurance would often fall beyond the means of up to a quarter of the working population.

Because the United States does not provide comprehensive, universal, publicly funded health care for its citizens, the HMO was developed as a mechanism to lower health care costs and thus make health care more affordable for less affluent portions of the population. However, as HMOs are largely privately owned businesses facing pressures from stockholders (the owners of these companies) for profits, the structure and performance of health maintenance organizations in the United States embody the central dilemma that bedevils health care in the United States—the struggle between economic demands for profitability and medical demands for effective care. Complicating this situation are issues of equity in the availability and implementation of care, ethics concerning the nature of the decision-making processes in HMOs, and efficiency in a system that attempts to balance important issues of medical treatment with overriding pressures for cost containment.

The historical origins of HMOs date from the early part of the 20th century. In several areas of the United States, innovative physicians established prepaid medical service arrangements within their communities. The most significant large-scale developments among these early efforts were the formations of the Kaiser Permanente group and the Health Insurance Plan (HIP). The system that became Kaiser Permanente started in the 1930s as a supplier of medical services to industrialist Henry J. Kaiser's employees throughout the Western United States; after World War II, it expanded into a publicly available, comprehensive prepaid health plan that was open to all interested groups. In the eastern United States, HIP emerged in New York City during the 1940s as a medical provider for the municipal employees of that city. Two important elements of these and other early efforts toward prepaid group health coverage were the nonprofit status of many of these emerging providers and the emphasis these providers placed on preventive care as a means to reduce overall health care costs.

Innovative efforts such as these remained a relatively small and isolated force within the overall health care system in the United States, though, until the convergence of significant medical and economic forces during the 1960s. That decade witnessed a substantial growth in medical technologies and advances in medical practices. Unfortunately, these technological and practitioner advances also stimulated substantial cost increases for access to these medical improvements. By the late 1960s, the cost for medical care in the United States was rising faster than the annual rate of inflation, which at that time was approaching the double-digit level. As pressures for a solution to this growing financial problem began to coalesce at the federal level, the administration of Richard M. Nixon adopted the concept of health maintenance organizations as a means to restructure the national health care system through private initiatives rather than through significant government interventions or expenditures as in Canada and Western Europe. This politically driven approach culminated in the Health Maintenance Organizations Act (HMO Act) of 1973, which provided the structural foundations for the national growth of HMOs.

The HMO Act imposed several requirements on businesses and the emerging HMO industry. For businesses in the United States, it required any organization that provided health care coverage for employees to offer a health maintenance organization option in addition to traditional health insurance. To encourage the growth of HMOs, the act then provided government loans and grants to stimulate the development of new HMOs across the country. Furthermore, the act defined the range of basic medical services required of HMOs and, finally, it established pricing parameters that required HMOs to offer the same premium rate for medical coverage to all enrollees in a covered group, regardless of each individual's previous medical history. These guidelines emphasized the "group" nature of HMOs, where by spreading the costs of medical risks across large populations of participating members, HMOs could provide increased levels of coverage at reduced rates of cost. These mandates of the act also provided an operating framework where the privately run health care industry could continue to fulfill its historical role as arbiter of the critical medical and economic decisions involved in health care.

Ironically, though, this set of requirements contained in the HMO Act led not to a continued absence of government intervention in the decision-making processes of health care providers but instead to the establishment of a baseline of governmentally defined standards that federal and state regulators could then use to develop oversight procedures for the health care industry. Because of the separation of powers between the states and the central government as defined in the U.S. Constitution (and interpreted in subsequent judicial rulings), health care regulation in the

United States possesses a fragmented oversight structure: differing elements of the health care system receive oversight from various federal or individual state regulatory agencies, depending on how their roles and practices are defined. This situation has stimulated the growth of conflicting regulatory agendas, particularly in the struggle between the definition of necessary services and the containment of costs, which in turn establishes the basis for decisions of equity in the availability and provision of care.

Since the U.S. federal government exercises considerable influence over the definition of services and the pricing of medical procedures through its financial support for Medicare and Medicaid patients—many of whom receive their care through HMOs—federal guidelines regarding these elements have been routinely implemented as the governing standards within most HMO systems. Yet at the same time, insurance plans such as HMOs can generally only be regulated by state insurance regulatory entities. These separate sets of standards and guidelines have inevitably led to problems in defining levels of equitable access to care, and these problems then have been further exacerbated by the wide range of variability among states in their levels of health care coverage, health care costs, and oversight provisions. Moreover, this dual federal-state regulatory structure, combined with the fundamental tension in the health care system between effective caregiving and cost containment, has spawned growing conflicts involving who will be covered under HMO coverage contracts, what service these patients can obtain, and most important, what will be the treatment costs affecting these patients.

Accompanying these questions of equity, ethical and economic dilemmas have arisen concerning the fundamental nature and role of HMOs in the U.S. health care system. These dilemmas highlight the shifting roles of government, private industry, physicians, and patients as medical costs have continued to increase and care options—in both medical and financial terms—have continued to multiply.

The first of these dilemmas arising from the growth of health maintenance organizations is an issue that the HMO Act intended to solve: the definition and delivery of affordable care. Escalating costs have continued to have an impact on the U.S. health care system, especially from the late 1980s into the 21st century, when yearly health care cost increases were often double or triple the overall rate of inflation. While HMO rate increases have trailed those of independent health care insurers, they have still run higher than both the national average inflation rate and the growth of worker wages. With increasing health care costs overtaking many individuals' ability to pay, more people have found even the lower cost medical option of HMOs to be too expensive. Thus, the percentage of medically covered individuals within the United States has actually decreased, and medical insurance costs have continued to increase, despite the legislated intention of the HMO Act to address both these concerns.

The second dilemma facing HMOs is the ethical tension between the provision of medically appropriate services and the financial incentives for cost containment built into this privately operated system. As medical technology has increased in its scope, providing treatment options for an ever-broadening range of afflictions, the cost of providing these treatments has likewise increased. This situation can place HMOs in the position of choosing among regimens of treatment on the basis of cost rather than efficacy: employing less effective methods or medications to treat conditions because they are less costly, and restricting, if not actually denying, access to specialized treatment regimens solely because of their costs. Practitioners in the health care field have noted an increasing tension between their fulfillment of the Hippocratic Oath, which urges medical treatment on the basis of its effectiveness, and the achievement of financial objectives, which the stockholders of these privately held and operated organizations demand.

In many HMOs, doctors are not paid on the basis of the number of procedures they perform or the number of patients they see: They act as salaried employees for the HMO and its owners. In other HMOs, an administrative body negotiates contracts for treatment by external physicians and facilities not employed or owned by the HMO. Both these structural formats for caregiving insert a third party—the HMO administration—into what was formerly solely a doctor-patient relationship. This changing set of relationships has led to the third dilemma facing HMOs: the growing ethical and economic conflicts among the major stakeholders involved with HMOs.

Since the early 1980s, the U.S. health care system has moved increasingly from a network of fee-for-service medical practitioners performing their duties at nonprofit institutions (such as religious or university-run hospitals and clinics) to a system of both fee-for-service and salaried physicians increasingly performing their duties in for-profit medical facilities operated by large, publicly traded health care businesses. Since the parent organizations of many HMOs either own their medical facilities (as they have purchased formerly nonprofit institutions) or contract directly with other facilities for services at preset rates, the role played by business administrators in the determination of health care standards has increased dramatically. This shift in the central guiding rubric of many HMOs from medical service to medical administration has produced a marked change in the fundamental nature of the doctor-patient relationship. Prior to the growth of for-profit HMOs, the major stakeholders involved in medical decision making were the individual physicians and their patients; the administrators of the nonprofit institutions where caregiving took place allowed this doctor-patient relationship to proceed largely unimpeded, under the assumption that this "hands-off" approach would produce the most beneficial health care results. However, as the definition of "beneficial health care results" has gradually changed since the passage of the HMO Act from ensuring comprehensive medical care to pursuing business profitability, HMO administrations have played an increasing role in deciding what procedures can or cannot be offered to patients, what procedures will or will not be insured by the HMO, and which practitioners will be authorized to perform prescribed or approved medical services.

A final dilemma arising from the growth of HMOs has been their growing influence in national health care decision making—an influence built on their successful growth. Even with the critical increases in all U.S. health care costs, including those of HMOs, these organizations have still multiplied in size and enrollment as they have become the primary provider of "lower-cost" health care options. By the mid-1990s over half of the U.S. working population that had health insurance coverage belonged to HMO plans. Accordingly, what were once local decisions about patient care (which were relatively insulated from the demands of economic efficiency) have grown into administrative standards of regional or national scope for the provision and pricing of services. As private corporations, HMOs can exercise a wide range of discretion in determining what factors will influence these standards: medical, economic, ethical, or administrative. This has furthered the influence of administrative decision making, based on criteria of cost and availability, into such medically defined areas as the provision of appropriate medications, the application of medical procedures, and the availability of both preventive and postevent medical care.

HMOs have provided both some of the benefits envisioned by supporters at the time of the 1973 passage of the HMO Act and some of the disadvantages feared because of their emphasis on efficiency in both the medical and economic realms. Nevertheless, they remain a central element of the privately run U.S. health care system and have changed the landscape of health care in the United States.

—William E. Martello

See also American Medical Association (AMA); Benefits, Employee; Dilemmas, Ethical; Health Insurance Portability and Accountability Act; Medicaid; Medicare; Patients' Bill of Rights

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Hedge Funds

A hedge fund is a private, loosely regulated, pooled set of investment monies managed by an individual or business for the benefit of the wealthy clients who contribute money to the pool. Hedge funds use a broad array of investment strategies, many originally conceived to protect a portfolio of stocks from the risk of a large market downswing. Alfred W. Jones, an American writer and financial journalist, is generally credited with creating the first hedge fund. In 1949 Jones created a fund that used leverage to buy or "go long" undervalued stocks, while simultaneously "short selling" overvalued stocks. By simultaneously buying some stocks and short selling others, Jones's portfolio was largely immune to general market swings. Today, hedge funds employ aggressive and sometimes speculative investment strategies and instruments that include short selling, buying on margin, program trading, swaps, various arbitrages, and derivatives. A hedge fund can invest in a variety of assets (worldwide) including securities (stocks and bonds), commodities, exchange currencies, and derivatives (futures and options).

The minimum investment in a hedge fund is typically high, usually $1 million, although recently some funds have altered this requirement to attract more investors. The large initial investment has raised concerns that hedge funds are financial vehicles only for the rich. The recent reduction in the minimum investment amount has likewise raised questions as to whether less wealthy investors (implicitly assumed to be less investment savvy) deserve more protection by the federal government. While an individual's initial investment is usually large, hedge funds are intentionally kept small enough to escape the federal and state regulations designed to protect investors in larger mutual funds.

Characteristics of a Hedge Fund

The two most common characteristics of hedge funds are the following: (1) the ability to "go long or short" and (2) the use of "leverage." Going long is the traditional method of buying a security (e.g., stock) at what is hoped to be an undervalued price and later selling it at a higher amount. This strategy profits by the amount the security rises in value. Going short is the process of first selling a security and incurring the obligation to buy it back at a later date. The strategy profits when the price of the security declines and the repurchase price is lower than the price for which the security was originally sold.

Hedge funds often implement strategies using a considerable amount of borrowing or leveraging of funds. Leverage is the straightforward borrowing of funds to increase the returns to an investment strategy. In the case of going long, a typical investor can only purchase a limited number of shares with their own money and the rate of return on the investment equals the rate of return on the security. A hedge can potentially earn a much higher return on an investment in the same security if they borrow money and purchase additional shares. If the cost of the borrowed money is lower than the rate of return on the security, this extra profit boosts the return on the fund's investment. In the case of going short, the fund is only required to deposit a fraction of the dollar amount of security value that has been sold to cover potential losses. In this sense, the fund stands to profit from the decline in the total value of the shares sold short with only a modest investment of the fund's money. However, the fund will incur the risk of substantial loss if the price of the security sold short does not move as expected because the fund must buy the security back at a higher price. This is the key element of leverage: The profits and losses associated with full security value are controlled by a fractional investment.

A common, distinguishing characteristic of hedge funds is the large performance fees charged by fund managers (usually between 15% and 25% of profits), in addition to a load fee and annual management fee. Fund managers are rewarded for the absolute return on the fund rather than performance relative to some benchmark, such as the return to the S&P 500.

However, the fund manager often has a significant amount of their own net worth invested in the fund. This may help to align the interests of the manager and fund clients. Hedge funds are often based offshore where investment regulations (by the SEC) may be more flexible, although fund managers are subject to penalties and criminal prosecution for fraud. The funds are typically offered within limited partnerships in the United States.

Hedge Fund Strategies and Sectors of Investment

The different strategies and sectors of hedge fund investment are quite broad and diverse. Historically, "equity hedge funds" have been the most traditional hedge fund type. These funds employ fundamental research to identify mispriced securities in the market. Managers buy undervalued stocks and short sell overvalued stocks, employing considerable leverage in the process. "Market neutral hedge funds" attempt to neutralize market risk by combining roughly equal long and short positions in the same, or different securities, commodities, or currencies, hence "hedging" a fund's market risk. Global "macro hedge funds" are another popular sector of investment activity. Fund managers attempt to identify temporary economic imbalances throughout the world and position themselves to profit when a restoration of equilibrium global relationships occurs. Hedge fund managers also look for investment opportunities in "emerging markets" in the global marketplace. In these less mature, high-growth emerging markets, it is difficult to obtain high-quality research material on investment opportunities because of poor information flows, and developing legal systems and market structures. All these market imperfections give rise to investment opportunities for hedge fund managers willing to expend the time and resources to uncover new investments. Currently, the most common emerging market regions are Asia, Eastern Europe, India, Latin America, the Pacific Rim, former Soviet Republics, and the Middle East.

Hedge fund managers may also operate within the "risk-arbitrage" sector where certain financial positions are taken to capitalize on specific events in a company. Usually, the events are associated with a merger, acquisition, divestment, or some other form of restructuring. One advantage of an investment that is "event driven" is that its success is typically unaffected by larger economic or market conditions. Other investment areas include "convertible bond arbitrage," where fund managers seek to exploit mispricing associated with the relationship between the price of a convertible bond, the price of the underlying stock, and the conversion factor. Hedge funds may also invest in "distressed" securities, where fund managers believe a company undergoing serious reorganization, restructuring, or bankruptcy may emerge in better shape than the firm's current share price reflects. "Mortgage-backed" securities are another area of investment sometimes tapped into by hedge fund managers. This market involves many derivative securities, which offer hedge funds the leverage they like to use.

Criticisms of Hedge Funds

The potential for large compensation from hedge fund performance fees may attract the brightest, sharpest, and shrewdest talent to manage these funds. However, many argue that, more commonly, the relatively loose regulation of hedge funds attracts unscrupulous fund managers. Basing performance fees on absolute return may also lead hedge fund managers to pursue progressively riskier investment strategies should initial investments not produce satisfactory returns. Hedge funds have also been criticized as an instrument only for the rich, as the minimum investment is usually $1 million, although this has changed recently.

Questions have been raised as to whether or not hedge funds create any true wealth, assuming that there is a fixed pie of return for which investors compete. Some contend that hedge funds are purely speculative vehicles given their unconventional investment strategies. Proponents argue that hedge funds are important catalysts for price discovery and efficiency in markets. Another criticism of hedge funds is that given the lack of regulation by the SEC, financial reporting and disclosure is, at best, less reliable. Cases of phony financial returns, misleading statistical reporting, fictitious financial statements, and outright fraud have been alleged. At the extreme, belief has grown that hedge funds have the potential to "destabilize" entire markets and economies.

With the recent growth in pension funds, endowments, and institutional investors, the hedge funds industry has come under increased scrutiny. The role and extent of government involvement in hedge funds continues to be an issue in the business and society literature.

—Daniel W. Greening and H. Douglas Witte

See also Agency, Theory of; Arbitrage; Commodity Futures Trading Commission; Economic Efficiency; Efficient Markets, Theory of; Financial Derivatives; Marginal Utility; Market Failure; Market Power; Pensions; Security Industry Association; Shareholder Wealth Maximization; Speculation and Speculator; Wealth Creation

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Hedonism, Ethical

The term *hedonism*, from the Greek root word *hedone* (pleasure), is the multifaceted philosophy that individuals should maximize pleasure and minimize pain. Two major views of this philosophy are psychological hedonism and ethical hedonism. *Psychological hedonism* is the belief that all humans have been developed to desire pleasure, avoid pain, and that it is impossible for humans to pursue anything else. In contrast, *ethical hedonism* refers to the view that although it is possible *not* to seek pleasure and avoid pain, it is morally wrong to do so. Furthermore, ethical hedonists believe that pleasure is an intrinsic value (for its own sake) and all other values are a means to pleasure. For example, if you attended a rock concert, the concert itself is merely a means to attain pleasure (intrinsic value). Nevertheless, there has been a great philosophical divergence among hedonists as to whether pursuing pleasure will guarantee happiness. One of these philosophies was utilitarianism, which advocated for the *collective* pursuit of pleasure and minimization of pain. This changed the focus of ethical hedonism from an individual's happiness to the happiness of the society as a whole.

Major Hedonistic Philosophers

One of the first hedonists, Aristippus (ca. 435–350 BCE), was born in Cyrene, on the coast of North Africa, and traveled to Athens to became one of Socrates' disciples. Eventually, Aristippus opened his own school of philosophy in Cyrene and taught what is now referred to as Cyrenaic hedonism, which was a belief that there were two states, pleasure and pain, and that one should pursue the former and avoid the latter. Furthermore, Cyrenaic hedonists believed that all pleasures were good, should be pursued without guilt, and this would lead to happiness. In addition, they believed that bodily pleasures were more intense and more satisfying than mental pleasures. Consequently, avoiding bodily pain was equally paramount in their pursuit of happiness for the same reason.

Interestingly enough, followers of Cyrenaic hedonism did not believe in delaying pleasure just for the sake of receiving more pleasure later and, therefore, encouraged pursuing whatever gave one the most immediate pleasure. However, all unrestrained behavior was discouraged because then you would be controlled by your pleasures rather than controlling them.

Another ethical hedonist philosopher was Epicurus (341–271 BCE), born on the island of Samos and considered the most famous of all hedonists. Oddly enough, Epicurus had been charged by many for plagiarizing Aristippus's theory of pleasure and using Aristippus's teachings as if they were his own. Like Aristippus, Epicurus believed happiness was the highest good and pursuing pleasure and avoiding pain would attain this.

Yet there were some fundamental differences between these schools. One major difference between the Epicurean and Cyrenaic philosophies of ethical hedonism was that the Epicureans believed in the importance of mental pleasures. Another dichotomy was that the Cyrenaic hedonists believed in the quantity of pleasure, while the Epicureans pursued the quality of pleasure. For example, a Cyrenaic hedonist would prefer a larger portion of food, whereas the Epicurean hedonist would prefer the most pleasant of fine dining, even if the portion were not substantive.

At one point in his lifetime, Epicurus visited Athens and studied with some of Plato's disciples. As a result, Epicurus valued the Platonic virtues of wisdom, temperance, and courage (or the strength of the soul) and believed this would lead to happiness. But, unlike Plato, who held that the highest good was not pleasure but was an ideal form of that which represented the likeness to God, Epicurus believed happiness was in the natural world, not the transcended world above.

Furthermore, Epicurus viewed pleasure as the end of life and virtue as the way to do it. Epicurus was of the view that a happy individual was the one who attained wisdom of discrimination and reflection, which would ultimately lead to a blessed existence of painlessness. In his *Letter to Menoeceus,* Epicurus gave special attention to the correct calculation for attaining pleasure. He did not believe in overindulging in alcohol, bodily lusting, or eating, and even supported deferring immediate pleasure if it would avoid pain later on. Although many perceive Epicureans as individuals without any constraints regarding the attainment of pleasure, it was the Epicurean philosophy of reason and reflection that differentiated it from the Cyreniac philosophy of ethical hedonism. In fact, Epicurus leaned more toward asceticism (self-denial of sexual love) than the unrestrained behavior that many attributed to hedonism. This is further supported by another of his hedonistic philosophies that the greatest happiness does not originate for the unrestrained enjoyment of physical pleasures but from a life that is free from anxiety. Happiness, according to

Epicurus, was interrelated with the health of the body and the tranquility of the mind, which would lead to the health of the soul.

However, when the Industrial Revolution emerged, the focus of pursuing pleasure for an individual's happiness was replaced with the happiness of society as a whole. This ethical hedonistic philosophy was termed utilitarianism, which advocated pursuing the greatest amount of pleasure for the greatest number of people.

Jeremy Bentham (1748–1832), born in London, was credited with coining the term *utilitarian* from a letter he wrote to a friend in 1781. This term was based on the notion of the greatest happiness for the greatest number, which he had found from a copy of Joseph Priestley's *Essay on Government,* 13 years earlier. However, Bentham's starting point was with the psychological hedonist philosopher Thomas Hobbes (1588–1679), who believed that individuals have been created by nature to maximize pleasure and minimize pain and could not do anything for another person unless it first benefited them. Although he concurred with Hobbes's first part, Bentham believed it was possible to seek pleasure for another person for altruistic reasons.

Furthermore, Bentham believed he could create a hedonic calculus, which could be used in computing the pleasure or pain that would be the result of a certain action. In his essay, *An Introduction to the Principles of Morals and Legislation,* Bentham identified four measurement values of pleasure or pain endured by an individual: intensity, duration, certainty or uncertainty, and propinquity or remoteness. Intensity referred to the strength of the pleasure, duration was how long the pleasure would last, certainty or uncertainty was the likelihood or unlikelihood that the pleasure occurred, and propinquity or remoteness related to how soon the pleasure occurred. This was the first major section of his utilitarian theory.

The second section of Bentham's hedonic calculus was based on the number of persons affected by given actions, with reference to each of their values of pleasure or pain. It consisted of the four measurement values discussed above and the addition of three others: fecundity, purity, and extent. *Fecundity* was the likelihood that the action would produce more pleasure, *purity* referred to the pain that would accompany the action, and *extent* was the number of individuals who would be affected by the action. Bentham believed that we all intuitively use a hedonic calculus when faced with making decisions to maximize our pleasure and minimize our pain. Therefore, he developed this hedonic calculus of seven values to add a scientific aspect to his theory, which has also been called the greatest happiness principle of utility or felicity of expression.

Another utilitarian, a friend of Bentham's family, John Stuart Mill (1806–1873) disagreed with Bentham's approach to a hedonistic calculus and believed it to be too narrow. Strangely enough, Mill was credited for coining the term *utilitarianism* and was unaware of Bentham's term, utilitarian. Nevertheless, the dichotomy in their theories mirrored the difference between Aristippus and Epicurus. Bentham, like Aristippus, believed in the quantity of satisfaction and that all pleasures were the same. Mill, like Epicurus, believed that all pleasures were not the same.

In his work *Utilitarianism*, Mill stated that some kinds of pleasures were more desirable and more valuable than others were. However, one of his fears was that a decision maker might not have experienced all the pleasures, which would be relevant when judging which one pleasure would be more desirable. For example, a child who has played a game may believe that she will receive more satisfaction from it than if she attended a poetry reading. Mill believed that many individuals, like this child who may not understand poetry or has never experienced poetry, were unable to evaluate the difference in quality between two different actions. As a result, they would not be able to determine which of these actions would yield the most satisfaction to the majority affected by them.

Mill was actually criticizing Bentham's quantity of pleasure theory and proposing a quality of pleasure theory, termed utilitarianism. Mill contended that there were two different types of desires: a higher level and a lower level. The lower level desires were like those of an animal, while the higher level desires were more valuable and could only be appreciated by a cultured person. Therefore, Mill was actually concerned that if given a choice between funding a symphony concert hall or a bowling alley, those not familiar with the arts would not fund the symphony hall, which he believed *ought* to be funded.

Yet ethical hedonism continues in the 21st century. For example, Peter Singer believed that if it is in the power of another to prevent something bad from happening, without sacrificing anything of comparable moral importance, it should be done. In measuring utilitarian pleasure, he believes that those "better off" should be in a position just below the worst-off people. In addition, he advocates euthanasia, abortion, and suicide. Furthermore, he believes that it may be more compassionate to conduct medical experiments on people with permanent disabilities than on sentient animals.

Criticisms of Ethical Hedonism

However, ethical hedonism has experienced many criticisms since its arrival in the philosophical world. Epicureanism clashed with the Cynics, who believed that civilization is corrupt and destroyed individuals by making them weak in their quest for the finer things of life. Also, it clashed with the Stoics, whose philosophy grew out of Cynicism. Stoics believed in self-control, detachment, and acceptance of whatever circumstances were created by a divine plan. The Romans, during the time of Cicero, believed that hedonism would lead to excess luxury, laziness, and self-indulgence, and was antithetical to Christian beliefs. Yet there were several 18th- and 19th-century critics as well.

One such critic was Immanuel Kant (1724–1894), who did not believe that any acts should be considered based on satisfying the majority of those affected by given actions but rather based on if they were the just thing to do. For example, giving money to charity to feel better or receive a tax break would not be a reason to do it. Kant believed one must always conduct his or her behavior based on duty and that any pleasure received should not be a motivating factor.

Another critic, Henry Sidgwick (1838–1900), believed that pleasure is when an individual experiences a favorable attitude toward the feeling (of pleasure). In other words, any feeling can result in pleasure, even an overstimulated nerve in a rotting tooth.

George Edward Moore (1873–1958), also a critic, believed that pleasure is *a good* but denied that pleasure is *the only good.* For example, he believed that pleasure could be the pleasurable feeling itself or the pleasure that eventually results. In addition, he believed that there were three intrinsic goods: pleasure, friendship, and aesthetic enjoyment, and that right actions increase these things. Another major criticism that could be used currently is that Enron, Ford, Exxon, Dow Corning, and several other corporations appear to be using ethical hedonism as a rationale for some of their unethical behavior.

—Martin J. Lecker

See also Bentham, Jeremy; Consequentialist Ethical Systems; Descriptive Ethics; Ethical Decision Making; Ethics, Theories of; Hedonism, Psychological; Instrumental Value; Kant, Immanuel; Kantian Ethics; Metaethics; Mill, John Stuart; Neo-Kantian Ethics; Sidgwick, Henry

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Hedonism, Psychological

Psychological hedonism is the view that all human action is ultimately motivated by desires for pleasure and the avoidance of pain. Since its defenders generally assume that agents are motivated only by the prospect of their *own* pleasures and pains, it is a form of psychological egoism. Psychological egoism is a broader notion, however, since one can hold that human actions are exclusively self-interested without insisting that self-interest always reduces to matters of pleasure and pain. As an empirical thesis about human motivation, psychological hedonism is logically distinct from claims about the value of desires. It is thus distinct from axiological or normative hedonism, the view that only pleasure has intrinsic value, and from ethical hedonism, the view that pleasure-producing actions are morally right. Psychological hedonism has been espoused by a variety of distinguished thinkers, including Epicurus, Jeremy Bentham, and John Stuart Mill, and important discussions of it can also be found in works by Plato, Aristotle, Joseph Butler, G. E. Moore, and Henry Sidgwick.

Psychological hedonists tend to construe "pleasure" very broadly, so as to include all positive feelings or experiences, such as joy, satisfaction, ecstasy, contentment, bliss, and so forth. Likewise, "pain" is typically understood so as to include all negative feelings or experiences, such as aches, discomfort, fear, guilt, anxiousness, regret, and so forth. Even construing pleasure and pain widely, however, it is implausible to think that all acts successfully produce pleasure or reduce pain. People are often mistaken about what will achieve these results, and in some cases aiming at pleasure is counterproductive (the so-called paradox of hedonism). Consequently, psychological hedonism is usually put forward as a claim about what agents *believe* or *take* to be pleasure producing and pain reducing. Hedonists also tend to assume that agents attempt to *maximize* their net pleasure over pain. They need not deny that agents frequently benefit others, however, since the thesis can be preserved by holding that other-benefiting actions are nonetheless hedonistically motivated. Hedonism itself is neutral as to which kinds of actions are a means to pleasure and about which kinds of experiences are pleasurable.

Psychological hedonism is usually defended by appealing to observations of human behavior, together with an implicit challenge to find alternative models of action that are equally explanatory and yet do not collapse into the hedonistic account. It would be refuted, however, by a clear case of nonhedonistic motivation. Standard counterexamples include the soldier on the battlefield who gives up his or her life to save comrades and the sacrifices of parents for their children. Hedonists usually respond to such examples by redescribing apparently altruistic motivations in hedonistically egoistic terms. The soldier, for example, may be said to have acted so as to avoid a lifetime of remorse. The fact that such redescriptions are possible, however, does not in itself make them plausible. Hedonists may also insist that attempting to obtain pleasure or avoid pain is part of what it *is* for something to be a motive. This move, however, transforms what purports to be a factual claim about human motivation into a trivial definitional truth.

—*Samuel V. Bruton*

See also Egoism; Hedonism, Ethical

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Herfindahl Index

The Herfindahl Index, often called the Herfindahl-Hirschman Index (HHI), is a measure of market concentration, which can be defined as the percentage of total industry sales that are contributed by the largest firms in an industry. The HHI is a measure of the size of firms in a given industry and an indicator of the degree of competition in that industry. It is a more sophisticated method of measuring market concentration than the more common method that uses the four-firm concentration ratio (the percentage of industry sales made by the leading four firms in a given industry). This measure is of interest to antitrust authorities who are trying to determine the impact of a proposed merger on competition in an industry. The formula for calculating the index is shown below.

$$\text{HHI} = (\text{Share } 1)^2 + (\text{Share } 2)^2 + (\text{Share } 3)^2 + \ldots + (\text{Share } n)^2,$$

where the terms in parentheses (Share 1, Share 2, etc.) are the market shares for each firm, the last term (Share *n*) indicates the market share of the last firm, and the superscript 2 indicates the market share is being squared.

For example, consider an industry consisting of six firms with the following allocation of market shares:

Firm A = 30%; Firm C = 20%; Firm E = 9%

Firm B = 25%; Firm D = 12%; Firm F = 4%

The HHI would be (900) + (625) + (400) + (144) + (81) + (16) = 2,166.

The HHI was first adopted in 1982 by the Reagan administration and is calculated as shown above by squaring the market share of all firms in the market and summing the squares. The premerger HHI number is then compared with the increase in the HHI that will be caused by a proposed merger. The HHI can vary from 10,000, in the case of a pure monopoly, to a number approaching zero in the case of an atomistic market. If the postmerger HHI is below 1,000, the industry is considered to have low concentration and the merger is unlikely to be challenged. If the postmerger index is between 1,000 and 1,800, the industry is considered to have medium concentration and the merger is likely to be challenged only if the increase is more than 100 points. If the postmerger HHI is above 1,800, the industry is considered to be highly concentrated and the merger is likely to be challenged if the increase is more than 50 points.

An advantage of the HHI is that it gives added weight to the largest companies on the assumption that these firms can exercise greater market control. The index helps differentiate between one industry in which four players have equal shares and another in which one player has a 70% market share and the three others only 10%. The former industry would be more competitive and have a lower HHI index. A disadvantage is that the HHI requires a substantial amount of information in that the market share of every firm in the industry is needed. In practice, however, the smallest firms in an industry can usually be left out of the calculation and this will not make a significant change in the final index.

—Rogene A. Buchholz

See also Antitrust Laws; Competition; Monopolies, Duopolies, and Oligopolies; Unfair Competition

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Hewlett-Packard

Hewlett-Packard (HP), the second largest computer company in the United States, was founded in 1939 by Bill Hewlett and David Packard. They were both graduates from Stanford University in 1934. The company originated from humble beginnings in a garage while they were still fellows at Stanford. The first product HP produced was a precision audio oscillator—used as a small night-light bulb to regulate a temperature dependent resistor in a critical portion of the circuit. The invention was one of many cutting edge designs that became the hallmark of excellence for HP. These types of products led to the firm being known as an innovator in developing precision instruments. HP over the next 50 years would develop many more breakthrough products that eventually provided it with a sizeable percentage of the precison measurement equipment market.

HP's corporate culture was modeled after a family-friendly environment driven by stability in a changing world. HP prided itself on using high ethical standards in conducting business activities. It invested not only in innovative concepts but in the very people who produced such ideas. Eventually, this collaboration between innovation and high ethical standards evolved into what is referred to today as "the HP way." It is important to note that HP is a company legendary for its innovations and respected widely throughout the industry as an institution with high business ethics. It has historically been recognized as an institution that practices social responsibility in every aspect of its business. Frankly, this was the legacy that HP's original founder left before retiring from the firm. HP has consistently been recognized for environmental excellence, energy conservation, engineering accomplishments, and most important, for having one of the best corporate environments to work in. The strategy of using breakthrough technology together with being a socially responsible firm led HP to become a leader in the technology field. HP was able to recruit top engineers to work for the firm, was successful in retaining top executives, and was renowned for having a great environment to work in. The company had this openness that exuded throughout the management ranks. It would be corny to say it had an open door policy, because it was much more than that. Employees actually believed in the company and were committed to the vision of the firm.

HP has developed a reputation over time for being an innovative company. It extended this perception in July of 1999, when it appointed Carly Fiorina as CEO. This appointment was significant because Fiorina was the first woman ever to serve as CEO of a company included in the Dow Jones Industrial Average, but in February 2005, Fiorina was forced to resign from her position as CEO. HP furthered that reputation when it appointed Patricia Dunn as the chairwoman of its board of directors. HP has always been a firm that was willing to take up socially contentious issues. Clearly having two females at the top of a Fortune 500 company helps to etch away at the myth surrounding the glass ceiling for women.

Recently HP had a setback that could have potentially destroyed its reputation and erased all the previous gains made over the past 70 years. In September 2006, a story was published that chronicled how the chairwoman of HP, Patricia Dunn, authorized a private detective company to search for the source of boardroom leaks to the media.

The purpose of this clandestine operation was to ferret out individuals who leaked confidential information regarding HP's long-term strategy to CNET. CNET Networks, Inc., is an Internet-based American media company in San Francisco cofounded in 1993 by Halsey Minor and Shelby Bonnie. A group of electronic-security experts spied on HP employees and business reporters, dug through their trash, and used a technique known as pretexting to obtain call records of HP board members and nine journalists, including reporters for CNET, the *New York Times*, and the *Wall Street Journal*. To obtain phone records, the investigators misrepresented themselves as the board members and journalists. Coincidentally, Dunn claimed she did not know beforehand of the methods the investigators were going to use in determining the source of the leak. One of the biggest mistakes HP committed was not doing the necessary due dilligence when hiring outside invesigators. It remains to be seen why HP contracted outside investigators in the first place—there's no question it hired the wrong ones.

It was later revealed that board members Gearge Keyworth and Thomas J. Perkins were the actual source of the leak. Subsequently, they were both removed from their position as board members. In addition, Dunn resigned as chairwoman of HP's board, and Mark Hurd, the CEO, was scheduled to succeed Dunn as chairman after the HP board meeting on January 18, 2007. Originally, California charged five people with four felonies, including conspiracy and identity theft. In January, the state dismissed its case against the fifth HP defendant, Bryan Wagner, a Colorado man believed to have been an employee of Action Research, when he pleaded guilty to federal charges relating to his role in HP's internal investigation of boardroom leaks. Under California law, the state cannot prosecute a defendant for conduct that has already been tried in another jurisdiction. On March 13, 2007, the three other remaining defendants—former HP attorney Kevin Hunsaker, private detective Ronald DeLia, and Matthew DePante of data-brokering company Action Research Group—pleaded no contest to a count of fraudulent wire communications at Santa Clara County Superior Court in San Jose, California. The trio was required to complete 96 hours of community service by September 12, 2007. Furthermore, the court stated that it would dismiss the case against them if this condition was satisfied. Similarly, in the same proceeding, Patricia Dunn did not enter any plea in response to the misdemeanor count, and the court exercised its discretion by dismissing the case against her.

On September 28, 2006, Ann Baskins, HP's general counsel, resigned effective immediately, hours before she was to appear as a witness before the House Committee on Energy and Commerce at which she would later invoke the Fifth Amendment to refuse to answer questions.

Even though HP is still combing through the tragic events surrounding Chairwoman Dunn's decision to monitor individuals, the company under the new leadership of Mark Hurd has continued to strive toward regaining that old HP standard for excellence. The stock has continued to perform exceptionally well. The company is achieving positive results from its strategy and is poised to regain its position as a leader in the electronics industry.

—Sylvester E. Williams, IV

See also Chief Executive Officer (CEO); Competition; Electronic Surveillance; Intellectual Property; Patents; Strategic Planning; Trade Secrets, Corporate Espionage and

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Hobbes, Thomas (1588–1679)

The powerful intellect of Thomas Hobbes was drawn to geometry, philosophy, the classics, ethics, history, and political theory. His reputation today turns especially on his political philosophy, which boldly advanced a materialist understanding of all things, denied free will, was atheist (beneath a thin disguise), and rejoiced in making the case that human beings are radically asocial and, if left alone, will tear one another apart. Not surprisingly, his books were sometimes banned, and he was often attacked as an enemy of religion and morality.

The practical thrust of Hobbes's political thought was conservative: He defended absolute monarchy and hence criticized liberty. But this conservative thrust took its impetus from the radical views listed above, and Hobbes thus is properly credited with being one of those groundbreaking thinkers who helped introduce the modern era at the expense of the intellectual world that preceded him, one dominated by Aristotle and the Scholastic thinkers of the Roman Catholic tradition.

Notwithstanding shallow bows to the religious tradition, Hobbes roots his anthropology and his politics in a naturalistic account of man. In lieu of the Garden of Eden and divine enjoinders to seek a heavenly perfection, Hobbes discovers an original condition of man in which we "enjoy" utter liberty, but our natures drive us into ceaseless and unmitigated conflict, a war of all against all. Under such circumstances, securing our earthly preservation is our first and most powerful preoccupation. Politics is merely the most important artifice in our struggle to secure our lives: We create a powerful state, if we are prudent, to distance ourselves as far as possible from the horrors of natural anarchy. To create this state, we agree with other potential citizens to limit our liberty and support a sovereign with all our power, in the calculated expectation that the sovereign will then see that it is in his interest to protect and advance the state over which he presides. This Hobbesian version of the social contract is thus binding on citizens, not on the sovereign—a point that would occasion objections from Hobbes's followers.

The creation of an absolute sovereign requires that a large measure of our natural liberty be surrendered; but Hobbes sees this as no sacrifice at all, for our natural liberty, though vast, is utterly without value: To be free to do whatever one wants is a deadly freedom, since others enjoy it as well. Absolute freedom is absolute anarchy, and for such antisocial creatures as Hobbes's human beings, absolute anarchy results in a life, as he famously put it, that is "solitary, poor, nasty, brutish, and short." It is on the foundations of a destructive absolute natural liberty for individuals that Hobbes makes the case for absolute authority of the sovereign.

Since Hobbes did not defend individual rights against governmental authority, he does not figure prominently in discussions of the history of capitalism. He did, however, attack prior ideas about inherent value or a just price, and this prepared the way for the market to become a key measure of value. Even of a human being, for example, Hobbes said, "The 'value' or 'worth' of a man is, as of all other things, his price; that is to say, so much as would be given for the use of his power." And Hobbes's attacks on loftier views of happiness or felicity paved the way for a new prominence of "acquisitive man." Hobbes stressed, for example, that there was no such thing as "the repose of a mind satisfied." To the contrary, happiness or "felicity" is the continual movement from a desire, to its satisfaction, to the emergence of a new desire, and so forth, ceasing only in death. Man is by nature a creature of desire and ineluctably a sort of consumer.

Hobbes's critique of liberty makes it right to distinguish him sharply from John Locke. Nevertheless, it was Hobbes who first proclaimed the right to life, Hobbes who first emphasized equality as a decisive political fact, Hobbes who first based his theory of asocial man and self-interested morality on a state of nature, and Hobbes who led the way in stressing the primary importance of rights sought by individuals for themselves rather than duties owed to either God or the political community. If the modern West is defined in significant measure by its candor and consistency in putting first the individual and his or her rights, Hobbes is one of its most influential founders.

—Wayne Ambler

See also Individualism; Locke, John; Rousseau, Jean-Jacques; Social Contract Theory

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HONESTY

Honesty is defined as being truthful or having integrity. Because these characteristics are generally regarded as desirable, honesty is considered a cornerstone for any social interaction. Its value is especially conspicuous in business because commerce requires a network of transactions between suppliers, consumers, employees, and the public. For a company to thrive, it must have the trust of all these entities, something that is possible only if they have confidence in the company's honesty. Indeed, a reputation for honesty is crucial to a company's sustainability and success.

Evidence that this is widely understood is found in many business practices. Employers often attempt to screen employees for honesty by, for example, checking on the facts included in a résumé or even requiring a lie detector test. Companies routinely include a commitment to honesty as part of their code of ethics or mission statement. Contracts can also be understood as a legal tool for enforcing honesty in transactions.

The impact of dishonesty on the fortunes of companies and individual employees is also clear. Employees are most likely to be dismissed and companies are most likely to be embroiled in scandal when they attempt to deceive supervisors, the public, shareholders, or regulators about a problem. In one recent example, the chief executive at Hewlett-Packard was obliged to step down after it was discovered that the company had attempted to plug information leaks by pretexting or using false pretenses to obtain personal information about reporters and members of the company's own board of directors.

Like other ethical concepts, honesty often proves elusive on closer examination. For one thing, the ethical question of when and whether people should tell the truth is easily confused with the epistemological question of whether people can know the Truth. Philosophers continue to struggle with the question of how Truth is to be determined, how it can be distinguished from error, and whether Truth can be communicated adequately by language. In addition, the points of view of different individuals create challenging issues about subjectivity and Truth, something that is obvious to anyone who has ever asked more than one person about what happened at a meeting.

Some critics also contend that 20th-century scholarship insisting all Truth is situated and vulnerable to deconstruction has seeped into public discourse and undermined the commitment to honesty as a default position. Also, in the empirical sciences, psychologists have evidence that many successful people and companies cultivate an optimistic, if not unrealistic, appraisal of their prospects. Positive thinking as well as public relations and spin control deliberately reinterpret facts to support a particular point of view, blurring the question of what is true. Harry Frankfurt and others have argued that such efforts erode a commitment to honesty because they focus on the task to be accomplished without attempting to honestly ascertain the facts of the matter.

Even Aristotle found it difficult to pin down honesty. Although he praised it as "noble," he also believed that honesty, like other virtues, was subject to the Golden Mean because it was vulnerable to excess and deficiency. Too much honesty becomes boastfulness or indiscretion; too little turns into false humility or leaving people in the dark about things they need to know. This understanding foreshadows contemporary tension between transparency and privacy. Some argue, for example, that honesty requires utter openness, especially about financial transactions. At the same time, many individuals and, for that matter, business entities claim that it is appropriate to keep financial information confidential.

When Dishonesty Is Forbidden

Because honesty is so difficult to define, many moral philosophers do not insist on a positive duty to be honest. Instead, they argue the less rigorous position that people have a negative duty to avoid dishonesty—a concept that is defined by two characteristics. First, dishonesty requires information that is, as far as the speaker knows, factually inaccurate. Second, it involves an attempt to communicate that information in a way that will mislead another person. Although a spoken lie is the most obvious form of deception, people can also be misled indirectly through dissembling. A company that sells counterfeit goods, for example, may not claim that they are genuine, but the appearance of the merchandise leads consumers to a false belief about their origin. Whether it is direct or indirect, dishonesty is the deliberate effort to convince the deceived person of something the deceiver does not believe to be true. Someone who is mistaken about the truth can be regarded as ignorant but not dishonest.

A few philosophers have taken the position that dishonesty of any kind is never justified. Augustine, for example, claimed that all lies are forbidden by God. Immanuel Kant is sometimes understood to have claimed that truthfulness is a duty that trumps most others. He contended that dishonesty undermined autonomy by treating other people as means and not ends. Lying to people even for their own apparent good is unacceptable according to Kant because it deprives them of the right to determine good for themselves.

Other philosophers have argued that other goods must override honesty under some circumstances. The legal philosopher, Hugo Grotius, for example, argued that honesty is owed only to those who deserve it. Indeed, many social scientists have observed that people often have different standards of honesty for those inside a favored group and those outside. A company may, for example, provide one version of the truth to upper management and a different version to labor, stockholders, or the press.

A few philosophers have actually argued that honesty is overrated. The Sophists of ancient Greece, for example, were committed to winning legal cases, not defending the truth—a legacy that is apparent in the legal profession today. Plato himself argued that politicians might need to use "noble" lies to keep their citizens content. Machiavelli and Nietzsche thought it legitimate for "superior" people to lie to their inferiors. A manager, for example, might justify misleading the sales department about a problem on the production floor, reasoning that it will undermine their morale if they know the truth and that, in any case, they are not in any position to solve the problem.

In fact, a person who is dishonest when others are trusting does have a competitive advantage. Evolutionary biologists point out that other living things regularly obtain survival advantages by deceiving both predators and competitors. There is considerable evidence that humans, too, have thrived in the past by being deceitful under certain circumstances. Most philosophers, however, are convinced that when animals band together into social units, the advantages obtained by deceit are short term at best.

This aligns with the commonsense intuitions of most people. Because they prefer that other people be candid with them under most circumstances, they are required by nothing more than the rule of reciprocity to be honest in return. Contemporary virtue ethicists argue that an honest person tells the truth, not because it is advantageous in a given situation but because the truth has intrinsic value to people who hope to have ongoing interactions. If people cannot assume that others are telling the truth, suspicion replaces cooperation and human society breaks down. Given the seriousness of this result, they insist that honesty must be the default position.

This approach does not rule out the possibility that dishonesty may be the right strategy under certain circumstances. In business, people often make a utilitarian analysis of honesty, deciding whether deception is warranted in light of potential risks and benefits. Companies, for example, routinely face issues about honesty in the marketing of their products. Advertising often involves a poetic rather than a scientific description of products. This is widely understood and tolerated by the public. When a company claims that a cleaning product smells "springtime fresh," consumers understand the statement as an opinion and not a verifiable fact.

On the other hand, blatant dishonesty in advertising is both illegal and self-defeating. The Federal Trade Commission (FTC), which is responsible for enforcing truth in advertising, points out that deceptive advertising can take many forms including misleading promises, incomplete or distorted descriptions and visual representations, partial disclosure of pertinent facts, misleading comparisons with other products, and false testimonials. The FTC requires companies to have evidence that supports statements of fact including claims that are implied by advertising. If, for example, a diet product claims to suppress appetite, a reasonable consumer would conclude that it leads to weight loss, and the company would need to substantiate those claims. Even when deceptive advertising does not run afoul of regulation, it risks alienating customers, who will feel betrayed when the product does not deliver what it has promised.

Evaluating the Consequences of Dishonesty

In evaluating the consequences of dishonesty, it is necessary to consider the harm done to both the deceiver and the deceived. The harm to the victim is most conspicuous. A lie always threatens autonomy because people who have been deceived look back on their decisions and realize that they might have made different choices if they'd had honest information. The harm to the dishonest person is often overlooked because liars tend to see only the advantages of their dishonesty. Sissela Bok points out that liars are harmed in three ways. First, their own sense of integrity is undermined. Second, they must expend energy in remembering the lie and, perhaps, telling other lies that reinforce it. Finally, should the dishonesty be uncovered, the person who practiced it is less likely to be trusted in the future.

Because it is difficult to make such an analysis on a case-by-case basis and because it is challenging to fully anticipate the consequences of dishonesty, many utilitarians try to determine rules that will help them decide when deception is acceptable. Even Aquinas proposed a hierarchy of deception. Malicious lies, told with the intent to cause harm, were the only ones he regarded as a mortal sin. Today, they are the lies most likely to be prosecuted as fraud. Jocose lies told in jest were considered less serious just as office pranks and April Fool's jokes are tolerated as annoying but harmless.

The third category, officious lies, continues to arouse debate. These minor deviations from the truth, undertaken because they will produce benefit or forestall harm, are well known in business. Mild forms of deception often seem justified or even necessary in social situations because they produce harmony among people who are actually quite different. When an employee, for example, asks about a colleague's weekend at the water cooler, there is no expectation of a thoroughly honest response. The gesture is understood on both sides as a superficial expression of courtesy. Similarly, an employee may feign an interest in the hobbies or children of a potential client. People justify these so-called white lies because they seem to do little harm, and they may create social benefits, such as a sense of commonality, that makes it easier to do business together. Far from being censured, these forms of dishonesty may actually be encouraged and rewarded.

Dishonesty to avoid harm is more problematic. Some people argue, for example, that it is acceptable to be dishonest in an effort to spare another person's feelings. Others point out that insincere compliments or inaccurate excuses are actually for the convenience of the dishonest person, so they cannot be justified as altruistic. Another form of officious lies deserves special attention from companies. Corporate policies can make people reluctant to admit mistakes because the penalties for error are perceived to be too great. Under these circumstances, people are more likely to be dishonest about errors and other problems. Businesses can reduce the incentive for this kind of dishonesty by redefining accountability in terms of problem solving rather than assigning blame.

One rubric for evaluating officious lies and, for that matter, other forms of dishonesty is proposed by Sissela Bok. She points out that honesty never needs justification but dishonesty must be able to meet three criteria: First, is there an alternative to dishonesty? If there is an honest way to avoid the unwanted harm or produce the desired benefit, it is preferable. Second, what are the moral reasons for dishonesty? Clarity about the principles that might justify dishonesty is crucial because then they can be weighed against the benefits of honesty. Finally, will the dishonest act pass the test of publicity? Lies are often motivated by self-interest that will not be persuasive to other interested parties such as employees, stockholders, the press, or regulatory agencies. Individuals and companies that apply these tests may, indeed, conclude that honesty is the best policy.

—Carolyn Jabs

See also Advertising Ethics; Privacy; Reputation Management; Scandals, Corporate; Transparency

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HOSTILE WORK ENVIRONMENT

A hostile work environment is created as a result of harassment that makes individuals feel uncomfortable and unwelcome. Speech or behavior that creates a hostile work environment is unwanted, uninvited, offensive to a reasonable person, and severe or pervasive enough to adversely affect the person's work environment. The speech or behavior may be verbal, nonverbal, and/or physical, and may be based on race, religion, sex, national origin, age, disability, veteran status, or, in some jurisdictions, sexual orientation, political affiliation, citizenship status, marital status, or personal appearance.

The primary challenge of harassment law is to define when speech or behavior becomes so severe and prevalent that it creates a hostile environment for the target. In general, when determining the existence of a hostile work environment, the court considers whether speech or behavior is appropriate in a workplace that strives to provide a pleasant, productive atmosphere for all employees.

Most antidiscrimination laws, such as Title VII, the Americans with Disabilities Act, the Age Discrimination in Employment Act, and various state and local laws, do not explicitly discuss harassment. These laws prohibit discrimination in the terms, conditions, or privileges of employment; however, the courts have interpreted these definitions to bar not only discrimination as it is traditionally understood but also harassment that may create a hostile work environment.

On its face, harassment law draws no distinction between slurs, pornography, political, religious, or social commentary, jokes, art, other forms of speech, and unwanted physical contact. All can be punished, so long as they are severe or pervasive enough to create an intolerable environment for a reasonable person. The vagueness of the terms *severe* and *pervasive* and the fact that the law is implemented by employers who have an incentive to be more rather than less cautious, means that the law may practically restrict any speech or behavior that an employer concludes may be found by the courts to be severe or pervasive enough.

In the current legal environment, it is not enough for employers to prove that they followed standard procedures in response to complaints of a hostile work environment; they also need to demonstrate that they have been proactive in preventing the behavior from occurring in the first place. A comprehensive harassment prevention program will include clear definitions of what a hostile work environment is and why it happens, ongoing assessment of the work environment, education for all employees, skilled professionals to administer the program, and effective and consistent follow-through on all complaints with a zero-tolerance response to violations.

—Carmen M. Alston

See also Age Discrimination; Disability Discrimination; Diversity in the Workplace; Employee Monitoring and Surveillance; Employment Discrimination; Equal Employment Opportunity; National Origin Discrimination; Religious Discrimination; Sexual Harassment

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Human Capital

Capital is an asset or advantage from which an economic return can be earned. Human capital is one of the various forms of capital. Human capital comprises an individual's knowledge and skills. Human capital can be broken down into general and specific forms. General forms of human capital, as the name implies, refers to knowledge and skills that can apply to a variety of settings and situations. Examples include a person's general mental ability and skills such as communicating, motivating, and information-processing that apply across settings and situations. Unlike general forms of human capital, specific forms of human capital tend to be of value only to targeted sectors or organizations. For these reasons, specific human capital is often further refined to reflect firm-specific and industry-specific dimensions. Firm-specific human capital refers to the knowledge, skills, and abilities that are particularly productive and valuable in working within the firm. Knowledge of internal operations of the firm, tacit knowledge of the eccentricities of various operational personnel, communication styles that are compatible with the culture of the firm, and the set of managerial skills "tuned" to the particular needs of the firm are all examples of firm-specific human capital. In comparison, knowledge of industry trends is indicative of a person's industry-specific human capital. Human capital is particularly important in more developed economies where upward of 50% of a nation's gross domestic product is knowledge based. Sectors such as the computer, software, pharmaceutical, and education industries are particularly dependent on human capital to compete.

Difference Between Human Capital and Other Forms of Capital

There are some key differences that distinguish human capital from more traditional forms of capital such as physical assets and financial capital. A key difference is that human capital resides inside individuals and individuals own their own human capital. While organizations may try to use an individual's human capital, the ultimate choice to deploy human capital rests squarely with the individual. Closely related to this point is the fact that human capital is a mobile good. It can leave the firm temporarily; such is the case when a person leaves at the end of the workday or it can be lost on a more permanent basis (e.g., when an individual quits current employment to work for a competitor). Thus, a major goal of most firms, usually through the Human Resources (HR) function, is to encourage employees and managers to share their knowledge and skills with others inside the firm and systematize such knowledge in the firm's routines and practices. When such sharing occurs, human capital is transformed from a private good to a public form of capital that the firm can choose to exploit for competitive advantage. A firm's HR practices should, therefore, devise ways to develop, enrich, and retain human capital and ensure that human capital stays within the boundaries of the firm.

Another pivotal difference between human capital and more traditional forms of capital is that human capital can actually appreciate, not depreciate, with use. It is important to note, however, that just as human capital can work to the benefit of the firm, human capital can also work directly against a firm's goals or mission. This phenomenon can take several forms. Specifically, whereas a production line or an oil field as forms of capital cannot refuse authority or become unmotivated, that very possibility is clearly evident with human capital. Said differently, human capital can resist authority or can even slow down or stop working with ebbs and flows of motivation. At its worst, human capital can be used to extort or exploit the firm in terms of theft, corruption, or sabotage. Indeed, over the last several years, there have been notable and well-publicized cases in which knowledge and skills were used to hurt, not help, a firm.

Another defining characteristic of human capital is that it is difficult to measure or assess. For instance, revenue per patent, percentage of employees holding an advanced degree, years of experience in a given profession, and turnover ratios have all been used to attempt to capture a firm's human capital. Very generally, education and amount of training are among the most widely accepted measures of human capital. Traditional proxies of general, firm-specific, and industry-specific human capital include educational level and pedigree, firm tenure, and industry tenure, respectively. Most experts on human capital suggest that to understand the value of human capital to the firm, one needs to examine how human capital contributes to a firm's competitive advantage.

Human Capital as a Source of Competitive Advantage

There are two broad theoretical perspectives that appear to embrace human capital as a source of firm competitive advantage. The first is that of the resource-based view (RBV) of the firm. According to the RBV, a firm can create and sustain a competitive advantage mainly by possessing, developing, and using resources. Not all firm resources are created equal, however, and for a firm to enjoy a true competitive advantage, the resource must be valuable, rare, inimitable, and nonsubstitutable. Unlike traditional forms of capital, human capital seems to meet most of these conditions and, as a result, provides a source for competitive advantage. Human capital is especially important for firms operating in complex and dynamic competitive environments, where the ability to rapidly notice, access, acquire, and assimilate knowledge and capabilities is critical to have advantage over competitors. While competitors can more easily understand and duplicate a firm's physical assets, it is very difficult to copy unique, complex, and tacit knowledge held by the employees of the firm. Therefore, both academics and managers tend to agree that human capital is the premier source of future competitive advantage for a firm. For instance, McKinsey and Company suggest that the most important corporate resources over the next 20 years will be talented individuals who are technically astute, globally aware, and sophisticated in thought. Economists and the like tend to agree by noting that traditional sources of advantage, such as financial capital and scale economies, are weakened by environmental forces such as globalization.

The other perspective closely related to the RBV described above is the knowledge and learning-based view of the firm. According to this perspective, firms enjoy advantages when they create new knowledge and then effectively use that knowledge in creating value-added products and services for superior returns. This perspective suggests that knowledge that is tacit, complex, and causally ambiguous helps firms create and sustain competitive advantages. Since individuals are the primary source of a firm's knowledge, firms with high levels of human capital and that can use such capital are likely to create and sustain competitive advantages. The processes of acquiring external knowledge and internally creating new knowledge are inherently human processes. Development of tacit, complex, and socially embedded knowledge is possible when a firm's human resources engage in "dialogue" to create new knowledge. This circumstance also suggests that for a firm to engage in innovation and entrepreneurial discovery, it needs to possess and/or develop requisite amounts of human capital. Both the RBV and knowledge-based perspectives suggest that compared with more traditional assets such as land, plant, and equipment, human capital provides more unique and enduring advantage to the firm by contributing to innovation, strategy development, and superior execution.

While human capital is important across all levels and functions of a firm, human capital of senior executives is pivotal from the perspective of firm strategy and competitive advantage. Human capital of the chief executive officer, other members of the top management team, and the board of directors becomes extremely critical in strategic decision making. These individuals often use their human capital to develop and formulate a firm's strategy. At the upper echelon of the organization, human capital is usually deployed to scan the internal and external environment, process relevant information for decision making, recognize and seize opportunities, and solve problems. Senior managers enjoy both tremendous scope and discretion in their decision-making process. In other words, when executives effectively deploy their human capital, they are likely to contribute to the firm's strategic advantage. Because of this contribution, executive human capital is highly researched and is also highly correlated with executive compensation levels: Those with higher levels of human capital are rewarded in the highly competitive executive labor market with higher compensation packages.

Human capital is of unequal value to the firm. In particular, human capital can either be a core or a peripheral asset. Core human capital reflects an individual's knowledge and skills that directly translate into firm benefits. Without core human assets, it is difficult for a firm to remain competitive. In contrast, some human capital is peripheral in nature, meaning that a person's knowledge and skills only weakly or tangentially affect a firm's ability to compete. Thus, the level of authority, the importance of the job, and the discretion afforded a particular person all influence how a person's human capital affects a firm's overall competitive stance.

Developing and Managing Human Capital

Human resource management practices (HR practices) can play a major role in ensuring the development, retention, and use of human capital for organizational advantage. One of the initial areas in which HR can have an impact on human capital is during the recruiting and selection stages of HR staffing. Rigorous and systematic selection standards ensure that a baseline level of human capital within the firm is achieved. Recruiting from diverse sources to include individuals from other firms and other industries is important since progressive firms attempt to seek and build a diverse set of skills and knowledge capabilities. Once individuals are hired and brought inside the boundaries of the firm, HR plays a critical role in developing human capital. Human capital can be developed through practices such as training, coaching, and mentoring. Indeed, a desired outcome of such efforts is an increase in learning, which improves individuals' knowledge and skills. HR managers need to ensure that employees and managers use their human capital to achieve organizational goals and outcomes. Perhaps the best way to ensure that human capital is used to support organizational goals is through well-designed compensation plans. For instance, variable pay plans that tie pay to some measure of performance is a mechanism to motivate individuals to use their human capital in a way that benefits both themselves and the firm. Another proven way to promote the sharing and deployment of an individual's human capital on behalf of the firm is to launch and administer a gainsharing type of plan. Gainsharing plans involve sharing financial gain between the employees and the firm for increases in productivity and profitability. One of the most notable benefits of gainsharing type plans is that they encourage employees at all levels to share their unique knowledge and skills on ways to improve processes through the "suggestion" component of a typical gainsharing plan. Without gainsharing plans that reward and recognize suggestions for organizational improvement, the knowledge and skills embedded within an individual are more likely to remain dormant and a private good. Finally, HR must ensure that their compensation plans are competitive with both the internal and external markets. If compensation equity is not monitored, HR runs the risk of losing their human capital to other firms, including competitors that are willing to pay more for an individual's knowledge and skills.

One common problem facing a firm is the decision to make or buy human capital. Recent well-chronicled cases within the technology and Web sector suggest that this make or buy decision toward human capital is driving a phenomenon termed *talent poaching*. Talent poaching is when a firm allows a competitor to train, develop, and "make" human capital and then offers a higher compensation package to the individual to lure the human capital from the very firm that spent so much on creating and developing it. One unintended consequence of talent poaching is that firms have less incentive to invest in the making and developing of human capital because trained and talented individuals may be lured away by a competitor. Because of this reduced incentive, many individuals choose to develop their own human capital rather than expecting an organization to do so. Hence, developing human capital is now more of a personal responsibility as opposed to a corporate one.

The role of human capital may well rest in a firm's ability to create social capital. When two or more individuals collaborate and share knowledge and skills, the human capital of the individuals is transformed to social capital, which can then be effectively used by the organization to pursue its strategies. This social capital is particularly important since sophisticated, refined, and potent knowledge is best achieved through combination, exchange, and collaboration. Also, some evidence suggests that tacit knowledge, a type of knowledge that is difficult to codify and also difficult for competitors to imitate, is best created when more than one person is involved. If, indeed, superior learning can only result from social interaction, then the imperative of the firm is to combine human capital in a manner that produces social capital. Keep in mind that the value of social capital is directly related to the quality of its inputs—namely, human capital. Thus, individuals with superior levels of knowledge and skills are a necessary, but not sufficient, condition for producing high values of social capital. An ancillary benefit of this human capital to social capital relationship is that social connectedness may help anchor or at least slow the mobility of human capital out of a given firm.

Ethical Considerations in Managing Human Capital

It is quite clear then that human capital should be managed; but what is particularly intriguing from an ethical vantage is the question of *how* human capital should be managed. Unlike traditional forms of capital, people holding human capital have emotions and feelings. For this very reason, attempts to manage human capital like other entities, such as factors of production that are bought and sold regularly, should be met with caution. If human capital is viewed primarily as a *fixed* asset that cannot be bought and sold in the market, firms would continuously invest in the development and utilization of human capital in their employees. On the other hand, if it is approached as a *variable* cost or asset that can be bought and sold through market transactions, companies may not invest in developing human capital and may even lose their existing human capital. Importantly, embedded in each orientation is an ethical concern regarding the inherent worth of an individual and a firm's obligation to consider the emotional factor that also accompanies an individual's knowledge and skills. Of course, this added emotional dimension is absent in traditional forms of capital and, for that reason, poses challenges to those who manage human capital.

If we think of human capital from an individual's perspective, some additional interesting ethical issues arise. For example, it is likely that people with high human capital will have greater influence and bargaining power inside an organization. As a result, they may be able to bargain for higher compensation, which will further widen the already large compensation gap in the organization. Another interesting issue is the appropriation of the value created by human capital. If a person with high human capital creates a certain amount of value to a firm, how much of that created value should be received by the person versus the firm? Another issue concerns the treatment of humans as a "resource" or a "piece of capital." Since business tends to exploit its capital and resources, there is a real danger that people will be treated as a resource that firms can increase and decrease whenever they want to do so. This approach could dehumanize the managerial ranks along with the labor force.

As long as developed nations continue to move away from traditional manufacturing as an economic engine in favor of technology, knowledge, and service type sectors, human capital will likely only increase in importance. Consequently, those who can effectively manage this unique form of capital are more likely to successfully compete in the new knowledge-based marketplace.

—Devi R. Gnyawali and Evan H. Offstein

See also Employment Contracts; Empowerment; Executive Compensation; Intellectual Capital; Leadership; Networking; Reputation Management; Social Capital

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Human Genome Project

The *Human Genome Project* (HGP) is a U.S. government project with the goal of mapping the entire genetic structure of humans. The project has raised a host of ethical issues and has complicated existing ethical topics involving genetics. Among these issues are those surrounding both prenatal and adult genetic testing, the proper use of genetic information and genetic profiling, gene therapy, gene patents, genetic enhancement of individuals, and issues involving the just distribution of genetic resources.

A *gene* is the fundamental unit of heredity. It is a *nucleotide* (a sequence of DNA) that contains instructions for making proteins, the basis of cellular structure and metabolism. The *genome* refers to the DNA contained in each cell, including so-called junk DNA (more than 98% of DNA), which does not code for proteins. The *genotype* is the entire genetic structure of the organism, which includes all the genes in the organism. The *phenotype* refers to the physical traits of an organism; these are not only determined by the genotype but also by environmental factors. *Genomics* is the study of genes, focusing on their role in disease processes. *Pharmacogenomics* studies the way in which drugs interact within a person's body based on that individual's genotype.

History of the Human Genome Project

In 1984, the Department of Energy (DOE) sponsored what was later labeled the "Alta Summit" in Alta, Utah. Ostensibly, the conference's goal was to find better means of detecting mutations in atomic bomb survivors, but discussions expanded to encompass genetic research in general. The summit catalyzed further discussion, including the possibility of mapping the human genome. As a result, Charles DeLisi, director of the DOE Health and Environmental Research Programs, formally proposed the Human Genome Project in 1986. After considerable debate and two failed bills in Congress, the HGP was funded as a joint project of the DOE and the National Institutes of Health (NIH), and it began in 1990. The goal was to complete the mapping of the human genome by 2005. In 1998, Craig Venter's company, Celera Genomics, began its own version of the HGP. His goal was to patent genes and gene sequences for eventual profit via selling rights for their use to pharmaceutical firms and other interested companies. His work was more cost-efficient than the federal project, costing only 10% of the official HGP. It is possible that the competition between the two projects speeded the process of sequencing the genome, and on June 26, 2000, U.S. President Clinton and U.K. Prime Minister Blair jointly announced the completion of a rough draft of the human genome. The full project was "completed" in 2003, 2 years ahead of schedule, with Celera and the NIH/DOE group making the announcement on April 14. Work on details and potential applications of the HGP will go on indefinitely.

Potential Benefits of the Human Genome Project

The HGP is thought to have great potential for improving human health. First, the genes associated with debilitating and fatal diseases could be identified. Genes for cystic fibrosis and Huntington's disease, a genetic-linked disease in which victims, usually around the age of 40, begin to suffer degeneration of brain tissue and eventual death, have already been discovered. The HGP opens the possibility of discovering genetic links to such conditions as Alzheimer's disease and some cancers; the BRCA gene, for example, has been linked to a higher risk of breast cancer in women. Once the genes linked to a disease are identified, research can then focus on methods of gene therapy to cure or mitigate such gene-linked conditions.

A second, more controversial, potential benefit of the HGP is the possibility of improving the human species. If certain genes could be found that are linked to athleticism or high intelligence, then gene therapy could be used to make "designer babies," with genetic traits correlated to the skill of their parents' choice. Many geneticists dispute the possibility of such improvements, arguing that (1) most genetic-linked traits do not involve only a single gene but rather the interaction of multiple genes and (2) the environment plays an indispensable role in the expression of the phenotype.

Ethical Issues Involving Prenatal Genetic Testing

Many of the ethical issues surrounding the HGP are the same ones that are raised by genetic research as a whole. The reason is that the success of the HGP will lead to more successful uses of existing genetic techniques. For example, if the HGP results in specific genes being identified as correlated with a serious health problem, such as abnormally high cholesterol, then it may be possible to use existing techniques of gene therapy to alter the affected genes. Issues arise surrounding the moral rightness or wrongness of gene therapy, whether somatic, in which the therapy targets the tissues or organs of the individual with a genetic disease and thus affects only that individual, or germ-line, in which the therapy targets the germ cells (sperm or egg) and thus the changes in the genetic code are passed on to the individual's descendants. These issues had been hashed over many times before the HGP became a reality, and the debate will intensify due to the success of the project.

As the techniques of identifying prenatal genetic problems improve, moral debates over issues such as abortion move to the new context of gene testing and gene therapy. If a fetus is identified as having the gene for cystic fibrosis, should the parents carry the fetus to term or abort the fetus? Some have argued that it is best for parents to abort on utilitarian grounds, for a child with cystic fibrosis will suffer a great deal before dying at a relatively young age. Opponents of abortion believe that since the fetus is a human person it is morally wrong to abort the fetus. They also argue that considerable pressure may be placed on the woman to have an abortion in such situations. But the issue becomes even more complex when extended to diseases that are not as strongly genetically linked. What if genetic testing determines that a fetus has a gene correlated with a greatly increased chance of breast cancer or a greatly increased chance of early onset heart disease? If there were no gene therapies available to alter the affected genes, would it be morally acceptable to abort a fetus for having these propensities? What if a fetus has a gene that is linked to a greater chance of schizophrenia or autism? Would abortion be acceptable in those situations?

In the future, gene splicing and recombinant DNA technology may become accurate enough to eliminate a gene-linked condition from the fetus before birth. Although somatic gene therapy on an embryo is relatively uncontroversial, germ-line therapy raises a host of issues about the advisability of altering human evolution and about the unintended negative consequences of "permanently" eliminating a defective gene from the human genome.

Genetic Testing, Genetic Information, and Genetic Profiling

First, a set of issues arises concerning how to deal with genetic information. The HGP has already led to the discovery of genes linked to tendencies for breast cancer and arteriosclerotic heart disease, and this list will expand over time. Suppose that a gene is discovered that is directly linked to a fatal disease; Huntington's disease, for which a gene has already been discovered, is an example. Huntington's is one of the potentially fatal diseases for which there is no effective treatment. It is an autosomal dominant disease; if one parent has the disease, the children have a 50:50 chance of having the disease. If a father knows he has Huntington's disease, should his children be tested? Even if some or all of his children have the disease, they will most likely not suffer symptoms until around age 40 (though they may suffer symptoms earlier or later). Some adult children of Huntington's patients do not wish to be tested for the disease. The question arises as to whether there is a moral obligation for those who have a strong potential of having a genetic-linked disease or being a carrier of the disease to receive genetic testing. Advocates of patient autonomy could argue that testing is up to the patient alone; a possible utilitarian response is that testing is necessary so fewer children with genetic disease will be born.

Advice concerning options after genetic testing is often given by genetic counselors, most of whom claim to be value neutral in their approach. They argue that neutrality is necessary because of past abuses (by the eugenics movement in the United States and by Nazi Germany) in which extreme control was placed over reproduction. In the United States, this involved sterilizing thousands of people with mental illness and mental retardation; in Germany, it involved selective breeding to create a "super race." Genetic counselors wish to avoid any hint of coercion. Thus, even in situations in which a child is tested for genetic defects, and it is thereby discovered that the male guardian is not the biological father of the child, genetic counselors do not believe that he should be informed. Critics argue that there is no such thing as value neutrality—that even the claim that "we should be value-neutral" is itself a value judgment. In addition, genetic counselors placing patient autonomy above other principles, such as beneficence or nonmaleficence, are making a value judgment. Critics argue that genetic counselors should admit from the start that they are not value neutral and that they should lay out what their values are.

A second issue surrounding genetic information involves health and life insurance coverage. As more genes are discovered that are correlated with an increased risk of major diseases, such as heart disease and cancer, insurance companies can use genetic testing to either deny insurance coverage (either completely or for a specific condition) or raise rates for people testing positive for genes connected with such diseases. Insurance companies may require genetic testing before offering coverage. In addition, life insurance companies could deny coverage to individuals or charge higher rates based on their genetic profiles. What is new about such denials of coverage is that the individuals denied do not actually have the disease but a genetic tendency for higher risk of getting the disease. Insurance companies argue that they should have the right to make decisions concerning coverage based on genetic testing. They claim that such decisions are in accord with actuarial fairness since higher risks mean higher costs for the insurance company because individuals at high risk for debilitating diseases often suffer from those diseases. Expensive treatment implies expensive claims, and these raise the insurance costs for everyone else. Critics reply that it is unfair and also a form of discrimination to penalize individuals for genetic susceptibilities, for not every susceptibility is translated into disease. Plus, people can no more help the genetic profile with which they are born than they can help their race or sex, and genetic discrimination is no different from racial or sexual discrimination.

There is also the possibility that employers will reject job applicants due to their genetic profiles. Critics argue that this is also a form of morally unjustified genetic discrimination. Most states have laws against genetic discrimination in health insurance and employment, and a few have laws against such discrimination in life insurance. Most of these laws restrict the genetic information available to an insurance company. But critics say that such laws concerning the privacy of genetic information are difficult to enforce and that insurance companies will find loopholes and find ways to gain access to genetic information from applicants (such as asking leading questions about genetic history on insurance application forms or requiring medical records to be sent to the insurance company).

Ethical Issues Surrounding Gene Patents

With the mapping of the human genome and a better understanding of the functions of particular genes, there is an increased demand for research on genes, not just for the purposes of pure science but also to find new treatments for diseases. Both the government and private firms have engaged in genetic research, and both have taken out large numbers of patents on DNA products. In the United States, a DNA product such as a gene or gene fragment can be patented if it is developed in such a way that it is in a unique form not found in nature. Some critics have argued that genes should not be patented at all, and information about them should be publicly available and access to their use should be available for free to both the government and to private firms. They claim that even if a laboratory can synthesize DNA and its components, they are still products of nature and are the property of humankind. Advocates of gene patenting argue that if the government or industry spends money to isolate a DNA product in a way that is not found in nature, then the product is, in a sense, "artificial," and the firm's intellectual property rights over that product should be protected.

The U.S. Government holds the largest number of gene patents, followed by several biotech and pharmaceutical firms. One problem that has arisen in the patent process is the following: Since gene fragments of the same gene may be patented (as well as the gene itself), several firms may hold patents on parts of the same gene. But this results in ambiguity regarding patent rights over that gene. Suppose Company 1 wishes to do research on "Gene A," but Company 2 owns patents on several fragments of Gene A. Do both companies own the rights to the gene? If so, would Company 1 have to pay Company 2 a licensing fee? One danger is that due to multiple patents and confusion over ownership of DNA products, licensing fees could multiply and become exorbitant, driving up the cost of pharmaceuticals and other products developed from research on genes. Critics of the present patent system have argued that there is a need for an agreement to bring order into the chaos of multiple patents on parts of the same gene. Some suggest that a commission composed of people from different professions, including bioscience, business, philosophy, theology, and law, meet to agree on precisely where the limitations of patents on DNA products should lie.

Another potential problem is related to the increasing concentration in the pharmaceutical industry due to mergers forming megacorporations, combined with big pharmaceutical firms expanding their research and development into genetics. As more and more companies merge, and pharmaceutical firms buy smaller biotech firms, the control they wield over genetic research and patents is growing. The knowledge and technology needed to effectively carry out research and development based on genetics is very complex, and increased company size offers an advantage in terms of resources and efficiency. But if control over genetic research and patents becomes concentrated in the hands of fewer companies, this raises the danger of monopolies, with the resultant risk of higher prices for products developed from genetic R&D.

Ethical Issues Surrounding Genetic Enhancement

The HGP will lead to the discovery of more genes connected to diseases, some with diseases directly linked to one or a few genes (such as cystic fibrosis and Huntington's disease), others correlated with diseases not directly gene linked, such as coronary heart disease and cancer. But it may also lead to the discovery of genes associated with nondisease traits, such as height, athletic ability, and intellectual ability. Much discussion has raged over using gene therapy to "improve" human beings. Part of this discussion relates to the older debates over the moral acceptability of germ-line gene therapy. Proponents of germ-line therapy argue that it could eliminate debilitating gene-linked diseases from the human species, such as Huntington's, cystic fibrosis, or sickle cell anemia. Opponents are concerned about the ramifications of rapid changes in a genetic code that developed slowly through evolution. They also argue that since the phenotype is partly due to the interaction of genes, we do not know the overall effects of permanently altering the germ line. In addition, they are concerned that some negative gene-linked traits, such as sickle cell trait, are conducive to human survival in certain environments: In the case of sickle cell anemia, it provides protection against malaria. Critics argue that the long-term results of permanently altering the human genetic code are unknown and potentially dangerous.

Even more controversial is the possibility of altering genes to produce traits that society considers positive, such as increased height, athletic prowess, intellectual ability, or artistic talent. Even if done at the somatic level without passing on traits to the germ line, these types of "improvements" are controversial, for they raise the specter of eugenics. There are fears related to both Nazi attempts to produce a "super race" of individuals and to the eugenics movement of the early 20th century. This movement was primarily focused on eliminating "undesirable" traits from the human population ("negative eugenics"), such as mental retardation. Unfortunately, this led to the forced sterilization of significant numbers of people who were either mentally ill or mentally retarded. The "new eugenics," based on contemporary genetics and the possibility of gene therapy, opens the possibility of "positive eugenics" in which genes for "positive" traits such as mathematical ability are inserted into a germ cell. Some writers have mentioned the possibility of parents choosing "designer babies" with the genetic traits of their choice.

Supporters of genetic enhancement argue that parents should have the right to make autonomous reproductive choices, including the choice of the genetic traits of their children. If there are traits most people in society would consider positive, such as mathematical ability, then it is morally acceptable for parents to agree to genetic manipulation of an embryo so that it gains the gene for this trait. We already support improvement of people's abilities through education and athletic training; what could be wrong with extending this to genetics? Opponents reply that there is a danger of creating two classes of people: Those whose children have received gene-linked positive traits and those who either choose not to have genetically enhanced children or those who cannot afford it. This could lead to discrimination against those "genetically less endowed."

But some geneticists say that the whole discussion may be a moot point. They argue that the debate is based on a false view of genetic determinism that does not stand up to scientific scrutiny. They argue that due to the strong influence of gene interactions, the complexity of gene therapy, and the powerful role the environment plays in phenotype, it will not be possible to program traits such as mathematical acuity or athletic ability into humans. Even limited success would lie in the far future.

Justice and Distribution Issues

The data from the HGP are freely available online. However, the fruits of the HGP, such as new genetic testing products, new drugs resulting from pharmacogenomics research, and so forth, are not free. Will genetic testing and effective drugs developed from genetics research be only available to those who are relatively well off? Will developing nations have effective access to the fruits of genetic research? If drugs are developed that are tailored to an individual's genetic code, it will be expensive to develop drugs for large populations. The danger is that the smaller populations treated will be those able to afford such drugs, and others will be left out. Questions of justice and fair distribution of resources arise. Should companies be required to discount their resources to help those who are economically disadvantaged? Or is the free market the best way to lower costs in the long run and make the products of genetic R&D available to the widest population?

—Michael Potts

See also Genetic Engineering; Genetics and Ethics; Informed Consent; Stem Cell Research

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Humanities and Business Ethics

The humanities have been variously defined, through the ages, to incorporate a range of subjects, including literature, philosophy, history, language, and more recently, even film. The unifying theme of these arts and disciplines is inquiry into human culture, although they may be distinguished in contemporary institutions from certain so-called performing arts, such as music and dance, and fine arts, such as painting and sculpture, which also explore what it means to be human. The lines between the humanities and the sciences and applied disciplines are often perceived to be clearer, in that we study the former for their supposed intrinsic value and the latter for instrumental purposes. Needless to say, the way in which institutions define and distinguish disciplines is often imprecise and reflects the worldviews of an epoch and those within it.

It is worth noting, given the above context, that business has never seriously been considered to be among the humanities. This is despite the fact that the endurance of business as a social institution depends on its capacity effectively to serve the needs and wants of human society. This service-oriented conception of business has been contrasted with the dominant conception of business in which owners employ managers as their agents to maximize the value of their property through efficient response to an abstract and amoral market demand. Moreover, the prevailing application among business ethicists of a moral theory that aspires above all to be general and reasonable does not easily reconcile with a humanistic ethic that values particular context and emotional compassion in seeking to answer how humans, including businesspersons, should live. In short, the juxtaposition of the humanities and business ethics faces numerous challenges requiring clarification.

Empirical Science and Normative Inquiry

Business scholarship has in recent decades been dominated by quantitative and scientific disciplines, and while business practice has in some respects moved beyond financial performance as the only meaningful indicator of business performance, it has not moved beyond the general prejudice that what matters to business must be quantified. These attitudes are one source of tension between the humanities and business ethics, although it is notable that business management has been viewed to be as much an art as it is a science. Meanwhile, normative ethics scholarship suffered years of neglect, particularly by the American and British analytic tradition, for being speculative rather than scientific. These attitudes are another source of tension between the humanities, which often raise more questions than they answer, and business ethics, whose practitioners often desire moral certainty. Even among laypersons who share a regard for ethics as being practically important, there are widely divergent views as to whether ethics consists of a rational system of absolute moral rules or is instead radically subjective, circumstantial, and/or emotional.

These diverging views about business and ethics have contributed, not surprisingly, to a scholarly debate about whether business ethics is properly empirical science (and thus not humanistic in approach) or normative inquiry (and potentially but not necessarily humanistic) and, consequently, to a chorus of voices claiming that the two are complementary and perhaps inseparable. Traditionally, empirical science is defined as the study of what is, whereas normative inquiry is defined as the study of what should be. Within the terms of these definitions, the argument for integration goes roughly as follows: Strictly empirical research cannot, without normative context, help human beings by answering what should be done to improve on what is. Strictly normative research cannot, without empirical context, be related to practical matters of importance to human beings. Therefore, advancing business ethics scholarship and the related goal of moral improvement in business requires an integration of empirical and normative research methods. Still, this convergence of research methods leaves fundamental questions unanswered. Whereas business ethics has tended to focus on the moral question, "What should I do?" the starting point for Aristotle was the broader ethical question, "How should one live?"

The diverging views about business and ethics have further contributed to a public debate about the basic purpose of business ethics education. One side argues that business ethics can and should be taught as a morally prescriptive system of laws and rules defining the limits of appropriate behavior. This argument is often linked to the economic argument that long-term financial performance is tied to so-called ethical performance, where ethical performance is essentially compliance with legal and prescriptive moral requirements. Another side is sympathetic to the claim that ethics is inherently imprecise. This latter claim can lead to significantly different conclusions: Business ethics is merely a descriptive exercise and need not be taught, or business ethics education is essential to cultivating ethical reflection and understanding in a more congenial setting than in the throes of business practice. Those who arrive at this latter conclusion are perhaps most sympathetic to the view that the humanities and business ethics belong together.

Using the Humanities to Understand Business Ethics

The debates summarized above hark back to an ancient quarrel between philosophy and poetry that Plato sought to resolve by banishing poets from his ideal society. His main grounds for doing so were that the potential benefits of art (which he thought could be enlightening and educational) were outweighed by its costs (it did not convey genuine knowledge and could be destructive of moral character). Aristotle, in contrast, thought poetry and certain other arts essential to the good life and good community, reasoning that the pleasure poetry afforded through imitation was essential to its capacity to contribute to moral improvement by depicting things as they might be.

Most business ethics courses use teaching methods inspired by the humanities, most often literature. Case method is based on the notion that business schools must ultimately prepare students for how to act in the so-called real world. Moreover, many courses in law and business use variations on the Socratic method. These methods, whether the raw material comes from the humanities or not, are committed to the ideal of learning general lessons from the particular experiences of others, real or fictional. However, business school case studies rarely have the valuable endurance, particular immediacy, emotional impact, and providential insight that good literature can provide. Aristotle's theory of ethics, which was more concerned with cultivating pursuit of the good life than with specific moral rules, made good use of his theory of poetry. As Nussbaum represents Aristotle, poetry, even more than history, is an essential complement to moral theorizing because it exhibits four key features of the Aristotelian ethical view: noncommensurability of the valuable things, the priority of particular perceptions, ethical value of the emotions, and ethical value of uncontrolled happenings. Furthermore, another recognizably Aristotelian claim is that a story, which is ordinarily a complete whole, can teach what unfinished experience cannot.

Accordingly, in addition to the influence of the humanities on business school pedagogy, the use of the humanities as a didactic instrument is common but by no means institutionalized:

- Numerous scholarly articles and books have been published examining the application to business of moral lessons from specific works of literature, drama, and film, as well as the use of such works in the classroom.
- Business ethics students have read novels, stories, and poems, viewed film, art, and even architecture as the basis for classroom discussions of business ethics topics, and performed dramatic acting in the learning process.
- A scholarly journal has been launched to explore the uses of film in understanding ethics, including but not limited to business ethics.

So, for example, the vanity and foolishness of such fairytale characters as the emperor in Andersen's "The Emperor's New Clothes" has been compared with that of fallen business executives; the Faust legend examines how much it would take for human beings to sell their souls; Rand's *Atlas Shrugged,* a fictionalization of her capitalist philosophy, attributes social and technological advancement to a few visionary leaders, whereas Tolstoy argues in his analysis of the military hierarchy in *War and Peace* that it is the collective activity of many people, rather than a few leaders, that moves the force of history; Shakespeare's *Hamlet* demonstrates the pain of being trapped in a difficult moral dilemma, while *Macbeth* illustrates the trials of organizational politics; and Achebe's *Things Fall Apart* and Conrad's *Heart of Darkness* explore the dark side of colonialism, often fueled by economic conquest. Beyond moral theory and literature, Plato's early Socratic dialogues can be used to study the nature of morality and the justice of the legal system—a theme that returns in King's historic "Letter from Birmingham Jail"; and Aristotle's theory of friendship sheds light on the unabashedly instrumental nature of most business relationships. Film, which is frequently produced by studios owned by big business, is more often than not hostile to big business, whose stereotypical mantra about greed being good is uttered by *Wall Street* corporate raider Gordon Gekko; meanwhile, the focal point of *Do the Right Thing,* a family-owned pizzeria in a racially polarized Brooklyn neighborhood that might as well be a world away from Wall Street, raises the issue of the responsibility of a business to the community it serves.

These examples suggest limitless potential applications of the humanities for understanding business ethics. They may well have the practical value of helping us explore moral dilemmas, but they also importantly communicate what it is to be human; that is, many characters throughout history and literature are materially self-interested, but they are not all equally so, as agency theory has tended to presume. Arguably, the increasing presence of business ethics itself in the standard business school curriculum is further evidence of its "humanization." On the other hand, the question of whether a business education should be humanized by requiring humanities texts and humanities-based courses in the business curriculum poses not only a logistical challenge but also a theoretical paradox. If the fundamental value of the humanities is intrinsic—that is, independent of immediate, functional objectives—then does not using them as a practical instrument undermine their real value?

Business Ethics and Humanity

The contrasts—between business as private property and service institution, empirical inquiry and normative inquiry, financial performance and social performance, moral prescription and description or ethical inquiry, instrumental and intrinsic value—may be exaggerated above for effect, but they are representative of a diversity of intellectual and practical perspectives that influence the extent to which business ethics and the humanities can be said convincingly to form a productive relationship. The uneasy presence of the humanities in business ethics education also raises important issues regarding the role of humanities in business ethics and business more generally. The goal of humanizing the business curriculum involves, most important, a shift in perspective about business practice, from a scientific endeavor pursuing quantitative performance targets to a human endeavor carried on by human beings to serve human demands.

The humanities have been credited with the capacity to enlarge our view of what it means to be human (whether or not in business), teaching us to think critically about business texts and other business phenomena, making us reflect on the foundations of business, and helping us cultivate a sense of community in business. However, contemporary artists and their advocates often do not see their works as primarily instrumental in purpose and quantifiably measurable in value. In fact, it has been argued that artistic and humanistic pursuits are often undervalued by capitalist markets in which the common unit of measure is financial. The humanities remind us that there is more to human value than financial performance, a lesson that does not necessarily teach us anything practical about what to do when faced with a particular dilemma between financial and social performance. What the lesson might do that is of relevance to business is remind us also that there is more to business value and human value than financial performance.

The value of the arts and humanities has been characterized as intrinsic rather than practical, instrumental, or even measurable. This position is represented by Kant's famous notion of purposiveness without purpose and the idea that art (and the humanities, for the sake of this argument) constitutes a disinterested pleasure. Contrast this perspective with that of business, which is fundamentally "interested," as exemplified by the term we use to describe the growth in our capital that results from doing nothing more than lending it temporarily for another's use. While the view that the primary value of the humanities is intrinsic is controversial, relatively modern, and overly simplistic, and the view that the primary value of business is instrumental is perhaps unfair, this contrast illustrates one final way in which the humanities can be (ironically) useful to business ethics: by challenging the foundations of any pursuit we undertake solely with the objective of being paid. Although capitalists have suggested that such an objective is not only defensible but morally obligatory, the suggestion fails to acknowledge the instrumental good that business can do for society as well as the intrinsic good that some businesspeople derive from business activity. Finding ways to value these goods would be the best evidence of the humanizing of business and thus of the value of the humanities to the ethical objectives of business.

—Christopher Michaelson

See also Agency, Theory of; Friedman, Milton; Moral Imagination; Normative Ethics; Teaching Business Ethics

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Human Nature

Human nature may be defined as the essence of the human species and consists of all the characteristics and behaviors that are inherent in human beings. While inquiries into human nature have occupied philosophers both classical and contemporary, practical men and women frequently attribute one or another experienced injury or benefit to some element of human nature and make decisions informed by their own hopes and fears. Advocates of business ethics often look to human nature to explain abuses or to propose a path of change.

What Makes a Human Being?

Humans are distinguished from animals by their ability to use tools, develop language, and reason. These last two are closely connected in that the practice of logic is intertwined with the structure of language. While rhesus monkeys have been taught to use sign language and domesticated animals are capable of understanding spoken words, the development of a formal language is unique to human beings. Indeed, humans have created a diversity of spoken and written languages, and the vocabularies of these languages reveals commonalities and differences among cultures. Written language permits a more detailed historic record and enhanced opportunities for self-consciousness and specialized labor.

In biological terms, the "human" is a mammal, large brained, has an "s"-shaped spinal column, an erect posture, opposable thumbs, an ominivorous diet, binocular vision, speech, practices bipedal locomotion, and dwells on the ground. The human or hominid is preceded in the mammalian chronology by pongids (apes or monkeys). Pongids and hominids share several characteristics with humans: their group living, their careful socialization of children, and their capacity for learning, among others.

The human brain is supple and responds to environmental challenges through reconfiguring its neural pathways. An individual's loss of a sense leads to a process in which the other senses compensate, and a new synthetic understanding of the environment emerges. Damage to the brain stimulates a reassignment of functions among the healthy parts of the brain. The individual's need to process information and interact with the environment stimulates the development of appropriate areas of the brain. The chemistry of the brain is thus altered. Nurture and broad experience may affect nature.

Humans live in groups, not as isolates. Human survival is crucially dependent on primary and secondary groups, from the dyad and nuclear family to larger kinship patterns. Families depend on an overarching organization or complex of organizations, ranging from the tribe and confederations of tribes, to the political structures of the city and nation-state. Pongids share the primary and secondary group structures in which humans live, but they lack the more complex political and economic institutions that characterize human experience.

One basic need satisfied by social organization is continuity in food supply. Participation in social organization with this purpose is not optional. A primary function of the economic system is to assure the availability of food and accommodations and, beyond this, to guide the distribution of wanted goods consistent with cultural values.

Religion has emerged among humans to explain and guide shared experiences of birth, illness, death, love, hurt, and disaster. These explanations are organized into a superstructure that provides reasons, names, and rationales, confers membership, allocates power, and promulgates a charter to order society. Religions proliferate but societies have more recently turned to secular forms of organization in which the influence of religion can still be discerned. Religions constitute one of the oldest forms of social organization and continue to shape business practice, political movements, and statecraft. Religion is an important element of culture that stands along with biology in explaining human behavior.

Determinants of Human Nature

Biology

Biologists have documented much of the human genome and, in doing so, have revealed fundamental elements of human nature. In a very real but limited sense, the genetic code accounts for human nature. Human DNA provides the biological basis for human consciousness, from which derives the human capacity for learning and the complex knowledge transmitted by culture. While the ancient Greeks speculated about fixed forms and ideas determining human nature, contemporary scholars find evolving intelligences, in dialogue with one another and interacting with the environment.

Human evolution is the process through which humans emerge within nature. That humans are animals has led some to claim that humans are inherently violent and aggressive, as some animals appear to be. Evolution is often described as the "survival of the fittest," which is taken by "Social Darwinists" like the 19th-century sociologist Herbert Spencer and his contemporary disciples to mean that humans necessarily struggle with one another, with some destined to lose. Konrad Lorenz argued that humans possess an aggressive instinct but proposed means to subdue it.

Charles Darwin did not intend that evolution be equated with violent competition. Rather, he emphasized the question of reproductive advantage. That is, the evolution of a species is the consequence of the development of characteristics that contribute to differential reproductive success in the local environment. Reproductive success is not necessarily a function of violent competition within or between species. The 19th-century social critic Petr Kropotkin and modern evolutionary biologists have demonstrated that cooperation within and between species also plays a critical role in promoting the survival of offspring. As discussed below, animals and humans have been said to practice a reciprocal altruism in which cooperation emerges as a strategy for survival.

Consider as well the process of symbiosis. Species may evolve in such a way as to intimately depend on conditions produced by other species and may even live within their bodies. This is far from Thomas Hobbes's and Spencer's war for survival.

Culture

Humans are unique in regard to the role played by culture, rather than biology, in shaping individual behavior. Culture is the set of values and customs in which individuals are socialized and that bind a community together. Cultural values shape but do not determine behavior because individuals and groups have the capacity to examine their culture's assumptions and subject them to analysis. Socrates counseled that "the unexamined life is not worth living." Descartes explored the uncertainties of his own existence, and every generation brings a new round of questioning.

Moreover, cultures may coexist, merge, or fragment. Cultures and nations may share boundaries but varied cultures may also blend in a single nation. Shared beliefs and behaviors rather than physical location or political jurisdiction characterize cultures.

The logical structure embedded in many of the languages of the world facilitates questioning. The concept of opposite or negation invites an experimental mind to invert culturally transmitted propositions. Any culture, however conformist, inspires movements of dissent and reformulations of received doctrine. No culture is fully stable.

It is possible almost everywhere to find borderlands where cultures mix and traditions bend or erode. Authority and challenges to it coexist in the borderlands and throughout the contours of cultural evolution.

Clyde Kluckhohn, a cultural anthropologist best known for his survey of the many definitions of culture, called culture an abstract description of the trends toward uniformity in the words, deeds, and artifacts of a human group. Kluckhohn and other anthropologists have noted that cultures are dynamic and are characterized by processes reinforcing both stability and change. Geography and legal jurisdiction shape but do not determine cultural change.

Anthropologists have found considerable differences among the peoples of the world in their practice of gender roles, in their construction of race and class, in their conception of the individual and the collective, in their interpretation of family responsibility and the extended family, in their treatment of elders and assessment of tradition, in their assessment of the proper relations between workers and managers (laypersons and clergy, amateurs and experts), and in their attitudes toward progress. Kluckhohn found these questions to be central to the differentiation of cultures: the conceptions of inherent good or evil in human nature; the perceived relationship of humans and nature; the emphasis on past, present, or future; the conception of life as being, becoming, or doing; and the patterns of emphasis in primary relationships.

Management scholar Geert Hofstede sought to apply the concept of culture to a business context. He surveyed the global population of IBM managers to illuminate national differences in values. He found national differences on the acceptance of power differentials (power distance), individualism (vs. collectivism), masculinity (vs. femininity), the tolerance of uncertainty, and future (or present) orientation. GLOBE researchers at the Thunderbird School of Management amended his model, identifying nine cultural dimensions: performance orientation, assertiveness, future orientation, humane orientation, institutional collectivism, in-group collectivism, gender egalitarianism, power distance, and uncertainty avoidance.

From an anthropological perspective, patterns of uniformity and divergence are of equal interest. The Hofstede and GLOBE models appear to emphasize uniformity rather than change and differentiation. They also assume the narrow vantage point of the multinational manager and cultural variation is understood in relationship to the constituent parts of a multinational enterprise. However, the multinational enterprise is perhaps too culturally specific to serve as a framework for comprehending cultural variation.

The United Nations Universal Declaration of Human Rights emerged from a process in which representatives from the world's nations debated the notion of rights in the aftermath of World War II. That such a document was written with broad international support underscores the possibility of communication and understanding across cultures. Beneath the evident cultural differences on dimensions like individualism and collectivism across the globe, there are underlying problems about the relationship of the individual to the group. Even violations of the

Declaration reveal similar patterns of social control and resistance across cultures and nations.

Diversity: Relationships of Gender, Race, Class

The wide variation in cultural practices across the globe and the visible differences among races and genders have inspired theories of difference and inequality. Explorers and scholars who recorded differences among races and cultures in the 18th, 19th, and 20th centuries, in many cases, assumed a fixed hierarchy of ability and intelligence. These views are increasingly contested by egalitarian perspectives that emphasize the complexity of language and belief systems in disparate civilizations. French anthropologist Claude Levi-Strauss studied the religions and other beliefs of so-called primitive societies and discovered similarities in the detail and complexity of understanding and argument. Franz Boas and more contemporary anthropologists have questioned the concept of race, noting that race accounts for minuscule differences in the genetic code and that there are far greater genetic differences within rather than between the races.

In the United States and many other industrialized nations, women increasingly participate in the labor force. Despite this, there are persistent disparities in income and occupational distribution. While feminists, professional groups, and trade unions agitate for corrective action, there remain significant constituencies who argue for a return to traditional gender roles.

Debate Over Essentialism

The ancient Greeks and particularly Plato and Aristotle contributed profoundly to the historical development of ideas about human nature. In various ways, they advanced the argument that human nature is fixed and personal qualities unalterable. Plato and Aristotle argued that human beings, animals, and things were expressions of underlying forms. For Plato, the material world known by sensation was merely a shadow of a more fundamental reality of unchanging forms or ideas perceived by the intellect or reason. Most important among forms is "goodness," accessible only to reason.

On the other hand, Aristotle saw form and matter as intertwined. According to Aristotle, humans share the same underlying form but differ in their material manifestations. The human soul or mind consists of the distinctly human faculties including consciousness and reason. From the material world come individual differences.

Aristotelian philosophy validates experience as a source of knowledge. Aristotle believed that the forms manifested in all living and inanimate things are accessible to the human mind through experience coupled with reason.

Like Plato, Aristotle embraced inequality among humans and rationalized a rigid class system. Aristotle specifically endorsed slavery as natural and argued that most slaves were mentally inferior to their masters. He placed humans at the peak of a hierarchy of all life-forms but suggested that some humans were brutish or animal-like, particularly non-Greeks.

Aristotle identified human fulfillment with the exercise of reason in a life of activity and social engagement. He proposed practical wisdom, moderation, courage, and justice as principal virtues to guide living. Virtue lies in the mean between extremes, and extremes of wealth and poverty produce manifold injustice.

Platonic and Aristotelian philosophies continue to shape modern thinking. Plato's notion of the separation of mind and body or "dualism" is reflected in Christian teaching about the soul's independence from flesh. Contemporary arguments about the superiority of reason to emotion recall his work.

Platonic idealism has an analog in the free market model in neoclassical economics. Many economists view the market as the underlying reality of economic life even as they de-emphasize the violations of neoclassical assumptions posed by the details of corporate power and the experience of individuals and groups at work. Institutionalists, Marxists, and other dissenters within economics have sought to counterpose the social realities of poverty and exploitation with the abstract formalism of economic models. Economists' adherence to the ideal of free markets, like Platonic idealism, is rooted in a preference for mathematical structures over subjective experience.

Aristotle's conception of human differences, characterization of human virtues, and empiricism have been influential. Modern conservatives find in Aristotle a justification of aristocracy in the political and economic realms. On the other hand, Robert Solomon and others have developed paradigms of multiple virtues in business ethics relying on Aristotle's works.

Forms in Platonic and Aristotelian philosophy represent means to explain what is common and what is different among humans, animals, and things. Contemporary scientists struggle with the same questions and have found that the DNA code constitutes a modern equivalent for form among living things. However, DNA does not determine all aspects of human nature or individual differences. For example, it is probably only one of many factors influencing intelligence.

Scholars and practitioners continue to debate the relevant contributions of nature and nurture to intelligence. The Intelligence Quotient is premised on the notion that there is one fundamental kind of intelligence that has a fixed and unequal distribution among the human population. Critics such as Howard Gardner now argue that there are multiple forms of intelligence, including social and emotional varieties, that depend on context and are not necessarily correlated. Others have suggested that apparent cultural differences in intelligence are an artifact of testing, in which culturally specific approaches to reasoning are privileged. Most important, critics find considerable evidence for the notion that individuals have multiple paths of intellectual development open to them and that they are not handicapped by a fixed amount of intelligence.

Given the near-universality of complex hierarchies in the business world and the phenomenon of the "pecking order" among animal species, it is tempting to say that hierarchy and inequality are embedded in human nature. From Plato and Aristotle to contemporary ethologists such as Desmond Morris, this has been the view. Others condemn this notion as an anthropomorphic fallacy. Dominant chimpanzees or roosters do not claim superiority relative to the others in their group. Their dominance is highly constrained and relates to the ordering of events rather than to the quality of existence. It is only among humans that hierarchy rations access to necessary goods.

Counterposed to the essentialist views of Plato and Aristotle are models of a malleable and flexible human nature. Jean-Jacques Rousseau, Karl Marx, John Dewey, and even the 20th-century management scholar Douglas McGregor argued that the reconstruction of social institutions could initiate new patterns of human development. Rousseau argued that humans were essentially good but corrupted by existing civilizations. He called for a new social contract informed by the "general will," freed of corrupting sectarian interests. Karl Marx imagined an emancipated human nature of unlimited capacity following socialist revolution and the transition to communism. Dewey believed democracy to be the key to the enhancement of ordinary individuals' abilities. McGregor argued that a more participatory approach by managers would uplift and fulfill most workers. The debates about the scope of human malleability and improvement are embedded within contemporary political discourse.

Behaviors Based in Human Nature

Self-Interest Versus Altruism

One of the most important debates in business ethics revolves around the relationship of self-interest, competition, profit-maximizing, and human nature. The obverse question is the relationship of altruism inherent to human nature. What are the relative shares of altruism and self-interest in the fundamental nature of the human actors?

Some argue that examples of altruistic behavior abound in nature. Care for family members is a characteristic seen in a wide variety of species. The careful protection of eggs by penguin parents is a remarkable demonstration of willing self-sacrifice. Of course, biological urges are supplemented by cultural traits in human society; the balance of cooperation and competition in animal nature does not determine the balance in human nature.

The care shown by a parent for a child is often explained as selfish in that it helps preserve the parent's genes. However, the wolf pack's embodiment of extended family and the human concern for community and humankind (described in robust form in Kristin Monroe's *Heart of Altruism*) cannot easily be construed as self-interest. It is noteworthy that neither narrow self-interest nor broad social solidarity, strictly defined, requiring either a developed personality or a science of politics, is present in the animal world.

Economists Samuel Bowles and Herbert Gintis posit that strong reciprocity and basic needs generosity are fundamental human motives. They contend that anthropological research and game theory suggest that people are not stingy, but that their generosity is conditional on context. By strong reciprocity, they mean a propensity to cooperate and share with others in a similar position, even at personal cost. By basic needs generosity, they mean a virtually unconditional willingness to share with others and assure them some means of subsistence. Evolutionary biologists find evidence of reciprocal altruism as an evolved behavior. Anthropologists find altruism and self-interest embodied in varying combinations in existing and ancient cultures.

Some have argued that altruism is linked to a particular formulation of self-interest. Altruistic service to others requires a healthy self, without which one's service may lack consistency and effectiveness. Someone who fails to attend to his or her health and other needs cannot be reliably helpful to others. Sustainably altruistic behavior, whether for business leaders, philanthropists, community activists, or helping professionals, cannot involve self-destruction. Altruism may be linked to a conception of self-interest that is broadly construed so as to be consciously embedded in the social. The altruist judges the welfare of others to be intertwined with his or her own interests.

Despite the long tradition of writing and argument that humans are inherently social (supported by Plato and Aristotle and their Christian interpreters among others), individualistic conceptions of human nature have grown in influence in the United States and Western Europe since the 18th century. Social contract models like that of Thomas Hobbes and John Locke played a critical role in the revolt against monarchical absolutism and feudal privilege; individual rights and reason were key to this process. Both Hobbes and Locke hypothesized that humans were equal in the state of nature but endorsed a civil society of individualism and unequal property relations. Individualistic ideas were a potent solvent that shook the feudal order to its foundations. Canadian political theorist C. B. Macpherson identified a contradiction in the "possessive individualism" of Hobbes and Locke between the logic of individual liberty and exploitative property relations.

The 18th-century political economist Adam Smith was one of the great architects of the capitalist system. One of his important contributions was to link individualism to a self-regulating natural order. His best known work, *The Wealth of Nations,* introduced the concept of the "invisible hand" guiding the self-interested behavior of economic actors toward the public good. Modern individualists continue to pay tribute to Smith's conception of the invisible hand. Objectivists like Ayn Rand add to Smith's embrace of markets a belief in the moral superiority of capitalists.

Despite Smith's celebrated role as an exponent of laissez-faire capitalism, he did not argue that selfishness was a sufficient explanation of human behavior. He worried that self-interest often led businessmen to conspire against the public and called attention to "sympathy" as a motive coexisting with selfishness. Indeed, he raised questions about the morality of individual capitalists.

Utilitarian philosopher Jeremy Bentham contributed much to the classical model of "economic man," the individual as utility maximizer practicing a hedonistic calculus. In this analysis, market transactions generate the greatest happiness of the greatest number, and no other motives need constrain self-interest. However, even within utilitarianism more complex views of human nature have emerged. John Stuart Mill found happiness to be something more than the sensation of pleasure. Mill's emphasis on the quality of happiness and his concern for workers' conditions in free markets led him to contemplate means to introduce a measure of solidarity in economics, thereby adding to self-interest as the primary human motive. Smith and Mill considered together reveal a developing argument for social responsibility to restrain capitalist excess within the classical economic paradigm.

Capitalists and socialists, reformers, reactionaries, and revolutionaries of all stripes have posited views of human nature that validate their political analyses. Capitalists find self-interest everywhere. Socialists find altruism prominent in both "primitive" and civilized societies. Ayn Rand and modern objectivists continue to argue for an atomistic individualism and interpret human interaction as a form of rational contracting.

Good and Evil

War and violence have bedeviled humanity throughout recorded history. While Rousseau posited a noble savage and Marxian socialists have forecast human perfectibility, Saint Augustine and succeeding generations of Catholic and Protestant thinkers have asserted the principle of original sin.

Immanuel Kant thought the human mind capable of discerning moral duties or categorical imperatives through the application of reason. Because reason is an inherent human capacity, the perception of duty is embedded in human nature. This does not mean that humans will always do that which is good. Their capacity to reason provides the opportunity to make choices, and these choices may reflect selfish interests and violate duty.

The 20th-century Protestant theologian Reinhold Niebuhr elaborated a view of human nature in which good and evil coexist and define the arc of human practice, and democracy is justified as a constraint on evil and a means to develop the good. Niebuhr warned of the children of light and the children of darkness, both of whom do evil as they dwell in illusion. The children of light assume that human nature is perfectible and fail to recognize the damage they do as they aggressively pursue what they regard as the good. The children of darkness know of no law apart from their own will and narrow interest. Niebuhr held that powerful corporations routinely abuse their power, both through the naïve optimism of the children of light and the manipulative cynicism of the children of darkness. Niebuhr's moderate pessimism about human nature led him to argue for extensive regulation of corporations, but he also warned of abuses in the exercise of governmental power.

Reason and Emotion

Philosophers from classical to modern times have cited reason as the faculty that distinguishes human beings from animals. It must be conceded that primates have the capacity for physical problem solving, but they lack the ability to consider abstractions and formulate principles. This gives humans the capacity to distinguish self-interest from group and societal interests and to choose rules for decision making.

While Plato and other dualists considered emotion to be inferior to reason, and others have linked emotions and the flesh to moral corruption, emotion plays a critical role in human behavior. It cannot be so easily distinguished from reason. Emotion provides information. When one experiences emotional pain, one recognizes a peril in the path of decision making. Pleasure reveals a favorable association. Emotions illuminate some of the personal and social consequences that derive from one's choices and situation. One is free to employ reason in the consideration of emotion. While Jeremy Bentham was probably a reductionist in his construction of a hedonistic calculus for human behavior, it is equally suspect to dismiss pleasure and pain as irrelevant to human action.

The Life Cycle

A challenge posed by human nature to the business world is the recognition of the life cycle. The utilitarian model premised on economic man fails to fully acknowledge the ways in which humans mature and develop distinct needs (rather than wants). Humans are distinguished from other mammals by their survival long past child-bearing years. Older humans have much to contribute to society based on their experience, and children have much to learn from society, but neither reality is fully reflected in any company bottom line. Industrialized societies now face difficult questions relating to the funding of private and public pensions given widespread employer pressure to attenuate historic commitments to retirees. The elderly face increased poverty and exclusion.

Social Responsibility and Solidarity

Business leaders, scholars, and the public at large vigorously debate about whether corporations owe society anything more than profit-maximizing. The advocates of profit-maximizing and of social responsibility often turn to conceptions of human nature to explain their positions. If rational self-interest is a sufficient explanation of human behavior, then corporate social responsibility receives little reinforcement from human nature. Classical notions of the social contract and contemporary economic models reinforce the notion of the atomistic individual. If, on the other hand, altruism is sustainable at the individual and group levels, then there may be a variant that is appropriate to the business enterprise. A third possibility is that human nature leaves individuals and groups with a wide array of choices and in no way determines the configuration and practice of business enterprise.

Of the three propositions, the weakest appears to be monistic interpretation of human nature and business practice as self-interested. Certainly anthropologists' survey of human behavior and social institutions finds multiple patterns of self-interested and altruistic behavior. Individuals' loyalty to tribes, businesses, or movements cannot be fully explained by self-interest. It should be noted that profit-maximizing corporations depend on considerable self-sacrifice from employees.

Social psychologist Lawrence Kohlberg describes the process of ethical development according to which an individual learns to behave according to the dictates of successively broader communities, from the family to peer groups and ultimately global humanity. Parental approval and avoidance of punishment determines the behavior of the child, but abstract principles may guide the decisions of adults.

Underlying this process is an expanding social consciousness. Humans see the consequences of their actions and derive lessons from what they see. They easily perceive their dependence on immediate and extended families. As they mature, they may increasingly identify commonalities with other individuals and families. They observe an array of "experiments" in which individuals and families pursue varied options with respect to patterns of cooperation and conflict with relevant others. As a result, they forge bonds of identity linking the local, regional, national, and perhaps global networks.

Regardless of one's values and background, one has the potential to embrace a consciousness of kind with global dimensions. This is true of the hard-nosed business conservative as well as the international unionist. What distinguishes the two is the choice of others with whom to identify. In neither case is the individual self-sufficient.

Social consequences may extend to considerations of the natural world. Humans cannot sever their relations with the natural world, but they can learn better how to evaluate the natural consequences of their actions. The human capacity to perceive consequences, experiment as to behaviors, identify with others, and invent ways of living and working together provide the intellectual and social context for conceptions of social responsibility.

Behavioristic psychologists like James McConnell and B. F. Skinner viewed human behavior as a set of responses to stimuli in which conscious choice is absent. This perspective recognizes few differences between rats and humans and omits culture as a significant element of human existence. On the other hand, if one accepts the notion of consciousness, one can see in cultural variety the multiplicity of social choices humans have made as well as the consequences. One might speak broadly of a "consciousness of kind" (following Giddings), ranging from familial (nuclear, extended) to group, nation, species, and nature. This "consciousness of kind" follows the contours of association and solidarity through which individuals and groups demonstrate their identity with and fidelity to others.

There is considerable opportunity for choice in the way in which business institutions reflect individual, group, and societal priorities. The multiple paths to corporate social responsibility depend on choices as to the institutionalization and reconciliation of the self-interests and altruistic concerns that coexist in human nature.

Consider Kant's maxim that one should treat others as ends and never solely as means. This categorical imperative has been interpreted by some to require the overhaul of organizations. Labor cannot merely be a factor of production and thus a means but must become an end as well. Producer cooperatives, employee ownership, collective bargaining, and employee involvement may be more consistent with Kantian ethics and represent means to reconcile the self-interested and altruistic motives in human nature.

—David Carroll Jacobs

See also Altruism; Aristotle; Autonomy; Capitalism; Cognitive Moral Development; Corporate Social Responsibility (CSR) and Corporate Social Performance (CSP); Darwinism and Ethics; Economic Rationality; Egalitarianism; Empathy; Evolutionary Psychology; Hedonism, Ethical; Hobbes, Thomas; Human Genome Project; Human Rights; Hume, David; Individualism; Kohlberg, Lawrence; Laissez-Faire; Locke, John; Mill, John Stuart; Pragmatism; Profit Maximization, Corporate Social Responsibility as; Rand, Ayn; Reciprocal Altruism; Reciprocity; Rights, Theories of; Rousseau, Jean-Jacques; Self-Consciousness; Self-Interest; Smith, Adam; Socialism; Spencer, Herbert; United Nations; Utility

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HUMAN RIGHTS

Basic human rights are moral rights that apply to all persons in all nations, regardless of whether the nation in which a person resides acknowledges and protects those rights. It is in this sense that basic human rights are said to be *inalienable.* Human rights can also be aspirational in the sense of specifying the ideal rights to which individuals ought to be entitled. The 1948 *Universal Declaration of Human Rights* is aspirational in this sense. To think about human rights in a meaningful way, it is helpful to answer certain philosophical questions about their nature. Three of the most basic questions are the following: How can human rights be justified? What basic human rights exist? How do human rights differ from other rights, such as legal rights? Let us consider each question in turn.

Philosophical Foundations

Human rights are rights enjoyed by humans not because we are members of the species *Homo sapiens* but because fully functional members of our species are persons. Personhood is a metaphysical category that may or may not be unique to *Homo sapiens.* To be a person one must be capable of reflecting on one's desires at a second-order level, and one must be capable of acting in a manner consistent with one's considered preferences. The capacity to reflect on one's competing preferences and to act in a manner consistent with one's second-order preferences is a key feature of personhood and one that distinguishes persons from mere animals. It is in this sense that the idea of personhood is properly understood as metaphysical rather than biological.

Rights theorists with a wide range of commitments readily agree that persons enjoy a basic right to individual freedom and that other persons have a duty not to restrict or constrain the freedom of others without strong justification. Sometimes, as in the case of John Locke, this right is merely assumed or asserted. Modern rights theorists such as Robert Nozick, Loren Lomasky, and Onora O'Neill typically ground this claim in Kant's second formulation of the categorical imperative, which holds that one must treat other persons always as an end and never as a means only. Kant provides a sustained defense of the doctrine of respect for persons, and he and his interpreters specify in detail its practical implications. Respecting other persons requires that one refrain from interfering with their decisions and actions. Typically, one person is justified in limiting the freedom of another only when her own freedom is unjustly restricted by that person. One traditional way of capturing this sense of a liberty right is that individuals should be free to as much liberty or freedom as is compatible with like liberty or freedom for all.

There is little controversy among rights theorists regarding the plausibility of a negative right to liberty or freedom. However, there is significant controversy over whether or not there are positive rights to certain economic and social goods. Positive rights entail not merely negative obligations on the part of others to refrain from certain actions, but a positive obligation to fulfill the right of the rights holder. One positive basic right that is often defended is the right to physical well-being. For example, if individuals have a right to economic aid or health care to ensure their physical well-being, then others have a duty to provide them with such assistance. The state may be called on to fulfill these duties, but in weak or corrupt states such duties may be neglected. And in states where market values trump consideration for positive human rights, such rights may also be neglected. Under such conditions the burden of fulfilling such obligations seems to fall on individuals, but most individuals are not well positioned to meet such obligations. Furthermore, even in cases where the state does meet such alleged obligations, traditional libertarians would argue that it is illegitimate to tax some citizens in order to ensure the well-being of others. Have we then reached an impasse?

Arguably, there are at least two philosophically sound reasons for thinking that we can move beyond this apparent impasse. First, there is an influential and persuasive argument that holds that the distinction between negative and positive rights is unsustainable. Second, there is a widely influential set of positive arguments that can be used to support both a right to freedom and minimal welfare rights, such as the right to subsistence or well-being. Let us consider each argument in turn.

Henry Shue has famously argued that the very distinction between negative and positive rights that the preceding analysis presumes is artificial and inconsistent with social reality. For example, consider the right to physical security (i.e., the right not to be harmed). It is possible to avoid violating a person's right not to be harmed by refraining from certain actions. However, it is not possible to protect a person from harm without taking proactive steps. At a minimum, Shue argued, law enforcement agencies and a criminal justice system are required so that individuals are not left to defend themselves against forces that they are unable to defeat on their own. The existence of these social institutions is predicated on positive actions in the forms of design, implementation, administration, and taxation. In this way, it can be seen that the protection of a prototypical negative right requires positive actions and not merely the avoidance of particular actions. Since negative rights entail both negative and positive duties, the notion of negative versus positive rights loses its meaning. There are only rights and corresponding duties; but the duties that correspond to these rights are both negative and positive. There is, then, Shue concluded, a strong argument against a theory of rights that includes negative but not positive rights.

Much of the most important and influential work on human rights has been produced by Kantians. Rather than beginning with rights claims, Kantians begin with obligations or duties to respect other persons. These duties constrain the pursuit of ends, whether they are self-interested goals or projects pursued on behalf of other parties such as shareholders. Respecting persons involves both negative obligations, such as refraining from using others as mere tools via physical force, coercion, or manipulation, and positive obligations, such as supporting physical well-being and the development of basic human capacities. When they stand in the appropriate relationship to an obligation bearer, persons have rationally justified rights-claims against them. Rights take the form of side-constraints that bound the moral space in which agents may pursue ends without unjustified interference by other agents or institutions. For example, a minor child has legitimate rights-claims against her parents regarding her physical well-being and the development of her human capacities by virtue of her relation to them. The morally legitimate ends of parents do not include actions that substantially undermine the physical well-being or normal development of their child. Similarly, a convenience store owner has a rights-claim against those in his community to be free from assault and robbery. The morally legitimate ends of other community members do not include actions that would undermine the freedom of the store owner.

Wherever corporations conduct business, they are already in special relationships with a variety of stakeholders, such as workers, customers, and local communities. In their global operations and in their global supply chains, corporations have a duty to respect those with whom they have relationships. Corporate managers, then, have obligations to both ensure that they do not illegitimately undermine the liberty of any persons and the additional obligation to help ensure that minimal welfare rights to physical well-being and the development of basic human capacities are met within their spheres of influence. For example, corporations have sufficient power and coercive influence to ignore the labor and environmental laws in many developing nations. These host nations typically lack the police and judicial infrastructure necessary to enforce such laws. Host nation governments may also be fearful that if they enforce their own laws, then the corporations may move their operations to nations that are willing to ignore local laws. However, such laws are essential for the protection of the basic rights of the citizens of developing nations. For this reason, it has been argued that corporate managers have an obligation to ensure that local host nations' laws are respected.

Human Rights Versus Legal Rights

Human rights are moral rights that apply to all persons in all nations, regardless of whether the nation in which a person resides acknowledges and protects those rights. Human rights attach to persons and not merely to citizens. Human rights differ from legal rights in that, unlike legal rights, the existence of human rights is not contingent on political institutions. This is true despite the fact that the enforcement of human rights typically does rely on institutional mechanisms.

Many nations grant their citizens certain constitutional or legal rights via foundational documents or legal precedent. However, the rights that are protected vary among nations. Some nations ensure that the rights of citizens are protected by effective policing and an independent judiciary. Frequently, however, poor citizens and disfavored groups are not provided with the same level of protection for their legal rights as the economic and political elite. Persons who are deprived of their rights do not thereby cease to have those rights. Employers may deny employees or other stakeholders their inalienable right to freedom and well-being, whether or not local governments are complicit, but in doing so they in no way diminish the legitimacy of the claims of their employees to those rights. However, by virtue of their failure to properly respect these stakeholders, such employers succeed in diminishing their own standing in the community of rights holders.

In the weak and failed states where many multinational corporations operate, they are often the most powerful institutions in existence. In such cases, corporate managers are uniquely situated to help ensure that the basic rights of individuals within their spheres of influence are protected. Many corporations have embraced this obligation. For example, Mattel ensures that all the factories in its global supply chains meet basic human rights standards. Nike provides microloans to community members in the areas where it has large contract factories, thus providing additional help to improve the economic well-being of these communities. And Adidas ensures that the basic rights of workers in its contract factories are respected while using its occupational safety expertise to help noncontract factories in those same communities improve working conditions.

Are Human Rights a Western Concept?

At this point in our discussion, it is worthwhile to consider an objection to the foregoing argument concerning human rights. This criticism stems from the observation that the idea of human rights emerged from the Western philosophical tradition but is taken to be universal in its applicability. The claim is then made that human rights are of less importance in the value systems of other cultures. For example, it is argued that "Asian values" emphasize order, discipline, and social harmony, as opposed to individual rights. In this view, the freedom and well-being of individuals should not be allowed to interfere with the harmony of the community, as might be the case, for example, when workers engage in disruptive collective action in an effort to secure their rights. This view might also be used to defend the claim that the moral norms that govern Asian factory operations should emphasize order and discipline, not such basic rights as freedom and well-being.

Several points may be made in reply to this objection. First, Asia is a large region with a vast and heterogeneous population. As Amartya Sen and others have argued, to claim that all, or even most, Asians share a uniform set of values is to impose a level of uniformity that does not exist at present and has not existed in the past. Second, in secular, democratic Asian societies such as India, respect for individual rights has a long tradition. Indeed, there are significant antecedents in the history of the civilizations of the Indian subcontinent that emphasize individual freedom and well-being. For example, Amartya Sen has noted that in the third century BCE, the Emperor Ashoka granted his citizens the freedom to embrace whatever religious or philosophical system they might choose, and at the same time he emphasized the importance of tolerance and respect for philosophical and religious beliefs different from one's own. Third, even if it was the case that Asian cultures shared a uniform set of values that de-emphasized human rights, this would not by itself provide good reasons for denying or disrespecting the rights to freedom and well-being. This is because the justification of human rights provided above is grounded in rational arguments that are valid across cultures.

The critic is likely to retort that such a view reflects Western prejudices grounded in Enlightenment ideals. This response is unpersuasive. Diverse intellectual traditions have emphasized the importance of values derived from reason, rather than mythology, traditionalism, mere sentiment, or some other source. For example, in the 16th century, the Mughal emperor Akbar arranged to have philosophers representing diverse religious and philosophical beliefs engage in rational discussions regarding the merits of their competing views and sought to identify the most persuasive features of each view. In so doing, Akbar was able to emphasize the power and force of rational analysis. Given that a similar emphasis on rational analysis concerning values may be found in the histories of other non-Western cultures, the claim that such analysis is uniquely Western is unpersuasive.

—Denis G. Arnold

See also Autonomy; Capabilities Approach; Deontological Ethical Systems; Dignity; Freedom and Liberty; Kantian Ethics; Natural Law Ethical Theory; Neo-Kantian Ethics; Rights, Theories of

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Hume, David (1711–1776)

David Hume was Scottish. One of the great philosophers, Hume's wide-ranging thought incorporates a skeptical attack on the power of human reason along with an explanation of how the natural operations of mind and conduct generate beliefs and contribute to the formation of moral and political order. Hume suggests that we are guided less by abstract reason than by stable currents of passion, sentiment, and custom. A significant influence on his peers, including Adam Smith, and a popular figure in Enlightenment Scotland, Hume has also provided a powerful legacy to contemporary philosophers. Born in Edinburgh, he studied at the University of Edinburgh and later served as the Librarian to the Faculty of Advocates.

During his lifetime, Hume was most famous for his essays—some of which first appeared in 1741 (*Essays, Moral and Political*)—and for his six volume *History of England.* However, his major work is *A Treatise of Human Nature.* Disappointed with its reception, Hume revised the *Treatise,* publishing *An Enquiry Concerning Human Understanding* and *An Enquiry Concerning the Principles of Morals.* Although differing in style from the *Treatise,* their content is similar. Other major works include *The Natural History of Religion,* a naturalistic explanation of religious belief, and *Dialogues Concerning Natural Religion,* published posthumously. In the *Dialogues,* Hume offers forceful criticisms of the Argument from Design, a powerful 18th-century argument for the existence of God.

Seeking a science of human nature, Hume devotes the first book of the *Treatise* to the understanding, the second to the passions, and the third to morals. The contents or perceptions of the mind are either ideas or impressions, but all ideas arise from impressions of sensation or internal impressions (passions or feelings). Reason is concerned with matters of fact or relations of ideas. Knowledge of matters of fact is founded on belief about cause and effect, but causal relations cannot be proved a priori; they can be gleaned only from the customary association of one thing with another. From the habitual experience of one object following another, we come to believe that these objects share a causal connection, even if there is no rational justification for assuming that future experiences of causation will be the same as in the past. Hume also contends that there is no justification for positing a self beyond particular impressions and ideas of the moment, nor is there reason for predicating a world that exists independent of us. Even without rational justification, we are, Hume explains, naturally constituted to believe in causality, a world external to ourselves, and a continuing self.

When he turns to consider the passions, Hume notes how, via a process of sympathy, we may come to share the passions and feelings of others. It is in fact the passions, and not reason, that motivate action, and because morality has a motivating force, morals must involve the passions. Moral judgments arise from the sentiment that occurs on considering, from a general rather than a partial point of view, the actions and qualities of other agents. The rules, or conventions, of justice—primarily rules of property—first emerge as a response to circumstances such as scarcity and limited benevolence. Rejecting any notion of a social contract, Hume argues that governments and laws find their justification in utility and that a cautious moderation is the appropriate attitude toward politics.

In his *Political Discourses,* which are essays devoted to economic questions, Hume distinguishes between money and wealth, argues for free trade, attacks several theses of mercantilism, and suggests that commerce helps rather than hinders moral and social progress. In *Of the Jealousy of Trade*, he argues that competitive trade is not a zero-sum game but a mutually beneficial condition of economic growth. In *Of Commerce* and *Of Refinement in the Arts*, Hume defends economic growth, arguing that commerce has significant and positive consequences for individual happiness, the enhancement of knowledge, the development of sociability and humane relations, and the maintenance of liberty.

—F. Eugene Heath

See also; Economics and Ethics; Ferguson, Adam; Ideal Observer Theory; Kant, Immanuel; Kantian Ethics; Mandeville, Bernard; Moral Sentimentalism; Smith, Adam

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I

IDEAL OBSERVER THEORY

Ideal observer theory purports to give the meanings of ethical terms or to provide normative standards by showing what judgments an ideal observer would make and what reactions an ideal observer would have. There are many different versions of the theory. Other ethical theories employ aspects of ideal observer theory as well. The most notable of ideal observer theories is that of Roderick Firth, but Adam Smith offers one of the first versions of the theory. Others who employ aspects of ideal observer theory are Richard Hare, in his discussion of the archangel as part of his two-tiered theory of moral thinking, and John Stuart Mill, in his use of the benevolent spectator as part of the explanation of his utilitarian theory. However, Hare's archangel and Mill's benevolent spectator are best considered ideal observers in the service of consequentialist ethical theories. Still other ideas that share some important similarities with ideal observer theories include Kurt Baier's "moral point of view" and Thomas Nagel's "view from nowhere." These share with ideal observer theory the requirement that moral judgments must be made from an objective standpoint if they are to be correct.

The requirement of objectivity is the main characteristic of ideal observer theory. Correct moral judgments are objective and impartial as well as devoid of particular interests, concerns, and attachments. Some versions, specifically Firth's, add omniscience as a necessary attribute of the ideal observer. Smith requires knowledge for the ideal observer, although not omniscience. For us to employ such a theory in decision making, we must imagine what it would be like to have those attributes, some of which are impossible for us to have. Our judgments are thus in an important respect always tentative since ours may not match the judgments of the ideal observer, given our less-than-ideal circumstances.

Firth's account is the most thorough and sophisticated version of ideal observer theory. He identifies and explains six characteristics of the ideal observer: (1) omniscience with respect to nonethical facts, (2) omnipercipience, (3) disinterestedness, (4) dispassionateness, (5) consistency, and (6) normality in all other respects. This combination of characteristics has the result that the ideal observer is also completely impartial, which is of great importance to the absolutist, or objective, character of Firth's analysis of moral terms. According to Firth, the ideal observer's impartiality results from disinterestedness and dispassionateness. Consistency, however, does not result in impartial decisions. Rather, impartial decisions will be consistent. Firth points this out by reminding us that it makes sense to say a person is consistently partial, so as to remind us that consistency is not enough to make for impartiality.

These six required characteristics of the ideal observer are intended to be significant but conceivable. If the ideal observer did not meet these requirements, we would not want to take his or her judgments as giving meaning to moral terms. Firth's analysis is such that moral terms are given meaning by the reactions of an ideal observer. So, for statements in which an ethical term is predicated on some act, agent, or characteristic, the ethical predicate is given its meaning by how the ideal observer reacts to that act, agent, or characteristic. For example, if we were to analyze the statement "Murder is bad," the term *bad* will reflect the ideal observer's negative reaction to or disapproval of the term *murder,* just as in "Giving to charity is good" the term *good* reflects the ideal observer's positive reaction to or approval of the term *giving to charity.* It is worthwhile to note that the ideal observer may also react with moral indifference, passing no moral judgment on an act.

Smith's version of ideal observer theory is different from Firth's. Rather than treating disinterestedness and dispassionateness as key characteristics, Smith argues that we offer moral approval when we sympathize with another, disapproval when we do not. Sympathy is then the agreement of moral judgments. Smith's ideal observer reacts both to the agent and to those who are affected by the act in question. The judgment of the observer takes all aspects of the act—who is involved, what the motivations of the agent are, as well as the intentions of the agent and consequences of the act—into account. While Smith's observer is informed of the facts of the case, he or she is not omniscient, and the judgments made may be changed later. Smith's ideal observer thus renders moral approval or disapproval and generates moral judgments accordingly. Smith's ideal observer sets a normative standard for moral judgments, whereas Firth's gives meaning to moral terms.

Hare and Mill both use an ideal observer in their consequentialist theories. For Hare, the archangel (who is akin to an ideal observer) makes the moral judgments that are to guide us in everyday life, and those judgments are the ones that are most clearly reflective of the ethical theory. The archangel's judgments give meaning to our moral terms, and to use moral terms correctly our judgments must match the archangel's when we are paying attention to all aspects of the moral theory. This is the most reflective and definitive tier of Hare's moral theory. The other tier of moral thinking in Hare's theory depends on the judgments of the archangel being correct according to the principles of the theory. Judgments from this tier are to be used in ordinary circumstances. For Mill, the benevolent spectator (who is akin to an ideal observer) is one after whom we are to model our own judgments. The key characteristic of the benevolent spectator is impartiality, which is also of great importance to Firth's ideal observer. The benevolent spectator makes moral judgments that are beneficial overall but that do not rely on a particular interest in those who benefit.

Some Criticisms

Common criticisms of ideal observer theories express worries about the knowledge requirements of an ideal observer, the possibility or lack thereof of the existence of ideal observers, whether or not ideal observer theories have problems dealing with questions of absolutism and relativism, and what effect all these problems might have on the meanings of our ethical terms if we subscribe to this kind of theory. Some of these criticisms can be dealt with relatively easily and are no more damaging than the criticisms of any kind of moral theory, but others are more problematic for the plausibility of the theory.

As noted above, Firth's knowledge requirement for ideal observers is quite strong—omniscience. It has been argued by Richard Brandt that this requirement is far too strong because it takes us out of the running for being ideal observers and makes the observers less "human" than we might want. One proposal is that it might be enough that the ideal observer has all the ethically relevant facts of a situation to make his or her judgment. Yet we might worry that an ideal observer without *all* the facts might have some false beliefs that would affect the judgment made in the situation. We might also worry that to specify the ethically relevant facts, we would need to employ other judgments of the ideal observer, and thus we would confront a circularity problem to identify those ethically relevant facts. Smith's version might also fall victim to a circularity criticism since the ideal observer's morality depends on his or her own judgments according to his or her own sympathies. In addition, we may worry that Smith's observer's judgments may be later changed on his account.

The second problem concerns the possible existence of ideal observers. On the one hand, if there are no ideal observers, we might think using such a fiction to give meaning to our ethical terms or to give a normative standard for judgments is dubious. The idea here is that we can only suppose what an ideal observer's judgments would be, and since we are not omniscient or do not possess the required knowledge, disinterest, and dispassion, our judgments will often be mistaken (this can also be construed as a merit of the theory since moral disagreement is easily accounted for).

On the other hand, if there is more than one ideal observer, we may run into ethical disagreements among them, rendering our ethical terms' meanings or normative standards questionable. This criticism, if persuasive, is troubling. The criticism goes like this: We could have two ideal observers who meet all the conditions of an ideal observer and yet due to differences in psychological makeup or circumstance or perspective make different moral judgments about one situation. They have at their disposal all the facts and are both disinterested and dispassionate yet still react differently to an ethical situation. Some have argued that the situation described is inconceivable, that if the two ideal observers are omniscient, disinterested, and dispassionate, they *must* by definition of those concepts make the same judgment. Others claim that there is good sociological and psychological evidence to suggest different judgments are possible. A question about the criticism is whether the sociological and psychological evidence would be applicable to an ideal observer as opposed to a human being. The differences between ideal observers and humans concerning sociology and psychology might render such evidence useless in accounting for differences in making judgments. Although we want to explain and account for moral disagreement among people, it is less clear whether moral disagreement among ideal observers can be seen as a virtue of the theory.

This is also the problem about absolutism and relativism. If the judgments of the ideal observer are supposed to be absolutist, holding true for everyone at all times as Firth contends, disagreement among ideal observers would challenge his account's absolutism. If we do end up with a relativist ideal observer theory, it is unclear how the ideal observer's judgments give meaning to our moral terms. This possibility of difference is part of Smith's account. He endorsed the idea that cultural differences would make for differing judgments of ideal observers.

Related theories such as Nagel's and Baier's do not involve an observer but a position from which we are to make moral judgments. These positions would befit an ideal observer, however. The "view from nowhere" and the "moral point of view" attempt to get at the same kind of objective and impartial judgments without positing an observer per se and thus avoid some criticisms.

Connections to Business

The characteristics of the ideal observer can be useful in making ethical decisions related to business. For example, if a stakeholder theory is correct, the ideal observer would have little trouble identifying the widest possible set of stakeholders and weighing their claims. Ideal observer theory can serve as an important reminder to those making business decisions, of both moral and nonmoral import, to strive to be dispassionate and objective. A further application of ideal observer theory to business decision making might be in mediation, where a mediator takes on a role similar to that of the ideal observer in that he or she is to be disinterested. Another application might be in the endorsement of a publicity requirement. The ideal observer from this standpoint has nothing to hide from others about his or her decision-making process. The absolutist quality of Firth's theory, for example, can also be useful for business insofar as it requires that we all use moral terms the same way and prohibits a business from making exceptions for itself that it would not give to others.

—Ellen M. Maccarone

See also Absolutism, Ethical; Consequentialist Ethical Systems; Ethical Decision Making; Impartiality; Mill, John Stuart; Moral Imagination; Moral Point of View; Relativism, Moral; Smith, Adam; Utilitarianism

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Identity Theft

Identity theft, also known as identity fraud, occurs when an individual's personally identifying information is used without permission and/or knowledge by someone else (often a stranger). It is a form of impersonation that enables someone to commit fraud and generally results in financial harm to the individual and financial gain to the impersonator. During the past decade, the increasing amount of personal information available on the Internet has made this a growing concern.

A person's identity refers to that information that distinguishes him or her from other people. In some ways, it encompasses a person's accomplishments and is closely connected to reputation. A person's identity relates to information that exists, whereas a person's reputation reflects opinions about a person's identity.

More specifically, particularly in the context of identity theft, identity refers to the pieces of information that are linked to personal and/or financial value. This set of information comprises both public and private information. For example, a person's telephone number and street address, often available in the public domain, are connected to a person's identity. Confidential information, such as a person's social security number, mother's maiden name, PIN numbers, credit card numbers, and so forth, also contributes to a person's identity. By acquiring access to this information, an individual can impersonate someone else to perform fraudulent transactions, often for financial gain.

Interestingly, there are generally two forms of theft at play. First, there is the theft of the individual's personally identifying information because the information is acquired and/or used without the permission of that individual. The theft that takes place is different from theft of property in that the original owner still has access to his or personal information. The difference is that the value of that information has been depleted because, once misappropriated, it no longer relates uniquely to the original individual but now also points to the imposter as well. Second are the benefits associated with the impersonation. While identity theft is often associated with financial gain (i.e., the theft of money), it can also be used to acquire unauthorized entry, privileges, and/or benefits.

Techniques

Although identity theft is ostensibly on the rise, it is not a new phenomenon. Prior to the Internet, unscrupulous people stole mail or rummaged through other people's trash (dumpster diving) to obtain personally identifying information such as credit card numbers. Others have been found to have eavesdropped on private conversations in public venues to obtain that sort of information (shoulder surfing). According to a 2003 survey by *Privacy & American Business,* only a small portion of identity theft—16%—is attributable to friends, relatives, or coworkers. People nevertheless remain wary of the people with whom they do business because anyone to whom you give your credit card or other personal information (i.e., in a bank, store, etc.) has the opportunity to misappropriate that information.

Two new techniques for facilitating identity fraud have emerged as a result of society's growing use of and reliance on the Internet and e-mail. Phishing, for example, occurs when someone impersonates a trusted entity in electronic messages aimed at securing confidential information such as log-in names and passwords. For example, some phishing attempts target the customers of banks and online payment services such as PayPal. These messages often urge individuals to log on to their accounts via provided Web links. In fact, the Web links are fake, and the messages end up tricking people into disclosing their personal information to strangers. The Web links are actually tools used by phishers to capture the desired personal information (i.e., account numbers, passwords, etc.) so that they can then use that information for their own purposes.

The second way in which e-mail and the Internet are exploited for fraudulent purposes is through spam. Spam refers to unwanted, unsolicited e-mail messages, often used for mass advertising. Fraud can occur through spam e-mail as mass messages are used to cheat people by enticing them to buy fake products or pay a fee for a useless or nonexistent service or luring them in some other way to give up money under false pretenses. Many of these messages direct recipients to Web sites that invite them to input personal information in exchange for the opportunity to receive gifts or win awards. These range from a $50 gift card of a department store to a chance in a lottery.

Technology has added new dimensions to concerns surrounding identity fraud. The increasing amount of personally identifying information that is created, exchanged, stored, and maintained in computer-based databases creates new vulnerabilities. The Internet provides a virtual playground for hackers, as do personal computers—used in most offices today. The skillful thief can rifle through electronic data to find what he or she needs without authorization.

Impact

Within recent years, it appears that, while the number of reported instances of identity theft has arguably decreased, the magnitude of financial harm has increased. According to a 2006 survey cosponsored by Javelin Strategy and Research and the Better Business Bureau, the actual number of adult victims of identity fraud in the United States has decreased from 10.1 million in 2003 to 8.9 million in 2006. The dollar amount suffered by victims as an aggregate has, however, increased from $53.2 billion in 2003 to $56.6 billion in 2006. This is in addition to significant out-of-pocket expenses reported by victims that increase losses by 10% or more.

Tremendous tangible and intangible costs are borne by both victims and businesses. The costs to individual victims, in addition to the dollar amount of actual losses, remain significant. Along with financial consequences, victims also suffer damage to their reputation and credit report and substantial lost time. According to a recent survey issued by the Federal Trade Commission (FTC), 15% of victims reported that their personally identifying information was misappropriated for use in nonfinancial ways, such as to obtain government documents.

According to a 2003 survey conducted by the Identity Theft Resource Center, victims on average spend 600 hours regaining their identities and repairing the harm. This same survey reports that the emotional harm associated with identity theft is equivalent to that experienced by victims of violent crimes.

Major costs accrue to financial institutions and other businesses as well. Business losses attributable to identity theft totaled $47.6 billion in 2002, according to the FTC survey. These financial costs are in addition to costs associated with loss of trust and damage to reputation. Additional costs are linked to increased security measures that businesses are finding it necessary to implement to protect the personal information of customers as much as possible.

Account hijacking (i.e., unauthorized access of bank accounts) is reportedly the fastest growing form of identity theft, according to the 2003 Identity Theft Resource Center survey.

Legal Framework

Identity theft is a crime. That having been said, from a legal perspective it remains a sort of moving target in that it transcends physical, geographic boundaries. It is also difficult to prove. While an individual can claim losses, those losses are not always attributable to a clearly identifiable person, particularly since the thief operates under the guise of a stolen identity. In the United States, local, state, and federal enforcement agencies handle investigation and prosecution under general laws.

Specific privacy and data protection legislation exists in other countries to offer protection from and compensation for identity theft. In Australia, for example, control over identity theft falls under the auspices of the Office of the Privacy Commissioner. In the United Kingdom, personal data are protected by the Data Protection Act, a British act of Parliament that governs proper use of personal data collected and used by organizations.

Responsibilities of Individuals and Businesses

There is no doubt that the victims of identity theft suffer significant unsolicited harm. It is also true, however, that some victims leave themselves vulnerable to this sort of harm. People who value their personal information have an obligation to take reasonable precautions to protect that information, if for no other reason than that, in many instances, they are in the best position to keep that information secure. All sorts of shredders and shredding services are available today to prevent dumpster divers from acquiring anything useful relating to a person's identity. Furthermore, Internet users can choose what information to reveal online and under what circumstances. Any individual who discloses personal information on nonsecure Web sites does so at his or her own risk.

This is not to say that individuals are always in a position to prevent the theft of their personally identifying information. In fact, according to the FTC survey, 49% of the victims of identity theft do not know how their information was stolen. People can, however, remain vigilant regarding the security of their identities. Regular monitoring of accounts, for example, can provide for early detection of suspicious behavior. Approximately 26% of the victims only become aware of the theft because of reports of suspicious activity by businesses (i.e., credit card companies, banks, etc.).

The arguably greater responsibility therefore falls on the shoulders of businesses. First, it is the responsibility of companies that gain access to personally identifying information to protect that information from unauthorized disclosure. This means that companies have to take particular care in choosing the people they hire and in training them to safeguard customer privacy. In addition, they have an obligation to create and implement systems to protect data from theft.

Second, it is also the responsibility of companies to monitor accounts to detect suspicious activity. American Express regularly verifies unusually large purchases with the account holder before authorizing payment. Similarly, Discover often requires account holder verification after several subsequent gas purchases in a short period of time. Self-serve payment systems, such as gas stations, are particularly vulnerable to accepting stolen credit cards. While this creates an inconvenience for automobile travelers, it represents one way Discover is able to mitigate losses linked to stolen credit cards.

Conclusion

The harm to individuals and businesses resulting from identity theft is significant and sometimes irreparable. Once a person's identity is stolen, while he or she can recover financial compensation, the associated emotional damages are much more difficult to repair. Businesses, too, suffer substantial costs linked to identity theft. Although a legal framework aims to prevent and punish identity theft, it nevertheless remains the responsibility of individuals and businesses to safeguard the personally identifying information in their care.

—Tara J. Radin

See also Electronic Commerce; European Union Directive on Privacy and Electronic Communications; Internet and Computing Legislation; Privacy; Reputation Management

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Immigration Policy

Immigration is the movement of individuals who are citizens of one country to residency within another country. The gamut of reaction from host countries runs all the way from a xenophobic refusal to accept immigrants (e.g., China and Japan) to being a country that makes immigrants part of its national identity (e.g., the United States). For historical, demographic, and economic reasons, the Western Hemisphere and Anglophone countries (the United States, Canada, Australia, and New Zealand) have a long tradition of immigration. The economic growth that accompanied the formation of the European Union (EU) has led to the influx of eastern Europeans and Muslims to western European countries such as Germany and even to Sweden. These countries are now beginning to experience some of the same problems that the United States has faced for some time.

Immigration may be looked at from the point of view of the immigrant or of the host country. The motivation of the immigrant may be either negative or positive: escape from undesirable political, economic, or social conditions or attraction to better such conditions. In other words, the major motives for immigration have been the desire to live under a different kind of regime or to better oneself and one's family economically.

From the point of view of the host country, there is a concern for the impact on national identity, the economy, the environment, unemployment, welfare, crime and security, education, culture, family life, religion, race relations, and domestic politics in general. Immigration, therefore, has always had an important political dimension and an economic dimension.

Precisely because of its economic and political dimensions, immigration is an important concern for businesses. Immigrants bring special benefits to employers and the economy of the host country and added costs both to employers and to society at large. The recent phenomenon of globalization has underscored both those dimensions. In what follows we shall focus on the United States, but we shall also show the extent to which these issues have become global.

Let us begin with some terminological clarification for those countries that have immigration. A *citizen* (or *subject*) of any country is any person born in that country or its territories or who has been *naturalized.* A person may have *derivative* citizenship if at least one parent was a citizen. An *alien* is any person who is not a citizen. Aliens may be of two types, temporary residents or permanent residents. *Temporary* aliens include tourists, students, and so forth. Temporary aliens also include refugees and *asylees. Refugees* are persons currently outside their country who are unable or unwilling to return to their country of nationality because of fear of persecution on account of race, religion, or membership in a particular social group or because of political opinions. Asylees are refugees who have been granted temporary alien status in another country. *Guest workers* are aliens who have been given special permission to reside and work in a country for a specified and limited period of time.

Immigrants are aliens who have been granted *permanent* residency; that is, they can reside in the United States and work without restriction, and they are protected by law, but they cannot vote in elections. Asylees and refugees may apply to become immigrants or permanent residents through *naturalization.* Immigrants may become naturalized citizens of the United States by fulfilling the following six requirements: They must be at least 18 years of age, achieve basic literacy in English, demonstrate some knowledge of U.S. history, have resided in the United States for 5 years, reflect sound moral character, and take an oath of allegiance.

Illegal immigrants are those who have entered the country illegally, that is, without permission and a designated status (*undocumented aliens*), or who have stayed beyond the legally permissible time period.

There are five important immigration questions:

1. What is current immigration policy?
2. What has been its evolution (history)?
3. What sort of impact does this have on businesses and businesspeople?
4. What are the social costs of immigration?
5. What is the future of immigration policy?

Current Immigration Policy

The 1986 Immigration Reform and Control Act (IRCA) prohibited employers from hiring undocumented aliens and imposed penalties. The 1990 Immigration Act provided for a 160% increase of admissions for employment-based immigration. Employment-based immigration is divided into five subpreferences. The first is for those with extraordinary ability, outstanding professors and researchers, and certain multinational executives and managers. The second is for professionals who because of exceptional ability will substantially benefit the economy, culture, education, or welfare of the United States (licensed nurses and physical therapists, for example, because of chronic shortages in those fields). The third is for those workers, skilled and unskilled, in fields in which there is a shortage of U.S. workers. Certification by the Department of Labor is required for admission of those in the second and third categories, and all but those of exceptional ability must have a U.S. employer petition for them. The fourth preference is for special immigrants, such as religious workers and former longtime employees of the U.S. government. The fifth preference provides for immigration of investors whose investments will create a minimum of 10 jobs in the United States.

There are some serious controversies in implementing employment-based preferences. Since the Department of Labor must certify that there is a shortage of available and qualified workers and that the hiring of aliens will not adversely affect local wages or working conditions, the burden of providing such evidence falls on the prospective employer. There is now a global market for talented individuals from around the world, so one question we now face is not whether there is someone in the United States who can do the job but whether someone from outside the United States can, in the estimation of potential employers, do the job better. This bears a distinct analogy to the issue of outsourcing. The process has generated a whole body of highly technical and complicated law. In addition, employers must pay at least the prevailing wage. This has led to controversies in determining the prevailing wage or what types of jobs are substantially comparable with the one being offered. This regulation brings into play the same economic questions that surround the minimum wage law.

In IRCA there is a provision to sanction employers who employ unauthorized aliens. It is unlawful to employ any individual (whether or not that person is an alien) without having proper documents. The employer is required to examine, and retain a verification form thereof, the potential employee's U.S. passport, a certificate of U.S. citizenship or naturalization, an unexpired foreign passport endorsed by the attorney general and authorizing U.S. employment, or a resident alien card (green card). The employer could be subject to a cease and desist order as well as a civil fine for hiring, recruiting, or referring violations. A pattern of IRCA violations may mean a criminal penalty of up to $3,000 for each unauthorized alien, imprisonment for up to 6 months, or both. The 1996

Illegal Immigration Reform and Immigrant Responsibility Act (Simpson Act) imposed sanctions on employers of illegal aliens.

Further penalties against employers are currently contemplated. Some employers prefer to hire "illegals" not only because of low wages but because no benefits are paid as well.

IRCA provides for a special counsel to investigate allegations that an employer has discriminated against individuals on the basis of national origin or citizenship status. If a complaint is made that an employer is engaging in an unfair immigration-related employment practice, a hearing will be conducted by an administrative law judge, who may require the hiring of the individual as an employee or the payment of back pay, and can even award attorney's fees to the prevailing party.

Evolution of U.S. Immigration Policy

Immigrants do not automatically and easily become members of a new culture. There are ties and loyalties to old identities; there is a period of transition sometimes lasting several generations, often difficult, in accepting a new identity; some immigrants never become fully acculturated or even accepted by the host culture; some even return to their former countries.

The history of immigration policy in the United States reflects the evolution of attitudes toward national identity. Thomas Jefferson was concerned that immigrants from monarchies would not support republican government; George Washington and the authors of the Federalist Papers were concerned that immigrants would challenge federalism. Benjamin Franklin was concerned that the large numbers of Germans in Pennsylvania would lead to German becoming the official language of the state. From 1820 to 1860, more than 10 million immigrants, mostly Irish and German Catholics, entered the United States. This led to an anti-immigration movement within the Protestant Anglo-Saxon community in the cities of the Northeast.

A second huge wave of immigration occurred in the first two decades of the 20th century. This led to the 1921 National Origin Quota Act. To maintain the then present ethnic and cultural balance, the annual limit of immigrants from a given nationality was set at 3% of the numbers already present (as of the 1910 census). In 1924, Congress passed the National Origins Act and set the 1890 census as the base year for quotas; it reduced the quota to 2%. Naturally, the resulting system favored Anglo-Saxon and other immigrants from northern and western Europe.

Here we witness a recurrent theme: Older established ethnic communities attempt to maintain what they take to be traditional culture by limiting immigration to countries of their own origin or perceived sharers of the same culture; more recent immigrants perceive discrimination and seek to achieve some sort of numerical parity. Some racial, ethnic, or religious groups already within the United States see themselves as penalized because they are a minority, and they believe that increasing their numbers will gain for them the respect they deserve.

Perceived or alleged discrimination is also connected with another phenomenon in U.S. politics. From the very beginning, immigrants were targeted as clients by political parties. The general presumption at present is that immigrants are more likely to vote for the Democratic Party than for the Republican Party. Some liberals and many radicals argue that the problems of the United States (racism, bigotry, economic exploitation, crime, welfare dependency, etc.) are the result of a lack of democracy resulting from the domination of the United States by the descendants of western Europeans. Greater or true democracy will come about, it is alleged, when the population is demographically altered, and immigration is one way of achieving that end. Foreign-born women have an average of 2.25 children, whereas U.S.-born women have 1.93 children.

In 1965, Congress abolished national origin quotas. That system was replaced by a series of preferences for relatives of present citizens or resident aliens. In addition, there are limits on any one country of 20,000 and a numerical ceiling for immigrants from the Eastern Hemisphere of 170,000. In 1968 Congress set a ceiling for immigration from the Western Hemisphere at 120,000 annually. Three fourths of all immigrants now come from Asia and Latin America. The 1990 Immigration Act introduced the Diversity Program, or "lottery visas," to correct the consequences of the quota system with regard to "underrepresented" countries.

Republicans (comprising classical liberals and conservatives) reopened the debate on immigration by calling attention to the increase in illegal immigration, especially across the California and Texas borders from Mexico. Compounding the problem of its illegality were the facts that "illegals" (a) do not reflect any rational policy of who should be allowed to come and (b) do not assimilate easily both because of their illegal status and because they often speak a different language, usually Spanish, which exacerbates growing social problems of crime and welfare dependency. Approximately 28% of immigrants above the age of 5 live in households where no one above the age of 14 speaks English. That is much higher than the rate (18%) for immigrants who arrived before 1980.

Conservatives identify the United States with a specific set of values (personal autonomy, individual rights, free market economy, rule of law, limited government) historically originating in Protestant northern and western Europe, especially Great Britain. They argue that the United States has absorbed and can continue to absorb immigrants who subscribe to those values or who can assimilate those values without disrupting the conditions that permit those values to continue to flourish among those who are already here. They insist that it is important to identify the cultural background of potential immigrants, that rates of immigration are important to the absorption process, and that speaking the English language is a crucial part of the absorption process. They argue that in the beginning of its history, the United States had a preference for those from northern and western Europe, most especially those from Great Britain, since these people are most likely to have shared the same cultural values. At the same time, the United States has steadily modified its policy by lifting exclusions as circumstances changed.

Neoconservatives see the United States as having two missions, not only the preservation of current values at home but also the promotion of those values worldwide. Legal immigrants are welcome to the extent that they can serve that double mission. Legal immigrants are welcome to the extent that they already subscribe to and practice those values, and they can also serve as a positive example to their previous nation and culture.

The historical demographic pattern has been for immigrants to cluster in cities (for economic opportunities) and neighborhoods (for maintaining some kind of cultural continuity—Chinatown, Little Italy, Little Havana, etc.). The existence of ethnic neighborhoods both eases and frustrates the transition to assimilation. It eases the transition by allowing newly arriving immigrants to benefit from the experience of older immigrants. It exacerbates the transition by allowing some to immunize themselves from change. This is a continuing problem for those at the low end of the economic spectrum. However, many new immigrants come with the possession of a large amount of capital, business expertise, high levels of education, and the presence of other family members who have already made the transition.

Economic Impact

Economic considerations have always loomed large in immigration. For example, the importation of slaves was a concern to all states, free and slave alike. Some slave states acted to prohibit the international slave trade, and some free states insisted that slaves entering the state would be free. Some slave states insisted that the movement of free blacks was essential to the preservation of the institution of slavery, and some free states erected barriers to the entry even of free blacks.

With the demise of slavery, the major concern was that immigrant labor might constitute a threat to domestic labor. In 1882 Congress passed the first immigration law targeting a specific ethnic or racial group, the Chinese Exclusion Act, which suspended immigration of Chinese laborers and forbade admitting Chinese to citizenship. In the same decade, Congress passed the Contract Labor Laws, which excluded cheap foreign labor that would depress the labor market and provided for deportation of aliens brought in violation of contract labor laws. A head tax was used to further discourage immigration of those likely to price their labor more cheaply than the existent workforce.

In the first decade of the 20th century, almost 8.8 million immigrants were admitted. The majority were from southern and eastern Europe and were slow to assimilate. As with the Chinese, Congress passed restrictive measures to discourage immigration. The addition of a literacy requirement in 1917 effectively barred numbers of illiterate southern and eastern Europeans, and an eight-dollar head tax further discouraged their immigration. Though these measures made it more difficult to immigrate, Europeans were not barred as were Asians.

In 1942, in response to a manpower shortage due to the Second World War, foreigners, mostly Mexican farm workers, were permitted to enter temporarily to work. This was extended in the 1951 U.S.-Mexican Migrant Labor Agreement (*Bracero program*) and then repealed in 1964.

In 1952, the Immigration and Nationality Act (McCarran-Walter Act) addressed issues of both national identity and economics. It preserved the quota system but added a quota for Asians (repealing Japanese exclusion) and added skilled workers. This act established a preference system preferring first those with needed skills and professions and then family members of those already citizens. Immediate relatives of citizens and permanent resident aliens were put in the highest category, while those of "exceptional ability" or in the professions were relegated to the third ranking.

Welfare and Social Problems

Article IV of the Articles of Confederation denied "paupers, vagabonds, and fugitives from justice" the privileges and immunities of citizenship. It was also standard practice for states to quarantine ships bearing passengers with infectious diseases. Other state concerns were the regulating of the movement of criminals in an effort to protect citizens from crime, persons with diseases in relation to public health, and those likely to become public charges.

Every major immigrant wave since the mid-19th century has brought with it a serious increase in crime, including organized crime. The Personal Responsibility and Work Opportunity Reconciliation Act and the 1996 Illegal Immigration Reform and Immigrant Responsibility Act (Simpson Act) are both intended to discourage poverty-stricken aliens from coming into the country illegally. They accomplish this by restricting the eligibility of noncitizens for public benefit programs. The Personal Responsibility Act emphasizes that self-sufficiency has been a basic principle of U.S. immigration law since the earliest immigration statutes. Prior to 1965 there were very few opportunities even for legal immigrants, but with the vast expansion of welfare, since then things have changed. Prior to 1965, immigrants either relied on their own capabilities and the resources of their families, their sponsors, and private organizations or they returned to their country of origin. According to a study done by the Urban Institute in 1994, the greatest impact of the presence of undocumented immigrants is on the states' public education systems, not the federal benefit programs that were always off-limits to them. The estimated expenditure for providing public education to undocumented aliens across seven states for fiscal year 1993 was $3.1 billion (as compared with $1.9 billion estimated to have been collected in taxes from these same "illegal immigrants").

The current grounds for exclusion are the following: communicable diseases, including HIV; physical or mental disorders dangerous to others; mental retardation; insanity; psychopathic personality; drug addiction or drug trafficking; chronic alcoholism; conviction of a crime of moral turpitude (theft, fraud, child abuse, violence, prostitution, polygamy); conviction of crimes with sentences totaling more than 5 years of prison; being a pauper; being a beggar; likelihood of becoming a public charge; illiteracy; being involved in espionage, sabotage, or terrorism; being a member of a communist or totalitarian political party; participation in Nazi persecutions; being a graduate of a foreign medical school planning to practice medicine; having been previously deported; being convicted of immigration fraud; being a stowaway; being a draft evader in the United States; and violation of a child custody order.

Future of Immigration

The debate over immigration will continue. There are three clearly identifiable major positions on the issue: liberal, libertarian, and conservative. Adherents of liberalism view aliens of all kinds (legal immigrants, illegal immigrants, asylees, etc.) in the same category. Once here, there is no difference between someone who entered legally and someone who entered illegally. In addition, aliens are viewed as belonging in the same category as the domestic poor or underclass. Since adherents of liberalism are likely to believe that people are naturally good and corrupted only by their environment, any problems that aliens have are seen as the product of structural barriers in the host nation such as discrimination. All aliens should be given full access to all welfare benefits. Adherents of liberalism tend to look on critics of immigration the same way they look on critics of welfare rights—as mean-spirited people standing in the way of progress. Hence greater government involvement is needed, specifically in the area of welfare rights. This also means that voting in elections becomes more important to provide broad-based support for the liberal legislation that will promote social reform. As a consequence, liberals tend to view immigration as part of a larger domestic agenda to enhance the welfare state. Immigrants are looked on as potential converts to this political agenda (in keeping with the liberal assimilation of immigrants to the poor). Illegal immigrants cannot vote. Therefore, liberals favor an amnesty and any other program that will increase the number of immigrants or aliens who will stay and who can be naturalized as citizens and thereby become eligible to vote. The liberal position is reflected, in part, by the American Civil Liberties Union (ACLU). The ACLU, among its many activities, helps refugees and immigrants facing deportation. The liberal position is also reflected by the American Friends Service Committee. This Quaker organization opposes sanctions on employers of illegal immigrants and documents what it identifies as human rights violations committed by law enforcement agents against immigrants. The foremost liberal think tank on immigration issues is the Brookings Institution.

Adherents of libertarianism are also generally favorable to immigration. But the similarities end there. Adherents of libertarianism insist on a distinction between legal and illegal immigration and view all immigrants as potential entrepreneurs, not as the poor or dispossessed. They also tend to believe that all or most immigrants could be great successes if only the welfare state did not corrupt them once they were here. If we do away with the welfare state and allow free markets to operate, then the poor and the immigrants will all succeed. Every success story of immigrants who become successful entrepreneurs in the United States becomes an argument about the failure of liberal social engineering as a domestic policy. Some doctrinaire libertarians advocate totally open borders both to allow the market to determine success and to undercut the notion of a sovereign state, which they see as a constant threat. Other libertarians, those who recognize that the world is not at present a totally free market, advocate controlled immigration but stress that economic benefits should be the sole or major criterion for admission. The libertarian position is best represented by the Cato Institute. The most influential libertarian publication on immigration is Julian Simon's *The Economic Consequences of Immigration.*

Conservatives share with libertarians a distrust of the liberal welfare state and of liberal immigration policies because they see such policies as intended to increase political support for the liberal welfare state. They do not trust liberal affirmations about ending illegal immigration as sincere since liberals always call for amnesty of those already here and oppose returning illegal aliens to their country of origin. Conservatives point out that in recent presidential elections, the Hispanic vote was greater for Democrats than for Republicans. Hispanics tend to live in 26 cities in nine states that control two thirds of the Electoral College vote. But conservatives do not share the libertarian belief that a free market economy solves every social problem. Conservatives favor tighter control over immigration and greater stress on criteria that reflect cultural support for individual responsibility. Conservatives argue among themselves about which factors (national origin, religion, family, etc.) are most relevant. They also advocate a moratorium on immigration to better assimilate those who are already here and to inhibit the massive naturalization of supporters of the liberal welfare state. The conservative position is most notably reflected in the work of the Heritage Foundation. The best known conservative work on immigration is Peter Brimelow's *Alien Nation.*

—Nicholas Capaldi

See also Affirmative Action; Environmentalism; Immigration Reform and Control Act of 1986; Racial Discrimination; Welfare Economics

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Immigration Reform and Control Act of 1986

Through the Immigration Reform and Control Act of 1986 (IRCA), Congress sought to regularize the status of millions of undocumented immigrants in the United States, regain control of the country's borders, and meet the needs of certain industries that relied on foreign-born labor through three major mechanisms. First, employer sanctions made employing anyone not a citizen or otherwise authorized to work by the federal government unlawful and subjected employers to civil and criminal penalties. Second, many persons who had been living in the United States without permission were enabled to apply for a legal status that led to Lawful Permanent Residence (LPR) and the possibility of naturalization. Third, agricultural workers who could demonstrate certain past employment were also able to achieve LPR. IRCA's enactment, procedures, and benefits were controversial from the start and have resulted in much litigation and disputes over eligibility that continue into the 21st century.

In 1978, Congress established the Select Commission on Immigration and Refugee Policy to investigate immigration in the United States and to recommend immigration law reform. The Commission had three goals: maintaining national borders, respecting the rule of law, both in terms of enforcement at the border and due process for those placed in immigration proceedings, and fostering an open society dedicated to welcoming a reasonable number of immigrants annually and providing a path to citizenship and full social participation. Congress received reports that anywhere from 0.6 million to 12 million undocumented persons lived in the United States, with the best estimates falling between 3.5 and 6 million persons.

IRCA revealed the complexity that exacerbates the difficulty of immigration reform in this nation. IRCA evolved out of a congressional effort to reconcile conflicting objectives such as encouraging an open democracy by furthering freedom of movement, trade, and tourism while retaining secure borders. Congress intended to prohibit unauthorized work without compromising civil liberties or encouraging new discrimination against citizens who might appear to be foreign-born. In addition, Congress sought to encourage economic growth without intensifying the economic magnet that pulls migrants across borders. Finally, Congress attempted to resolve the justice issues raised in treating a large population that lives out of status, in part, due to an overburdened immigration process in which many fall through the cracks and that divides families into different legal statuses that force otherwise eligible families to live apart for many years.

Through IRCA, Congress attempted to balance these needs by adopting most of the Select Commission's recommendations. First, Congress sought to stop unauthorized immigration by turning off the magnet of jobs. Second, Congress offered legalization to most persons who had been living in an unlawful status since 1982. Third, Congress provided legalization to farm workers who could show past employment.

IRCA first broke new ground in limiting the freedom of all U.S. citizens to seek employment wherever they chose by requiring virtually every employer to initially determine whether an employee was either a citizen or otherwise authorized to work by the federal government. Almost every new employee hired after November 6, 1986, filled out an I-9 form with copies of documents that demonstrated both identity and citizenship or work authorization. IRCA required the employer to document this information and empowered the government to issue warnings, impose fines, and seek criminal penalties should a pattern or practice of hiring unauthorized workers be found. Penalties were also established for record-keeping improprieties, although employers could rely on a good faith defense if documents appeared to be valid.

Fears that employers would refuse to hire certain persons due to concerns of violating employer sanctions provisions necessitated enactment of nondiscrimination provisions prohibiting employers from discriminating against eligible applicants who might appear foreign-born or who might have a foreign accent, a form of discrimination known as "national origin discrimination," which might not otherwise be covered by the nation's other antidiscrimination laws. IRCA established an Office of the Special Counsel for Immigration-Related Unfair Employment Practices to investigate and review any claims.

Second, the legalization provisions initiated a number of new lawful immigrant categories. Congress established a new category of lawful presence called Lawful Temporary Resident (LTR). Otherwise admissible applicants who could show that they had been living continuously in the United States in an unlawful status since January 1, 1982, and who applied within a 1-year window from May 5, 1987, until May 4, 1988, could become LTRs. More than 2.7 million persons applied within the 1-year period, with almost two thirds eventually becoming LTRs. IRCA set up a formal procedure for LTRs to apply for LPR and eventually apply for U.S. citizenship. IRCA also recognized the role of nongovernmental agencies designated as a Qualified Designated Entity (QDE) in assisting in the education and preparation of LTR applications. A special appeals process provided review for denied applications.

Third, the Seasonal Agricultural Worker (SAW) program also permitted undocumented farm workers to apply for LTR status. Given the exigencies of migrant farm work, with workers often moving frequently during a growing season, the SAW provisions set up two different grounds for eligibility; one required a worker to show a minimum of 90 days of agricultural employment each year for a continuous 3-year period, and the second required one to demonstrate 90 days of agricultural employment within a 1-year period. All members of the first group automatically became LPRs on December 1, 1989, with members of the second group obtaining their LPR status on December 1, 1990. Approximately 1.3 million workers received SAW documents.

IRCA's success in legalizing almost 3 million persons cannot be minimized, but the act itself did not accomplish all its goals. First, by leaving a large gap between the 1982 eligibility date and the application period of 1987 to 1988, IRCA undermined its own goal of wiping the slate clean and starting anew with no unauthorized persons living in the United States. The very quick time frame from enactment to establishing the process for the 1-year window for applications left many legal issues unresolved, and litigation continues almost two decades later. The discrimination issues have not been easily remedied and continue to pose difficult issues for employers. Resolution of the discrimination issue has also led to proposals for a national identity card that raises great concerns among civil libertarians, although IRCA specifically precluded such a card. Finally, the 2000 Census estimates that 7 million unauthorized immigrants reside in the United States, which exceeds the number Congress had sought to reduce through this legislation.

—Craig B. Mousin

See also Employment Discrimination; Immigration Policy; National Origin Discrimination

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Impartiality

The concept of impartiality figures in ordinary morality and philosophical discussions of morality in several ways. A virtue in many everyday contexts, impartiality is widely seen as crucial to the very meaning of morality. Moreover, normative theories of various types view impartiality as central to moral justification and see themselves as reflecting, displaying, or building in some way on this value. In recent years, however, some philosophers have challenged the priority that traditional ethical theories place on impartiality.

Impartiality in Everyday Life

To be impartial is to be free from bias or prejudice, to be detached, objective, and disinterested, and to favor neither one side nor the other on a given question. Because we expect and require impartiality from judges and public officials, whose job it is to administer policies and enforce the rules without playing favorites, impartiality is sometimes seen as primarily a public virtue—not just a desirable trait of government agents, but also a defining feature of the rule of law and of modern, rationalistic bureaucracy. But we also demand impartiality from Little League referees and, in certain contexts and in certain ways, from teachers and employers. Morality may even require impartiality within personal relationships. Parents, for example, should not favor some of their children over others.

But impartiality has its limits, and it may have to be balanced against other legitimate moral concerns. Sometimes, indeed, impartiality would be inappropriate or even wrong. Although teachers should be impartial, good ones also cater to the particular needs of their charges, sometimes lavishing more attention on some children than they do on others. And no one expects parents to be impartial between their own children and those of other parents. It is helpful therefore to distinguish the group in regard to which a person is supposed to be impartial and the respect in which the person is supposed to be impartial with regard to members of that group. For example, an employer must be impartial with respect to the religion of employees but not their job performance. In contrast, when socializing outside work, the boss is free to favor coreligionists. Identifying in this way the group toward which, and the respect in which, one is to be impartial may allow us to pinpoint the moral rationale behind the required impartiality, such as fairness, for instance, or some role-based responsibility.

Impartiality and the Nature of Morality

Most philosophers believe that moral judgments must be reversible and universalizable. If it is right for you to do X to Frank, then it must be right in an exactly reversed situation for Frank to do X to you. More generally, if one judges something right or wrong, then one must make the same judgment about any other situation the universal properties of which are the same. As a result, many philosophers believe that taking the moral point of view means looking at things in a detached and impartial way and acting on the basis of considerations that are objective and free from personal bias. For this reason, some deny that egoism is, properly speaking, an ethical theory at all.

Impartiality seems central to the moral enterprise. Some philosophers have tried to capture this thought by offering ideal observer or impartial spectator interpretations of morality. According to these, moral judgments are judgments that would be endorsed by a fully informed observer, one who transcends any particular point of view and looks instead at things dispassionately, impersonally, and objectively. Sometimes this device is intended merely to elucidate our concept of morality; other times it is used to generate substantive normative principles, frequently of a utilitarian sort.

Utilitarianism requires us always to act so as to bring about as much overall happiness as possible. Because it views the happiness of each person as equal in value to that of any other (including the agent) and because it requires the maximization of net happiness without regard to the identity of individuals or the distribution of happiness among them, utilitarianism takes impartiality to an extreme. But many other normative theories also see themselves as respecting the fact that morality is objective, and not simply an expression of personal opinion or interest, and that each person matters just as much as, and no more than, any other person. For example, the categorical imperative of Kant, the original position of John Rawls, and the contractualist theories of writers such as Thomas Scanlon and Brian Barry can be seen, each in its own way, as grounded in an impartial respect for person.

Partialists Versus Impartialists

In the past two decades, some communitarians, virtue theorists, feminists, and other philosophers have denied that impartiality is a fundamental component of morality or an overarching value. They see utilitarianism, Kantianism, social contract theories, and other popular normative systems as committed to an impartiality that violates everyday moral experience. Not only is it impossible for human beings to attain the impartiality, neutrality, and detachment these theories require; the pursuit of impartiality is also incompatible with family ties, with personal relationships, and with virtues such as loyalty and patriotism. According to the partialists, morality is primarily a matter of particular attachments, personal relationships, and individual commitments, rather than an abstract injunction to treat all others impartially.

Impartialists respond by distinguishing first-order impartiality from second-order impartiality, that is, impartiality as a guiding principle of daily conduct from impartiality as a test to be applied to the selection of the moral rules or principles one is to follow. A normative theory might strive to justify its rules on impartial grounds, and yet those rules permit certain kinds of partiality. Utilitarians, for example, might permit parents to show special regard for their own children on the basis that it maximizes well-being overall for parents to do so. It remains an open question, however, whether this response removes all possible tension between morality, on the one hand, and personal relationships and other apparently admirable forms of partiality, on the other.

—William H. Shaw

See also Ethics of Care; Feminist Ethics; Ideal Observer Theory; Moral Point of View; Moral Reasoning; Rawls's Theory of Justice; Social Contract Theory; Universalizability, Principle of; Utilitarianism

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IMPLIED WARRANTIES

A warranty is a guarantee or promise surrounding a commercial transaction. An express warranty is an explicit guarantee or promise openly and voluntarily offered by one party to the other to cover a specific transaction. An implied warranty is a guarantee or promise mandated by law, ordinarily running from a seller to a buyer, concerning the fitness or value (the "merchantability") of the product or service being sold. Exactly what warranties are mandated, how long they run, whether and how a seller can disclaim any of them, and what remedies are available if any implied warranties are breached are all determined by the specific laws covering the transaction. In the United States, implied warranties are usually enacted and enforced under state law, while some transactions are covered by federal law, and a few transactions can be governed by both federal and state laws that are applicable.

Under the Anglo-American common-law system, a warranty comprises a promise between a seller and a buyer that a product or service will meet designated criteria of use or value; and if there is a failure to meet any criterion in whole or part, some remedy (such as compensation, repair, or replacement) will be forthcoming. A warranty is typically given by the seller to the buyer in explicit form such as a written document, detailing the specific promises associated with the particular sale. (In some transactions, buyers might also make certain promises that legally constitute a warranty that protects the seller: for example, that a license limitation for use of a patent will not be violated and the buyer will indemnify the seller if a breach results in legal action.) This express warranty is agreed between the parties—sellers and buyers—of the product or service at the time of sale and forms the foundation of the contractual agreement between them, along with the usual terms surrounding delivery and price.

Another form of warranty has become common—particularly though not exclusively in the United States, where the promises and criteria and remedies are determined by operation of law, not by agreement of the parties. In such cases, a legislature or court decides for the parties what promises a seller owes a buyer (or vice versa)—beyond any express promises about which the parties might negotiate and eventually agree. In some cases, these implied promises can lawfully be disclaimed by the seller (i.e., they will not come into existence if proper notice is tendered by the seller to the buyer before the transaction is settled). Still, in most consumer transactions, applicable statutory provisions and court decisions severely limit or deny altogether a seller the ability to disclaim any implied warranties that run in the consumer's favor.

Implied warranties may be best known from ordinary consumer transactions, both large and small in nature, but they also are mandated in many other commercial transactions. For example, under Article 2 of the Uniform Commercial Code (UCC)—a code that has been adopted in some form by every state in the United States—there is an implied warranty of merchantability, whereby goods are held to six established criteria that circumscribe the quality, quantity, fitness for use, and even packaging of the goods.

Similar language is embodied in international treaties, such as in the United Nations Convention on Contracts for the International Sales of Goods (CISG), to which more than 60 developed and developing countries are signatories, and potentially covers a significant proportion (up to two thirds of the movement) of commercial goods in international trade. According to its Article 35, the seller is bound to supply goods according to criteria covering the quantity, quality, general and particular fitness for use, and packaging to preserve and protect the goods.

The specific terms (standards, remedies, permissible disclaimers, etc.) associated with an implied warranty of merchantability and with which most consumers are familiar in the United States is a function of the Magnuson-Moss Warranty Act, federal legislation that stipulates minimum criteria for warranties of consumer products nationwide. Importantly, it provides the national legislative foundation for individual state enactment of consumer protection and product liability laws, not least of which are statutes commonly called "Lemon Laws," enacted by the several states safeguarding consumers in the sales and leases of new and used vehicles. For example, California consumers are protected under the Song-Beverly Consumer Warranty

Act and Tanner Consumer Protection Act under that state's civil code, which together provide a variety of implied warranties, legal presumptions, and remedies, including mandated repairs, purchase price refunds, and compensatory and punitive damages, if vehicles present problems that substantially impair the use, value, or safety of the vehicle. These protections run concurrently with the term of the manufacturer's express warranty.

The UCC and CISG likewise provide for implied warranties that arise by a course of dealing and usage of trade. Under these provisions, if a particular sale is one of a pattern of regular transactions between the parties or is a type of transaction that regularly occurs between the seller and other buyers similarly situated to the current purchaser who intends to use the good or service in a specified vocation or trade (e.g., a construction company purchasing building materials from a buildings supply firm—regardless of whether the construction company has previously dealt with that supply firm), the terms of the current transaction will be so interpreted and thereby shall import implied warranties from previous or similar dealings. Article 1 of the UCC details the expansive range of such usages and courses of dealing covered, including places, vocations, and trades wherein expectations can arise, and so implied warranties will be imposed.

In addition to merchantability, a warranty of fitness for a particular purpose can also be implied. This promise is imported into the contract by operation of law when the sale is made to a buyer who is informed or assured that the product or service at the core of the transaction is fit for the particular purpose envisioned; that is, not only is it to be held merchantable in general terms (e.g., this SUV will function as a new transportation vehicle ought, or that computer will operate as computers of its type should) but should also meet the need for the purpose specified (this SUV on the showroom floor is capable of towing the buyer's boat and trailer, or that computer as manufactured can function as expected in the context of rough handling and wide temperature variations regularly encountered in the buyer's anthropological fieldwork).

A variety of other warranties can be implied by operation of law. For example, many states provide for an implied warranty of

- workmanship for construction projects (an implied promise running from builders and home renovators to home buyers and owners);
- marketable title or title free of encumbrances for real estate transactions (from a real estate seller or agent to a buyer);
- good title to chattels (from a seller of personal, moveable goods to a buyer);
- seaworthiness in marine insurance (from an insured of a ship to the insurer);
- habitability of rental residential property (from landlord to tenant);
- quality and wholesomeness of foods (from seller to consumer);
- fair or noninfringing use of intellectual property (from licensor to licensee or vice versa in appropriate transactional settings); and
- a promise that professional services will be rendered with reasonable care (running from professionals to their clients).

Other specialized legislation can provide for additional, distinct warranties. Under the Uniform Computer Information Transaction Act (UCITA), for example, there is an implied warranty of accuracy of informational content covering software programs and data sold or licensed to buyers that otherwise fall outside the reach of the UCC. These sorts of warranties relating to intangibles (specifically, digital goods and services) are likely only to increase in the future as UCITA is adopted and applied by more states to a variety of cyberspace products and services.

As initially noted, though this entry uses the language of promise and contract, none of these implied warranties are technically promises or guarantees properly so called that are contractually agreed between the parties. Rather, implied warranties are statutory or court-mandated obligations that are held against one party for the benefit of another. Just what the proper extent or range of these obligations should be and what remedies are appropriate for their breach are matters of business ethics and public policy and not (typically) reserved as a function of the bargain to be struck in the market by the parties to the transaction.

These implied warranties are generally mandated when one party is in a naturally weak position relative to the other or is at some significant bargaining disadvantage, such as an individual consumer negotiating with a large business operator. In those cases, the asymmetries in market power and information about the product or service can be great, unfairly advantaging the seller against the buyer. The implied warranty becomes a principal means of helping level the contractual "playing field" for that transaction, by enhancing the weaker party's power or access to pertinent information, both before and after conclusion of the transaction. In other cases, such as those referencing trade usage in commercial transactions where the parties are likely to be more closely equal in bargaining strengths, the mandate typically permits one party to disclaim an implied warranty, with that disclaimer then becoming a matter for negotiation before the final deal is struck. Implied warranties then arguably help raise the levels of trust—between market actors in individual transactions as well as their general confidence in the market itself—that aid the market to operate smoothly, ultimately benefiting all parties.

In addition, implied warranties are invoked when a society, speaking through its political leaders and court officials, determines that some transactional terms concerning one party's obligations toward the other are simply not to be permitted; disclaiming those obligations are not and are never to be part of any bargain between the parties, regardless of their relative levels of wealth or business sophistication, the mutual desire of the parties involved, or any resulting benefit to market operations. They represent political and ethical judgments of what deals should and should not be, rather than pragmatic responses to market imperfections or power imbalances. These obligations are also the ones most likely to be assessed punitive damages when a court determines they have been breached, even when the material loss to the damaged party is minimal.

—Daniel Walter Skubik

See also Consumer Product Safety Commission; Consumer Protection Legislation; Product Liability; Warranties

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Incentive Compatibility

Incentive compatibility means that the interests of two or more individuals are aligned; in contrast, when interests are not aligned, the incentives governing behavior are said to be incompatible. From an organizational perspective, incentive compatibility means that the incentives that motivate individual members in their actions are consistent with the organization's goals.

Incentive compatibility is important in situations in which there is asymmetric information, that is, when at least one participant in an interaction does not know perfectly what another participant knows or does. The problem is that the participant with the more complete information might use that information in a way that benefits him or her at the expense of others. Incentive compatibility means that the interaction is structured in such a way that the participant with the more complete information is motivated to act in the interest of the other party (or has less incentive to exploit his informational advantage). For instance, if an insurance company offers a discount to people who do not engage in high-risk behaviors, such as smoking or skydiving, then persons who engage in such behaviors might try to identify themselves as low risk to take advantage of the discount. This type of problem is known as adverse selection—high-risk persons know they are high risk but have an incentive to "select" or identify themselves as low risk. An incentive-compatible solution would ensure that people who engage in high-risk behaviors identify themselves as such. For example, if the insurance company requires a medical exam for all persons reporting themselves as low risk, then high-risk persons may have less incentive to misrepresent themselves. Similarly, if workers promise to work hard in exchange for a high fixed salary, and if the boss cannot directly observe worker effort, then the workers might have an incentive to shirk. This type of problem is known as moral hazard—after obtaining employment, the workers work less hard than promised, thus creating a "hazard" for the boss. An incentive-compatible solution would ensure that workers work hard as promised. For example, the boss could pay workers on commission, with pay tied to observable performance measures, thus mitigating the incentive to shirk.

In economics, incentive compatibility is used as one of two important constraints in an optimization problem in which a person (such as a firm owner) must rely on others to maximize some social welfare criteria (such as profits). The *participation constraint* ensures that people want to participate, in that they are at least as well off by participating as they would be by not participating. The *incentive compatibility constraint* ensures that people are motivated to behave in a manner consistent with the optimal solution. Usually this means that the compensation people receive when the desired outcome is achieved is at least as high as the compensation they could earn when some other outcome occurs. For example, suppose a factory owner needs employees to work in his or her factory. The participation constraint ensures that some people would rather be employed in the factory than do something else. The incentive compatibility constraint ensures that the employees are motivated to act in the owner's interest.

The notion of incentive compatibility is widely used in the analysis of business and societal issues. For instance, considerations of incentive compatibility have been shown to be relevant to the design of appropriate compensation structures within firms, the regulation of business, the structure of efficient taxation rules, the organization and operation of auctions, and the development of poverty alleviation programs. Importantly, incentive compatibility has implications for business ethics. Many ethical problems in business—fraud, breaking of promises, corruption, tax evasion, misrepresentation of products or people—arise because the incentives people face are incompatible with agreed-on business or social goals. Accordingly, solutions to business ethics problems can often be found by the establishment of appropriate incentive-compatible mechanisms.

—Harvey S. James, Jr.

See also Adverse Selection; Asymmetric Information; Economic Incentives; Moral Hazard; Rationality

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Incipiency Doctrine

The Incipiency Doctrine is a rationale used to evaluate and potentially block mergers that might result in harm to competition among American businesses. It arises under the Clayton Act and is used in evaluating whether the effect of a proposed merger may be to substantially lessen competition or to tend to create a monopoly. If so, the potential harm that could result from the merger is deemed under the Incipiency Doctrine to be sufficient to block the merger. In addition to the difficulty of determining whether harm will, in fact, result from a merger, the type of harm that may result has not been clearly defined, thus leading to confusion about when to apply the doctrine.

Antitrust laws in the United States such as the Sherman Act, the FTC Act, and the Clayton Act contain provisions describing unlawful business practices. The Clayton Act, an amendment to clarify and supplement the Sherman Antitrust Act of 1890, was passed by Congress in 1914. Whereas the Sherman Antitrust Act prohibited monopolies, the Clayton Act was designed to define illegal business practices that were conducive to the creation of such monopolies or that result from them. Although the Clayton Act prohibited stock purchase mergers that resulted in reduced competition, loopholes existed, allowing individuals to find ways around the Clayton Act by simply buying up a competitor's assets. The Celler-Kefauver Act was passed by Congress in 1950, in part to address such loopholes, and strengthened Section 7 of the Clayton Act by prohibiting one firm from securing either the stocks or physical assets of another firm if competition would be reduced as a result of the asset acquisition. The legislative history of the 1950 amendments contains a dominant theme evidencing a fear of what was considered to be a rising tide of economic concentration in the American economy. In stating the purposes of their bill, both its sponsors, Representative Celler and Senator Kefauver, emphasized their fear, widely shared by other members of Congress, that this concentration was rapidly driving the small businessman out of the market. Congress appeared to see the process of concentration in businesses as an increasing tide and, to stem that tide, provided authority for arresting mergers at a time when the trend to a lessening of competition in a line of commerce was still in its incipiency or onset. Thus the Incipiency Doctrine was born. The Celler-Kefauver Act 1950 amendments included descriptions of illegal business practices designed to block mergers, the effect of which may be to lessen competition substantially or to tend to create a monopoly. In using such language, Congress indicated that its concern was with probabilities, not certainties. The language makes it clear that courts have the authority to declare mergers illegal that didn't necessarily in themselves represent a lessening of competition but rather represented the onset of a trend of lessening competition.

The Incipiency Doctrine was never fully and clearly defined, although a number of significant court cases cited the legislative history of the Celler-Kefauver Act and its Incipiency Doctrine to rationalize the blocking of mergers. The doctrine at a minimum appears to call for strict antimerger enforcement due to a perceived fear of trends toward concentration, although the understanding of how to achieve that enforcement as well as the application of the doctrine itself has varied throughout the years. The Incipiency Doctrine calls for a variety of predictions about the anticompetitive effects of mergers that may include leading to small decreases in competition, causing an industry trend or wave toward mergers and looking further into the future for possible harm.

—Mary Ellen Wells

See also Antitrust Laws; Competition; Efficient Markets, Theory of; Federal Trade Commission (FTC); Free Market; Market Failure; Market Power; Mergers, Acquisitions, and Takeovers; Monopolies, Duopolies, and Oligopolies; Perfect Markets and Market Imperfections; Price-Fixing; Restraint of Trade; Unfair Competition; Wage-and-Price Controls

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Income Distribution

Income distribution, the apportionment of total national income among all the individuals and families in a country, is an issue closely tied to the way business operates within a society. In any market economy, it is business that generates most personal income, not only through wages and benefits but through interest, dividends, and stock appreciation as well. Therefore the distribution of income is a central concern of business ethics, for evaluating both the fairness of particular business practices and the overall contribution of business to the well-being of society.

Income distribution is generally measured in one of two ways. The simpler way is to divide a society's total income into segments, such as tenths or fifths, based on either per capita or family income. These slices can then be compared with one another at either a given point in time or over an extended period. Thus one can compare, for example, how much income growth the top 10% experienced over a decade compared with the bottom 60%. A more mathematically sophisticated measure is the Gini coefficient, which gives a single number indicating the income distribution of an entire society. This coefficient ranges from 0 (perfect equality) to 1 (all income is received by a single individual), and it is especially useful for comparing distributions between nations.

The social and economic significance of income distribution depends on its interaction with other trends regarding a particular society, especially changes in the absolute level of average or median income. Increasing disparity is less significant in an environment in which most individuals are experiencing growing incomes compared with a situation where median income stagnates or even declines since the latter situation is more likely to weaken social solidarity and political unity.

Over the past generation, the United States has experienced this second, more contentious, set of circumstances. According to the Census Bureau, the Gini coefficient for the United States, which held fairly stable at about 0.40 between 1967 and 1977, has risen steadily since then and hit 0.46 in 2000. Furthermore, figures compiled by the World Bank put American society at the high end of income inequality among industrialized nations. U.S. income is more unevenly distributed than income in Japan, Korea, Taiwan, Australia, Canada, all of Europe (including Turkey), and India, though it does remain a more equal distribution than in China, Hong Kong, and Singapore and a number of poorer countries.

This rising inequality in income distribution in the United States coincides with the nation's weakest generation of average income growth. Until the mid-1970s average compensation tended to track increases in productivity over time. During the postwar generation between 1947 and 1973, for example, both productivity and average family income grew 103% in inflation-adjusted dollars. In contrast, between 1973 and 2003, productivity grew 71%, while family income increased only 22%. Furthermore, according to figures compiled by the Department of Labor, average hourly compensation (adjusted for inflation) has actually declined slightly since 1973 for the four fifths of the population not working in professional or managerial occupations.

Some have argued that tracking compensation over time produces unduly pessimistic results because income numbers do not adequately capture the improved quality of life that comes from innovation. This argument, however, fails to recognize how important innovation has been throughout almost all of American history and how it has traditionally occurred side by side with wage increases. The postwar generation not only doubled its pay but also saw the introduction of television, transistors, commercial jets, home air conditioning, plastics, new medical treatments, and a variety of other product breakthroughs. It would be difficult to argue that a business sector that generates new products but does not share the financial gains from productivity improvements with most of its employees contributes as much to society as a business sector that does both.

The issue of fairness in income distribution has been highlighted in recent years by the well-publicized relative rise in executive compensation in the United States. In 1978, the average CEO earned about 35 times the salary of the average worker. This ratio doubled by 1989, just as the bull market started on Wall Street, and then hit 300:1 in 2000, as the market peaked. It has since come down to 185:1 in 2003, but this ratio remains more than five times what it was a generation ago, a period when American business was the envy of world.

A number of factors have been offered for this divergence in income. These include the following: increasing returns to certain kinds of vital technical and professional knowledge, weakening of union power to organize workers or bargain effectively, subcontracting work to less generous employers, movement (or even the threat of movement) of manufacturing overseas, declining value of the minimum wage, less generous benefits for workers and retirees, and a growing reluctance by employees to demand a raise in an era in which downsizing has become routine. Others put the responsibility on new ways of compensating executives through stock options and other means that tend to reward short-term cost cutting, including the cost of labor. While all of these explanations appear to be somewhat plausible, researchers find that none of these, alone, can explain either the timing or magnitude in this sea change in American income distribution, suggesting that a number of factors share responsibility for this change.

Whatever the precise causes, some people find this trend problematic from an ethical perspective. Income divergence raises important questions about fairness and organizational commitment when the benefits of success predominantly accrue to a few. For ethicists influenced by Rawls, such a trend threatens to violate his rule of fairness—that gains to the productive few should not be at the expense of the least fortunate.

Libertarians, on the other hand, would be more cautious about making assumptions regarding the ethical implications of increasing income inequality. Unless inequality is generated by coercion or fraud, or by favoritism on the part of government toward one group at the expense of another, libertarians view fluctuations in the relative fortunes of different individuals as a normal part of the operation of markets as the demand for various skills, experiences, and professions shifts over time. Nonetheless, many business ethicists have argued for two decades that corporate executives need to honor and preserve implicit social contracts and, following Kant, to treat employees as stakeholders having ends of their own. Implementing such advice requires grappling with the reality of a diverging distribution of income.

—Richard Marens

See also Capabilities Approach to Distributive Justice; Egalitarianism; Globalization; Libertarianism; Marxism; Poverty; Power, Business; Rawls's Theory of Justice; Redistribution of Wealth; Social Contract Theory; Stakeholder Theory; Utilitarianism

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INDIVIDUALISM

Individualism espouses four basic ideas: (1) the intrinsic value, or dignity, of the individual human being, (2) individual autonomy or self-direction, (3) privacy, or the freedom to be left alone from outside interference, and (4) the right and duty of self-development (pertinent to most, if not all, conceptualizations of individualism). The normative conceptualization of individualism includes, at a minimum, these four elements, whereas the methodological definition—equally important but not the main focus of this entry—has a different emphasis. Methodological individualism refers to the idea that individuals, not some collective, constitute the ultimate unit of analysis in describing social relations. In other words, based loosely on definitions provided by Friedrich Hayek and George Homans, there is no other way toward an understanding of social phenomena but through our understanding of *individual* actions directed toward other people and guided by their expected behavior. In his influential book on individualism, Steven Lukes showed how the methodological and normative conceptualizations of individualism have been intertwined.

The introductory paragraph alluded to the distinction between normative and methodological aspects of individualism, with the former being the focus of this entry. However, another fundamental distinction, made by Friedrich Hayek, is between *true individualism* and *false individualism. True individualism* acknowledges the limitations of human knowledge and the possibility of social order that emerges spontaneously from individuals' actions. In contrast, *false individualism* has no confidence in the invisible hand but instead places great confidence in collective, rationalistic guidance of social relations or social engineering. According to Hayek, this distortion of individualism tends to lead to socialism and collectivism.

As is apparent by now, the different meanings and applications of *individualism* are multifaceted and range from political science to sociology to psychology and, most important in this context, to ethics. In short, individualism is a worldview that is very difficult to capture in one catchall definition. Paying tribute to this diversity of conceptualizations, I first present a brief overview of the basic elements and outcomes of individualism and describe different perspectives or manifestations of individualism in different disciplines. The entry then delves into the linguistic history of the concept, discusses implications for the field of business and society, and canvasses some critiques of individualism.

Elements and Outcomes of Individualism

The aforementioned four ideals or values are central to the individualistic worldview. First, individualists do not regard the good of the state, race, class, or some other social group as the ultimate value. Instead, they uphold the dignity of the individual as the ultimate moral principle. Although some trace this doctrine of the intrinsic value of the individual human being to the New Testament, respect for individual dignity lost some of its meaning in the Middle Ages. According to Steven Lukes, this doctrine was deemphasized in medieval times because of the overriding importance of law, the Church as the main legal institution, and the organic conception of society. Then, the doctrine of the dignity of the individual was openly proclaimed during the Italian Renaissance. Three philosophers whose work focused on this first element of individualism are Immanuel Kant, Jean-Jacques Rousseau, and Thomas Paine. Kant explained one implication of this doctrine, namely, that individuals—*because of their dignity*—cannot serve merely as the instruments of others. This first element, which is really the overriding and pivotal moral axiom of individualism, has found expression in the 1776 American Declaration of Independence and in the 1948 Universal Declaration of Human Rights by the General Assembly of the United Nations.

The second element of individualism is the idea that an individual's actions or thoughts cannot, and must not, be determined by agencies or causes outside the individual's control. Thus, Steven Lukes applied the label of self-direction or autonomy to this idea. Some philosophers, such as Kant, see a place for objective, universal principles in the autonomous human will. Others consider individualism to be an escape from obedience to social standards or customs and, thus, move it closer to ethical subjectivism. However, both variants of this second element, whether epistemologically objectivist or subjectivist, reject determinism. While many economists regard economic freedom as the essential element of an efficient capitalist system, some sociologists and psychologists, such as Erich Fromm, see autonomy and freedom threatened by the increasing corporate and market-based order of Western civilization. Those interpretations of autonomy form the great paradox of individualism: Autonomy is the sine qua non of capitalism, but—at the same time—capitalism itself may diminish or threaten autonomy (at least according to some analyses).

Third, individualism presupposes privacy, which, according to Lukes, refers to a sphere that is not the proper concern of others. In this private realm, the individual is or should be left alone by others and should be able to do and think whatever he or she chooses. Isaiah Berlin linked privacy to negative liberty. According to Benjamin Constant and Hannah Arendt, this idea of liberty refers to the peaceful enjoyment of personal independence, which may not be renounced in the interest of the state or some other collective. Whereas ancient civilizations (ancient Greeks and Romans) typically devalued the private sphere in favor of public life, religious mysticism but also secular liberalism emphasized the necessity and sanctity of the private realm. Most modern interpreters of this third element (such as David Riesman) regard conformity to some prescribed collectivist ideal (e.g., “Communist revolution”) as fundamentally opposed to individualism. Interestingly, advocates of socialist collective ideals such as unity (e.g., Mao Tse-Tung) concur with this interpretation.

Fourth, most conceptualizations of individualism include the goal of self-development. This value originated with the German Romantics, who in their *Weltanschauung* made a cult of the formation and development of individuality. (Although Aristotle also praised self-development, he did so in the arguably communitarian tradition of a virtue ethic situated within the institutions of the Greek city-state.) Thus, this distinctly modern element of individualism emphasizes individuals’ uniqueness and diversity. Most individualists (such as the early German Romantics but also Ralph Waldo Emerson) emphasize the need for development of one’s own character in opposition to society or social conformity (which is the main distinguishing feature from Aristotle’s conception of self-development). However, a second vein (in the Marxist or socialist tradition) redefined self-development as communal, that is, as impossible without community with others or without dependence on society. John Stuart Mill, influenced by Wilhelm von Humboldt, and other utilitarian philosophers tried to merge both (the atomistic and collectivist) traditions of individualism in his emphasis on individual happiness *and* its aggregation as the ultimate arbiter in moral decision making.

Frequently underpinning these four elements of individualism is the assumption that individuals’ needs, interests, or purposes are given and independent of a social context. Steven Lukes calls this assumption the element of the abstract individual. The contours of this idea, which run counter to social constructionism or communitarianism, were introduced in the introductory paragraph of this entry as “methodological individualism.” Social constructionist and communitarian philosophies hold that individuals are constituted by (the different roles they occupy in) society. In those conceptualizations, popular with writers on both the political right and left, individuals do not exist apart, and thus cannot be abstracted, from society. Yet many psychologists (e.g., Sigmund Freud), sociologists (e.g., George Homans), and quite a few experimental and behavioral economists reaffirm the view that individuals can indeed be analyzed without a necessary reference to society. This is also expressed in Niklas Luhmann’s radical yet logically compelling thesis that individual/psychological systems form the *environment* of social systems, which goes to show that not all sociological theories support collectivism.

Different Manifestations of Individualism

In different social spheres or disciplinary contexts, individualism may manifest itself differently. For example, political individualism includes (a) a view of government as based on the individually given consent of individuals, (b) political representation as the representation of individual interests (not stakeholder group interests), and (c) the purpose of government solely as purveyor of individuals’ wants or interests and protector of individuals’ rights. This last aspect of political individualism shows a bias toward laissez-faire (as opposed to welfare) liberalism with minimal government, as prescribed by Thomas Jefferson. Individualism can also manifest as religious, epistemological, or methodological individualism—with different foci (in his 1973 book, Lukes presents further explanations and examples of these other forms of individualism). But the two manifestations that are most important to consider for the present purpose are economic individualism and ethical individualism.

Economic individualism is the belief in the economic liberty and private property of individuals and implies an opposition to economic regulation and welfare state policies. Hence, economic individualism is not only conceived as a description of economic reality but also, more important, a normative set of political *desiderata.* Many 20th-century Austrian and neoclassical economists (Ludwig von Mises, Friedrich Hayek, Milton Friedman) regarded the defense of "free civilization" as one of their central scholarly tasks because a market system with minimal state interference and maximum economic liberty is seen as both most economically efficient and morally desirable. For example, Hayek explains how this normative economic view would abolish economic planning, progressive taxation, and the exclusive control of education by the state or some other authority.

Ethical individualism regards morality as individual in nature. It follows from carrying the second element mentioned above, autonomy, to its logical conclusion. With the ideological decline of Christianity as the objectivist foundation of moral certainty, advocates of ethical individualism took center stage in moral philosophy. Nineteenth-century philosophers Soren Kierkegaard and Friedrich Nietzsche are exemplars of ethical individualism—as well as the French existentialists (such as Jean-Paul Sartre) in their emphasis on the importance of individual choice. Ethical individualism generally presumes that the individual is the source and creator of moral values and principles. This way, it bears great affinity to ethical subjectivism but still must not be confused with ethical egoism. Ethical egoism is, roughly, the doctrine that one's object of morality should be oneself. One of the most famous advocates of this doctrine is Ayn Rand. An individualistic worldview is necessary for ethical egoism, but ethical egoism is not a necessary outcome of individualism.

Historical, Geographic, and Semantic Roots

The discussion so far has hinted at the fact that there are about as many definitions of individualism as there are writers about it. This is unsurprising because *individualism* has its semantic roots in so many different countries and contexts.

French conservatives and reactionaries coined the term *individualisme* in pejorative reference to the ideas of the French Revolution and the Enlightenment. They saw those ideological and historical developments as serious threats to social order and stability. In particular, Catholic restorationists in France in the 1800s, such as Joseph de Maistre, were adamant that too much freedom and too little religion would destabilize post-Enlightenment Europe. They advocated the imposition of a hierarchically organized, harmonious social order as a means of constraining individualism. Alexis de Tocqueville used the term with fewer pejorative connotations than did most of his French contemporaries, but he was still quite suspicious of what he assumed was one important consequence of individualism: the withdrawal of individuals from public life into a private sphere and the consequent weakening of social bonds. Only active citizenship (which Tocqueville observed in America) could, in his view, prevent democracy's own destruction, which individualism may enable through individuals' retreat into their private lives.

In Germany, the term preserved some of its pejorative connotation when it was used by German socialists and nationalists (such as Friedrich List) as a rallying cry (and indeed straw man), which had to be overcome with a less abstract, more holistic economic order. However, since the Romantic era, the German term of individuality has strong positive overtones with its celebration of genius and originality. However, as it was soon transformed into the previously mentioned type of "false individualism," it ominously foreshadowed 20th-century German history: the *Volk* as the organic basis of individualistic self-expression, invested with the power and almost mystical quality to unify heterogeneous individualities, especially when governed by an individual whose genius was seen as self-evident.

Swiss historian Jacob Burckhardt integrated the French and German meanings of the word in his influential analysis of the Italian Renaissance. Individualism, in his view, not only combined the notions of self-direction, escape from authority, and withdrawal into the private sphere but also engendered a simultaneous emphasis on self-development and cultural refinement. In this sense, the Renaissance ideal of a human being can be regarded as the exemplar of the four elements of individualism as described above.

American conceptions of individualism generally embrace capitalism and liberal democracy. Some U.S. authors, such as Emerson, attributed to individualism a mystical quality as a tool for self-improvement. American Social Darwinists (in particular William G. Sumner), following Herbert Spencer, were less idealistic because they emphasized the necessity of individualistic competition as a mechanism that facilitates the weeding out of the weak. The evolutionary logic of survival of the fittest rather than individual self-improvement was seen as the guarantor of societal progress. Importantly, in the United States, individualism is not synonymous with individuality, originality, or creativity (as it is in Germany, for example). Several perceptive writers (such as Friedrich Hayek and Richard Rapson) have gathered some evidence that, paradoxically, American individualism seems to require individual conformity and voluntary submission to tradition to function well.

Implications for Business and Society

Arguably, the most important implication of individualism is the creation and reinforcement of individual rights. Without individualism, considerations of positive aggregate outcomes could outweigh and overrule individual rights. In contrast, individualism reaffirms the necessity of respect for the individual, who must not be made subservient to some *Gemeinschaft,* or community.

Similarly, individualism forced many scholars in business and society to abandon amorphous concepts such as "society at large" or "public interest." Individualism suggests that interests, needs, and moral motivations can only be inferred at individual levels of analysis. Such epistemological doubts about the attribution of morality to collectives are rooted in an individualist philosophy. Some business and society scholars (e.g., Manuel Velasquez) are even skeptical of the attribution of moral responsibility to organizations.

Individualistic values may also have important implications for organizational behavior. Managers in more individualistic cultures typically lay greater emphasis on, for example, employee independence, competition, or individual rewards than do managers in collectivist cultures. Consistent with the second principle of individualism, they may emphasize autonomous decision making rather than collaboration. Some organizational researchers believe that, of all the cultural and ideological influences, the individualism-collectivism dimension may have the greatest impact on management practice.

Critiques

Individualism has been a key element of Western civilization and progress, but it has recently come under fire from many sides. First, many on the political left believe that markets cannot be left to their own devices. They do not have confidence in the invisible hand as the generator of optimal outcomes. Instead, they may propose a starting point of either "false individualism" or explicit collectivism in postulating the necessity of a broader, visible steering mechanism that constantly interferes with markets. As was pointed out before, false individualism usually lays much greater emphasis on reason and deliberate design as the guide of human action than does true individualism. According to such rationalistic views typically embraced by the political left, spontaneous order is either impossible or ultimately doomed because it degenerates into chaos or exploitation. Without a steering mechanism (e.g., the setting of a minimum wage), the free market would not produce optimal outcomes that are actually consistent with human dignity.

On the other hand, many conservatives embrace a collectivist tradition more explicitly than does the left and doubt that moral decision making can be left to the autonomous individual. In this sense, some people generally considered to be right wing are opposed to the liberal connotations of individualism. Conservatism often presumes an ethical absolutism to which individuals *must* (be made to) subscribe. Unlike many doctrines of socialism with typically totalitarian outcomes, which, according to Hayek, can have individualistic roots, the starting *and* end points of particular types of conservatism are explicitly collectivist and can have coercive overtones.

A more recent intellectual movement, communitarianism, shares quite a few features with the right-wing attack on individualism, although it presents itself in the guise of a middle-ground, moderate philosophy. According to communitarians, the common good prescribes or determines what is right. Thus, this kind of collectivism starts with the teaching of shared values because, according to communitarianism, civic virtue is impossible without them. It can be implemented either at subsocietal levels (e.g., church, family, neighborhoods) or higher levels of government. Many communitarians prefer their own collectivist "deep community" to the "shallow community" of individualism. They do not seem bothered by evidence presented by feminists such as Marilyn Friedman or liberals such as Jeffrey Reiman that many types of community may be oppressive to women (such as the family or church). In some ways, communitarianism can be interpreted as a rebellion against voluntary decision making and individualistic tolerance, in other words, against not being able to force one's values on others.

Another modern doctrine that harkens back to the past and firmly opposes individualism is the sort of tribalism that has spawned modern terrorism. Many terrorists proclaim to act for the good of some (i.e., their own) collective that overrides concerns for individual lives. Individuals, whether they are victims or suicidal perpetrators of this tribalism (which is manifested as a collectivist egotism), can be sacrificed for some higher cause without concern for their rights or indeed survival.

The discussion has alluded to the fact that many critiques of individualism are flawed. However, they all raise one troubling point: Does individualism contain the seeds of its own destruction? The social nature of humanity and the social search for meaning in our lives may limit the usefulness of individualism as a guide for human action. As history has shown, the urge to find larger meaning ("beyond ourselves") may give rise to the emergence of frequently dangerous collectivist doctrines. However, in this context, it is important to keep in mind that individualism is not opposed to social connectedness and community (see McCann's book *Individualism and the Social Order*); in fact, many advocates of individualism (such as Hayek) affirmed both individualism and the social nature of human beings.

—*Marc Orlitzky*

See also Absolutism, Ethical; Communism; Communitarianism; Darwinism and Ethics; Existentialism; Freedom and Liberty; Free Market; Friedman, Milton; Hayek, Friedrich A.; Invisible Hand; Liberalism; Libertarianism; Locke, John; MacIntyre, Alasdair; Market Socialism; Marxism; Mill, John Stuart; Nozick, Robert; Rawls, John; Rights, Theories of; Socialism; Spontaneous Order; Utilitarianism

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Individual Retirement Accounts (IRAs)

An Individual Retirement Account (IRA) is a personal savings account which allows taxpayers in the United States to set aside money for retirement, while offering tax advantages. The umbrella term for the concept is legally Individual Retirement Arrangement. The IRA can either be an annuity (typically deferred) or a trust set up that meets specific criteria the Internal

Revenue Service (IRS) has defined. This trust and funding by financial instruments makes it an account, and thus the term *Individual Retirement Account* is the most common name by which IRAs are known.

Traditional IRAs and Roth IRAs

Congress established IRAs in 1974 to encourage people to save toward their retirement. Contributions may be made to traditional IRAs if the taxpayers received taxable compensation during the year and were not age 70.5 by the end of the year. Individuals who are age 50 by the end of the tax year for which the contributions are being made may make an additional catch-up contribution. Taxable compensation includes wages, salaries, commissions, tips, bonuses, or net income from self-employment; it does not include earnings and profits from property, such as rental income, interest, and dividend income, or any amount received as pension or annuity income, or as deferred compensation. Married couples are allowed to establish a special "spousal IRA" when only one spouse has earned income.

A traditional IRA is allowed whether or not the taxpayer is covered by any other retirement plan. However, if the taxpayer or spouse is covered by an employer retirement plan, contributions may not be fully deductible. Determining whether contributions made to a traditional IRA are fully or partially deductible also depends on the income and filing status of the taxpayers and whether or not they receive social security benefits. Generally, amounts in a traditional IRA (including earnings and gains) are not taxed until distributed. After taxpayers turn 70½, mandatory minimum distributions based on life expectancy tables are required, which will be taxed as ordinary income, other than any nondeductible contribution portion.

Penalties apply to withdrawals made before reaching the age of 59½, although exceptions can be made for withdrawals for medical expenses, qualified education expenses, and first-time home buyer expenses. Assets (money or property) can be transferred, tax-free, from other retirement programs (including traditional IRAs) to a traditional IRA. These transfers can be from one trustee to another, through rollovers, or through transfers incident to a divorce. Any excess contributions made to IRAs are subject to an excise tax.

A traditional IRA can be an individual retirement account or an annuity. It can be part of either a simplified employee pension (SEP) or an employer or employee association trust account. The trustee or custodian for a traditional account must be a bank or other entity approved by the IRS to act as a trustee or custodian. Money in these accounts cannot be used to purchase life insurance policies, and assets in the account cannot be combined with other property, except in a common trust fund or common investment fund.

As an alternative, an individual retirement annuity may be set up by purchasing an annuity contract or an endowment contract from a life insurance company. The entire interest in the contract must be nonforfeitable and it must provide that no portion can be transferred to any person other than the issuer. There must be flexible premiums so that if compensation changes, payments can also change and contributions are limited. Distributions must begin after age 70½.

The Taxpayer Relief Act of 1997 established Roth IRAs, championed in Congress by Senator William Roth of Delaware. There are no age limits on when Roth IRAs can be set up and contributions made. Unlike contributions to a traditional IRA, no part of a contribution to a Roth IRA is deductible. The benefit of a Roth IRA is that income earned by the Roth IRA is not taxable to the owner (or the owner's beneficiary) when withdrawn if certain requirements are met. The maximum amount that can be contributed to a Roth IRA is the same as the maximum amount that can be contributed to a traditional IRA. However, if an individual makes a contribution to a traditional IRA, the amount that can be contributed to a Roth for any tax year is reduced by that amount contributed to the traditional IRA. Distributions are never mandatory, regardless of age, and any distributions taken from a Roth IRA are not taxed as long as certain criteria are met.

Amounts can be converted from a traditional IRA into a Roth IRA if, for the tax year of the withdrawal from the traditional IRA, the modified adjusted gross income for Roth IRA purposes does not exceed a specified amount. All or part of the assets from a traditional IRA can be withdrawn and reinvested in a Roth IRA, which are then called conversion contributions. Income distributions from a traditional IRA that would have been included in income had they not been converted into a Roth IRA must be included in gross income at the time of conversion.

Other Types of IRAs

An SEP is a written arrangement that allows small businesses that do not have any other type of retirement plan to make deductible contributions to a traditional IRA (an SEP-IRA). Generally, distributions from SEP-IRAs are subject to the withdrawal and tax rules that apply to traditional IRAs. An SEP-IRA is based only on employer contributions, and vesting is immediate. Any employee who is at least 21 years old, has been employed for 3 of the 5 preceding years, and has earned a minimum compensation of $450 in the current year is eligible to participate. There are three formulas that may be used to allocate contributions to an SEP-IRA: a flat dollar amount, a specified percentage of eligible compensation, or a Social Security integration formula. SEP-IRAs are easy to set up and maintain compared with other retirement plans, and no annual tax returns are required. The employer contribution is optional, which eliminates the problem of required contributions in years when cash flow is a problem.

A Savings Incentive Match Plan for Employees (SIMPLE) IRA is a tax-favored retirement plan that certain small employers (including self-employed individuals) can set up for the benefit of their employees. Employees may choose to reduce their compensation by a certain percentage each pay period and have their employers contribute the salary reductions to a SIMPLE IRA on their behalf, up to a specified maximum amount each year. The employer is then required to match up to 3% of employee pay or make a 2% nonelective contribution. SIMPLE IRAs require little documentation and no annual tax filings. Employer and employee contributions are both vested immediately. Although it is possible to reduce the contribution percentage in designated years, these may not be reduced to zero.

—Paula J. Thielen

See also Employee Retirement Income Security Act of 1974 (ERISA); Pensions

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INDUSTRIAL POLICY

Industrial policy is a form of government influence on business sectors and firms within an economy. Industrial policy has been both distinguished from and closely associated with other forms of government planning and intervention in the marketplace, such as a nation's competition policy, its trade policy, or its macroeconomic policy. Definitions of industrial policy vary. Many traditional definitions have been fairly narrow ones, such as the selective and strategic targeting of certain business sectors and/or firms over others to receive greater government support to improve or take advantage of their productivity and competitiveness. Definitions of industrial policy have also shifted somewhat in recent decades, and industrial policy often has been more broadly described as government interventions to support multiple or particular economic goals, such as increasing exports or R&D spending, that assist a nation's industries and firms. The paragraphs that follow the next one assume a fairly narrow definition of industrial policy, and then later paragraphs introduce additional or broader viewpoints that have been suggested.

Debate concerning an appropriate role and strategies for government intervention to promote more national economic growth can be traced back centuries. Certain government interventions to assist business activities have generally been supported. Examples include spending on education and the physical and social infrastructure in a country, as well as programs offering low-cost loans and incentives for small businesses. Nonetheless, arguments for forms of industry policy, even subsidies or protection for promising, infant industries from threatening competitive markets, have often been raised. Strong critics of industrial policy, particularly some neoclassical economists, question the effectiveness of government interventions, versus the role of free markets and more laissez-faire attitudes, to determine business sector "winners and losers." Other critics of industrial policy stress that such research, planning, and interventions can have positive impacts on targeted business sectors, but they question its effectiveness in terms of the overall costs versus benefits for the nation's economy.

Countries differ significantly in the extent to which industrial policy is accepted as a legitimate government role and applied. France and Japan, for example, have had mixed results with more formal and elaborate types of industrial policy, while the United States has applied industry policy in more of an inconsistent and ad hoc manner. For example, political pressures following unusual or unexpected events in the United States led to loan guarantees for Lockheed and Chrysler in the 1970s, the closing of savings and loan companies after the crisis in that business sector in 1989, and cash assistance and loan guarantees for the airline industry after attacks on the World Trade Center and Washington, D.C., in 2001.

Issues involving industrial policy have been investigated using tools from econometrics as well as from academic specialties such as sustainable development, technological change, political science, international relations, and others. Early studies of government interventions targeting selected industries or sectors, particularly within command economies employing central planning, did not generally support the effectiveness of these forms of industry policy. The rapid economic development and success of certain East Asian countries in the 1970s and 1980s fueled studies of their individual patterns of investment in selective industries, along with their macroeconomic policies and various government/business/society relationships. It was thought that much more sophisticated planning and careful execution of industrial policy might prove beneficial for both more advanced and emerging national economies.

Financial and other problems confronting some of these East Asian economies in the 1990s and intensive research investigating selective sector investments in these individual nations tempered initial optimism that these strategies might also be applied effectively elsewhere. A diversity of policies and their varying consequences led to complicated analyses and simple conclusions. In addition, plans for selective sector investments were not always implemented consistently during planning of time horizons in certain countries. Yet when compared with factors such as sound macroeconomic policies, level of investment in human capital, and other factors often associated with productivity, these selective sector investments appeared as a less important contributor. In some cases, these selective sector investments also had adverse effects on financial markets, in addition to consequences for disfavored business sectors. This and other forms of industry policy demanded competencies and integrity from government officials and civil servants that were not always present, particularly in many less developed countries. Political forces and constituencies favoring certain business sectors were created that could not always be overridden when economic conditions changed. New and more promising sector opportunities or innovations were also difficult for government officials outside these industries to identify and evaluate appropriately.

There has been less criticism for selective sector support from government in the case of less developed countries undergoing early stages of industrialization compared with such sector selection practices in more developed countries. Additional and complicating factors for these more developed economies, such as European Union (EU) versus member nation priorities or World Trade Organization (WTO) concerns about subsidies and protections, have resulted in calls for other government strategies to improve national competitiveness and productivity. Among these broader suggestions for more effective government interventions have been reforms of the financial sector so that developmental funds flow appropriately to promising industries; use of incentives, instead of directives, from government that are contingent on evidence of productivity and export success; efforts to promote continuing diversification and upgrading of exports; and support for any industry clusters or new learning networks from which spin-off and spillover potentials might occur. Unlike typical networks or voluntary partnerships of business companies, networks involving business and other institutions are being encouraged and facilitated in certain countries. The main purpose for such networks is the creation of learning opportunities through the voluntary exchange of information and dialogue about experiences and factors contributing to productivity and performance improvement.

Research on national productivity in the context of global competitiveness and the role of government in fostering these goals continues, even if many theorists and researchers view traditional notions of industrial policy as discredited or outdated. If industrial policy is an evolving paradigm, it now seems to encompass multiple government strategies and activities in light of emerging global concerns and complications such as terrorism or pandemic flu protection. Selective investment in certain business sectors is just one of many possibilities, and it and broader strategies are influenced by many contingent factors or societal needs.

—Stephen L. Payne

See also Barriers to Entry and Exit; Competition; Development Economics; Free Market; Laissez-Faire; Market Failure; Subsidies; Unfair Competition

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Industrial Revolution

The *Industrial Revolution* refers to a period of economic, technological, and social transformation that occurred primarily in Great Britain beginning in the 1760s and ending approximately 80 years later. The major innovations associated with this revolution include steam powered manufacturing, cheaper and higher quality iron and steel, increased use of chemicals in industry, the invention and diffusion of railroads, and the appearance of the first large, mechanized, high-output factories for producing cotton textiles and some other consumer goods. Some historians argue that this was only the first of two such revolutions, and a second Industrial Revolution took place in the United States and, to a lesser extent, Germany during the last decades of the 19th century. This second revolution was characterized by the emergence of giant industrial corporations that exploited petroleum and electric power in both their manufacturing and their products.

The impact of the initial British revolution was felt most dramatically in a handful of industries, leading some to argue that the term *revolution* exaggerates overall trends. Others defend the term by pointing out that industries most thoroughly transformed had an overwhelmingly disproportionate impact on the workings of the British economy and on patterns of world trade. The cotton industry, for example, had gradually climbed to 6% of British exports in 1784, but 50 years later, cotton textiles accounted for 48.6% of a much higher total of exports. Even traditional industries were transformed during this era, if somewhat less dramatically. Josiah Wedgewood, the grandfather of Charles Darwin, made himself the most successful pottery producer of his time by applying steam power, chemistry, factory organization, and rail transportation to his ancient craft. As a result of such innovations spreading throughout the economy, the volume of industrial output in Britain, which grew about 1% a year between 1700 and 1780, increased by 3% to 4% annually over the following 80 years, an extended explosion of industrial output unprecedented in world history up to that time.

Among the many factors that help explain the timing and location of the Industrial Revolution, two in particular stand out. The first is Britain's preindustrial coal industry, which supplied a major source of heating fuel before 1760. This coal industry did not only provide power for industrial machinery and an essential input in the new metallurgy; mining coal stimulated demand for the first steam engines to run mine-pumps and the first railroads to transport the heavy mineral to ports. Perhaps the more important factor, however, was the heavily commercial nature of British society at the eve of the revolution. For more than two centuries, first English and then Scottish agriculture had been undergoing their own transformations. Dramatic changes in the uses and ownership of agricultural land, loosely referred to by historians as "the enclosure movement," led to increased commercial husbandry, higher agricultural productivity, and the destruction of peasant self-sufficiency. These in turn stimulated a number of interdependent and reinforcing developments: greater use of wage labor, growing consumer markets, innovations in farming technology, and a willingness to invest in roads, canals, and shipping to further strengthen this market system. As a result, when the powerful woolen goods lobby blocked the importation of Indian cotton goods, the textile center of Manchester already possessed the necessary labor, technology, energy, banking, and transportation infrastructure necessary to support the world's first consumer industry based on mechanization and mass production.

Historians agree that the Industrial Revolution eventually raised living standards, and its technology changed daily life significantly in other ways as well, such as making practical the production of mass circulation newspapers. The revolution, however, produced losers as well as winners. Precious metals coinage seized from the Indian subcontinent helped finance the revolution, and slave labor in the American South fed the cotton mills of Manchester. Closer to home, the new processes spawned new externalities in the form of industrial pollution, unhealthy work environments, the obsolescence of many once respected craft skills, and pressures toward long workdays to maximize the value of the expensive new equipment.

These new, frightening social problems generated a variety of responses. The Luddites, a group of skilled craftsmen who felt threatened by these innovations, sabotaged industrial machinery, risking execution in the process. Workers dissatisfied with their pay and working conditions organized themselves in the workplace and in the political arena, leading to industrial unionism and eventually the world's first labor-based political party.

Politicians, thinkers, and artists joined the discussions and even the agitations. Charles Dickens and Elizabeth Gaskell wrote about the terrible working conditions in factories. Revolutionaries, including Karl Marx and Friedrich Engels (who managed his family's Manchester factory), argued that the negative impact of industrialization was inevitable under a system of market competition based on the exploitation of wage labor. John Stuart Mill, an employee of the East India Company, helped found modern liberalism by acknowledging the benefits of markets and technology while invoking the utilitarian tradition to argue for political reforms aimed at ameliorating their negative consequences. More practical-minded reformers such as Robert Owen attempted to practice manufacturing without the usual social costs. Still other critics and reformers took a more "conservative" stance, arguing that unbridled industrialization and unchecked greed betrayed traditional values and threatened the social fabric of the nation. Among more conservative figures, Ashley Cooper, Earl of Shaftesbury, stands out for leading the campaign to regulate the factory workday.

As the Industrial Revolution spread around the world, so did many of these associated social problems and the responses to them. The "Lowell Girls" of the first factory town in the United States struck in 1836 against wage cuts and unhealthy working conditions. In the mid-19th century, Bishop Leo Ketteler of Mainz initiated a Catholic approach to the labor question that was later enshrined in the papal encyclical *Rerum Novarum* of 1893. Today, the antisweatshop movement, composed of unions, religious groups, political figures, and college students, continues the tradition of trying to assure that industrial growth occurs responsibly and to the general benefit of all the groups that it affects.

—Richard Marens

See also Capitalism; Child Labor; Colonialism; Consumerism; Development Economics; Mill, John Stuart

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Inflation

Inflation is a continued and sustained rise in the general price level or, equivalently, a continuous decrease in the value of money. Thus, it is not an increase in just one price or a few prices but in a large number of prices at once; not a one-time increase, but an increase that spreads out over time; and not a temporary, reversible increase, such as the increase in the prices of certain consumer goods around Christmas, but a sustained increase. Usually, inflation is measured by the change in some price index, based on a broad basket of goods and services, such as the gross domestic product deflator or the consumer price index.

What Causes Inflation?

Many different factors may cause the price of a good to increase on a one-time basis: an increase in demand for that good, a reduction in supply (a bad harvest, for example, in the case of some farm produce), an increase in production costs (wages, raw materials, energy), an increase in taxes on that product, and so forth. But an increase that affects most, or nearly all, prices can only be caused by something that affects the entire economy, such as a general increase in wages (above the increase in productivity) or in the price of oil and other imported raw materials (due, for example, to a depreciation of the currency) or in taxes on production or sales. Nevertheless, events such as these may explain one-time price increases, but not continued and sustained increases in the prices of large numbers of goods over an extended period.

There is a broad consensus among economists that inflation can only be caused by an excessive increase in the supply of money in a country over a period and that a continued, sustained, and excessive increase in the money supply may turn a one-time increase in a few prices into full-blown inflation. That is why inflation is often said to be a monetary phenomenon: too much money chasing too few goods. If a country's financial system creates more money—that is, more purchasing power—than the value of the goods available, there will be a "bidding war" among potential buyers. That leads to price increases, which are passed on from one market to another and persist over time.

Therefore, to understand inflation, we need to understand how the money is created and controlled, in other words, how monetary policy is designed and implemented. But if it is public knowledge that excessive growth of the money supply leads to inflation, why do governments and central banks promote it or allow it to happen? There are many reasons why they might do that: to stimulate demand and production, to avoid a recession due to cost increases, or as a consequence of mistakes or accidents. Whatever their motives, the monetary authorities choose a short-term advantage—often a political advantage, such as winning an election—at the cost of a long-term disadvantage—higher inflation.

Nevertheless, the most common cause of excessive growth in the money supply, leading to high inflation, tends to be the financing of the budget deficit: When a government spends above its means, it is tempted to ask the central bank for a loan, and that loan will give rise to an increase in the amount of money in the economy. In many countries, the ultimate cause of what is often chronic high inflation is the government's inability to finance public spending out of its regular revenues, prompting it to resort to inflationary means of financing the deficit (of course, this will not happen if the deficit is not financed by the central bank).

Consequently, wherever inflation is high and persistent, it tends not to be an isolated "disorder" but part of a much broader "illness" whose clinical picture usually includes inappropriate fiscal policies, incompetent governments, a central bank hostage to government pressure or interests, lack of monetary policy tools, and so forth. In the long run, the price increases may become self-perpetuating: If money is constantly losing value, consumers will try to spend it as quickly as possible, which will increase the pressure on prices to the point where hyperinflation sets in—with prices rising at an annual rate of more than 1,000%. Hyperinflation occurred in Germany after World War I, when the rate of growth of prices reached 3.25 million percent in a single month (August 1923), and more recently in several Latin American countries (Bolivia, where the annual inflation rate reached a peak of 23,447% in August 1985, Argentina, where the highest annual rate was 20,266% in March 1990, etc.).

Economic and Social Effects of Inflation

Inflation is more than just an economic problem; it is also a social, political, and ethical problem and has far-reaching consequences. As a rule, inflation has its most severe effects when it is unpredictable, when the economic agents are unable to protect themselves against it (e.g., because regulations limit price and income flexibility), and when it varies considerably over time.

Under a fixed exchange rate (a rate the government sets and maintains as the official exchange rate, usually in terms of a major world currency, such as the U.S. dollar), a country that has higher inflation than other countries will become less competitive. That may result in lower output growth, higher unemployment, or even a recession. Moreover, to maintain the fixed exchange rate the central bank must buy its own currency and sell the foreign currency to which it is pegged, and this operation is limited by the amount of foreign currency reserves owned by the central bank. When this limit is reached, the national currency will suffer a sudden, large devaluation that will accelerate inflation, disrupt production, and cause severe adjustment costs to the country and, probably, a recession. And if the financial markets fear this outcome, an acceleration of inflation may discourage foreign investment and even cause a capital flight, hindering or even stopping sustainable economic development.

Inflation gives rise to economic inefficiencies that may reduce the country's capacity for growth. For example, if inflation is high and variable, it may be difficult for companies to distinguish between changes in relative prices (i.e., the prices of some products compared with others) and changes in the general price level, and this can result in mistaken decisions about investment, technology, and markets. Also, as uncertainty increases, the maturity of credit is shortened; this makes it very difficult to finance companies' investments in the long term.

Inflation is a tax on money (keeping a dollar bill for 1 year with 10% inflation is equivalent to losing 10 cents of purchasing power). Accordingly, households and companies try to reduce their cash holdings, which leads to financial stress. In conditions of high and variable inflation, cash management becomes more important than production efficiency, and speculation may be more profitable than a job well done.

Also, when taxes are progressive (i.e., the tax is larger as a percentage of income for those with larger incomes), as income tax is in many countries, inflation accentuates the tax progression (unless appropriate corrective measures are taken) by pushing the tax base up into higher tax brackets, without any corresponding increase in real income. In a sense, citizens' wealth is expropriated.

High inflation brings about a potentially unjust redistribution of income. Inflation tends to hurt those on a fixed income, such as a state pension (unless subject to periodic review) or, in some cases, a rent or a wage. It also leads to a redistribution of wealth. Those who hold cash (inflation is a decline in the value of money) or fixed income securities, for example, stand to lose. Thus, particularly if inflation is unexpected, creditors tend to lose, while debtors win. After an episode of high inflation, savers may find that their wealth has evaporated, unless it was invested in financial instruments whose value kept pace with inflation or which generated sufficient income to offset the loss of purchasing power.

In society at large, high and variable inflation will generate ill feeling and conflict, if only because employees will see how prices increase day by day while their wages increase only once a year. Whenever inflation is high, people think that "someone" is to blame and tend to pin the blame on some minority or on "speculators" or "big business," nurturing social rejection, violence, and so forth. Moreover, in an environment of high inflation, important ethical and social values, such as honesty, industry, and saving, deteriorate: It "doesn't pay" to be honest because you end up forfeiting your assets, while others who resort to more morally questionable methods make significant gains.

Also, inflation tends to spread. A rise in one price leads to a rise in another (probably because of the same underlying cause, or as a defensive reaction); prices push up wages, and wages push up prices, in a continuing spiral. So people who expect inflation increase prices, because their defense mechanism is precisely to try to increase whatever prices they control and, in the case of employees, their wages. For all these reasons, a country is unlikely to be able to maintain a stable, low rate of inflation unless it explicitly makes that an economic policy objective.

How Can Inflation Be Reduced?

If it is true that inflation is a monetary phenomenon, reducing a country's inflation rate will be a task for monetary policy. Basically, the monetary authority—the central bank or the government—will have to curb the growth of the money supply by draining liquidity from the financial system and raising interest rates. And that will almost always be a traumatic process. Because of the credit squeeze, households will curtail their demand, and many will find themselves in financial difficulties. Companies will start to lose money, halt their investments, cut back their spending, and lay off workers. And the country is likely to see a slowdown in the rate of growth, or even a recession.

Many countries that have tried to reduce inflation have found that implementing a restrictive monetary policy is not enough. The policy must also be credible, which is to say that the authorities must have a firm political will to reduce inflation, that is, to bear the economic, political, and social costs of preventing prices from rising, particularly in a recession. In practice, an anti-inflationary policy may have high social and human costs, and governments must bear them in mind and try to mitigate them. Ultimately, however, they will have no choice but to take whatever steps are necessary, just as a doctor will carry out emergency surgery to save a patient, however painful it may be.

Also, a monetary policy will only be credible if it is compatible with other macroeconomic policies, above all exchange rate policy (the exchange rate, if it is not fixed, must be compatible with the inflation target) and fiscal policy. An effort to bring inflation under control will not be credible if the government does not undertake to reduce its budget deficit and stop financing it with central bank borrowing. Finally, the battle against inflation will be easier if institutions and policies are in place to facilitate price adjustment: labor market flexibility, competitive markets, abolition of price and wage controls (so-called incomes policy), and so on.

Once the inflation rate has been brought down, monetary policy will have to be aimed at keeping it down. The rate of growth of the money supply must be sufficient to finance the potential growth of the economy, in real terms, plus a strictly limited inflation rate. And, once again, that will require a credible deficit-containing fiscal policy, a sustainable exchange rate (frequent devaluations fuel inflationary expectations, which drive up the costs of imported products, and then inflation), moderate cost growth (wage pressure must not exceed the moderate increase in prices plus reasonable productivity growth), . . . and a fair dose of good luck.

All of this brings us back to the attitude a socially responsible government should take toward inflation. The most important thing is not to allow unduly expansionary policies, which merely generate inflation. Excessive, unexpected money supply growth has a stimulating effect on the real economy, just as a stimulant does on a normal person; yet the effect soon wears off, while the dose needed to achieve the same effect keeps on increasing. Usually, getting inflation under control is an arduous process that may have high economic, social, and human costs. For that reason, it is best to avoid inflationary policies and tackle rising inflation as quickly as possible to put in place moderate monetary policies that keep inflation low and stable—because macroeconomic stability is a necessary (but not a sufficient) condition for the prosperity of nations and the well-being of their citizens.

—Antonio Argandoña

See also Justice, Theories of; Just Price; Labor Unions; Monetary Policy; Regressive Tax; Wage-and-Price Controls

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Information Costs

The term *information* is generally assumed to mean a message. It usually takes an audible or visible form and involves a sender and receiver. Information is meant to change the way the receiver perceives something, to have an impact on judgment and behavior. The term *cost* has traditionally been viewed as the value of inputs that have been used up to produce something. Since the inputs have been used up, they are not available for use anymore. Putting the terms *information* and *cost* together adds an interesting twist because the inputs that comprise a message may not be used up and may well be available for other uses. The issue becomes how much someone is willing to pay for information, in other words, what the value of information is. From the catchphrase "Information is power," we can imply that information is highly valued.

The cost, or value, of information is difficult to determine because information is intangible, immaterial, highly fungible, and nonexclusive. Information can be replicated at little or no cost. Its use is infinite because it doesn't wear out or deteriorate. Information's value may increase as it is exchanged or interchanged with other information. The production of information goods involves high fixed costs and low marginal costs, as well as high sunk costs involved in creating information. Fixed costs are related to assets or expenses whose total costs do not change in proportion to the amount of information that is produced, such as rent and utility bills. Marginal costs change as the quantity produced changes, and in the case of information this would include the cost of the media on which the information is distributed, for example, a digital video disk. Sunk costs are those that have already been incurred and that cannot be recovered to any significant degree, for example, the costs of obtaining the information. Since information is relatively inexpensive to replicate, it has perfectly increasing returns. Once the initial investment is made, information can be reused at no additional cost.

These properties cause several dichotomies. The first is that users want information to be free, while its producers may want it to be expensive. The rationale that information should be free is based on the fact that information is cheap to distribute, copy, and recombine. This is juxtaposed with the concept that information may be expensive because of its immeasurable value to the recipient.

A second dichotomy is the value of information related to time and distance. Buyers of information may be willing to pay a premium to be among the first who possess it and act on it. Information generally costs more the closer the purchaser is to its collection. In addition, the quality of information may degrade over time and over distance, since much of its use is contextual, or as it becomes obsolete or untrue with time. However, it is also possible that the value of information increases over time because it is compounded.

A third dichotomy is information's scarceness and familiarity. Items typically become more valuable when they are scarce. People may be willing to pay for information that is not generally known. While the exclusive possession of certain information may make it more useful, some researchers have found that its intangible value increases as it becomes shared. It is recognized that the availability of information and the free flow of data are the cornerstones of a democratic society and market economy. Sharing information resources means that organizations can make their resources available for other projects and may enable quick responses in emergencies; for example, information sharing among several governments helped contain the SARS outbreak to a limited geographical area.

There are three important considerations in the cost of information. These are reciprocity, reputation, and altruism. Reciprocity is a mutual or cooperative interchange of favors or privileges. Often, the holders of information will provide it if they expect others will provide them with information when they are in need. Reputation is the general estimation in which a person or organization is held by the public. Information is more valued if the reputation of the provider is good. Altruism is the practice of placing others before oneself and exhibiting unselfish concern for the welfare of others. Sometimes, providers of information make it available for the good of society.

The cost of information may be affected by the market structure. A monopoly on information occurs when one group has exclusive control over the means of producing or selling it. Monopolies may cause costs to rise. The most common method of maintaining monopoly control of an information resource is the enforcement of copyrights and intellectual property laws. Monopolies also arise in the information market when the information is difficult to copy, because of its medium, or too complex for someone else to assemble comprehensively. Likewise, the value of information may decrease the more it is replicated. Trade barriers, such as censorship activities of governments, may also affect the cost of information.

Ethical decisions regarding the cost of information affect the ability to access information and to pay for it (e.g., the digital divide illustrates the gaps in the ability to access information and may result in disparities among cultures, classes, and races), the availability of information (e.g., censorship, as seen in China's policy of limiting its citizens' access to information about the 1989 uprising at Tiananmen Square), and sharing of information (e.g., patents and copyrights may limit how information is copied and used).

—Donna M. Schaeffer

See also Altruism; Reciprocity; Reputation Management

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Informed Consent

Informed consent is a legal and ethical condition of voluntary agreement based on adequate knowledge and understanding of relevant facts, implications, and consequences when participating in research or undergoing a diagnostic, therapeutic, or preventive measure. Subjects must be in possession of all their faculties without impairment of judgment at the time of consenting. Furthermore, subjects may not waive or appear to waive any of their legal rights or release or appear to release the investigator, the sponsor, the institution, or agents thereof from liability for negligence.

Although the legal concept of informed consent is most commonly associated with medical procedures and research studies, it also has ethical relevance in the broader context of business, particularly in protecting employees from potential privacy violations by employers. Certain legal guidelines have been enacted to protect employee rights to informed consent, such as the Polygraph Protection Act of 1988, which not only prohibits most employers from using a polygraph (lie detector) as preemployment testing but also requires exempted employers to obtain the informed consent of their candidates prior to testing. The concept of informed consent in this sense has as much to do with business ethics as business law since employers in the United States continue to enjoy a great deal of latitude in choosing when, where, and how to limit the privacy of their potential and present employees.

Informed consent implies deliberation and free choice. Subjects must be allowed to deliberate on the basis of sufficient information of what exactly they are consenting to and how it may affect them in the future. And, of course, such information needs to be in language the subject can understand, minimizing legalistic or other specialized vocabulary. Sometimes employers assume that merely informing their workers of a pending privacy intrusion such as monitoring employee Internet use, installing hidden cameras, drug tests, personality tests, or criminal and health background checks is to comply with this rule. After all, the employee has been informed and is usually free to quit at any time. But this common assumption overlooks the pressures, expressed or implied, exerted on employees to conform to organizational policy. Not only is there social pressure to conform; often employees cannot expect to obtain gainful employment elsewhere at short notice. When these factors are in place, which is often the case, the subject is informed of the procedure, but genuine consent is difficult to ascertain. This is why polygraph tests have been forbidden as a condition of hire for most jobs that do not require a high degree of security clearance. The legal claim here is that subjects should never be coerced into sacrificing their right to privacy unless there is a greater interest in preserving the public from undue harm.

Thus, contractarians tend to interpret informed consent as placing equal emphasis on consenting as being informed. They point out that if employees cannot opt out of the procedure, full consent has not been obtained. Employers will then reply that none of their common screening procedures will be possible if most candidates opt out. This is the point at which ethical and legal dilemmas occur. Most ethicists maintain that employers do have the right to invade their employees' privacy without their full consent so long as a strong case is made for the necessity of the procedure, namely, to protect the public and/or business from a clear and present danger sufficient to override the right to privacy. Still, libertarians claim that all private employers should have the right to infringe on their employees' privacy within the confines of the law, so long as employees are informed of the infringement. Coercion would thus be acceptable in a capitalist system in which employees are free to leave jobs at will.

Polygraph Tests

Courts have upheld the Polygraph Protection Act, which bans the use of lie detector tests unless there is potential for significant harm if the test is not used, say, as a screening procedure. Thus, private security firms are exempted, including drug companies, specialized government contractors, and "ongoing investigations of economic loss or injury." And even when such tests can be used, the employer must clearly explain the test's purpose and the reason why the employee is expected to take it.

In addition, the subject has the right to consult with someone better able to explain the workings and limitations of the test. In this case, independent studies taken together have found polygraphs, which function by detecting a person's physiological reactions such as heart rate, blood pressure, and respiration when answering specific questions, to be only about 53% effective. Finally, subjects retain the option to reject the test and cannot be fired on the basis of a polygraph test "without other supporting evidence."

If we extend this standard to other invasions of employee privacy, employers would have to justify those procedures by showing that the public and/or business would be in significant jeopardy if they were not carried out. Interestingly, although this standard is partly upheld in widespread screening policies, it is just as often disregarded in other ways, even within the same company. Common examples are drug and personality tests, employee monitoring, and criminal and health background checks.

Drug Testing

Companies often require drug tests when screening job candidates. Advocates usually defend the practice on the basis of three ethical arguments:

1. Drugs are illegal, and the company prefers not to hire anyone who habitually engages in illegal activity.
2. Drugs lower job performance, and the company has a right to expect the highest performance possible.
3. Drugs are harmful, and the company has a duty to protect itself and the public from such harm that could be caused by employee drug use.

While these arguments have merit, they are nevertheless highly controversial in business ethics literature. First of all, it's not clear that employers have a right or interest in ensuring that their workers never engage in any kind of illegal activity. For example, it might be in the interest of employers to know if job candidates have ever cheated on their taxes. Nevertheless, most employers would never consider asking candidates for their latest tax return despite the fact that doing so might provide an excellent indication of moral character in an area that would seem highly relevant to myriad occupations especially in financial industries. This is why political candidates routinely disclose their tax returns to the public while campaigning. But it remains a widespread ethical belief that employers should not go so far as to audit tax returns when screening applicants. And this is the case even in business sectors where such information is highly job relevant. Thus the drug illegality contention is considerably weakened by such inconsistency. Still, libertarians maintain that private employers should be free even to ask for tax returns to screen job candidates. The fact that this is considered by many as unacceptable does not in itself make it so.

When this is pointed out, defenders often respond by appeal to the second argument, namely, that drugs lower job performance. Hence they are more job-relevant than, say, tax returns. Although this may be the case for certain drugs in certain professions, for example, heroin and cocaine use by surgeons and airline pilots, it does not usually seem so elsewhere. Interestingly, such professions are in such high demand for qualified candidates that they are often the last to require drug tests since most applicants would not willingly submit to them. A serious question of fairness arises here when privacy intrusions are selectively carried out only in professions in which workers are less skilled and easily replaced.

But with respect to decreased performance, it is neither obvious that any drug use, especially off the job, will decrease any job performance nor that employers have a right to demand the highest performance possible from their workers. If, however, performance slips significantly below acceptable levels, the employer may then have the right to investigate and attempt to correct the problem. If a drug problem is involved, then offering treatment may be appropriate. Contractarians argue that to preemptively invade *any* employee or candidate's privacy in anticipation of *any* potential lowered productivity is to disregard a possible abuse of power. But libertarians maintain that employees have no positive right to a job—only negative rights against harm—and since the employee is free to leave at will, no real harm is done.

The third argument concerning potential harm is much less controversial. As stated above, Congress and the courts have already upheld this standard exception to full employee or candidate consent with respect to polygraph tests. But it only applies to those professions in which a clear and present danger to the public or business overrules the right to privacy. Hence most jobs do not meet this criterion. Employers who cannot meet that high standard convincingly before invading employee privacy with drug tests cannot make use of this defense. Instead, they must advocate a weaker standard such as a right to protection from any potential harm.

Personality Testing

Personality tests are another common example of privacy invasion by employers. Many of the ethical problems concerning polygraph testing also apply to personality tests, which can vary widely in accuracy depending on the scientific quality of the test. Often, highly personal questions are asked in a context that critics argue conveys a thinly veiled expectation of absolute submission to authority. Taking personality tests can therefore be most unpleasant, making subjects feel violated and demeaned by projecting the image of an exploitative work environment. In addition, many personality tests are of dubious reliability. The Myers-Briggs test, for example, which millions of candidates take each year, has been found to be unreliable in independent tests, attributing a different personality type to subjects 53% of the time on different days.

On the other hand, when the questions are not overly personal or demeaning, and assuming they are scientifically valid and reliable, personality tests may be useful in determining which positions applicants would be best suited for. They tend to categorize candidates into a relatively small number of basic categories such as the classic introvert or extrovert. To many, such tests are relatively harmless and simplify the complexities of management decision making. Nevertheless, participation is usually less than fully voluntary since testing is often required as a condition of employment. Still, critics contend that people rarely fall squarely within a given personality type in all social contexts and that most personality tests are therefore invalid as they oversimplify human nature and employee potential.

Employee Monitoring

Employee monitoring via cameras, e-mail, or Internet use is a more invasive intrusion on privacy than are drug and personality tests. Hence employees are often given more detailed disclosures of the reasons for such policies. Nevertheless, it's not always clear that such practices are morally justified. Again, if we apply the Polygraph Protection Act standard, there would have to be a clear and present danger to the company such as theft of expensive equipment or highly sensitive intellectual property. Of course, this is usually the case, as such surveillance systems are considerably expensive.

However, critics argue that when such dangers are not present, those intrusions can contribute to an oppressive work environment likely to erode employee loyalty, thereby increasing theft and absenteeism. Indeed, critics point to independent studies indicating that overreliance on employee monitoring can help create the very problems it seeks to solve. But defenders argue that businesses have a right to protect their property even if it means undermining an atmosphere of trust. Indeed, employee theft amounts to billions of dollars in losses to U.S. businesses every year. These staggering costs provide a strong incentive for companies to install hidden and/or unhidden cameras. The result is that many Americans have become inured to the increasing prevalence of security cameras in the workplace. Complex concerns such as these are best addressed on a case-by-case basis.

Criminal and Health Background Checks

Companies routinely conduct criminal background checks of their perspective employees. Full disclosure of such policies is usually given to obtain informed consent. The reasons for such background checks are fairly obvious, especially for certain positions such as those involving children in which there is a need to protect the public from, say, pedophiles that have an extremely high rate of recidivism. There is widespread agreement that checks of this kind are entirely ethical since they clearly uphold the potential harm standard. But critics argue that conducting background checks indiscriminately is an unwarranted invasion of privacy that systematically impedes those with criminal records from obtaining gainful employment. The social costs of such exclusion are arguably great as they include higher crime rates and taxes to cover increased legal and punitive costs. Still, companies may have a right to protect themselves from potential criminals with existing records. To this, many critics reply that criminal backgrounds should not be the litmus tests they so often are—excluding candidates from further consideration. Other factors should be considered such as the severity and job relevance of the crime(s) as well as recent personal and professional references. If such factors are also taken into account and the policy is disclosed to job candidates, then a high standard of informed consent is fairly balanced by the employer's right to self-protection.

Health background checks, however, are not (as of yet) common practice. Although health records are entirely confidential, a company's insurance providers sometimes require new hires to disclose myriad costly preexisting medical conditions. Once disclosed, coverage can be denied or employee premiums can skyrocket. Critics argue that this is tantamount to discrimination and that informed consent has not been upheld when preexisting conditions are a litmus test for obtaining affordable health care through employment. Since certain health conditions can make medical coverage extremely costly, many have argued that those conditions should be insured by the government.

—Julian Friedland

See also Civil Rights; Consent; Disclosure; Employee Rights Movement; Libertarianism; Privacy; Property and Property Rights; Social Contract Theory; Workplace Privacy

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In-Kind Contributions

Nonprofit organizations are often the recipients of in-kind contributions as well as monetary contributions. In-kind gifts are noncash transactions that involve goods or services donated by individuals, corporations, and associations. Instead of cash, the nonprofit organization receives some other gift that assists in carrying out its mission. Common examples of in-kind contributions are donated space, office supplies, printing and shipping, health aids, land, technical advice, discounts not otherwise available, and many other types of goods and services. In 2003, the value of in-kind contributions accounted for nearly 50% of all giving, surpassing monetary giving from both foundations and corporations in the United States.

While in-kind contributions are as widely varied as the missions that drive nonprofit groups, there are generally three categories of contributions. First, it is common for businesses to give products, supplies, and equipment to nonprofit organizations. A charity that supports children may receive products for meeting clients' needs (e.g., diapers and baby clothing) and operating the organization (e.g., furniture and office supplies). Second, nonprofit organizations are often allowed to use facilities and services for free or a reduced fee. A women's shelter hosting a dinner and silent auction may receive in-kind donation of a hotel ballroom and a catering discount to reduce expenses and increase proceeds from the event. Finally, some firms donate professional services and employee expertise to nonprofit organizations. All organizations need legal, marketing, and tax advice, but these services are expensive. Instead of raising funds to cover these expenses, a nonprofit manager may seek in-kind donations of time and expertise.

While most nonprofit organizations have plans for increasing financial resources, fewer have formal in-kind contribution strategies. A formal approach to in-kind gifts goes beyond a "wish list" to include a broad analysis of the organization's needs and ultimately allows the nonprofit organization to use monetary funds for directly supporting clients and enhancing programs. Gifts In Kind International assists both nonprofits and businesses in meeting their goals for in-kind contributions. The organization, which is the third largest charity in the United States, uses online technology to match business donations to the specific needs of nonprofits around the world. Gifts In Kind has facilitated more than $4 billion in "product philanthropy" since 1983 and works with 200,000 charities and nearly half of Fortune 500 companies in the United States and other countries.

Given its significance and potential benefits, it is important for nonprofit organizations to properly document and account for in-kind contributions. A key task is to determine the value of contributions, which is typically based on fair market value or the cost to the organization if the goods and services were not donated. For example, if a software firm donates new software packages to a nonprofit hospital, the software is likely to be valued at the price the hospital would have paid to receive the software. If the software is dated or used, the fair market value would be determined differently. Once the in-kind gift has been valued, it is recorded as both an expense and a contribution in the general ledger. This accounting reflects the fact that the gift represents a contribution as well as an expense normally incurred for operating the nonprofit organization and/or its programs. Finally, the donor should receive a signed receipt that describes the in-kind contribution, its estimated value, the date of donation, and other details.

Donors receive several benefits from their in-kind contributions. First, certain donations may be tax-deductible up to twice the cost of the donated goods and services. Second, donations may reduce inventory handling and carrying costs for firms that contribute products normally sold to customers. Third, these contributions demonstrate a commitment to the community, provide evidence of social responsibility, and often lead to positive recognition and other intangible rewards.

—Debbie M. Thorne

See also Nonprofit Organizations; Strategic Philanthropy

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Insider Trading

In a broad sense, insider trading is obtaining information from nonpublic sources and using it for purposes of enhancing one's financial advantage. In a narrower sense, it refers to the purchase or sale of securities of a company, to the benefit of the seller or a third party, using inside information, understood as nonpublic information that the seller possesses as a result of having a fiduciary relationship with the company in question.

Inside information tends to be about something that may have an impact on the expected return or risk of a company: investment projects, appointments to the management team, plans for (or results of) research on new products, and so forth. For example, the purchase of shares of a pharmaceutical company by one of its managers hours before the public announcement of the results of research into a new drug that is likely to make the share price rise sharply would be classified as insider trading.

The person possessing inside information may be a manager or employee of the company who has a relationship of loyalty with the company; or a person or organization (legal counsel, advertising agency, auditor, consultant firm, or bank) that has dealings with the company, under a similar relationship of trust; or a person (a relative or friend, an employee of the bank) who has received information from one of the above. Inside information does not include public information or information made available to the public (to a journalist who is writing an article about the company, for example) or any information a person may obtain by his own effort and ingenuity, using licit means (such as the information obtained by a financial analyst by studying press reports and published accounting records of the company). Obviously, the legal and moral problem is about how inside information is used, not the mere fact of possessing it.

Close to insider trading are conflicts of interest, which can arise in any situation in which an interest interferes, or has the potential to interfere, with a person, organization, or institution's ability to act in accordance with the interest of another party, assuming that the person, organization, or institution has a legal, conventional, or fiduciary obligation to do so. An example might be an investment bank that uses the information it has about one customer to benefit another.

Often, insider trading is said to be a victimless crime, the suggestion being that it does not in fact have any moral consequences because the extent of the damage (which often takes the form of lost income) is unknown or because we cannot say exactly who suffers the damage or because the supposed damage is shared among large numbers of people in very small amounts, whereas the benefit tends to be highly concentrated. Yet it poses some interesting ethical problems, deriving from the fact that the person who carries out the insider trading has an informational advantage that outsiders lack—although that does not make every insider trading transaction immoral.

Ethical Arguments

There are three ethical arguments against insider trading: (1) It is (or may be) unfair for ordinary investors, (2) it hurts (or may hurt) a property right of the firm, and (3) it threatens a fiduciary relationship among the firm, its shareholders, and its employees. A fourth argument is that insider trading can cause harm to the ordinary investors or to the market, and we will discuss it under the economic arguments.

1. The fairness argument focuses on the disparity of information between the two parties to the transaction. There are two versions of this argument. According to the first one, insider trading is unfair because the two parties do not have equal information. But it is impossible that all market participants have the same information: In a free market economy, there has to be different (asymmetrical) information; otherwise, there would be no need for a market. Moreover, there is no moral right to equal information: We have a right to truth, but not necessarily to the whole truth. For example, we are not morally obligated to tell the other parties in a transaction everything that would be in their interest to know—for example, the buyer of shares in a company who has good reason to believe that it will earn extraordinary profits is under no moral obligation to reveal that circumstance to the seller.

The second version of the fairness argument accepts that some disparity of information could be fair but argues that insider trading will be unfair if the insider has information that is not accessible by hard work and ingenuity to the other party. The problem with that argument is that the notion of equal access to information may be attractive in principle, but we do not know how it can be applied in practice. In ordinary life we all have inside information about a lot of things, and we all try to obtain it and benefit from it, without that raising any problems of justice toward others (obviously, there would be injustice if the inside information were obtained by theft, fraud, espionage, or other criminal means). To sum up, an abstract concept of fairness alone cannot settle the insider trading issues.

2. The second argument concerns who the owner of the information is, how it is acquired, and what entitles people to make use of it. Information always belongs to somebody, and there is no doubt that companies have a right to the information about their affairs, be it news of mergers, scientific or technological discoveries, or investment plans. In that sense, managers, employees, or even shareholders (and also consultants, auditors, bank employees, tax inspectors, etc.) who know such information possess a good that belongs to the company and must use it to the company's benefit (unless they receive the company's permission to do otherwise), or at least they are not entitled to make use of it against the will of the firm, either for their personal advantage or for the profit of other people, any more than they are entitled to the company's assets.

It has been argued that if managers or employees stand to gain from any inside information that they themselves generate, they will be more likely to engage in innovative and entrepreneurial activities. That may be so, but the reverse may also be true: They may engage in activities that are of no interest to the company but that benefit them personally; or they may sow unfounded or manipulated news stories, again for their own benefit.

There are others, apart from shareholders, managers, and employees, who may claim a right to be informed about the company: bondholders, bankers, customers and suppliers, employees, the local community, and so forth. Each has a right to certain information—the information that concerns them—because a law, a contract, or a code says so. But in no way does that include the use of such information for their benefit.

A more complicated case would be if, by chance, a person receives inside information as a result of, say, overhearing a conversation in the street or receiving an e-mail by mistake. Must that person respect the company's right to such information? This is not a case of inside information, as this person is not an insider, but it is much the same as when a person finds an object that someone else has lost: The object still belongs to its owner, who is entitled to claim it back—although, in the case of information, it is not lost, but simply shared. We can conclude that information cannot be used against the company's will, just as a found object cannot be retained against the (implicit) will of its owner. Nor is there any obligation to share such information with others, much less make it public.

3. The third ethical argument on insider trading is that of trust. The managers, employees, or advisers of a company who use inside information for their own benefit or that of third parties betray the trust the company has placed in them. Likewise, the bank employees who know a company's secrets because of their job at the bank are in the same situation with respect to the bank and with respect to the company.

Obviously, disloyalty must be judged in light of the circumstances. A shouted conversation in the street cannot be said to be secret; but if it takes place in a private office, it can. Some information will be trivial and does not have to be kept secret, whereas other information is important (and we can assume that the latter is what insider trading is about).

To sum up, insider trading must be analyzed in the context of the relationships among the firm, its shareholders, and its employees (and other stakeholders), insofar as it threatens the fiduciary relationship that is central to business. It is not necessarily immoral, unless it violates the trust that the company has placed in those people, either inside (managers, employees) or outside (advisers, financial intermediaries) the company, or infringes the company's right to own its information, so that the use of such information by other people amounts to misappropriation. This not being the case, the use of inside information may be ethical, unless it causes harm to other investors or to society at large.

Economic Arguments

Some economists claim that insider trading is ethical, and should be legal, because it is positively beneficial, insofar as it enhances the efficiency of the financial market as a mechanism for gathering, storing, processing, and diffusing information. In the simplest terms, trading based on inside information makes the market price come to the "true" price sooner than it otherwise would, and this has clear economic benefits to the market in general.

In the financial markets, it is assumed that the price of an asset is equal to the discounted present value of the future flow of expected net returns, taking the asset's risk into account. It is also assumed that if the market is efficient, it will react to each new item of information about those variables by instantly modifying the asset's price. Therefore—the argument goes—the flow of information to the market should be as free as possible; whether the flows take place via insider trading or not is irrelevant. Moreover, if the information comes from an internal (and, therefore, reliable) source, it may be less uncertain (though that need not be the case).

However, the argument that insider trading fosters market efficiency is highly questionable because what we are talking about here is not important information that would otherwise remain hidden for a long time but information that is due to be made public in the very near future. In such cases, the benefit to society of receiving that information slightly earlier will be minimal, while the private benefit—and the moral harm—may be substantial. And most likely it would be best if the information were disclosed to the whole of the market, as is generally required by law. Also, the mere possibility of insider trading may erode the investors' confidence, pull the investors out of the market, and reduce its efficiency.

In any case, critics reply that trying to justify insider trading on the grounds of efficiency is too much like saying the end justifies the means. In the capitalist system, the goal of efficiency must be subject to ethical conditions, and the mere possibility of obtaining extraordinary profit through insider trading may encourage immoral behavior, such as information theft or espionage, or market manipulation.

—Antonio Argandoña

See also Capitalism; Conflict of Interest; Fiduciary Duty; Finance, Ethics of; Manipulation, Financial; Trust

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INSTITUTIONAL FRAMING

Frames are the cognitive categories or schema people use to describe, interpret, and sort events, issues, and entities for themselves and others to understand and predict their environment. Institutions can be described as a set of societal rules or expectations that govern interactions and/or as organizations created to achieve a specific, collective purpose. The concept of institutional frames considers both descriptions. Institutional frames provide one a context for understanding the complex interrelationships among organizations and their policies, processes, products and services, and relationships with stakeholders.

Numerous social science disciplines including communications, economics, psychology, social psychology, political science, and organization studies use the concept of frames to explain a multiplicity of phenomena. Scientific inquiries have focused on the nature of frames and how frames influence a variety of outcomes including how risks are perceived, how decisions are made, how political issues are perceived, how social dilemmas are resolved, how ambiguity and change are managed, and how leadership is exercised. Although various disciplines use different terms to refer to and discuss frames, all converge on the concept that individuals do not passively perceive their environment. Instead, they actively (and often unconsciously) sift through information, constructing and applying meaning to their surroundings. The process of framing involves active interpretation of objects, events, and issues. Frames are interpretive devices that individuals use to understand their own world and that can be strategically used to shape the sense-making of others.

Cognitive frames are analogous to picture frames. Imagine framing a photograph: The way the photograph is matted and framed highlights some aspects of the photograph more than others. Certain matt colors and frame shapes can dramatically alter the appearance of the photograph, making particular aspects of it central and other aspects peripheral, and cutting some out entirely. A cognitive frame operates the same way: A given frame may emphasize certain aspects and angles of an issue, entity, or event and de-emphasize or ignore other aspects. The way we frame an issue shapes our perception of reality and informs our future action.

Threats and opportunities are examples of important and commonly discussed frames in the organizational literature. When an individual categorizes or interprets an event as a threat, information is perceived and processed differently compared with how it would be if the event were categorized as an opportunity. Framing an event as a threat may initiate defensive strategies, whereas framing an event as an opportunity would most likely result in more innovative and creative responses. Similarly, research on ethics and framing suggests that if managers do not initially frame an issue as having ethical implications, ethical reasoning and decision making will not occur.

Organizational researchers have used institutional framing to help explain decision-making behaviors affecting various corporate stakeholder groups. For instance, how business strategy is framed is demonstrated to affect decision-making style. When decision makers frame their company's strategy as "cooperative," decisions tend to be made participatively. When strategy is framed as "entrepreneurial," decision makers tend to act autonomously. Also, the presence of sanctioning systems within an organization affects whether decision makers hold "business frames" or "ethical frames." Business frames trigger decision makers to engage in cost-benefit analyses when deciding to act cooperatively versus competitively. Ethical frames are more likely to trigger cooperative behavior, regardless of the existence or strength of the sanctioning system.

The way the purpose of the corporation is framed is an important subject within the domain of business and society. The ownership theory of the firm frames a corporation as an entity owned by the shareholders. This frame defines the sole purpose of the corporation as maximizing the value of the firm for stockholders. From this perspective, shareholders' interests always take first priority over any other stakeholder group. Business leaders who frame the raison d'etre of business as maximizing shareholder wealth are unlikely to make decisions and take actions that explicitly consider stakeholder concerns.

Conversely, stakeholder theory frames the purpose of the corporation as creating value for society. Framed as such, corporations must make a profit, thus creating economic value, but they must create social value as well. The stakeholder frame suggests that along with the interests of the stockholders, the interests of multiple stakeholder groups, such as employees and customers, must also be considered.

Institutional framing affects the perceptions of those both within and outside of the organization. It is advantageous for an organization to use framing in an effort to garner support and legitimacy from its internal and external constituents.

—Barrie E. Litzky and Tammy L. MacLean

See also Business, Purpose of; Business Ethics; Economics and Ethics; Ethical Decision Making; Strategy and Ethics

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Instrumental Value

Instrumental value refers to the value that something has in virtue of its being conducive to something else of value. As such, to value something instrumentally is to value it as a means to some other end. For instance, currency has merely an instrumental value to most persons, insofar as it enables them to procure other goods and services that they value. Instrumental value is contrasted with intrinsic value. To value something intrinsically is to value it in and of itself, for its own sake, and not as a means to anything else. Furthermore, something that is of instrumental value can come to lose that value: when it is no longer necessary to achieve the end in question, when something else is found that can be used to achieve that end equally well, or when the end in question is no longer desired. However, the intrinsic value of something cannot be replaced by something else or lost in a similar manner. Since people only value things instrumentally insofar as they are means to something else of value, many philosophers hold that people must value some things intrinsically; otherwise there could be no instrumental value. It is important to note that the categories of instrumental and intrinsic value are not necessarily mutually exclusive, as something might have both an instrumental and an intrinsic value for a person. For example, a person might value a piece of artwork intrinsically as an aesthetic object as well as instrumentally as an investment.

Although attributions of instrumental and intrinsic value are not necessarily mutually exclusive, a number of concerns in contemporary business ethics turn on the extent to which some business practices reduce certain values to the merely instrumental level. While there is much debate on what precisely can have intrinsic value, there is a large vein of philosophical ethics that maintains that persons have intrinsic value. Deontological theories, such as Kantian ethics, typically stress the intrinsic value of persons as ends in themselves. To recognize someone as having intrinsic value is to recognize his or her value independent of the projects or desires of others. Since persons, on such views, have an intrinsic value, it is morally wrong to treat them as mere means toward one's own ends. This entails, on most deontological accounts, a basic duty of respect for others and, often, acknowledging a corresponding set of human rights that ought to govern our interactions with others. Such views would rule out coercive or deceptive practices and prescribe behavior toward others that enhances their autonomy and respects their individual value.

In this vein, a number of business practices have been singled out as instances in which persons are treated as having merely instrumental value. For instance, deceptive advertising practices and predatory marketing to vulnerable groups have been seen as paradigmatic cases in which consumers are treated as mere instruments for the generation of revenue, at the cost of failing to respect their individual worth. Likewise, employers are accused of treating their employees as having a merely instrumental value when they subject them to working conditions that are inherently dangerous or degrading or that infringe on their basic human rights. Criticisms of the latter sort have been particularly prominent in regard to the use of sweatshop labor in undeveloped countries.

More general concerns about commodification and consumerism can also be tied to issues involving questions of intrinsic and instrumental value. Some critics, for example, argue that commodification refers to social practices that reduce nearly everything to mere commodities that are viewed only in terms of their monetary, and thus instrumental, value. Such critics contend that the commodification of things such as art, education, knowledge, and even personal relationships has led people to overlook what they take to be the intrinsic nature of such goods. Similarly, critics of consumerism maintain that the rampant consumption of unnecessary and trivial goods found in postindustrial economies involves a leveling of all value to mere instrumental value and in doing so undermines people's ability to recognize and engage with social goods of intrinsic value.

Finally, there is also a good deal of contemporary debate in business ethics about the value of the natural environment. Traditionally, much economic thinking and, perhaps as a result, many business practices treated the environment as having a merely instrumental value. In particular, the environment was seen as only providing instrumental value in the form of natural resources. As such, natural ecosystems, biological diversity, and even the existence of particular species of flora or fauna were seen as having no value except in relation to human production and consumption. Many contemporary environmental ethicists argue that this view was responsible for much of the environmental degradation, pollution, and other environmental problems that currently exist. These environmentalists argue for a more biocentric view that recognizes the intrinsic value of elements of the natural world. If they are correct, then businesses might have some responsibilities toward the environment that are not merely reducible to their responsibilities to other persons. Of course, whether or not such critics are right will turn upon a more careful examination of the nature of intrinsic value itself.

—Daniel E. Palmer

See also Commodification; Environmental Ethics; Human Rights; Intrinsic Value; Kantian Ethics; Moral Standing; Normative Ethics

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Integrative Social Contract Theory (ISCT)

The term *integrative social contract theory* (ISCT) was coined by Tom Donaldson and Tom Dunfee, two business ethicists at the Wharton School of the University of Pennsylvania who, as a philosopher and a legal scholar, respectively, elaborated a methodology for developing norms for corporate morality on the basis of a social contract model. As in the work of classical contract theorists such as Hobbes and Locke, who used the contract model to specify the principles for the legitimate exercise of power by the state, ISCT seeks to specify the principles for socially responsible corporate conduct on the basis of a social contract model especially adapted for this purpose.

An explicit goal of the ISCT project was to improve on the practical guidance of general ethical theories such as utilitarianism, Kantianism, virtue ethics, or the stakeholder model. By their very nature, these general ethical theories will always remain insufficiently specific to provide concrete practical guidance. The general thrust of the ISCT project can be seen from the examples with which the project was introduced, Royal/Dutch Shell's dispute with the Ogoni, an indigenous people living in the Niger Delta, and the bad publicity over the *Brent Spar* affair. The idea here is that in any practice of foreign direct investment there may well arise conflicts between (usually stricter) moral norms in the home country of the firm and the (generally more lenient) standards practiced in the host country. ISCT then presents itself as an instrument preeminently suited to resolving these kinds of conflicts.

At the core of all contractarian approaches is the idea that all parties involved in the social contract ("the contractors") voluntarily *consent* to whatever the terms of the contract are. Any social contract theory must therefore give some characterization of the parties to the contract and their motivation to come to agreement. ISCT describes the contractors as motivated by a mix of preferences, in which some are greed driven, some altruistic, but in which most are simply somewhere in between and do not know to which economic community they will belong or their personal wealth. But they have settled understandings of deep moral values, which are used as ingredients for the moral norms the contract will sanction.

Having thus characterized the choice situation, ISCT argues that contractors will agree on a procedural model of four steps that will help specify some universal principles, called hypernorms, which may be presumed to be valid in all places and circumstances. The core idea of the ISCT model is that any conflicts among local norms can be reconciled by these universal principles. And as more empirical evidence is gathered, these presumed hypernorms acquire a stronger status (and supposedly more moral authority).

Criticism of ISCT

Ever since the beginning, commentaries have pointed out some major ISCT problems. For present purposes these criticisms may be divided into challenges of the empirical applicability of the project and the more conceptual criticism of the actual setup of Donaldson and Dunfee's social contract model. Many empirically oriented commentaries have criticized the project in its present form for failing to specify more concrete hypernorms. Conceptual commentaries point out that the contract model is only suited to formulating formal principles that still require an act of judgment by practitioners before they can provide concrete practical guidance.

—Ben Wempe

See also Business Ethics; Kantian Ethics; Stakeholder Theory; Virtue Ethics

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Integrity

Integrity can be defined as the quality of being honest and morally upright. Integrity is a crucial foundation for all trustworthy stakeholder relations in business. More specifically, integrity is both a personal and a social capacity to coherently process moral awareness, deliberation, character, and conduct, to regularly render balanced and inclusive judgments regarding moral results, rules, character, and context, to routinely demonstrate mature moral reasoning and relationship development, and to design and/or sustain morally supportive intraorganizational and extraorganizational systems. The four dimensions of integrity are process, judgment, development, and system capacities; they both enable and reflect moral coherence, moral wholeness, moral maturity, and moral environment.

Process Integrity and Moral Coherence

Process integrity capacity is the coherent alignment of individual and collective moral awareness, deliberation, character, and conduct. The need to address lapses in process integrity capacity is evident by the frequent disconnect between business moral rhetoric and actual behavior that provokes stakeholder criticism of moral hypocrisy, for example, multinational corporations that tout their public relations images of being responsible corporate citizens while engaging in morally objectionable practices that pollute the natural environment and exploit indigenous workers.

Ordinary language definitions of personal integrity as embodying cohesive and sincere adherence to moral principles and commitments refer to process integrity capacity. A person of integrity is commonly understood to be one who is morally aware (i.e., perceives, discerns, and is sensitive to moral issues), demonstrates both autonomous reflection and interdependent moral deliberation in the analysis and resolution of moral problems, is ready to act ethically (i.e., exercises intellectual, social, moral, emotional, and political virtues that build strong character and motivation to act ethically), and engages in responsible, aligned, and sustainable conduct (i.e., takes action that is consistent with personal moral resolutions on a regular basis, even at great personal sacrifice, and can publicly applaud the moral justifications for doing so). Moral coherence between belief and expression, awareness and deliberation, word and deed, and among moral judgments, commitments, and actions is a hallmark of authentic personal integrity.

Moral coherence also entails social process integrity. Teams, firms, cities, and institutions, for example, with high process integrity capacity are more likely than competitors to be aware of and rapidly respond to multiple stakeholder moral concerns, arrive at balanced decisions that form sound policies, and build supportive moral systems that sustain business and social excellence. They exhibit a coherent unity of purpose and action in the face of moral complexity rather than succumb to collective inertia or biased decision making.

Judgment Integrity and Moral Wholeness

Integrity also entails moral wholeness that is enabled by and reflected in judgment integrity capacity. Judgment integrity capacity is the balanced and inclusive use of key ethics theories and dialogic resources in multiple stakeholder relationships to analyze and resolve individual and/or collective moral issues. Ethics theories can be organized into four categories: teleological ethics theories (emphasizing moral results/purposes), deontological ethics theories (emphasizing moral rules), virtue ethics theories (emphasizing moral character), and system development ethics theories (emphasizing moral contexts). Personal moral wholeness is determined by the degree to which an individual in interaction with multiple stakeholder relations achieves good results, follows the right rules, cultivates virtuous character, and sustains morally supportive contexts throughout life without underemphasizing or overemphasizing any of these factors. On the other hand, ruthless individuals who overemphasize the achievement of good short-term financial results while violating moral and legal rules, forging vicious character traits such as callous insensitivity to others and destroying morally supportive contexts, demonstrate a lack of moral wholeness and dishonor the diversity of stakeholder relationships.

At the social level, exhibiting moral wholeness and judgment integrity capacity for teams, organizations, cities, and institutions means optimally achieving good results (profits in the private sector, votes in the public sector, and donations in the nonprofit sector) by adhering to standards of right conduct and following the right rules, while habitually developing virtuous character traits in moral work climates and creating or sustaining morally supportive intraorganizational and extraorganizational contexts. All four theories and their arguments communicated in a dialogic relationship, with appropriate emphases for each issue, are necessary for inclusive and balanced analysis and resolution of moral issues. Business leaders who refuse to engage in the moral dialogue process and unilaterally insist on overemphasizing or underemphasizing good results, right means, virtuous character, and/or morally supportive contexts incur the same adverse consequences as business leaders who cannot handle behavioral complexity, that is, offended individuals, neglected opportunities, eroded trust, and corrupted environments.

The moral wholeness of social judgment integrity capacity is also demonstrated by the extent to which specific moral principles guide role relationship decisions in the private, public, nonprofit, and corporate domains. In the private domain of shared interests, for example, role relationships between doctor and patient, producer and consumer, or teacher and student, moral wholeness is demonstrated by the extent to which the moral principles of equality, decency, reciprocity, and honesty are included in and guide transactional and participatory ethics decisions. In the private domain of conflicting interests, moral wholeness is demonstrated by the extent to which the moral principles of justice, honoring diversity, and beneficence are included in and guide recognitional ethics decisions. At times morally whole persons give precedence to the rights of others over their own interests out of respect for retributive justice, the inherent value of relationship diversity, and beneficence, that is, avoid doing harm, repair or compensate the harm you did, prevent harm being done by others, avoid bringing about conditions that generate harm, and do good wherever and whenever you can to sustain trustworthy relationships.

In the public domain, for example, role relationships between elected officials and citizens, public employees and government authorities, and public administrators and natural resources, moral wholeness is demonstrated by the extent to which the moral principles of public deliberation, fairness, civic cooperation, concern for the common good and public trust, secure civic reciprocity, and responsible natural stewardship are included in and guide representative and ecological ethics decisions. In the nonprofit domain, for example, role relationships between donors and recipients, volunteers and NGO administrators, and needy populations and international aid agencies, moral wholeness is demonstrated by the extent to which moral principles of cultural openness, transparency, respecting resource boundaries, compassionate sensitivity, accountable generosity, planetary citizenship, and emancipation are included in and guide civil society and philanthropic ethics decisions. In the corporate domain, for example, in role relationships between employees and employers, suppliers and distributors, and investors and managers, moral wholeness is demonstrated by the extent to which the moral principles of meritocratic justice, respect for ownership rights and multiple stakeholder interests, legal growth and responsible property management, corporate citizenship, and triple bottom line accountability are included in and guide market ethics decisions.

Developmental Integrity and Moral Maturity

Developmental integrity capacity is the cognitive and affective final improvement stage of individual and collective moral reasoning and caring relationship formation capabilities from an initial stage of preconventional self-interested concern (morally immature, selfish connivance) through a stage of conforming to external conventional standards (partially morally mature, external-governing compliance) to a final stage of postconventional commitment to universal ethical principles and responsive caring relationships (morally mature, self-governing civic integrity). Postconventional principled moral reasoning and caring relationship prioritization demonstrate moral maturity. Morally mature leaders are living examples of developmental integrity capacity who have internalized their identity-conferring commitment to universal principles such as justice and responsive caring relationships, are emotionally attuned to their stakeholders, and elevate the moral expectations and performance of stakeholders to the level of social integrity. Erik Erikson, for example, regarded integrity as the highest stage of personal ethical and psychological development.

Individual and collective connivance is the lowest stage of moral development, characterized by the use of direct force and/or indirect manipulation to determine moral standards. Business leaders and work climates that sustain this stage of moral immaturity are either issuing threats of force (e.g., "Get it done now or else") or developing exclusively exploitative relationships based on mutual manipulation (e.g., "I'll lie for you if you lie for me") to enact a moral jungle. Firms and societies that abuse their members perpetuate this moral immaturity.

Individual and collective compliance is the intermediate stage of moral development, characterized by either conforming to popular work norms or adherence to externally imposed standards. Business leaders and work climates that sustain this stage of partial moral maturity abandon the moral jungle and are either admonishing employees to secure peer approval (e.g., "Everyone in your work group must follow these traditional standard operating procedures") or commanding them to comply with organizational hierarchy and/or externally imposed regulations (e.g., "You must conform to government regulatory standards or you will be imprisoned"). Corporate external compliance efforts prevent criminal misconduct and limit corporate legal liability, but they do not enable responsible internally governed moral behavior. Compliant business leaders whose highest moral aspirations are to stay out of jail are not operating at the level of commitment to developmental integrity.

Individual and collective commitment to integrity is the highest stage of moral development, characterized by the use of substantive democratic participation and/or internalized respect for universal moral principles and caring stakeholder relationships as a basis for determining moral standards. Business leaders and work climates that sustain this stage of moral maturity are either identifying and satisfying the wishes of the majority (e.g., "Everyone should participate in public deliberations and vote, but the majority opinion will prevail in policy formation") or eliciting commitment to universal moral standards (e.g., "Whatever policies we adopt by consensus must meet universal standards of justice, care, and global citizenship"). Firms and societies committed to developmental integrity standards act like morally mature citizens on behalf of other internal and external stakeholders—domestically and globally.

System Integrity Capacity and Moral Environment

System integrity capacity is the demonstrable capability to design or sustain organizational moral infrastructures and extraorganizational relationships that provide a supportive moral environment for ethical conduct. The system contexts within an organization and outside it can either support or inhibit ethical action; for example, the morally impoverished environment of a corrupt organization located in a crime-infested city in a bribery-riddled nation on a heavily polluted planet inhibits viable institutionalization of system integrity capacity. Individuals and collectives that design or sustain supportive moral environments at the intraorganizational and extraorganizational levels demonstrate system integrity capacity.

At the intraorganizational level, system integrity leaders design or sustain purposes, policies, processes, and procedures that not only meet legal compliance standards, for example, conformity to the revised U.S. Federal Sentencing Guidelines and the Sarbanes-Oxley Act, but also support relational integrity, for example, individual respect for employees as citizens; secure trustworthy, reciprocal interpersonal work relations; empowered, justly compensated, and collaborative teams; use of organizational ethics needs assessments and system moral performance improvement measurements; and reward/reporting systems that hold all employees accountable to ethical standards.

At the extraorganizational level, subnational entities such as cities, states, or regions, national sociopolitical cultures, and international human and nonhuman standards create moral environments that enhance or inhibit process, judgment, and developmental integrity capacities. For example, since business leaders and firms are a part of the system of domestic civil society, the extent to which they form cooperative partnerships with city, state, regional, and national sociopolitical leaders to cosponsor projects that mutually support human flourishing and intergenerational coprosperity indicates their capacity for designing and sustaining domestic system integrity. In addition, since business leaders and firms are a part of the system of global civil society, the extent to which they promote responsible industry standards globally, support international laws, treaties, and standards for free and fair trade, endorse global human and natural sustainability standards, for example, the Global Compact principles of respect for human rights, fair labor standards, natural environment stewardship, and anticorruption and the Earth Charter provisions of caring for the community of life, ecological system integrity, socioeconomic justice, and democracy, nonviolence, and peace, indicates their capacity for designing and sustaining global system integrity.

—Joseph A. Petrick

See also Authenticity; Autonomy; Honesty

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INTELLECTUAL CAPITAL

To speak of intellectual capital is to speak of a new class of assets that emerged toward the end of the 20th century and rapidly achieved strategic, financial, and economic significance in the world of business and the affairs of society. While these intellectual assets were long recognized in some inchoate sense, and referred to as “goodwill” by accountants and financial executives, it wasn’t until the end of the 20th century that they became formally recognized and monetized, got placed on par with the traditional physical and financial assets, and began to gain their ethical character.

Economically, intellectual capital is the asset base of a new, knowledge-based economy that is producing significant levels of equity and wealth based on the formalization of ideas, innovation, and creativity. Equally important, intellectual capital has achieved immense significance strategically and managerially in the world of business because of its ability to create new enterprise value, establish differentiation in the marketplace, and deliver often sustainable competitive advantage. Thus, socially and culturally, this new class of assets articulates an expanded role for knowledge and creativity within civilization.

The concept of intellectual capital embraces the products and creations of thinking and feeling, the arts and the sciences, the professions, and the world of business insofar as they are treated as assets and leveraged for business or enterprise purposes. Specifically, in the world of business, intellectual capital includes all the ideas and creations that have become central to the modern enterprise, such as brands, intellectual property portfolios, innovation, knowledge, and the competencies and talents of human capital.

Early Terminology and History

When defining *intellectual capital* one must articulate it with regard to a set of terms and phraseologies that are often confusingly similar, with each describing a dimension of intellectual capital as seen from the perspective of a particular profession and its body of knowledge.

Intangible assets, goodwill, nonfinancial assets, intellectual property, intellectual assets, and *knowledge-based assets* are discipline-specific terms that are often used interchangeably and more or less synonymously to refer to what, at its most articulate, has become known as *intellectual capital.*

Intangible assets and *goodwill* are accounting and financial terminologies that predate the 21st-century understanding of intellectual capital. Such terms are used by accountants and financial professionals to refer to the "intangible" entities or factors of financial analysis that couldn't readily be captured and reported in the traditional documents of financial reporting such as the balance sheet and profit and loss statements. Thus, for example, until the turn of the 21st century, any monetary value allowed to brands and intellectual property was commonly captured as goodwill.

Intellectual property of course has long been recognized in modern law as those ideas, inventions, processes, names, and creations that could be protected and asserted under the law as patents, trademarks, copyrights, and trade secrets. At least since the European Renaissance, the economic and political significance of ideas and inventions has been acknowledged in some form or another, often as business monopolies or commercial grants that were bestowed on a citizen of the realm by a monarch or noble. Near the end of the 20th century, as it became clear that intellectual property had previously unrecognized economic and strategic significance and was thus a business asset that could be deployed to deliver competitive advantage, lawyers and managers began to refer to it in its strategic deployment as an *intellectual asset.* And soon a new discipline, referred to as *intellectual asset management,* began to emerge. During the early 21st century, intellectual asset management sufficiently formalized itself to become the topic of numerous scholarly publications, journals, seminars, conferences, and corporate strategies.

Simultaneously, economics and the emerging knowledge management and informational technology practices began to refer to the same intellectual phenomena as *knowledge-based assets.* As the production process for creating intellectual assets became increasingly clear, data were collected and turned into information and, finally, knowledge, and *knowledge-based assets* became the operational term for increasingly palpable intellectual assets.

Strategically, and at the senior and executive levels within corporations, *intellectual capital* became the synthetic terminology used to refer to all the intangible, intellectual, knowledge-based material and goodwill that could be managed and fruitfully leveraged toward some strategic business purpose.

Ethics and Intellectual Capital Practices

The managers of both tangible and intangible assets are, of course, always bound by the generally accepted ethical constraints commonly associated with society and business, the responsibility to manage and optimize enterprise assets within the law for the good of the business and its shareholders, and the concern with matters of mismanagement, misappropriation, fraud, and greed.

However, intangibles, because of their imprecise nature and volatile dynamics, also invoke new, often subtle considerations of intellectual property infringement, interference in business relations, unfair competition, failure to report assets, and regulatory and compliance violations. It is with this management and deployment of intellectual capital assets that ethical issues can emerge. The primary ethical issues that have emerged around intellectual capital assets may be classified as concerning the creation, the monetization, or the responsible management of intellectual capital assets.

The Creation of Intellectual Capital Assets

In many cases, the ease with which intellectual assets such as a trademark or a patent can be created has led to forms of abuse that, while not always prima facie illegal, may misappropriate intellectual material or unfairly block competition from market access. The earliest such form was a practice that became popular in the closing decades of the 20th century and that was known as *trademark banking.* In such cases, large corporations that could afford to file innumerable trademark applications adopted the practice of registering often large numbers of trademarks in case they decided to use them and to prevent competitors from adopting the same or similar names for their own purposes. In such cases, organizations would prepare and sell some small token of an apparently new product under the desired trademark so as to be able to comply with the minimum requirement of interstate commerce for filing a trademark registration. Then they would file a formal application for that product name, often followed by related or similar versions of the name, intending to abandon the trademarks after 5 or 6 years if they had not used them or when they no longer had critical commercial value to the organization or its competitors.

Similarly, during the 1990s, large corporations began filing what later became know as *junk patents* to prevent competitive technologies from entering the marketplace. In these cases, a large company would build a wall around their existing technology by filing many patents with incremental and often insignificant differences. When representative of novel expansions of a core invention, building a "thicket" around a valuable technology is a wise and generally accepted way of protecting a core technology. However, when an array of "junk patents" is simply a "log in the public road" blocking a competitor from gaining legitimate access to a market, it becomes an unethical practice.

At first both trademark banking and patent thickets simply seemed like smart strategic thinking, and they were eagerly embraced by many large organizations. In time, however, it became increasingly difficult for legitimate market entries to find names they could trademark as so many were taken up by apparently legitimate trademark registrations that actually had no presence in the marketplace. Inventions and innovation were also frequently blocked by junk patents, preventing innovations from reaching the public marketplace. In both cases, while originally accepted as a way of expanding and insulating valuable intellectual property from infringement, once it began to prevent legitimate competition from entering the marketplace it became unethical and even illegal in some cases. The line between best intellectual asset practices and unethical practices is subtle, and it is easy for a brilliant strategy when taken to an extreme to become unethical, anticompetitive, monopolistic, and even predatory.

The Monetization of Intellectual Capital Assets

Because intellectual assets are much more volatile than are the traditional physical and financial assets, these assets are more susceptible to manipulation. Primary among the ethical problems that have emerged with the monetization of intellectual assets are the "min-maxing" of intellectual assets, causing fluctuations in asset valuation, and the matter of "hidden assets," or unreported intellectual assets.

During the early 1990s, boards of directors and visionary executives wielding the then new power of the expanded intellectual asset market capitalization of their company gave birth to the modern stock-based mergers and acquisitions strategy. Suddenly, even in relatively cash-poor companies, new growth was possible through the pooling of assets allowed in stock-based business combinations. In many such cases, as no cash or debt was involved, executives became star performers by acquiring businesses, delivering apparently unending corporate growth, and providing stock price appreciation—while simultaneously building their careers and personal wealth. As the buying of corporations progressed, and the orderly exiting of executives with their newfound wealth proceeded, it became clear that deal-makers had manipulated or otherwise justified intangible asset valuations to enhance the value of or to ensure the consummation of a business deal, while often knowing that such maximized valuations would later be hard to maintain in an ongoing business.

The discovery of valuable intangible assets and how they could be leveraged to effect highly valued merger and acquisition transactions made it also likely that many deals would be consummated at values that were unsustainable because the intangible asset valuations, arrived at without a proven intangible asset valuation methodology, had been set high on enthusiasm. As the highly volatile nature of intangible assets became more understood, financially unsustainable, overvalued transactions that benefit only the short term began to be seen as unethical. While temporarily gaining from the peaks of stock appreciation, in the end longer-term shareholders later had to reconcile the losses driven by the speculation and unsustainability of the respective asset value. *Making the deal* was often more important than the later insolvency of overvalued deals and their impact on long-term shareholder value.

Subsequently, to discourage such manipulation, the Financial Accounting Standards Boards passed new regulations that require intangibles acquired in a business combination be recognized on the balance sheet and to be tested annually for the impairment of their value, with overvaluations entailing a write-down in enterprise valuation. Prior to impairment testing, when no write-downs were required, it was easier to put together overvalued or poorly valued mergers or acquisitions that allowed some financiers, corporate executives, and investors to make large amounts of money, only to leave the company with overvalued assets and large, potential write-offs later.

During the early years of the 21st century, regulations and ethical best practices identified this min-maxing of intangible assets as a form of market manipulation, thus sharpening the ethical focus on fair and accurate valuation and long-term shareholder benefit.

At another extreme lies the ethical problem of "hidden (intellectual) assets," which remain unrecognized to reduce financial reporting volatility and remain undisclosed to investors. Somewhere between the requirements of disclosing "material assets" and the realization that intellectual assets are extremely volatile and can experience dramatic shifts in value lies the proper and ethical accounting recognition and enterprise management of intellectual assets.

In this respect, managers are often caught between formalizing and gaining managerial control over intangible assets and leaving them "hidden" and unrecognized to avoid being held financially accountable for them. Building the asset base of the organization with a volatile intangible asset that could be difficult to manage, fluctuate in value, or unfavorably affect the stock price of an organization can be premature or irresponsible. However, recognizing valued intangibles, such as "brands" and "patent portfolios," even though they could affect enterprise valuation if they were recognized, is essential to gaining managerial control over such assets.

For many, the ethical solution lies in recognizing that intangible assets move through stages of concretization, ranging from being entirely intangible to being well-identified, formalized, managed, and eventually benchmarked, valued, and possibly monetized. The place at which they are adequately concretized and stabilized to allow meaningful management is the point at which they become a potential financial reporting disclosure. At that point, to keep them out of financial reporting documents may be to act unethically. To underscore the ethical and legal responsibility to disclose and manage material assets, during the beginning of the 21st century, organizations began to experience not only SEC censure for the failure to disclose material assets that affect financial performance, and Sarbanes-Oxley reprimands for failing to establish internal controls for such assets, but also the first shareholder lawsuits for a failure to manage intangible material assets.

The Responsible Management of Intellectual Capital Assets

Unmanaged or poorly managed intellectual capital assets represent liabilities to investors and culpabilities to management. Assets that have not been identified and formalized cannot be managed and optimized to deliver enterprise performance.

In cases where the rigor brought to the management of tangible and financial assets doesn't also characterize the management of intellectual assets, organizations are unable to certify either proper managerial controls or the veracity of the financial reporting document; in doing so, they also renounce the opportunity to monetize and securitize their intellectual capital assets, thus leaving assets underleveraged and unoptimized. Because it is an ethical responsibility to manage and optimize enterprise assets, the failure to do so is an ethical failure on the part of management.

While broad and frequently undefined security interests during the latter quarter of the 20th century would often include statements in contracts that bound or included reference to "all intellectual property," it was only during the 1990s that this practice was replaced by intangible asset-specific agreements that broke new financial and monetary ground by defining, for example, specific patents or trademarks and their assigned values, much as equipment or inventories may be specified in contracts surrounding tangible assets.

Soon thereafter, intellectual assets began to make their appearances as the substance of traditional financial vehicles allowing, for example, royalty streams associated with intellectual property to become securitized in the public markets, intellectual property pools to emerge to set industry or application standards, sales and license-backs of intellectual property to become increasingly common, and intellectual assets to be used to secure debt or as credit enhancements in banking transactions.

The Ethical Future of Intellectual Capital

These and other ethical issues typify the issues of right and wrong in managing intellectual capital assets, which is so important because of their ability, when handled ethically, to enhance the fulfillment of strategic purposes and the creation of new levels of individual and societal prosperity and well-being.

The most optimistic observers have suggested that, just as we watched an Industrial Revolution unfold across the 19th and 20th centuries, the 21st-century economy will, with the rise of intangible assets, behold the unfolding of an era of intellectual capital assets that may last as long as, if not longer than, the former tangible asset era and generate levels of global wealth and human well-being that are as different from the dawning 21st century as that time is from the world of commerce at the beginning of the Industrial Revolution.

It is perhaps no coincidence that intellectual capital has emerged at the same time that tangible assets have begun to approach optimal levels of efficiency and leverage, and the traditional industrial era markets have begun to reach maximum levels of saturation, signaling that maximum possible levels of consumption have been reached.

Thus, the priorities for knowledge, the opportunities for creativity, and the focus of innovation will drive future economic growth. At the turn of the 21st century, the ethics of these increasingly conscious choices are characterized by discussions of corporate social responsibility, personal privacy, intellectual property ethics, environmentalism, globalization, social policy, and the greater good.

Furthermore, the shift to intellectual capital drives a great focus on its means of production—these being thinking, imagination, invention, innovation, know-how, and creativity. Accordingly, ideas and talent will become the currency of an era of intellectual capital that will place a high premium on the ability of individuals to imagine and create. This represents a substantial shift in our modus operandi as a society and will require the development of creative capabilities among many that previously had been limited to the few. Progressively, more corporations are likely to become engines of innovation, increasing the importance of education, while individuals will become more right-brain focused, emotionally intelligent, primarily concerned with meaning and purpose, and alert to the ethical fabric of society.

As intellectual capital becomes the new means of production, and as we shift paradigms from an industrial era and an industrial economy based on labor and tangible assets to a new economy based on intangible assets, information technology, the advancement of knowledge, and the creations of the mind and intelligence will become increasingly essential to the advancement of society, culture, and civilization.

—Lindsay Moore

See also Brands; Capitalism; Conflict of Interest; Copyrights; Corporate Citizenship; Corporate Moral Agency; Corporate Social Responsibility (CSR) and Corporate Social Performance (CSP); Economics and Ethics; Financial Accounting Standards Board (FASB); Globalization; Human Capital; Industrial Revolution; Intellectual Property; Long-Term Capital Management; Mergers, Acquisitions, and Takeovers; Natural Capital; Patents; Sarbanes-Oxley Act of 2002; Securities and Exchange Commission (SEC); Social Capital; Strategic Planning; Trademarks; Trade Secrets, Corporate Espionage and; Transparency; Wealth Creation

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Intellectual Property

Intellectual property, as distinguished from real property, pertains to products of the mind (or intellect)—it refers to those rights or entitlements that attach to intangibles such as artistic expressions and technological inventions. Protection is afforded to intellectual property to encourage development of ideas, expressions, and processes for commercial gain.

Types of Intellectual Property

There are various types of intellectual property. Distinctions are made according to the nature of the proprietary innovation.

Copyrights

Intellectual property such as computer software, video games, songs, and movies are granted legal protection in the form of a *copyright.* A copyright is a set of exclusive legal rights accorded to the expression of a particular literary, artistic, or scientific work. Any moral rights are separate and distinct from the legal rights. The purpose of copyright law is to protect and promote creative endeavors by deterring unauthorized use.

Copyrights are not granted automatically. For material to be protected, it must reflect some degree of originality. Furthermore, copyrights are not indefinite; in fact, they typically expire after a predetermined period of time (typically, 50 years).

A fair use exception excludes some uses of copyrighted material from legal protection. To determine whether the fair use exception applies, the purpose of the use is considered, along with the nature of the work. Copyrighted material is often given fair use treatment when used for educational purposes. Also considered are the proportion used, compared with the size of the whole, and the effect of the use on the potential market for the copyrighted material.

The granting of copyright protection is defended on public policy grounds. First and foremost, copyright law provides an incentive for creators to share their ideas with the public, and, at the same time, it militates against intellectual piracy. Through copyright law, copyright holders can enforce their rights through civil lawsuits.

Patents

Patents are issued with regard to systems, processes, and other inventions. New mechanical contrivances, for example, are appropriate subjects for patent protection. A patent offers the patentee exclusive rights for a defined period of time—often 20 years—in exchange for sharing information with the public about the protected systems, processes, or other inventions. The proprietary right allows the patentee to restrict others from making, using, or selling the patented invention until the term of the patent expires.

A condition for a patent to be granted is that the patentee provide a written description of the invention in sufficient detail so that another person could reproduce that invention. Once a patent is granted, the patentee's rights can be enforced through the vehicle of civil lawsuits.

Four reasons are generally offered to justify the protection of intellectual property rights: disclosure, innovation, product investment, and design development. Generally, patents are given to encourage inventors to share information about their inventions. Through disclosure to the public domain, inventors are able to build on the inventions of others. Without the protection of patents, inventors might be reluctant to share their creations with the public.

Patents are also widely considered economically beneficial. The promise of exclusive rights to an invention is believed to promote innovation of new systems, processes, and devices. This encourages companies to invest in research and development up front because of the anticipated financial returns often linked to the patenting of successful inventions.

Finally, patents arguably provoke new innovations in that, once a patented invention exists, competitors are inspired to develop new designs to work around the patented invention. In this way, the patent system promotes technological progress and economic growth.

Trademarks

A trademark is a distinctive symbol or sign to which commercial value is attached because of the connection between the symbolic representation and organizations, products, or services. Trademarks distinguish organizations, products, and services from those of their competitors. Traditionally trademarks have taken the form of names, phrases, symbols, designs, and images.

The primary purpose of a trademark is to identify organizations, products, and services in the marketplace. Rights are enforced to protect the ability of organizations to benefit financially from their investment in distinguishing their products and services through a brand image from those of competitors. For rights to be enforced, however, trademarks must be registered.

To be registered, a trademark must be distinctive. Fanciful designs and made-up words (i.e., *Kodak* as a camera company) are often de facto eligible for trademark protection. Similarly, arbitrary words (i.e., *Apple* as the name of a computer company) are also considered acceptable, although apparent trademark infringements, as with Apple Records, must sometimes be resolved through negotiation and, often, compensation. Suggestive words (i.e., *Salty* for sailing equipment) can serve as legitimate trademarks, whereas descriptive or generic marks (i.e., *Salty* as used with saltine crackers) are not protected.

Unlike copyrights and patents, trademark rights do not expire within a predetermined time period. For rights to be enforced, however, the trademark owner must continue to use the trademark.

Public policy considerations underlie the granting and enforcement of trademark rights. In fact, trademarks are generally considered to benefit consumers. While companies are able to reap the financial benefits of establishing strong brand reputations and linking those reputations to identifiable trademarks, the consumers benefit from making more informed decisions about the companies, products, and services in which they invest.

Ethical Considerations

The granting of intellectual property rights is often controversial. Assigning rights to intellectual contributions creates negative rights, in that rights attributed to intellectual property involve excluding others from using that property. This can arguably stifle competition and inhibit consumer choice and artistic appreciation.

Furthermore, intellectual property rights are distinguishable from the rights that attach to real property in that their abridgement does not result in harm, other than perhaps the financial loss of opportunity costs to the innovator. Even this is not certain, however. Many musicians, for example, argue that Internet-based file-sharing actually increases their name recognition and the popularity of their songs. When intellectual property is shared or copied, there is no tangible loss.

Not all information, expressions, or ideas are eligible for intellectual property protection. Some argue that the choice of what is protected is arbitrary, serves commercial interests, and is not linked to inherent moral entitlements.

Conclusion

It is generally assumed in the United States that free market societies must protect intellectual property to reward innovation and promote economic growth. Individuals and businesses assume and expect that their information, expressions, and ideas deserve the protection of copyrights, patents, or trademarks. The emergence of the Internet, however, has introduced increasing challenges to this framework. On the one hand, technology facilitates the infringement of digitized intellectual property. At the same time, the Internet increases the exposure of intellectual property to other cultures that have different values and regulations pertaining to intellectual property, its use, and its protection.

—Tara J. Radin

See also Competition; Copyrights; Intellectual Capital; Patents; Piracy of Intellectual Property; Property and Property Rights; Public Domain; Trademarks; Trade Secrets, Corporate Espionage and; Unfair Competition

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Interest Groups

Interest groups are associations of individuals or of organizations that form to advance a common political, economic, or social agenda. The political science discipline sees interest groups as crucial to the American political system and as complementary to the political parties. People organize into associations and interest groups for nonpolitical purposes as well, as part of their economic, social, and religious existence. In the political realm, meanwhile, interest groups articulate and advance the political positions and beliefs of citizens, while the political parties attempt to aggregate those positions into coherent party platforms. For instance, during the New Deal Era, the Democratic Party of President Franklin D. Roosevelt aggregated the interests of farmers, industrial unions, big cities, and the southern states in what was known as the New Deal coalition. Interest groups include professional and occupational associations, business and trade associations, labor unions, farm organizations, religious organizations, education organizations, cause-oriented citizen groups and lobbies, legal foundations, think tanks, and public and private foundations.

Political Pluralism

Political scientists such as David Truman, Edward Banfield, and Robert Dahl have defined the structure of political power in America as political pluralism, with interest groups serving as the foundation of the system. The premises of political pluralism feature the key roles that interest groups play, along the following lines:

- Power is measured by outcomes of decisions—those who occupy formal governmental positions may not exercise as much power as do informal institutions such as interest groups.
- Coalitions of minorities rule on issues—the majority democratic sentiment is not as important in determining policy decisions as the actions of organized and intense publics.
- Different groups dominate on different issues—business may win on some issues, labor on others, and environmental groups on still others.
- Internal divisions within classes exist on issues—even business groups do not march in lockstep and may disagree with one another on trade, regulatory, and antitrust issues.
- Leadership roles and resources differ from group to group—while business may enjoy more economic resources, labor might be able to mobilize more people, and citizen groups might possess greater moral rectitude and commitment.
- Power alignments vary over time—while labor unions possessed more power in the 1940s, social movements exercised more power in the 1960s and 1970s, and business won more political battles in the 1980s and 1990s. Power fluctuates over time, and the political pendulum swings from one era to the next.

Types of Interest Groups

The concerns, issue focus, organizational structure, and tactical approaches vary from one interest group to another, along the following dimensions:

Economic (business, labor)	Noneconomic (cause oriented)
Multi-issue	Single issue
National	Local or grassroots
Mainstream	Activist or militant
Membership	Nonmembership

While economists claim that self-interest drives economic and political decisions, not all groups necessarily focus on economic concerns. While business and labor groups might usually be so driven, the self-interests of other groups might relate to noneconomic causes such as the environment, cultural and historic preservation, or consumer safety and privacy. Regarding issue focus, an environmental group might focus on multiple issues, such as air and water pollution, hazardous waste, and global warming, or it might focus on a narrower single issue, such as rainforest protection or animal rights.

Regarding organizational structure, a business group might be organized solely at the national level, such as the Business Roundtable, a group of 160 corporate CEOs, as might an environmental group, such as the World Wildlife Institute. Alternatively, other groups might organize and be active at the state and local levels, such as the chambers of commerce in virtually all cities and the many state chapters of the Sierra Club.

Most interest groups are in the political mainstream, using an assortment of traditional political tactics that include lobbying and litigation. That would include business and labor groups and even the major national environmental and consumer groups. Such groups lobby both the legislative and executive branches, often including participation in regulatory agency proceedings. Meanwhile, grassroots activist groups often use militant tactics such as protests and boycotts. Such groups include local environmental, civil rights, religious, and consumer groups. Community organizers often focus their protests on specific companies, such as the various campaigns around the country to prevent Wal-Mart from building stores in their communities.

Decentralized groups at the grassroots level usually depend on local memberships for their meager financing, while national groups may be either member or nonmember organizations. Some business groups are confederations of local chapters and/or corporations throughout the country, such as the Chamber of Commerce of the United States. Meanwhile, some citizen groups and think tanks have few or no members at all and rely on foundations, corporations, or wealthy patrons for their funding. Decisions in such groups are more centralized in the hands of founders, key staff members, or board members.

Selective Versus Collective Incentives

Public choice economists who believe that all decisions are based on self-interest argue that interest groups must provide selective incentives to their members or supporters to remain viable. They argue that people will not support groups simply out of altruism. Economist Mancur Olson was the leader of this line of thinking in the 20th century. His theory does not mean that groups cannot organize to protect the collective good, only that such groups must also provide selective benefits to their members. For example, the Sierra Club sponsors trips and wilderness hikes for its members, and even sells merchandise, while also lobbying to protect the environment. Critics of Olson maintain that some cause-oriented groups can and do exist by appealing to the public interest or ideological motivations of their members, demonstrating that certain individuals are not driven simply by self-interest. Meanwhile, it is still possible for cause-oriented groups to evade Olson's dilemma by ignoring any membership base entirely and relying on corporate philanthropy or foundation support for their existence. Most citizen groups have taken just this approach.

Business Groups

Business groups, called trade associations, are specific to a given industry and provide a range of selective benefits to their members. Those benefits include lobbying on issues crucial to their members, proprietary information on industry trends and public policy, and training for and communication with industry members. Other business groups, fewer in number, encompass groups that cut across industries and take positions on issues common to the corporate community. Such groups include the Chamber of Commerce of the United States and the National Association of Manufacturers. They necessarily have a more difficult time arriving at consensus positions with which their diverse memberships agree. Business will also develop formalized or ad hoc coalitions with other corporations on specialized issues. For example, manufacturers that use steel have combined to lobby against protection for U.S. steel producers, and food manufacturers that use sugar have coalesced to oppose price supports and quotas for U.S. sugar growers.

Labor unions have been on a steady decline since the New Deal. Meanwhile, business groups have been on the ascent, especially since 1975. During the 1960s and early 1970s, social movements on civil rights, consumerism, women's rights, peace, and the environment challenged the power of business. Business responded in the mid-1970s by imitating some of the tactics used against it—building grassroots lobbying networks, supporting national and regional litigation centers, developing national and regional think tanks, and engaging in public policy philanthropy. For the first time in any serious way, business joined the fight over the power of ideas.

As business developed a wider range of political tactics after 1975, its agenda of political issues also expanded. No longer was it content to fight narrow battles over tax and regulatory issues. It engaged in battles over grand issues that faced the corporate community in general, such as tort reform, winning more of those battles at the state level than at the federal level. Through organizations such as the Public Affairs Council, the Citizens' Research Foundation, and the Committee for Economic Development, it also joined the debate over campaign finance reform. Finally, in 2005 and for the first time in American history, business through the National Association of Manufacturers and the U.S. Chamber of Commerce lobbied in favor of a U.S. Supreme Court nomination, that of John Roberts for chief justice of the United States.

Interest Groups and Regulatory Politics

Two so-called capture theories reflect the comparative political power of business groups and citizen groups, or of economic and noneconomic groups. One theory applies to economic regulation and the other to social regulation.

Capture Theory and Economic Regulation

The more conventional theory is that of the iron triangle, developed by Nobel prize–winning economist George Stigler, and relates to the political power of business groups over economic regulation. He demonstrated that in industry-specific regulatory agencies, such as the Interstate Commerce Commission, incumbent regulated firms had the incentive and ability to capture the agency established to regulate them. By doing so, they would promote the creation of entry barriers against new competitors and protect existing firms from onerous regulations. The firms in the industry and their trade associations played a dominant role in capturing the agency in question.

The tactics used by the industry were economic in nature—providing important information and future employment to regulators to influence favorable treatment of the incumbent firms and to provide campaign contributions to members of congressional committees with oversight responsibility of the agency, ensuring that the agency would not stray from its favorable treatment of the leading firms. This gave rise to the concept of an iron triangle, with industry at one corner of the triangle extending its influence to the regulatory agency and to congressional committees at the other points of the triangle.

Capture Theory and Social Regulation

A milder form of the capture theory relates to social regulation and speaks to the power of noneconomic citizen interest groups. By its very nature, social regulation is economywide in nature and extends beyond a specific industry. For instance, the U.S. Environmental Protection Agency regulates air pollution caused by a host of industries, from utilities to paper companies to steel companies. The agency's broad scope necessarily lowers the incentive for any particular company or industry to attempt any capture of its policies. Environmental and health groups, however, have a far greater incentive since they have a wider range of interests in the agency's decisions. Hence, they will consistently be policy actors in agency decisions.

Although they lack the economic clout and resources of industry as tools of influence, citizen groups do possess other tools and can provide negative incentives to prevent the agency from violating the public good and showing any favoritism to industry. Those negative incentives include lobbying and litigation and, most important, exposure and negative publicity. In such campaigns, the news media serve as willing collaborators with citizen groups and as a transmission belt for any negative information. Hence, the political actors at the various points of the social regulation triangle now change to become the agency, citizen groups, and the media.

Certainly, these alternative capture theories do not fully explain any particular agency decision, whether in the context of economic regulation or of social regulation. The influence of business in economic regulatory decisions and of citizen groups in social regulatory actions might be overwhelmed by other variables specific to a given policy dispute. However, the logic of the two theories does help explain the overall difference in decision patterns in economic regulations and social regulations. The political backlash to the tighter iron triangle of economic regulation also explains the wave of economic deregulation that existed from the late 1970s onward. After exposing the nefarious impacts of the iron triangle, economists and other policy analysts were able to overcome the power of special interests through the power of good ideas to create economic deregulation.

Interest Group Values

One way of comparing the values related to the universe of interest groups is through application of the values of liberty, equality, efficiency, and community. Civil liberties groups such as the ACLU and libertarian think tanks such as the Cato Institute relate of course to liberty. Civil rights groups and some labor unions advocate equality concerns. Business typically adheres to efficiency interests, while environmental groups that promote better quality of life relate closely to communitarian values. Obviously, some groups would represent a hybrid set of related values. Many human rights groups, for instance, would embrace both communitarian and egalitarian values, while many business groups would embrace both efficiency and libertarian values.

—John M. Holcomb

See also AARP; American Bar Association; American Federation of State, County and Municipal Employees; American Federation of Teachers; American Institute of Certified Public Accountants (AICPA); American Medical Association (AMA); Association of Trial Lawyers of America (ATLA); Business Roundtable; CFA Institute; Chamber of Commerce of the United States; Iron Triangles; National Association of Securities Dealers (NASD); National Federation of Independent Business; Nongovernmental Organizations (NGOs); Revolving Door; Trade Associations

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INTERGENERATIONAL EQUITY

Intergenerational equity is a conception of justice or fairness regarding the distribution or the availability of material and social goods for future generations. According to proponents of this concept and its application, members of each generation possess a natural and cultural inheritance from past generations and, thus, are beneficiaries as well as custodians with a duty to pass along key aspects and benefits of this heritage to future generations. Issues pertaining to the concept of intergenerational equity that have been raised and debated include ecology and sustainable development, income or social security, accumulation and payment of national debt, educational investments, health care, and technological risks and benefits.

Although obligations to future generations have long been expressed in political philosophy and governance documents, the concept of intergenerational equity has received spirited attention in recent decades. Some of this attention extends from the work of John Rawls and his concern for this and other forms of distributive justice. Intergenerational equity has been discussed, though, from various ethical theories: utilitarianism, deontology, social contract, the ethics of caring, and virtue-centered ethics. For example, justice or equity might be considered among virtues, such as compassion, that could be demonstrated toward those in future generations.

The issue of intergenerational equity with regard to the natural environment arose during the 1972 Stockholm Conference on the Human Environment. This conference led to the creation of the United Nations Environment Programme (UNEP) and the application of the concept of intergenerational equity to part of developing international law concerning the natural environment. The UN-sponsored Brundtland Commission released a report in 1987 urging that economic development take into account planetary ecological limits. The report popularized the conception of sustainable development as development that meets present needs without compromising the ability of future generations to meet their own needs.

Advocates for intergenerational equity have claimed that market mechanisms cannot ensure that certain scarce resources are protected for future generations. Multiple business competitors over time can deplete natural or cultural resources through a "tragedy of the commons" effect. Short time frames and narrow interests in conceptualizing organizational goals, along with uneven power distributions among those making important decisions concerning resource usage, are among the factors commonly cited as criticisms of typical marketplace processes. Those supporting a strong position on intergenerational equity and sustainable development stress that each generation should conserve levels of the diversity, quality, and human accessibility of natural resources so as not to restrict the options available to meet the needs and values of future generations.

Alternative positions that argue for fewer obligations or sacrifices toward future generations include those who believe that (1) present consumption should not be constrained since it is not certain that future generations will exist, (2) unconstrained present consumption will not diminish the well-being of future generations, or (3) future technological innovations will provide for acceptable resource substitutions in the future. Robert Solow, as a prominent economist, for example, expresses technological optimism with regard to issues of intergenerational equity as well as emphasizes the difficulty for decision-making or policy-making purposes of knowing or predicting the preferences and values of future generations.

Proponents of the concept of intergenerational equity have difficult challenges in developing effective decision processes for actually implementing this concept. Human biases and differences in perceptual/cognitive frames influence actual decisions that are made with regard to potential impacts on future generations, and such biases can lead to disagreements concerning types and degrees of future obligations. Problems of stakeholder representation and forms of accountability hinder more satisfactory decisions. Future generations cannot actually be represented in critical decision-making forums, and therefore the potential interests and values of future generations in these processes can fail to be raised. Strong advocates of intergenerational equity seek ways of improving representation for future generations in the marketplace as well as in political, legislative, and judicial decision processes. This representation would involve broader stakeholder participation in improved decision processes that have longer time horizons and that more thoroughly consider diverse gains and consequences of these decisions. Broader stakeholder representation in such important decisions also affects "buy-in" or willingness to commit to sacrifices or discipline that might be necessary to achieve more intergenerational equity. Fuller representation might come from special interest groups or advocates. One example of an intergenerational interest group is the Foundation for the Rights of Future Generations (FRFG). Established in 1996 as a "think tank" and an agent for social and political change in support of intergenerational justice and sustainability, FRFG is based in Germany and has members around the world. The organization rejects notions of generational war, has a culture of discussion and dialogue, and focuses on learning about intergenerational issues and change.

Beyond specific representation or broader stakeholder participation in decision-making processes, other changes have been suggested by proponents for intergenerational equity to establish and implement improved policies. Even aspects of the role and functioning of existing institutions have been questioned, particularly current applications of particular institutional tools and instruments, such as regulations, taxes, laws, standards, incentives, and investments in R&D.

There is limited agreement among theorists in various academic disciplines on better approaches to calculating and comparing opportunities for welfare or well-being across many generations. The issue of fairness across generations has been studied through forms of measurement of the aggregate welfare or quality of life that has been and might be available to cohorts living in different generations. Economists generally favor forms of utility comparison using quantitative approaches and assumptions of exchangeabilty or fungibility of different forms of capital. Some suggest the creation of trust funds or capital savings over time to compensate for the loss of natural or cultural resources. These economic approaches of quantitatively accounting for future utilities relative to present utilities through substituting and discounting mechanisms have been criticized, though. Although appropriate for certain types of cost-benefit and other economic analyses, such discounting of future well-being into a present value scheme has been questioned when applied to public versus private goods and in the case of multigenerational time dimensions.

Environmental advocates often insist that a set of natural or ecological qualities should be saved for future generations since this natural capital cannot easily or simply be exchanged or compensated through other forms of capital. Complications for comparisons of utility or other forms of well-being across generations generally involve lack of knowledge about the future. Questions include the following: How far might obligations extend into distant generations? What identities, characteristics, and needs might these people actually have? To what extent can we anticipate the effects, many unintended, of present decisions on future conditions?

Business or private sector participation in recent international deliberations on sustainable development, such as in the Johannesburg Summit in 2002, has been increasing. Improved dialogue and learning by business and other relevant stakeholders concerning the complex factors and difficult choices associated with responsibility for future generations has been emphasized by those advocating intergenerational equity.

—Stephen L. Payne

See also Discounting the Future; Duty; Environmental Ethics; Rawls's Theory of Justice; Sustainability; Tragedy of the Commons

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INTERNAL AUDIT

Internal auditing has two key functions. First, it provides management with information on the extent to which the control systems are working effectively. This is especially relevant for those responsible for the governance of an organization. Second, it can deliver advice to management for improvements in the functioning of control systems.

An internal audit is executed mainly by people working within the organization. In contrast, external or independent audits are performed by public accounting firms. External audits attest to and report on the effectiveness of internal controls to the audit committee and the company's officers as part of the preparation and issuance of an annual report. The cooperation between internal and external auditors may be restricted depending on applicable regulatory requirements. In general, the information of internal auditing activities can be passed on to the external auditors to review whether the controls of the audited company are adequately evaluated and documented.

Internal control systems relate to the policies, procedures, practices, and organizational structures and are designed to provide reasonable assurances that business objectives will be achieved and that undesired events will be prevented or detected and corrected. Generally, effective control systems require seven coherent elements:

1. Compliance with norms and procedures to prevent violations of the law
2. Organizational leadership that promotes a culture of compliance
3. Screening of employees in high-risk functions
4. Training, education, and communication over compliance norms
5. Internal monitoring and auditing
6. Maintenance of appropriate disciplines and incentives
7. Corrective actions when violations occur

Internal auditing is thus a part of the comprehensive internal control systems. Interactions between the elements of the control systems are crucial, and therefore internal auditors need to cooperate with all those involved.

The application of internal auditing activities has accelerated due to the imposition of standards and regulations requiring organizations to demonstrate the effectiveness of their control systems. The Federal Sentencing Guidelines (United States), effectuated in 1991, the Cadbury report (United Kingdom), published in 1992, the COSO report (United States), published in 1992, and Sections 302 and 404 of the Sarbanes-Oxley Act, enacted in 2003, are especially relevant in this respect.

The main social function of internal auditing reflects its added value for stakeholders of organizations in demanding that boards demonstrate publicly that they are in control of their organizations. To fulfill this function, internal auditors need to apply and uphold ethical principles of integrity, objectivity, competency, and confidentiality. To achieve this, it is important that the internal audit function be adequately resourced and competently staffed, and that it have direct reporting lines to the audit committee, the board, and the chief executive officer.

Internal auditing professionals are internationally represented by the Institute of Internal Auditors (IIA), established in 1941. Internal auditing is used increasingly in privately owned organizations and governmental and nongovernmental institutions. In 2005, the IIA represented more than 100,000 auditors in 160 countries.

—*Andre H. J. Nijhof*

See also Corporate Ethics and Compliance Programs; Corporate Governance; Ethics Training Programs; Federal Sentencing Guidelines; Sarbanes-Oxley Act of 2002; Social Audits; Total Quality Management (TQM)

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INTERNAL REVENUE SERVICE (IRS)

The Internal Revenue Service (IRS) is the largest bureau within the U.S. Department of the Treasury and is responsible for enforcing federal statutes relating to the reporting and remission of income and other taxes by individuals and organizations through the promulgation of treasury regulations to interpret and apply these statutes, and through the administration of procedures collecting taxes and transferring them to the U.S. Treasury.

Predecessor Institutions to the IRS

On August 5, 1861, the Revenue Act of 1861 imposed an apportioned real property tax, and the first federal income tax, to finance the prosecution of the Civil War. The income tax portion was a flat tax, but the federal government did not establish the infrastructure to collect it before July 1, 1862, when the Revenue Act of 1862 superseded this act with a progressive scheme of taxation and withholding requirements for employers. The 1862 act also created the Bureau of Internal Revenue (BIR), a federal agency for collecting the tax, under the leadership of a commissioner of internal revenue. Due to the unpopularity of the tax, and changing budgetary needs of the government, this legislation underwent almost annual amendments through 1870, and in 1872, Congress allowed it to expire.

In 1894, Congress passed the Wilson Tariff Act, which reinstated the income tax, and created a dedicated income tax division within the BIR. However, 1 year later, in *Pollock v. Farmers' Loan & Trust Co.,* the Supreme Court struck down the new tax as unconstitutional because it was a direct tax and not proportionate to the respective populations of the states. With the tax defunct, the BIR dismantled the income tax division.

In 1909, President Taft promoted a constitutional amendment to authorize the federal government to impose income taxes directly, without the sort of apportionment requirement that the Supreme Court had raised in its ruling in the *Pollock* case. That same year, Congress enacted a 1% tax on net corporate incomes exceeding $5,000. With Wyoming's ratification of this 16th Amendment to the Constitution in 1913, Congress acquired the power to enact a broad-based income tax. It repealed the corporate income tax of 1909, and it imposed an income tax on natural persons of 1% of net personal income exceeding $3,000, with a surtax of 6% for incomes greater than $500,000. That year marked the publication of the first Form 1040, a tax form for individuals for reporting their income and calculating and remitting this tax.

The Revenue Act of 1918 codified and systematized the tax laws then in force and created a progressive income tax scheme with a marginal rate of 77% for the BIR to administer, largely to finance the nation's effort in World War I.

The following year, a sufficient number of states ratified the 18th Amendment, rendering illegal the manufacture, sale, transportation, importation, or exportation of alcoholic beverages, and this began the Prohibition era. The responsibility of enforcing Prohibition fell on the commissioner of internal revenue, pursuant to the Volstead Act, which Congress passed in 1919. It would be more than one decade before the Department of Justice would assume this duty. In the meantime, the BIR participated in law enforcement activities, including an undercover operation through its intelligence unit that gathered evidence for the eventual conviction of gangster Al Capone.

The tax rate had declined dramatically after the war, to 24% by 1929. It rose again during the 1930s, to help finance the New Deal. With the repeal of Prohibition in 1933, the BIR resumed collecting taxes on alcohol, and it also assumed this responsibility for taxes on tobacco and for enforcing the National Firearms Act. It would remain responsible for these duties until its Alcohol, Tobacco, and Firearms Division would split off to become a separate federal bureau in 1972.

Through the early 1940s, the scope for income taxation on individuals remained modest, with a small percentage of the population paying the tax. By the end of World War II, most of the working population was paying some tax. To manage the growing burden on the BIR arising from the dramatic increase in the reporting and remission of taxes, Congress passed the Current Tax Payment Act of 1943, which formalized the requirements for employer withholding of income taxes and estimated quarterly payments by taxpayers whose income did not fall under this regime.

Establishment of the IRS as a Nonpartisan, Civil Service Agency

The BIR had operated according to a political patronage system through World War II. In 1952, President Truman promoted a plan to restore public confidence in the bureau by reorganizing it, decentralizing its services, and professionalizing its workforce by bringing it within the career civil service system. President Eisenhower endorsed the plan the following year and changed the bureau's name to the "Internal Revenue Service." The institutional role for the IRS has been to implement policy, rather than to formulate it, and, since that time, only the commissioner and general counsel have been political appointees, subject to Senate confirmation.

The IRS has largely conformed to this nonpartisan, civil service role, despite periodic scandals, for example, President Nixon's pressure on Commissioner Donald C. Alexander to use the IRS to intimidate his political enemies in the 1970s and the October 2006 order of Commissioner Mark W. Everson to suspend tax collection actions against delinquent taxpayers until after the fall 2006 midterm elections, during the second Bush administration. The latter incident elicited heated criticism from four former commissioners from both political parties for its damage to the reputation and credibility of the IRS as an impartial agency.

Modernization of the IRS and Expansion of Its Operational Scope

The IRS made its first major investment to enhance its technological infrastructure by opening the National Computer Center in Martinsburg, West Virginia, in 1961. Four years later, it began to offer toll-free telephone support for taxpayers. In 1986, the IRS began to allow some taxpayers to file their returns electronically. By the early 2000s, it was actively encouraging individuals to file electronically, and it was imposing electronic-filing requirements on corporations, including exempt organizations, in phases.

With the passage of the Employee Retirement and Income Security Act in 1974, Congress assigned responsibility to the IRS for the formidable task of regulating employee benefit plans.

Major Changes in Tax Policy and the Implicit Repoliticization of the IRS

During the Reagan and first Bush administrations, the concern for controlling the spiraling federal budget deficit and the objective of reducing the proportion of the tax burden on capital and corporate interests led to several landmark pieces of legislation, including the Economic Recovery Tax Act of 1981, the Deficit Reduction Act of 1984, the Tax Reform Act of 1986, the Omnibus Budget Reconciliation Act of 1987, the Technical and Miscellaneous Revenue Act of 1988, the Revenue Reconciliation Act of 1989, and the Omnibus Budget Reconciliation Act of 1990. The legislation that passed early in the Reagan administration heralded dramatic decreases in several taxes, with an uncertain legacy in terms of the putative objective of promoting economic growth. The 1990 act raised some taxes slightly, and support for this legislation from President George H. W. Bush reflected a reversal of a campaign pledge, a change in position that harmed his credibility among the public and likely contributed to his loss during his reelection bid in 1992.

To help justify their positions on tax policy, President Reagan, President George H. W. Bush, and other leaders in Washington characterized government agencies, including the IRS, as institutionally dysfunctional and inherent impediments to economic growth and personal initiative. This ethos reflected the ambivalence of the American electorate toward the IRS and the tax system. On one hand, there was a desire to enhance the effectiveness and fairness of the tax collection process and to ensure that every taxpayer paid an appropriate share of taxes. On the other, there was a concern for the negative effects of taxation on economic growth and for the impliedly menacing presence of an active IRS bureaucracy.

This ambivalence among the public and the combative rhetoric of politicians regarding tax policy and the IRS increased pressure on the organization and dampened the morale of many of its employees in the 1980s and 1990s. Meanwhile, although these pieces of legislation led to some efficiencies in the administration of tax laws and the collection of taxes, the budget deficit continued to grow, in part because of escalating military expenditures and health care costs and the acute recession from 1990 to 1992.

With the passage of the Omnibus Budget Reconciliation Act of 1993, and the tax revenues and reduced welfare costs arising from the formidable economic expansion of the 1990s, President Clinton and

Congress were eventually able to eliminate the budget deficit and realize the first budget surpluses in many years. During this period, the IRS also pursued several initiatives and enforcement actions to increase its efficiency and effectiveness in collecting taxes, including renewed attention to international transactions, payments for personal services, investigations of tax shelter abuses, and operations of exempt organizations.

Major Enforcement Activities and Organizational Developments After the Mid-1990s

The impetus for IRS scrutiny of exempt organizations arose out of numerous high-profile scandals affecting religious, charitable, and educational organizations and led to the Coordinated Examination Program (comprehensive multiyear audits) for universities. Other products of this period were legislation and regulations in the mid-1990s to impose "intermediate sanctions" on leaders of exempt organizations for "excess benefit transactions," that is, excessive salaries and benefits. These sanctions were "intermediate," in that they were less than revocation of an organization's exempt status (the principal previous remedy), but were more than doing nothing. These sanctions applied to the individuals who realized these inappropriate benefits, rather than to the exempt organizations themselves. After another round of high-profile scandals in the early 2000s involving exempt organizations, Congress and the IRS again moved to stiffen public- and private-sector compliance requirements involving this sector, which by 2003 managed approximately $2 trillion of assets.

The IRS Restructuring and Reform Act of 1998 dramatically reorganized and modernized the IRS according to progressive management practices in the private sector, to reflect a stronger customer service focus by migrating toward a functional configuration and away from the traditional geographic model. It took about 2 years for the IRS to implement many of the changes, including reconfiguration into four main sections: (1) Wage and Investment Income, (2) Small Business/Self-employed, (3) Large and Mid-size Business, and (4) Tax Exempt and Government Entities. This legislation also enumerated a "Taxpayer Bill of Rights" to establish standards for due process in dealing with taxpayers and to encourage taxpayers to seek assistance from the IRS without fear. These standards arose out of public- and private-sector discussions beginning in 1981 and built on formal versions from 1988 and 1996.

In the wake of the terrorist attacks of September 11, 2001, an additional mandate for the IRS was that of assisting in monitoring transactions, especially involving international payments to and from putative charities, ensuring compliance with exempt organization tax laws and regulations, and remaining vigilant for abuses that supported funding for terrorist activities around the world. When it discovered suspicious activities, the IRS worked closely with domestic and foreign law enforcement agencies to investigate them and to take enforcement action when necessary. These efforts were in addition to increasing cooperation with fiscal authorities around the world over many years to conclude, administer, and enforce tax treaties and other cooperative agreements.

Among the more controversial initiatives within the IRS in the early 2000s was the project to privatize some collections activities, a process that got under way in the fall of 2006. A handful of private collections agencies received thousands of names of taxpayers with delinquent balances of $25,000 or less that the taxpayers did not contest, along with private information about the taxpayers to enable collection of the debts. The agencies' contracts with the IRS called for them to retain fees of almost 25% of the amounts they collected. While the IRS said that it did not want to resort to this method for collections, at a minimum because it was more expensive, it said that it had no alternative because of Congress's refusal to appropriate funds for additional revenue officers.

The Contemporary Mission and Operations of the IRS

The IRS describes its contemporary mission as follows:

> Provide America's taxpayers top quality service by helping them understand and meet their tax responsibilities and by applying the tax law with integrity and fairness to all.

This mission statement describes the IRS's role and the public's expectation about how the IRS should perform that role:

- In the United States, Congress passes tax laws and requires taxpayers to comply.
- The taxpayer's role is to understand and meet his or her tax obligations.

- The role of IRS is to help the large majority of compliant taxpayers with the tax law while ensuring that the minority who are unwilling to comply pay their fair share.

Internal Revenue Code Section 7801(a) authorizes the secretary of the treasury to administer and enforce the internal revenue laws of the United States. This is the statutory authority that underwrites the existence of the IRS. Section 7803(a) provides for the appointment of a commissioner of internal revenue to administer and supervise the execution and application of the internal revenue laws.

Among the means for executing and applying these laws is the promulgation of treasury regulations to interpret and apply the Internal Revenue Code, as amended. The IRS also publishes administrative rules in the form of revenue rulings and private letter rulings. The former, just like treasury regulations, can furnish reliance for taxpayers generally, while the latter are valid only for the parties to whom the IRS issues them. The IRS regularly publishes its announcements and pronouncements in the *Internal Revenue Bulletin,* and it provides additional procedural guidance for taxpayers in its *Internal Revenue Manual* and by issuing revenue procedures, tax counsel memoranda, and technical advice memoranda.

In addition to its headquarters in Washington, D.C., the IRS maintains dozens of field offices in and around federal buildings, military bases, diplomatic posts, and other facilities around the world, as well as regional service and processing centers to process returns and applications, to respond to taxpayer inquiries, to conduct research, and to perform other taxpayer services.

—Lester A. Myers

See also Double Taxation; Economic Recovery Tax Act (ERTA); Flat Tax; Nonprofit Organizations; Regressive Tax; Regulation and Regulatory Agencies; Tax Ethics; Tax Havens; Tax Incentives; Tax Incidence; Tax Reform Act of 1986

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International Business Ethics

The question of what ethical norms, if any, should guide the conduct of business across national boundaries is the primary subject of international business ethics. We live in an era of increasing economic globalization. While trade among nations has been an important feature of the global economy for centuries, recent years have seen a rapid increase in international trade. Multinational corporations (MNCs) are powerful actors on this global stage, and their influence is increasing. Outsourcing of the production of consumer goods to developing nations is a standard feature of nearly all MNCs that design, market, and sell apparel, footwear, electronics, toys, and household goods. In response to increased demand for natural resources, MNCs in the extractive industries have increased their exploration and extraction operations throughout the world. And, increasingly, all MNCs that market to individual consumers are targeting relatively affluent consumers across national boundaries. These are staple features of the global economy. Typically such globalizing strategies enable MNCs to meet increased demand, offer goods and services to customers at lower prices, and at the same time enhance their own profits.

MNCs operate in a multitude of political jurisdictions and so are subject to a multitude of legal frameworks. Frequently, the laws regarding matters such as the treatment of customers, the treatment of employees, and protection for the environment are significantly different in different host nations. In the case of developing economies, consumer protection, worker safety, and environmental safeguards are often poorly developed or nonexistent. Even when such laws exist in developing nations, the law enforcement and judicial apparatus necessary to ensure compliance does not exist. MNCs operating in such nations are often free to determine for themselves whether or not they will adhere to host nation laws. As a result, MNCs must determine for themselves what minimum moral standards ought to be adhered to in their global operations.

Global Justice

Global justice has become a centrally important issue in moral and political philosophy in the era of economic globalization. The facts that inspire much contemporary work on global justice are increasingly well known. Nearly 1 billion people are malnourished and without access to safe drinking water. Approximately 50,000 human deaths per day are attributable to poverty-related causes. When the attention of trade economists is called to these stark facts regarding global poverty, they are wont to point to the need for economic liberalization in the interest of job creation in the world's poorest nations. They argue that the exploitation by MNCs of cheap labor supplies, abundant natural resources, and lax regulatory regimes allows developing countries to expand export activities and to improve their economies. This economic growth brings desperately needed jobs, which cause labor markets to tighten, which will eventually force MNCs to improve the treatment of workers to attract workers. As wages rise, workers spend more and local economies expand. However, the present-day costs in human health and welfare of such development schemes are frequently at odds with basic ethical norms. Workers are often treated as disposable tools, and local environments are often polluted in ways that harm human welfare and inhibit future well-being. Furthermore, critics of this strategy of alleviating global poverty point out that the global labor supply is so vast that the theoretically sound idea that tighter labor markets alone will lead to improved working conditions is, in practicality, implausible.

Most of the philosophical literature concerning global justice may be divided into two competing views. First, proponents of the *cosmopolitan* view maintain that a system of global socioeconomic justice must be grounded in core ethical norms such as respect for basic human rights. Cosmopolitans see political institutions as a means of ensuring respect for such universal norms. Nation-states that contribute to the violation of basic rights, or merely tolerate the violation of such rights, are problems that must be overcome. Typically, cosmopolitans advocate a global system of government, such as a federal system, that has both the power and legitimate authority to compensate for failed states, stabilize weak states, and successfully coerce successful states into respecting relevant ethical norms. Furthermore, some prominent cosmopolitans regard a global government as an effective means of imposing a global fair distribution of wealth via taxation of the world's affluent populations and redistribution of those resources to the world's poor.

Second, proponents of the *political* view of justice maintain that a system of global socioeconomic justice should be grounded in political systems, rather than in core ethical norms such as human rights. Essential to the legitimacy of political systems in this view is the idea that state legitimacy is grounded in the democratic origins of the political systems. Proponents of this view of global justice, such as John Rawls, maintain that justice should be understood exclusively as a political value, rather than a moral value. They see justice as a virtue of sovereign states, one that legitimately extends to the citizens of such a state as a result of the willingness of citizens to honor the laws of the state and defend it against the aggression of other states. Socioeconomic justice, in this view, is the product of shared political relationships; as such, obligations of justice do not extend to noncitizens.

Protagonists on each side of the debate over global justice focus mainly on the obligations and interrelationships of nation-states and to a lesser extent on the obligations of individual persons. However, nonstate actors such as MNCs also have a profound influence on global justice. MNCs have capacities that enable them to have a significant impact on global justice. First, MNCs and their contractors employee hundreds of millions of workers and as such have a direct impact on the welfare of those workers. Second, MNC environmental practices have a direct impact on both the local communities in which they operate and the entire global community insofar as those practices have an impact on global climate change. Third, MNCs manufacture countless products, such as pharmaceuticals, water filtrations systems, high-yield crops, and wireless global communication systems, that can be used to dramatically improve the welfare of the world's poor. Finally, MNCs wield considerable coercive influence over sovereign-state governments, local governing authorities, political elites, labor unions, contractors, and individuals. The coercive influence that modern MNCs are inherently capable of wielding is not grounded in military power but rather economic power. This influence has been used to enhance the profits of individual MNCs and their owners, but it has also been used to improve the welfare of the citizens of the nations in which MNCs operate. Stories of MNCs engaging in the unjust exploitation of workers, despoiling local environments, and illegitimately interfering in the affairs of sovereign states are commonplace. Less well known are stories of MNCs employing legions of workers at just wages and in safe and humane working conditions, engaging in sustainable environmental practices, and cooperating with the needs and demands of local governments. MNCs are capable of respecting basic ethical norms and of acting as agents of global justice, yet the global justice literature has largely ignored these important global actors.

Proponents of the political view of justice, such as John Rawls, are least well equipped to account for the role of MNCs in promoting global justice. This is because MNCs are transnational actors operating across national boundaries. While MNCs are legitimately subject to the conceptions of justice of the sovereign states in which they are based, they are normally free to ignore that system of justice when they operate outside the political boundaries of that state. Furthermore, MNCs based in democratic nations frequently operate in developing nations that lack basic democratic institutions such as equal voting rights, multiple political parties, democratic elections, politically neutral militaries, and an independent judiciary. The laws in place in these nations lack democratic legitimacy. The concern here is not merely that the laws of nondemocratic regimes lack legitimacy, but that in the absence of such legitimacy proponents of the political view of global justice can offer MNCs no guidance regarding the appropriate norms of behavior in such nations. Of course, a single world government, the political legitimacy of which is grounded in the democratic will of the global population, could provide the necessary guidance. However, such a solution is not regarded as realistic by many theorists and is regarded by others as one of the worst possible solutions to global injustice given the loss of sovereignty this would entail.

Proponents of the cosmopolitan view are better equipped to account for the role of MNCs in promoting global justice than are proponents of the political view. Since cosmopolitans maintain that there are core ethical norms that ought to be respected by different political systems, the fact that some political systems lack democratic legitimacy poses less serious challenges. The crucial step here is to recognize that MNCs, and not merely states, can act as agents of global justice. We can see this better if we imagine a democratically legitimate but weak state. Typically, weak states lack the institutional means to act as a proper agent of global justice. For example, such a state may be unable to protect the basic rights of its workers or to protect its environment against toxic pollution. An MNC that operates in such a state may be better equipped than the local government to ensure that basic ethical norms are adhered to in its operations. Similarly, MNCs that operate in states that lack democratic legitimacy are in a position to model respect for core ethical norms in their operations. In doing so, they may advance the cause of global justice in even the most transparently illegitimate nation-states.

Ethical Norms

If the claim that MNCs are properly regarded as agents of global justice subject to the constraints of ethical norms can be established, it is still necessary to identify those ethical norms. One common view regarding the ethical norms that corporate managers must adhere to holds that it is the obligation of managers to maximize profits while adhering to certain side-constraints on their actions. Proponents of this view typically emphasize the positive impact corporations can have on the welfare of society and argue that managers who expend corporate resources on activities that are not focused on corporate profits are, in effect, stealing from shareholders. Typically, defenders of this view adhere to broadly libertarian attitudes toward markets, governments, and individuals. Libertarians hold that it is the obligation of publicly held corporations to maximize profits for shareholders within the bounds of certain moral side-constraints. The most well-known defender of this view is Milton Friedman, whose stockholder theory of the corporation remains influential despite having been subjected to significant criticism. In *Capitalism and Freedom,* Friedman argues that the normative function of the corporation is to use its resources and engage in activities designed to increase its profits so long as it stays within the rules of the game, which is to say, engages in open and free competition, without deception or fraud. The rules are determined by the will of the majority of citizens in democracies. Actions that do not violate these rules are permissible, whereas actions that violate them are not.

As Denis Arnold has argued, this view provides no guidance for MNC managers operating internationally. This is because, as was noted above, many nations in which corporations operate lack democratic institutions. Furthermore, he argues that even if such a democracy were found to exist, one that acted always in a manner consistent with the will of the people and never at the behest of corporate lobbyists, basic ethical norms would still need to be operative irrespective of the will of the people. For example, one's liberty right should trump a majority of citizens in a democratic society who approve of slavery.

The United Nations "Draft Norms"

One set of ethical norms that is a prominent feature of contemporary public discourse, especially as it pertains to globalization, is that of human rights. The promulgation of the United Nations Universal Declaration of Human Rights, together with the advocacy of organizations such as Amnesty International and Human Rights Watch, has led to the widespread acceptance of human rights as a basic tool of moral evaluation by individuals of widely divergent political and religious beliefs. This increased popular attention to human rights has prompted a resurgence of interest in theorizing about human rights in recent years.

The UN Declaration of Human Rights has well-known conceptual limitations. First, it presents a list of rights that would ideally be granted to individuals (e.g., the right to paid vacation time) rather than a rigorously grounded set of core ethical obligations. Second, the U.N. Declaration does not distinguish between the ethical obligations of different global actors and instead implicitly concerns itself with the obligations of nation-states to their citizens. More recently, the U.N. Working Group on the Methods and Activities of Transnational Corporations has produced "Draft Norms on the Responsibilities of Corporations and Other Business Enterprises With Respect to Human Rights." These draft norms articulate a robust list of ethical obligations and specifically identify MNCs as responsible for their fulfillment. Furthermore, once adapted, adherence to these norms on the part of corporations is to be monitored and verified by the United Nations. The list of basic rights identified by the Working Group includes rights that enjoy relatively universal acknowledgment in a wide range of regional and international codes, and agreements such as equal opportunity, nondiscrimination, collective bargaining, and safe and healthy working environments. However, the Draft Norms go well beyond this, stipulating, for example, that corporations must

- seek to ensure that "the goods and services they provide will not be used to abuse human rights";
- contribute to "the highest attainable standard of physical and mental health; adequate housing; privacy; education; freedom of thought; conscience and religion" for all people; and
- ensure that "human rights, public health and safety, bioethics, and the precautionary principle" are respected in all their environmental practices.

Unsurprisingly, the Draft Norms have met with strenuous resistance from business interests. Part of this resistance is due to the fact that the Draft Norms attribute such a wide and imprecise range of obligations to MNCs and do so without the benefit of a conceptual scheme for distinguishing between the basic ethical obligations of MNCs on one hand and states on the other.

Integrative Social Contracts Theory

One influential view among social scientists working in business ethics is integrative social contracts theory (ISCT). Developed by Thomas Donaldson and Thomas Dunfee, this social contracts approach for determining the ethical norms for economic ethics has three core components: hypernorms, macrosocial contracts, and microsocial contracts. At the global level, there are "hypernorms." These are the fundamental principles or norms by which lower-order norms are to be derived. The sources of these hypernorms are intentionally left unspecified by Donaldson and Dunfee. Hypernorms are divided into three distinct categories: procedural, structural, and substantive. Procedural hypernorms set the terms for contracting microsocial contracts implied in the macrosocial contracting situation. The terms specified are the right to exit the microsocial community and the right to exercise one's individual voice within the microsocial community. Structural hypernorms are described as the principles that support the core background institutions of society. These include the right to property, the right to fair treatment under the law, and necessary social efficiency. Finally, substantive hypernorms specify fundamental conceptions of the right and the good, especially with respect to economic activity.

These hypernorms are derived from outside the macrosocial contracting situation. Substantive hypernorms such as prohibitions against bribery and gender discrimination are said to emerge from the convergence of religious, cultural, and philosophical beliefs around certain core principles.

Hypernorms are identified and validated by macrocontractors who are imagined to convene in a sort of parliament of humanity. These rational global contractors would, according to Donaldson and Dunfee, derive a macrosocial contract for economic ethics that gives moral free space to microsocial economic communities so long as the microsocial contracts were compatible with hypernorms and authentic local norms. By microsocial contracts, they mean the extant agreements, both formal and informal, that exist within companies, industries, and other economic groups. The hypernorms agreed to by macrosocial contractors are necessarily general and lack specific moral guidance.

As a system of international business ethics, ISCT has been criticized on two primary grounds. First, several theorists have argued that it is relativistic with respect to substantive hypernorms and thereby fails to meet the theory's own internal standards of viability. Second, critics of ISCT argue that by invoking religious and cultural norms as a basis for hypernorms, while eschewing traditional ethical theory, ISCT fails to provide reasonable grounds for businesses operating on the global stage to adhere to any one set of hypernorms. In defending ISCT against criticism, Donaldson and Dunfee deny that their theory is relativistic and point out that their theory is the first to focus on the relevance of microsocial contracts in everyday economic life.

Kantian Rights and Duties

Kant's second formulation of the categorical imperative famously holds that individuals must always "act so that you treat humanity, whether in your own person or in that of another, always as an end and never as a means only." This principle constitutes the core of the Kantian doctrine of respect for persons. Respecting people requires honoring their humanity, which is to say it requires treating them as ends in themselves and not merely as a means to an end. This means that it is impermissible to treat persons as mere tools for the accomplishment of one's own ends. Kantians believe that persons ought to be respected because persons have a unique dignity that mere objects lack. Persons have dignity because they are self-governing beings.

Kantian agents act autonomously, and when they do so the principles they act on are grounded in morality rather than in mere inclination. Considering the proper role of self-interest will help clarify this point. Kantians hold that it is wrong to act out of self-interest when doing so conflicts with certain impartially determined moral norms such as respect for other persons. For example, suppose that a supply chain manager knows that he will be rewarded with a significant bonus if he can reduce costs by 19%. In pursuit of this bonus he decides to impose a unilateral 10% cut in the amount the MNC pays a major supplier for apparel of the same quality and quantity as before. The supplier faces the same material and energy costs and is already operating with a narrow profit margin. The only way for the supplier to meet the MNC's demand is to reduce labor costs. However, for the order to be completed on time, the same number of workers is required. The only option for the supplier is to forgo health and safety maintenance in the factory and not pay all legally required wages and benefits. In this way, the supply chain manager's actions result in workers being treated as mere tools and not as ends in themselves. In this case the pursuit of self-interest is unethical because it is accomplished by harming the dignity of factory workers. However, a creative supply chain manager may be able to work with a supplier to enhance efficiency and productivity in the factory and thereby cut costs. In this way, a supplier may be able to obtain the desired cost reductions in an ethical manner, and his self-interested pursuit of the bonus would be ethically permissible.

Kantians begin with obligations or duties to respect other persons, rather than beginning with rights claims. These duties constrain the pursuit of ends, whether they are self-interested goals or projects pursued on behalf of other parties such as shareholders. Respecting persons involves negative obligations, such as refraining from using others as mere tools via physical force, coercion, or manipulation, and positive obligations such as supporting physical well-being and the development of human capacities. When they stand in the appropriate relationship to an obligation-bearer, persons have rationally justified rights-claims against them. On the Kantian account, rights take the form of side-constraints that bound the moral space in which agents may pursue ends without unjustified interference by other agents or institutions.

Whereas liberty rights to be free from being constrained or assaulted hold against all who would cause such harm to others, welfare rights appear to hold only when certain relationships exist. For without such a relationship, there appear to be no bearers of obligations and so the claimed rights could not be established in any binding manner.

If the world's poor have claim-rights, who are the corresponding obligation-bearers? One answer is that in cases where relationships already exist in the global economy, rights-claims are binding on specific obligation-bearers. Wherever MNCs do business, they are in relationships with a variety of stakeholders, such as workers, customers, and local communities. In their global operations and in their global supply chains, MNCs have a duty to respect those with whom they have relationships. MNC managers, then, have obligations to ensure both that they do not illegitimately undermine the liberty of any persons and that minimal welfare rights are met.

Critics of Kantian accounts of international business ethics argue that because of its theoretical foundations, it is susceptible to all of the criticisms that have been mounted against both Kant's ethics and Kant's metaphysics. Since this is the case, they argue, Kantian international business ethics is not a viable research project. Kantians respond by arguing that the resurgence in work by Kant scholars and Kantian ethicists in recent years has reinvigorated Kantian ethics and disarmed many traditional criticisms. Furthermore, they argue that elements of Kantian ethics, such as the doctrine of respect for persons, can be assessed independent of other elements of Kant's philosophy and have been shown to merit allegiance in their own right.

Labor Practices

Arguably, the use of global "sweatshops" for the manufacture of consumer goods is the most well-known human rights issue involving U.S. businesses since the collapse of South Africa's apartheid regime. Nongovernmental organizations (NGOs) have led boycotts and waged media campaigns against companies that they believe exploit factory workers in the interest of excessive profits. Responding to such critics, MNCs have made significant efforts to eliminate the worst abuses of worker rights in their contract factories. MNCs have significant coercive economic influence over suppliers. Typically, MNCs set the price at which they will purchase goods from contractors, and as a result they have considerable influence regarding working conditions. In many cases, contract factory owners may not have the resources to improve working conditions and wages without assistance from the MNC. Given this imbalance in power, MNC managers are well positioned to help ensure that the employees of its contractors are respected. In addition, MNCs can draw on substantial economic resources, management expertise, and technical knowledge to assist their business partners in creating a respectful work environment.

An efficient mechanism for MNCs to improve working conditions is via the adoption and implementation of voluntary codes of conduct. Such codes are created voluntarily by MNCs and are not based on the laws of any one nation but are instead designed to help managers and suppliers ensure that the basic rights of workers are protected. The mere voluntary adaptation and promulgation of a code of conduct is insufficient. Instead MNCs must oversee the full-scale implementation of their codes. A firm that merely produces a code and provides it to a contractor without further action sends a message that a similar lack of attention is all that is expected from its contractors. Serious and effective integration of a code throughout an organization's culture requires that a firm hold its contractors to the same standard regarding respect for employees to which it holds itself.

However, some companies are too small to contract for the use of all of a subcontractor's capacity but must instead place orders that represent a small percentage of a supplier's capacity. In such cases, the company has little influence over the contractor. This is especially true if the subcontractor is dealing with multiple companies at the same time, each with somewhat different standards or codes for the treatment of workers. Nonetheless, companies genuinely interested in ensuring that workers in their supply chains are treated with dignity at work can collaborate with one another to ensure that uniform standards are adopted and implemented. Efforts of this kind can help ensure that smaller and medium-sized companies meet their obligations regarding the preservation of basic human rights in their global supply chains.

Some theorists of economic globalization who are concerned about the welfare of the world's poorest people contend that what are needed are not fewer sweatshops but more sweatshops. These individuals argue that improving sweatshop conditions and respecting worker rights will result in greater harm than good. They argue that a free market eventually improves both working conditions and the overall economic well-being of host nations. Because the existence of more sweatshops will facilitate this process, such theorists argue that what is needed is more sweatshops, not fewer. In reply to this view, Kantians such as Denis Arnold, Norman Bowie, and Laura Hartman argue that morally imaginative MNC managers can voluntarily choose to improve working conditions and wages in their global factories, without laying off workers, while remaining competitive within their industry. In support of this claim they cite the current respectful treatment of workers at MNCs such as Motorola, Mattel, Nike, Adidas, and other companies.

Natural Resources

The ethical management of natural resources is an issue of increasing importance to managers of MNCs. Since the Industrial Revolution, Westerners have consumed vast quantities of resources with little attention to efficiency or conservation. More recently, growing Asian, eastern European, and Latin American populations have begun to emulate Western, consumer-orientated lifestyles. These consumption patterns place significant demands on natural resources such as oil and coal and global commons such as the oceans and the atmosphere. MNCs encourage such consumer demand via marketing and make choices regarding production and design that directly affect the global environment. Increasingly, the global environment is at risk and with it the welfare of human populations.

MNCs do not always meet minimal ethical obligations regarding the protection of the natural environment. For example, over an 18-year period, Texaco dumped hundreds of millions of gallons of toxic waste into the Ecuadorean and Peruvian Amazon. Critics correctly pointed out that in doing so Texaco ignored prevailing industry standards and put the health of the inhabitants of those regions at risk. However, it is important to keep in mind that critics of MNCs are not always correct about the moral status of MNCs' environmental actions. For example, in the late 1990s Royal Dutch Shell planned to sink the obsolete deep-sea oil rig *Brent Spar* 150 miles off the coast of Scotland at a depth of 6,000 feet. Shell engineers had determined that this was the most environmentally friendly manner of disposing of the rig. The international environmental group Greenpeace disagreed and waged a public relations campaign against Royal Dutch Shell to stop the sinking of the *Brent Spar.*

Greenpeace leaders erroneously claimed that the *Brent Spar* contained 5,500 tons of oil that would escape and contaminate the North Sea. Shell claimed that only 50 tons of oil remained on board and that this amount of oil would not have a substantial negative impact on the ocean environment. When the rig was eventually dismantled, 152 tons of oil was found to be on board. This estimate, while it was three times the amount claimed by Shell, was 36 times less than the amount claimed by Greenpeace. Despite the fact that its position was well supported by scientific evidence, Shell lost the public relations battle to Greenpeace. In the end, Shell was forced to dismantle the rig on land. Shell's total costs came to $97.6 million, as opposed to its initial estimate of $14.4 million. The environmental costs of disposing of the rig on land, as opposed to deep-sea disposal, were substantial as well. The energy spent was equivalent to 875,000 gallons of gasoline and more than 11,000 tons of atmospheric CO_2 emissions.

The *Brent Spar* case illustrates that the science matters when assessing controversies concerning corporate environmental practices. Greenpeace was able to win the public relations battle with Shell, despite vastly overestimating the environmental harm of sinking the *Brent Spar* in the North Sea, because of superior public relations management. However, Greenpeace's position was scientifically unsound, and in the end its actions appear to have led to greater environmental and economic harm than if Shell had disposed of the rig as it initially planned. All environmental issues faced by MNC managers have an important scientific component. In many of the most controversial cases, such as global climate change and the use of genetically modified organisms, many of the facts are contested. In such cases it is necessary to consult the best available scientific evidence and only then make appropriate ethical and strategic judgments regarding MNC practices. However, as illustrated in the *Brent Spar* case, it is also necessary to successfully manage one's ethical stance.

Climate Change

During the 1980s and 1990s there was substantial debate over the existence of global warming. Today, the scientific debate is largely over. In 2001 a consensus emerged in the global scientific community that global climate change (GCC) is occurring and that it will have a dramatic and adverse impact on ecosystems, nonhuman species populations, and human populations. Global warming is occurring primarily as a result of anthropogenic CO_2 emissions. The increase in average global temperatures is expected to alter weather patterns, resulting in droughts and floods in many different regions and a rise in the global mean sea level. Scientists predict the extinction of a huge number of plant and animal species as a result of climate change. Among human populations, the negative impacts of climate change will be disproportionately borne by the world's poor since they are least well equipped to alter their geographical and environmental circumstances.

A basic principle of justice holds that it is unfair to require others to pay for the costs of benefits one has secured for oneself without their uncoerced consent. The atmosphere is a common resource, one that the global community holds in common. U.S. industries make use of a disproportionate level of atmospheric resources on a per capita basis. At the same time, the harm caused to present generations of non-U.S. citizens will be disproportionate to their use of atmospheric resources. So too, presumably, will the harm be to future generations. Denis Arnold and Keith Bustos argue that those who enjoy the benefits resulting from burning fossil fuels, and thereby contribute to GCC, ought to pay more for such benefits than those who do not enjoy such benefits. In the United States the transportation and electricity generation sectors are the two sectors that contribute the most to the total U.S. CO_2 emissions. For example, between 1990 and 2003, the transportation sector contributed an average of about 31% of total CO_2 emissions from fossil fuel combustion in the United States. Arnold and Bustos have argued for a historic accountability for CO_2 emissions by corporations that is effective from 2001 forward. They argue that corporations that failed to take proactive measures from 2001 forward are morally blameworthy for this failure. They argue further that corporations that have not sufficiently reduced energy emissions would be justified in being penalized by governmental agencies with a carbon tax.

In response, many libertarians and others argue that corporations are merely responding to consumer demand and that it is the obligation of consumers to alter their consumption patterns to reduce CO_2 emissions. For example, consumers should choose to use public transportation or drive smaller, more fuel-efficient cars rather than to drive large, energy-inefficient sport-utility vehicles. In this view, the obligation to reduce carbon emissions, if any, falls on individuals and their elected representatives.

Looking Forward

International business ethicists are beginning to confront a range of new issues tied to rapid increases in economic globalization. First, some companies, such as Royal Dutch Shell, Adidas, Mattel, Merck, and BHB Billiton, have taken on roles as ethical leaders within their sectors of the global economy. It remains to be determined whether such companies will be rewarded for such leadership with competitive advantages so that ethically challenged MNCs will feel pressure to act more consistently with basic ethical norms. Second, MNCs based in recently industrialized nations such as South Korea, Brazil, China, and India are beginning to take a more prominent role on the global stage. These MNCs have the opportunity to "leapfrog" into the forefront of the ethical conduct of global business by following the examples set by the most ethically forward-thinking global corporations. Some companies, for example India's Tata group, appear to be demonstrating such leadership in their global operations. It remains to be seen how many emerging MNCs will follow suit. Third, not all companies that operate globally are large MNCs. Small and medium-sized companies have supply chains that extend across national boundaries. They also outsource many services abroad. Typically such companies lack the resources necessary to closely monitor activities at their suppliers or global service providers. One challenging issue confronting managers at such organizations, as well as business ethicists, is how to ensure compliance with basic ethical norms by their suppliers or global service providers. Finally, the role and responsibilities of NGOs in promoting global justice is beginning to come under increased scrutiny. NGOs frequently market themselves as the ultimate defenders of human rights and global justice. However, NGOs have mixed records when it comes to accurately representing the practices of MNCs. As has been the case with the corporate world, we may expect to see ethical leaders emerge among these organizations. The emergence of a core group of NGOs with ethical integrity should allow careful observers of debates concerning the practice of business in a global economy to render more informed judgments. NGOs should be held to the same high ethical standards as the MNCs that they themselves critique.

—Denis G. Arnold

See also Autonomy; Capabilities Approach; Coercion; Deontological Ethical Systems; Dignity; Ethics, Theories of; Freedom and Liberty; Global Business Citizenship; Globalization; Just Wage; Kantian Ethics; Living Wage; Moral Point of View; Moral Reasoning; Multinational Corporations (MNCs); Neo-Kantian Ethics; Rights, Theories of; Social Contract Theory; Sweatshops; United Nations Global Compact; Universalizability, Principle of

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International Labour Organization (ILO)

The International Labour Organization (ILO) is a specialized agency of the United Nations (UN) headquartered in Geneva, Switzerland. The ILO was formed in 1919 as an agency of the League of Nations through the negotiations of the Treaty of Versailles. It was created in response to labor and social movements that resulted in worldwide demands for social justice and higher living standards. In 1946, the League of Nations was dissolved, and the ILO became the first specialized agency of the newly formed UN. It received the Nobel Peace Prize in December 1969 for its work in social justice and its ability to institute positive change throughout its history.

The overarching purpose of the ILO is to promote humanitarian labor standards and labor rights and improve worldwide labor conditions so that social justice and economic health are supported and maintained. Its goals are to strengthen worker rights, improve working conditions, create employment, and provide information and training opportunities. It fulfills its mission and goals with its unique structure, the annual International Labour Conference, and through its Governing Body and the International Labour Office.

The ILO has a unique tripartite structure composed of representative governments, employers, and workers, all participating as equal partners. The Governing Bodies include 28 governmental members, 14 employer members, and 14 worker members. Ten of the government seats are held by countries of primary industrial importance, and the remaining 18 seats are elected every 3 years from countries representing a broad geographic distribution. The employers and worker members elect their own member representatives in separate electoral colleges.

The International Labour Conference is held each year, convening member country delegates who represent the tripartite structure: government, employers, and workers. The conference provides an international forum for discussion of world labor and social problems. Minimum international labor standards and the broad policies of the ILO are adopted at the conference. These standards are presented in the groups's Conventions and Recommendations and may address issues such as freedom of association, the right to organize, the right to engage in collective bargaining, the abolishment of forced labor, equality of opportunity and treatment, and other standards regulating conditions of work-related issues. In addition, the governing bodies are elected, and work programs and budgets are adopted at the conference every 2 years.

The work of the ILO is guided by its constitution and its governing body throughout the year. The director-general oversees the ILO's secretariat, known as the International Labour Office (Office), where the operational headquarters, research center, and publishing house are located. The International Labour Office employs 1,900 officials of more than 110 nationalities in 40 field offices across the world. Its research and documentation center produces studies, reports, and periodicals. There are also 600 experts who participate as technical specialists. Technical specialists work with the field offices to promote the strategies and work of the ILO through the Technical Assistance Program for Cooperative Development. This program is one of the primary tools for translating the fundamental principles and rights of the ILO into practice.

Conclusion

The ILO serves an important role in addressing the world's labor issues. With its lengthy history, defined purpose, and international presence, it has the ability to create global influence. It uses its influence in a wide range of roles. For example, it may recommend sanctions on a country engaging in forced child labor in an effort to impose negotiations on labor standards that have previously failed. On the other hand, it may be commissioned to complete a study that explores employment policies and practices regarding women in nontraditional jobs.

Social justice is a dynamic concept. Critics say that the ILO's influence may provide a viable solution that quickly evolves into a new set of challenges that create a different ethically charged circumstance. In addition, its authority is as strong or as weak as its member country representatives. These members are susceptible to unique pressures that are specific to the history and politics of their respective countries, particularly economies long impoverished that are realizing newfound economic progress. The pursuit of economic development and prosperity does not always blend with social justice without ethical consequences, particularly in the case of a country that has not previously had a strong focus on its labor rights and practices. Furthermore, its policies may be incongruent with a country's established labor standards and policies. For instance, most states in the United States maintain an at-will employment relationship between employer and employee. This legal doctrine dates back to the late 1800s, and it specifies that an employee works at the will of the employer and that either party may terminate an employment relationship without liability and without cause (unless formal employment contract agreements specify otherwise). One of the declarations of the ILO's Fundamental Principles and Rights states that employers will commit to "the elimination of discrimination in the workplace." At-will employment principles depart from the protections identified under discrimination laws, so compliance with both the at-will doctrine and the ILO's policies are at odds, creating an ethical and moral conflict between two well-established visions of terms of employment.

Despite its challenges, the ILO serves as a moral compass in its role in setting labor standards and promoting social justice. It is a voice that is heard, whether the desired outcomes of its negotiations are successful or not. It raises awareness of labor issues and social injustice. Furthermore, its network of workers permeates the majority of industrialized countries, which creates a worldwide forum for dialogue on important labor issues that arise.

—Pamela C. Jones

See also Developing Countries, Business Ethics in; Economics and Ethics; Employment Contracts; Employment Discrimination; Equal Employment Opportunity; Equal Opportunity; Global Codes of Conduct; Humanities and Business Ethics; International Business Ethics; Moral Leadership; Sweatshops; Women in the Workplace

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International Monetary Fund (IMF)

The International Monetary Fund (IMF) is an international governmental organization, operating as a specialized agency of the United Nations Organization. Headquartered in Washington, D.C., the IMF was established to manage the international financial and balance of payments systems and to help its members manage their currencies and national financial accounts. As outlined in the IMF's charter, its articles of agreement, the institution's primary purposes include the promotion of international monetary cooperation and exchange stability, thereby aiding the expansion of international trade and ultimately the overall economic prosperity of its members by helping to maintain high levels of employment and increase levels of real income.

The IMF's membership comprises only countries, those recognized as sovereign nation-states. There is no provision for joint membership of economic or monetary unions of states, such as the European Union. Rather, individual states join as independent members. Membership has grown from 29 states, at the IMF's founding in December 1945, to a total of 184 states as of June 2005.

The IMF was to become one of a trio of international economic organizations (what Sir Joseph Gold, a leading international lawyer handling the novel legal affairs of the IMF from its inception, called a "trinity of comparable institutions") envisaged near the end of World War II. These three institutions—a cooperative monetary fund, a development bank, and a global trade organization—were together to help rebuild the national and international economies devastated by the war and to ensure that the economic ravages of the Depression era that presaged the war would not recur.

The IMF the and International Bank for Reconstruction and Development (IBRD, otherwise known as the World Bank) were crafted during a meeting of 45 government representatives at Bretton Woods, New Hampshire, in July 1944. Led by Lord John Maynard Keynes of the United Kingdom and Harry Dexter White of the United States, charters for these two institutions were drafted to manage the international economic affairs of member states. These two institutions are thus commonly referred to as the Bretton Woods sisters. (The third institution was stillborn: The global trade organization's charter, drafted in 1947, found insufficient political support, and in its place was crafted the General Agreement on Tariffs and Trade, or GATT, which came into force in 1967 and finally evolved into the World Trade Organization, or WTO, only in 1995.)

Under the articles of agreement, ultimate authority for the functioning of the IMF resides with its board of governors. This board comprises one governor plus one alternate governor, appointed by each member, and meets annually. The managing director of the IMF is appointed by the governors and acts as the board of governors' chair. Though the governors gather together formally only once each year, provision is made for communication and voting between annual sessions. In practice, significant power has been delegated by the governors to a board of executive directors (currently numbering 24), who, with the IMF staff under the leadership of the managing director and three deputy managing directors, direct day-to-day operations and decide how best to manage IMF resources.

Members are assigned quotas or subscriptions, amounts that must be paid into the IMF's common fund. This amount is determined primarily by an assessment of the country's size, its relative economic strength, and vibrancy. The quota of the United States is the largest of all members (contributing just more than 17% of the IMF's prime resources), with Palau having the smallest (contributing 0.001%). While members operate as sovereign equals, voting power is related to quotas by an intricate formula. Every member receives 250 "basic votes" on membership—thus recognizing equality, plus one additional vote for each specified quota increment—thus recognizing key differences in economic and political power. Hence, the United States also controls 371,743 votes (just more than 17% of all votes that can be cast), while a country such as Palau controls 281 votes (0.01% of all votes available).

When the IMF was established, currencies were fixed; that is, the value of every currency was linked to each other currency by a set formula, determined by the IMF, and ultimately to gold. Currencies were permitted to vary from this par value only within a very narrow band above or below that set. In addition, the U.S. dollar became the world's reserve currency, meaning that all currencies were in practice valued against and quotas were fixed in U.S. dollars, and the United States guaranteed it would convert dollars to gold. When a country was assigned its quota, it was to pay a substantial portion of that quota into the IMF in gold or U.S. dollars and only the remainder in its own currency.

After a series of international monetary crises during the 1960s, this regime of fixed exchange rates was replaced by a floating regime after 1971, when the United States, finally, formally decoupled the dollar from gold and no longer guaranteed conversion. In place of gold, the IMF in 1969 created the Special Drawing Right (SDR), which operates as a unit of account and reserve asset. The value of an SDR is set by weighting a basket of key currencies, including the U.S. dollar, the euro, and the Japanese yen. SDRs are then distributed to members as a percentage of their quotas, thereby increasing reserves available for members to draw on, while replacing reliance on gold under a defunct fixed exchange regime. Quotas are now denominated and paid in SDRs, along with the member's own currency.

As a cooperative monetary fund, the IMF technically does not "loan" monies to its members who need assistance, even though that term is commonly used even in the IMF's own publications. Rather, when a member seeks aid, currencies are "purchased" (e.g., tendering Brazilian reais in exchange for euros), with the stipulation that a member will repurchase its currency at some future date, usually within 1 to 3 years' time (e.g., by swapping euros or SDRs for the Brazilian reais originally tendered). Such exchanges should not exceed 300% of a member's quota. In this manner, a country can obtain the exchange currency it needs to manage its monetary affairs without disrupting capital markets. (There are IMF loan programs for extending resources beyond this quota calculation, but those resources are drawn from special funds and are often arranged conjointly with the World Bank.)

Such exchanges are typically arranged under IMF conditionality: A country will access those resources only after arranging a specific plan to manage its economy so that the member can regain stability and grow. IMF technical assistance to member states is thus deemed critical to achieving its overall mission, both before a crisis arises, to help members avoid macroeconomic difficulties, and after resources are disbursed to manage a crisis that has arisen. This makes the process of surveillance and regular consultation as required under the articles of agreement between the IMF and member states quite important, with the IMF publication series a source of valuable comparative data for policy makers and foreign investors in all member states.

Nevertheless, criticisms have been urged concerning the effective and ethical operation of the IMF. Matters such as its governing structure (control by a few developed countries), conditionality (too much external control over a developing country's economy, with too little attention paid to impact of conditions on the poor), and creation of resources (too few SDRs available for development) have been advanced even by those otherwise in broad agreement with IMF purposes and operations.

—Daniel Walter Skubik

See also Bretton Woods Institutions; Development Economics; World Bank

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International Organization for Standardization (ISO)

The International Organization for Standardization (ISO) is the world's leading institution for standard development, having published more than 15,000 standards in many diverse fields ranging from traditional activities, such as agriculture and construction, to the newest developments in fields such as mechanical engineering, medical devices, and information technology. More recently, in 2004, ISO decided to further extend its activities by starting the development of an international standard addressing the *social responsibility* of organizations.

ISO is a truly global organization—a network association among 157 national standardization bodies worldwide—representing both government institutes and private, industry associations. It was founded in 1947 with the overall mission "to facilitate the international coordination and unification of industrial standards." Its modus operandi in the process of standard development is based on some key concepts. (1) *Market-driven approach:* Any ISO standard setting initiative is based on results of an assessment that indicate a need for a standard by an industry or business sector. (2) *Technical competency:* The development of each standard is the responsibility of a specific technical committee of experts nominated by national standard bodies. (3) *International consensus:* The whole process is based on the search for consensus on a draft agreement among the technical committee members first and the wider ISO membership thereafter. (4) *Representation of interests:* Within each technical committee ISO seeks a wide representation of different competencies and interests, including those of industry, government agencies, labor, consumer associations, environmentalists, experts from academia, and so forth (this tendency has been affirmed with the development of ISO 26000, the ISO standard on social responsibility [SR]).

Among the family of standards developed by ISO, the most famous are undoubtedly ISO 9000 ("quality management," primarily focusing on the customer's and other regulatory requirements to enhance customer satisfaction) and ISO 14000 ("environmental management," dealing with the organization's environmental challenges such as pollution and other harmful effects on the natural environment), which have been adopted by more than 700,000 organizations worldwide. While most ISO standards are highly specific to a particular product, material, or process, both ISO 9000 and 14000 are *management standards,* that is, standards that refer to management systems that *any* organization has to put in place to manage its processes and activities and ultimately improve its performance in the areas regulated by the standard itself. This also means that they are *generic* standards, that is, they are designed to be applied by organizations of different sizes, large and small, and operating in different industry sectors, manufacturing or services, or by different types of organizations, such as private firms, public administrations, or governmental departments.

The ISO Standard on Social Responsibility

In 2004, ISO formally decided to initiate the development of a new international standard for SR: ISO 26000. With regard to the nature of the standard, ISO decided to produce a guidance document, that is, a standard not intended for third party certification but able to provide meaningful guidance to all kinds of organizations on SR issues. In recognizing the uniqueness and originality of this area of work with respect to its traditional standard-setting activities, ISO created a new international working group designed to ensure balanced representation of six different stakeholder groups: industry; government; labor; consumers; nongovernmental organizations; and service, support, research, and others, as well as geographical and gender balances. A precise reference was made to existing quality and environmental management systems to build on the intellectual and practical infrastructure of ISO 9000 and ISO 14000 management system standards. The ISO Advisory Group on Social Responsibility pointed out possible benefits of an active engagement by ISO in the field of social responsibility:

> From a standardization perspective, international SR standardization is desirable if it facilitates trade, in particular by harmonizing an unnecessary proliferation of overlapping national, regional, and other SR initiatives. From a public policy perspective, international SR standardization is desirable if it helps to increase SR actions by (1) leading to the development of better SR regulations; (2) helping

organizations to implement SR more easily; and (3) helping to create economic incentives to undertake SR actions.

Moreover, the need to create a "level playing field," not only for private organizations but also for developing and developed countries, is seen as a further benefit of an internationally accepted SR standard.

With regard to the features of the standard, ISO decided to base the new standard on the same, general approach of ISO quality and environmental management systems (i.e., policy; planning; implementation and operation; performance assessment; improvement; and management review). The following elements have been considered as the basic areas on which the ISO SR standard should provide guidance:

- Compliance with relevant international norms pertaining to environmental, consumer, and fair labor standards, human rights, and health and safety protection
- Processes for meaningful stakeholder engagement
- Development, implementation, and communication of SR and ethics policies, including those pertaining to antibribery and corruption
- Training of the workforce, including executives and management
- Relations with communities, philanthropy, outreach, and involvement
- Measurement and regular reporting to the full range of stakeholders and the general public

Standards Strengths and Weaknesses

There are a number of considerations concerning the development and implementation of standards in business, highlighting the potential benefits that can be generated but also the potential limitations of standards use. On the positive side, the following benefits can be pointed out:

- *Clarification and conformity:* Standards help eliminate confusion, particularly in new fields, by clarifying what the state of the art is and by defining a common language and appropriate methodologies. Moreover, they facilitate the worldwide compatibility of technology and the establishment of internationally accepted practices.
- *Assurance:* Through mechanisms of third party certification, or independent conformity assessment, standards provide consumers and other stakeholders a reliable way of evaluating product quality and other relevant aspects of the organization's management, processes, and performance.
- *Operationalization:* Standards provide practical frameworks to apply general concepts—such as "quality" or "environmental management"—in day-to-day business processes and operations.
- *Innovation and know-how:* Standards can be applied by any organization, regardless of the field in which it operates or its size, type, and geographical location; therefore, they facilitate the process of diffusion of innovation and technology (and knowledge) transfer.

On the other hand, potential weaknesses of standards include aspects such as the following:

- *Rigidity:* By focusing on compliance with a set of requirements, standards may induce less flexibility in organizational processes and reduce creativity and innovation in management.
- *Cost:* To apply a management standard within an organization and obtain independent certification requires a certain level of investment by the organization itself—in terms of the necessary competencies, time, and financial resources—which may be particularly burdensome for small and medium-sized businesses.
- *Enforcement:* Being adopted on a voluntary basis, standards cannot rely on strong enforcement mechanisms, such as those available to laws or other mandatory requirements. Therefore, the legitimacy of standards also depends on the credibility of third party certification.

Like many other global organizations, the ISO has not been immune from criticism concerning its management procedures—faulted as being too slow, bureaucratic, and not responsive to society's concerns—and the legitimacy of its governance structures, which may generate conflicts between the requirements of international standards and local (national) social and cultural norms or even legal and other regulatory frameworks.

Particularly in the field of SR, the issue of "bureaucratization" remains an open concern because the establishment of standards inherently favors the development of *formal* routines that can be operationalized (and verified), and this in turn generates the risk of losing touch with the importance of the standard's *substantive* content (i.e., the focus on concepts such as ethics, individual responsibility, and organizational culture).

—Simone de Colle

See also Corporate Social Responsibility (CSR) and Corporate Social Performance (CSP); Sustainability

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International Trade

International trade encompasses the exchange of goods and services between residents of different countries. The bulk of international trade consists of what economists describe as "merchandise trade," or trade in physical goods. The other category is services trade, the exchange of nonphysical goods. The largest categories of merchandise trade are machinery and transportation equipment, agricultural products and foodstuffs, and crude oil and petroleum products. The largest categories of services trade include business, professional and technical services, insurance and finance, and travel and transportation.

Some Characteristics of International Trade

The increasing prominence of international trade is illustrated by the fact that the growth of world merchandise trade has consistently outpaced the growth of world production since the middle of the 20th century. As a result, an increasing percentage of world production over time has been dedicated for sale in foreign countries rather than domestic economies.

Notwithstanding the importance of China as a major trading nation, international trade primarily takes place among developed countries. There are several reasons for this. One is that agriculture accounts for a larger share of production in developing countries than in developed countries, and nontariff barriers to trade are particularly onerous in the case of agricultural products. A second is that international trade reflects, in part, a taste for product variety on the part of consumers. The demand for product variety, in turn, is positively related to a nation's standard of living. A third reason is that the majority of international trade is carried out by multinational companies (MNCs). The location and distribution of MNC production facilities reflects the geographic pattern of foreign direct investment, and developed countries are most often the host and home nations for foreign investors.

Several other characteristics of international trade are worth noting both for purposes of information and for contributing to a better understanding of several major controversies surrounding international trade. One is the prominent role played by MNCs in the international trade process. An MNC is a company with affiliates in foreign countries. The bulk of international trade consists of goods shipped among affiliates of MNCs. Hence, the growth of international trade is mirrored by the growing economic importance of MNCs. Those who are concerned that MNC activities have adverse impacts on both host and home countries are therefore skeptical of the social benefits of international trade.

A second characteristic to note is the predominance of intraregional trade. In the three major economic regions of the world, namely the European Union, North America, and Asia, trade involving countries within each region is greater than trade across those regions. The importance of intraregional trade in part reflects the growth of regional trade agreements such as the North American Free Trade Agreement (NAFTA).

Critics of regional trade agreements argue that the world, especially developing countries in Asia and Africa, would be better served economically by strengthening and extending multilateral trade institutions such as the World Trade Organization (WTO).

Factors Promoting International Trade

Several phenomena have been cited as underlying the dramatic growth of international trade summarized above. One factor is technological change, particularly as it has affected telecommunications and transportation. From the adoption of the telegraph through the spread of the Internet, innovations in telecommunications have reduced the real cost of communicating over long distances and speeded the dissemination of information about economic conditions and developments in distant markets. Consequently, it is less costly and easier for companies to do business at a distance. Moreover, the marriage of computer and telephone technology has spawned the emergence of computer-based management information systems that enable MNCs to better and more cheaply manage far-flung affiliate business activities, including the export and import activities of foreign-based affiliates.

The transportation sector has also enjoyed remarkable improvements in technology that have both lowered the costs of transporting goods long distances and expanded the range of goods that can be shipped. For example, containerization of ship cargo along with the adoption of surface transportation systems that can move containers to and from ports is a major development facilitating the efficient and safe transportation of goods internationally. Double-hulled, large oil tankers are the basis for the major growth in exports of petroleum and petroleum products from oil-rich regions such as the Middle East to oil importers such as China and the United States. The jet airplane along with declining airfares has facilitated the ability of MNCs to quickly move technicians, salespeople, and managers throughout their global organization to facilitate efficient worldwide operations.

Without gainsaying the importance of these technological developments, many economists believe that the single most important factor encouraging the growth of international trade has been government efforts to reduce barriers to international trade through the creation of multilateral and regional trade agreements. From the General Agreement on Tariffs and Trade (GATT) to the WTO, the nations of the world, through these multilateral agreements, as well as regional agreements such as NAFTA, have implemented major reductions in tariffs and other barriers to trade, particularly for manufactured goods. Certainly, major barriers to international trade still exist, particularly in agriculture and services; however, the trend toward expanding regional trade associations and deepening multilateral trade liberalization remains in place.

The Economic Basis for International Trade

The underlying rationale for international trade is the theory of comparative advantage, developed by the British economist David Ricardo in the 18th century. The theory posits that countries can improve their real standards of living by specializing in the production and exportation of goods in which they have *relatively* low costs while importing goods for which they are *relatively* high-cost producers. Equivalently, countries should specialize in producing and exporting goods that are relatively cheap in their home markets and import goods that are relatively expensive.

The concept of comparative advantage is illustrated by the information summarized in Table 1. The illustrative example involves two countries, the United States and China, and two goods, steel and cloth. While the example is obviously a gross simplification of reality, it illustrates the principle of comparative advantage as well as more complicated examples. The information shows that China uses 5 units of labor to produce a unit of cloth and 10 units of labor to produce a unit of steel. The United States is assumed to use 2 units of labor to produce a unit of cloth and 3 units of labor to produce a unit of steel. Another simplifying assumption here is that labor is the only input for producing steel and cloth. Again, the assumption doesn't change the logic of the discussion.

Table 1 Assumed Labor Requirements per Unit of Output

	Product	
Country	*Cloth*	*Steel*
United States	2	3
China	5	10

Note that the United States is assumed to need less labor than China does to produce either cloth or steel. The United States has an absolute advantage in producing both cloth and steel because it can produce both products with fewer inputs than does China; however, the United States is relatively low cost in the production of steel, while China is relatively low cost in the production of cloth. To see this, imagine that the United States stopped producing 1 unit of steel and used the labor that was saved to produce cloth. It could produce an additional 1.5 units of cloth since 3 units of labor used in cloth making would result in (3/2) or 1.5 units of cloth being produced. In China, if 1 unit less of steel were produced, the economy could increase the production of cloth by 2 units, that is, 10 units of labor divided by the required 5 units of labor per unit of cloth. Another way of viewing the situation is that the U.S. economy would need to give up two thirds of a unit of steel for each unit of cloth produced domestically, whereas the Chinese economy would only need to give up 0.5 units of steel for every unit of cloth produced domestically. In terms of economic sacrifice, it is cheaper to produce cloth in China and steel in the United States.

Domestic prices for steel and cloth in the two countries should reflect the assumed differences in relative costs. For example, since steel production in the United States requires 1.5 times the amount of labor per unit of output required for cloth production, steel would presumably cost 1.5 times as much as cloth in the United States if all steel and cloth sold there was domestically produced. By the same logic, the price of steel would be twice that of cloth in China assuming that all the steel and cloth sold there was domestically produced. In effect, steel is relatively cheap in the United States, and by deduction, cloth is relatively cheap in China. Therefore, to the extent that consumers in the United States want more cloth, they would be better off buying it from Chinese suppliers, while consumers of steel in China would be better off importing steel from suppliers in the United States.

In fact, by opening up international markets for trade in cloth and steel between the two countries, such as by eliminating tariff and nontariff barriers to trade, export and import agencies would engage in precisely the behavior predicted by the simple theory of comparative advantage as described above: Namely, companies would go into business importing cloth from China for sale in the United States while importing steel from the United States for sale in China. As this process took place, the price of steel relative to cloth would fall in China and rise in the United States as steel left the United States for China while cloth entered the United States from China and as steel entered China from the United States while cloth left China for the United States. Eventually, the relative prices of the two goods in the two countries would converge to the point where further international trade was not profitable, given transportation and other costs of serving foreign markets. The trade that does take place between the two countries should, of course, benefit consumers in both countries since they are able to import specific products at prices lower than those being charged by domestic sellers.

The simple logic of the theory of comparative advantage is compelling, if not intuitively obvious; however, even those critics who readily accept the logic of Ricardo's theory question the overall net benefits to economies arising from unrestricted international trade. Some specific reservations to the economic argument for free trade are discussed in the next section.

Some Criticisms of International Trade

A variety of criticisms have been leveled against international trade in conjunction with a growing and vocal opposition to the "globalization" process. Since it is impossible to be comprehensive in cataloging the criticisms, this portion of the entry focuses on what are arguably the most prominent or most durable criticisms.

Unemployment

Perhaps the most long-standing and fundamental complaint about international trade is that imports displace domestic production and lead to increased unemployment in the domestic economy. An appropriate response to this complaint is that increased exports enhance employment opportunities in the domestic economy; however, many of those who lose their jobs or suffer reduced wages as a consequence of increased imports may not be able, for one reason or another, to move quickly into activities that are expanding as a result of growing exports. For example, older workers may find it difficult or uneconomical to spend significant periods of time acquiring additional education or new skills necessary to work in expanding businesses. Workers living in rural areas may find it economically difficult to afford higher-priced housing in urban areas where most new jobs are likely being created. Perhaps of greatest relevance, some domestic workers may need to accept lower wages and reduced benefits, with the associated hardships, to maintain their jobs.

To the extent that increased international trade benefits society overall, it seems "appropriate" for government to offer assistance to those who suffer significant economic hardship from increased imports. In fact, most developed governments do have programs to assist domestic workers who can document significant economic injury from growing imports. What is noteworthy is how relatively few workers, particularly in the United States, apply for assistance under those programs. In the past, the burden of adjusting to import competition has been disproportionately borne by workers in unionized manufacturing industries such as steel and automobiles, in both the United States and other developed countries. In fact, these have been relatively slow-growing industries with a declining workforce anyway, thereby helping to mitigate the need for major labor market adjustments to international trade. More recently, increased imports from countries such as India and China are occurring in major and growing sectors such as electronics and software. Hence, labor market impacts of international trade in developed economies such as the United States may be larger in the future than in the past.

Unfair Trade

The argument that expanding exports to trade partners will create new (and possibly more highly paid) employment opportunities to replace those "lost" due to increased imports is undercut somewhat by protective measures undertaken by a country's trading partners that discourage exports by other countries. Critics of international trade frequently argue that trade might be free, but it is rarely "fair." Measures that promote a country's exports, while discouraging imports to that country, encompass a range of actions that are often labeled unfair trade practices. They include suppressing an appreciation of the exporting country's currency, laws and regulations that are particularly costly for foreign firms to obey, government subsidies to domestically owned firms, and a failure on the part of some governments to enact or enforce environmental regulations, minimum wage laws, worker protection laws, and other corporate obligations that other countries have put in place.

One point that should be made with respect to the unfair trade argument is that trade will still follow the basic pattern dictated by comparative advantage; that is, countries will still be encouraged by market forces to export goods that are relatively cheap domestically and import goods that are relatively expensive domestically. Hence, if unfair trade practices are being pursued by certain governments, they will affect trade only to the extent that they alter established patterns of comparative advantage. For example, if developed countries have minimum wage laws while developing countries do not, products produced using relatively unskilled labor will be even more expensive in developed countries compared with developing countries. This will accentuate the comparative advantage that developing countries have in goods that are produced using relatively large amounts of unskilled labor.

A second point is that unfairness is in the eye of the beholder. For example, workers in developing countries might not place the same importance on occupational health and safety as do workers in developed countries. For the former, abundant and relatively well-paying jobs are of primary importance. Hence, workers in developing countries might see it as unfair for their governments to implement the same occupational health and safety laws as the United States does under duress from the U.S. government, particularly if it leads to fewer or lower-paying jobs available in those developing countries.

The Race to the Bottom

Closely related to the unfair trade argument is the argument that free trade will inevitably lead to a weakening of social legislation, including environmental regulations, and an erosion of public spending in developed countries. The basic notion is that companies will relocate production facilities to countries that do not have social and environmental legislation but that do have low tax rates because there is relatively little government spending. The resulting loss of jobs and income tax revenue will put pressure on governments in developed countries to change public policies to make them more similar to those of developing countries to discourage "outsourcing" of domestic jobs. Outsourcing in this context can be thought of as the relocation of production capacity abroad while serving the former production location by exporting from the new location.

Critics of globalization presume that MNCs systematically prefer to locate in low-tax political jurisdictions characterized by weak social and environmental regulations and that appeals to notions of morality to change this preference are likely to be futile; however, there are theoretical reasons to question the validity of the presumption. In particular, skilled, educated workers essential to operating modern businesses arguably prefer to live and work in safe and clean environments, where their children can receive good educations and where there is good public infrastructure in the form of roads, parks, and the like. Such preferences are likely to encourage more rather than less social spending by government, as well as environmental and occupational regulations and laws more prevalent in developed countries.

The available empirical evidence also fails to provide any convincing support for the race-to-the-bottom concern. In particular, there is no evidence that MNCs significantly favor investments in countries with weaker environmental protection laws when other factors are held constant. Moreover, over the past four decades, government spending on social programs as a share of national income has risen in the developed world notwithstanding an explosive growth of international trade.

Economists therefore continue to defend international trade as an important channel by which countries, especially developing countries, can improve their living standards. At the same time, critics of international trade continue to raise the specter of powerful MNCs weakening the sovereign power of federal and local governments to enact policies that are not in the economic interests of big business. In this respect, international trade raises a basic concern about trade-offs between economic and noneconomic objectives that characterizes most economic policy issues.

—Steven Globerman and Brian K. Burton

See also Bretton Woods Institutions; Comparative Advantage; Developing Countries, Business Ethics in; Developing World; Doha Development Round of 2001; Foreign Direct Investment (FDI); Free Trade, Free Trade Agreements, Free Trade Zones; Globalization; International Monetary Fund (IMF); Maquiladoras; Multinational Corporations (MNCs); North American Free Trade Agreement (NAFTA); Trade Balance; World Bank; World Trade Organization (WTO)

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Internet and Computing Legislation

As a business and public tool, the Internet is in its infancy, especially when compared with other forms of communication technology such as radio, television, and the telephone system. It follows then that the relevant government legislation is also in its infancy and that the regulatory and legislative pace is fast and evolving very quickly. As with other major shifts in the culture, with the Internet, the government has struggled to understand its potential impact on business and society, how it is both similar to and different from other forms of communication, and what public policy role the government should assume. Because of this, most of the legal framework that applies to and affects the Internet emanates from regulatory and judicial bodies interpreting existing law rather than from legislative actions. This is especially true when issues such as equal access, copyright protection, and consumer privacy are considered. In these and similar cases, existing law, written in another time for other business and technology situations, is being interpreted in the context of new applications of a new emerging communications medium.

Society and governments view communications technologies and their associated systems as vital public infrastructure, increasingly necessary for conducting private and governmental business. At heart, all communications technologies, from the telephone and telegraph to satellite television to the Internet, share common features: They move "information" of some type (pictures, voices, data); they require a network of common users to be practical and valuable; they spawn innovation and foster economic growth; and they convey societal and business advantages to those who have access to them over those who don't. It is these last two features that inform (involve?) most government regulation of communication technology. Universal access to communication services, fair pricing, and ensuring usage for public good have driven communications legislation in the past and likely will do so in the future.

In that context, early communications legislation, and now Internet and computing legislation, has been concerned with two sometimes competing aspects of public policy: promoting growth, usage, and public access to communications media, while also attempting to specify and at times control how that medium is used and what "content" it may communicate.

All such modern legislation has its roots in two predecessors: the Communications Act of 1934 (which established the Federal Communications Commission and addressed radio broadcasting) and the Modified Final Judgment, a judicial ruling in 1984 that governed the dismantling of the AT&T telephone monopoly. Both were primarily concerned with placing restrictions on companies: specifying what broadcasters could not do, placing limits on ownership, and erecting barriers to cross-market services (e.g., preventing long-distance telephone carriers from entering local phone markets). The main focus was on preventing monopolies and unfair pricing and controlling the influence of broadcasters.

Both predecessors reflected the fact that until the 1960s there was a clean division in the primary forms of communication: Radio broadcast only sound (broadcast meaning communicating from one sender to many receivers), television broadcast pictures and sound, and telephone carried sound from a single point to another single point. The 1960s started a revolution in electronic technologies, eventually creating new opportunities for the existing telephone infrastructure (particularly in carrying data), jump-starting the cable television business, creating new ways of transmitting data and voice, and blurring the formerly clean lines of communications media. Data could be carried on telephone lines. Pictures and sound would eventually be translated into data. By the mid- to late 1990s the telephone network (in the form of Internet services) could "broadcast" radio, television, and music. Television technology (especially cable networks) could be used for transmitting the same data, making it possible to provide telephone services, television, radio, and data communication through the same network. In the intervening 60-plus years between 1934 and the late 1990s, a confusing, overlapping, sometimes conflicting, and ultimately unworkable collection of regulations and policies were created by a variety of state and federal entities.

The first successful attempt to address the changes was the Telecommunications Act of 1996, signed by President Bill Clinton on February 8, 1996. The act covers almost all segments of the communications industry, including broadcast radio and television, cable television, telephone service, and Internet and online computer services. For all of these the act attempts to simplify the regulatory environment. Most critically, the act eliminated cross-market and cross-industry barriers, allowing companies to provide service in multiple sectors (e.g., cable companies offering telephone services, long-distance companies offering local telephone services) and promoting competition in previously near-monopoly environments. Arguably, the loosening of restrictions is considered by some to be a major factor in the growth of affordable high-speed communications access not only to business but also to the home, setting in place the necessary infrastructure for the explosive growth of the Internet in the next 10 years.

Specific to the Internet, the Telecommunications Act of 1996 included Title V, the "Communications Decency Act of 1996" (CDA). Title V attempted to place limits on what could be transmitted over the Internet, prohibiting "indecent" or "patently offensive" and/or harassing materials from being transmitted, e-mailed, posted on Web sites, or used in chat rooms or online discussion groups. In doing this the act posited a clear parallel between radio and television broadcasting and the Internet, and it applied to the Internet the standards already in place for public broadcasters. In contrast, though, the CDA also exempted operators of Internet services (Internet service providers [ISPs], chat room providers, etc.) from liabilities arising from the content that third parties placed on the Internet, in that context drawing a clear line separating traditional publishers and broadcasters from Internet operators. (In fact, newspapers were now held to a double standard. For example, classified ads for housing placed in print editions of newspapers could not be discriminatory, but the newspaper was protected from legal harm if a similar ad placed on a newspaper Web site classified section discriminated against a protected class.)

Civil liberties organizations immediately reacted to what was viewed as an infringement on free speech rights, arguing that the Internet is a unique communication medium, more like a newspaper than television, and should be protected by the First Amendment. Opponents argued successfully that because the CDA preempted parents' prerogatives of deciding what was or wasn't appropriate for their children, because the phrase "patently offensive" had no clear legal definition or precedent in law, and because the restrictions extended beyond commercial speech, those parts of the CDA were clearly unconstitutional. By 1997, the Supreme Court had ruled the content-oriented parts of the CDA as unconstitutional and concluded that the Internet deserved the same free speech protections as other print media.

In response to the Supreme Court CDA ruling, Congress passed the Child Online Protection Act (COPA) on October 21, 1998. Specifically targeting the World Wide Web, COPA makes it a crime to use the Internet for "any communication for commercial purposes that is available to any minor and that includes any material that is harmful to minors" without restricting access to minors through means of a credit card, debit card, adult access code, or digital age verification certificate. While COPA was more narrowly constructed than the CDA, it was nonetheless seen by civil liberties organizations and many others as again infringing on free speech rights, especially with regard to language that applies "contemporary community standards" to judge which materials would be harmful. Legal challenges began on October 22, 1998, and continued over the ensuing 6 years, culminating in a Supreme Court decision blocking enforcement of COPA because of its overly restrictive language. The Supreme Court sent the case back to the lower courts with a charge to investigate changes in technology, especially parental controls and sophisticated Internet filtering, which would be more effective than a broad Internet pornography law.

Fundamentally, the CDA and COPA were attempts to apply traditional legislative thinking and constitutional ideas (control of content, definitions of obscene material, free speech protections) to a new technological phenomenon that was not only unique but also only in its infancy. Congress critically misjudged the Internet and assumed it was a communications medium rather than an enabler of business and personal innovations that would transcend its original intent of being a robust, survivable network connecting distributed computers. While focusing on obscene materials, Congress was not able to anticipate a wide range of Internet-related issues that would arise from innovative application of the basic Internet technology, including piracy, copyright, free speech, and privacy questions. Because the cycle of technologic innovation is much shorter than that of legislative response, private citizens and businesses would create new uses for the Internet that would inevitably outpace legislative efforts to respond.

Arguably preeminent among these uses is electronic commerce, in which the Internet is used to replace and augment traditional commercial transactions and which has created new types of transactions that did not exist in a pre-Internet world. And, where commerce flows, taxes are soon to follow. From a taxing perspective, the Internet presented new problems and opportunities for government taxation. As many commerce-based taxes are location dependent, the "locationlessness" of the Internet allowed most transactions to be outside traditional taxing mechanisms. In addition, the global reach of the Internet, coupled with global logistics and delivery capabilities, expanded the range of commercial transactions and hence the possible number of government entities desiring a piece of the tax pie.

In the United States, by the mid-1990s individual states began the process of imposing taxes on Internet access and on e-commerce transactions, based on the location of the transacting parties. States required ISPs to monitor locations and provide the government with detailed information for tax purposes, and the prospect of at least 50 separate jurisdictions imposing differing requirements on ISPs forced the discussion to the national level. Proponents of a tax-free Internet argued that tax burdens would stifle the growth and innovation of the Internet and related services and should be banned for Internet commerce and access. Alternatively, states argued that e-commerce would reduce taxes from traditional commercial transactions to such a degree as to harm states' revenue streams and that they should be allowed to tax Internet access to make up the shortfall. In response, Congress passed the Federal Internet Tax Freedom Act (F-ITFA), which was also signed into law on October 21, 1998 (along with COPA). The F-ITFA imposed a 3-year moratorium for local, state, and federal taxes on Internet access, as well as multiple or discriminatory taxes on e-commerce transactions. (States which had such laws on their books before October 1, 1998, were allowed to continue collecting taxes.) The moratorium has been extended twice and is now set to expire in

November 2007. As with the Supreme Court decision on COPA, the F-ITFA was put in place to provide time to study how e-commerce issues would develop and mature over time.

On a different but no less important front, the Internet has created enormous pressure for laws dealing with copyright protection and prevention of piracy of digital content. As writing, video, music, movies, software, and most other content have been digitized, legal and illegal copying have become simplified to the point of triviality. Combined with the Internet's capabilities to quickly move large amounts of data between computers, copying and distributing copyrighted materials literally exploded onto the Internet. (At one point in the mid-1990s, it was estimated that 80% of all communications capacity at U.S. colleges and universities was being taken up by students trading music and movie files.) Again, legislative and judicial action has been slower than technical innovation, creating tremendous opportunities for copyright infringement, illegal copying, and piracy of all manner of digital content. (The classic example of this phenomenon was Napster, a service on the Internet started in 1999 specifically designed to allow individuals to "share" music over the Internet. By compiling inventories of songs that had been digitized and stored on private computers, between 25 and 40 million users shared songs across the Internet, essentially violating the copyrights on almost every song that was copied. Napster was subsequently sued by artists and record companies and was eventually shut down by the courts and forced into liquidation in late 2002.)

In response to the increased level of copyright infringement, Congress passed the Digital Millennium Copyright Act (DMCA), signed into law by President Clinton on October 28, 1998. The DMCA was the U.S. implementation of the World Intellectual Property Organization (WIPO) Performances and Phonograms Treaty and the WIPO Copyright Treaty, both of which were designed to address global copyright issues brought about by technological and social changes related to improved communications and digitization methods. In addition to increasing penalties for copyright infringement on the Internet, the DMCA specifically criminalized any attempt to defeat software- and hardware-based copy protection systems being developed by copyright holders to protect their works from illegal use and copying. As with the CDA, the DMCA also limited the liability of ISPs arising from copyright infringement and copy protection circumvention initiated by their customers or users.

As the Internet matures and society continues to find new uses for this tool, the legal landscape will change to include laws specific to the Internet rather than merely including laws that are written for other media and are then applied to the Internet. In addition, the global nature of the Internet will force nations to standardize laws across national boundaries. The key issue will be balancing public interests with governmental and business interests and creating an environment that continues to promote innovation and universal access.

—Tom Bugnitz

See also Communications Decency Act; Copyrights; Electronic Commerce; Piracy of Intellectual Property; Plagiarism; Pornography; Telecommunications Act of 1996

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Interpersonal Comparison of Utility

Utilitarianism posits that the ethical good is the greatest good for the greatest number. This moral principle implies simple aggregation of individual utilities without accounting for interpersonal comparisons. Needs and tastes may differ, however, and two problems appear paramount in determining what the greatest good actually is. The first problem is variety: How do we allow for the different needs of men and women, poor and wealthy, Christian and Taoist, and so forth? The second problem, given such variety, is interpersonal utility judgment: Who is in a position to make the comparisons necessary for maximizing the good?

Both problems received notice in classical utilitarianism. Jeremy Bentham maintained in *The Rationale of Reward* that utility is a simple calculus of personal pleasure and pain, so he resolved the problem of variety by stating that the game of pushpin had objectively equal value to poetry. John Stuart Mill, in *Utilitarianism,* replied by distinguishing between higher and lower pleasures (or pains) and suggesting that lovers of lower pleasures know only half the story. Mill had to address the problem of judgment, in consequence, so he distinguished sages, who can solve the problem, from fools, who cannot.

Mill's reference to those who "know" both sides of the comparison necessarily introduces the theory of knowledge into the problem of judgment. Marxist and feminist epistemologists, referred to as perspectivists and standpoint theorists respectively, have argued that those in disadvantaged social positions will gather superior knowledge of many social situations, for the simple reason that their survival demands it. If these theorists are right, then the disadvantaged might be the sages that Mill refers to, despite his apparent intention that the bourgeoisie would hold that position. Research cited by Martha Nussbaum suggests that perspectivism may be false, however, insofar as the truly downtrodden may set their sights so low that they will not voice very pressing needs, even when asked to do so. The problem of judgment may be intractable.

A proposed solution to the problem of variety is to substitute a theory of human flourishing for the utilitarian focus on pleasure (or pain). Both Amartya Sen and Nussbaum argue that a decent standard of living might be a revised goal that would require very different resources for different people. Interpersonal differences between elderly women and children with disabilities, then, would entail different specific demands for social resources that allow for individual capabilities for flourishing, though these distinct demands may be considered approximately as the same abstract right. This approach may lead back to the Marxist notion of somehow transferring resources to individuals with greater needs—on someone's judgment.

—Eric Palmer

See also Consumer Preferences; Consumer Sovereignty; Contingent Valuation; Economic Rationality; Ethical Imperialism; Primary Goods; Utilitarianism; Utility; Utility, Principle of

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Interstate Commerce Commission (ICC)

The Interstate Commerce Commission (ICC) was the first major regulatory agency created in the U.S. government, and the first independent regulatory commission. The commission regulated the rates and business practices of interstate shipping by railroads and, later, trucking companies and barge lines, from 1887 until significant deregulation under the Staggers Rail Act in 1980, and final termination of the agency at the end of 1995. Some remaining functions were deposited in a new Surface Transportation Board (STB).

The design and functioning of all subsequent independent commissions have been influenced by the ICC. Regulatory tools that originated in legislation applying to the ICC also became the models for methods of regulation used extensively not only elsewhere in the federal government but in most state governments as well. In addition, the creation and evolution of the ICC have been the focus of intense study by scholars seeking to understand how regulation begins and changes over time.

Origin of the ICC

The construction of railroads in the mid-19th century was rapid and speculative, resulting in considerable overbuilding; multiple lines connected population centers, often with significant overcapacity. Railroads competed to steal market share from rivals, setting rates below actual costs, that is, engaging in "cutthroat competition." The goal was to drive competitors out, so that rates could be raised to supracompetitive levels, that is, permitting the collection of monopoly rents. Thus, shippers faced frequently varying transportation costs.

In addition, geography, the technical characteristics of goods, and market conditions led to price discrimination across shippers, localities, and commodities. Secret rebates went to the largest shippers. Railroads faced competition over longer hauls, at least in the shipment of bulk commodities, from barge traffic. But that was often not the case over short segments, for example, to rural areas away from major water routes. Hence, railroads created long-haul/short-haul differentials in their rates, charging more for shorter runs than for the longer runs that faced competition.

So-called "value-of-service" pricing set higher rates for shipment of "higher-valued" manufactured goods. Such goods had fewer shipping alternatives than did bulk commodities that could go by barge. Bulk commodities were more sensitive to shipping costs because such costs were a relatively higher part of their final price than for manufactured goods. Thus, elasticity of demand for rail transport was higher for bulk commodities than for manufactured goods. The railroads took advantage of this by charging higher rates for manufactured goods.

Shippers of bulk commodities, such as farmers; small shippers paying higher rates than larger competitors; producers in interior locations without a competitive means of transport; and manufacturers paying higher shipping rates bristled at such discrimination by the railroads. Even some railroad managements were unhappy about the instability in the industry and their inability to create steady, predictable rate conditions and shipping traffic that consistently met capacity.

Thus, for different reasons, there was considerable support for regulation that would eliminate the abuses and stabilize the industry. Initial attempts at regulation at the state level—many in partial response to the Granger movement of farmers centered in the Midwest—met failure as railroads bribed legislators and "captured" the regulation in a number of states. Historians now recognize that support for regulation came from multiple groups with the diverse interests noted above, that is, from farmers, merchants, and shippers in river towns; manufacturers and eastern, including New York, merchants; independent oilmen in Pennsylvania chafing against the competitive disadvantage they faced because of the high rebates extracted by Rockefeller's Standard Oil for large shipments; and so on.

In the U.S. Supreme Court's decision in *Wabash, St. Louis and Pacific Ry. Co. v. Illinois,* 118 U.S. 557 (1886), the Court invalidated the state commissions by applying the U.S. Constitution's commerce clause to railroad transportation crossing state boundaries—the states could not regulate within their state boundaries if the transport was interstate in character. The effect of the decision was to mobilize support for federal regulation. In their 1989 study of congressional voting on the Interstate Commerce Act, Thomas Gilligan, William Marshall, and Barry Weingast found that constituency effects, working through the institutional structure of Congress, that is, committees, seemed to be reflected in the vote—for example, legislators with constituents adversely affected by long-haul/short-haul differentials voted accordingly. The act received broad support from multiple interests whose congressional representatives responded to those interests.

The Interstate Commerce Act of 1887 established standards for the treatment of shippers: Rates had to be "reasonable and just"; there was to be no "unjust discrimination" in rate setting, that is, secret rebates were outlawed; undue or unreasonable preferences were not to go to any person, company, firm, or type of traffic; and long-haul/short-haul differentials were forbidden.

Value-of-service pricing remained legal, however, and some authors, such as Ann Friedlaender, argue that this was done deliberately to provide an incentive to develop the West: Shippers of bulk commodities, such as agricultural products or mineral ore, would be encouraged by the rate structure to locate in the West, shipping their goods eastward and enjoying what amounted to cross-subsidies from the higher rates for shipment of manufactured goods inside the developed East.

The economic importance of the new regulatory agency can perhaps be seen from the fact that when the Dow Jones stock average began in 1885, 12 of the 14 stocks it included were railroad stocks.

Evolution of the ICC

The ICC was established inside the Department of the Interior. But the White House changed parties in the election of 1888, with Benjamin Harrison becoming president. According to Louis Brownlow, Senator John H. Reagan of Texas, former postmaster general of the Confederacy, who had been a major player in passage of the 1887 act, did not trust Harrison, a "railroad lawyer." As a result, he helped engineer a bill in the rump Congress that met after the election, signed by President Grover Cleveland in the last days of his first administration, that took the ICC out of the U.S. Department of the Interior and made it an "independent" commission—inside no department of the federal government, floating freely in administrative space. It was an invention copied to this day, rationalized on the basis of the claim of promotion of impartial, expert, and nonpolitical decision making but originally done on the basis of a political calculation.

The first chairman of the ICC, Thomas M. Cooley, was a distinguished legal scholar who gained legitimacy for the new commission's process by making its procedures work like a court of law. This created a precedent followed in most subsequent regulatory agencies, making U.S. regulation highly judicialized, with use of detailed administrative procedures, a judge-governed process for adjudication of cases, and reliance on adversarial development and examination of case evidence.

The initial reactions of railroad executives were mixed, though at least some observed that the commission could promote long-needed stability. At the same time, it was recognized that opportunities existed to take advantage of the commission's limited powers and limited staff.

In the 1890s, Supreme Court decisions constrained the ICC's powers. By the turn of the century, however, the commission gained members determined to acquire new enabling legislation that would permit it to reassert its control of the railroads. The approach of these members, and of those in the Congress that soon provided this legislation, reflected the views of the Progressive Movement as well as of a Progressive president, Theodore Roosevelt. Government would be removed from politics and run like a business, but in the public interest. Government officials were to behave like professional public servants, and regulators were to remain free of the taint of business influence, regulating industry so as to retain the benefits of a market, but under government controls. Among the new ICC members was Franklin K. Lane, later secretary of the interior, one of the most able officials ever to serve in the U.S. government. He joined the commission in 1906. At his untimely death in 1921, he was so popular and widely respected that many considered that, had he not been born in Canada, he would have been a likely candidate for president.

As a result of scholarship in the last half of the 20th century, ICC regulation was widely discredited; the effects of commission regulation on consumers and even the regulated industry were criticized. But it is important to recognize that the ICC in its earlier decades was considered by those who administered it—and, indeed, by a public who respected it—as a noble experiment to control an industry whose abuses would reappear without such controls. The highest norms of public service were reflected in such ICC commissioners as Thomas Cooley, Franklin K. Lane, and the long-time chair of the commission in the 1920s and 1930s (and, for a time, coordinator of transportation), Joseph Eastman. It was only relatively recently, in 1883, that the Pendleton Act had created the Civil Service System, bringing the merit system to the U.S. government. Thus the ICC was the centerpiece of a new set of expectations for the behavior of government officials in the United States; it was in its first decades the laboratory for what constituted a new ethics of the public service. Thus, among the legacies of the commission were not only the sometimes ineffective design of independent commissions, the rigidities (as well as due process benefits) of a new administrative process, and the particular industry-protective regulatory tools, such as rate-of-return regulation, that were introduced in the commission but also a view that the public service could and should be conducted with the highest dedication to the public welfare.

A steady flow of Progressive legislation restored and expanded the ICC's powers. These included the Elkins Antirebating Act of 1903, the Hepburn Act of 1906, the Mann-Elkins Act of 1910, and the Valuation Act of 1913, which led to a massive study by the ICC to value railroad properties in order to be able to regulate rates and investment. The stream of new legislation culminated in the Transportation Act of 1920, a watershed in the history of regulation in the United States. One effect of the act of 1920 was to establish rate-of-return regulation as the standard model for economic regulation in the United States; it was copied in many regulatory settings across the federal and state governments. Economic regulatory agencies were to set rates based on a study of the fair rate of return. In practice, this was difficult to do accurately and at any rate tended to protect the industry, guaranteeing its continued existence, if not its consistent profitability. Rate setting, like other activities of the commission, was done on a case-by-case basis, perpetuating the legalistic model established by Judge Cooley.

Over time, the size of the commission itself grew, from 5 to 9 to 11 (in later years reduced to 7 and to 5), with commissioners assigned to “divisions” of the commission, to which some decisions were delegated. The sheer number and complexity of this casework caused much of the commission’s work to be further delegated to staff members and inhibited overall policy making and planning by the commission. Carriers had to submit detailed lists of tariffs for the shipment of every item between every pair of locations for commission review. The commission also controlled routes for service, starts and stops of service, mergers, and many other features of the provision of transportation services.

A new technology of transportation—motor vehicles—raised new issues for the ICC. Trucking companies had competitive advantages over regulated railroads. They could set and adjust their rates to gain quick competitive advantage over the railroads, who would have to ask the ICC for rate adjustments in a relatively lengthy process. Large trucking companies, however, feared competition from smaller truckers and disliked the rate wars that destabilized the industry. A railroad group, the Association of Railroad Executives, helped write new legislation that brought the large truckers into the ICC in the Motor Carrier Act of 1935, treating them as if they were railroads. The effect was to erect barriers against interstate competition by smaller, nimble trucking competitors, who would not want to pay the expense of maintaining elaborate lists of tariffs—shipping rates that had to be approved by the ICC—for the shipment of any item between any two interstate locations.

The regulation of air transportation, under the Civil Aeronautics Act of 1938, which was later performed by the Civil Aeronautics Board, copied ICC regulation and narrowly escaped becoming part of the ICC itself. The Transportation Act of 1940 added major barge lines to the ICC’s authority, and the ICC’s task became one of allocating traffic among three modes of transportation—railroads, trucks, and barges—according to what is now recognized as a mythical theory of what kinds of traffic and rates were proper across the different modes. In essence, the ICC became a protector of these regulated modes of transportation, approving their rates so as to stabilize conditions of competition among the modes. Indeed, representatives of the companies would haunt the ICC’s tariff filing room and file challenges whenever companies filed tariffs that undercut their rate pricing.

Criticism of the Effects of ICC Regulation

Because the system of regulation under the ICC was consistently deferential to each mode of transportation, shipping rates were maintained at higher than the competitive level. Although in its last decades the ICC tended to serve transportation company over consumer interests, the effect of its regulation was also to perpetuate a system of transportation that lacked innovation and was resistant to change. Despite their protection, transportation companies still struggled. The agency itself seemed unable to do systematic transportation planning, was slow to react, and was unable to innovate. Except in several notable cases, its leadership was consistently mediocre. The administrative process, dominated by case-by-case reviews, was unable to view issues from a perspective other than that of cases and produced long delays in decisions. In 1970, a muckraking but careful overview of the ICC’s performance directed by Robert Fellmeth (as part of a Ralph Nader study group) found serious administrative deficiencies. The appearance of potential industry favoritism was inescapable. Of the last 11 commissioners to have left the ICC at that time, 9 either took jobs in the regulated industry or practiced law before the commission. The other two retired. Senior ICC staff members had very long tenures and no inclination to change ICC practices. Over numerous advisory committees and liaison groups in which the agency participated to assist it in gathering information and developing policy, none had any representatives of consumers.

Deregulation of the ICC

By the late 1950s, studies by economists had established that the effects of ICC regulation did not seem consistent with the nominal purpose of the agency. Regulation had frozen into place an industry that had performed less well than other industries while not protecting the interests of consumers and shippers—precisely the reason that had led to regulation in 1887. Pressures to reform the agency mounted. Under the Staggers Rail Act of 1980, signed by President Jimmy Carter, many of the rate- and route-setting powers of the ICC were deregulated. The general trend since then has been improvement in the financial performance of the railroad industry, together with lower shipping rates for many, though not all, shippers.

The ICC Termination Act of 1995 transferred some of the functions of the ICC to a new agency, the three-member STB, and to other federal agencies, eliminated other functions, and abolished the ICC at of the end of that year. Ironically, the STB remained, functionally, an independent commission, though administratively located inside the Department of Transportation. Thus the demise of the ICC was actually partly symbolic in that significant regulatory functions continued in the STB, while members of Congress took public credit for terminating the oldest of the federal regulatory agencies. But the influence of the old ICC lives on in the administrative processes of the independent regulatory commissions and of other regulatory agencies in the federal and state governments of the United States.

—Barry M. Mitnick

See also Administrative Procedures Act (APA); Barriers to Entry and Exit; Comparative Advantage; Competition; Consumer Activism; Deregulation; Due Process; Iron Triangles; Market Failure; Price Discrimination; Public Interest; Regulation and Regulatory Agencies; Unfair Competition

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Intrinsic Value

Intrinsic value is traditionally understood to be the value a thing has in virtue of its own nature, or its own intrinsic properties. Thus, a thing has intrinsic value "in itself" or "for its own sake" or "in its own right." This implies that intrinsic value is "nonderivative" or "nonrelational" since things that have intrinsic value do not have it because of their relation to other things. For example, many writers argue that pleasure is intrinsically valuable because pleasure is good in itself and not because of its relation to something else. Other things sometimes said to be intrinsically valuable are, for example, happiness, virtuous acts, knowledge, or experiences of beauty, friendship, or love. Contrasted with intrinsic value is extrinsic value, which is the value a thing has in virtue of its relation to something else and not in itself or in its own right.

Final Goods and Instrumental Goods

Closely related to the distinction between intrinsic and extrinsic value is one between final goods and instrumental goods. Final goods are things desired or chosen for themselves or for their own sake. Instrumental goods are means or methods selected to accomplish final goods. For example, suppose you are looking at job openings on the Internet. Someone asks you why you are doing this. You reply, "I am trying to find a job." The rest of the conversation continues—Why do you want a job? So I can make money. Why do you want money? So I can provide my family with a decent standard of living. Why do you want to do that? So I can be happy. Why do you want to be happy?—Now what do you answer? Probably that you do not want to be happy for the sake of something else but for itself. Thus, happiness is your final good, and all the steps you take to achieve happiness, the means you use to move toward that goal, are instrumental goods.

Final Goods and Intrinsic Value

A controversial issue is how to characterize the relation between intrinsic and extrinsic value on one hand, and final and instrumental goods on the other. Consider first the relation between intrinsic value and final goods. There are several possibilities. One is that something is intrinsically valuable if and only if it is a final good. Thus, all final goods are intrinsically valuable, and only final goods are intrinsically valuable. If so, to say that something is intrinsically valuable is just to say that someone values that thing for itself or as a final good. Call this possibility "subjectivism" since intrinsic value is tied to what is desired or chosen for its own sake by some person.

A second possibility is "modest objectivism." Modest objectivists believe that the only things that are intrinsically valuable are certain human experiences. However, they deny that what makes such experiences intrinsically valuable is that they are valued for themselves, that is, that they are final goods. Instead, they argue that some experiences are intrinsically valuable by virtue of their own nature or their own intrinsic properties. For example, modest objectivists claim that happiness is valuable in itself or in its own right and not merely because happiness is valued for itself by some people.

A final possibility is "total objectivism." Like modest objectivists, total objectivists argue that things have intrinsic value by virtue of their own nature and not because they are valued by some person. However, they deny that human experiences are the only things that are intrinsically valuable. They argue that intrinsic value can be exemplified by, for example, natural states such as biodiverse environments, old-growth forests, wilderness areas, and other things that exist independent of human experience.

Until fairly late in the 20th century, modest objectivism was the mainstream philosophical view about intrinsic value. More recently it has to a large extent been displaced by various forms of subjectivism and to a lesser extent by total objectivism.

Instrumental Goods and Extrinsic Value

Instrumental goods are means used to achieve a goal. Hence, instrumental goods have derivative value; they are not chosen for themselves but for the sake of the goal. It seems, then, that instrumental goods have extrinsic value. However, if the three positions discussed above can be mirrored in the distinction between instrumental goods and extrinsic value, then subjectivists, modest objectivists, and total objectivists could each have a different understanding of the relation between instrumental goods and extrinsic value. For example, subjectivists could argue that things have extrinsic value only because they are valued as instrumental goods by some person, while modest objectivists might claim that some means to ends can contribute to final goods in ways that are not instrumentally valuable and so have extrinsic value that is not simply instrumental.

According to several writers there are things that have extrinsic value but are not means to ends. For example, the copy of the Declaration of Independence in the National Archives derives its value from its relation to the founding of the United States. Since it has derivative value, it is not intrinsically valuable in the traditional sense, but neither is it instrumentally good. Thus, its value is extrinsic but not instrumental. There are many things of this kind. They are of no particular instrumental use, but we value them for their relation to something else. Our lives would be much the poorer were they lost or destroyed.

Intrinsic Value and Ethics

Many ethical theories construct an account of "the right" on the basis of "the good," that is, intrinsic value. Thus, ethical theories often appeal to intrinsic value either to explain why some things are ethically right and others wrong or to justify choosing one action instead of another or to ground judgments of what is ethically appropriate or worthy. For example, classical utilitarians claim that actions that create intrinsic value, which they take to be states of pleasure or happiness, are ethically right, and actions that create intrinsic disvalue, that is, unhappiness or pain, are ethically wrong.

Intrinsic value plays a different role in ethical theory depending on whether one is a subjectivist, modest objectivist, or total objectivist about intrinsic value. As one might expect, this complicates things. Subjectivists, for example, believe that intrinsic value just is whatever is valued for itself by some person. But people can have final goods that are distinctly undesirable from an ethical point of view. For instance, exceptionally cruel or malicious people might choose the pain of others, or destruction and disorder, as their final good. If so, then from the fact that something is a final good, and hence intrinsically valuable for subjectivists, one can infer nothing about whether that final good is ethically acceptable, worthwhile, or admirable. To show that it is ethically acceptable, subjectivists need an independent argument, one that, on pain of circularity, does not appeal to intrinsic value.

A subjectivist might reply that, as a matter of fact, people only choose final goods that we know are ethically acceptable. For example, suppose, as some writers claim, that happiness is everyone's final good. Thus, as cruel, malicious, or even evil as someone might be, happiness is what they really want. It is not their final good that is the ethical problem but the means they use to achieve it. However, other writers argue that this is much too restricted a view of human potentiality and of the possible range of human choice and desire. Not all people choose happiness as a final good, and even if, in their quest for their final good, they manage to achieve happiness, it is a by-product or side effect of their choice, not the reason they choose it.

In contrast to subjectivists, modest objectivists use intrinsic value to construct an account of what is ethically acceptable, worthwhile, or admirable that does not depend on what people might happen to desire or value as a final good. A typical example of modest objectivism in ethics is classical utilitarianism, which uses intrinsic value in two ways. First, for classical utilitarians, the fact that something is ethically acceptable, worthwhile, or admirable is explained by the fact that it is intrinsically valuable. For example, the fact that happiness is an ethically acceptable final good is explained by the fact that happiness is intrinsically valuable. Second, utilitarians argue that if one action creates more intrinsic value than another, then we are ethically justified in performing the first instead of the second. Thus, intrinsic value plays a dual role in classical utilitarianism: It explains why some things are ethically acceptable and justifies doing some acts as opposed to others.

Cruel and malicious people also cause trouble for utilitarian ethical theories. If happiness is intrinsically valuable, then any happiness such people get from their misdeeds is intrinsically valuable. Are utilitarians thus committed to saying that happiness derived from cruelty or that malice is ethically worthwhile, that is, that it is a good thing that such people are happy? How they might escape this conclusion is a topic for the next section of this entry.

Finally, total objectivists believe that intrinsic value can be exemplified in things that exist independent of humans, such as states of the natural environment. They face two different problems. The first is that they need to show how we can know that natural states, for example, wilderness areas, exemplify intrinsic value. This is an epistemological problem, one that goes far beyond the limits of this entry. It is fair to say, however, that all the proposed solutions to the problem are extremely controversial. The second is that they need to show that the intrinsic value exemplified by wilderness areas is ethically relevant to persons. In other words, unless the intrinsic value of wilderness is in some way intimately related to human interests, concerns, and desires, what ethical pull can it exert on us? Why should it be a part of our ethical deliberations, judgments, or actions? If total objectivists cannot convincingly answer this question, then the intrinsic value of the wilderness and other natural states has no obvious relevance to ethics. On the other hand, if it does have an intimate relation to human concerns, then it is not clear in what sense it is independent of humans.

Objectivism and the Usefulness Objection

Objectivists argue that intrinsic value comes in different amounts or degrees. For instance, a situation in which many people feel pleasure has more intrinsic value than one in which no one feels pleasure. Now, a difficulty is determining how much more, and the reason this is important is because situations with more intrinsic value are supposedly more significant or important from an ethical point of view. Thus, we need a reasonably precise way of measuring intrinsic value. However, there is no widely accepted method for measuring pleasure or anything else said to be intrinsically valuable. The best that most writers have been able to do is come up with rough intuitive judgments, often disputed by other writers, that, for example, situation X has more intrinsic value than Y. It is an open question whether these rough judgments will bear the ethical weight often placed on them.

A second difficulty is that several writers argue that intrinsic value comes in different kinds as well as different amounts. For example, pleasure is one kind of intrinsic value, knowledge another, and virtue still another. Because these are different kinds of value, a different kind of measurement is needed for each one. However, no one knows what these might be. Furthermore, there is no agreement about how we might compare one kind of value with another and so arrive at a final judgment about the ethical significance of value present.

Of course, proposals have been made about how to measure intrinsic value. One of them, made by G. E. Moore, suggests that to measure intrinsic value we need to see it in the context of what Moore called an organic unity. Basically the idea is that we must be aware of the "big picture" before we make any judgments about amounts of intrinsic value. For example, a malicious person might derive happiness from the pain he causes, but when we take into account his evil motives and all the unhappiness his actions cause for other people, we see that the total situation is intrinsically bad, not good, and so not ethically acceptable. Thus, his happiness, while intrinsically valuable, is part of a larger situation that is not intrinsically valuable.

Moore's proposal seems intuitively right, but it still does not allow us to make the specific assessments of value needed to justify specific actions or policies. For that we need accurate results, but at best we can get only vague indications. Given all this, the question is whether intrinsic value is of any real use in practical ethics. If we cannot make reliable estimates of intrinsic value, then it is hard to see how we could make reliable judgments about what we ought to do based on those estimates. If this is right, then even if intrinsic value helps explain why some things are right and others wrong, it is of little or no use in helping decide which specific actions are right or wrong.

Intrinsic Value in Business

Businesses, we are often assured, are in the business of satisfying the needs and wants of customers. Thus, business is one of the instrumental links in the chain that leads to intrinsic value. From an ethical point of view this is surely a strength of business since people have lots of needs and wants that ought to be satisfied. But it is also the place at which many of the traditional objections to business are made. One such objection is that businesses typically do not discriminate between those needs and wants that ought to be satisfied and those that do not. Long experience shows that satisfying some of our needs and wants is not conducive to long-term pleasure or happiness and so is incompatible with creating intrinsic value. However, businesses often appear unmindful of this issue and will supply anything that is legal regardless of its long-term effect. Moreover, the argument continues, business tries as best it can to create needs and wants, where none existed before, with little thought to the long-term consequences for customers. Business creates customer demand to accommodate its own interests, not to create the means to intrinsic value for the people business claims to serve. Since businesspeople are well aware of the damaging consequences of creating and satisfying needs and wants that are in the long term harmful rather than helpful, business as a whole is not merely an amoral institution, it is an immoral one.

The usual response to this argument is that business is not, and ought not to be, the authority on what is best for individuals. That is left for individuals to decide and to bear the responsibility for decisions made. Business is in no position to substitute its ideas of the good life for the judgment of persons who live those lives. If someone decides that using a product or service is not in his or her interests, the solution is simple—do not purchase it. If a sufficiently large group decides that a product is harmful, then laws can be passed to prohibit it. This is an appropriate exercise of individual and social control and provides a straightforward solution to the problem of regulating products that some think harmful.

A second objection is that businesses do not satisfy some legitimate wants and needs. Products and services are provided for money, but not all who genuinely need them have the money to pay. Thus, they are unjustifiably—some say unscrupulously—denied the means they need to give their lives the intrinsic value that all persons deserve.

The response is that business serves a vital function in society that it cannot fulfill without making a reasonable profit. If business were forced to provide goods and services to everyone, regardless of his or her ability to pay, then it would not survive long. This would be to the detriment of everyone, both those who can pay and those who cannot. Thus, providing for those who cannot pay is not a problem business can solve. It is a social and political problem, and if it can be solved at all, it can only be solved by social and political methods.

—Robert Frederick

See also Consequentialist Ethical Systems; Environmental Ethics; Ethical Nihilism; Hedonism, Ethical; Instrumental Value; Intuitionism; Moral Realism; Moral Reasoning; Noncognitivism; Virtue Ethics; Well-Being

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INTUITIONISM

Ethical intuitionism (or intuitionalism, also known as moral intuitionism) is the doctrine that ethical beliefs can be justified noninferentially through intuition. It designates those philosophical systems that consider intuition as our fundamental moral basis.

Intuition is both a psychological and a philosophical construct signifying knowledge or perceiving something without deductive or inductive reasoning. The knowledge or perception results from an amalgamation of cognition, affect, common sense, and ethical sense, all used to formulate moral rules for ethical decision making.

Moral intuition is characterized by some moral philosophers as a kind of apprehension of moral truth akin to mathematical knowledge, in which certain self-evident axioms are understood by mathematical intuition. For instance, one is justified in believing the proposition "Parallel lines never meet" by reflecting on and adequately understanding the proposition's content. Ethical intuitionists claim that such self-evidence also holds for certain ethical propositions (e.g., "It is prima facie wrong to deliberately cheat customers"). Nonetheless, while in mathematics, principles claimed to be self-evident are precise and largely agreed on by the experts, in ethics, so-called self-evident principles are vague and widely disputed. Consequently, various intuitionists differ on the nature of the moral truths that are apprehended via intuition.

People frequently face difficult moral choices such as whether to hire people with disabilities despite their lower productivity levels or whether their company should relocate overseas. They do so by intuiting what to do, relying on *subjective* feelings. Hunches, flashes of insight, and "executive experience" might be regarded as intuitive knowledge.

Examples of intuitions that most people would agree are moral truths include the following: Enjoyment is better than suffering; it is unjust to punish a person for a crime that person did not commit; courage, benevolence, and honesty are virtues; and if someone has a right to do something, then nobody has a right to forcibly prevent him or her from doing so. In each case, the appearance of truth is intellectual; you do not perceive that these things are true with your five senses.

Examples of ethical claims that are *not* intuitive, even for those who believe them, include the following: The United States should not go to war to defend other countries but only to defend itself; taxation for welfare purposes is unjust because it involuntarily takes money from some citizens; and capital punishment is wrong. Although these propositions appear true to many, they do not count as intuitions since they depend on other beliefs.

Therefore, while reason underlies the basis of most theories of moral philosophy, it has a more limited role to play in intuitionism. Although some basic truths are known without reason, once these truths about prima facie obligations are known, reason along with other knowledge can be used to form other ethical beliefs. For instance, the notion that "Taxation to raise welfare program funds is unjust" depends on beliefs such as "Most welfare recipients lazily avoid work" and "Most people's taxes are already too high," and so it is not directly apprehended. Nonetheless, intuition has a role in one's concluding that the taxation for welfare is wrong, for intuition informs this individual that taking people's money for uses those people disagree with is prima facie wrong.

In addition to reason, religion provides another general ethical foundation. Christian religious ethics, for example, inspired by *divine revelation* and *divine command theory,* implies that we are innately sinful and need God to reveal moral truth to us. Intuitionism, on the other hand, suggests that moral truth is known by intuition rather than by either divine revelation or reason.

Intuitionism's Truth Claims

Intuitionism generally makes six truth claims, based largely on the work of 20th-century philosophers G. E. Moore, W. D. Ross, and H. A. Prichard. However, not all intuitionists subscribe to all these truth claims.

1. Moral truth is about simple constructs like "good," which are inexplicable through words. Nonetheless, moral common sense suggests the veracity of these truth claims. Hence, while the concept "ought" cannot be readily defined, its characteristics are clearly discerned as entailing a duty to act on what is good.

Moore argued similarly regarding the moral claim "good": Goodness is an indefinable, nonnatural property of which we have intuitive awareness. For instance, if someone defines "good" as "socially approved," we should ask, "Are socially approved things good?" If "good" means "socially approved," this question should not be significant. But this question is significant, showing that "socially approved" is not the definition of "good." It is not the "obvious wrongness" of many socially sanctioned actions that refutes this definition, but the fact that the question is meaningful shows that this is not at all a definition.

2. *Moral realism:* There are *objective* moral truths, existing independent of human thinking or feeling. For instance, hatred is wrong in itself, and it would still be wrong even if everyone approved of it. Intuition can sense such truths.

Consequently, intuitionism should not be confused with *emotivism,* which suggests that moral judgments are merely expressions of *personal feelings* and are *not* expressions of facts. When emotivists say "This is wrong," they really mean, "I don't like it." Emotivists' moral judgments are expressions of attitudes. Thus, if a manager believes that making a minor cosmetic change in a product and calling it "new and improved" will bolster sales without hurting anyone, that is an emotivist moral decision. The emotivist's only *moral authority* is oneself.

3. Moral truths are self-evident to a mature mind through a kind of immediate, intellectual awareness or "intuition," the foundation of our ethical knowledge. To arrive at the self-evident principles of morality requires reflection and intellectual maturity. Hence, a true ethical judgment is self-evident as long as we are reflecting clearly and calmly and our judgment is not distorted by either (1) self-interest or (2) faulty moral upbringing.

4. These self-evident beliefs are sufficient in themselves for their justification. The central intuitionist claim is that an agent's noninferential understanding of moral propositions is sufficient for the agent to be justified in believing the proposition. Such beliefs are not justified inferentially but rather intuitively by reflecting on and adequately understanding their content.

5. Evaluative facts cannot be reduced to natural facts. Such *ethical nonnaturalism* suggests that moral philosophy is fundamentally autonomous from the natural sciences. This contrasts with *naturalism,* a philosophical perspective, popularized by the philosopher David Hume during the 1700s, that holds that all phenomena can be explained by natural causes and laws, and so moral truths can be discovered by observing and experiencing the world. The moral philosophy consequentialism is naturalistic in that it focuses on actual outcomes to determine if an act is morally justified. G. E. Moore rejected this philosophy and called it the "Naturalistic Fallacy," believing something is good or bad in itself rather than because of any effects it produces.

6. Our innate knowledge of moral truths gives us reasons for action independent of our desires, again differentiating intuitionism from emotivism. Ethical intuitionism is essentially an externalist theory, arguing that there is no essential internal connection between moral beliefs and motives and that there is no essential reason that the belief "X is wrong" leads to a desire not to do X. Hence, ethical intuitionism denies internalism—the view that moral beliefs function as a motivating factor, that is, that there is an internal connection between one's belief that "X ought to be done" and that person's motivation to do X.

Variations in Intuitionism

Although not all intuitionists agree on the exact nature of intuitionism, nonetheless, all ethical intuitionists agree in characterizing intuitions as cognitive mental states that do not depend on observation or inference.

The first literature on intuitionism suggested that moral intuitions result from an independent sixth sense, the "Moral Sense," often considered synonymous with conscience. Consequently, people distinguish rightness with their moral sense, analogous to perceiving odors with their olfactory sense. This thinking was rejected by some intuitionists because people lack independent verification that such a sixth sense exists.

Ethical intuitionism has also varied in its popularity over the past several centuries. It was the dominant moral theory in Britain from the 18th century through the first third of the 20th century. However, its popularity waned by the mid-20th century—it was apparently the victim of the rise of both logical positivism (which says that only empirically verifiable ideas are significant) and philosophical naturalism. More recently, however, hostility toward ethical intuitionism has subsided, and some recent work suggests it might be enjoying a resurgence of interest in academic philosophy.

Advantages and Disadvantages of Intuitionism for Moral Decision Making

Advantages of Intuitionism

Intuitionism provides several benefits for ethical decision making:

- If something strikes us as intuitively wrong it probably is. This is embodied in the cultural truism "When in doubt, don't," keeping the businessperson from moral lapses most of the time.
- We will not end up with a hurt conscience and can therefore be guilt-free and pass the "sleep test," thereby conserving energy for business and personal endeavors.
- Intuitionism is simple to implement; no hard thinking or philosophical calculations are required. Intuiting can become a habit of thought resulting in quick decision making, so important in the fast-paced business world. Hence, by default it is probably the most widely used approach in solving everyday life and business ethical dilemmas.
- This approach is often experience based (although, strictly speaking, it is not supposed to be so). The well-seasoned manager presumably knows best.
- Independent people, notably senior business executives, appreciate that there is no authority to answer to but one's self.
- Everybody has an innate awareness of right and wrong (the law or general revelation of conscience). For instance, most people are intuitively aware that murder, rape, child beating, stealing, adultery, and disrespect for parents are wrong.

Disadvantages of Intuitionism

There are some serious problems with intuitionism:

- Not everyone shares the same innate awareness of right and wrong. There is lack of agreement when it comes to gray areas such as binge drinking, cheating on tests, and the medieval sins of gluttony and usury; that is, not all intuitions are equal—some are more credible than others since (1) some intuitions are stronger, or more clearly seem true, than others; (2) some intuitions are more widely shared than others, and, all else being equal, an intuition that many agree with is more likely to be true than is an intuition that many disagree with; (3) some intuitions have simpler contents than others and are therefore less prone to error; and (4) some types of intuitions are more open to bias than others. For these reasons, intuitions should not be embraced uncritically.
- There are no objective standards by which to judge intuitionism's accuracy. However, the intuitionist would say that the experience is so powerful that it is self-authenticating. Nonetheless, most intuitionists would admit that at most, some moral truths are self-evident.
- It is often difficult to justify intuitive decisions. In business, scientific, objective analytical decision making is preferred to relying on subjective feelings. One does not justify a business proposition by announcing, "I just feel this would be the right thing to do." Yet, with intuitionism, at best, decisions are made on an emotional basis and then rationalized after the fact ("I honestly did what I thought was right"; "I made a good faith effort"). Unfortunately, conscience is then used as a license or rationalization of bad behavior.
- Our self-interested tendency is to rationalize our behavior, convincing ourselves that an action is excusable,

at least in a particular instance ("It is lawful, so I'm respecting the law"; "He did it to me, so I'm just reciprocating"; "They had it coming to them, thus I'm serving justice"; "Everyone is doing it, so I'm just respecting the culture around here"). Such rationalizations are perhaps the biggest cause of unethical behavior in a business world demanding rational analysis. When such people say something is right or wrong, they are really just expressing their preferences and then using moral language to give greater persuasive power to their argument.

Nonetheless, intuitionism reminds us not to act when our conscience is violated. A pang of conscience is a warning to stop and reflect on the rightness of what you were doing. One final caveat: You cannot justify your action simply by saying you were following your conscience.

—Geoffrey P. Lantos

See also Divine Command Theory; Ethical Decision Making; Ethical Naturalism; Moral Realism; Utilitarianism

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Invisible Hand

The *invisible hand* is a phrase, originally used as a metaphor by Adam Smith, that summarizes how social and economic outcomes arise without design or explicit agreement. The *invisible hand* refers, then, to how individuals, interacting in purposeful ways, could bring about a result that was not part of their intention. Such an unintended outcome is sometimes referred to as a spontaneous order, but the concept of the invisible hand is employed to designate either the *process* by which the pattern or outcome is produced or an *explanation* of that process. In either sense, the idea should be kept distinct from the notion of a hidden hand that purports (as Robert Nozick describes) to explain seemingly unpatterned events as, in fact, the result of someone's intention or design. The invisible hand has been employed to explain the division of labor, the emergence of a medium of exchange, the growth of wealth, the patterns (such as price levels) manifest in market competition, and the institutions and rules of society.

Adam Smith and Others

Adam Smith invokes the phrase, on two occasions, to illustrate how a public benefit may arise from the interactions of individuals who did not intend to bring about such a good. (Smith also employs the phrase in a third instance—in the essay "History of Astronomy"—to describe how the god Jupiter produces disorder.) In Part IV, Chapter 1 of *The Theory of Moral Sentiments* of 1759, Smith explains that as wealthy individuals seek their own interests, employing others to labor for them, they "are led by an invisible hand" to distribute the necessities that all would have received had there been an equal division of the earth. In Book IV, Chapter 2 of *The Wealth of Nations* of 1776, arguing against import restrictions and explaining how individuals prefer domestic over foreign investments, Smith uses the phrase to summarize how self-interested actions are so coordinated that they advance the public interest. In these two instances, a complex and beneficial structure is explained by basic principles of human nature and economic interaction. However, there are other occasions in which Smith employs the idea of the invisible hand without invoking the phrase itself. In the opening paragraph of Chapter 2 of Book I of the *Wealth of Nations,* he describes how the division of labor is not the result of far-seeing wisdom but a gradual outcome of a natural "propensity to truck, barter, and exchange." Later in this same treatise, he delineates how individuals are so guided by prices that the supply of goods tends to meet demand. More generally, Smith explains how the patterns of commerce, including the overall creation of wealth, arise out of individuals responding to and endeavoring to succeed in their own local circumstances. Although Smith often refers to economic agents as self-interested, he does not mean to suggest that their motivations are selfish. Rather, the agents are motivated by beliefs and intentions that manifest their local knowledge and particular concerns (including those relating to their families) rather than some broader conception of a public good.

Smith devises the phrase *invisible hand,* and even incorporates the notion of unintended outcomes into his account of the emergence of moral standards (in *The Theory of Moral Sentiments*), but he was not the first to use this idea. Earlier in the 18th century, Bernard Mandeville had contended that prosperity could be brought about only if individuals were permitted to act on their self-interest as constrained by a rule of law. Mandeville also set forth an account of how moral norms might develop among egoistic creatures prone to love praise and flattery. David Hume's account of the conventions of justice (*A Treatise of Human Nature,* 1739–1740) seems to assume their unintended emergence via an invisible hand process. And further along in the 18th century, Adam Ferguson, in his *Essay on the History of Civil Society* of 1767, maintains that many institutions—such as language, property, governmental structures, and some traits of character—are, as he writes, "the result of human action, but not the execution of any human design." In the 19th century, in *Principles of Economics* of 1871, Carl Menger, the father of the Austrian School of Economics, traces the origin of money not to contract or legislative act but to a process in which individuals seek to secure an item, not of immediate need, that may be exchanged for a more desired good. In *Problems in Sociology and Economics* of 1883, Menger articulates the idea of a genetic theory that reconstructs, out of the purposive acts of individuals, the "organic institutions"—language, law, money, and the market itself—that were not otherwise intended.

In the 20th century, Friedrich Hayek has most notably used the idea of the invisible hand, contending that the market itself is an unintended or spontaneous order. Within that order there are other patterns, such as market prices and rules of conduct, that manifest the unintended coordination of disparate actions. Hayek describes how the prosperity of the market (or "Great Society") is possible only because the general and abstract laws that constitute its framework allow for spheres of liberty within which individuals can make use of their own knowledge to produce and to experiment. The disparate and dispersed knowledge of anonymous individuals is coordinated by prices that signal to individuals how best to meet one another's expectations. Hayek has also defended the invisible hand evolution of moral and cultural norms. His theory, though not a consistently stated one, seems to suggest at least two lines of cultural evolution. In his earlier works (such as *The Constitution of Liberty,* 1960), he propounds a thesis that rules will gradually evolve in an unintended and trial-and-error fashion. Under a framework of law that is general, impartial, and protective of private property, rules will emerge and survive that will, in general, transmit knowledge relevant to success in a variety of circumstances. In his later works (e.g., *Law, Legislation, and Liberty,* 1973), he suggests that the unit of evolutionary selection is not the rule but the whole group: A rule survives only insofar as it is practiced by a population that itself is favored by some evolutionary process.

Invisible Hand Explanations

We may distinguish the invisible hand as a metaphor for unintended processes (and their outcomes) and as a type of explanation. An invisible hand explanation may be invoked for any complex state of affairs that is, was, or could be an unintended outcome of individual actions. Such an explanation, which is a descriptive or value-free rather than a normative account, may be of two basic types. The classic, Smithian, explanation is a genetic account of how a structure, pattern, or regularity comes into existence; such an account typically involves an aggregative or equilibrium process in which small adjustments combine or accumulate into a larger result. The other type of explanation, often taking on a functionalist form, explains the survival or persistence of a regularity in terms of some specific property that contributes to the survival of that pattern (e.g., that the regularity has some effect or function that contributes to the survival of the society). These two general types of invisible hand explanations are sometimes merged into a single account, but they are, in principle, separable.

The classic invisible hand explanation of emergence must illuminate how a pattern arises unintentionally (or "spontaneously") from some initial conditions or circumstances. Such an explanation proceeds in three stages: (1) Along with a specification of the initial conditions, there must be some description of the agents (including, for example, their rationality, knowledge, and moral beliefs). These initial conditions may, of course, vary from one explanation to another, and there is no requirement that the agents possess perfect information or be completely rational. (2) Some lawlike principle(s), or some description of a stable mechanism, is employed to describe the process by which the outcome emerges. The lawlike principle could, for example, express some feature of human nature (e.g., that human beings are generally motivated by self-interest or that human beings relish praise). (3) Finally, there must be a narrative of how agents, situated in these circumstances and acting in conformity with the lawlike principle, would bring about a structure, pattern, or norm that was not part of their intention. There must be a plausible case that the resultant structure, pattern, or norm was not intended. Given that intention, at both the individual and collective level, is a matter of degree, it follows that the invisible hand process is also a matter of degree. Finally, in any such explanation, one may distinguish whether the outcome arises at some specified moment (synchronic) or over the course of time (diachronic). In an evolutionary explanation of *emergence,* the aggregation may occur over time, perhaps as a cumulative process of trial and error in which individuals imitate other successful persons. On the other hand, an evolutionary explanation of the *persistence* of a pattern or structure takes either a biological or cultural form, depending on whether, say, the gene or a cultural regularity is the unit that contributes to the survival of either individuals or groups.

As an illustration of an explanation of emergence, consider how Mandeville attempts to show how moral norms develop out of conditions in which there is no morality and in which agents are often ignorant and not fully rational. He appeals to a natural desire for praise and flattery as the lawlike principle that allows the emergence of norms of evaluation via a cumulative process of praise and flattery. And, as already mentioned, Adam Smith maintains that the division of labor results from a natural "propensity to truck, barter, and exchange." More recently, Robert Nozick has sought to show that in anarchical conditions governed by natural rights, a state could emerge without violating those very rights. In so doing, he uses lawlike assumptions about the economic behavior of firms (private protection agencies), as well as some commonplace assumptions about human action.

Reflections and Implications

Hayek suggests that many of the rules, structures, and patterns of society are the outcomes of invisible hand processes. However, it is an open question as to whether such a broad conclusion is correct and, in particular, whether moral norms are the outcomes of such spontaneous processes or reflect the influence of reason or biology. Hayek also contends that unintended processes that occur under certain conditions are preferable to designed structures: Only an invisible hand process could generate a society of great complexity, for only a spontaneously ordered process allows the coordination and use of dispersed, and often tacit, knowledge. Insofar as important outcomes may be achieved if individuals are allowed to act on their own local knowledge, the invisible hand provides a theory of how a society can be prosperous without being designed, directed, or planned by a sovereign. Although there is no doubt that many unintended outcomes are beneficial, their positive character will, in large measure, depend on the conditions that provide the framework for the invisible hand process. Therefore, it is important to understand the nature of the laws and conditions that underlie successful invisible hand processes.

Yet even if an unintended outcome is beneficial, the fact of that benefit does not imply that this outcome is the *only* good or value that society should embrace, for there may be other values (e.g., equality of some sort) that compete with the benefit produced by the invisible hand process. Nonetheless, invisible hand processes might secure the ends that would otherwise be sought through legislative or regulatory efforts. And even well-intentioned legislation may elicit unintended and deleterious consequences. For example, although the "sweatshop" wages of some developing nations may seem low, a consideration of invisible hand processes might suggest that the situation may be improved not so much by prohibiting or regulating such wages (which may increase unemployment, thereby depressing wages further) but by permitting the competitive process to continue, thus increasing the demand for labor and raising wages. Similarly, although well-intentioned policies of foreign aid may have plausibility, the aid may serve to support corrupt governments or to subsidize projects or industries that would not otherwise succeed. Such aid may strengthen the forces that would forestall the development of a legal framework that would provide the conditions for an invisible hand process that would (by allowing individuals to interact freely and to risk their capital securely) generate prosperity.

Such reflections suggest that the concept of the invisible hand has relevance to two major theories of business ethics—social responsibility and stakeholder theory. If there are spontaneous processes of coordination in society, then the operation of business firms, under conditions of the rule of law and with an eye to profits, may bring about better consequences than if owners and managers also expended company funds toward some specified set of social responsibilities. And if the idea of the invisible hand challenges the idea of social responsibility, then it may also test the stakeholder theory. This theory suggests that managers should take into account the claims and concerns of various classes of stakeholders. But if market prices are the invisible hand mechanism that coordinates the knowledge and expectations of disparate and anonymous individuals, then attention to stakeholders may lead managers to act contrary to price information, perhaps disrupting the invisible hand process. This may or may not be a welcome event, but it is a relevant consideration for business ethics.

—F. Eugene Heath

See also Ferguson, Adam; Game Theory; Hayek, Friedrich A.; Hume, David; Mandeville, Bernard; Methodological Individualism; Nozick, Robert; Self-Interest; Smith, Adam; Spontaneous Order; Unintended Consequences, Law of

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IRON TRIANGLES

The term *iron triangle* has been used both by scholars and by muckraking popular writers to refer to the alignment of interests and actions among three key actors in public policy making in the United States: regulated industry or other special interests, the oversight committees in the legislature, and the regulatory agency or other bureaucracy. The typical outcome of this alignment is the production of both specific regulatory decisions and regulatory policies, including the regulations themselves, that tend to protect and promote the regulated industry. For example, in recent years, critics of the U.S. Food and Drug Administration (FDA) have argued that pharmaceutical companies, with the support of Congress, have had undue influence in the decisions of the FDA, resulting in the marketing of drugs whose sometimes dangerous side effects have not been tracked by the FDA or reported in a timely way by the companies.

Sometimes the role of the regulatory agency is played by a public bureaucracy that has the ability to make decisions or allocate resources that are important to the industry. For example, the so-called *military-industrial complex* may be seen as an iron triangle among oversight committees in Congress, the Defense Department or particular branches of the military, and components of the defense industry. The term *military-industrial complex* was introduced in President Dwight Eisenhower's Farewell Radio and Television Address to the American People on January 17, 1961. The speech was written by the political scientist Malcolm

Moos. In the speech, Eisenhower warned that "in the councils of government, we must guard against the acquisition of unwarranted influence, whether sought or unsought, by the military-industrial complex. The potential for the disastrous rise of misplaced power exists and will persist."

Concern over the ill effects of the undue influence of private power was not new at the time of Eisenhower's speech. This theme was common, for example, in Populist complaints in the 19th century, New Deal era criticisms of business, and the work of critical economists and political scientists of the mid-20th century such as Horace Gray and Grant McConnell. Political scientists of that era, such as Merle Fainsod, Samuel Huntington, Marver Bernstein, and, later, scholars such as Edwin Epstein, began to develop models linking the efforts of interest groups with the institutional structures in government that they sought to influence.

Bernstein's life cycle model is perhaps the best known. In it he argued that a regulatory agency follows a path of maturation, from aggressive regulation supported by the activist interest groups instrumental in the agency's creation as a response to a social or economic problem, to an old age in which those groups no longer provide active support and are replaced by the regulated industry. Over time, via repeated interactions in which the agency adjusts to the positive and negative pressures coming from the industry, the industry "captures" the regulatory process. Congress either gives little attention to the agency or provides oversight that responds to the industry's interests.

Core Logic of the Iron Triangle

The classic iron triangle is structured by the incentives that flow among its actors, as well as the opportunities provided by the institutions that populate the system. The same basic logic applies at any level of government, with appropriate adaptations of the argument (see Figure 1). The core logic is described by Roger Noll and by Barry Mitnick, among others: The regulated industry is a significant economic actor in the constituencies of a set of legislators. Because the legislators desire to be reelected, and because they need the votes of constituents as well as funds to pay campaign expenses, they are sensitive to the requests of the industry. The industry can influence votes via its own employees and the dependence of the constituency on the economic success of the industry. In addition, either via its political action committee(s) or via allies, the industry can steer important resources to the elected politicians to aid in their campaigns. As a service to their district, and to promote their reelection, legislators seek to serve on committees of oversight that handle the most significant industries in their districts. Thus, legislators on such committees are predisposed to listen to the policy communications that come from such industry in their districts. The legislators are able to originate legislation that promotes the industry (and to stop legislation that is hostile to it); they are gatekeepers for the industry. Although they may not have a direct role in appropriations, they may be able to influence the funds that go to support activities in the industry, whether through authorizations or through quid pro quos (e.g., vote trades) with legislators who do serve on appropriations committees.

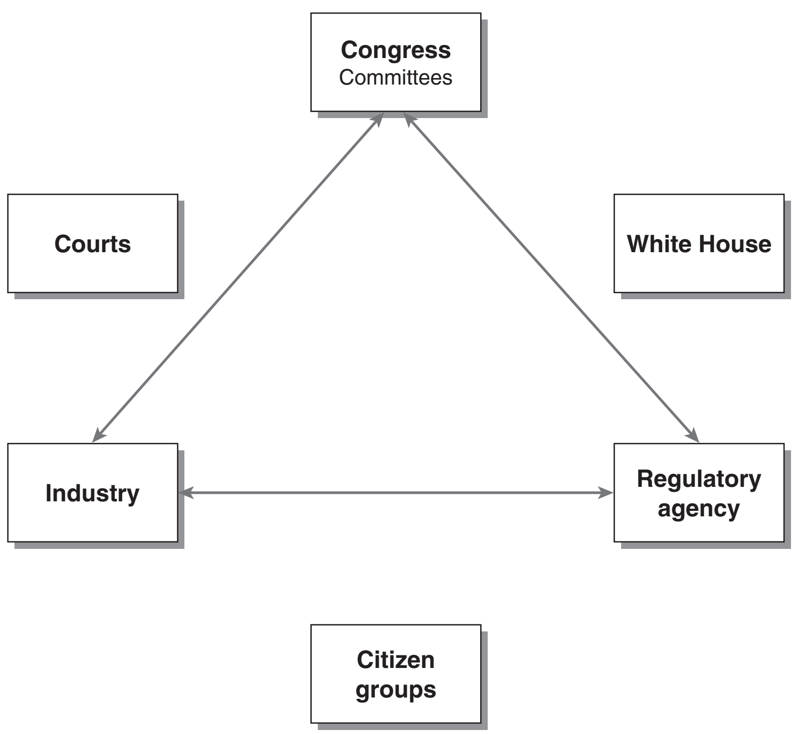

Figure 1 Iron Triangles and Jelly Hexagons

Note: A description of the relationships within the triangle, as well as the relationships among the six actors in the policy subgovernment—the "jelly hexagon"—appears in the entry text.

The regulatory agency receives a budget from the legislature. The size of that budget is influenced by perceptions of the agency's performance, holding the existence of any pending social or economic problems in the area constant. Poorly performing agencies are likely to receive less. For example, criticisms of the Interstate Commerce Commission's performance made Congress reluctant to appropriate funds for it in the years before its termination and replacement by the Surface Transportation Board, a smaller agency. The actual performance of an agency is difficult to measure, and perceptions of its performance are influenced by reports of the media and, especially, by complaints from the regulated industry that go to the legislators on the oversight committees. Thus, the agency is motivated to defend its budget by reducing complaints in the media and from the industry.

Oversight hearings in regulation do not attract much attention unless they deal with a pressing social or economic issue and are often perfunctory in character. Officials in the agency also prefer them to be this way because it is usually only poor performance, such as a social or economic issue that the agency has failed to deal with adequately, generating wide popular discontent, that produces more elaborate, media-rich hearings. Agency officials who testify at such hearings are invariably held up for scorn in the media and sharply criticized by legislators responding to constituent complaints. This threatens their existing jobs, as well as making their prospects of a remunerative position after government service less likely. Thus, agency officials are led to anticipate the desires of the legislators on the oversight committee, consulting with them on an informal basis, and adjusting the actions of the agency to be responsive to them. Agency officials also know that they will be responsible for implementing new legislation that is assigned to their agency and that they may have to write regulations to fill in the areas of discretion that the usually vague laws leave for them. They will want to do this in a way that satisfies the legislators.

Most areas of regulation deal with arcane, highly technical issues specific to the industries being regulated. Regulators must become familiar with these issues and must acquire the professional expertise on which regulation in the area is based. To satisfy the demands of the administrative process, which in the U.S. federal government is based on the Administrative Procedures Act of 1946 and its amending legislation, there is a high demand for submission of what is termed "substantial evidence" to create a record that allegedly supports the decision-making process in the regulatory agency. Often, the best and easiest source of such information is the regulated industry. Because the industry often controls the supply of information essential to the regulatory process, regulators become dependent on it. Of course, they see information that is structured to make the industry's case. In addition, personal relationships grow around the many contacts necessary to conduct the regulation. Regulators come to see executives in the industry as people with the same issues as anyone else trying to make it in business, rather than as adversaries trying to dupe them into granting favorable rules and decisions. Because few others than the industry itself actively follow the regulatory process, regulators find that they receive continual respect and even prestige from the industry in their roles as industry regulators. No one else seems to care.

Appointments to the top positions in the agencies are often determined by presidential staff members (or, at other levels of government, by the staffs of the chief executive at that level); the president may not even meet the appointees. There is little public attention to the appointments, though the industry pays close attention and seeks to influence appointments. Usually, regulatory appointments are people who are at least not hostile to the industry and for whom confirmation by the U.S. Senate is likely because legislators perceive that their constituencies will take no issue with the appointments. Legislators from districts or states where the industry is important are likely to put holds on nominations of prospective regulators opposed by industry in their constituencies. Thus, new top regulators are usually not committed to regulating against the fundamental interests of the industry they regulate.

Finally, after making a personal investment in knowledge of the industry and its areas of professional expertise, regulators look for ways to cash in on this knowledge and expertise once they leave the agency. The data show that top regulators, such as independent regulatory commissioners, and top administrators in single-headed bodies, do not on average stay their entire terms of appointment, nor do they even stay for an entire presidential administration, if the setting is the U.S. government. Thus, these regulators are frequently looking for their next job. The one place that is sure to have an interest in employing them, as long as they have not acquired a reputation for poor personal performance as a result of adverse public hearings, is the regulated industry. The regulated industry will even hire regulators who have been more aggressive in dealing with them because of their expertise both in the industry and in the conduct of such regulation.

In their classic 1970 muckraking study of the Interstate Commerce Commission, Robert Fellmeth and associates found that 9 of the last 11 commissioners to have left the commission at the time of the study had gone to work in the regulated industry or as lawyers representing it. The other two commissioners simply retired. The traffic between government and the private sector and back again has even acquired the name *the revolving door.* It is not uncommon for all three actors in the triangle to take part in this: Top congressional staff members, often attorneys, may be appointed to top regulatory positions as a reward for service to congressional leaders, only to later rotate out to industry or to Washington law and lobbying firms that represent the industry. Often, regulators have held other jobs in government and rotate to the regulatory body from another government job. Of the five members of the Federal Communications Commission in 2006, three were attorneys; two were former congressional staff members; one was an industry lobbyist whose duties involved advocacy to Congress; four of the five had had jobs elsewhere in government before their appointments to the FCC; and the fifth had extensive experience in politics.

Especially in past decades, the most common profession of a top federal regulator was the law. This is a highly fungible profession, of course, but what it allows regulators to do is to move to Washington law firms or, sometimes, lobbying firms, after their service, and provide legal services to the industry they lately regulated. Conflict-of-interest laws are not difficult to end-run in this regard. As long as the former regulator is not the attorney of record in representations before the agency, she or he can still provide consulting services to industry clients during the period of exclusion under these laws and to his or her own law firm colleagues at any time. Having relied on the industry for information, received respect and prestige from the industry, gotten to know people in the industry as reasonable, credible folks, and seen the opportunity of future employment in or dealing with the industry, regulators in this iron triangle find that, over time, their decisions as regulators tend to favor the industry.

Thus, going around the triangle, we end up with legislators who take actions in the industry's interests, as well as regulators who do the same. The industry gets what benefits it. The structure of the triangle is remarkably stable, as long as the incentives stay the same, and no new actors enter to confuse the flow of such incentives.

This rational choice model of the iron triangle assumes that regulators are often self-interested or become so after being exposed to the incentive system in which they are embedded. Yet the model itself is overly simplistic. It is not hard to find cases of regulators, both historical and of more recent service, who viewed their roles as being stewards for the public interest or arbitrators of how the public interest should be pursued in the area being regulated. In addition, regulators who are civil servants, that is, below the appointed levels, are often highly professional in orientation, especially in areas requiring technical expertise. They see their roles more as implementers and problem solvers, rather than as de facto servants of the industry. In some historical contexts, belief in the desirability of a regulation that in practice protected the industry has been joined with dedicated service to the public. One example is Joseph Eastman, the longtime chairman of the Interstate Commerce Commission in the 1920s and 1930s. For him, any suggestion that his selfless dedication to the goals of transportation regulation represented protection of the modes in that industry (railroad, trucks, barges) against competition with one another—a conclusion reached by modern economists—would have seemed insulting.

Yet one cannot dispute that iron triangles were and are real and are actively maintained and defended by the industry, political, and bureaucratic actors who run them. Iron triangles were very common in U.S. regulation before the last decades of the 20th century and remain active in a number of regulated areas today. For example, those in agriculture, such as navel oranges, are particularly protective of the industry.

Beginning in the early 1970s, however, the public interest movement began to supply counterpressures that often cracked and even rusted the triangles away completely in some issue areas. For example, muckraking work by Fellmeth and associates revealed an Interstate Commerce Commission whose rate-setting policies protected each of three modes of transportation, railroads, trucking, and barges, against competition. Such citizen groups, often founded in the early years as a result of the entrepreneurship of Ralph Nader, provided an alternative source of information about the industry, both to the legislature and to the regulatory agencies.

In addition, beginning in the late 1960s, the operative standards for judicial review changed, with appeals courts in the United States much more willing to provide reviews of the substance of agency decisions—whether, for example, the substantial evidence collected by the agency actually supported the decisions made by the agency—rather than of only whether they followed their procedures. Finally, in a few high-profile cases, the president actually became involved, either in agency decisions or in agency appointments as a result of notable agency failures (e.g., the bribery case at the Environmental Protection Agency [EPA] during President Reagan's administration). All these things raise doubts as to whether the triangle will function as described above, with guaranteed benefits to the industry.

With three additional actors (courts, public interest groups, the appointing executive), the iron triangle becomes a hexagon. Mitnick terms this a "jelly hexagon" because the outcome—benefit to the regulated industry—is no longer certain. Indeed, the common structure of policy making today among many such interest areas has been termed an *issue network* by Hugh Heclo; it is also called a *policy subgovernment*. In such a system of policy making, the set of people participating is often remarkably stable—they are often leaders of interest groups, industry lobbyists, and legislators who are reelected almost indefinitely, together with their key staff members. Hence policy making takes on the character of an iterated game, in which actors stake out positions in policy space, look for allies, and seek to build support. The outcomes can rotate as now one, and now another, of the interests emerge triumphant on any given issue. Interest groups in such systems often act in concert, creating what Paul Sabatier calls "advocacy coalitions." Indeed, as early as the mid-1970s, Jeffrey Berry, in his classic study of public interest groups, found extensive use of coalitions in advocacy.

Critics of policy making in federal and state governments raise questions about the ethical character of any government that seems to exist only to steer benefits to an industry, without some general debate about whether such benefits truly serve the public interest. Even governance by a policy subgovernment, which in effect negotiates the terms of new laws and regulations, constitutes an essentially undemocratic system. Here we see that the agents who act as representatives of different interests, both those of industry and those of assertively "public" character, and who thus determine the content of our laws, are only partly those agents who are elected by the people. In such a government, critics see the claim of democracy as little more than a convenient myth that brings stability and helps establish the institutional rules within which the actual work of interest representation and of regulation occurs.

—Barry M. Mitnick

See also Administrative Procedures Act (APA); Corporate Political Advocacy; Interest Groups; Interstate Commerce Commission (ICC); Rational Choice Theory; Regulation and Regulatory Agencies; Revolving Door; Trade Associations

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Islamic Ethics

Islam provides individuals with guidance that encompasses the entire range of their spiritual and material experience of living, including teachings that offer direction about the proper conduct of individuals and groups for mutual benefit and in the service of God and in accordance with the "laws of nature." Islamic ethics is therefore a vast and continuously evolving project; this summary includes an overview of the origins of Islam, the sources of ethics in Islamic thinking, some examples of ethical teachings as reflected by the life of the Prophet Muhammad, and ethics in business practices within Islamic societies.

Origins of Islam

Islamic tradition holds that Muhammad first received revelations from God (Allah) while fasting and meditating in a cave outside the city of Mecca, in the year 610. These revelations continued throughout Muhammad's life, and his oral transmissions were eventually collected, organized, and recorded to form the Quran, Islam's holy book. As the first Muslim, Muhammad bore witness and took a vow (Shahada) of submission to Allah, a vow that included acceptance of the biblical story from Adam to Christ. Through force of personality and leadership, and by his own example as a Muslim, Muhammad, by the time of his death in 632, had united most of the Arabian tribes into a single community (Ummah).

Muhammad's faith of Islam (literally meaning submission to God) came to extend far beyond the Arabian Peninsula to include most of the vast Persian empire and parts of Byzantium, and within a century encompassed lands ranging from western India and Central Asia through northern Africa. Later, this Islamic World (Dar al-Islam) expanded into Spain and penetrated parts of France and eastern and southern Italy. Malaysia and Indonesia, currently among the most populous Islamic countries, did not embrace Islam until the 14th century, when Arab traders transported the faith along with their wares. Today Islam is the world's second largest and fastest growing religion, with more than 1 billion followers worldwide, including many millions in the West.

Sources of Islamic Ethics

Islamic morality, ethics, and jurisprudence are all derived from two primary sources that together constitute Sacred Law (Shariah). The first is the Quran, revealed to the Prophet Muhammad. The second source, and perhaps most accessible, is the Sunnah, or life of the Prophet, which was transmitted through sayings attributed to Muhammad himself, as well as by detailed narrations of his life that can be traced to his contemporaries. Instead of constituting a formal code of morality or ethics, the hadiths are rather a guide for everyday living, and, although their historical validity is often the subject of debate, Muslims believe in their authenticity and follow them closely.

The Quran often uses phrases that are "reminders" to the faithful to pay attention to their religious faith and to remember Allah and their obligations to neighbors and society. In Islamic cities and villages this reminder is manifested on a daily basis through the calls to prayer (*namaz*) of the muezzin. The Quran goes beyond addressing a single individual's obligations since it also prescribes a doctrine for the community as a whole that is both social and political in nature and that has morality, compassion, justice, honesty, peace, tolerance, and self-sacrifice as its basis.

Muhammad as Example

In contrast to the more exalted pronouncements in the Quran, the Sunnah refers to many specific incidents in which the Prophet was the protagonist and which serve to illustrate proper behavior. Muhammad did not claim he was a divine being, and Islam doesn't treat him as such; rather, he was an ordinary human being who listened carefully to—and then orally transmitted—the divine message. Muhammad himself believed that the model of his life was the best means by which to show humanity the way of salvation. As a merchant, statesman, and warrior, Muhammad was a man of this world as much as he was a religious and spiritual leader, and there were plenty of opportunities for his society to observe the Prophet in action.

While working as a wealthy merchant in the midst of the free enterprise world within which Mecca served as a hub, Muhammad was steadfast in living a simple life and in supporting the defenseless, the poor, orphans, widows, and slaves. In Islam, therefore, the concern for social justice and responsibility is dominant and permeates throughout society, business included.

Business and Charity

Muhammad himself was successful as a businessman who bought and sold merchandise for profit, and consequently the Quran has a number of chapters (suras) that deal with how to trade justly. He encouraged Muslims to undertake economic activity in the same spirit as they did their daily prayer, honestly and with purity. For example, the Quran is clear that people should conduct business in a straightforward manner and not seek to gain unfair advantages. Muhammad produced injunctions against selling spoiled or overpriced goods; he was intolerant of lying and cheating merchants and of monopolist speculators who kept back grain to sell at a high rate, while also forbidding underpricing to secure a deal that would hurt a competitor; he believed that resources should not be used in the production of unnecessary goods until the needs of all had first been addressed; and he pressed employers to be fair to their employees and to pay them promptly.

The Prophet prohibited the taking and giving of interest (*riba*). Most likely he took this position because Mecca, where he spent most of his youth, had a reputation for brutal financiers. It was not uncommon, for example, for lenders to use violent means, such as raids on unlucky merchant homes, to extract loan repayments and interest when caravans were lost to bandits. Generally, Islam does not allow gain from a financial activity unless the financial capital is also exposed to the risk of loss; the idea is that the entrepreneur and the investor or lender should proportionately share both the profit and the loss of the business activity in such a way that the lender in fact becomes a partner in the enterprise (*musharakah*). To this day Islamic banks distribute a percentage of their income among depositors as profit sharing through equity participation, instead of paying interest. Islamic law does allow higher payment than fair market value if the goods are purchased on credit but for immediate delivery. It is a fundamental principle of Islam that rewards be the result of real efforts, not speculation or the leverage of unfair advantage.

Muhammad was a social reformer who actively taxed the wealthy to support the poor, and he expected the rich to leave something in their will for the less fortunate. Income inequality and class ranking is certainly permitted to occur within Islam, but one of the pillars of the religion requires Muslims to contribute every year a portion of their wealth to charities that benefit the poor (*zakat*). The amount of *zakat* varies by type of wealth, with 2.5% being the *zakat* for cash holdings. In Islamic societies this obligation is taken over by the state, which includes *zakat* in its tax structure.

Women and Business

During his lifetime Muhammad accomplished a great deal on behalf of women, not the least of which was to put an end to his society's practice of female infanticide. With Islam, women acquired unprecedented rights, such as the ability to choose their husbands, own property, keep their earnings separate, and enter into contracts independent of their husbands or fathers. Islamic societies were among the first to recognize inheritance for women: In Islam a wife can inherent wealth from her own family, has the right not to share it with her husband, and can be fully in charge of managing her assets. According to some estimates, close to 40% of total private wealth (nongovernmental) in Saudi Arabia belongs to women. This validates the notion that even during the Prophet's lifetime women were already fully engaged in economic activities and that Islam doesn't in itself raise barriers to women's economic involvement but that any such barriers have cultural and tribal, not religious, origins. Equality in economic activity stems from equality between men and women as spiritual beings.

Leadership

Jihad refers to religious struggle, either literally, as when Muhammad's Muslim community first established itself in the midst of violent opposition, or figuratively, as is the case with "internal" jihad, which refers to the effort required for human beings to better themselves and which is a core ethical principle of the faith. Muhammad often made references to how this personal Jihad might be carried out in specific cases, such as by prayer, by caring for one's parents, or by being a just and ethical leader, and he referred to this type of struggle as the "Greater Jihad."

Reflecting on the teachings of the Prophet, the 12th-century Islamic scholar Muhammed ibn Zafar wrote that a wise leader must be guided by ethical considerations and that he (or she) must always trust God's guidance, be knowledgeable, perceive facts as they are, be prepared for all eventualities, and be fast in correcting mistakes.

Conclusion

The Islamic prescription for human behavior is based on concepts of justice and humanity as recorded in the Quran and practiced by the Prophet Muhammad and his followers. A study of Islamic ethics is thus best approached by first understanding the Quran, the life of the Prophet, and the society that served as their ground of creation. As the modern world moves forward, Islam will continue to contribute, along with other world religions, to the ongoing dialogue regarding the ethical future of human societies and their business practices.

—Sousan Urroz-Korori

See also Religious Discrimination; Religiously Motivated Investing

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Is-Ought Problem

The is-ought problem in ethics arises from the is-ought, fact-value distinction. It is the problem of moving from the factual to the normative, of obtaining a prescriptive claim from a set of descriptive claims.

The problem was first raised by David Hume in the 18th century; he pointed out that while many ethicists make claims about what ought to be solely from the basis of what is, there is a big difference between the two, and writers make an imperceptible switch from *is* claims to *ought* claims with no explanation offered. He argues that the move to the *ought* introduces a new relation or affirmation that needs to be clarified and justified. But he can find no justification, the implication being that such a move cannot be made. According to Hume, knowledge of anything is based either on logic and definitions or on observations, but *ought* statements are seemingly not able to be known in either way, and thus it would seem that there can be no moral knowledge.

In the 20th century, G. E. Moore also questioned the supposed link between the *is* and the *ought* from a related though different direction. Many philosophers, ethical naturalists, held that moral terms are completely definible in nonmoral terms. Moral judgments are a subspecies of empirical judgments, and moral terms stand for purely natural characteristics. They tried to prove some of their claims about ethics by turning to an analysis of the meaning of the term *good* in the sense of intrinsic moral goodness, holding, for example, that *good* can be defined in terms of one or more natural properties that we already understand, such as *pleasure* in the case of hedonists, or that which promotes human survival in the case of evolutionary ethics, or the satisfaction of desires, and so forth. But, Moore points out, we can always ask, for example, whether pleasure is always good and whether it is not a contradiction to say that some pleasures are not good or some satisfactions of desire are not good, and this holds for any empirical property or set of properties that can be offered. These are significant questions regardless of what properties are substituted; the questions are neither obvious nor trivial. But according to naturalism, asking these questions should make no more sense than asking if daughters are always female, and a negative answer would be as obviously contradictory as to say that some daughters are not female. Moore concludes from this that value cannot be analyzed or defined, and any attempts to do so will necessarily fail.

Moore, in defending ethical nonnaturalism, argued that a fallacy is committed when one identifies moral properties with natural or empirical properties. The moral property or quality of good in the sense of intrinsic goodness is simple, indefinable, nonnatural, or nonempirical and must be immediately grasped by a moral intuition. Moral qualities can be known neither by sense experience, as they are nonsensible, nor by defining them in terms of some sense quality, for they are simple and hence indefinable. Rather, a primitive ethical term stands for an objective reality that we must recognize directly with what he calls an immediate nonnatural grasp or nonnatural intuition.

Analogously, if one wants to understand the meaning of *yellow,* one has to be shown examples of it; it will do no good to learn that *yellow* names the primary color between green and orange on the spectrum or that the perception of yellow is stimulated by electromagnetic radiation within a certain range of wavelengths or even that ripe lemons are yellow. Moore argues that these do not provide the meaning of *yellow,* and to take any or all of them as a definition of *yellow* would be to commit the same fallacy that is committed when "pleasure is good" is taken as a definition of *good.* One must immediately experience the color yellow through an immediate sensible grasp or natural intuition.

Moore calls the fallacy involved the naturalistic fallacy in ethics because it involves confusing a natural object, such as survival or pleasure or satisfaction of desire, with the nonnatural property of goodness, but the naturalistic fallacy is an instance of a more general type of fallacy that is committed whenever a statement saying that something has a simple indefinable property is taken as a definition of it.

Many people tend to use the phrase *naturalistic fallacy* to characterize inferences claiming that because certain types of behavior are natural they are therefore morally right, or because certain types of behavior are unnatural they are therefore morally wrong. Although such inferences can be analyzed as fallacious, this is not at all what is at issue with Moore. Moore is concerned with the metaphysical and epistemological foundations of ethics, and this use of the term *naturalistic fallacy* is a misapplication, to say the least.

The challenge to the move from any descriptions of what is to prescriptions concerning what ought to be is one that must be met "head-on" by any descriptive or naturalist ethics. Many ethicists, finding the challenge to be one that is impossible to meet, have embraced moral skepticism of some sort or various forms of noncognitivism or relativism. While noncognitivism takes various forms, the position usually taken as most representative of that movement is A. J. Ayer's emotive theory, which holds that moral utterances are neither true nor false, for they are meaningless, nonfactual utterances. These utterances are purely emotive and serve such functions as evincing the emotions of the speaker or influencing the emotions of others to conform to those of the speaker. Ethical relativism takes the position that there are no universally valid moral principles. Morality is purely conventional, and moral claims are valid if they conform to the conventions of the particular culture (cultural relativism) or individual choice (individual relativism).

The is-ought dichotomy has been highly influential in the manner in which business ethics has developed. Scholars interested in business ethics seem, for the most part, to have split into two camps in delineating two kinds of business ethics, the normative and the empirical. The former is considered to be a prescriptive or value-laden approach and the latter an explanatory, descriptive, and/or predictive approach concerned with empirical facts. While the two domains may be held to rely on each other in a practical relationship, they are two differently oriented conceptual sets with distinct methodologies. There are attempts to bring normative and empirical inquiry together under one big conceptual tent, but these are still usually understood in terms of the endeavor of trying to bring into a symbiotic relationship two distinct realms, facts and values, the realm of *is* and the realm of *ought.*

American pragmatism, best represented in ethics by the philosophy of John Dewey, affirms a naturalism that, with its enriched understanding of experience and nature, undercuts the is-ought dichotomy. Empirical experience can include the immediate experience of value, and value need not be a nonnatural property to be a real, irreducible, indefinable quality. *Ought* claims develop as experimental guidelines concerning how best to act to enrich value experience for all those affected by one's actions.

The issue of the is-ought dichotomy has led ethics down many diverse paths, and the problem of obtaining an *ought* from an *is,* introduced by Hume and reinforced by Moore, remains one of the major issues in ethical theory.

—Sandra B. Rosenthal

See also Descriptive Ethics; Fact-Value Distinction; Hedonism, Ethical; Hedonism, Psychological; Intrinsic Value; Naturalistic Fallacy; Normative/Descriptive

Distinction; Normative Theory Versus Positive Theory; Pragmatism

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J

Jainist Ethics

Jainism is an ancient religion that originated in India. The Jains, primarily concentrated in India, numbered approximately 3.2 million in the latest census, but Jains also live in other parts of Asia, East Africa, Europe, and North America. Jains believe that their religion is eternal, although the earliest historical record of Jain activity dates from about 850 BCE. There are two main sects of Jainism, the *Digambara* and the *Shvetambara*. *Digambara* means "sky clad," and its male ascetics renounce all clothing. *Shvetambara* means "white clad," and its male and female ascetics wear white robes, which are a sign of purity.

Along with Buddhism, Jainism is considered to be one the great non-Vedic heterodoxies, in that it rejects many of the precepts from the Hindu sacred texts, the Vedas. Jainism does share, however, several doctrines with the other two traditions—for example, reincarnation, karma, and liberation. Etymologically, the religion's name derives from the Sanskrit word *jina,* which means conqueror in English. The term was used to describe certain teachers, who were spiritual conquerors, able to overcome human passions, attain enlightenment, and escape the cycle of reincarnation. The great Jainist teachers, who are considered omniscient albeit human, are called *tirthankaras*, which means "fordmaker." Their teaching provides a spiritual ford across the ocean of rebirth. The last *tirthankara* was Vardhamana Nataputta, called Mahavira, who was a contemporary of Buddha during the sixth century BCE. Mahavira is sometimes wrongly referred to as the founder of Jainism.

The Three Jewels, or guiding principles, of Jainism are right faith, right knowledge, and right practice. Jainism stresses renunciation, even for the laity, although expectations for their right practice are lower and somewhat different from those for the monastics. The five main ethical principles of right practice are *ahimsa* (nonviolence), *satya* (truth), *asteya* (nonstealing), *brahmacharya* (chastity), and *aparigraha* (nonpossession). The laity is responsible only for the associated "Lesser Vows," which parallel the "Great Vows" of the ascetics. Laypeople also have three "Subsidiary Vows" and four "Vows of Instruction."

Ahimsa requires the ascetic to reject the killing of any life form (including insects and microscopic beings) and to avoid harming them in any way. Laypeople must avoid the pointless destruction of life, and this principle limits their potential occupations. *Ahimsa* also governs the way that laypeople follow the other principles, in that they may be overridden to avoid violence. *Satya* requires monastics to avoid all lying and other hurtful speech, while laypeople must avoid them as much as possible. In business, laypeople are expected to avoid deception regarding the goods that they are selling. *Asteya* requires ascetics to avoid all theft and even the desire of someone else's property. Laypeople must observe the external aspect of this principle, by not stealing or otherwise taking property that does not specifically belong to them. *Asteya* prohibits all forms of business fraud, and recent commentators have also claimed that it prohibits tax evasion. *Brahmacharya* requires celibacy for the monks and nuns, including the avoidance of sexual thoughts and desires. They should also avoid any activity that might stimulate sexual impulses. Laypeople are expected to be monogamous and faithful in marriage.

Like the monastics, they should avoid desire when it comes to nonspouses. *Aparigraha* requires the ascetics to renounce all possessions and any attachment to them. They must not even think of the things renounced. The laity must avoid excessive attachment and end desires for more than is just for them to have. Religious giving is expected. In business, they must consider their profession to be a means to social benefit, rather than an end in itself.

The first "Subsidiary Vow" for laity restricts travel to minimize the destruction of life forms, which is ironic in that the monks are required to be traveling mendicants. The other Subsidiary Vows call for laypersons to avoid excessive enjoyment of material goods and to abandon various spiritually harmful activities. The four Vows of Instruction relate to religious practices: restricting activities, performing the *samayika* ritual, fasting, and religious and charitable giving.

Jain laypeople tend to be merchants because farming and various craft and industrial vocations involve the destruction of life forms. Trade rather than production better facilitates the practice of *ahimsa,* with banking and the gem industry as historically the most common fields. Concern for all life forms leads Jainism to reject the modern industries and manufacturing practices that cause pollution and the use of animal products. The Jain worldview thus overlaps with contemporary environmentalism, although the underlying motivations differ.

Jainism has been likened to Protestant Christianity and the Protestant work ethic, in that it supports commercial practice through principles of self-reliance, self-restraint, and responsibility. One important way that they differ is that in Jainism, business practice has not separated from its religious origins. Credit is both an economic and ethical notion. A business family's credit depends not only on its financial standing but also on its social position, reputation, and moral and religious conduct. Good behavior is seen as indicative of internal piety. Bad behavior, such as unscrupulous business practice, may result in short-term profit, but Jains hold that such people will suffer in the end, through loss of credit and bad karma (used here as destiny due to wrong actions).

Following the notion of karma, wealth and poverty are considered reward and punishment for past and present deeds. Voluntary poverty is virtuous but involuntary poverty is not. Wealth and commerce are not considered sinful per se, but they do bring their own particular moral and religious hazards related to conflicts with renunciation. Jains avoid these hazards by rejecting conspicuous consumption and by making large charitable donations to the building of temples, schools, hospitals, etc. The term *punya* (merit) can be used for any good action, moral or religious, but it most commonly refers to a generous public donation, and it results in good karma for the donor. Karma also has a this-worldly impact because outward signs of piety are crucial in business communities dominated by Jains and contribute to a positive business reputation.

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See also Buddhist Ethics; Christian Ethics; Environmental Ethics; Islamic Ethics; Jewish Ethics; Protestant Work Ethic; Weber, Max

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JEWISH ETHICS

Jewish ethics is part of an unbroken ancient religious tradition dating back more than 3,000 years. The Jewish Bible and the Talmud serve as the foundation of the Jewish religion. In Judaism, the notion of a covenant between God and Israel where both parties bear legal and ethical responsibilities is one of the most central themes.

Five Themes of Jewish Ethics

The following five themes of Jewish ethics were selected out of the vast ocean of Jewish literature because they are relevant to contemporary decision makers, especially in the context of business. There is no claim that this list is exhaustive or that it includes the most important issues in the history of Jewish ethics. Furthermore, the descriptions and interpretations that follow are not necessarily universally accepted in Judaism. The claim *is* being made, however, that these themes provide a useful and practical launching point for a consideration of the use of Jewish ethics in business.

Judaism underscores the importance of right actions. It is certainly not the case that Judaism is indifferent to right intentions and correct beliefs as has sometimes been asserted. Perhaps no value is more important in Judaism than the study of *Torah*. Nevertheless, in Judaism, there is a clear preference for appropriate actions and good deeds. As one famous Talmudic sage noted in the Ethics of the Fathers, "Say little and do much."

Traditionally, it has been understood that Jews have been commanded to observe 613 *mitzvot* or commandments. These *mitzvot* are contained in both the Written *Torah* (the Jewish Bible) and the Oral *Torah* (the *Mishna*, *Talmud*, and related commentaries) and have been identified and elaborated in every generation by Jewish scholars for thousands of years. In Judaism, it is believed that human action is necessary for both human welfare and for God for repair the world (*tikkun olam*).

There is a famous and often quoted rabbinic statement cited in the Jerusalem Talmud that illustrates the seemingly unlimited power of right action and good deeds. "Whoever destroys a soul, it is considered as if he destroyed an entire world. And whoever saves a life, it is considered as if he saved an entire world."

Jewish ethics is focused on the here and now. In every instance, the rabbis made an attempt to interpret, develop, and apply Jewish law and ethics in light of contemporary social and economic conditions.

Judaism teaches that each individual person is endowed with free choice (see especially Deuteronomy 30:19). Further, Judaism rejects outright the belief in original sin. The ancient rabbis meticulously and creatively interpreted every single word of the Written *Torah*. A good example of this can be found in their understanding of the following biblical verse. "And God saw all that He had made, and found it *very* good. And there was evening, and there was morning, the sixth day" (Genesis 1:31, italics added). In this case, the rabbis asked themselves why the text included the seemingly extraneous word "very"? How does this word add to the meaning of this verse, as it must? Here is how they answered this question:

> Rabbi Nahman said in Rabbi Samuel's name: "Behold, it was good" refers to the Good Desire; "And behold, it was very good" refers to the Evil Desire. Can then the Evil Desire be very good? That would be extraordinary! But without the Evil Desire, however, no man would build a house, take a wife, and beget children.

This is an extraordinary idea and it is fundamental to an appropriate understanding of Jewish ethics. According to one contemporary Talmudic scholar, this statement represents an unqualified rejection of ethical dualism (the doctrine that holds that two forces—one for evil and one for good—exist within a human being). According to the ancient Rabbis everything comes from God and is therefore good. The Evil Desire is so called because of its destructive side, but at the same time the need for desire and its positive overtones is emphasized.

In Jewish thought, neither selfless love nor selfish love is seen as ideal. One of the most often quoted passages in Jewish ethics is Hillel's famous dictum, "If I am not for myself, who will be for me? And, being for myself only what am I?"

Hillel's view captures the dialectic between individual autonomy and the individual's responsibility to the community. In Judaism, both poles are seen as necessary components to energize an appropriate and life-affirming ethic. Interestingly, Hillel formulated his insight not in the form of a statement but as questions, leaving it to each individual to formulate an appropriate answer in light of existing (but changing) circumstances. Hillel's dictum echoes the biblical commandment to "love one's neighbor as one loves oneself" and foreshadows Maimonides well-known endorsement of the "golden mean" in ethics.

At the heart of Jewish ethics is the idea of covenant. It is a truism to note that the idea of covenant or *brit* is deeply rooted in the rich soil of biblical narrative. It is a term that describes not only the climactic events of the revelation at Sinai but is also a term that echoes through every book of the Bible. Covenant is the central organizing theme of biblical thought.

For the purposes of developing a full blown Jewish ethics it is useful to provide a contemporary definition consistent with traditional Jewish sources. Covenant may be defined formally as a voluntary agreement among independent but equal agents to create a "shared community." The primary purpose of the agreement is to self-consciously provide a stable social location for the interpretation of life's meanings to help foster human growth, development, and the satisfaction of human needs.

This definition is meant to highlight three aspects of *brit*. First, they are purposely ambiguous and open-ended, thus allowing for change and growth. Second, they are long term in nature. And third, covenants are respectful of human integrity.

Jewish ethics is dependent on open and free dialogue. No modern Jewish thinker has done more to promote the notion of dialogue as central to Jewish ethics than Martin Buber. Throughout all of his writings, but especially in his book *I-Thou,* Buber expressed a deep and profound appreciation for interpersonal communication and human connection. As Buber stated, "God is not in me, and God is not in you, but God is what is between us." Or, on another occasion, "When two people relate to each other authentically and humanly, God is the electricity that surges between them."

Buber's understanding of dialogue is well grounded in traditional Jewish sources. For example, in Genesis, Abraham responds to God's decision to destroy Sodom by engaging God in a conversation. Abraham asks God, "Will not the judge of the whole earth act justly?" In rabbinic writings, even a cursory examination will show that dialogue among the rabbis is the defining characteristic of Talmudic thought and engagement. No rabbinic phrase captures this idea better than the expression "It [Jewish law and ethics] is not in heaven."

None of these five themes listed above is unique to Judaism and Jewish thought, but each of them is integral to it. Given the human ability to choose freely, Judaism underscores the importance and significance of human action. Such action is taken in the context of covenant and is based neither on selfless love nor on selfish love but seeks a middle ground. Reciprocal responsibility is strengthened through study, discussion, and dialogue.

Using Jewish Ethics to Understand Contemporary Business Problems

Jewish ethics, with its emphasis on free choice and right action, contains no inherent bias against business. With its this-worldly and practical approach, Jewish ethics contains numerous texts and sources useful to contemporary business.

Although a full elaboration of this point is beyond the scope of this entry, consider three examples and how they relate to the themes discussed above.

Corporate Social Responsibility

There is little doubt that among the most important issues in business ethics today is the notion of corporate social responsibility, especially a responsibility to the least well-off members of society. This concern is consistent with the very foundations of Jewish ethics, especially as understood in the prophetic writings. Consider just one example from Amos, Chapter 58:

> Hear this, you that would swallow the needy and destroy the poor of the land saying, when will the new moon be gone, that we may sell grain? . . . Making the epha [ancient unit of measure] small and the shekel great, and falsifying the balances of deceit? That we may buy the poor for silver, and the needy for a pair of shoes.

From a Jewish perspective, it would be impossible to defend a view of the corporation that holds that its sole purpose is to maximize profits for shareholders. Any view that rejects the rights of all stakeholders would be inconsistent with the themes identified above, especially Judaism's insistence on finding the appropriate balance between individual autonomy and the individual's responsibility to the community.

Sustainability

Like corporate social responsibility, sustainability is emerging as a key variable in business ethics. While there is yet no one definition for sustainable business practices, it is clear that business must now factor long-term environmental and social impacts into the decision-making process in addition to financial considerations. There is a recognition that each generation must leave behind a world at least as healthy and rich as the one it inherited.

To more fully understand the appropriate contours of sustainability, it is simply not enough for one person, firm, or even country to go it alone. A reasonable conception of sustainability flows from a shared and just consensus beyond national borders. While there is certainly no necessary reason to include a vocabulary derived from religious sources in this dialogue, common sense dictates a familiarity with something like the idea of a covenant as an important consideration in this discussion.

Accountability

The call for increased transparency and accountability is critical to the well-being of an economic system based on free and autonomous business enterprises. Corporate accountability can be defined as the systematic and public communication of information that is designed to justify an organization's decisions and actions to various stakeholders. According to this definition, corporate accountability is primarily a form of ethical communication directed toward those parties who are affected by corporate activities and outcomes. It is an attempt by the corporation to explain itself in a reasonable and meaningful way to the society in which it operates.

During most of the last century, corporate accountability was successfully achieved almost entirely through the use of corporate annual reports. Although the annual report continues to play a crucial role in communicating useful information to stockholders and other interested parties, the concept of corporate accountability has broadened dramatically in recent years.

To legitimately justify an organization's decisions and actions, corporate accountability is now viewed and described by many as a dialogue between the corporation and its stakeholders and not as a monologue on the part of management. This means that corporate accountability requires listening to a company's diverse stakeholders as well as responding to them. It also means that business ethics would be well served by a thorough examination of the religious roots of dialogue, both ancient and modern.

Conclusion

This entry makes no claim to provide an exhaustive or an authoritative characterization of Jewish ethics. Rather, it has attempted to highlight a number of the most prominent themes in Jewish ethics: right action, free choice, balance, covenant, and dialogue. These themes were chosen because they are especially useful to help understand and resolve contemporary business ethics issues. Great care should be given to any attempt at mixing religious thought and business practice. The religious ideas examined here grew out of social and economic conditions very different than those we face today. Nevertheless, if we maintain an attitude of pragmatic realism and reasonableness, and if we hold our focus on building better and more equitable democratic societies, religious resources can play an important role in promoting business ethics.

—Moses L. Pava

See also Accountability; Corporate Accountability; Ethics of Dialogue; Free Will; Transparency

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Job Security

The concept of job security relates to the level of stability a job has over time. In addition to the actual stability of a job, job security also relates to the perception held by an employee that his or her job is secure. Historically, job security held a central role in the psychological contract between workers and their employers. The employee believed that in return for providing his or her services and loyalty, the employer would provide stable employment. However, there is a sense that the contract has been broken, that the work rules have changed, driven both by employer and employee actions.

The employment relationship takes a number of forms, from temporary or contract employment intended for a specific term or project duration, to a relationship perceived by the employer and/or the employee as a long-term commitment. That relationship can be covered under the terms and conditions of a specific employment contract, as is the case in a unionized employment relationship, or simply exist as long as it satisfies the needs of the parties. In such an "at-will" employment relationship, both parties retain the right to end the relationship for any reason or for no reason.

In the United States, the employment relationship is based on the doctrine of employment at will. This doctrine holds that in the absence of a specific employment contract, an employee can be terminated for any reason or no reason, and in turn the employee can quit for any reason or no reason. Under this doctrine, employers were under no legal constraints to provide secure or stable employment. They could terminate any employee, at any time, with no requirement to provide justification to the employee. In the

1970s and 1980s the courts began to weaken this doctrine, holding that employer actions could create an implied contract that changed the relationship from "at will" to one of "just cause." Shifting to a "just cause" doctrine of employment requires an employer to provide a valid and justifiable reason for terminating a worker and allows the worker to challenge that reason in court. The courts found that statements in employee handbooks or made by managers, which implied career-long employment, or job security for good performance, were sufficient to limit the employer's right to terminate without reason or cause. Thus, to protect their rights to terminate employees "at will," many employers began explicitly to indicate to all new hires, and periodically to existing employees, that the employment relationship between the company and worker is one that is "at will" and that they may be terminated at any time without the need for a reason. Such declarations had the effect of highlighting for all employees the tenuous nature of the employment relationship and further eroded perceptions of job security. The doctrine of employment at will, while somewhat restricted by a number of court rulings and statutes, is still the prevailing employer-employee relationship in the United States and holds that flexibility in the employment relationship is more important than security.

In European countries, the employment relationship is based on regulations and statutes that give much greater protection to the worker and make it much more difficult for employers to terminate them. Many believe that the flexibility employers have with regards to terminating employees in the United States is, in part, the reason that unemployment in the United States tends to be consistently lower than in EU countries. The argument goes that in the United States, an employer would be more willing to add workers as business needs require, knowing that those workers can be removed should conditions warrant, while in EU countries, employers, knowing that once hired they will not be able to terminate the worker easily, will hold off hiring new workers for as long as possible. To address this structural unemployment, several European governments sought to modify existing work rules early in the 21st century that would make terminating younger workers easier for employers, giving employers greater flexibility in terminating workers. These proposals have generally been met with widespread protests.

Japan has long been viewed as providing lifetime employment. Following World War II, the practice in large firms in Japan was to hire a worker directly out of school and retain him or her until a mandatory retirement age (originally 55 years but now 60 years). This was not a mandated requirement but an implicit agreement honored widely by both employer and employee. This led to the corresponding practices of promotion from within and seniority-based pay. In the Japanese scheme of lifetime employment, higher wages were tied to longer seniority, thus providing the financial incentive for individuals to remain with one firm. Those not employed by large firms went to work in economic sectors protected by the government from international competition. This system resulted in extremely low unemployment. However, that system began to weaken in the 1990s. By the end of the 1990s, unemployment among young workers reached nearly 10% and part-time employment made up nearly 24% of all employment, with the government advising its citizens to get used to the idea that lifetime employment could not be sustained.

In the United States, labor unions offered one way of limiting the seemingly arbitrary and insecure nature of employment under the "at will" doctrine. In the 1940s and 1950s unions were able to offer a degree of job security by negotiating specific labor contracts that specified who could be terminated and for what reasons; this remains a key issue in today's labor contract negotiations. However, unions are less able to provide job security when the threats to job security stem from the forces of globalization. As both products and labor can be sourced globally, many jobs have moved to countries where the supply or cost of labor is more advantageous. In addition to job loss due to globalization, U.S. workers' perception that companies have a reduced commitment to workers has been fueled by the large numbers of high-wage jobs eliminated in the auto, rubber, steel, and other industries through advances in automation and robotics.

While concerns over job security have always existed, there is a perception that in the past the concern was based on more manageable issues related to one's performance or the financial performance of his or her employer. Both were factors on which the employee either directly or indirectly could have some impact. However, today workers are frequently reading reports of job losses or layoffs impacting tens of thousands of employees from single employers as a result of mergers or other major market disruptions. Furthermore, in the era of 24/7 media coverage, not only are facts reported, but the most compelling personal stories are found, which highlight the consequences of job loss on a personal level, adding to the anxiety and insecurity of all.

The commitment that workers are willing to make to employers is also changing. This is caused in part by the perception of decreased employer-provided job security and in part due to increased educational opportunities and greater mobility. Today, individuals may be less likely to believe that their careers are defined by location or company. The idea of working for several different companies, and even changing career direction, is more acceptable to today's workers.

However, despite the widespread perception that job security has declined, there have been a number of studies that challenge that conventional wisdom. Job security and job stability are measured through a number of metrics, including tenure, separation rates, retention rates, and worker perceptions.

The data on job stability present a picture suggesting that job stability has not changed dramatically in the U.S. workforce. Studies indicate that in the 1990s average job tenure rose and the percentage of employees with more than 10 and 20 years of seniority with the same firm had increased. Another study compared the careers of older men in 1969 to those of older men in 2002, examining the average of the longest jobs held by the men in each cohort. In 1969, the men averaged 21.9 years, whereas in 2002, they averaged 21.4 years. In both cohorts, slightly more than half the men held one job over 20 years. Similarly, U.S. Bureau of Labor Statistics data show that the median job tenure of all workers more than age 25 has remained stable from the 1980s to the present. While the majority of studies support the position that job stability has not changed over time, some that challenge that view, especially those who focus on white-collar mid-level managers.

Despite data that suggest jobs in the 2000s are not substantially less secure today than they were in the 1980s and 1990s, the perception that jobs are less secure has grown with several surveys indicating that nearly half of the respondents worry that a member of their household will be out of work in the near future. Part of the reason for this disparity between empirical data and perceived security lies in the psychological concept of "salience bias." For example, many believe that air travel is dangerous because a few high-profile air crashes do occur, even though there is overwhelming evidence that air travel is among the safest forms of travel. Similarly, high-profile examples of job loss have a disproportionate impact upon public perception. When icons of U.S. industry like General Motors or AT&T have large and well-publicized downsizings, this seems to prove that a great transformation of economic conditions is taking place.

Regardless of what the empirical data suggest about the long-term trend in job stability, the prevailing perception of job security has a significant impact on the employment relationship. In the 1990s, workers were more concerned about losing their job with the next year than they were in any period during the 1980s. This led Alan Greenspan, former chair of the Federal Reserve, to conclude that concerns over job security have had a dampening effect upon wage growth. Similarly, Robert Reich, former secretary of the U.S. Department of Labor, asserts that as workers become more anxious over retaining their job, they are investing less in firm specific capital and more in developing general skills and a network that would help them in the event of job loss. Thus, whether the nature of employment has undergone a structural change toward less security and stability, or the increased awareness of the topic and the threats organizations face has led to an increased perception that jobs today are less secure, there are significant implications for both workers and organizations. These range from a decreased willingness to accept jobs in areas with fewer alternative employment opportunities, reducing the desirability of many small and medium sized towns, to investment decisions that employers make about the training and development of their workers.

—Ken A. Sloan

See also Downsizing; Employee Rights Movement; Employment Contracts

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Johns-Manville

The Johns-Manville Corporation was a pioneer in the use of Chapter 11 bankruptcy as a strategic defense against exposure to product liability lawsuits. Manville was a major supplier of insulation materials. Unfortunately, asbestos was one of Manville's main insulation products. Exposure to even small quantities of airborne asbestos particles can cause debilitating and often fatal lung disease. There is evidence that Manville knew of the link between its asbestos and lung disease as early as the 1930s. An appeals court judge even held that Manville had engaged in a conspiracy to hide that link. Not surprisingly, the industrial workers who had been exposed to asbestos began to file lawsuits in increasing numbers during the 1970s and 1980s.

In 1982, faced with this burgeoning potential liability, Manville sought protection in the bankruptcy court through a reorganization that created two separate entities: an operating company whose assets would be shielded from asbestos liability and a trust that would handle payouts of asbestos-related claims. The trust was funded by a grant of 50% of Manville's common stock and 20% of the operating company's profits (a payment that continued until the operating company was sold in 2001). Shareholders opposed the arrangement as a dilution of their equity but the bankruptcy court accepted the company's plan in 1986.

The original formula for payouts from the trust was 100% of a claim's settled value on a first-come, first-served basis. The number of claims against the trust quickly swelled, however, and as of 2004 the trust was paying just 5 cents on the dollar for claims.

The Manville case raises serious ethical questions about how to apportion the assets of a firm between shareholders, creditors, and victims when the firm is faced with liability claims that approach or even exceed the value of the firm itself. Shareholders naturally feel that as owner-investors they are entitled to retain the firm's equity value and profits. Yet creditors believe that they have a binding claim based on prior corporate promises. And, of course, victims of the company's products claim that they are entitled to be made whole for injuries that were not their fault. If the bankruptcy court does not shield firms when they are exposed to such enormous liability, the odds are that those victims who file their lawsuits early may receive full compensation while creditors and other victims will receive little or nothing. However, if the court accepts this strategic use of the bankruptcy laws, it is likely that no injured party and no creditor will be fully remunerated. Shareholders, in either case, are likely to lose both equity value and future dividends.

—John McCall

See also Bankruptcy, Ethical Issues in; Compensatory Damages; Dalkon Shield; Implied Warranties; Justice, Compensatory; Liability Theory; Litigation, Civil; Negligence; Product Liability; Punitive Damages; Tort Reform; Torts; Warranties

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Justice, Compensatory

Compensatory justice concerns making a person whole after a wrong by another person. Key in determining the amount of compensatory justice is determining the value of what was lost. In some situations determining the cost is simple: What were the actual expenses incurred as a result of the wrongdoing? In other situations such as damage to a reputation, pain and suffering, and loss of expected benefits in the case of breach of contract, calculating the amount of damages due is very difficult.

Conditions Required to Establish Duty to Compensate

Traditionally, three conditions are required to find that a person has a moral obligation to compensate an injured party:

1. *The action that caused the injury was morally wrong, legally prohibited, or negligently committed.* If you are prevented from achieving a particular goal

because I deliberately put blocks in your way, perhaps intentionally spreading a false rumor about your ability to perform a contract, then you would be entitled to compensation.

2. *The person's action must be the real cause of the injury.* If I use my money to purchase a defective forklift for the company and you are injured, then I am responsible for that injury. If my connection to the injury cannot be established, then I am not liable.
3. *The person's injury was inflicted voluntarily.* In this instance "voluntarily" means that I intentionally caused the injury or I acted negligently, with such a disregard for the consequences of my action that I am held morally liable for the injury.

To diffuse the financial liability, the community may choose to bundle resources for compensation, such as the purchasing of insurance, to spread the costs of compensation more equally across the community. The degree to which the community should demand reallocation of resources without regard to fault in causing injury is a perennial source of controversy.

Compensatory Damages in Breach of Contract

Historically, three measures of compensation may be due to a person who has suffered damage because another defaulted on a contract.

First, a person may receive compensatory damages to protect the restitution interest. This allows a court to deprive the person who defaulted on the contract any gain that resulted from the breach of contract. The purpose of this award is to prevent unjust enrichment to the party who is in the wrong.

Second, the person may receive compensatory damages to protect the reliance interest. If a person purchased goods or services to fulfill the contract, the cost of those goods or services should be repaid. If someone forgoes another opportunity in reliance on the contract, that lost revenue may also be recovered.

The third measure of compensation is protection of the expectation interest. This compensation is made to place the person in the position she would have been in if the promise had been performed. Thus, if a person expected a certain amount of profit from the contract being honored, the party in breach of the contract may be required to compensate the nonbreaching party for the profits that were expected.

The ethical basis for the first two types of compensation is malfeasance, deliberately choosing to not honor a contract or to keep one's word. In these situations, theorists agree that compensation is due. The ethical basis for the third measure of compensation is nonfeasance, granting damages for something that was never done. Theorists do not agree on this basis for compensation. The argument is that one should not recover damages for a failure to receive the anticipated financial benefit. Regardless of the theoretical controversy, the courts consistently recognize all three types of compensation.

Compensatory Damages in Tort

The most typical form of compensatory justice in tort law is the award of money. The idea is, to the degree possible, to use money to put the injured person back into the position he would have been in before the injury. This interest is recognized when the injury was intentional as well as a result of negligence.

Actual damages, the first type of compensation, are not controversial. The moral obligation of the one who caused the damage is to pay the actual expenses of the one who was injured. These damages may be hospital bills, personal expenses for care, or loss of income due to the act.

Consequential damages are more controversial because of the difficulty of proof. A common example is determining appropriate compensation for pain and suffering, which can only be inferred from the seriousness of the injury.

Problem Cases

Two situations are problematic in the area of compensatory justice: (a) no-fault or strict liability and (b) affirmative action. In the case of no-fault liability or strict liability, the notion is to place responsibility for compensation of damages either in a pool of persons through insurance or with the person who is most able to absorb the cost of the injury, the corporation. In this sharing of responsibility, one person is not given the overwhelming burden of meeting the financial obligations, but the risk is diffused through the community. The notion behind affirmative action is that those who have benefited from the wrongdoing of another should be required to compensate the victims of the wrong. Thus, particularly in the distribution of community goods such as jobs or contracts, those who have historically been unable to compete fairly should be compensated. The critique of affirmative action has been that those who were not directly responsible should not be required to compensate those who have indirectly been harmed.

The moral basis for compensation is our personal interest in preserving our life and our bodily integrity. The second protected interest is our right to preservation of our property. The moral justification for compensatory justice has always been the concept of responsibility for action: if a person takes intentionally or negligently takes an action that injures another, the damage caused should be compensated. To the degree that the connection between actual agency and damage is lost, such as with pooled responsibility or affirmative action, arguments for compensatory damages become weak and theories of distributive justice become more persuasive.

—Catharyn A. Baird

See also Affirmative Action; Agency, Theory of; Contracts; Freedom of Contract; Justice, Retributive; Justice, Theories of; Procedural Justice: Philosophical Perspectives; Procedural Justice: Social Science Perspectives; Torts

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Justice, Distributive

Distributive justice concerns the way in which the resources of a society are to be justly distributed among its members. The theory of distributive justice attempts to answer the following question: "How should the scarce goods of society be allocated among claimants?" Thus, distributive justice contrasts with other questions of justice such as compensatory justice, commutative justice, retributory justice, and so on. Distributive justice is also sometimes called social justice or economic justice.

The theory of distributive justice assesses alternative distributional principles, outcomes, and institutional arrangements of a society from a moral perspective. For example, some would consider a society in which goods are unequally distributed to be *prima facie* unjust based simply on that unequal distribution. By contrast, other theories focus exclusively on the justness of procedures in a society with respect to the transfer of goods from one person or group of persons to another. For example, some would see any interference with strict property rights as unjust, even if such interference were designed to bring about a more equal distribution of goods across the members of a society.

Theories also differ on the question of which goods can be justly or unjustly distributed. These goods could range from various social and political rights, such as voting privileges, to awards and honors, to the material goods of a society, such as those that can be valued in monetary terms. In contemporary discussions, the overwhelming focus of concern is the distribution of material and financial resources. This is due partly to the fact that questions of the just distribution of various nonmaterial resources seem to be settled issues, at least in industrialized societies. For example, the question of how voting privileges should be allocated across individuals or groups based on wealth, race, and gender are no longer controversial in many societies.

Many theories focus on the distribution of material and financial resources, rather than the full range of things valuable for human life, because so many of the good things in life are incommensurable, plus they may not be subject to redistribution. What goods are to count in assessing whether a distribution is just: money, beauty, life prospects, well-being, resources, intelligence, or even happiness? Some of these desirable features of a human life are not subject to very effective redistribution, such as beauty, intelligence, happiness, and life prospects. Many are incommensurable with others. For example, how can we value the relative worth of intelligence, beauty, happiness, and money? It seems reasonable that possessing these virtues or assets in some measure adds to the quality of human life, but the contribution of each of these to the quality of a human life cannot be readily assessed in terms of the others. For example, we are told that money cannot buy happiness, but as Aristotle duly noted, a life of destitution is unlikely to be fully happy. What is the trade-off between money and happiness in general? It seems that there is no answer to such a question and that the trade-off between any two of the assets or qualities on the list will differ from person to person—some place a relatively higher value on beauty compared to intelligence than do others.

This entry focuses on the question of distributive justice as it pertains to the distribution of wealth, services, and material sources, as this is the most important area of current discussion and it is the aspect of distributive justice that is most relevant to the ethics of business and the role of commerce in society. Because these resources can be denominated in money, at least to a reasonable approximation, this entry will speak of the distribution of wealth, considered not only to embrace money but also to include the entire range of material goods and services that a society might possess and be able to allocate or reallocate.

Given this concentration on the just distribution of wealth and material resources, the issue of distributive justice is critical to business because businesses generate the overwhelming bulk of wealth and material resources in modern industrial societies. The question of how the rules of society are to be established to govern the distribution of wealth intimately affects the well-being and rights of all those who work or who establish businesses.

Some theories of distributive justice address how to move from a current distribution to one that is supposedly just. Such schemes depend upon the proper identification of a just distribution and then focus on how to redistribute wealth to achieve that distribution. Much public discourse and many governmental programs are directed to this end. For instance, government welfare programs aim at achieving a supposedly more just distribution of wealth. Similarly, colleges and universities routinely charge children of wealthy parents more than they charge children of less wealthy parents, and they justify this practice in part by an appeal to principles of distributive justice. This entry will consider only static theories of distributive justice rather than attempting to discuss theories that specify how society should move from a current supposedly unjust distribution to a future supposedly just distribution.

Egalitarianism

One of the simplest, and for many one of the most intuitively appealing, conceptions of a just distribution is egalitarianism—the view that all members of a society should have the same wealth, material resources, and access to services. According to this view, all persons are equally worthy of respect and consideration, and this implies that everyone should have the same allocation of societal wealth. For a strict egalitarian, considerations of the person's contribution, effort, and desert do not come into play. Instead, egalitarianism views a just distribution as one in which all persons share equally.

A problem for egalitarianism, again a difficulty that besets a number of theories of distributive justice, is the question of the time at which the just distribution is to be achieved. If one could achieve such a distribution at one point in time, the next moment would see the distribution become unequal. In an egalitarian world, is the goal to set an equal distribution at one moment and let the future play out as it will, or is the task to maintain an equal distribution over time, including perhaps even over the entire span of a human life?

A second criticism of egalitarianism focuses on considerations of social welfare. It is clear that such an equal distribution will not maximize welfare across all the members of a society. For example, you may value money more than another. In such a circumstance, it is clear that the total well-being of society could be increased by a distribution that gives you more money than another. This problem arises even in the simplest case of imposing an equal distribution of just a single asset such as money. But the issue is really more complex and difficult. Assume now that there are two goods that are to be subject to an egalitarian distribution: money and leisure. A distribution that gives every person the same money and the same hours of leisure per week will be vastly inferior to other distributions. If one person values leisure more than another who places a higher value on money, both persons are worse off in the egalitarian distribution than they could be in another. Specifically, in this example, the money-loving person could perform some task for the leisure-loving person for compensation, with the result that the welfare of both would increase. The problem becomes even more intense as additional goods and services are brought into consideration for redistribution. Note also that an initially equal distribution, followed by free exchange among members of a society, will be immediately subject to the timing problem discussed above.

Related to the timing question is the implication of human psychology for the viability of egalitarianism. We might call this a problem of incentives. If an initial redistribution of resources gives everyone an equal starting endowment, then each person will have incentives to manage his or her resources well going forward. However, it is virtually certain that considerable differences in subsequent distributions will quickly follow, either due to superior resource management or due to simple luck. In either case, the egalitarian distribution that seems important to these theorists will be upset. If the egalitarian distribution is to be reestablished periodically through time, incentives to manage resources well and to contribute to the social product will be greatly reduced. Such persistent egalitarian policies would undoubtedly create a society that is much poorer in the aggregate than one in which incentives were preserved better. Some egalitarians, however, concede this point but insist that the principle of equality is paramount and more desirable than an arrangement with greater aggregate social wealth.

Egalitarianism is a prime example of what Robert Nozick has called a "patterned" theory of distributive justice, a theory that holds that a just distribution is one that conforms to a certain pattern of distribution—in this case, one of equality. Such patterned theories are subject to serious criticism in that they appear to conflict with widely accepted views of people's rights. To take the simplest case, it seems that egalitarian theories of distributive justice are entirely incompatible with even the most rudimentary conception of property rights. The effort to achieve an equal distribution will necessarily require the compromising of the property rights of some to distribute to those with less. In response, the egalitarian might assert that property rights are certainly not to be taken as generally inviolable and conceivably might be justly abridged to secure other values. However, even if this be granted, egalitarianism seems to conflict with other rights that are even more basic. Some see egalitarianism as incompatible with any robust conception of human freedom. This is especially apparent for an egalitarianism that seeks to maintain an equal distribution across time, because such a policy would dramatically restrict the freedom of an individual to work to acquire additional resources and would necessitate a program of constant interference with the activities of all to restore the equal distribution. When one considers the incentive destroying effects of constant rebalancing of assets to achieve equality, it is evident that such a society would be markedly poorer than one with a modicum of respects for property rights.

As a final objection, egalitarianism seems to entirely neglect the idea of desert—the view that some can deserve more than others due to the contribution they make or the efforts they undertake. For egalitarianism, the only feature of human life that matters in determining a just distribution is the simple fact of personhood. For an egalitarian, the differences in people and the differences in what people do cannot give rise to one person's deserving more than another. In short, egalitarianism seems to require the total abandonment of the intuition that some person can justly deserve more than another in virtue of what a person contributes or the effort a person makes.

Resource Egalitarianism

Resource egalitarianism, a theory most closely associated with Ronald Dworkin, asserts that a just distribution is one that gives each person an initial endowment of equal resources from which they can construct a life. Beginning with this starting point of equality, people are then free to make whatever life they wish and they are responsible for subsequent differences in outcomes, with whatever outcomes result being considered just.

To explore resource egalitarianism, let us assume that everyone possesses an equal package of natural endowments. That is, we simplify by assuming that everyone has the same total capacity for achieving their life prospects, even though that equal capacity may be composed of different bundles of intelligence, beauty, health, physical vigor, and so on. Under this simplification, resource egalitarianism advocates giving everyone the same initial endowment of those resources that a society can distribute, such as wealth and access to education. After the initial distribution of resources, people then assume freedom to act and they are responsible for the resulting outcomes. Dworkin explains this view by imagining a society of shipwreck survivors landed on a deserted island with some rescued stores from the ship. For this society, the problem is to divide all of the resources to create an initial starting point of resource equality. Dworkin imagines an auction in which everyone receives the same money endowment and can bid on a division of lots on the island and tools and stores rescued from the ship.

Resource egalitarianism is clearly directed to resolving some of the problems with strict egalitarianism that were noted above. On Dworkin's island, under the initial simplifying assumption of equal natural personal endowments for everyone, the resolution of the timing problem is clear. There is to be a one-time distribution of resources. It is also relatively clear that the resources to be distributed are things such as land, tools, and other things that money can buy. After the distribution of resources, each person will have clear incentives to manage his or her resource allocation well. Also, the assumption that everyone has the same total packet of natural endowments seems to address the issue of maximizing social wealth. One reasonable interpretation of equal natural endowments is the view that every person is equal in capacity to use his or her resource endowment effectively.

However, some problems remain. Dworkin's desert island situation does not resemble the actual problem of allocating resources equally in real society. On arriving on the deserted island, no one has a prior claim on particular assets. For example, no one seems to have a claim on land, because the island was conveniently bereft of any initial inhabitants. Also, the stores saved from the ship do not have any owners among the survivors. For example, by contrast, it could have been one person's previously owned trunk of valuable resources that happened to wash ashore. Thus, Dworkin has imagined a situation in which a society is created from a convenient starting point. In actual human life, however, people arrive in a preexisting social order in which others have standing claims on resources. When one is born today, there are no unclaimed resources awaiting distribution to the new arrival. Thus, it seems that resource egalitarianism must repudiate the preexisting rights claims of putative owners of resources. According to this theory, it would seem that a person born today would have the same claim on resources as an existent person who has worked to create the resource pool that greets the new arrival. This leads into a second problem area for resource egalitarianism in terms of desert. On what basis does a newly born person deserve an equal share of resources that he or she did nothing to help create? Presumably, resource egalitarians are committed to the view that the principle of equality trumps such rights claims and issues of desert.

To this point, we have considered resource egalitarianism under the vastly simplifying assumption that everyone has an equal total package of personal natural endowments. Of course, this is far from true, as we know that some people are born with enormous personal gifts, while others come into the world with limited talents and with dramatic physical and mental disabilities. In this more realistic situation, resource egalitarianism maintains that the resources of society should be redistributed so that each person has the same total life prospects. Thus, a person with serious physical disabilities might need considerable resources for nursing, therapy, and so on in order to have the same life prospects as another person would.

This more robust and realistic version of resource egalitarianism retains the potential problems with rights and desert already noted. It also involves additional complications. With the recognition of different natural endowments and a commitment to distribute resources to create equal life prospects for all, the problem of what goods to distribute and how to implement a distribution returns to prominence. For example, consider a three-person world in which one person has an average endowment of intelligence, health, beauty, and so on; a second person is otherwise similar but has serious physical limitations; the third is also similar to the first but suffers remarkably low intelligence. What kind of redistribution would establish equal life prospects for these three people? In actual circumstances, it is not clear what should or even could be redistributed to create the intended equality. The force of this objection is perhaps not so apparent, given the level of abstraction for the analysis. In a real society, any implementation of ideals will always be imperfect and approximate at best. Furthermore, virtually all ideals of justice will face similar difficulties of implementation.

A more serious objection to the redistribution of assets required by resources might be called the "invasion of personhood" objection. In our simple three-person society, resource egalitarianism would require that considerable resources must be transferred to the two people with disabilities from the one person without disabilities. What resources are those likely to be? It seems that equality of resources would require that much of the labor, wealth, and life prospects of the person without disabilities must be taken from her to benefit the other two individuals. Here the issue is not merely the abrogation of a person's property rights, but it seems that the resources that will be appropriated are much more integral to one's personhood. This objection essentially asserts that such resource egalitarianism would interfere with a person's basic liberty to an impermissible degree.

Utilitarianism and Welfarism

Although better known as a theory of ethical conduct, utilitarianism also has strong implications for distributive justice. In the context of distributive justice, utilitarianism requires the maximization of pleasure across all members of society without regard to the distribution of that pleasure among persons. While originally cast in terms of maximizing pleasure, variants of utilitarianism can also specify the maximization of happiness, preference satisfaction, or personal welfare. As such, utilitarianism also requires the maximization of social welfare—the sum of welfare across all individuals in a society, again without regard to how that welfare is allocated among persons.

Utilitarianism clearly contrasts with egalitarianism and resource egalitarianism. While both versions of egalitarianism were primarily concerned with achieving an equal distribution across persons, utilitarianism totally neglects the question of who gets the benefits of welfare and focuses entirely on maximizing the sum total of welfare. We might say that utilitarianism focuses exclusively on creating a larger pie, whereas egalitarian theories focus on the just way to divide the pie.

Because it focuses on outcomes, whether those be conceived as pleasure or welfare, utilitarianism also clearly contrasts with resource egalitarianism, which was concerned with an equal distribution of resources with which individuals would then be free to create the outcomes they choose. In this respect, utilitarianism is closer to egalitarianism—at least versions of egalitarianism that focus on outcomes. But utilitarianism also contrasts with those forms of egalitarianism because utilitarianism focuses on total social welfare, rather than on achieving an equal division of welfare across persons. Because of this shared focus on outcomes, utilitarianism also inherits some of the problems of outcome-based theories of egalitarianism. One basic question is that of measurement—how is one to measure welfare, given that different individuals have different personalities and tastes? For example, will transferring money from person A to person B increase or diminish social welfare? In other words, utilitarianism faces its common problem of the "interpersonal comparison of utility"—how can we compare the welfare that one person enjoys with those enjoyed by another?

However, this difficulty of comparing welfare attainments between persons may be perceived as a mainly technical problem. Instead of focusing on the welfare of individuals, we could consider matters at a broad policy level. For example, some utilitarians hypothesize that, as a practical matter, utilitarianism might require a roughly egalitarian distribution of wealth. Because wealth exhibits diminishing marginal utility, the welfare maximizing distribution might be one in which everyone has approximately the same wealth. However, the real criterion of the correct distribution remains the one that maximizes total welfare.

If the utilitarian social planner wants to institute policies to maximize aggregate welfare, he or she must also consider the effect of social policies on the behavior and rights of citizens. Because each person's welfare is part of the total, it might be the case that the welfare maximizing policy would be to allocate resources to those who do nothing to increase total welfare. Under such a distributional scheme, some would receive benefits without working to create social wealth and incentives across society might be destroyed. Alternatively, because the policy is to maximize aggregate welfare, the welfare maximizing policy might be to force some people to work against their will. Even if this policy maximized welfare, many would see it as a serious invasion of the rights of those unwilling workers.

Moral criticisms have been lodged against utilitarianism as a theory of distributive justice. First, it gives no weight to the principle of equality. As we have seen, the welfare maximizing distribution might be one of rough equality but it need not be. Utilitarianism has also been criticized on the grounds that it gives inadequate respect to persons and their individual rights. Because the theory views persons merely as repositories for welfare and is concerned only with total welfare, it does not take account of persons as individuals. Because the theory focuses only on total welfare, it might require the seizing of assets from one person and the distribution of those to another. Thus, utilitarianism gives absolutely no consideration to property rights as such, unless respect for property rights happened to be the welfare maximizing policy. Finally, because of its single focus on maximizing aggregate welfare, utilitarianism ultimately does not even respect the basic liberties of persons. In strict theory at least, utilitarianism infamously appears to justify the possibility of enslaving some if doing so would maximize social welfare.

Rawls's Theory of Justice

The most influential work on distributive justice in the last 100 years is undoubtedly John Rawls's massive *A Theory of Justice* published in 1971 and later modified and refined in *Political Liberalism* and *Justice as Fairness: A Restatement.* Rawls attempts to create a theory of distributive justice that addresses some defects of earlier theories, such as the problems with rights and incentives discussed above with respect to other theories.

Rawls's theory centers around two principles of justice. The first principle concerns the rights of citizenship and personal liberties. Everyone is to have the maximal set of liberties consistent with everyone else having those same liberties. This implies that all are to have equal rights of citizenship—the right to vote, to have a voice in political decisions, and so on. We can construe this first principle as either a guarantee of rights or as a principle of distributive justice in which the benefits of liberty are to be distributed on an egalitarian basis—everyone gets the same basic set of liberties. This first principle has absolute priority over the second principle. The rights and benefits of citizenship granted by the first principle are not to be bargained away for any material advantage, and it is clear that the first principle does not embrace considerations of social and economic well-being.

The second principle of justice focuses on social and economic matters and has two parts. According to the second principle departures from social and economic equality are to be allowed under only two circumstances: (2a) "the difference principle"—that they lead to advantages for the least advantaged person or persons in society and (2b) that these inequalities are attached to positions and offices that are open to all persons under conditions of equal opportunity. This second principle is quite egalitarian in underlying spirit, even though it clearly intends to allow inequalities to exist under certain constrained conditions.

In allowing for social and economic inequalities that raise the condition of the worst off, Rawls is attempting to allow for incentives to come into play. For example, consider a brilliant medical researcher who could contribute vastly to the well-being of all by diligently pursuing her research and creating an important vaccine. In a purely egalitarian system, she might prefer not to work and the benefits of her creativity would be lost to society. Under Rawls's Principle 2a, she would be allowed to have a greater income than others because doing so would improve the condition of the worst off in society. In this example, creating a vaccine might well help many others besides the worst off, but that would be an incidental benefit.

As a second example, consider a talented entrepreneur who has the potential to create a business that would offer benefits to the worst off, perhaps in the form of jobs or in the form of superior cheap products that meet basic human needs. In the Rawlsian framework, the entrepreneur could justly receive superior social and economic enrichment, because his efforts would provide benefits to the worst off. Note that the condition here focuses on the absolute position of the worst off. It is possible to allow economic differences if they both raise the absolute position of the worst off even while making their relative position worse. As a final example, consider a plastic surgeon who performs purely optional cosmetic surgery for the rich. The surgeon's efforts do not affect the position of the worst off—they cannot become his patients. Therefore, in the Rawlsian scheme, such a surgeon could not receive superior social and economic benefits.

Principle 2b is also important because it places further significant restrictions on departures from egalitarianism. The requirement of equal opportunity for Rawls is quite far reaching. First, it considers current differences in social and economic circumstances as violating the condition of equal opportunity. For example, positions of political authority cannot be open to only the wealthy or the well connected. It also seems that children of wealthy parents should not have access to costly educations that are not available to children of less wealthy parents, especially as a superior education is likely to lead to further differential advantages.

But Principle 2b goes quite far beyond an attempt to eradicate the effects of differential social and economic circumstances—it also covers differences in natural talents and abilities, such as intelligence, health, athleticism, and personal appearance. Rawls claims that such individual traits are morally irrelevant in that they are the product of a "natural lottery," just as being wellborn is a function of a "social lottery." Some persons get a great genetic endowment by chance; others do not. In both the natural and social lotteries, the outcome is merely the luck of the draw for an individual and morally irrelevant according to Rawls. As the talents and abilities awarded in the natural lottery do not depend on choice or effort, they cannot be justly rewarded with superior social and economic circumstances.

Rawls believes that the undeserved natural talents and abilities encapsulated in various persons—intelligence, beauty, and so on—properly belong to society as a whole. The natural lottery merely places them in some human vessels and not in others. Within the Rawlsian framework, one of the problems for a theory of justice is how to gain access to those resources for social benefit without violating the basic rights of the persons who are those vessels. For example, the brilliant medical researcher discussed above cannot be enslaved to research for the good of society because such enslavement would violate the first principle of liberty. Therefore, Rawls is prepared to allow the researcher superior social and economic benefits if, and only if, doing so would create advantages for the worst off.

Criticisms of Rawls's theory come from several quarters. Egalitarians object to the permitted departures from equality by arguing that relative inequalities matter as well as absolute inequalities and that permitting any inequality results in a society with objectionably strong class differences and reduces a sense of community among peoples. Utilitarians criticize Rawls as fundamentally abandoning the principle of maximization. By permitting inequalities only if they raise the position of those who are worst off, Rawls makes impossible many welfare enhancing benefits for others. For example, why prevent cosmetic plastic surgery for the wealthy if it benefits the surgeon and patients while leaving the worst off undisturbed? Perhaps more sympathetically, what if the position of the badly off, but not worst off, could be improved by allowing some inequalities? This seems to be ruled out according to Rawls. For example, it seems that Rawls's theory would not permit an inequality that benefits the working poor but that did not benefit the destitute.

Advocates of maximal liberty criticize Rawls for too narrowly defending liberties in the first principle of justice. For example, the first principle does not protect property rights at all, and some see the restrictions on freedom and the redistributive intent of the difference principle as violating fundamental liberties. Resource egalitarians object to Rawls for failing to adequately compensate the losers in the natural lottery because they believe that those who are disadvantaged in the natural lottery should be awarded additional resources to compensate them for their natural disadvantages.

As a final objection, consider the view that Rawls too narrowly construes the nature of personhood. By viewing the intelligence of an individual as a social asset, he or she denies that such a feature of a person is integral to that individual's personhood. By contrast, some would find such an integral feature of a person as largely constitutive of what it is to be a person, or at least to be that person. On such a view, interfering with an individual's free exercise of that intelligence and attempting to capture the benefits of its employment would be an unconscionable violation of an individual's basic human rights.

Libertarianism

Libertarian theories of justice focus on the protection of individual liberties rather than being concerned with the actual distribution of social and economic benefits that happens to occur. In its simplest statement, the libertarian maintains that a just distribution of social and economic goods is whatever actual distribution happens to result from the uncoerced and just actions of individuals. Thus a libertarian theory would find egalitarian theories, for instance, quite irrelevant. Libertarian theories are very much in the spirit of John Locke's *Second Treatise of Civil Government*, and the most prominent recent theory that might be characterized as libertarian was advanced by Robert Nozick in his *Anarchy, State, and Utopia.* Nozick's theory consists of three principles: justice in original acquisition, justice in transfer, and rectificatory justice. While acknowledging that a complete theory of justice would require a treatment of rectification, Nozick focuses almost exclusively on justice in original acquisition and justice in transfer.

According to Nozick, if some social or economic good is originally acquired in a just manner and it is transferred in a just manner to others, then the resulting outcome or distribution is just, and a person holding such a social or economic good is justly entitled to its possession. There is no other way in which one can justly come to hold some social or economic good. Coercively removing such a holding from someone is unjust. This theory of justice focuses only on procedures, not outcomes. If goods were justly acquired originally and were justly transferred subsequently, then whatever distribution of goods that results is just.

Compared to the theories we have considered above, it is important to note that libertarian theories tend to focus on the history of holdings rather than a particular pattern of holdings. On Nozick's view, the history of original acquisition and subsequent transfer determines the justice of a holding. This contrasts markedly with views that Nozick criticizes as patterned theories. For instance, egalitarianism requires that a distribution must meet a pattern of equal holdings to be just.

Regarding the just original acquisition of a holding, Nozick largely follows the spirit of John Locke and begins by contending, with Locke and against Rawls, that one owns oneself, including one's natural talents, abilities, and labor. For goods originally in the commons, one acquires title to them by mixing one's labor with them in a way that increases their value. For Nozick this justifies the original acquisition, subject to the "Lockean Proviso" that this original acquisition must leave "enough and as good" in the commons for others. For goods that are justly acquired originally, the question of just distribution entirely depends on the justness of subsequent transfers. Just transfers are those that occur without coercion, force, fraud, or deceit. Thus if a seller correctly describes a good and willingly sells it to a purchaser who voluntarily pays for it with good funds, then the transfer is just.

Libertarian theories in general, and Nozick's theory in particular, are highly compatible with a strong system of property rights and market economies. The principle of self-ownership, which is central to both Locke and Nozick, argues against redistributive efforts, with Nozick going so far as to compare income taxation to slavery. Full ownership of oneself and one's labor contrast very strongly with Rawls's view of a person's natural talents and abilities as a common societal resource. Nozick further argues that systems of taxation and redistribution violate the Kantian ideal of treating people as ends-in-themselves. If the talents, abilities, and labor of individuals are goods within the control of society and may be coercively deployed for the benefit of others through taxation and redistribution, Nozick argues that such treatment fails to respect the dignity and rights of individuals and treats them merely as means to achieving some putatively social good.

Libertarian theories have been attacked from a wide variety of perspectives. First, many of the theories considered above find libertarian views largely irrelevant. If we view the present arrangement of holdings of social and economic goods as predominately infected by original acquisitions that were largely unjust, followed by a series of various unjust transfers, then the present-day distribution of holdings might be seen as largely irrelevant to identifying a just distribution. This criticism does not even need to oppose the reasoning of libertarian theories but dismisses them as virtually irrelevant to the conditions that obtain in human history and in today's society.

Against the account that libertarians give of just original acquisition, some critics deny that the "mixing of one's labor" with the commons could confer the dominion over property that libertarians claim. For instance, why should mixing my labor with the commons give me property rights over goods formerly in the commons instead of merely dissipating my labor into the commons? Similarly, even if the mixing of my labor increases the value of some item formerly in the commons, why should that act give me exclusive control and dominion over that good? Notably, someone else might have been able to mix their labor with the item in the commons and create greater social value by doing so. Critics argue that libertarians have not given, and are unable to give, an adequate account of just original acquisition.

Some critics attack the libertarian view of freedom and liberty as too narrow. Libertarian ideals of individual freedom and liberty focus on the conception of self-ownership and the property rights that are supposed to flow from that self-ownership. Thus, libertarians emphasize "negative freedom," essentially maintaining that one is free if one is not coerced. Other views of freedom focus on "positive freedom," emphasizing abilities, resources, and capacities to realize one's goals and aspirations. According to these critics, the narrow view of freedom adopted by the libertarians is incorrect and therefore cannot support libertarian positions regarding property rights. This same attack on the libertarian conception of freedom is also used to counter the libertarian argument regarding respect for persons and the requirement that persons be treated as ends-in-themselves. On this criticism, another way of treating persons as ends-in-themselves is not only to respect their negative freedoms but also to adopt a social organization that empowers people with positive freedoms, and such a requirement might require redistributive principles that run counter to a libertarian conception.

The Capabilities Approach

In the debate over distributive justice, "capabilities" refers to the abilities of individuals to have the resources to create meaningful and fulfilling lives. In this sense, capabilities would embrace the material wealth necessary to sustain human life at a level of functioning well beyond subsistence. One cannot achieve a full life on a starvation wage. Similarly, education and health are required too. This approach to distributive justice is most closely associated with Martha Nussbaum and Amartya Sen and most fully developed and encapsulated in Sen's *Development as Freedom.* This approach to justice is highly consonant with a positive conception of human freedom. Its focus is on what people can do with their lives and the resources necessary to achieve.

In a rich society with relatively few poor people, the capabilities approach might require a redistribution that stopped well short of egalitarianism. The distribution recommended by the capabilities approach might well set a resource minimum below that of resource egalitarianism as well. A society might be sufficiently wealthy to provide basic capabilities for a rich life to everyone without reducing the wealth to a position of equality. By contrast, in a poor society, even an egalitarian distribution might not give everyone the capabilities for a full life. For the rich society just described, the demands of the capabilities approach are fairly clear, but this is not the case for a poor society. For example, in a poor society an egalitarian distribution might dramatically reduce the capabilities of all beyond the level sufficient for a full and rich life. In such a situation, does the capability approach require that the rich give up not only the excess resources beyond that necessary for a full and rich life but that they also give up their own capabilities for a full rich life too?

Distribution by Desert

According to desert-based theories of distributive justice, people come to deserve social and economic benefits through the actions they perform or the virtues they possess. In accordance with this view, a just distribution is simply one that gives people what they deserve. The question then becomes, On what basis do people come to deserve something? With respect to contemporary discussions of distributive justice, people are generally said to become deserving through one or more of several factors related to increasing social welfare. First, one might become deserving simply by contributing to social welfare. For example, a worker might deserve compensation for the work he or she does because that work creates products that benefit others. Second, the effort that someone makes might make him or her deserving of compensation. A student might be said to deserve a good grade due in part to the effort he or she made in a class. Third, one might deserve reward due to the costs incurred in an effort to provide an increment to social welfare. Someone who sacrifices personal wealth to increase social welfare might be thought to deserve a reward in compensation for that sacrifice.

All of these desert bases are similar in that they are backward looking—one deserves something now in virtue of actions performed in the past. So, desert-based theories of distributive justice do not really address incentives. This contrasts with the Rawlsian view that justice might allow someone extra resources if doing so would create incentives for that person to perform future actions that improve the position of the worst off. Egalitarianism is not generally regarded as a desert-based theory, but we might say that egalitarianism is a desert-based theory with a very narrow conception of the basis for desert. Under egalitarianism, one deserves material goods simply in virtue of being a person rather than through performing any action or increasing social welfare.

The concept of desert is similar to that of entitlement, the difference being that entitlement generally refers to desert within the context of a particular institutional framework. For example, within the institutional framework of a market economy, one might become entitled to riches if he creates products or services that others value and are willing to purchase. If we approve of market economies, we might also say that one deserves the profits that arise from legitimate market-based transactions. This distinction allows the possibility that you can be entitled to what you do not deserve, and you can deserve that to which you are not entitled. For example, if egalitarianism is the correct theory of distributive justice one would deserve an equal share of material resources, but if the economy is organized according to free market principles, one might not be entitled to any such resources. Similarly, if one follows the rules of a game, one could be entitled to be the winner of the game. However, if the rules are defective, it is possible that a person who is entitled to be the winner might not deserve to be the winner.

Desert-based theories generally face the problem of specifying which contributions to social welfare might be deserving. If I work, does that mean I deserve compensation, and if so, how much do I deserve? Merely saying that contributing to the economy creates a basis for desert does not really say how the goods of the economy are to be distributed with sufficient specificity. While some other theories share this problem, others do not. Egalitarianism, for example, specifies quite exactly the principles for how much each person is to receive, even if implementation is difficult. Desert-based theories need to connect the desert basis with further principles to specify the actual distribution more clearly. As we have seen, one way of making this specification is to endorse market-based transactions as correctly specifying how reward is to be allocated. Furthermore, if the only basis for desert is taken to be a contribution to social welfare, then it might seem that desert-based theories are incomplete. A newborn infant makes no contribution to social welfare, but would we want to say that the infant does not deserve any care or sustenance?

Feminist Approaches

Feminist approaches to ethical theory are actually quite diverse and continue under rapid development. Thus, this entry attempts mainly to focus upon just two common themes: justice in the public versus private sphere and the relative importance of justice versus caring.

In contrast with the history of ethical thinking in the West and its focus on the public sphere, many writers in the emerging feminist tradition focus on the private sphere of home, family, and interpersonal relationships. In general, they attack what they see as the male-dominated focus on distributive justice operating only in the public sphere and a disregard for injustices that may be perpetrated against women in the private sphere. For example, paid work in the United States is typically documented and leads to social security payments in later life. By contrast, unpaid work in the home receives no public recording and generally does not receive any subsequent public benefits or acknowledgment.

A number of feminist writers argue against the traditional nuclear family as a system that creates distributive injustices for women. The fact that women bear a disproportionate obligation in child-rearing and that women's work in this context is generally unpaid lead to injustice, they maintain. These theorists often maintain that there exists a rigid distinction between the public sphere in liberal Western societies, in which the political system distributes society's goods, and the private sphere, which has been free from governmental intrusion. This makes the private sphere a zone in which injustice persists and one in which redress is necessary. These writers generally attack liberalism and want to make the distinction between the public and private sphere less distinct. For example, some advocate that homemakers and child rearers have the value of their work recognized by inclusion in the social security system. Against this view, critics point out that the demand is unclear and perhaps quite counter to women's real interest. Just how much intrusion by government in the previously private sphere of the home do feminists truly wish? Further, some see that women have done much better in liberal societies with a strong public/private distinction than they have in more traditional societies.

Some feminist writers also attack what they see as the long-standing focus of the Western ethical tradition on rules and moral judgments. They believe that caring and nurturing relationships, traditionally the province of women, deserve greater moral weight. Instead of being so concerned with what justice demands, these authors argue that perhaps we should be much more involved with the giving of care. Some of these authors see caring relationships, notably the relationship between mother and child, as forming the basic relationship for understanding morality. In a sense, then, this is an attack on the importance of the traditional principles of distributive justice.

Global Distributive Justice

Perhaps due to globalization, the entire topic of global distributive justice has gained increased attention. Demands of egalitarianism have traditionally been applied to single societies or nation-states. John Rawls, in his later work for example, makes this restriction explicit. However, why should the demands of justice stop at the confines of a particular society, geographical area, or political unit?

This line of reasoning has vast implications for actual social policy. Egalitarianism might be controversial as a policy within the United States, but if justice were to demand egalitarianism across all humans, the income and distributional effects would be even more radical. A similar issue obtains for the capabilities approach. Does the world contain enough resources to provide the capabilities for a rich human life to all?

Extending the province of justice from one society to all humanity causes fewer issues for other theories, such as libertarianism and desert-based theories. Libertarianism focuses on the procedures for acquiring and transferring assets, and the needs of others do not come into play. Similarly, if desert-based theories are applied globally instead of being applied to just one society, the desert bases might not be changed at all. The exploration of the question of global justice is in its infancy, but it seems clear that the extension of the sphere of justice to all humanity can have enormous policy implications.

—Robert W. Kolb

See also Capabilities Approach to Distributive Justice; Communitarianism; Commutative Theory of Justice; Desert; Egalitarianism; Entitlements; Equality; Fairness; Freedom and Liberty; Income Distribution; Interpersonal Comparison of Utility; Justice, Compensatory; Justice, Retributive; Justice, Theories of; Libertarianism; Meritocracy; Nozick's Theory of Justice; Primary Goods; Procedural Justice: Philosophical Perspectives; Rawls's Theory of Justice; Redistribution of Wealth; Utilitarianism; Utility, Principle of; Well-Being

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Justice, Retributive

Retributive justice concerns fairly blaming or punishing people for their wrongdoing. Descriptions of retributive justice are found throughout recorded history. Often the notion of retributive justice is described as "an eye for an eye," a concept that provides the basis for Western theories of punishment.

Those who favor punishment based on concepts of retributive justice believe that treating people as responsible adults is core to recognizing the essential humanity of each person. To not deny someone the privilege of being held responsible for his or her choice is treating them as less than a full human being or as a child. Thus, those who align themselves in the deontological tradition—duty and rationality governing our search for the ideal—are often vocal proponents of retribution for wrongdoing.

In recent years, the principle of retributive justice has been moderated by the idea of rehabilitation, providing people the skills and resources necessary to avoid a life of crime. The belief behind the theory of rehabilitation is that people basically are good and violate the laws only because they believe they have no other choice. Theorists in this camp believe that illiteracy and poverty are two of the greatest drivers causing people to choose a life of crime. Thus, those who align themselves in the teleological tradition—seeking happiness while living a virtuous life—are often vocal proponents of rehabilitation.

The tension between the two approaches was seen in the sentencing of ex-Adelphia CEO John Regas. The court sentenced the ailing 80-year-old to 15 years in prison, which seemed a moderate punishment compared to the 215-year sentence sought by the prosecution. However, rehabilitation is clearly not an objective as the 15-year sentence seemed designed to send a message to all other executives who might be considering bending—or breaking—the rules.

Social Purpose of Retributive Justice

While in a community and even in individuals the pendulum swings between the desire to punish and the desire to rehabilitate, the idea of retributive justice is important in establishing and maintaining social norms. Neil Vidmar suggests that before the desire to retaliate occurs, the perpetrator must have intentionally violated a norm or rule of the community. When the violation threatens the personal self, status, or internalized group values, those who are aggrieved become angry. That anger often becomes focused on the perpetrator and is released or dissipated during the punishment.

Thus, desire for retributive justice is often emotion laden and can lead to mob action, as seen during mob lynchings or "self-help" responses to injustice, which inflame an entire community. The 1992 Los Angeles riots, named the "Rodney King uprising," erupted after the acquittal of white officers who were charged with assault in the televised beating of Rodney King. In that situation, the community believed that the judicial system failed to punish appropriately and so took the law into their own hands. Because of situations such as those particular riots, many who argue against severe punishment believe that retribution is in fact nothing more than vengeance or revenge, thus punishment should be severely curtailed.

Retribution Distinguished From Vengeance

Robert Nozick asserts that retribution differs from revenge in that a social norm—a wrong to the community—has been committed. This wrong is of greater significance than a slight or injury that is unintended but can result in a desire for revenge. Further, retribution is constrained by the legal community. Every effort is made to ensure that the punishment is proportional to the wrong. The constraints of the legal system strive to strike a balance between a healthy sense of anger at the violation of a personal or community norm and unbridled anger that may result in the desire for revenge not being satiated.

Because seeking revenge in a rational and measured way is difficult, retribution demands impartiality. The judge who is meting out the punishment is not to have any personal interest in the offense. An example of the testing of the limits of impartiality came when a Colorado judge was overseeing the trial and sentencing of an arsonist who set a national forest on fire. The fire came within yards of the judge's home. The determination was made that even though the judge's home was threatened, he was able to be impartial and fairly apply the law in the sentencing of the convicted arsonist.

Retribution is also to be emotion free. To ensure an appropriate punishment, one is not to get satisfaction from the specific incident of retribution. One meting out punishment may have a hatred of wrongdoing but should hold no particular bad feelings against the person being punished. Finally, retribution is principled and rejects collective guilt. In this way, those who commit similar crimes are given similar sentences. Also, the individual who committed the crime is punished, not every person who is part of the same racial or ethnic class.

Conditions Required for Retribution

Three conditions are traditionally required to find that a retribution for a wrong is permissible.

1. *People are capable of knowing what they did.* If a person is incapable of knowing what they did because of mental incapacity or insanity, then retribution may not be appropriate. Determining what punishment is appropriate if the person voluntarily became mentally incapacitated due to use of alcohol or drugs is always perplexing. The general rule is that self-imposed incapacitation does not relieve a person of responsibility for the act. A second problem arises if the person became incapacitated after the event. One solution is to place the person in a mental hospital until he or she regains "sanity." This solution sometimes results in the anomaly of people serving more time in the hospital than they would if they were jailed for the offense.

2. *The person being punished must be the person who actually committed the wrong.* Correctly identifying the perpetrator is important to meet this requirement.

Furthermore, scapegoating or punishing someone who is not responsible for the action but who is a representative for the offending group or person is not permitted.

3. *The punishment must be consistent and proportional to the wrong.* Retributive justice depends on meting out everything proportionately to what the action deserves, either positively or negatively. In terms of punishment, retributive justice results in the deprivation of goods or in actual punishment. Fines that are imposed should bear some relationship to the damage caused by the wrong that was committed.

Punishment as a Deterrent

One of the functions of punishment is to act as a deterrent to members of the community from taking actions that are against the community norms. Many long-term studies show mixed results. Some studies indicate, for example, that the death penalty does not deter murders. Other studies indicate that longer sentences neither deter crime nor reduce recidivism. Other research shows that in times of greater punishment, the crime rate appears to go down.

One intriguing approach to deterrence focuses on both the frequency of enforcement and the severity of the punishment. To effectively deter crime, the legal system must either have infrequent enforcement with very steep penalties or frequent enforcement with more modest penalties. Infrequent enforcement with low penalties tends to have no deterrent effect; frequent enforcement with very high penalties leads to overcrowding of prisons and overwhelming the system.

Punishment as Method of Balancing Power Between the Injured and the Perpetrator

Another purpose of retributive justice is to counteract the perpetrator's dominance over the victim. The community is able to stand in solidarity with the victim and demonstrates that the action of the criminal is not acceptable to the community. During the past 20 years, the practice of having a victim advocate center in the judicial system of the United States has gained in popularity. These advocates are able to present evidence to the court to ensure that the interest of the victims is articulated. From time to time the desire for revenge will result in dissatisfaction with the resolution of the criminal case. In those cases, care must be taken to remember that the primary function of retribution is to restore the honor of the state, the community as a whole, not to make the victim happy with the result.

Conclusion

Perhaps the most famous attempt of a community to use the tools of restorative justice to stop the cycle of revenge fueling retributive justice was the Truth and Reconciliation Commission in South Africa. Designed to mitigate the ongoing anger and violence resulting from years of apartheid, the Commission brought together victim and perpetrator to meet, dialogue, and hopefully forgive.

Key to the success of this effort was the genuine remorse on the part of the perpetrators. Indeed, all of the research on retributive justice indicates that the remorse of the perpetrator is a significant factor in determining the severity of punishment deemed appropriate by a jury and judge. The more genuinely remorseful the perpetrator, the more likely the jury is to show mercy and the victim is to extend forgiveness.

Retributive justice thus becomes a critical tool for assuring that the norms of the community are upheld, cycles of violence and vengeance are stopped, and ethical balance is restored to the community. To have maximum effectiveness, judges and juries charged with the administration of justice must carefully weigh the claims of both the victim and the perpetrator to find the proper balance between justice and mercy.

—*Catharyn A. Baird*

See also Compensatory Damages; Fairness; Human Nature; Justice, Theories of; Legal Rights; Media and Violence; Moral Agency; Procedural Justice: Philosophical Perspectives; Procedural Justice: Social Science Perspectives; Self-Deception; Self-Regulation; Shame

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Justice, Theories of

The question "What is justice?" is the first problem addressed by Plato's *Republic.* It has remained a central question in all moral, legal, and political thought. There are narrow and broad uses of the terms *just* and *justice.* In its narrowest sense, justice is close to lawfulness, and a just act is a legal one, meaning primarily that it is not illegal. Another narrow use is procedural, with the sense that certain decision-making procedures deliver a product that a state calls justice.

In its broader senses, which are of the greatest interest to philosophers and other theorists, justice is thought of as an attribute either of acts, including transactions and decisions; of conditions, including rules and laws; or of entities, including persons, gods, societies, and states.

Aristotle held that the creation and maintenance of justice was the most important task of the state. A just state was ruled in the interests of the whole population, while an unjust state was ruled in the interests of its ruling class. Aristotle distinguished between distributive and commutative justice. The first deals with the distribution of rights, benefits, costs, and responsibilities within a class, for example, among citizens of a state, among family members, or among stakeholders in a corporation. The second, now widely known as retributive justice, deals with the treatment of individual persons or interests—for example, in a transaction or in meting out punishment. This second way of thinking about justice involves consideration of what people deserve according to some standard, such as law or precedence. Poetic justice, in which one unexpectedly gets what he or she deserves, is a notion of retributive justice. The distributive notion of justice involves, as Aristotle has it, treating equals equally and unequals according to their relevant inequality—so that, for example, juveniles and adults are accorded differing rights and responsibilities with regard to alcohol, marriage, driving, and voting. Injustice would clearly arise from treating a member of one class according to the rules laid down for the other class.

Today, theorists are unlikely to assert that there are two distinct conceptions involved in our thinking about justice, though most will agree that we have notions about justice that can be at odds with one another. Each of several employees might deserve all of the bonus dollars available in a given year, but it might still seem more just to divide the money among them. In that case, the desire for a kind of distribution is apparently at odds with the desire to give what is deserved. Some contemporary theorists emphasize the notion of distributive justice while others emphasize individual rights and thus the retributive notion of justice.

The concept of social justice takes justice as the attribute of a society in which a certain pattern of distribution is roughly realized throughout the most important institutions of society. To discover the right distributions, John Rawls attempts to produce a hypothetical social contract. His basic idea is that a contract made under certain constraints will guarantee justice. These constraints involve assuming a "veil of ignorance"—we choose social arrangements from behind this veil by supposing that we must enter the world our policy choices create, though we are ignorant about how we will enter it, meaning that we might enter it in any condition of wealth or poverty, health or ability, race or gender. The veil of ignorance ensures choices for political and social arrangements that will be acceptable to all because it prevents choices based on discrimination among types or classes. By ensuring impartiality in decision making, it guarantees fairness in the distribution of benefits and costs in a society, and hence a just society. Many have argued that Rawls's method of achieving impartiality refers all decisions to rationality alone, apart from habit, passion, or prejudice. However, that claim has often been rebuffed with the suggestion that Rawls merely rationalizes moral intuitions that may themselves be rationally unfounded or unappealing.

For Robert Nozick, Rawls's thinking concentrates too heavily on the outcome of transactions and thus violates our sense for the just transaction. Nozick defends unequal accumulations of private property as results that, rather than being good in themselves, can be reduced only at the cost of denying significant rights. Starting from John Locke's assumption that individuals have rights, and that their rights include the right to engage in activities that do not harm the rights of others, Nozick develops rules for just transactions. So long as transactions are just, their outcomes must be just. On that basis Nozick is able to defend social stratification and huge differences in accumulated private property, while also arguing against socialist schemes for redistribution as covert justifications for injustice. Nozick's thinking has often been challenged on the ground that it does not deal with the notion of a just original acquisition, nor with the justice or injustice of the historical conditions into which individuals are born. Rawls's theory of justice as fairness is frequently held up against Nozick because it addresses those areas.

When justice is taken as an attribute of acts, the retributive notion of justice is highlighted, as demonstrated by Nozick. When it is taken as an attribute of social conditions, the distributive notion is paramount, as in the case of Rawls. When justice is taken to be an attribute of persons, or parts of persons, such as intentions or other states of mind, theorists tend to find acts and conditions just or unjust according to whether the just individual would recommend them. These views subordinate justice to a theory of virtue and turn legal and political theory into adjuncts either of the theory of the just individual or the theory of the impartial judge. Aristotle famously took this course. Plato took the same course, defining justice as "performance of one's proper function"—which is usually taken to mean something close to minding one's own affairs. For Plato, each of the three parts of the soul needs its own virtue to rule it. The appetites require temperance. The emotions require fortitude. The intellect requires prudence. But the entire soul, taken as a unity, requires justice—assuring that the virtuous soul does not squander itself on minor affairs. Plato's view entered into Christian doctrine under the rubric of the four cardinal virtues. The apotheosis of justice as an attribute of beings is reached in the monotheistic view of a deity who, as the ultimately just being, is the only proper adjudicator of the universe.

The question of whether positive law, meaning law as "posited" or laid down by lawmakers, can be judged as just or unjust by appeal to a higher law, usually called natural law, is a perennial concern of political theory. Natural law, if there is such a thing, would be a body of law binding on people because they are human, rather than because of local customs or powers. It would also be the basis for natural justice, meaning justice to which people are led by their natures alone, rather than by rules or rulers. Many medieval philosophers, including Thomas Aquinas, attempted to derive natural law from an even higher, divine law. Immanuel Kant and others objected to this approach by claiming that it makes natural law into a species of positive law—namely, law as posited by God—while also eliminating the possibility of an objective natural justice to which God must conform because he knows what is just. Thomas Hobbes, Locke, and Kant offered theories of natural rights on the basis of their understanding of natural law. These are supposed to be rights people have because of their natures, not because of political structures, and are often said to be inalienable due to the fact that human nature is inalienable. The theory of natural rights survives in the contemporary theory of human rights. Procedural conceptions of justice tend to reduce the list of human rights to procedural concerns, so that instead of rights to life and liberty, for example, one has rights pertaining only to adjudication before an impartial judge and perhaps to an appeal of that decision to another impartial judge.

Natural law is often appealed to as a standard for criticizing positive law. However, objections to positive law need not be understood as deriving from insight into a law behind the law. Skeptics about natural justice include the positivist school of legal scholars, who recognize no basis for justice outside of positive law. Others, such as Karl Marx, deny natural justice but nevertheless admit that people are prone to the illusion that there is such a thing as natural law, and aim to accommodate that illusion by setting up states and creating conditions purportedly in accord with it.

The most time-honored way of rejecting the notion of a standard to which all positive law must conform arises from viewing positive law as convention. A convention is a human contrivance that solves a problem, as exemplified by laws requiring either that one drive only on the right or only on the left side of the road. It seems unlikely that there is a higher standard that could decide which of these contrivances is more just. The theory that law is conventional was held by Marx, who thought of justice as the set of legal decisions made by and in the interests of a ruling group. Rawls also holds that laws are conventions. Unlike Marx, however, he also holds that just laws are conventions that anyone will see the advantage of maintaining. Wherever conflicting interests and claims require means of resolution, few will deny that the fairest means of deciding between those claims ought to prevail, and Rawls thinks he can ensure the fairest means. Marx can offer as a means only the decisions of a preferred ruling group, such as the proletariat rather than the bourgeoisie.

Meanwhile, Nozick appears to hold that law is not merely conventional and that it cannot be contained strictly within positive law. His libertarianism rests on something outside the realm of conventions, such as inviolable natural or human rights, because he holds that it is always or almost always unjust to have a convention that allows rights pertaining to the outcomes of transactions to supersede the rights realized within transactions, so that, for example, a restriction on the amount of a region's media that a single interest can own must always or almost always be unjust. Conventionalist and positivist approaches sense something too restrictive in Nozick's thinking about the writing and proper use of public conventions such as law. Justice, these theorists like to point out, presupposes conflicting claims and interests. Impartially adjudicating claims has the statistically predictable result that at least occasionally one's claims will be treated more harshly than those brought by others. Thus it looks unrealistic to hold that the rights realized within transactions must always be of greater merit than those pertaining to the outcomes of transactions. At least occasionally, they assume, claims supporting otherwise just transactions will have less merit than those concerned with preventing the outcome of those transactions.

—Bryan Finken

See also Aristotle; Divine Command Theory; Equality; Ethics, Theories of; Fairness; Hobbes, Thomas; Human Rights; Impartiality; Kant, Immanuel; Locke, John; Marx, Karl; Natural Law Ethical Theory; Nozick, Robert; Political Theory; Positivism; Preferential Treatment; Rawls, John; Redistribution of Wealth; Rights, Theories of; Self-Deception; Social Contract Theory; Social Ethics; Socialism; Stakeholder Theory; Virtue; Virtue Ethics

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Just Price

The classic idea of the just price is that it is a sum of money roughly equal to the real value of an object in an exchange. Modern economic theory gives considerable attention to the mechanisms of price-setting but tends to be agnostic with regard to the question of whether prices are or can be known to be fair or just. The question itself is often regarded by economists as a relic of a primitive precapitalist society. On a more practical level, though, the justice of prices is a very real concern for business, law, politics, and even religion, to say nothing about anyone who must attend to the affairs of daily life. While acknowledging the limitations of premodern economic theories, it is still the case that the concept of just price is meaningful and in some contexts genuinely useful.

History of the Concept

The starting point for most traditional discussions is the *Nicomachean Ethics* of Aristotle. In his treatment of the larger topic of justice in Book V, he indirectly offers some principles for treating the issue of fair price. The context is a discussion of what he calls "rectificatory" justice, which is that part of justice that concerns transactions between persons and that rectifies or makes equal the situation of the parties to a transaction.

To illustrate the essence of a voluntary transaction, Aristotle chooses the sale of goods. The sale is just when the objects exchanged are comparable in value and unjust when one party receives less than he gives.

Aristotle says little about how the value of objects ought to be determined, but he does recognize that value is not intrinsic to the objects exchanged. Indeed, he insists that the real root of value is human need (*chreia*) and that money becomes a measure of this. On his account, the fact that a voluntary transaction proceeds is a sign that the parties have satisfied themselves that they are exchanging objects (or money for objects) of equal value.

Therefore, a price, which is the value of an object in an exchange measured in money, is known to be just when persons who need or desire that object willingly pay the price to receive it. To put it another way, the price is just when it is an accurate measure of the value of the object in that place and time. No one, in Aristotle's view, would voluntarily sell something for less than its value nor buy it for more than its value, in the context of the exchange.

In adopting this view, Aristotle and the just price theorists who followed him, implicitly reject a subjective theory of value as a meaningful concept for analyzing exchanges. What matters is not the value that a particular individual might place on an object in an exchange but the value that would be assigned to it by a market, that is, by the common estimation of knowledgeable persons who have no special interests in the matter. One person may attach a very high value to my house because he or she has pleasant memories of children growing up there—and that person may be unwilling to sell it for that very reason—but the subjective value that person grants to the property has nothing to do with its value in exchange (at least, not for a classic just price theorist).

Roman law offers two other helpful contributions to the practical resolution of questions of justice in pricing. The foundation of Roman law concerning sales is the principle of freedom to bargain. According to this principle, buyers and sellers, acting in good faith, are free to agree to whatever terms they wish in a transaction. Unless fraud is involved, willing parties to a transaction have no grounds to sue for a remedy if they later decide that the transaction was unfair in its terms. The assumption is made, as in Aristotle, that the terms are fair if all parties have willingly agreed.

The second Roman legal contribution is the doctrine of *laesio enormis* or "great injury." This was an innovative principle that provided grounds for a lawsuit if, under certain circumstances, the price paid for a parcel of land was unfair. Specifically, if, subsequent to the sale of a tract of land, the seller, or his heir, came to believe that he had received an unfairly low price for the land, he could sue the buyer. If the suit was successful, the buyer was required to restore the land to the seller or to pay the difference between the actual purchase price and the "fair" price.

In commenting on the passage from Aristotle discussed above, Thomas Aquinas, an important representative of medieval thinking about price, agreed that the value of an object does not derive from the "dignity of its nature" (*secundum dignitatem naturae ipsorum*) but rather from human "need" (*indigentia*). He acknowledged that one way of determining value might be to assess the costs involved in making the object available for a transaction, but in his later work he seemed to prefer to base a judgment of monetary value upon the common estimation of the community. Of necessity this estimation is highly dependent on time and circumstances. Nevertheless, a seller (or a buyer, for that matter) cannot legitimately take advantage of the distress of another and enrich himself o herself. To be fair a price must be available to all, regardless of the circumstances of the buyer or seller.

For Thomas, then, the price that an object would fetch in the marketplace is presumed to be the fair price. In general, sellers and buyers are guilty of a sin of injustice if they knowingly conclude an exchange at a price which differs from what one of them believes the fair market price to be. Circumstances of scarcity or special demand may justly raise the market price to some degree, but perhaps only modestly. In practice, the human need for the necessities of life imposes limits of profitability upon the sellers of necessities, whose ownership of them is contingent.

In its principles, medieval thinking about just price is congenial to modern pricing theory, but another dimension of the medieval doctrine provoked later misunderstandings. Medieval lawyers and theologians (who provided spiritual counsel to merchants) were skeptical about the fairness of markets and not without reason. Markets were often imperfect, and this permitted merchants to exploit individuals and communities. As a consequence, these thinkers defended the common practice whereby authorities in the community set prices and wages arbitrarily. Most prices set in this way were understood to be just by definition since they resulted from a legitimate exercise of civil or religious authority.

It may be the defense of this practice that provoked modern economists to assume mistakenly that ancient and medieval thinkers grounded the concept of just price in a notion of objective or natural value, or perhaps even a labor theory of value, rather than the common estimation of a market. In truth, however, every influential ancient or medieval thinker defended the notion of just price as that price determined by common estimation or the market.

Just Price in a Modern Economy

Drawing on the traditional analysis of just price, three conditions can be identified that must be satisfied if a price is to be considered just. (The price in a transaction in which these conditions are not satisfied may still be just but only incidentally so.) These conditions can be accommodated to a modern economy.

The first condition is that the buyer and seller must both be adequately informed about the relevant characteristics of the thing sold. Neither a buyer who is unaware of a hidden defect nor a seller who is ignorant of special characteristics can be said to have truly estimated the value of a thing. Buyers or sellers who are ignorant in one of these respects, therefore, cannot be said to have acted voluntarily.

Second, both buyer and seller must be free not to conclude the transaction if either is dissatisfied with the price. A more contemporary way of putting this is to say that buyer and seller must both be free to negotiate the price. This condition may be satisfied when there are multiple buyers and sellers in a marketplace—such that a buyer is free to seek another seller and a seller free to seek another buyer.

Third, both buyer and seller must be free from extraordinary pressures or constraints with respect to the transaction. A transaction in which one of the participants acts under duress, out of fear, or because of extraordinary need fails to satisfy this condition.

In a developed economy these conditions are ordinarily satisfied for most consumer purchases, though in some important instances this is very clearly not so. Relevant information is generally available, though packaging or advertising can sometimes conceal or mislead. Buyers can seek another merchant or a substitute product, while sellers can wait for another buyer. And neither party is normally under extraordinary pressure. There are, however, some common transactions where the conditions for just price cannot, in principle, be satisfied. These include sales under monopoly (single seller) or monopsony (single buyer) conditions or the sale of some items (some pharmaceuticals, for example) where the purchasers are almost always under some unusual pressure.

Note, however, that sales of singular items (a parcel of land, a unique work of art, a historical artifact) can usually meet the ordinary conditions for just price.

In these other circumstances a judgment about the justice of a price can still be made by considering upper and lower limits to prices or estimating what price would result if there were a functioning market for the item in question. Just prices are normally to be found within the boundaries described by the cost of bringing an item to the sale (the lower limit) and the value of the benefit derived by the purchaser (the upper limit). Under normal circumstances, no one would sell an item for less than he paid to acquire it. Similarly, no one would buy an item for more than the cost of an acceptable substitute or for more than the cost of the harm he hoped to avoid by purchasing the item.

The case of pharmaceuticals is more subtle. Some medications are very costly to develop and bring to market. Companies would not reasonably invest in developing a new medication if they thought that sales of the product over a period of time would not compensate for the investment and provide a profit. On the other hand, many individual patients may not be able to afford the sophisticated medications they require and their need may be desperate.

Nevertheless, the high price for these medications may well be just, even though individual patients find it unaffordable. The special circumstances or limitations of a buyer do not make a price unjust but they may call into play other resources from the larger community to insure that both seller and buyer are able to obtain what they need.

In sum, a just price is always an estimation, even in unusual situations, of the value that would attach to the object of a transaction in a properly functioning market.

—Robert G. Kennedy

See also Commutative Theory of Justice; Deceptive Advertising; Fairness; Freedom of Contract; Intrinsic Value; Justice, Theories of; Marketing, Ethics of; Predatory Pricing and Trading; Pricing, Ethical Issues in

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JUST WAGE

Alasdair MacIntyre has explained that when speaking of justice, we are always faced with the question of "whose justice" and which tradition. In facing the definition of a just wage, we encounter a similar problem as well as a further complication of application: Whose justice and whose application of justice to wages? This entry will explore two visions of justice and their applications to wages, which can be generally divided into a "market" or "neoclassical," or "strategic" notion of a just wage *and* a communitarian, social, or Aristotelian/Thomistic notion. Both sides agree that a just wage is fair and equitable compensation for work; however, what constitutes fairness in the determination of a just wage is the basis of significant controversy. At the heart of this controversy is an understanding of what good is exchanged in the wage between employer and employee as well as two different notions of a corporation. This entry lays out the underlying values and principles of each perspective and then applies these different principles and values to a particular case.

A Market View of Just Wages

For those who advocate a market understanding of wages, the buying and selling of labor is much the same as buying and selling any other good or service, with its price being determined by the interaction of supply and demand. In the event that quantity supply and quantity demand are not in equilibrium, then the price of labor (the real wage) will adjust upward (to alleviate a shortage of labor) or downward (to alleviate a surplus) to reestablish the equilibrium market clearing price. This understanding of wages has two principal values that inform its notion of whether a wage is just or not: freedom—the ability to freely exchange so as to protect one's autonomy and efficiency—the ability of the market to reward those who contribute to production.

In terms of freedom, this market function provides the ability of individuals to freely contract with others in pursuit of their own self-interests and utility preferences. Freedom of exchange through the price mechanism will allow a wage to adjust according to both parties' perception that what they receive in value is at least as much as what they surrender. In terms of efficiency, the market allocates the amount of a wage predicated upon talent, effort, and contribution of what it produced. Those with more education, greater productive skills, more ingenuity, harder work ethic, etc., directed toward providing goods and services that people want, will be rewarded according to their contribution. John Bates Clark, the originator of the marginal productivity theory of income distribution, argued that the distribution of income is regulated by a natural law, and when this law operates without friction, people are provided the amount of wealth they have created. While this process may create initial inequality, in the long run its efficiencies will eventually raise all boats, since it creates proper incentives for people to acquire education and skills as well as to work harder and smarter.

Interruptions or "friction" in this market process, through the state, unions, or other nonmarket entities, will weaken the role of price signals and disincentivize people from higher education, skill development, and risk taking, which will lower the efficiency of the market, producing less wealth and consequently resulting in greater injustice. It will also lessen the freedom of employers and employees by preventing them from acting according to their own preferences, unnecessarily limiting their freedom and consequently curtailing their autonomy, all of which reduces the possibility of justice.

Corporate human resource policies, influenced by the market view of wages, define compensation in "strategic" terms: the purpose of pay is to attract, reward, retain, and motivate employees who best achieve the strategic goals of the organization. These strategic goals tend to be economic in nature: beating the competition, growing market share, enhancing quality, raising customer satisfaction and retention, increasing efficiency, motivating performance and maximizing shareholder wealth—goals that create the proper incentives to generate greater efficiencies in the organization. Key here is the proper alignment of pay to performance that strengthens the strategic direction of the company.

According to the market view of wages, paying employees according to their skill or contribution will increase efficiency whereas failing to pay according to their talent and skill will decrease efficiency. To reduce pay of talented employees in order to reduce labor rates will often foster turnover, resulting in poor morale and lower reputation of the firm. It will also increase opportunity costs by missing out on future business opportunities, all of which increases labor costs and lowers efficiency, which results in a less stable organization.

The obvious question for this market/strategic view of wages is what happens when human performance is not a major determinant of organizational performance? What happens when jobs require little skill, a large labor supply, and weak protection for workers? From a strategic perspective higher pay and benefits have no apparent pay back in terms of producing benefits for the strategic goals of the corporation. In this situation, it is unnecessary to raise pay, largely because employees have no other company to work at, limiting the inefficiency of turnover within the firm. Such low pay will also provide proper incentives for employees to seek more education and skill development, which will increase their value to organizations.

The bottom line for this market/strategic view of wages is that people and organizations must be free to negotiate and contract the wage price. This freedom will produce justice by allowing markets to determine wages based on the contribution of production. This in turn will produce the greatest efficiencies precisely because one is neither overpaying nor underpaying for individual contributions. Here justice and injustice derive not from equality or inequality but from the consequences of efficiency and inefficiency that create the conditions for more or less wealth. A just wage is what produces the greatest amount of wealth to be distributed according to contribution, effort, and skill.

A Communitarian View of Just Wages

A market understanding of justice is very different from the communitarian view of an Aristotelian/Thomistic view of justice. Justice within this perspective is a habit that directs the person's actions to the good of the other so as to contribute to stronger bonds of community. A just wage here refers to employers' and employees' habit of heart and mind to pay and receive wages that helps to build authentic relationships between the two. A just wage is not simply only about the amount given or the efficiencies produced but also about the intentions of the parties involved and ultimately about the relationships that are necessary to establish a community of work.

The key to understanding a just wage within this view of justice, then, is whether the wage fosters "right relationships" between employer and employee. Justice comes from the Latin *ius*, which means "right"; that is, the just person is in *right relation* to others, or well disposed toward another. Within this communitarian virtue tradition, "right" is not understood individualistically in terms of "my rights," especially in terms of private rights to have autonomy over body, property, or company; but rather predicating itself on the social nature of the person, it sees that one is right when one is in right relationship with another.

When the word *justice* is used in reference to wages, the question is what the characteristics of "right relationships" between employee and employer are. According to Josef Pieper, key to this relationship is that both parties recognize that the wage given can never fully account for the work done, precisely because work is always "more" than its economic output or instrumental value. If this insight of incommensurability of the wage is not recognized and that the wage is reduced to the market value of the work, then the wage becomes a mere exchange and, depending on the power relationship, one party will instrumentalize and manipulate the other to his or her interests. Therefore, it is better to avoid speaking of wage as primarily an *exchange*, and to speak of pay instead as part of a work *relationship* between employer and employee, a relationship that when it is in right order can serve to strengthen a community of work.

The principles of need, contribution, and order begin to describe what a right relationship looks like in determining a just wage. These three principles define a just wage as being simultaneously a living, equitable, and sustainable wage.

Need and a Living Wage

When an employer receives work from an employee, they participate not only in an economic exchange but also in a personal relationship. In order for this relationship to flourish, an employer must recognize that employees (in particular full-time adults) "surrender" their time and energy and so cannot use it for another purpose. A living wage, then, is the minimum amount due to every independent wage earner by the mere fact that he or she is a human being with a life to maintain and a personality to develop.

Contribution and an Equitable Wage

Yet a just compensation is a complex system within a complex organization. It cannot be determined by only one principle such as need. The principle of need is *necessary* for determining a just wage, but alone it is *insufficient*, since it only accounts for the consumptive needs of employees and does not factor in their productive contributions to the enterprise. Because of effort and sacrifice as well as skill, education, experience, scarcity of talent, and decision-making ability, some employees contribute more to the organization than others, and are "due" more pay. In other words, a living wage, while a minimum floor, is not necessarily an equitable wage. To honor someone in the wage relationship is to recognize his or her talents and efforts. An equitable wage, then, is the contribution of an employee's productivity and effort within the context of the existing amount of profits and resources of the organization.

Order and a Sustainable Wage

But pay is not only income for the worker; it is also a cost to the employer, which has a significant impact on the economic order of the organization. A just wage cannot be determined without considering the effect wage and reward levels have on future resources. There is an ecological principle operative in pay systems: Actions cannot be taken without reactions. Without the foresight of how a living and equitable wage will affect the economic order of an organization, a just wage becomes a high sounding moralism that is impractical. A sustainable wage, then, is the organization's ability to pay wages that are sustainable for the economic health of the organization as a whole.

These principles, as well as the fundamental insight of justice, will help a manager to realize that there are at least "three bottom lines" to a just wage: needs of all employees, the different contributions of each of the employees (internal equity and external equity), and the economic order of the organization. The manager of a company will often find these principles in tension with each other and will be tempted to emphasize one or two but ignore a third. These tensions are very real and raise an obvious question for this communitarian view of wages: What happens when employers cannot pay a living wage without violating a sustainable wage? What happens when paying a living wage could lead one to bankruptcy? Within this communitarian tradition, justice is located at different levels in society. While only individuals are capable of virtue, social justice emphasizes that any individual firm's living wage can only be an *instance* of a *social* achievement founded in cooperation with other employers, employees, unions, government, and other social institutions. For, apart from a comprehensive commitment—a social commitment—to a living wage, those who decide unqualifiedly to pay living wages in highly competitive, commodity-driven, price-sensitive markets risk economic disadvantages that cannot long be borne. If the market wage in the industry is below a living wage, and there is no place to reduce labor costs, employers who decide to raise wages unilaterally will price themselves out of the market. Obviously, this constraint becomes increasingly decisive in international markets. It is here that the virtue of social justice is most appropriate—indirect employers such as the state, employer associations, unions, in collaboration with direct employers who together seek to find ways to foster conditions for people to grow.

Applications of Theory

To understand the differences between market and communitarian understandings of just wages, we need to examine a case to see how each of these views of justice will understand the determination of a just wage. Reell Precision Manufacturing is a producer of hi-tech clutches and hinges for the office machine and computer industries in St. Paul, Minnesota. The company faced the following situation in 1996: The actual market wage or "sustainable wage" for assemblers in the company was $7 per hour ($14,000 per year). In 1996, their estimate of a living wage in St. Paul was $11 per hour ($22,000 per year). The question for the management team was how to make up the difference. The $4 discrepancy between a living wage and a market wage was a tension between the desire of management to pay according to need and market reality. While the management of Reell desired to pay its employees a living wage, management was all too aware that customers would only pay for the "instrumental value" of work. If Reell would pay $11 per hour to its employees while competitors paid $7, Reell's cost disadvantage would increase their likelihood of losing customers, thus projecting the company in an uncompetitive situation.

How would the two perspectives of a just wage evaluate this case? First, both perspectives would most likely agree on the problem at Reell—namely, that low wages at Reell were merely a symptom of a much larger problem of how the company worked. When work is designed to use $7 of talent, it is difficult to pay people anything more than that amount. Prudence dictated that the living or what Reell management called the target wage could not come automatically. The reason the company called it a target wage was that it was something it worked toward. When an employee is hired with no experience and no skills, the company pays the worker the market rate ($7 per hour or whatever it is at the time) but then makes a commitment to move that employee to the target or living wage ($11 per hour) through training and skill development. So when employees learn the skills and gain experience, which Reell provides, their pay goes up accordingly.

Where the differences between the market and communitarian views come about is over why be just and where justice is located. In understanding the differences, it is important to key in on several terms utilized in their descriptions of a just wage: freedom, intention, efficiency, consequences, and relationships.

Within the market view of a just wage, this focus on intention within the communitarian view of just wages is a bit puzzling, since the location of justice is not found in intentions and internal qualities of people but in the external results of actions, and in particular, the results of what markets produce. Actually from its vantage point, the intentions of Reell management seem to reflect more of management's enlightened self-interest than any altruistic reasoning for employees. Reell was simply trying to improve the efficiencies of its assembly line, which was the basis of increased pay. Management did not raise wages until employees were able to raise their skill level that would be commensurate with market rates. What generated justice in this case was not the intentions of management but the efficiencies of a new management system and the consequences of this to generate greater wealth to pay employees according to their contribution. Attempting to locate justice in intentions and relationships misplaces the focus of management on generating greater efficiencies.

A communitarian view would respond with a similar accusation that the market view has misplaced the location of justice. The reason why intentions matter so much is that they form the character of the person, which in turn determine the nature of relationships between employer and employee. Justice is to be observed not merely in the distribution of wealth but also in regard to the kind of community of work that is established. If Reell's management was only concerned with generating greater wealth, there is a good chance they would not have developed the target wage. It was principally management's concern for employees' needs that generated such a target wage policy, not a strategic calculus for greater efficiency and wealth. This is why the communitarian view of justice insists on calling a wage a relationship and not simply an exchange. Exchanges tend to generate contracts with minimal responsibilities, not covenants, which produce strong bonds of communion. Covenants inspire collaboration, goodwill, creativity, and even sacrifice, which in most, but not all, situations will generate a more vibrant, dynamic, and, in the long run, more efficient and productive company.

The market view would respond that this communitarian view is attempting to get more out of the corporation than it can provide. Corporations are not families. They are places of exchange that need to be efficient so as to generate wealth for future survival of the company. The question of meaning and character is a noneconomic reality and belongs largely in the private or cultural domain. Business is an economic institution and its focus must be placed on increasing efficiencies and wealth creation. To begin to speak of a "community of work," formation of character and other noneconomic issues confuses the roles of business and culture.

At this point the communitarian view would point to the assumption of the market view of wages of the separability of private and public spheres of life. The communitarian view would argue that one of the reasons why the relationship of employer and employee is so important in business is of its influence on the culture and vice versa. People's private and public lives are not separable divides but are realities that are distinguishable but never divided from each other. If wages are not livable, equitable, and sustainable, they cannot bear the relationship of real community, which will negatively impact the kind of society in which we create.

Where the market and communitarian view of wages would agree is where the company's responsibilities lie in light of their virtue. Both would argue that Reell (or any firm) is not responsible in justice to pay employees in excess of a market or sustainable wage (a wage consistent with the sound financial management of the firm), even if that wage falls below a living wage. To do so would unjustly place Reell—and all the firm's employees—at risk of economic failure. In a market economy no firm can be obligated to pay without regard to labor costs' effect on its competitive position, since that would amount to the imprudent choice of self-defeating means (what often destroys justice is not prudence but a false prudence). For the communitarian perspective, Reell does have an obligation in justice to create right relationships with employees to work toward a living wage. This is why Reell can pay less than a living wage so long as it is working toward correcting the situation through some set of means such as training and skill development. From the market perspective, Reell is only obligated to move down this route if it increases efficiencies and produces greater wealth.

This argument of course can go on, but one sees the importance of the underlying assumptions of both viewpoints. For the market perspective, a wage is an exchange commensurate with the price determined by a market. A just wage is defined by the creation of efficient labor markets that generate more wealth to be distributed. The level of analysis is principally focused on the aggregate outcomes of such markets, which produces the greatest amount of wealth. For the communitarian perspective, a wage is a relationship that cannot be only determined by market price mechanisms. A just wage is principally found in the relationship between employer and employee and the bounds of communion that are created between them. The level of analysis is focused on the particular relationships generated in particular companies and whether such relationships create communities of work where people flourish.

—Michael Naughton

See also Agency, Theory of; Communitarianism; Consequentialist Ethical Systems; Executive Compensation; Incentive Compatibility; Living Wage; Prudence

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K

Kant, Immanuel (1724–1804)

Immanuel Kant was born April 22, 1724, in Konigsberg, East Prussia. (Today, Konigsberg is called Kaliningrad and is in the part of Russia that is just above Poland and split off from the main part of Russia.) Kant was one of nine children. He attended the University of Konigsberg and then for the next 15 years served as a tutor to wealthy families in East Prussia. During this time, Kant's financial resources were severely limited. Finally, in 1770 Kant was appointed Professor of Logic and Metaphysics at the University of Konigsberg. During the first 10 years of his professorship, Kant published output gave little hint of what was to come. Most of his essays were in the natural sciences. Kant made his most notable contributions after the age of 50, when he made major original contributions to epistemology and metaphysics, ethics and aesthetics, and, toward the end of his life, political philosophy.

Kant's contributions to philosophy in the traditional sense began with the publication in 1781 of his monumental *Critique of Pure Reason*. This major contribution to epistemology and metaphysics showed that knowledge was a cooperative enterprise on the part of both reason and experience. As Kant put it, concepts without percepts are empty and percepts without concepts are blind. By this he meant that the content of knowledge came from experience (percepts) but that this content had to be organized according to certain concepts. Otherwise experience would be a booming, buzzing confusion. In this way Kant showed that the rationalists and the empiricists who had been warring for over two centuries were both partly right and partly wrong. Kant also showed that at the theoretical level the traditional questions of metaphysics—are we free, is there a god, and is there a promise of immortality—cannot be answered.

For the next 17 years, Kant was unimaginably productive in terms of both the quantity and quality of his work. In ethics, his emphasis on duty and the consistent following of maxims of action have been so influential that deontology is often simply referred to as "Kantian ethics." His two most important works in ethics are *The Foundations of the Metaphysics of Morals* and the *Critique of Practical Reason*. Kant also made major contributions to aesthetic theory (*The Critique of Judgment*) and to political philosophy and the philosophy of law (*The Metaphysics of Morals Part 1*). Kant represents the classic statement of the retributive theory of punishment. One of his last works, *Perpetual Peace*, was a forward-looking proposal aimed at bringing the state of war between nations to an end. In the philosophy of religion, Kant articulated a rationalistic theology that complemented his ethical theory. Finally, Kant is identified as the classic thinker of the Enlightenment with its emphasis on universal values, cosmopolitanism, and rationality.

Since Kant never traveled far from his birthplace, spent his entire university career at the University of Konigsberg, and never married, it might appear that he led a rather dull life. However, he was a popular lecturer, was known for his charm and wit, and frequently entertained. On receiving his professorship, his financial situation improved and he was served by his loyal servant Lampe.

Kant was rather rigid in his activities. He retired promptly at 10 and Lampe awakened him each morning at 5. His walks along the riverbank were so punctual that it is said the housewives of Konigsberg set their clocks to his walk. Although Kant was slight in build and his health was considered fragile, he lived until 1804, dying just short of his 80th birthday.

—Norman E. Bowie

See also Deontological Ethical Systems; Kantian Ethics

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Kantian Ethics

Immanuel Kant (1724–1804) is arguably the greatest ethical theorist philosophy has produced. However, his writings on ethics are difficult to understand, and his ethical theory has been subject to multiple interpretations and to considerable criticism. Kant's ethics is the central theory in a branch of ethical theory known as deontology (duty-based ethics). Indeed Kant's ethics is so prominent in deontology that "Kantian ethics" and "deontology" are often treated as synonymous terms.

Goodwill

Kant begins the *Foundations of the Metaphysics of Morals* by asking what is intrinsically good, that is, what is good in and of itself rather than being good for something else. Kant considers a number of possibilities—obvious ones such as wealth and power and less obvious ones such as intelligence, wit, and other talents. All are found wanting. Why? Because they can all be misused for immoral ends. When one reflects on the matter, only goodwill passes the test of being intrinsically good.

Interpreters of Kant have often identified goodwill with good intentions and thus said that Kant's ethics is an ethics of good intentions, of doing right because it is right. On this interpretation, Kantian ethics looks like ordinary morality. If there is something in it for you, then even if your action conforms to morality, it is not really moral because it is not motivated by morality. "Honesty is the best policy" is a principle of prudence for Kant rather than a moral principle. In business ethics, behavior that contributes to the bottom line is rejected as truly moral by the person on the street. "That company is just doing good because they make money from it" is what is often said.

The problem with this interpretation is that the emphasis on intentions is too psychological. Kant is looking toward reasons rather than motivation in the psychological sense. An action is right if it is performed for the right reason and the person of goodwill is the person whose actions are based on or are in conformity with good reasons.

The Categorical Imperative: The Universal Law Formulation

To understand how goodwill reasons about a moral issue, one must understand the role of maxims and the distinction between hypothetical and categorical imperatives. Although it is tempting to say that Kant's ethics evaluates the ethics of actions, that is not strictly correct. What need to be evaluated are the maxims on which one acts. Some maxims are hypothetical because they are means to an end. "If you want an A, you need to study" and "If you want to have a good reputation, you cannot overcharge a child" are examples of hypothetical imperatives. If you do not care about getting an A or about having a good reputation, then there is no need to study or avoid overcharging the child. On the other hand, a categorical imperative is one that binds you no matter what your other goals or purposes are. A categorical imperative obligates you with no ifs, ands, or buts. Kant's first formulation of the categorical imperative presents this demand: Act only according to that maxim by which you can at the same time will that it should become a universal law.

In explaining this formulation, the imperative resembles the formal principles of reasoning, and thus Kant's ethics is sometimes called formalistic. It is evident that if something is to count as a reason for you, it is to count as a reason for anyone like you in relevantly similar circumstances. Thus, to use one of Kant's examples, if, whenever you are in grave financial difficulty, you have as your maxim to promise to repay a loan with no intention of doing so, you must be willing to allow everyone to act on that maxim. However, such a maxim could not become a universal law because if it did no one would make a promise. Such a maxim would be self-defeating. Indeed such a maxim would be self-contradictory because it would imply that you endorse a world with promises and that you endorse a world without promises. Many of the actions that we learn as young children are wrong are just those actions whose maxims could not be universalized without being self-defeating. Stealing is wrong because if a maxim permitted stealing to be a universal law, then it would undermine private property on which stealing depends. A universal maxim that permits stealing is self-defeating. So is a universal maxim that permits cheating. Thus Kant has shown the reason why it is wrong to lie, cheat, and steal. Universalized maxims permitting these activities would be self-defeating and thus irrational.

Maxims that permit an individual to lie, steal, or cheat when universalized create maxims that are contradictory in the logical sense. Such maxims are conceptually contradictory because they would assert something like "It is permissible for me to steal" and "It is not permissible for me to steal." However, Kant also believes that the categorical imperative requires that we help others and develop our talents. Kant believed there is nothing conceptually contradictory in denying that we ought to help others, but he believed that a denial of beneficence results in a contradiction in the will. Kant says that the reason there would be a contradiction in the will is because situations can arise in which one would need the love and sympathy of others but could not ask for it, since one had denied beneficence (love and sympathy) to others. Although some have rejected Kant's arguments here, contemporary Kantian ethicists have interpreted Kant in ways that make his argument quite plausible.

Critics of Kant have focused on the difficulty of providing the appropriate maxim to see if it passes the test of the categorical imperative. Consider the act of lying. If the maxim is very general, such as, "It is OK to lie," then lying would be absolutely prohibited under all circumstances. Kant actually took an absolutist perspective with respect to lying and argued that lying was always wrong under all circumstances. That is why some have criticized Kant for having an ethic of absolute rules. But most Kantians would agree that lying is morally permitted in certain circumstances, to save a life, for example. Of course the maxim could be amended to say, "One should not lie except to save a life." That maxim can become a universal law of nature. However, if one allows maxims that are highly specific, then they could be made so specific that they would just apply to you or to you and a select group and the whole force of the exercise of seeing if maxims could become universal laws would be defeated. The proper formulation of maxims remains one of the active areas of debate in Kantian ethics.

Kant's Theory of Freedom

Kant's ethics is an ethics of respect for persons. Why should persons be respected? Kant noted that persons were different from everything else in that they were the only things on earth that could act from a law of their own making. Or to put it in other terms, persons are the only things on earth that can act on the basis of universal laws and thus are the only things on earth that can have goodwill. In other words, persons are free. Indeed, human freedom is the ground of Kant's ethics.

It is important to note that Kant's theory of freedom has two components. The first one is negatively free in that one is not simply a cog in the causal chain in nature. But the second is positively free if one can act on laws of one's own. To put it another way, one is positively free if one can act on the basis of categorical imperatives. It is tempting to say that either we act as part of a causal chain on the basis of sufficient causes or we act from laws of our own making. Kant argued that for free actions, there are both causal explanations and rational (law-giving) actions. How is that possible? Early interpreters of Kant defended a two-world explanation where we were subject to the empirical world of cause and effect and an intelligible world of freedom. But many found the two-world scenario as creating an unbridgeable dualism. Contemporary Kant scholars speak of two standpoints rather than two worlds. Whether the two-standpoint perspective resolves the issues depends, in large part, on whether one is a compatibalist with respect to free will and determinism. Compatibalists believe that free will is possible in a deterministic world.

Kant himself argued that it was impossible to have sense experience knowledge that we are free, but as rational and ethical beings we had to presuppose that we were free. Of necessity we think we are rational and moral (capable of following laws of our own making including the categorical imperative). This is Kant's transcendental argument for freedom. The fact that we all must see ourselves as free rational moral creatures gives us a dignity that is beyond price.

The Categorical Imperative: The Respect for Persons Formulation

Kant's ethics can fairly be characterized as an ethics of respect. Kant believed that each person recognizes that he or she is free in the full sense and that he or she is bound by the moral law. This recognition provides the basis for each person's claim to respect. Applying the universal law test here, Kant argues that if I make a claim for respect, then in turn I must honor the same claim made by every other person. After all, each person, Kant believed, recognized his or her freedom and obligation to the moral law. He thought that people should always treat others and themselves with respect.

In nearly all personal interactions, especially in business relationships, each person gains something from the relationship. The fact that another person is providing you with something you want does not automatically mean that you are using another as a means in a way that is morally offensive. Kant's position is that you cannot use another as a means *merely*. Thus, loving relationships and business relationships pass the moral test so long as one is not using another solely as a means.

It is this formulation of the categorical imperative that is most often appealed to in applied ethics. In business ethics, for example, Kantian scholars try to determine what respecting other stakeholders requires of managers or what the business firm should look like if it were organized along Kantian lines.

The Categorical Imperative: The Kingdom of Ends Formulation

Although many interpret Kant's ethics as an individualist ethics, the categorical imperative applies to human communities as well. Since institutions are composed of persons, all persons in the institution must be treated with respect; they must be seen as having dignity. In a business situation this means that people cannot just be treated on a par with capital or machinery. Kant's term for these communities or institutions was *kingdoms of ends*. In such communities, the categorical imperative insists that people act as if they were legislating members in the universal kingdom of ends. What rules should govern a kingdom of persons? Only those that can be universalized should. By requiring universalization, one is sovereign because in some sense one makes the rule, and of course since it is universalized one is also subject to the rule. In other words a moral community is one where the obligatory nature of the first two formulations of the categorical imperative is recognized.

One can argue that Kant's ethics is defined by the categorical imperative. Who is the person of goodwill? The person who acts on maxims that are based on the obligatory nature of the categorical imperative.

Perfect and Imperfect Duties

Kant distinguished between obligations that always bind us such as "Don't lie" and "Don't cheat" and duties such as the duty of beneficence, which bind us only to a certain extent. The former duties are perfect duties, the latter are imperfect duties. What does it mean to say that imperfect duties bind only to a certain extent? Consider the imperfect duty of beneficence. Each of us is obligated to help another, but no one is obligated to always help others. In other words, we are not obligated to help everyone who needs aid whenever they need it and we are in a position to do so. That would make morality too demanding. But how beneficent are we required to be? Kant provided few clues to help in answering that question, and various answers have been proposed by contemporary Kantian ethicists.

Duties to Oneself and Duties to Others

Some ethical theories do not emphasize duties to ourselves. However, Kantian ethics certainly does. There is an absolute prohibition (duty) against suicide. There is an imperfect duty to develop one's talents. Servility is a moral fault because it undermines one's claim to respect.

Duties That Can and Cannot Be Enforced by Law

In the *Metaphysics of Morals*, Kant turned his attention to more specific moral duties. He distinguished those that could be enforced by law (externally required) from those that could not be so enforced and thus were enforced internally. In discussing the former, Kant developed his theory of law, property, and penal justice. In that first section of the *Metaphysics of Morals* known as the "Metaphysical Principles of Right," Kant defends an absolute duty to obey the sovereign and a retributivist theory of punishment that included a strong endorsement of capital punishment. Many contemporary Kantian ethicists are somewhat embarrassed by these positions and have attempted to develop a Kantian position that would provide for civil disobedience or would reject capital punishment and other features of a harsh retributivism.

The second section of the *Metaphysics of Morals* is called the "Metaphysical Principles of Virtue," which describes the duties that cannot be enforced by law. For Kant, virtues are those character traits that enable us to obey the demands of the categorical imperative in the face of obstacles that stand in the way of our obedience, while vices are those character traits that indicate a weakness in the face of obstacles that stand in the way of obedience. The key to virtuous behavior is control over oneself, which again shows the centrality of freedom in Kant's ethical theory. In addition to freedom, the concept of respect for persons is the guiding force in developing a set of specific duties of virtue. This can be seen, for example, in Kant's discussion of concepts like servility.

Criticisms of Kantian Ethics

Despite the great influence of Kant, a number of criticisms have been leveled against his views. The difficulties in formulating the appropriate maxim as well as determining just what is demanded by imperfect duties have already been noted. It is argued that Kant emphasizes reason at the expense of emotions or the moral sentiments of sympathy and caring. Indeed, if someone is beneficent out of the emotion of caring, Kant would not consider the act of caring to be truly moral. Some critics see the problem as Kant's overemphasis on duty. People may do the right thing for a variety of reasons. Why should the presence of prudence and sympathy eliminate the morality of the action as Kant seems to say?

Others have argued that Kant does not say enough about the virtues. Of particular importance is the criticism that Kant misunderstands and does not give sufficient room for our particular obligations—that is, obligations to friends and family. Some of the harshest critics say that for Kant, the interests of your spouse or closest friend are no more significant than the interests of a stranger. After all, each is a person with equal moral worth, so how could Kant justify giving special treatment to a friend? In business relationships, it seems that loyalty might not be permitted because it requires treating some relationships as special. Kant's ethics is an ethic of impartiality, but doesn't morality sometimes at least require that we ought not be impartial?

Contemporary Responses

These criticisms have been carefully examined and responded to by a score of contemporary ethicists. There is consensus that Kant's ethics is not a system of absolute moral rules and that Kant is not a rationalist in the sense of determining our duties on the basis of rational insight. Kant's ethics does allow facts of human nature to play a role in ethical judgments.

Other criticisms have forced some amendments to Kant's ethical thought. Some contemporary Kantian ethicists have supplemented moral decision making by the categorical imperative with various theories of moral judgment or by introducing rules of moral salience. Some Kantians have argued that the mere presence of emotions like sympathy or even prudential reasons do not by themselves eliminate the morality of an action so long as the motive of duty is sufficient for the action to be done. For example, particular relationships might be justified by universalizing them. In other words, maxims where friends or family may be given preferential treatment may be universalized and be instances of respecting the humanity in a person. In this way contemporary Kantian ethicists have tried to find a place for particularity and the moral emotions while still being true to the central ideas of Kant's ethics.

—Norman E. Bowie

See also Autonomy; Duty; Ethics, Theories of; Kant, Immanuel; Neo-Kantian Ethics; Self-Respect

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KEIRETSU

The Japanese word *keiretsu*, which literally means "series," denotes a set of companies that are loosely lumped together by cross-shareholding and/or long-term transactional relationships such as assembler-supplier relationships. *Keiretsu* can best be understood as an intricate web of economic relationships that links banks, manufacturers, suppliers, and distributors.

There are two types of *keiretsu*: the horizontal and vertical types. The big, leading firms that form the core of a *keiretsu* are horizontally linked by capital and transactional relationships, and each core company ties up with many subcontracting firms, which are in vertical relationships with the core companies. The firms that are vertically connected with the core companies through subcontracting contracts and that can obtain financial and technological support from the parent company are usually termed as affiliated subcontracting companies.

The "Big Six" enterprise complex (Mitsui, Mitsubishi, Sumitomo, Fuyo, Sanwa, and Dai-ichi Kangyo Group), which are also known as the Kigyo Group, constitute a horizontal *keiretsu*. The Big Six enterprises have different historical origins. The former three were established shortly after World War II, following the American occupation authorities' dissolution of the family-owned conglomerates known as *zaibatsu*. The latter three were organized around the newly developing big banks in the 1950s and 1960s: Fuji Bank, Sanwa Bank, and Dai-ichi Kangyo Bank. In addition to the Big Six, Toyota, Hitachi, Toshiba, and Sony form their own *keiretsu*, termed the Independent Corporate Group.

A feature of the Big Six *keiretsu* is that it has within itself a central bank, a general trading company, an insurance company, an iron and steel company, and a chemical company. As an example, consider the Mitsui Group, which includes Sakura Bank as its main bank, Mitsui Trust & Banking, Mitsui Mutual Life, Mitsui Marine & Fire, Mitsui Bussan, Japan Steel Works, and Mitsui Toatsu Chemicals. Each of the core firms has subcontracting companies under its control, and the subcontracting companies on their part are forced into competition with each other to obtain better contracts from the parent firm.

Close capital ties, long-term contracts, and financial and technological support are considered to be the advantages of the foundation of a *keiretsu*. According to a recent economic theory, *keiretsu* can contribute toward economizing transaction costs; therefore, the structure has economic rationality. However, the existence of *keiretsu* is said to be representative of the closed system of the Japanese market for foreign investors and firms, and it has hampered free trade. The other problem with *keiretsu* is that many affiliated subcontracting firms are "locked" or remain "captive" in long-term transactional relationships with the core companies, making it easy for the core companies to subordinate and control the subcontracting firms.

In the 1990s, during the decline of the Japanese stock market, stable shareholding among the core companies began to decline. As a result, the *keiretsu* were in the process of dissolution and regrouping. For example, Mitsui Bank and Sumitomo Bank merged to form Mitsui-Sumitomo Bank in 2001. The subcontracting companies, on their part, have begun to be more market orientated and now tend to move away from *keiretsu* relationships.

—Keigo Tajima

See also *Chaebol*; Contracts; Deregulation; Economic Efficiency; Economic Rationality; Mergers, Acquisitions, and Takeovers; Pareto Efficiency; Transaction Costs; Unfair Competition; *Zaibatsu*

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Kohlberg, Lawrence (1927–1987)

Lawrence Kohlberg, a psychologist and a professor at Harvard University, investigated the individual's moral reasoning, which led to the creation of his theory of moral development. Born in Bronxville, New York, Kohlberg began his career as a developmental psychologist in the early 1970s before moving to the field of moral education where he fashioned his well-known stages of moral development, which traced an individual's progression of moral reasoning across identifiable, universal moral perspectives. Kohlberg died under suspicious circumstances, probably suicide, after contracting a parasitic infection, which caused him to suffer for 16 years.

Kohlberg's work was influenced primarily by Jean Piaget, a cognitive developmentalist. Based on a long-term study conducted at Harvard's Center for Moral Education, Kohlberg recorded responses provided by his male subjects, beginning at age 7 through adulthood, to hypothetical dilemmas that required the subject to make a moral choice. However, Kohlberg was not concerned primarily with the subject's moral choice but with the moral reasoning provided in support of that choice. Based on his results, Kohlberg concluded that an individual progresses sequentially through six identifiable, universal stages of moral reasoning, which could be more generally classified into three levels.

At the Preconventional Level (Stages 1 and 2), an individual understands "right" and "wrong" in terms of the personal consequences involved, such as punishment, rewards, or an exchange of favors, or focuses on the imposition of physical power by authority. Avoidance of punishment and unquestioning deference to power are highly valued at this level. Reasoning at the Conventional Level (Stages 3 and 4) emphasizes performing good or right roles, maintaining traditional or acceptable order as determined by a group or society, or meeting others' expectations. Adherence to the Golden Rule or following the Ten Commandments is characteristic of this reasoning level. In the Postconventional Level (Stages 5 and 6), the individual defines moral values and principles apart from established moral authority and relies on self-chosen principles, from a set of universally acceptable principles, to guide reasoning.

Carol Gilligan, Kohlberg's student and later colleague, raised objections to Kohlberg's work, which used all male subjects. Gilligan argued that Kohlberg's model espoused a "theory of justice," a predominantly masculine cognitive process based on adherence to ethical principles. Gilligan advocated a "theory of care," which is often found among females and emphasizes the maintenance of relationships. Kohlberg and his associates responded to their major critics by addressing issues of stage sequencing, subjectivity in the moral reasoning scoring method, gender bias, or the lack of cross-cultural universality. In each of these responses, empirical support was offered in support for Kohlberg's theory and stages of moral reasoning, resulting in the continued use of his theory by developmental psychologists years later.

—James Weber

See also Cognitive Moral Development; Ethics of Care

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Kyoto Protocol

The Kyoto Protocol is an international agreement to reduce greenhouse gas emissions by establishing reduction targets for participating nations. It is an amendment to the United Nations Framework Convention on Climate Change and was signed in Kyoto, Japan, in December 1997. The Protocol is based on the belief that increases in carbon dioxide and other greenhouse gases are a major cause of global warming, a position supported by the Intergovernmental Panel on Climate Change. It is modeled in many respects on the Montreal Protocol, an international agreement that focuses on the reduction of ozone-depleting substances to restore the planet's ozone layer, which is widely regarded as a success. By contrast, the Kyoto Protocol was off to a slower start in achieving significant progress in meeting greenhouse gas reduction targets.

The Kyoto Protocol went into effect in February 2005, 90 days after the Russian Federation signed the agreement, thus reaching the threshold of participation to initiate its provisions. The Protocol calls for the reduction of the six primary greenhouse gases: carbon dioxide, methane, nitrous oxide, hydrofluorocarbons, perfluorocarbons, and sulfur hexafluoride. The most significant human-caused sources of greenhouse gas emissions are use of fossil fuels (especially petroleum and coal), deforestation, and use of chlorofluorocarbons.

The Kyoto Protocol separates countries into two categories: Annex 1 and non-Annex 1. Annex 1 countries include industrialized countries that belonged to the Organisation for Economic Co-operation and Development in 1992 and the so-called economies in transition, which include the Russian Federation and a number of central and eastern European countries. Annex 1 signatories produced most greenhouse gases and agreed to reduce emissions collectively by 5.2% below the levels occurring in 1990 by deadlines between 2008 and 2012. Non-Annex 1 countries are developing countries, such as Brazil, China, and India, which have signed the Protocol but do not have targets for controlling the growth of greenhouse gas emissions yet.

Annex 1 countries committed to specific reduction targets in the Protocol. For example, the European Union (EU) agreed to use a joint approach by its then 15 members to meet an 8% overall reduction in emissions. The United States offered to meet a 7% reduction over 1990 emissions levels, while Canada and Japan agreed to a 6% reduction. The Russian Federation agreed to a 0% reduction, meaning that it would not exceed its 1990 emission levels. Several countries were permitted small increases in emissions to allow for modest growth, for example, Norway at 1% and Australia at 8% over 1990 levels.

Countries may meet their targets within their borders in many ways, such as by improving energy efficiency, by shifting energy sources away from heavy reliance on fossil fuels, and by planting forests. The Kyoto Protocol also encourages the use of three market-based "flexible mechanisms" to allow Annex 1 countries to meet their targets at lower costs. These flexible approaches are the clean development mechanism, joint implementation, and emissions trading. The clean development mechanism allows Annex 1 countries to implement emission reduction projects in developing countries in return for certified emission reductions. Joint implementation allows an Annex 1 country to aid in an emission reduction project in another Annex 1 country, while counting the emission reduction credits toward its own country. Finally, emissions trading allows for the trade or sale of emission reduction credits between Annex 1 countries.

A good example of joint implementation is occurring within the EU. In 2002 when the EU ratified the Protocol, the then 15 member countries decided on the goals to reach the 8% overall reduction from 1990 emission levels. Some member countries accepted larger reductions, such as Germany and Denmark, which are committing to a 21% reduction, while others were permitted to increase their emissions but at a lower rate than what would have occurred without the Protocol, such as Greece limited to 125% and Spain to 115% of 1990 levels.

Critics of the Kyoto Protocol focus on several issues. Early criticisms were based on lack of sufficient scientific evidence on which to establish the phenomenon of global warming and the role of human activity in influencing climate. Another criticism is the failure to establish targets for the developing countries whose economic growth was likely to trigger a large increase in greenhouse gases. A third issue was the high cost of limiting fossil fuel use and taking other steps to reduce emissions. Thus, two large producers of greenhouse gas emissions, the United States and Australia, decided not to ratify the Kyoto Protocol after initially signing it. These countries represent one third of the industrialized world's greenhouse gas emissions. The United States instead is developing its own approach of setting voluntary greenhouse intensity reduction goals, which would reduce emissions per unit of overall economic output but are likely to increase emissions as a whole. Australia chose not to ratify the Protocol because it did not include clear targets for developing countries and because the United States would not agree to comply. It argued that only 1% of greenhouse gas emissions would be controlled unless all the major emitting countries committed to meeting Kyoto targets. Nonetheless, Australia indicated a commitment to meet its Kyoto targets despite abstaining from ratification.

In 2006, on the 1-year anniversary of the Kyoto Protocol coming into effect, progress in meeting the 2008 to 2012 targets was judged to be slow, and concerns were expressed about the commitment of countries to meet their targets. The EU's carbon trading program had been operating for 1 year with mandatory participation by companies in energy-intensive industries, such as electricity generation, iron and steel production, and manufacturing of glass, pulp and paper, and cement, but the impacts of the emissions trading program were still to be measured. The European Environmental Agency predicted that only the United Kingdom and Sweden would be able to meet their Kyoto targets by the 2008 to 2012 deadline through current efforts, while other EU countries would need added projects and policies to meet their targets. Many other participating industrialized countries were also behind schedule in meeting their targets.

Impacts on business are likely to be significant as they adapt to reducing greenhouse gas emissions. Emitters in Annex 1 countries are dealing with mandated participation in conservation projects, carbon trading, and clean development programs while companies outside of Annex 1 have to decide whether to engage in voluntary reduction efforts, whether government-sponsored or oriented toward satisfying other stakeholder concerns. Companies with "green" technologies, such as photovoltaic solar panels or wind energy systems, are in a favorable position to increase revenues from higher demand for clean energy alternatives.

Performance in implementing the Kyoto Protocol was significantly lower in its first 10 years compared with the 1987 Montreal Protocol, on which it was modeled. Ratification of the Montreal Protocol by participating countries occurred much more rapidly, and by 1997 it was ahead of meeting its goals. The Kyoto Protocol was ratified much more slowly by participating countries, and two of the largest producers of greenhouse gas emissions, the United States and Australia, have still not ratified the Protocol although they express commitment to the goals of greenhouse gas emission reduction. Experts predict that the 2008 to 2012 goals will not be met by all industrialized nations without a much stronger commitment by governments, businesses, and consumers.

Explanations for these differences between the Montreal and Kyoto Protocols focus on the nature of the problem, the costs of achieving emission reduction targets, and the number of actors that would be significantly affected. Global warming is a much more contentious and difficult problem to address than ozone depletion because of the greater complexity and uncertainty in scientific evidence and because energy is central to economic welfare and growth compared with the relatively narrow uses of ozone-depleting substances. Second, the aggregate costs to meet Kyoto targets are high even with market-based flexible mechanisms such as emissions trading compared with compliance costs for phasing out ozone-depleting substances when substitutes were easily identified, produced, and distributed. Finally, ozone-depleting substances were largely produced by a few large corporations in a few industrialized countries, so cooperation and monitoring were more easily achieved. By contrast, the use of fossil fuels and deforestation occur virtually everywhere on the planet, and it is much more difficult to implement agreements to achieve a collective good for large numbers.

—Jeanne M. Logsdon and Phoenix Forsythe

See also Commons, The; Emissions Trading; Externalities; Greenhouse Effect; Montreal Protocol; Pollution Externalities, Socially Efficient Regulation of

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LABOR UNIONS

A labor union is an association of employees that advances member interests through collective bargaining with an employer. Areas of negotiation typically include wages, benefits, work rules, and other conditions of employment, such as hiring, discipline, and termination of employees.

A significant power imbalance between employers and employees during the early stages of the Industrial Revolution (1760–1830) led to the formation of unions. Employers took advantage of a labor glut caused by large numbers of agriculture workers who, searching for a better life, flooded cities for nonskilled factory jobs. The workers hoped for decent wages, job security, and respect for their labor. Instead, managers dictated the conditions of work based on their own interests and paid very low wages to those willing to work long hours in unhealthy work environments. There was always someone willing to do the work.

Labor unions organized workers based on their common interests. Unions defended workers against abusive employers and negotiated wages on their behalf. A union organizer, often risking his or her own employment at the company, inspired unfairly treated employees to collectively withhold their labor in an attempt to financially cripple the business. If replacement workers, referred to as "scabs," did not cross the picket line (see the University of Bridgeport case discussed below), then the employer would have to negotiate with the union for better wages, benefits, and working conditions. Unions collected dues from members to pay for safety net features, such as funds for striking families, and administrative expenses. Despite current legal protections, certifying a union continues to require courage by employees leading the unionizing effort. Labor union accomplishments include higher wages, shorter hours, prohibitions on child labor, grievance procedures, and worker's compensation.

This entry describes the process of certifying a union and presents empirical research examining the impact of unionization. Next, the roots of "class conflict" analysis between employers and labor is explored in the writings of Adam Smith, particularly his understanding of the wage issue. This is followed by a summary of labor union history in the United States and other selected nations, the problem of union corruption (particularly in the Teamsters union), a profile of the union organizer Cesar Chavez, and the ethics of union management tactics. The entry concludes with a survey of the current status of unions around the world and a brief discussion on the future of unions.

The Process of Certifying a Union

In the United States, workers have the legal right to be represented by a union. Prior to 1935, employers could refuse to negotiate with a union. The National Labor Relations Act of 1935 codified regulations governing the process of certifying a union. These regulations have been modified by subsequent legislation, most notably by the Landrum-Griffin Act of 1959.

Unions are typically initiated by an employee responding to a workplace injustice or by an external union recruiter. The process begins with union organizers clearly defining the bargaining unit in terms of work commonality. Unions represent a particular job classification rather than everyone employed by a particular business. For instance, airplane pilots and airplane maintenance employees belong to two separate unions based on the type of work they perform. For the certification process to continue, 30% of the targeted employees must sign a confidential authorization card or petition requesting union representation.

Unions often recommend that at least 70% of the employees sign these cards as a sign of solidarity before incurring the financial and psychological costs associated with certifying a union. It takes tremendous courage for an employee to lead a union organizing effort. Whereas forming a union may give hope to some employees, other employees may not welcome an external third party participating in work-related decisions, thereby creating dissension among coworkers and conflicting loyalties.

Next, the union organizers present the authorization cards to the National Labor Relations Board (NLRB), which then notifies the employer. The employer can either accept the union as the employee representative based on the confidentially signed authorization cards or request that an election be held under the auspices of the NLRB. Typically, employers require an NLRB-sanctioned election. After the NLRB establishes an election date, the union and the employer can lobby employees to vote for or against unionization.

There are strict rules governing what employers can and cannot do during the preelection time period. For instance, employers cannot threaten to terminate the union organizers nor promise employees incentives to vote against the union. Employees vote by secret ballot on the established date. If more than half the employees in the proposed bargaining unit vote in favor of unionization, the NLRB certifies the union. Following certification, the employer and the union must negotiate with each other in good faith. Violations of these rules can be submitted by either party to the NLRB for a hearing.

The Impact of Unions: Empirical Evidence

A significant amount of research has been conducted comparing attributes between union and nonunion organizations. In their classic book *What Do Unions Do?*, Richard Freeman and James Medoff reviewed the empirical research on the impact of unionization. The findings can be categorized in terms of impacts on wages and benefits, governance, employee turnover and layoffs, and productivity.

In comparison with nonunion facilities, unionized facilities have the following impacts:

- *Wages and benefits impacts*
  - Higher employee wages, particularly for less educated, younger, and more junior employees
  - Higher fringe benefits, such as pensions and life, accident, and health insurance
  - More wage equality by increasing blue-collar earnings relative to the higher white-collar earnings
- *Governance impacts*
  - Less decision-making flexibility for managers due to contracted work rules
  - Fewer subjective and arbitrary management decisions due to documentation requirements
  - Greater procedural protections for employees, particularly those with high levels of seniority
  - Greater employee voice in determining work rules and other conditions of employment
- *Employee turnover and layoff impacts*
  - Less turnover
  - Greater employee protection against job loss
  - Greater likelihood of using temporary, rather than permanent, layoffs during economic downturns
  - Fewer wage cuts during economic downturns
- *Productivity impacts*
  - Higher levels of productivity

The higher levels of productivity associated with union facilities are attributed to a variety of factors. Managers often complain about the restrictive rules and lack of flexibility in managing a unionized workforce. In some instances, local unions have falsified the number of hours union employees work, the number of union employees working, and the job qualifications of union employees, which create productivity problems. Some local unions also refuse to perform any tasks that are not clearly stated in their contracts. But research has found that organizations with unions attract more productive employees because of higher wages and better job security. In addition, the employee "voice" provided by unions results in more efficient work processes and resolutions to employee grievances.

Owner Objections

Are the higher wages and benefits associated with unionization good or bad? The answer often depends on one's point of reference. Neoclassical economists maintain that unions artificially increase wages, which in turn leads to inflation. Higher labor costs reduce the amount of money available for other purposes, such as profit, advertising, or capital expenditures. Higher labor costs also put firms at a competitive disadvantage, motivating them to relocate to nonunion regions of the United States or to developing nations with less stringent labor laws.

According to classical economic theory, private property rights are at the foundation of a free market economy. Owners, and their management representatives, have the legal right to determine the rules and regulations governing workplace activities as long as they do not conflict with existing laws. Unions bring into the workplace a third party that creates dual loyalties, where both the employer and the union compete for the employee's loyalty. Owners complain that unions are insensitive to the impact of wage increases on the organization's existence.

But from a worker's perspective, higher wages mean more disposable income. Unions represent the interests of workers in this wage conflict between competing class interests—a conflict noted in the original conceptualization of capitalism by Adam Smith.

Unequal Bargaining Positions in Adam Smith's *Wealth of Nations*

Throughout economic history, the issue of employee wages has been framed in terms of a zero-sum game. In *The Wealth of Nations*, the Scottish moral philosopher and economist Adam Smith writes admirably about the many virtues of an economic system that Karl Marx would later refer to as capitalism. Smith argues that individuals should be extended liberty to pursue their own interests in economic matters, free of government dictates and impositions that restrict economic behavior. Self-interested individuals will pursue economic activities that benefit their own economic well-being, which, coincidentally, also increases a nation's overall wealth. The pursuit of economic interest, Smith argues, typically occurs within a moral framework because individuals are naturally restrained by a sense of justice and by their conscience. When these moral restraints break down and harms are generated, then a strong system of justice must take corrective action.

Smith distinguishes between self-interest and selfishness. Self-interested individuals take into account the interests of others. Selfish people care about their own interests to the exclusion of others. In the opening sentence of *The Theory of Moral Sentiments*, his treatise on ethics, Smith claims that no matter how selfish people are assumed to be, they are guided by some principles that make them interested in the well-being of others. People are trained by parents, teachers, and friends to be both other-regarding and self-interested, but not selfish. Looking after your own welfare relative to others is a virtue, not a vice. Whenever selfishness arises, it is discouraged.

Writing within the economic context of the 1700s, Smith discouraged employers from misusing their economic liberty when determining employee wages. Smith observed that in many circumstances owners and employees negotiate wages. These two parties have competing interests. Employees naturally form coalitions among themselves to request high wages. Owners naturally form coalitions among themselves to offer low wages. Being fewer in number, owners can remain unified more easily and force compliance on employees who need wages to pay for that day's food. According to Smith, owners often outlast striking workers because they, unlike the striking workers, have accumulated stocks and savings to draw on.

Smith points out that this power imbalance is codified in law. Great Britain's parliament passed laws prohibiting employees from conspiring to raise wages but there were no equivalent laws against owners conspiring to lower wages. This was to be expected because the members of Parliament had greater affinity and interaction with manufacturers and landlords, sharing common interests and backgrounds. Members of Parliament were also recipients of gifts and privileged stock from business owners.

Given all these negotiation advantages, Smith notes, some owners pay subsistence wages, insufficient money for the purchase of food and shelter. This is shortsighted and selfish. Smith appeals to the owners' moral sentiments, including their self-interests, not to abuse their economic power. Well-fed and motivated employees work better than those who are frequently sick and disheartened. Smith reasons that workers must earn a wage sufficient to sustain themselves and their families. Otherwise, they will be unable to raise the next generation of workers.

But some employers were either unmoved by, or ignorant of, Smith's moral arguments and took advantage of their unequal bargaining power. As a result, the natural tendency of workers to form coalitions for the purpose of increasing wages evolved into labor unions.

The Growth of Unions in the United States

Labor unions are an equalizing force, leveling the playing field between owners and workers. They evolved out of the medieval guild system and industrial mutual aid societies that assisted workers based on their common interests. The unions counteracted the strong coalition of politicians, judges, and business owners, who feared that higher wages would threaten the profitability and competitiveness of local businesses.

The unequal power positions between owners and laborers accompanied the arrival of European settlers to what became the United States and was evidenced in rules and regulations governing work relations. The early laborers consisted of four classes of people: indentured servants, criminals with minor offenses, kidnapped peasant children, and African slaves. White servants and black slaves who attempted to run away from abusive employers were whipped and branded with the letter "R" for runaway. A Maryland slave owner was acquitted of murder in 1656 after he had killed a slave by pouring hot lead over him.

A free laboring class emerged in the port cities of Boston, Philadelphia, and New York. Northern merchants preferred to employ freemen rather than slaves and indentured servants because freemen did not have to be housed, fed, or sheltered. English laws that placed limits on maximum but not minimum wages were adopted in the British colonies. At the time of the Revolutionary War, approximately 75% of the three million colonists were, or had been, indentured servants, and 16% were African slaves.

The first recorded strikes in the colonies were conducted by groups of journeymen tailors in New York City and shoemakers, printers, and carpenters in Philadelphia. In 1786, Philadelphia printers conducted the first successful strike for increased wages. Six years later Philadelphia shoemakers formed the first local union. But in 1805, a jury composed of merchants found eight shoemakers guilty of engaging in a criminal conspiracy to raise wages. The merchants feared that the higher wages would force businesses to abandon Philadelphia for another city. Persecution against unions drove organizing efforts underground, forcing many of them to become secret societies.

The Industrial Revolution reached the United States from Great Britain in the early 1800s, and the first factory appeared in Waltham, Massachusetts, in 1815. The workforce consisted of newly arriving immigrants, including seven boys and two girls under the age of 12, who worked from 5 o'clock in the morning to 7 o'clock at night. In addition to long hours, features of factory life included low wages, poor ventilation, payment in scrip redeemable only at a high-priced factory store, girls living in boardinghouses leased by the company and other workers housed in crime-ridden slum tenements with high mortality rates, and a severe fine system for the purpose of maintaining discipline.

The formation of labor unions and obtaining worker rights were hindered by strong political opposition. Throughout the 1800s, business representatives attended local, state, and national political conventions and meetings with bags of cash available to those who pledged to vote for their preferred candidates or probusiness legislation. In 1840, Philadelphia strikers won the right to work only 10 hours a day; this became the standard for federal employees. But 40 years later, approximately 80% of all laborers were still working a minimum, rather than a maximum, of 10 hours a day.

Some union organizers were inspired by the revolutionary thoughts of Karl Marx and Friedrich Engels, who wrote in response to the inhumane working conditions they documented in Western Europe. Marx and Engels argued that owners of the means of production stole a portion of wages from workers, calling it surplus value, or profit. In the *Communist Manifesto,* published in 1848, Marx and Engels declared that the workers of the world should unite against their oppressor, the greedy capitalist, and take ownership of the means of production.

Union leader Samuel Gompers opposed the affiliation of the union movement to secure worker rights in the United States with a revolutionary political party, or any political party for that matter. He also opposed violent unions, such as the secret society of immigrant Irish mine workers, known as the Molly Maguires, that intimidated and killed unscrupulous mine owners and the police who protected their property rights. Following a national uprising of railroad workers in 1877, Gompers helped found the Federation of Organized Trades and Labor Unions to unite independent labor unions, which in 1886 became the American Federation of Labor (AFL). On May 1, 1886, unions across the nation declared a strike in support of an 8-hour workday. Proponents maintained that a day should be equally divided into three parts: 8 hours for work, 8 hours for personal interests, and 8 hours for rest. More than 300,000 people participated in the strike. In a rally at Chicago's Haymarket Square, anarchists led protestors in a confrontation against police. A bomb blew up, shots were fired, and police and civilians were killed, leading to massive rioting and more strikes.

Some business leaders, such as Andrew Carnegie, had conflicting feelings about unions. In response to the growing union movement, Carnegie wrote that trade unions, on the whole, were good for both laborers and business owners. He argued that salaried managers, representing their own interests rather than the interests of owners or laborers, were the source of the problem. Carnegie recommended that wages be directly linked to the price of the product or service. He favored the 8-hour workday only if it were widely adopted, so that everyone competed based on the same rules.

At the same time, Carnegie attempted to break the Steel Workers union, which represented employees at his Homestead, Pennsylvania, steel mill, in 1892. Management had unilaterally cut wages and locked out the union. Guards from the Pinkerton Detective Agency were hired to protect the plant against union demonstrators. The union rioted and occupied the town. The governor called in the militia to restore order. In the ensuing battle, 14 people were killed and 163 wounded. Carnegie reopened the plant as a nonunion facility.

In the late 1800s and early 1900s, union leaders more readily identified themselves with the anarchists, socialists, and communists who believed that capitalism was inherently unethical and cruel toward laborers. In response to inhumane working conditions and union strikes, Congress created the Department of Labor in 1913. William B. Wilson, the first secretary of labor, began working in the coal mines at the age of 9 and had been both an officer of the United Mine Workers and a congressman.

At the onset of the Great Depression, 7% of all employees were union members. Union membership grew in response to these economic hardships, forcing political leaders and President Franklin Roosevelt to develop a new set of laws governing labor relations. The passage of the National Labor Relations Act of 1935 legally obligated employers to negotiate with duly elected unions. Workers now had a legal right to collective bargaining.

The Taft-Hartley Act of 1947 was passed in response to the rise of dictatorial communism as a worldwide threat to democratic capitalism. Fearing that politically motivated strikes could ruin the economy, the legislation prohibited Communist Party members from holding union offices and established limitations on strikes and picketing. In 1955, the AFL merged with the Congress of Industrial Organizations (CIO), which organized employees according to industrial interests and had previously pursued more militant tactics. The Landrum-Griffin Act of 1959 was enacted in response to concerns about union corruption; it required democratic reforms within unions, such as regular open elections and the filing of membership and financial reports with the Department of Labor.

By 1960, approximately one third of all wage earners were union members. In 1962, federal clerical and technical employees gained the right to unionize, though not the right to strike. The union movement also spread to the service sector, farmworkers, and academia. Beginning in the late 1960s, unions began organizing higher education professors for the purposes of collective bargaining. By the early 1970s, the American Association of University Professors (AAUP), the American Federation of Teachers, and the National Education Association represented faculty at community colleges and public and private 4-year institutions throughout the nation. Currently, approximately 31% of the faculty teaching at 4-year institutions and 63% of full-time faculty at 2-year institutions are members of collective bargaining units.

Despite these new areas of recruitment, union membership steadily declined as the United States began to shift away from its manufacturing base, the most heavily unionized sector in the economy, due to foreign competition. Currently, more than 50 unions operate under the AFL-CIO banner. The AFL-CIO advocates for union interests at the local, state, and federal government levels and partners with unions from other nations on global trade issues.

More important, labor unions evolved differently in other nations. In Great Britain, union leaders formed their own political party, the Labour Party, and obtained legal recognition sooner than unions in the United States. Some European nations had rival Christian and Socialist trade unions. In the Soviet Union and other Communist nations, unions became tools of politicians to obtain economic goals, until the collapse of dictatorial communism, which began in 1989. In Germany, codetermination laws require medium and large employers to allocate up to half the seats on their boards of directors to union members.

Union Violence and Corruption: The Teamsters

Historically, the union movement has been hampered by the stigma of violence and corruption. In the late 1800s, employers bribed police, militia, and criminals to harass and physically attack union organizers and their families. Some union members responded to violence with violence. In addition, unions organized migrants who traveled from one hard labor job to another. Some of these migrants used union membership as an opportunity to exercise their bitterness and resentment against those who had either been born with, or accumulated, more social privileges.

One such person was the union hero Joe Hill. Hill arrived in New York City from Sweden in 1902 and became a journeyman laborer, traveling from state to state looking for work. He joined the Industrial Workers of the World (IWW), a militant union based on the Marxist critique of capitalism. Hill composed prounion folk songs to inspire union organizers and strikers in their fight against abusive business owners and scabs who crossed the picket line. He was jailed for sabotaging an employer, which made him more militant. Hill obtained work in a Utah mine, but ill health and a bad economy led to unemployment. He was later accused of killing a Utah grocer, found guilty by a jury, and executed in 1915. Most scholars believe Hill was indeed guilty, but the IWW supporters claimed he was framed and declared him a martyr. Songs written by him, and about him, continue to be sung at union gatherings.

Most unions have high ethical standards, but not all. The International Brotherhood of Teamsters is allegedly the most notoriously corrupt union in the United States. The Teamsters were chartered by the AFL in 1899 to organize the transportation industry and quickly became the nation's largest union. Teamster leaders represented working-class laborers who worked 70 hours a week driving teams of horses to deliver products. Membership was expanded to laborers loading and unloading products at shipping docks, railroad depots, and warehouses. Within 6 years, the union won higher wages and a 52-hour workweek.

Unfortunately, people with criminal histories rose to leadership positions and formed alliances with well-organized criminal gangs. Teamster leaders, aware that employee wage demands and strikes could destroy a business, extorted money from business owners. Teamsters solicited payments either to not go on strike against a company or to conduct a strike against a competitor. The Teamsters intimidated nonunion employees to force them to join the union, using threats of physical violence. They also refused to transport products to or from businesses unless union members were employed or an extortion fee paid. Organized crime gangs, like Al Capone's group in Chicago and the Mafia in New York City, took control of local Teamsters unions when Prohibition ended and raided their pension funds.

During the 1950s, the Teamsters, still the nation's largest union, were led by Dave Beck and Jimmy Hoffa, both of whom had strong ties to organized crime. Their threat to interstate commerce transactions led to Senate committee hearings on union corruption. The public learned about unfair elections, extortion, embezzlement, kickbacks, money stolen from member benefit plans, no-show workers, and bribery, which led to some of the union reforms codified by the Landrum-Griffin Act of 1959. The Teamsters were expelled from the AFL-CIO in 1957 for their involvement in illegal activities; they were readmitted 30 years later but voluntarily withdrew from the AFL-CIO in 2005.

Profile of a Union Organizer: Cesar Chavez

Cesar Chavez represents a typical profile of a union organizer. Chavez, inspired by Gandhi's message of nonviolence and by Catholic social justice teaching, unionized immigrant farmworkers in California and led a 10-year nationwide boycott against nonunion grapes, until his death in 1993.

Chavez was born in Arizona in 1927, the son of illiterate Mexican immigrant parents. His father lost the family farm during the Depression and migrated to California. The poverty-stricken family lived in a tent and traveled throughout the state picking grapes, strawberries, tomatoes, and cotton. Chavez enlisted in the United States Navy following World War II and returned to California when his service ended. There he was recruited as a community organizer by Saul Alinsky's Community Service Organization and led a voter registration campaign for Chicanos.

In addition to receiving below-poverty wages, farmworkers were charged for ice water and had no bathroom facilities. Some supervisors charged for transportation to the fields and collected social security payments that were never recorded. Chavez started an underground newspaper, held secret meetings, and eventually founded the National Farm Workers Association in 1962, later renamed the United Farm Workers, to represent the rights of farmworkers.

Filipino grape workers went out on strike in 1965 for better wages and unemployment insurance. Chavez persuaded Mexican and Latino workers, fearful of being deported for immigration violations, to join the strike. Landowners accused Chavez of being a communist and imported Mexicans to work the fields. Local police sided with the landowners, threatened strikers with attack dogs and deportation, beat them up, and sprayed the strikers with pesticides. Some union members were illegally arrested for saying the word *strike* in public.

Chavez raised public awareness about these events by speaking at churches and universities. He called for a nationwide boycott of Schenley Industries, which purchased the farmworker-picked grapes for its liquor products. In the spirit of Gandhi and Martin Luther King Jr., Chavez led a 300-mile march to Sacramento, the state's capital, demanding political action. In 1966, Schenley Industries capitulated and recognized the union as the farmworkers' bargaining agent. Chavez spent the rest of his life expanding the union, participating in collective bargaining negotiations, and conducting strikes and boycotts.

The Ethics of Union Management Tactics: The University of Bridgeport Faculty Strike

Managing in a union environment can be extremely difficult. Most union contracts restrict managerial discretion. Strikes are very emotion-laden events that contain a plethora of ethical dilemmas. The behavior of the University of Bridgeport's administration and faculty union exemplifies some of these issues. The longest faculty strike in U.S. higher education history began in 1990 at the University of Bridgeport and lasted 2 years. The university administration locked out striking faculty and hired permanent replacement faculty. With the school on the verge of bankruptcy, the union was decertified.

The AAUP collective bargaining agent was certified in 1973, when a combination of declining enrollments, inflation, high capital expenditures, and large deficits suppressed wage increases. When administrators refused to negotiate with a faculty wage committee, the faculty authorized the AAUP as its bargaining agent. During the next 17 years, contract negotiation disputes focused on shared governance issues, managing faculty reductions during a time of declining enrollments, and determining fair wages. These deliberations resulted in a 3-day faculty strike in 1975, a 16-day strike in 1978, and a 2-day strike in 1987.

The faculty union never fully recognized the depth of the university's precarious financial situation. Union leaders, predominantly from lower-paying liberal arts departments that were threatened with the greatest position reductions, were convinced that the university had substantial financial resources. In January 1990, banks that had extended loans of more than $10 million demanded immediate cost reductions. The university president declared financial exigency in March 1990 and unilaterally eliminated 50 faculty positions, representing 27% of the faculty, without 1-year prenotification or severance pay. The union sued for failure to abide by its contract's legally binding due process clause. The president agreed to honor the contract until it expired in May 1990.

The university president hired a well-known union buster. During summer negotiations, the administration proposed a new contract that included a draconian 30% pay cut, a reduction in prenotification to 30 days, and no severance pay. This translated into a reduction in average salaries from $46,000 to $33,000 and a one-in-five chance of being laid off in 30 days without any severance benefits. By the time school began in September, a contract agreement had not been reached and 125 of the 175 full-time faculty went out on strike. Most of the 50 faculty who crossed the picket lines were from the professional schools. The union offered to return to work under the terms of the previous contract. The administration rejected the offer because it could not afford to pay faculty salaries under a temporary continuation of the previous collective bargaining agreement. Doing so would have put the university in default of its bank loans.

Students began withdrawing their tuition payments, which worsened the university's cash flow crisis. The administration declared a back-to-work deadline, and 40 of the original 125 striking faculty returned to work. For all intents and purposes their crossing the picket line broke the strike. The administration hired 20 permanent replacement faculty where needed. By mid-September, the university had 110 professors on its payroll. The administration achieved a labor reduction of 65 faculty by locking out the striking faculty.

Returning faculty crossing the picket line provided several justifications for doing so: They could not financially afford to lose their jobs to permanent replacements; the union was asking for too much given the university's financial distress; a continuation of the strike would destroy the university; and they wanted to help students enrolled in their programs complete the semester. The remaining locked-out strikers tended to be older faculty with a strong commitment to academic freedom and faculty whose positions would have been eliminated in March, though there were several exceptions.

The now jobless striking faculty, having worked at the university for an average of 25 years, were outraged at being permanently replaced. This had never happened before in academia. The striking faculty lobbied students to withdraw from the university, picketed the board of trustees, requested that local high school guidance counselors not recommend the university to graduating students, and disrupted graduation ceremonies.

When the Fall 1991 semester began, enrollment was down 25% from the start of the strike. The university, technically in default on its bank loans, was on the verge of losing its accreditation and bankruptcy. The university president was forced to resign by the board of trustees. The university avoided bankruptcy when the Professors World Peace Academy, an organization funded by a controversial Korean religious leader, supplied $50 million in exchange for majority control on the board of trustees. The university lost 75% of its enrollment during the 2-year strike. The inability of both union and administrative leaders to engage in cooperative trust-based negotiations ruined the careers of many faculty and administrators and nearly destroyed the university.

Current Status of Unions

Union membership totals differ from nation to nation. According to the 1997 to 1998 World Labour Report, the percentage of wage earners who are union members has declined worldwide since the 1980s due to economic, political, and cultural factors.

In the United States, union membership steadily declined from 35% in 1955 to 20% in 1980, and to just 12.5% in 2004. The highest unionization rates were in the public sector, namely employees in government, education, and protective services, such as firefighters and police officers, all at around 36%. Unions claimed only 8% of private sector employees. On the high end are transportation and utility companies at 25%. At the low end is the financial service industry at 2%.

Union decline in the United States is attributable to a host of factors, including the following:

- A job shift from manufacturing with high employee density to a service economy with low employee density
- Relocation of facilities to overseas regions that lack unions
- Employee satisfaction with existing work conditions being enhanced because of the adoption of participative management techniques and profit sharing
- A strengthening of antiunion labor laws
- Damage caused by corruption within unions
- Inadequate union leadership

According to the 1997 to 1998 World Labour Report, Western European union membership was highest in Sweden (77%), Iceland (71%), and Denmark (68%), and lowest in France (6%) and Spain (11%). Germany had 30% union membership and the United Kingdom had 26%. Most Western European nations had experienced declines from a decade earlier.

Former Eastern European communist nations tended to have higher rates of union membership than their Western counterparts, with Belarus at 96%. But Eastern European nations also experienced significant declines. After being liberated from Russian domination, trade union membership in Poland dropped from 47% in 1989 to 27% in 1995.

In Africa, Egypt had the highest level of union membership at 30%, but this was down from 39% a decade earlier. South Africa had 22% and Kenya had 17%. Mauritania, Guinea, and Gabon each had rates less than 3%.

In Asia, democratic capitalist Taiwan had 28% union membership compared with 55% for dictatorial communist Republic of China. Japan had 18% and India just 5%. In Latin America union membership ranged from 32% in Brazil and 31% in Mexico, down to 4% in Guatemala. Elsewhere, Russia had 75% union membership.

A union's ultimate weapon against a recalcitrant owner is a strike, the collective refusal to work. An owner's ultimate weapon against a recalcitrant union is a lockout, the refusal to allow employees to work. The 1997 to 1998 World Labour Report collected statistics that combined the number of strikes and lockouts in each nation. Leading the list were Russia (8,856), France (1,671), India (1,062), Spain (883), Australia (643), and Italy (545). The United States had just 31 strikes and lockouts.

The Future of Unions

Union membership is historically low. Dissension within the AFL-CIO regarding appropriate recruiting and political strategies threatens the federation. In 2005, four unions boycotted the 50th anniversary convention of the AFL-CIO merger to protest its current leadership. Then the Service Employees International Union and the Teamsters—the two largest AFL-CIO unions, representing one fourth of the federation's membership and accounting for one sixth of its budget—withdrew from the coalition, leaving it with 54 unions and 10 million members.

Nonetheless, the issues relevant to unions remain salient. According to the Economic Policy Institute, 24% of working Americans have incomes below the federal poverty level. Wages have been stagnant for 30 years. During the 1960s, scholars predicted that by the year 2000, technological advancements would reduce the average workweek to just 20 hours. Instead, between 1973 and 2000, the average annual hours spent working increased by 199 hours. Labor-saving technologies continue to create anxiety over job loss. Downsizing has caused the survivors to do the work of two people, while those dismissed work two jobs to achieve an equivalent prior income.

Research has shown that long working hours have negative impacts on employee productivity, employee health, family issues, and the natural environment:

- *Employee productivity impacts:* increases error rates and reduces productivity
- *Employee health impacts:* increases stress, fatigue, depression, high blood pressure, heart attacks, obesity, diabetes
- *Family impacts:* decreases the time available for family meals and increases job-escape drinking
- *Environmental impacts:* increases consumption and greater use of disposable items

The modern union agenda shares many similarities with the original union agenda. Employees continue to need better wages, benefits, and working conditions, and shorter working hours. Immigrants need more protection from abusive owners and managers. Other future items on the AFL-CIO agenda include universal health care, elimination of discrimination, and wage and income equality.

Conclusion

Unions can be agents of social change and workplace justice. They can also be corrupt and destructive. One thing is clear: For the past 50 years they have been steadily losing more members than they have gained.

Labor unions perform an essential equalizing function, leveling the playing field between powerful business owners and organizational managers, who seek to minimize employee wages and benefits and dictate workplace rules, and individual employees who lack the power to adequately represent their own interests. Unions typically arise in circumstances where employees are continually dissatisfied with wages, benefits, and working conditions. They counteract managerial power by providing a unified employee voice.

—Denis Collins

See also American Federation of State, County and Municipal Employees; American Federation of Teachers; Capitalism; Due Process; Marxism; Minimum Wage; National Labor Relations Board

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Laissez-Faire

It is said that the 17th-century French finance minister Colbert once asked a group of businessmen what he could do for them. One of them, Legendre, is supposed to have replied, "Laissez nous faire" ("leave us alone!"). The reply became a slogan, serving ever since as a tag for the policy of keeping government direction of the economy to a minimum. (Some argue that the minimum should be *none.*)

The theory of laissez-faire stems from the fact that what we call an *economy* is a vast array of interactions among individuals, each of whom is concerned with making his or her living by organizing and exerting skills and energies to that end. In the process, the agent will frequently find it advantageous to benefit from the productive energies of other agents by making trades. There are two hallmarks of these trades. First, each party is motivated by his or her *own* interests—not "advancing the general good" or some other theoretically questionable motive, but by his or her own interests, *whatever* they are. Second, each individual participating is free to take or leave any particular proposal made by the other party. The two are linked together in that when parties freely exchange, we infer that each sees the choice as being to his or her own benefit—otherwise why would they do it? But given that it is to one's benefit, why would not one do it? Having an actual interest in something is an intelligible explanation of why someone did something, and having an interest in oneself, whatever else, is something we're generally safe in presuming for anyone.

The case for "leaving them alone" derives from this presumption. Each participant is inherently motivated to seek out trades and to take the best options available. It is not obvious why any direction or regulation would be required to accomplish this end. Why might it be?

Here are several familiar answers.

1. Countering Force and Fraud. One answer is that while people are indeed motivated to promote their respective advantages, they are not necessarily motivated to do so in a way that respects the freedom of others. Besides trading, another way of getting something from someone is simply by taking it, by stealth or force. Still another is by fraud—claiming to be offering one kind of good or service when in fact what will be delivered is not as described, or perhaps not delivered at all: "Take the money and run" is, in short, a temptation. The need for intervention of some kind is inferred from this possibility. We may need to set up mechanisms either for preventing fraud and violence in the first place, or at least for detecting, apprehending, and punishing those who engage in it. In this respect, of course, the need for intervention in exchanges is the same as in the case of any interpersonal actions.

2. Limited Knowledge. The other answer is rather different. According to it, trades take place on the basis of knowledge on the part of each participant. But what if the individual's knowledge is insufficient? That party may then be unable to pursue advantage as intended. The proposal, then, is to see to it that all operate within an environment of relevant knowledge. The state is then called on to provide it, on a basis of equal provision for all.

3. Providing the Framework for the Market. A variant of this second idea is that trade takes place within a framework provided by the law. Law and regulation establish the forms for trade and thus encourage it, smoothing the way and providing paths, as it were. In one version of this reply, we need law to make trade possible at all: Trade, it is claimed, cannot proceed without a framework of law. Specific ways in which government is said to be needed in this respect would include the provision of forms of currency or money and laws and regulations governing exchange. In the other version, government is needed for the provision of infrastructure, such as roads, bridges, canals, and communication facilities, and economic policy to prevent inflation, deflation, and other economic ills that are thought to have bedeviled economies over the past few centuries.

Advocates of laissez-faire have replies to all of these. They point out that there is no obvious reason why people cannot make exchanges among themselves without any external overseers, and that trades occur all the time among people without police standing over them. Trade has occurred among very primitive peoples as well and between people from distant tribes or communities with no common state to oversee the activity. They also note that infrastructure can be and has often been provided by privately acting parties. This includes even the provision of monetary facilities such as coinage and banking procedures and forms. Economists explore the potential for nongovernmentally based facilities of these kinds, and it seems fairly clear that the case for the literal necessity of the state as the provider of them has been by no means established.

In any case, an advocate of laissez-faire need not be a philosophical anarchist. The free market proponent can simply suggest that the minimum amount of governance needed to make exchange function is very tiny and that substantial control over the terms of trade, whom we may trade with, and control of prices is inimical to the securing of the benefits to which trade can lead.

The Model of "Perfect Competition"

Economic theorists in the late 19th century developed a theory of a "perfectly competitive" economy, proposing that such an economy would indeed maximize the utility of all parties—if certain conditions were met. The following are required: first, perfect *information*, so that each participant knows everything about what is offered, and about all alternatives; second, *many producers*—so many that no single one or small number of them can influence prices by unilateral actions; third, no *transaction costs,* so that the only relevant costs and benefits are those sought from the exchanges themselves; and finally, no *externalities,* these being effects on "external" persons, that is, people not participating in the exchange in question, and such that the effects of the exchange on these parties is either not wanted by the parties or not wanted by the exchangers themselves, but nonetheless they affect the pattern of benefits and costs. In fully "internalized" trade relations, each party to the trade would bear the cost if and only if that party also received the relevant benefits, and vice versa. If any of these conditions is lacking, so it is argued, there will be departures from perfect efficiency. And it is also argued that rectifying these deficiencies, again, justifies the intervention of government.

Again, supporters of laissez-faire have replies. First, they point out that the "ideal" of a perfectly competitive economy is idealized in the sense that it would be impossible for any of its conditions to obtain. It is commonly said that a completely free or a so-called perfect market could not exist. That is obviously true: "Perfect information" makes little sense, as well as being obviously impossible; transaction costs are inevitable; and the category of externalities is so broad that it is again unclear even what the condition is supposed to exclude, other than violence and fraud. This makes it dubious to use the model for the purpose of describing economic reality. Information simply does have costs, and others do not automatically have a right to it. So the laissez-faire advocates propose that the right thing to do is to have those who discover it sell it to those who do not have it but want it. Transaction costs simply do happen, and people can make fortunes by discovering and marketing ways to lower them: Banks, for example, are in that business. Negative externalities too can be managed by firms protecting people from them and via arbitration services to sort out disputes regarding them. Violence is avoidable—easily so among reasonably civilized people—and it is possible to take measures to reduce or eliminate it in cases where it is a problem without resorting to centralized authority. Defenders of laissez-faire also argue that state intervention as a cure for these supposed shortcomings is worse than the disease. (And "anarcho-capitalists" argue that it *always* is and thus that government as such is not justifiable.)

Laissez-faire supporters propose that the correct model of the *ideal* market is not the so-called perfectly competitive market but simply the market in which there is no authoritative intervention by persons external to exchanges and not themselves affected by them. This would be the situation where the relevant factors were simply the resources of the various parties, which are recognized by the others as belonging to their owners, and their interactions, which are with a view to securing the best outcome that can be achieved by each participant.

If a "perfectly competitive" economy is unrealizable, the more relevant idea of a market in which no agent is coerced by further agents is quite realizable and often is, in limited ways, realized. When we go to the supermarket, no one prevents us from choosing whatever we want from what is available, unless it turns out that we cannot pay for it. There is typically a lot of competition, no store being in a position to charge whatever it likes, but never so much competition that prices absolutely do not vary from one to another. In any case, no one can charge "whatever he or she likes," since at some point their hoped-for customers simply will not buy. The condition of perfect competition is in fact impossible to define, since everyone competes in one way or another with everyone else, and price adjustments, great or small, are continually being made.

Monopoly

An instructive application here concerns monopoly. Critics of laissez-faire contend that monopoly is an evil that clearly justifies state intervention to prevent it—a point of view that has led to antitrust legislation in many countries. Upholders of laissez-faire argue that the claim that free markets tend toward monopoly is not obviously true and, if anything, the reverse. The purpose of monopoly would be to be able to charge above-market prices; yet if firm X charges above-market prices, it would mean, by definition, that others could make money by charging less than that. Why would they not do so? As long as entry into the market is not artificially impeded, most notably by government, it seems that they would indeed do so.

Reflection on this point leads to the need to distinguish between two kinds of monopoly: one in which the monopolist enjoys government support, *compelling* potential competitors to stay out, and the other in which even though competitors are not prevented by law from entering the market, no one else is in fact able to make a go of it—the monopolist is so because of superior efficiency, organization, quality, and price. In this latter case, supporters of the free market point out, it's hard to see why the public should be motivated to break up what is apparently a good thing. But in the former case, monopoly is not a problem for the laissez-faire theorist but rather a manifestation of its absence. If monopoly is bad, then the state shouldn't be creating it. In the unlikely case that it's good, why should government suppress it?

The "Invisible Hand" Thesis

A famous thesis from Adam Smith's *The Wealth of Nations* introduced the expression "the invisible hand" in support of laissez-faire. All individuals direct their industry so as to produce what is of greatest value, even though they aim at only their own gain, and so, as if "led by an invisible hand," they promote a good public end that was quite unintended. Smith's claim is that the wealth of the *nation* is promoted by the individual's promotion of his *own* interest, without any aim of advancing the wealth of the whole. Why would this be plausible? The answer is that when the market is a socially supported institution, there is a general recognition of the rights of property. People own various things and are entitled to them just because they have either created those things by their work or gotten them by freely trading with others: Theft, violence, and fraud are not permitted. So long as those restrictions are observed, the market works for the public good in that the only ways in which it can work for the reverse are blocked. So, all trades will work to some people's good and no one's harm. Moreover, when person A gains something valuable to her by an exchange with B, who in turn has something more valuable from his exchange with A, the stage is set for further, still more beneficial exchanges with yet other people. Trade generates *positive* externalities in that sense. This is most clearly illustrated in the case where A acquires from B capital goods enabling A to produce consumer goods more efficiently than A would otherwise have been able to do. The benefits of this exchange to A's later customers continue indefinitely at a level higher than they otherwise would have been. In general, freely acquired gains tend to generate still further gains, and only interferences with those free activities will make for the worse. Smith's thesis, then, looks promising.

Equity and Equality

An area in which opponents of the free market have been vocal is equality. Their thesis is that the free market pays no attention to equality and indeed creates inequality. Given a free market, we will expect some people to do better than others—probably, much better. First, some people are much more productive than others, and so will be able to make trades more profitable to themselves. This may be because they are more clever, more hardworking, or more skillful. Or, second, it could easily be that some people just happen to be "in the right place at the right time" as, for example, in stock market purchases or because their particular talents are just what people need at that time and place. Even the ingenious inventor needs to be born in the right age so that his or her talents can generate the goods that people in that age and place will be able and willing to buy. In short, luck is also likely to cause some to prosper more than others.

This argument raises a deep question of social philosophy: Are people indeed entitled to the sort of "equality" that consists in having similar levels of income? The most forthright response of the free market theorist is to deny that they are. The free market philosophy certainly treats everyone as equals in other basic respects. No one is entitled to use force against *anyone* else for *any* reason other than for protection of person or property, and this applies whether the victim is black or white, male or female, religious or irreligious, and so on. Moreover, the market cares, as it were, only about "the color of your money." People may select trading partners on any basis they like, but if they are hiring people to help them produce, or to appeal to customers, the market works strongly against what we usually consider "discrimination." One has but to witness the success of black athletes in professional sports, where once legally imposed color barriers were broken down, to see the powerful forces of the market at work in eliminating irrelevant distinctions—much to the improvement of those sports, as well, in the view of virtually all enthusiasts.

The market does indeed "discriminate" against those who lack productive skills or savvy, and certainly luck will often play a part. But why would these be objections? The former effect works greatly to society's benefit, by encouraging what is more to social advantage. As for luck, a main point about it is that it is unforeseeable, by definition, and attempts to eliminate its effects are sure to be counterproductive. Moreover, the rules of the market ensure that those effects will be good rather than bad, though not, of course, equally good for all.

In countries such as the United States, where the free market flourished, probably more effectively than anywhere else for a long time, prosperity has been their reward. A major effect of this prosperity is that it has been very widespread: Poverty in the United States is rare, and what is called "poverty" there would be considered great good fortune in most of the world. If the concern about equality is that some people will be, not just less well off than others, but actually suffering, starving, or in desperate want, then the free market supporter can plausibly reply that the market will do far better than any other kind of social system in reducing or eliminating those evils. Apart from that, it surely should be doubted if it is a good thing when people with amazing talents or extraordinary business acumen get no more than the untalented and incompetent. Given the enormous benefits to most people from the fact that people *can* become wealthy performing socially useful services, it is arguable that the egalitarian has no real case. It must be remembered that the only way to make a lot of money on the market is to sell a lot of things that people want to a lot of people. How can we complain about *that?* So asks the supporter of laissez-faire.

Complaints About the Market: Cultural

One often-heard complaint is that a market economy leads to a market *society* and that this would be a bad thing. The market society, it is claimed, would be full of extremely competitive people—a sort of "dog-eat-dog society." People would be fixated on owning as much as they could and would turn into greedy people with shallow values, and so on. Defenders of the market respond that this familiar and fashionable criticism is almost impossible to evaluate. We all live in a society in which such behavior is possible, but most of the people we know are not like that. Even highly competitive businesspeople are often civilized, interesting, intelligent, outgoing, and warmhearted in their social lives. Clearly, any tendencies in that direction are resistible by individuals and have apparently been resisted by most of them. Where do we go from there?

As regards the marketplace for culture in a more literal sense, proponents of the market can point to the enormous support of museums, operas, symphony, and the like in 19th- and early-20th-century America prior to substantial public financing of those things. They argue that capitalism can and does support the arts. Artists, musicians, and other creators have always faced the question of how to make a living by their talents, and they appear to do so very well in fairly free market societies.

Complaints About the Market: Economic and Technical

Somewhat more technical criticisms of the market are widespread. It is widely claimed that the market is subject to "market breakdown," which requires government action to counteract it. And it has long been held that market economies are subject to "business cycles"—namely, "booms and busts," as classically exemplified by the Great Depression in America. This general issue is the subject of much controversy in the economic literature, but supporters of the market have strong arguments on their side as well. They point to the fact that downturns have been of much more modest proportions in the past 60 years and cite extensive research that has shown that bad monetary and fiscal policies by governments are the main cause of depressions, rather than anything internal to the market.

—Jan Narveson

See also Anarchism; Austrian School of Economics; Capitalism; Commerce and the Arts; Conspicuous Consumption; Consumerism; Economic Efficiency; Efficient Markets, Theory of; Externalities; Hayek, Friedrich A.; Income Distribution; Pareto, Vilfredo; Poverty; Redistribution of Wealth; Smith, Adam; Spontaneous Order

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Land Ethic

The Land Ethic is a perspective within environmental ethics that grants ethical priority to ecosystems and other ecological entities. Although the Land Ethic is sometimes used to refer to any ecocentric environmental ethic, the phrase originated in the writings of the American ecologist and writer Aldo Leopold (1887–1948) and is most commonly identified with Leopold's views.

"Ecocentric" ethics integrates ethics and ecology by bringing such ecological wholes as species, populations, habitat, and ecosystems to the center of ethical consideration. Thus, an ecocentric approach is distinguished from biocentric ("life-centered") approaches by its emphasis on ecological concepts rather than on individual living animals and plants. Ecocentric ethics also gives ethical consideration to nonliving natural objects, such as rivers, wetlands, and mountain ranges, in ways that a life-centered biocentric ethics does not.

The science of ecology developed during Leopold's lifetime, and he was the first person to call for a radical rethinking of ethics in light of this new holistic science. Leopold's thinking was presented in the posthumously published *A Sand County Almanac* (1949), and the definitive section of that book, an essay titled "The Land Ethic," is the first systematic presentation of an ecocentric ethics.

Leopold began that essay by retelling the story of Odysseus, who, on returning from the Trojan War, hanged a dozen of his women slaves for misbehavior. Because slaves were understood as property, Odysseus's action was not seen as unethical or inappropriate. Since that time, ethics has evolved so that moral standing now is extended to all human beings. "The Land Ethic" is Leopold's call to continue this extension of ethics to include land, plants, and animals. Leopold appears to defend a version of biocentric ethics by extending moral consideration, what he termed "biotic rights," to birds, soils, waters, plants, and animals.

Yet throughout his life, Leopold remained an active hunter and fisherman, and an advocate of other activities that treat natural objects as resources for human use. The apparent inconsistency between advocating biotic rights for natural objects and supporting hunting, fishing, and timber harvesting was resolved by Leopold's insistence that we view the land ethic holistically. It is the "land community" that is granted moral standing. Individual members of that community can still be treated as resources as long as the community itself is respected. The "ecological conscience" teaches that humans are but members of the biotic community—"biotic citizens," rather than conquerors of nature. Ecology shifts the focus of moral consideration away from the individuals emphasized by biocentric approaches and onto biotic wholes.

Accordingly, the extensionism that is at work in the Land Ethic does not ask that we simply extend moral consideration to other living beings and make room in our moral deliberations for yet another type of individual moral subject. Leopold asks that we make a category shift away from individuals and grant moral standing to communities, symbolically represented as the land. This shift to an ecocentric approach is central to the Land Ethic.

This aspect of the Land Ethic is concisely summarized in Leopold's most celebrated and controversial statement that "a thing is right when it tends to preserve the integrity, stability, and beauty of the biotic community. It is wrong when it tends otherwise" (from *A Sand County Almanac*). When combined with some basic ecological observations, this principle can be used to generate the specific normative conclusions of the Land Ethic.

The Land Ethic uses the image of a "biotic pyramid" or "land pyramid" to help us understand the nature of the biotic community. The land pyramid represents the structure of biotic and abiotic elements through which solar energy flows. This structure can be understood as a pyramid, with soil on the bottom, followed by a plant layer, an insect layer, a bird and rodent layer, and so on up through the larger carnivores. As long as the structure and function of this pyramid is maintained, individual components of that structure can be used as food and resources for humans. Indeed, this fact simply acknowledges that all living beings use both other living beings and the abiotic components of their environment as resources.

Given the complexity of this highly organized structure, however, Leopold argued that humans should disturb or change ecosystems slowly and with great humility. Preservation of life-forms in all their diversity is the first general rule that we ought to follow because not even ecologists understand how this complex system operates. Because this complex structure has developed through millions of years of evolution, human interference with it ought always to be humble and constrained. Any change in the system requires that many other elements adjust themselves to it. When this occurs slowly, as it does through evolution, the system is self-regulating. When change is introduced abruptly and violently, as it typically is through human intervention, the potential for disaster is genuine. Thus, we should tread lightly on the ecosystem.

It is also wise to assume that native plants and animals are best suited for a particular locale. As a result, we can speculate that Leopold would support the preservation of biological diversity and oppose habitat destruction and monoculture agriculture. The Land Ethic makes it ethically permissible to hunt individual animals as long as the "integrity, stability, and beauty" of the population are preserved. In fact, in the many cases in which an overpopulation threatens the stability of the herd or the integrity of an entire ecosystem within which the animals live, we might even have an obligation to selectively kill individual animals. On the other hand, introducing nonnative species is courting disaster. The Land Ethic would warn against reliance on chemical pesticides, herbicides, and fertilizers.

There are several elements of the Land Ethic that make it an attractive philosophical option. First, the Land Ethic offers a fairly comprehensive environmental perspective. It appears to offer a decision process for most, if not all, environmental and ecological issues. Unlike the animal welfare movement, it can offer normative guidance for issues as diverse as wilderness preservation, pollution, conservation, energy, resource depletion, and so forth.

Second, it can also avoid many of the counterintuitive conclusions that burden the individualistic biocentric approach. We do not need to be overly concerned with seemingly insignificant issues such as killing a mosquito, cutting a tree, or hunting and fishing. The continued healthy functioning of the system is the primary concern.

Finally, the land ethic is thoroughly nonanthropocentric. Humans are said to have no privileged status in the ecological community. They are, in Leopold's image, reduced from conquerors to mere community members. Not only does this shift accord natural objects and systems moral standing; it is also more consistent with the teachings of ecology. For many environmentalists, this is the single most important prerequisite for a sound environmental perspective.

Criticisms of the Land Ethic

Two general challenges can be raised against Leopold's Land Ethic. The first challenge focuses on what philosophers have called the "naturalistic fallacy," and the second focuses on the nature of ecological wholes that deserve moral consideration.

A central challenge to any attempt to ground ethical values in natural facts is the claim that a logical gap exists between statements of fact and judgments of value, between *is* and *ought*. Identified in recent decades as the naturalistic fallacy, the conclusion that something is good or right based solely on a description of what is natural is rejected by many philosophers as fallacious. Leopold's famous dictum, "A thing is right when it tends to preserve the integrity, stability, and beauty of the biotic community. It is wrong when it tends otherwise," would seem to be an example of exactly this type of reasoning.

The Land Ethic appears to bridge this gap by using a type of teleological reasoning reminiscent of the Aristotelian tradition. Teleological ethics holds that every being has its own natural end or purpose and that by attaining this end or purpose, beings are doing what is naturally good. By attributing such characteristics as health and stability to ecosystems, the Land Ethic treats ecosystems as having a natural end or purpose. From a natural scientific description of the normal development of an organic whole, with its own identifiable integrity and stability, we are to draw conclusions about what is good or bad, right or wrong, and healthy or unhealthy for elements of that system. Predators are good and ought to be protected, for example, because they contribute to stable populations within the system and, thus, to its health. Eliminating exotic species or reintroducing native species is right because it maintains the natural integrity of the ecosystem.

But note that one question always remains: Why *should* we value the overall integrity or stability of the system itself? We could appeal to the role that that particular ecosystem plays in the overall stability and integrity of some larger organic whole. Thus, like a heart, a wetland performs a function for some organic whole. Accordingly, we ought to preserve the integrity and stability of an ecosystem because, in doing so, we are promoting the good of some larger whole of which the ecosystem is a part.

Following this line, we would eventually argue, as Leopold sometimes does, that the earth itself should be considered an organic whole. But even if this were scientifically valid, this line of reasoning simply pushes the open question back a step. Why value the integrity and stability of this larger organic whole? Because instrumental and individualistic reasons (for example, that the larger whole should be valued because it preserves the well-being of its constituent parts such as human beings) are not part of the Land Ethic, we would have to argue that some teleological goal exists for the entire system. Here the teleological model seems to break down. Neither ecology nor philosophy has produced a plausible account of what the earth's telos might be.

The other option is for the Land Ethic to argue that an ecosystem, like an individual organism, goes through developmental stages. The normal developmental progression would thereby provide a basis, as it does in human medicine, for evaluating the health and well-being of that system. Unfortunately, this is logical only if we assume the validity of an organic model of ecosystems, wherein every locale has a single climax stage toward which ecological succession aims, and each ecosystem is separate and unique. But given that most ecologists have long since abandoned the organic model, use of this option is weakened. There does not seem to be a single ecosystem that develops through time. For example, over time the biological populations of a field might go through a series of ecological transformations from weeds to perennials and grasses, to shrubs, to pine forests, to oak forests. What would the "integrity and stability" of this system be? Should we seek to preserve the field as home to prairie grasses and shrubs, as a pine forest, or stay out altogether and let whatever happens happen? The important point is that we can meaningfully ask these questions. Hence, the leap from ecological fact to ethical value remains an open question. Abandoning the organic model of ecosystems in favor of a less metaphorical food chain or energy circuit model does not rescue the Land Ethic. Why is the preservation of the integrity and stability of a food chain or energy circuit good or right?

We can summarize the philosophical point of these challenges. The Land Ethic's normative conclusion ("a thing is right when it tends to preserve the integrity, stability, and beauty of the biotic community") seems to be derived, in some way, from the facts of ecology. Even assuming that a factual and meaningful basis exists for attributing integrity, stability, and beauty to ecosystems, how these facts are connected to the value conclusion remains an open question. If we speak of ecological functions in an Aristotelian teleological sense as aiming toward some goal, either as parts within a larger whole or as a whole with its own goals, we might have some basis for reaching normative conclusions. But the Darwinian account of natural selection casts serious doubts on the meaningfulness of teleological explanations in biology. In this account, members of an ecosystem do not function the way they do because of some forward-looking goal or purpose toward which they are aiming. Components of an ecosystem function the way they do because functioning in this way has, in the past, proved adaptive.

We should be careful to avoid overstating the force of these criticisms. The point is not that we cannot support ethical judgments by appeal to naturalistic facts. The point is that in defending something as right or wrong, we need to do more than simply say that it is normal or natural. Ecological facts, in themselves, do not "prove" that ecological integrity and stability are ethical values. Nevertheless, developing environmental policy in ignorance of ecological facts would seem perverse. Thus, while the facts of ecological science do not prove the normative conclusions of the Land Ethic, they do provide sound evidence for environmental policy.

A second group of challenges to the Land Ethic centers on its holism. Two separate concerns underlie these challenges: Can a meaningful account of ecological wholes be defended, and are the ethical implications of holism acceptable?

One problem for any ecocentric ethics, and for the Land Ethic more specifically, is that ecologists do not agree on proper scientific methods, models, and conclusions. Ecology has not become a single, unified science, and therefore, attempts to draw normative conclusions from ecology face serious challenges. In particular, the Land Ethic seems to rely on highly contentious models and metaphors of ecological wholes.

As the science of ecology developed in the early decades of the 20th century, ecologists often referred to ecosystems as *superorganisms* and *communities*. Such terms suggest teleological, goal-directed, stable, cooperative, and unified structures. In this situation, normative concepts such as health, integrity, and stability seem readily applicable. But as ecology has developed as a science, such models have been rejected increasingly as overly metaphorical and anthropomorphic. Replacing an ecological model using "biotic community," with biochemical cycles of water, nitrogen, carbon, and photosynthesis, makes drawing normative conclusions from scientific evidence less plausible. After all, what practical conclusions could be drawn from the normative commitment to preserve the health or integrity of the nitrogen cycle?

Furthermore, some ecologists see more change than stability, more chaos than integrity in ecosystems. The Land Ethic appears to endorse ecological models of stable and enduring ecosystems. To the degree that the facts of ecology raise questions about these models, the persuasiveness of the Land Ethic's normative conclusions are in doubt.

The second concern with the Land Ethic's holism is the ethical unease that the Land Ethic may condone sacrificing the good of individuals to the good of the whole. If we do define right and wrong in terms of the biotic community, it would seem possible to sacrifice individual members—for example, individual human beings—for the good of the community. For example, Leopold seems willing to condone hunting individual animals to preserve the integrity and stability of the biotic community. But because he also describes humans as equal members of that community, he would seem to be committed to the permissibility of hunting humans if doing so would preserve the integrity, stability, and beauty of that community.

Various critics have offered versions of this challenge. Some have called ethical holism totalitarian and "environmental fascism." These are serious charges, particularly when humans are treated as equal members of ecological communities. If they cannot be answered by defenders of the Land Ethic, we will have good reason to look elsewhere for a satisfactory environmental ethic.

Thus, serious philosophical challenges to the Land Ethic remain. Nevertheless, Leopold's work holds promise for philosophical reflection on the environment. The greatest contribution of the Land Ethic lies in focusing attention on ecosystems and relationships—in short, in taking ecological wholes as worthy of serious moral consideration.

Implications for Public Policy and Business

Three aspects of the Land Ethic make it an attractive basis for public and business policy directions. First, the reliance on ecological science provides a rational and objective basis for policy prescriptions. Although ecology may be unable to offer unequivocal prescriptions, it does provide a strong foundation on which to develop sound environmental policy. Science provides the best starting point from which any consensus might emerge among various and competing points of view.

Second, the Land Ethic provides a middle ground between those who seek to preserve natural areas from any human intrusion and those who would value natural objects as mere resources to be exploited for human use. The emphasis on ecological holism means that the integrity of the ecosystem can be preserved while still directing some resources for human use. Limits to the economic use of resources can be established, but their very use is not prohibited by the Land Ethic.

Finally, the Land Ethic also offers the possibility of practical advice in ways in which some environmental perspectives do not. Concepts such as the stability and integrity of ecosystems offer practical guidance for deciding the range and limits to which ecological systems can be managed. Furthermore, as business and political institutions become increasingly concerned with sustainability, the Land Ethic can offer an ecologically grounded ethical framework for conceptualizing sustainability. Ecosystem health, stability, and integrity would seem a plausible approach for translating the language of sustainability into ecological terms.

—Joseph R. DesJardins

See also Animal Rights; Animal Rights Movement; Anthropocentrism; Biocentrism; Deep Ecology; Environmental Ethics; Environmentalism; Environmental Protection Legislation and Regulation; Gaia Hypothesis; Green Values; Sustainability; Wilderness

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LEADERSHIP

Leadership is any process of leaders influencing followers. A leader, sometimes likened to a magnet, is one to whom others look for guidance. Influence is the ability or capacity to get another person to do or believe X rather than Y. One vital source of influence is formal authority to command, held for example by business executives. An individual not possessing any formal authority may acquire moral influence equivalent to informal authority through persuasion, example, or ideas. Varying sources and means of influence, together with the morality of ends and means of influence, are key dimensions of leadership. Where control of important resources overlaps with formal or informal authority, it is an aspect of leadership.

This entry will first explain the prevailing prescriptive theory of leadership. Subsequent sections comment on examples of business leadership, ethics of leadership, methods for effective leadership, competing conceptions of leadership, the relationship between leadership and management, and the roles of emotional intelligence and charisma. The conclusion guides the reader to the classical literature on leadership.

The Prescriptive Theory of Leadership

Prescriptive theory emphasizes good leadership as a calculated process of leaders honorably influencing followers to achieve group welfare gains. Leadership in democratic societies should be "servant leadership," defined as service on behalf of others. Organizational or societal success requires executives with effective leadership skills and strong moral values, and also widespread distribution of such skills and values in the sense of "empowerment" of followers. General Norman Schwarzkopf, commander of U.S. forces during the 1991 Gulf War, characterizes this prescriptive theory of leadership in terms of a combination of competence and character. Good leadership has the connotation of successful outcomes achieved through effective and moral means. Bad leadership has the connotation of ineffectiveness or unethical means resulting in unsuccessful outcomes for the group. Pragmatic leadership has the connotation of flexibility rather than of tolerance for unethical means to obtain moral ends.

Success, effectiveness, and ethics may not automatically coincide. A successful leader improves group welfare; an unsuccessful leader does not. Evaluation of success involves goal legitimacy and the definition of a time horizon over which success occurs. A competent leader is effective at influencing followers. Ethical leadership means that individuals of high moral standards seek ethically desirable ends through ethically acceptable means. Unethical leadership involves an amoral or immoral leader who acts for purely personal benefit regardless of consequences to others. An amoral person has no moral standards, no sense of right or wrong. An amoral leader simply calculates personal returns and risks. An immoral person has low or corrupt moral standards. An unethical leader may be just as effective at influence as a moral leader. An effective leader may be successful or unsuccessful depending on circumstances beyond his or her control. The prescriptive theory predicts that over time, moral leadership will outperform unethical leadership in terms of influence, effectiveness, and successful group outcomes.

William James's 1880 essay on leadership makes a distinction between leadership in thought and action. Action leadership has immediate impact. It occurs in response to prevailing conditions. Action leadership can be thought of as acting directly. A business executive is engaged in action leadership. Thought leadership has long-term consequences. It can be thought of as acting indirectly. An artist or scientist is engaged in thought leadership.

Action leadership occurs directly through formal or legal authority (i.e., command) or through informal (i.e., moral) authority in dyads, groups, teams, formal organizations or their subunits, communities, and societies. Formal leadership involves a position or office in which resides lawful authority to act. Executives and managers hold such positions. Informal leadership may be exercised unofficially by individuals or groups acting through moral authority. In formal leadership, an individual fulfills a socially sanctioned role. In informal leadership, an individual establishes a role accepted by others as legitimate. Informal leadership relies on persuasion, example, or ideas. The intentional exercise of influence overlaps markedly with the art of politics. Much of leadership is essentially the activity of a politician. Leadership and management in business may be regarded as involving as much politics as does behavior in government.

Thought leadership occurs indirectly through the power of example or idea in the sense of best or *avant garde* achievements in artistic, educational, intellectual, scientific, or technical spheres. Followers are individuals or groups who look to those achievements for guidance. Indirect leadership might be officially sanctioned (e.g., a poet laureate or a national academy) or informally exercised through accomplishments (e.g., recognized by a Nobel Prize or best-seller status). In his 1844 essay on "Politics," Ralph Waldo Emerson ascribes a moral essence to influence: The motivational power of an idea has no boundaries. John Maynard Keynes argues similarly at the end of *The General Theory of Employment, Interest, and Money* (1934) that ideas are extremely powerful and often influence behavior without the knowledge of the actor.

Contrasting Business Leadership Examples

There has been a dramatic shift in perception and understanding of action leadership since James M. Burns's pathbreaking book *Leadership* in 1978. The long-established conception had been of hierarchical authority, whether socially legitimate or not, and intentionally manipulative practices in nondemocratic settings. This tradition was associated with Niccolò Machiavelli's *The Prince,* on Renaissance statecraft, in which the end is held to justify the means. *The Prince* was a study of amoral leadership illustrated by Cesare Borgia. *The Prince* is superficially a manual of statecraft but one written to explicate the methodology of seeing through deceptions to realities: One must first understand the ways in which one can be misled. Burns emphasizes fundamental changes in leadership for modern democratic settings. Consent of the governed implies accountability of elected and appointed leaders. Today's literature includes a large body of work on the leadership styles of U.S. presidents.

The basic shift in perception was followed by studies of new styles of business leadership that emerged in the 1980s and 1990s. Much of the recent interest in leadership arises with strong if disputable evidence that change and transformation in businesses can have large financial payoffs. The earlier tradition stemming from Machiavelli had been that leader-guided change, illustrated by a few successful founders of new political orders, is risky.

The very model of a modern business leader is widely held to be John F. (Jack) Welch, who took over as the youngest ever chairman and CEO of General Electric (GE) in 1981. He is likely the most studied business executive of modern times. A large literature on Welch includes books he has published. A chemical engineer with a Ph.D. (University of Illinois, 1960), Welch joined GE on graduation. He was dissuaded from quitting in 1961 (over bureaucratic red tape, an indifferent boss, and a measly $1,000 raise) by a perceptive young executive who personally promised Welch a better working environment. Twelve years later, Welch wrote in his annual performance review that his goal was to become CEO of GE.

The present assessment of Welch following his retirement is, however, more mixed or controversial. During his tenure as CEO of GE, he was clearly a very effective leader and highly successful at increasing shareholder value. Welch has a strong claim to be an early innovator in the shareholder value maximization movement of the 1980s and 1990s. The market value of GE rose from $12 billion in 1981 to $280 billion in 2001 (about 23-fold). Welch restructured the GE portfolio (ruling that each business must be first or second in its industry), oversaw a shift from products to GE

Capital and services as the key profit drivers, adopted the Six Sigma quality process, and built a strong management team throughout the company. That Welch is an effective business executive is beyond dispute, although the Welch "formula" described above has not proved automatically transferable to all other business situations.

It is difficult to judge whether Welch is a good leader in the broadest sense because doubts have been raised about the sources of GE's success under Welch, GE's sustainability after Welch's departure, and the ethics of some of Welch's actions. Christopher Byron targeted four well-known CEOs for criticism: Jack Welch of GE, Dennis Kozlowski at Tyco, Ron Perelman at Revlon, and "Chainsaw" Al Dunlop at Sunbeam. The general criticism is personal misconduct and womanizing. Welch reduced the GE workforce substantially and instituted a "rank-and-yank" evaluation system in management. Both steps have been criticized. Whether Welch is successful or simply lucky is also now disputed. Market value dropped roughly in half during the general stock market decline after Welch's retirement. Byron argues that Welch was no more than lucky: He took charge of GE at the trough of the deepest bear market since the Great Depression to that point and remained in charge through the longest bull market in U.S. history. A combination of luck and financial engineering may explain as much as leadership vision and strategy.

A dramatic contrast to Welch's business accomplishments, cited by Rakesh Khurana, is the reported failure of Michael Armstrong as CEO of AT&T. Armstrong came to AT&T from outside in 1997, with 31 years at IBM and 4 years heading Hughes Electronics. On the day his appointment was announced, the firm's market value rose by $4 billion in anticipation of outstanding performance. On taking charge, Armstrong initiated an aggressive acquisition strategy aimed at turning AT&T into an omni-Internet corporation including cable TV and cellular phones. The cost of this strategy was a 10-fold increase in debt from $6.7 billion to $67 billion. Much of the acquisition assets were subsequently divested at huge losses. By December 2000, AT&T had cut its dividend for the first time, and the stock had fallen from a $69 peak in 1999 to $18 (having hit a bottom of $10). On July 17, 2002, the AT&T board announced that Armstrong was leaving to become chairman of Comcast's cable TV business—sold by AT&T at a $13 billion loss.

The Ethics of Leadership

Notorious corporate scandals of recent years have focused attention on the ethics of leadership. Many of these scandals involve criminal fraud by top executives. Stakeholder management unavoidably involves value judgments concerning fairness. The leadership at Enron, Parmalat, Royal Ahold, Tyco, and WorldCom failed this simple standard. The organizational or social cost of unethical as well as just plain ineffective leadership can be enormous. There has been great turnover recently in the top leadership at Boeing because of procurement scandals and personal misconduct.

Arthur M. Schlesinger Jr., Pulitzer Prize winning historian, wrote an introductory essay, "On Leadership," to a series of short volumes titled *World Leaders: Past & Present.* Schlesinger contrasts modern democratic leadership with absolutist tyranny. Means boil down to a choice between "authoritarian" command rooted in the threat of force and persuasion rooted in "democratic" consent of followers. Ends define the purpose for which authority is sought by leaders. Schlesinger uses William James's 1880 notion of leadership as the inspiration and mobilization of masses of people by individuals—a talent James regarded as genius. The thesis is that leadership—for ethical or unethical purposes—transforms history and demonstrates that individuals can make a difference through free choices. This leadership proposition is the antithesis of various forms of historical determinism such as historical inevitability or class determinism. Determinism in any form abolishes the idea of individual moral responsibility and leaves masses susceptible to a cult of leadership. The relationship of leadership and ethics is, however, a matter of continuing dispute.

One school of thought, echoing Machiavelli, argues that leadership is simply a tool for influence. Leadership may be ethical or unethical—servant leadership or power wielding—independently of effectiveness and success. The unethical leader treats people always as instruments and never as ends—the exact opposite of Immanuel Kant's most fundamental principle of ethics. Nevertheless, one can learn useful lessons in effective leadership techniques from the totalitarian likes of Hitler, Lenin, Mao, Mussolini, and Stalin—or Saddam Hussein. On July 18, 1979, on the fifth day of his "presidency" of Iraq, Saddam Hussein held a meeting of more than 300 Baath Party senior personnel. The discovery of a "plot" to overthrow the new regime was revealed, and one of the alleged "instigators"—returned from the torture chamber and promised his life—"confessed" the details. Some 66 individuals were arrested on the spot, and were executed some 2 weeks later. Saddam asked the others to volunteer for service on the firing squads; the confessed "instigator" was executed as an Israeli spy—as distinguished from participation in the plot.

The opposing view of leadership—shaped by the rise of modern democratic institutions—is fundamentally different. In the longer run, unethical leaders tend to become the victims of their own excesses. Leadership unavoidably concerns ethics and values. Ethical (i.e., servant) leadership is influencing others for their own benefit. Ends and means are subject to moral standards. Henry (Lord) Acton emphasized in the late 19th century that kings and popes were not by position elevated above morality and that if not subject to law in their own time, they were subject to historical judgment passed subsequently. The proper task of leadership is defined as improvement of human welfare and is always based on a servant leadership model. Franco Bernabè, the CEO and Ph.D. economist who transformed Eni from a corrupt state-owned Italian energy enterprise into a cleaner and much more effective privatized company, has commented that business leadership is about humanity and morality.

Effective and Ineffective Leadership Methods

Effectiveness connotes strategies and tactics for influence. Every adult has an intuitive understanding of the general meaning of leadership and practical experience of its effects if not its actual exercise through personal authority. Societies, communities, and organizations everywhere generally have leadership functions and roles. A leader is someone "in charge" of or "responsible for" an informal group or a formal organization (or subunit) or spurring an intellectual movement by example if not deliberate intention. The military and police and fire services, the Roman Catholic Church, and corporations have formal hierarchies of command defining who has formal authority to act. The term *leadership* typically appears in a standard dictionary as a variant of *leader* or *lead*. The relevant senses of *lead* include the following: conducting, directing, escorting, or guiding; influencing or inducing; to be ahead of or at the head of; command; example or precedent; principal role; and prerogative to make the first play.

Leadership is the art and science of intentionally influencing others to change behavior, beliefs, or both in some desired direction. Any person leads as he or she influences others in some manner. Such influence may be direct, for example, by command or persuasion, or indirect, through successful example or intellectual development. Leadership is stimulation of followers in some manner: Why and how are the decisive questions. In the approach of Chester Barnard and Richard Neustadt, leadership is influencing others to comply and/or cooperate. Leadership involves both action initiative and acceptance of moral responsibility for outcomes affecting the welfare of others. Leadership skills play a vital role at all levels in an organization—from individual participant at the lowest rank to chief executive.

The leadership process is highly situational, being dependent on the leader, the followers, and the circumstances. A theory of situational leadership, closely related to varying styles of leadership, seeks to link leader (i.e., the influencer) and followers (i.e., the influencees). The theory basically argues that effective leaders must and can vary their approach to situations. One variant of situational leadership theory, associated with the Center for Leadership Studies, focuses on follower readiness for personal responsibility and exercise of initiative in relation to task characteristics to generate a leadership style profile and a leadership adaptability measure. The approach generates a two-by-two matrix in which relationship of leader to follower is high or low and task behavior is high or low. The leadership profile moves from telling to selling to participating to delegating.

The role of the leadership is to direct a group or unit or organization in the absence of a satisfactory science of management. Edward C. Banfield argued, therefore, that preparation for leadership concerns both effective skill development (and skills can be studied) and "wisdom" concerning sound choices (and is more highly dependent on character and experience). An organization is both a system of relationships (*administrative management*) and a system of concrete activities (*administrative tasks*). Banfield suggests four inherent limits on a science of management: (1) Decisions involve unique cases rather than regularities; (2) these decisions are "difficulties" coped with rather than "problems" solved as if they are "puzzles"; (3) management science is descriptive of regularities rather than prescriptive of specific actions and choices; and (4) the descriptions are contingent on circumstances or conditions not controllable by an executive. The essence of leadership is the art of sound judgment concerning goals, duties, future probabilities, and possibilities. Education for leadership is therefore difficult at best. Banfield argues that executive direction of an organization is an art or skill, rather than a matter of technical knowledge, and that sound judgment cannot be taught by case studies. Feel of the situation based on background knowledge and experience is the indispensable knack.

In a 1931 lecture at the Harvard Business School, the philosopher Alfred North Whitehead argued that "foresight" is the fundamental requirement of the businessperson. His definition of this foresight is capacity to develop generalities from details and to anticipate future developments despite insufficient information and changing conditions. This necessary foresight is a function of deep understanding of present realities and future trends. Foresight is unavoidably a creative act of the individual mind, which can be better prepared in advance of a decision situation.

An outstanding example illustrating the issues in defining successful and effective leadership is Sir Ernest Shackleton's escape from Antarctic disaster. Sir Edmund Hillary, conqueror of Mount Everest, has commented that in disaster Shackleton is the man on whom to rely for survival. Success in this disaster meant that Shackleton brought his polar expedition back without the loss of a single man—a criterion for servant leadership and moral character. In doing so, he had to handle a virtual mutiny due to loss of confidence in his leadership and then motivate his personnel to have confidence in survival and his recommended actions. The expedition had the most minimal resources for survival in a harsh environment with no prospect of outside relief. Shackleton (1874–1922) entered the merchant marine at age 16 and advanced rapidly on ability, exhibiting what can be described as dogged determination and audacity, while learning how to lead subordinates. Shackleton, knighted in 1909 for an earlier Antarctic expedition that reached furthest south before Roald Amundsen's successful push to the South Pole, took another expedition south just as World War I opened. In January 1915, his ship, HMS *Endurance*, became trapped in the unusually heavy and early ice—with no radio contact—and then sank 11 months later, first snapped and then swallowed by the ice; the crew abandoned ship in October 1915. Shackleton subdued what amounted to a virtual mutiny over the question of his formal and informal authority to command on loss of the ship, which was ill-designed for ice conditions. One can say that he lacked foresight, in the sense of not anticipating what could go wrong. But he steadfastly instilled discipline, inspired confidence, and ultimately saved everyone. The crew eventually moved northward in lifeboats to Elephant Island. Shackleton then sailed a small lifeboat through mountainous seas to South Georgia Island, and with two companions on foot, he crossed a mountain barrier—peaks to 10,000 feet and unexplored glaciers—from south to north with virtually no mountaineering equipment to reach a whaling station in May 1916. On the fourth attempt, he managed to reach Elephant Island with a rescue ship in August 1916.

A contrast to Shackleton's success is the failure of two commercial expeditions to the summit of Mount Everest on May 10, 1996, when two experienced leaders, Rob Hall and Scott Fischer, and three customers died, and others were seriously injured. Both expeditions summitted well behind schedule and had to descend in the dark through a severe and unexpected blizzard. Foresight was plainly missing. The vital lesson, according to Michael Roberto, is that leadership must always balance competing forces. There were three kinds of interacting adverse effects at work. Cognitive biases in individuals, exacerbated by the effects of low oxygen at high altitude, included the sunk cost effect (escalation to commitment), overconfidence bias, and "recency" effect (recent weather had tended to be favorable). Poor group dynamics led to expeditions that were not effective teams because of lack of open and candid discussions and defective shared beliefs. A fatal problem was the lack of a fixed rule for turning back when running behind schedule. Layered onto cognitive biases and poor group dynamics was system complexity such that the interaction of multiple causes rather than a single cause resulted in tragedy.

The large and expanding literature on leadership is highly diffuse. Much of the diffuseness turns on prescriptions of best practices for effective leadership—especially in difficult circumstances. Some of the diffuseness is due to differences between exceptional leadership and more widely distributed adequate leadership. The functions of the executive are different from what is required by distributed leadership. One of the vital tasks of the executive is to empower others. Another vital task is to cultivate leadership talent and skills throughout an organization. Robert Katz delineated three phases or stages in the career progression of executives, beginning with purely technical competence, moving through human relations skills (i.e., group leadership, peer cooperation and influence, and people insight), and culminating in conceptual skills (i.e., strategic insight and organizational overview).

There are various prescriptions for successful leadership. A couple of examples will serve here. Donald Phillips's analysis of Lincoln's leadership during the American civil war divides the lessons into four sets. One set deals with Lincoln's handling of people addressed through "management by walking around," building alliances, and persuasion methods. A second set describes Lincoln's character in terms of integrity, no malice toward others, willing acceptance of criticism, and tolerance for paradox. A third set on "endeavor" provides specific action recommendations on being decisive, being led by others, being goals and results oriented, and finding "Grant" (a satisfactory field commander who can beat Lee). A fourth set concerns communication of vision (with substantive content) through public speaking, conversation and storytelling techniques, and preaching to reaffirm the vision.

Richard Mahoney, former CEO of Monsanto—responsible for the firm's transformation—suggests six rules for people management: (1) having an attractive and understandable mission or theme; (2) "buy in" by and personal role for "good" people (i.e., possessing competence and character); (3) encouraging what we might term *empowerment*, so there are no excuses for failure; (4) giving financial and psychic rewards for success; (5) punishing recurrent failure; and (6) finding and installing individuals with leadership capability at all key points.

Competing Conceptions of Leadership

Leadership appears to reside in three basic elements of the individual actor: mind, will, and emotional intelligence. The mind can be better prepared, the will can be better tempered, and emotional intelligence can be acquired. Leadership concerns simultaneous interaction or interdependence of several factors. These factors would include strategic foresight and insight, vision or direction setting, character and values, people and political skills, emotional intelligence (EQ), and the ability to vary style according to the situation at hand.

There are three competing conceptions of leadership in the literature. One conception is based on trait theory. In this conception, leadership effectiveness results from personal traits or attributes. Leaders are born, not made. A second conception is based on great events theory. In this conception, great events call upon individuals who may not be exceptional in traits but who respond successfully to circumstances. Leaders emerge from events. The third, and prevailing, conception is transformational leadership. In this conception, individuals can and do learn effective skills of leadership. John Kotter argues that effective leadership skills can be learned.

Dwight D. Eisenhower, Allied supreme commander in the European theater of operations during World War II and then U.S. Army chief of staff and president of the United States, arguably illustrates both traits and styles. As reported by Stephen Ambrose from Eisenhower's unpublished memoirs draft, Eisenhower carefully studied leadership as a skill. Eisenhower became noted in the interwar army as an organizer, planner, and trainer—although he had no combat experience whatsoever, having been in a training command in the United States during World War I. Eisenhower worked for Chief of Staff Douglas A. MacArthur in Washington, D.C., and then in the Philippines. British Field Marshal Bernard L. Montgomery, with whom Eisenhower had many policy and personality clashes, commented nevertheless that Eisenhower possessed great charisma. Fred Greenstein characterized Eisenhower's presidential style as hidden hand, meaning that Eisenhower operated indirectly to exercise influence.

A reasonable linking of these three conceptions is that individuals with strong leadership traits and leadership experience should perform well in great events. That particular linking does not automatically exclude other possibilities. One should distinguish in this regard between competent leadership and exceptional leadership. The former can be learned by virtually everyone; the latter may be partly dependent on innate traits of unusual individuals. Truly exceptional leadership may be in very thin supply relative to demand and need. Exceptional individuals (e.g., Washington, Bolivar, Lincoln, Gandhi, FDR, Mao Zedong, and JFK) arguably supplemented effective skills with valuable and scarce personal traits. Scientifically, it may be less important to establish that leadership is important than to determine when it is important—as a highly contingent practice.

Leadership and Management

Much of the material above has focused on the formal roles of executives and managers in organizations. There is continuing debate in the literature concerning the appropriate relationship between "leadership" and "management." One reason for the debate is that an executive or manager may not be effective at leading, while leadership may arise elsewhere in an organization or community. Another reason for the debate is that the prescriptive theory of leadership has tended to emphasize vision and direction setting as inspirational and motivational tools, in contrast to the arguably more mundane tasks of management, such as budgeting, personnel evaluation, problem solving, and so forth.

Robert Danzig, who rose to general manager of the Hearst Corp., argues that management "skills" can be learned but that leadership "traits" are inherent qualities that can be polished to "powers." He lists first charisma and then perseverance, followed by seven other traits not necessarily in any order of priority: character, energy, enthusiasm, innovation, inspiration (i.e., ability to motivate others), passion, and quality. Norman Augustine, commenting that there is no single style of effective leadership, identifies seven common "qualities": competence, courage, inspiration, integrity, perseverance, selflessness, and vision.

One school of thought holds that leadership is quite different from management. In a business context, the CEO leads; the COO manages. General Colin Powell, former chairman of the Joint Chiefs of Staff and secretary of state, has defined leadership as an art of being more effective and successful than would be predictable in the circumstances from a science of management. The difference lies in the motivation of people to outperform predictable expectations. Another school of thought argues that leadership and management are substantially the same and that indeed the distinction is misleading. The COO leads as well as manages; the CEO manages as well as leads. The dispute is partly bound up with the question of "charisma" and related personal traits—whether leadership is strictly a natural quality or a set of skills that can be learned by virtually anyone.

The first school—that leadership is different and superior—is directed at change in organizations through skills for inspiration and vision. John Kotter treats leadership and management as complementary systems of human action. Leadership focused on inspiration and motivation is concerned mostly with change and transformation, while management focused on command and control is concerned mostly with coordination and complexity.

The contrasting school of thought blurs this proposed dividing line between leadership and management. Henry Mintzberg argues that the distinction is dangerous. The argument is one strand of Mintzberg's critique of business school education. Business schools focus on analysis of functions—to the neglect of management. This focus results in emphasis on technique and formula. Mintzberg argues that the essence of management is the synthesis of multiple, specialized functions into a "vision" or "system" for the overall enterprise. Mintzberg is particularly critical of the notion equating people to "human resources."

"Empowerment" of employees or followers more generally is a popular but arguably ambiguous notion. Chris Argyris concludes that virtually nothing useful about the art and science of empowerment is known. The word "empowerment" has two linked meanings. One meaning is enabling others—with resources, preparation, and opportunities. This meaning suggests that prepared and motivated individuals or groups voluntarily accept responsibility. The other meaning—perhaps more difficult to implement in business settings—is democratic participation, in the sense of increased devolution of authority in a previously hierarchical organization. This meaning suggests that responsibility links to initiative. Empowerment thus connotes both responsibility and initiative. Jack Welch sought during his tenure as CEO to increase responsibility and initiative within the GE management ranks in terms of both enablement and devolution.

Emotional Intelligence

One cannot overemphasize the importance of Shackleton's unflagging confidence in success, an optimism emphasized by Eisenhower in the unpublished draft of his memoirs. Confidence or optimism is an aspect of EQ. Daniel Goleman has been instrumental in spreading the notion of EQ, developed in psychology as the core element of outstanding leadership. If "intelligence quotient" (IQ) is innate, EQ is a learned skill—however difficult learning may prove for a particular individual. EQ is the difference between outstanding leadership and adequate leadership. Goleman conceptualizes EQ as the combination of self-management skills (self-awareness, self-regulation, and motivation) and ability to work with others (empathy and social skills—or ability to influence others). An individual possesses some variable combination of IQ, technical skills, and EQ. Goleman fits EQ to the well-known situational theory of leadership. This theory argues that leadership style is not a function of personality (mood or temperament) but of strategic choice. The high-EQ individual develops the learned ability to vary style according to situation. Goleman suggests six alternative styles: coercive, authoritative, affiliative, democratic, pace setting, and coaching. Mood may remain the primal driver.

Cult of Charismatic Leadership

Rakesh Khurana argues that an unhealthy cult of the charismatic CEO has developed out of the long period of corporate wealth creation during the 1980s and 1990s. This cult is predictable from Schlesinger's comments on leadership, and dictators like Stalin and Hussein cultivate such cults intentionally. In Khurana's view, the cult in business conflates the CEO personally with the success or failure of the firm. Prominent examples cited by Khurana include Jack Welch at GE and Lee Iacocca at Chrysler. At GE, while not to dismiss Welch's contributions, especially in setting the corporate change process in motion, much credit must be given to the 300,000 employees and to the success of GE Capital, headed by Vice Chairman Lawrence Bossidy (who went on to lead Allied Signal and take over Honeywell). Chrysler was saved by a $2 billion federal loan guarantee and United Auto Workers givebacks.

The proper definition of charisma is any special charm or allure that inspires allegiance or devotion. David Hawke, in his biography of John D. Rockefeller, founder of the Standard Oil monopoly, argues that Rockefeller deliberately eschewed charisma in favor of quiet manipulation. Rockefeller was a master practitioner of flattery and clubbiness. He made some calculated decisions to operate with greater subtlety in influence—a variation on Greenstein's description of Eisenhower's approach.

Thomas Carlyle viewed history as largely the activities of "great men" (*Heroes, Hero Worship, and the Heroic in History*)—illustrated in his works on Cromwell and Frederick the Great. For the 19th century, Napoleon Bonaparte was a kind of cult figure. Emerson published profiles of six *Representative Men* including an essay on Napoleon as "man of the world" (the other five were a philosopher, Plato on Socrates, a mystic, Swedenborg, a skeptic, Montaigne, a poet, Shakespeare, and a writer, Goethe). The word "representative" deliberately contrasted with Carlyle's "hero" concept. Napoleon, a commoner, was both despot and inspiration to devoted commoners against the rich and aristocrats. Emerson argued that Napoleon was ultimately indistinguishable from the old nobility. Napoleon's character defects ultimately led to his downfall. Carlyle and Emerson differed in their views concerning democracy. Perhaps in his views of *The French Revolution* and the costs of industrialization, as set forth in *Chartism,* Carlyle was antidemocratic and admired medieval society, as evident in *Past and Present.* Emerson was concerned rather with the possible excesses of democracy, a theme reiterated in modern times about the superficially democratic forms of totalitarianism.

Conclusion

Leadership is the subject of increasing study looking for useful prescriptions. This attention reflects the rising perception that the combination of effective leadership and ethical leadership is crucial to the success of organizations and societies. These concepts are analogous to General Schwarzkopf's ideas of competence and character. Leadership is a process. In today's democratic contexts, success means outcomes for group welfare. Effectiveness means influencing followers for their own benefit. Both ends and means are subject to moral standards. There is a continuing dispute in the literature concerning whether innate traits, great events, or transformational skill development are the keys to effective leadership.

A growing literature draws leadership lessons from various well-known historical figures, such as Alexander the Great, Attila the Hun, and Cortez the conqueror of the Aztecs, and from high-performing athletes and coaches focused on teamwork. Kellerman suggests the following basic works for the student of leadership: (1) Machiavelli's *The Prince* on amoral leadership; (2) Carlyle's *On Heroes;* (3) Freud's works *Group Psychology and the Analysis of the Ego, Civilization and Its Discontents,* and *Moses and Monotheism* on the leader as father figure dominating a social group; (4) Arendt's *The Origins of Totalitarianism* on what is in reality the functional interdependence of tyrant and followers; (5) Barnard's *The Functions of the Executive* on the leader as organizer of incentives for cooperation; (6) *The Federalist Papers* contributed by Hamilton, Madison, and Jay on servant leadership; and (7) Martin Luther King Jr.'s "Letter from Birmingham Jail" and Betty Friedan's *The Feminine Mystique* on the leader as liberator.

—Duane Windsor

See also Accountability; Amorality; Arendt, Hannah; Authority; Carnegie, Andrew; Chief Executive Officer

(CEO); Chief Financial Officer (CFO); Chief Operating Officer (COO); Corporate Governance; Empowerment; Enron Corporation; Ethical Role of the Manager; Grasso, Richard; Moral Leadership; Parmalat; Patriarchy; Rand, Ayn; Royal Ahold Company; Scandals, Corporate; Servant Leadership; Tyco International; Virtue and Leadership; WorldCom

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LEGAL ETHICS

Legal ethics refers to those norms that regulate the members of the legal profession in the practice of law. The concept refers to two distinct yet interrelated kinds of norms: first, those principles and rules specified in the professional codes of conduct and the various statutes that formally govern the practice of law; and second, those moral or public interest norms and principles, not necessarily codified, that *ought* to govern the practice of law.

The first meaning refers to actual ethics codes as well as state and federal statutes that regulate the practice of law. An example of such practical regulation of the legal profession includes the American Bar Association's Model Rules (or some variation on these) adopted by the state bar associations. Practical regulation of the statutory type includes a wide variety of legislatively enacted and common-law adopted rules and procedures governing everything from the treatment of witnesses and disclosure of evidence to the handling of client funds and the confidentiality of client declarations.

The second meaning draws on the relation between the practice of law and the public good. This sense of legal ethics refers to the normative regulation of legal practice toward the creation or maintenance of a just society or the attainment of some public good. For example, when the public good requires the conviction of the guilty, and a lawyer knows that his or her client is guilty, at the very least, the lawyer ought to convince the client to plead guilty rather than run the risk of him or her being acquitted. This obligation runs counter to the practical requirements of both the Bar Association Model Rules and statutory requirements, which specify that the principal duty of an attorney is to provide a vigorous defense of the client's interests.

From this brief consideration, it should be apparent that the practical and the normative regulation of legal practice may not only work at cross purposes (client's private interest vs. public good), but even when their purposes are harmonious, they may demand that the practicing attorney follow incompatible or mutually exclusive courses of action.

Practical Regulation of the Legal Profession

The legal profession is a self-regulating profession. In many countries, the privilege of self-regulation is typically extended to a variety of professional organizations. However, self-regulation does not entail the complete absence of governmental regulation. This is generally true for the practice of law where good professional practice is established through a combination of self-imposed ethics codes and externally imposed governmental statutes or regulations. In the United States, as in most common-law countries, the practice of law is strictly regulated through a combination of individual state bar association ethics codes and state and federal legislation.

For an ethics code to be binding on legal practitioners within any jurisdiction, it must first be approved by the highest court in that jurisdiction. The regulation of the practice of law is typically delegated by the courts to the ethics committee of the state bar association. Each state also governs the professional practice of law through the regulatory mechanism of legislative statute. Each state has statutory regulations governing professional legal conduct and enforces these through various criminal penalties for serious breaches. With respect to the regulation of legal practice, it is the high court that has the final enforcement and punitive authority over legal practitioners. As a result, breaches of ethical conduct by legal practitioners may bring punitive measures enforced both by the legal profession itself and by the courts. Punishment for ethical violations may range from monetary fines or private reprimands, to public reprimands, suspension of licenses, or even prison sentences for gross violations.

The Normative Functions of Legal Ethics

Law and justice have an ancient connection. A failure of law is reasonably understood as a miscarriage of justice. Laws that violate requirements of justice, as, for example, the legally sanctioned though arguably unjust segregation laws of the southern United States, ought to be revised or removed from the statutes. This connection between law and justice is often extended to include the practice as well as the making of law. According to some legal scholars, one of the principal means for justice to be obtained within a given society is to ensure not only that its laws are morally justifiable but that they are employed and enforced in such a way as to ensure that the public good obtains in each case. This is especially so, it is argued, for common-law legal systems, in which precedent plays a central role.

For other legal scholars, the problem of the proper relation of the practice of law to the public good is more complex. Not least among the ethical problems lawyers face are those found in the adversarial system itself. It has been argued by some legal scholars, most notably David Luban and Deborah Rhode, that the practice of law ought to be governed by higher moral standards than those determined merely by client interests. At issue here is a competing view of the lawyer and a more complex understanding of the relation between individuals and the public good. While lawyers typically work for individual clients, the practice of law affects all members of society, not exclusively the affairs of individual clients. Where lawyers act, all are affected. A legal ruling obtained for a client applies to everyone. As such, it is argued, lawyers should always and only act in ways that can be understood as good for everyone, not merely good for the client. This use of one's legal skills entails a special responsibility to ensure that one's professional actions serve the broader public by ensuring that the application of the law is directed toward the public good. In this view, the normative regulation of legal practice by standards assessed in terms of the public good brings the whole legal endeavor closer to justice, in both individual cases and the practice of law generally.

Lawyers' obligation to be guided in their professional conduct by the public good is clearest in the case of prosecutors, public attorneys, and other government lawyers. Even the staunchest proponents of the adversarial method and the obligations of lawyers to advocate zealously for their clients' interests concede that prosecutors and other government lawyers have a special duty to ensure that their professional conduct adheres to broader claims of the public good. The duty of a prosecutor is to ensure that a conviction, once won, is also consistent with the public good, as far as the law will allow and requires. The special duties of prosecutorial and governmental lawyers derive from the special authority inherent in the prosecutor's role as representative and advocate of the state's interest. In democratic systems, the state's interest ought to be directed toward the public good.

This tension between professional conduct under existing practical regulations and professional conduct according to normative principles can be most clearly seen through an example. Consider the lawyer whose client is a major corporation and whose charge is to negotiate a settlement with the U.S. Environmental Protection Agency over allegations of dumping toxins into a nearby river. The children in the neighboring town have developed incurable leukemia as a result of the toxins, and most of the affected families have no medical coverage and no means to ensure their own legal rights. As an advocate of his or her client's interest, the lawyer may feel that in the cause of professional duty the client's interests should be pursued exclusively within the context of the adversarial system. As a fellow citizen, however, the lawyer may feel that his or her duty is to ensure that polluting companies fairly compensate those who are harmed by the pollution.

A similar tension arises in the case where a corporate lawyer must act to secure his or her client's interest in winning a hostile takeover bid for a competing manufacturer. If the client's interests prevail, the corporate board will close the competitor down, maximizing profits, yet laying off hundreds of employees. In the narrower view of legal ethics, the lawyer's duty is to ensure that the hostile takeover succeeds and the client's interests prevail. In the broader normative view of legal ethics, the lawyer may take his or her obligation to be to ensure that the hostile takeover fails or includes provisions to keep the competitor's facility operating. The public good is better served, he or she may argue, when more people are employed in good jobs than when corporate earnings are maximized in each endeavor.

One objection to this understanding of legal ethics is that no lawyer, in his or her everyday practice, can live up to the demand that they advocate for their client's interests *and* serve the public good simultaneously, since the public good is often contrary to the specific and particular interests of the client. In this view, it would be an unreasonable constraint on a lawyer's ability to practice when that practice must always and only be oriented toward social justice or the public good.

Alternatively, for advocates of a narrower normative regulation of legal practice, such as Freedman, a more fitting standard for ethical legal practice would be limited to the zealous defense of the client's interests within an adversarial system of justice. This emphasis on zealous defense within an adversarial system as the best standard for the normative regulation of legal practice firmly embraces the assumption underlying the adversarial system of law: Through the vigorous contestation of individual interests by opposing sides of a legal dispute, the truth of every matter will be revealed and the public good will be achieved. The only ethical challenge, according to this view, would be to ensure fair procedures for contesting competing interests. This position on the relation of legal practice to the public good finds its philosophical justification in legal pragmatism and the legal positivist tradition. In both these views, what makes legal practice legitimate or "right" are the actual standards and rules recognized and accepted by legal practitioners as those that govern their practice. No appeal is made to principles or standards external to the legal system itself, such as the public good or social justice.

According to advocates of the broader normative regulation of law, instances of moral conflict such as those demonstrated in the preceding cases reveal the limits of effective ethical regulation through ethics codes and statutes alone. According to this view, ethics codes and statutes that do not require practitioners to adhere to universal moral principles or standards of the public good are inadequate as codes of *ethics.* The metaclaim underlying this argument is that there ought to be no normative distinction between good professional conduct and good moral conduct. Just as good conduct ought to be aimed toward justice in our everyday relations with others, so also the actions of the lawyer should be guided by the same universal standard of justice. In these and similar situations in which the tension between professional duty and moral duty (understood in terms of the public good) is resolved in favor of professional duty, the worry is that society will be taken further and further from a just and good society, toward one where the law serves the few whose interests are zealously defended at all costs.

Legal Ethics and Business Ethics

What does legal ethics have to do with business ethics? The answer to this question exposes a twofold relationship between the practice of law and the conduct of business. First, the private practice of law is almost uniformly conducted as a business. Either lawyers operate as partners or associates in law firms structured along a corporate model, or they establish their practices privately as individual small-firm owners. Whichever form the business structure takes, almost universally the private practice of law is undertaken as a business enterprise. Exceptions to this business model of the law firm are few and consist of nonprofit public service lawyers, who provide legal services for those who cannot afford their own private practitioners, and government lawyers, who practice law on behalf of the public's interests, as either prosecutors or investigators.

Insofar as the lawyer while practicing law does so as a businessperson, he or she must also be bound by the professional obligations regulating all other business activities. The various Bar Association Codes of Ethical Conduct clearly regulate lawyers in their business practices. Among the business ethics concerns contained in such codes are prohibitions against fraudulent, excessive, or anticompetitive billing practices; regulation of the collection and use of client funds; and prohibitions against conflicts of interest between clients or between clients' interests and those of the lawyers or their firm. When we consider legal practice to be a business in its own right, its practitioners are in many ways no different from businesspersons, entrepreneurs, and corporate managers.

Second, business and legal ethics converge most frequently in the practice of those areas of law that directly regulate corporations: corporate law, tax law, antitrust law, privacy law, and environmental law. Why these areas of legal practice? Corporations are, on one hand, creations of law. It is the law itself that allows the formation and transformation of corporations, defines their rights and responsibilities, and determines their status as legally recognized entities. On the other hand, corporations act in the world; they conduct business by producing, selling, transporting, and acquiring goods. They undertake these activities because they also hire and fire personnel, train employees, manage their workforces, and provide employees with benefits of various sorts. Corporations are regulated by a variety of laws that determine what business they may conduct, how they may conduct it, and for what purposes.

In this way, the practice of corporate law is very much a practice that bridges legal ethics and business ethics. The example provided by the Enron bankruptcy case illustrates the point: Many of the engineers behind the ethically suspect (if not illegal) schemes were corporate lawyers. Furthermore, as corporations are regulated by increasingly complex regional, national, and international laws, lawyers serve as indispensable consultants to the business enterprise. Lawyers in such practices must be attentive not only to the ethical obligations they have as lawyers (legal ethics) but also to the ethical obligations their corporate client may have (business ethics). When we consider that the practice of law is an important part of the regulatory structure of society and that businesses are subject to regulation and legislation that affect their ability to operate, we can see that the practice of law becomes an important element in the normative regulation of business.

—Christina M. Bellon

See also American Bar Association; Association of Trial Lawyers of America (ATLA); Autonomy; Codes of Conduct, Ethical and Professional; Common Law; Confidentiality Agreements; Justice, Theories of; Legal Rights; Professional Ethics; Self-Regulation

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Legal Rights

Legal rights are rights attributed by law. A "right" is an entitlement, which can operate as either an opportunity to do something or a restriction to prevent individuals from interfering with the rights of others. There is a set of rights, considered "natural rights," which are considered universal—that is, they exist in nature—and are not contingent on particular beliefs. In contrast, while there is overlap sometimes between natural and legal rights, this is not always the case; legal rights exist by virtue of the laws that establish them and are not inherently connected to moral rights.

In the United States, the Constitution establishes fundamental rights in its first 10 amendments, called the Bill of Rights. It is here that rights such as free speech and due process are articulated. Additional federal, state, and local legislation sets up other legal rights as defined by each jurisdiction.

While legal rights pertain to individuals generally in civil society, a number of the more significant conflicts arise as pertaining to workplaces and interaction through commerce.

Public/Private Distinction

The protection of rights in the United States is influenced by the so-called public/private distinction. The public/private distinction dates back to the founding of this country. In response to the impositions placed on the colonies by England, political leaders of the newly freed colonies recognized that the formation of a central government over these colonies was unlikely without significant provisions to safeguard the rights of individuals from action by the government. The Bill of Rights thus operates to provide this protection; in fact, its presence played a central role in convincing the colonies to accept a central form of government. In other words, the rights identified in the Constitution are rights that exist vis-à-vis the individual's interaction with the government. This is significant in that it means that these rights are protected only for the individual's interaction with the government—not for his or her interaction with other citizens or organizations.

The public/private distinction is the name given for this because of the view, on which it is grounded, that life can be divided into two separate domains: the "public" and the "private." The public domain exists where the government (or its agents or agencies) is involved; the private domain exists where the government is absent. The primary contribution of this distinction lies in its effect on employment. While the same sort of work takes place in both types of environments, the nature of the employment relationship and the rights that are accorded to employees vary significantly. Employment in local, state, and national government departments and their agencies, considered "public," is governed by the Constitution and the Bill of Rights. Employment in non-government-owned entities, such as for-profit corporations, considered "private," is not subject to the Constitution, Bill of Rights, or many other legal provisions. While the distinction is arguably artificial, it is real according to the operation of laws in the United States.

This means that in determining legal rights in a workplace, it is first necessary to determine whether that workplace is public or private. If the workplace is considered public, it is governed by all the laws in the United States that pertain to the individual's interaction with the state. This means that rights such as free speech and due process apply. If, on the other hand, the workplace is considered private, it is restricted only by that legislation, such as the Civil Rights Act of 1964, explicitly intended to apply to both the public and private domains.

Rights of Corporations

Corporations are fictitious entities, also known as legal persons, created solely by operation of law. They are legal persons separate and apart from their human organizers because the law creates them as such. As a result, they are treated as separate individuals subject to, and entitled to, many of the same legal provisions applicable to individuals. They are not, however, entitled to many of the rights that protect individuals from the government. While the law maintains the fiction of the separate existence of a corporation for many purposes, the distinction can be destroyed if the corporation behaves in a manner inconsistent with the statutory scheme under which it was created. Since corporations are largely creatures of state laws, the manner in which their distinct corporate existence can be destroyed depends on the laws of the particular state in which they are faced with such a challenge.

Jurists have confronted numerous questions regarding the applicability of constitutional provisions to corporations. In many instances, courts have found that corporations are included among legal persons intended to be protected. Rights and responsibilities attributed to corporations tend to correspond to the constitutional protections afforded to human persons. Corporations are not guaranteed protection as human persons, but they are afforded protection similar to human persons. For example, courts have extended protection to corporations for behavior encompassed by the First, Fourth, Fifth, and Fourteenth Amendments.

The due process rights of corporations have been protected, as well as their rights to freedom from illegal searches and seizures. In addition, courts have determined that corporations have citizenship, even though they are not biological individuals. Corporations can also sue, or be sued, in their own name. Perhaps most important, the chief function of a corporation is to provide individual shareholders of the corporation with protection from liabilities imposed on corporations; as a general rule, individual shareholders do not incur liabilities or debts for which the corporation is itself liable absent special circumstances.

Where courts have refused to recognize the rights of corporations, it is regarding provisions such as double jeopardy and self-incrimination, where it would serve injustice, not justice, to treat corporations as legal persons, for these rights are reserved for human beings. Such decisions underscore the meaningful differences between corporations and biological persons.

Litigation

Protecting legal rights in the United States is frequently accomplished through the court system. A person who believes he or she has been aggrieved by the actions or inactions of another may institute legal proceedings to seek a judicial determination of those rights. The plaintiff, or person seeking to enforce legal rights, can force the defendant, from whom the legal right is allegedly owed, to answer in a court of law as to the charge that the plaintiff's legal rights have been abridged. The court, through the judge or a jury, permits both parties to present their case before determining (1) if a legal right exists, (2) if it has been breached, and if so, (3) the extent to which the plaintiff may recover for the failure of the defendant to fulfill its legal obligation.

There is no shortage of litigation in the United States. While many people argue that American society is overly litigious, there is little doubt that civil litigation—a form of settling disputes regarding legal rights—is a much more advanced and appropriate approach to dispute resolution than force. Furthermore, in an egalitarian society in which judicial independence is highly valued, such a system encourages resolution of disputes concerning legal rights in a manner that is designed to be consistent in its disregard for immaterial factors that might otherwise lead to unequal treatment of citizens. Though financial hurdles and practicalities continue to exist, individuals can and do successfully enforce their legal rights against powerful individuals and corporations through a system that is designed to be blind as to the litigants and aware only of the pertinent facts related to the legal rights for which enforcement is sought. Fairness extends in both directions and provides protection to large corporations from juries that might seek a redistribution of wealth based not on a sound analysis of a legal right but on an improper desire to compensate individuals from conveniently available sources of funds.

Conclusion

Legal rights are, therefore, the rights that accrue to human persons and legal persons (corporations) by operation of federal, state, or local law, or by virtue of their interaction in commerce and the common law that has developed to control this interaction. The specific rights that exist often vary depending on whether the employment relationship exists in the public or private sector. Regardless, both individuals and corporations have protected rights by virtue of legislation, and these rights are considered legal rights.

—Tara J. Radin and Steven R. Zahn

See also Americans with Disabilities Act of 1990 (ADA); Civil Rights; Equal Opportunity; Free Speech in the Workplace; Hostile Work Environment; Legal Ethics

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Lemon Laws

A purchaser of a car expects that the car will be free of material defects. Lemon laws have been enacted by all 50 states and the District of Columbia to protect such purchasers when their newly purchased vehicle experiences one or more defects that have not been repaired within a reasonable period. The defects must result in the vehicle not conforming to the manufacturer's warranty to be eligible for lemon law protection. Court cases have concluded that an effective lemon law should reduce the inconvenience and frustration that a consumer faces in a lawsuit. They should provide a method of achieving satisfaction directly from the manufacturer by creating a framework establishing when vehicles should be repurchased or replaced by the manufacturer.

Prior to the 1970s, recourse for purchasers of new cars with defects was available through the Uniform Commercial Code and the legal doctrine of warranty. A warranty is a contractual promise by a seller regarding the quality, character, or suitability of the goods sold to the buyer. A warranty holds a manufacturer responsible, or liable, for the manufacture of a product that is defective. However, many manufacturers provided warranties that were insufficient to restore the vehicle to its proper working condition, leaving consumers without a viable remedy that fully rectified the defect and made the consumer whole after purchasing a vehicle with one or more material defects. In 1975, Congress enacted the Magnuson-Moss Warranty Act designed to protect purchasers from such unfair consumer warranties. This is a federal statute that makes breach of warranty a violation of federal law.

This remedy failed to address all the issues for automobile owners, and by 1981, complaints about automobile dealers were the most frequent complaints received by the Federal Trade Commission. In response, states expanded on the protection provided by the Magnuson-Moss Warranty Act by enacting their own lemon laws specifically protecting the purchasers of cars in each state. The Connecticut legislature enacted the first lemon law, and eventually all the states followed suit. Each state's lemon law varies as to its scope and coverage, but there are similarities among the laws. Early court cases held that the newly enacted lemon laws did not create a new cause of action against the dealer who sold the car but rather clearly placed the liability solely on the manufacturer who built the vehicle in the first place. Since that time, some courts have determined that there is a cause of action against dealerships but not against distributors or private parties. The specific law of the applicable state should be researched if someone is experiencing problems with his or her vehicle, regardless of the seller. There are states that include the sellers of used or leased cars in their lemon law statutes.

If a vehicle makes a clicking noise while being driven, the cigarette lighter breaks off in the owner's hand, or the paint on the vehicle is faded, but it still reliably conveys passengers from point A to point B, the car needs repair but is not a lemon. Conversely, if the car stalls on the way to work, the driver's seat wobbles, or the passenger door flies open, the vehicle may be a lemon. The determination of whether a vehicle is materially nonconforming to the warranty can be based on an objective or a subjective standard. Often, consumers are subjectively dissatisfied with their vehicles, but if the court applies an objective standard, such consumers may not be entitled to relief. States vary as to whether a subjective or an objective standard is applied in determining whether the nonconformity is material.

For a vehicle to be considered a lemon, the manufacturer has to have been given an opportunity to fix the defect. In fact, depending on the applicable state's laws, the manufacturer is allowed three or four attempts to fix the vehicle before it is determined to be a lemon. In most states, 10 different defects during the vehicle's warranty period will not be sufficient to brand the car a lemon under the relevant lemon law statute. Conversely, a single defect is sufficient to trigger lemon law protection, provided the operation of the vehicle is compromised for the statutory length of time.

Asymmetric Information

Automobile purchasers typically possess less information about the vehicle that they are purchasing than the seller of the vehicle. The sellers of vehicles, both new and used, are more likely to be aware of potential problems with the vehicle than the purchaser. This asymmetry of information could cause the market for automobiles, especially used automobiles, to break down. As demonstrated by George A. Akerlof, markets with extreme asymmetric information could simply cease to exist or, at the very least, function poorly. In both cases, the asymmetry of information gives rise to a rationale for the government to intervene to provide a method to obtain a balance of power between the buyers and sellers of automobiles. One of the methods for achieving that balance in the automobile market is through lemon laws.

Structure of the Law

Although each state's lemon laws vary, they tend to be structured similarly. Generally, a vehicle that continues to have a defect that substantially impairs that vehicle's use, value, or safety is considered to be a lemon. The vehicle qualifies as a lemon if it has been repaired for the same defect three or four times required by the relevant state's lemon law statute within the vehicle's warranty period, the repairs have not successfully fixed the defect, and there has been a sufficient period of time for which the vehicle was out of commission. However, application of the foregoing principles differ by state. Current Arkansas law, for example, deems a vehicle with only one unsuccessful repair a lemon, provided that the problem is likely to cause death or serious bodily injury within the longer of 24 months or 24,000 miles. At issue would be the determination of whether the problem is likely to cause death or serious bodily injury within the specified period.

Purchasers that have abused, neglected, or undertaken an unauthorized modification of their vehicle are not eligible for lemon law protection. Unauthorized modification would consist of any change to the vehicle that the dealer or manufacturer did not perform or recommend. For example, if a vehicle was making an annoying clicking noise while driven and the purchaser took it to a shop where the brake system was repaired to stop the clicking noise, the vehicle would no longer be eligible for coverage under the lemon laws.

Some statutes state that if the vehicle is out of service for 30 calendar days it qualifies as a lemon, while others require it to be inoperable for 30 business days. Certain statutes further qualify the time out of service requirement by allowing the 30 calendar days to be nonconsecutive; but they should fall within a particular time or mileage period such as the shorter of 18 months or 18,000 miles. Others give the time period for the nonconsecutive calendar days as 12 months or within the warranty period. Again, it is imperative that the relevant state statute be researched to determine the rules applicable to each consumer's situation.

Documentation and Notification

Determining whether a particular vehicle is potentially a lemon is the threshold requirement to establishing liability under a lemon law. Next, the consumer must protect his or her rights by obtaining and maintaining the proper documentation of the issues and repairs and then notifying the manufacturer of the defect or defects. Frequently, a car is not suspected of being a lemon until the vehicle is out of warranty, at which time it is too late to begin the documentation process. Consumers must retain repair documentation beginning with an initial repair to preserve their rights under the lemon law statutes. Consumers should ensure that they and the repair shop document complaints, and they should retain all receipts. The time that a vehicle is out of commission should be documented precisely to establish applicability of the lemon law statute. Documentation should include notes of all conversations including dates, times, and those involved, as well as odometer readings.

Each state provides its own notice requirements in its lemon law statute. Some states require written notification to the automobile manufacturer, while others are more specific and require notice via certified mail. In any case, it is advisable for the consumer to notify the manufacturer's headquarters and any local office and also to send a copy of the written notice to the dealer where the vehicle was purchased. Under some state statutes, notice to the manufacturer serves to give that manufacturer one final chance to remedy the vehicle nonconformity.

Applicable Vehicles

At their inception, lemon laws applied primarily to the initial purchase of a particular vehicle. This resulted in a situation in which a purchaser of a new vehicle that required 6 repairs of a failing engine was able to obtain lemon law protection, while another consumer who had leased an identical vehicle on the same day with identical engine problems would have no recourse under such statute. Similarly, a purchaser of a previously owned vehicle with 1,000 miles on the odometer and still within its warranty period was also precluded from obtaining relief under lemon law statutes. Some states now include used and leased cars in their lemon law statutes, while other states have separate laws for used vehicles. In addition, demonstrator vehicles under the original warranty are also included in the parameters of vehicles covered under the lemon law statutes of many states. Some states still do not provide lemon law protection for used, leased, or demonstrator vehicles. Motorcycles and motor homes are other products for which some states have provided lemon law protection against defects. However, other state legislatures have chosen to exclude such products.

Motor homes, if protected at all, may be covered by statute only for the nondwelling portion of the home.

Arbitration

In the event of a dispute between the manufacturer and the vehicle owner regarding repair or replacement of a vehicle, most states' lemon law statutes require such disputes to be arbitrated. Arbitration is the process of resolving a dispute or a grievance outside of the court system by presenting it to an impartial third party or panel for a decision. Arbitration under lemon law statutes is usually binding on the manufacturer, but not on the consumer. Typically, it is handled by panels set up by auto companies. Arbitration terms required under the lemon law statutes are typically set forth in the vehicle's written warranty. Several states offer their own arbitration programs for lemon law complaints. State lemon laws have withstood federal constitutional challenges that the statute violated due process by requiring manufacturers to submit to compulsory arbitration.

Governing Law

Due to the mobile nature of vehicles, the issue of which state's laws apply in lemon law disputes has been an ongoing matter of controversy. Courts have held that a vehicle must have been purchased within the state in order for that state's lemon law to apply, while other courts have concluded that as long as the vehicle was registered in their state that state's lemon law could be applied. Additional cases have determined that state lemon law provisions apply as long as the car was either purchased or registered in that particular state. One court even allowed a lemon law action under their state's laws when the repairs had been attempted in that state. Clearly, the law is somewhat unsettled as to who qualifies under each state's applicable lemon laws.

Additional Lemon Laws

Currently all states provide lemon law protection for defective automobile purchases. However, many states have recognized that although cars are one of the most expensive purchases that consumers will make, other consumer products are worthy of lemon law protection as well. Computers represent a significant consumer expenditure, are prone to serious defects, and have become almost as ubiquitous as automobiles. There have also been lemon law statutes proposed and, in some cases, enacted for other consumer products. For example, Arkansas has enacted a lemon law statute for wheelchairs.

—Mary Ellen Wells

See also Asymmetric Information; Consumer Rights; Federal Trade Commission (FTC); Market for Lemons; Warranties

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Lesbian Ethics

Lesbian ethics advocate the creation and maintenance of community among lesbians, independent from male-defined social structures, policies, attitudes, and laws. Lesbian approaches to ethics are varied and do not subscribe to a systematic set of rules but rather support practices that enable women to break away from patriarchal dominance, including patriarchal ethical theories. Traditional ethical theory articulates rules by which men can live together, respecting each other's rights and property, fulfilling duties that accompany particular social roles, and adhering, with some exceptions, to commonly shared norms such as honesty, protection of human life, and promise keeping.

Lesbian ethicists recognize that traditional ethical theory supports the status quo of structures that are sexist, racist, ageist, classist, and heterosexist, to name a few of the isms that lesbian approaches attempt to overcome. Heterosexualism, the embrace of male-dominated social practices and institutions, is seen to validate oppression. For example, definitions of property rights long excluded, and in many parts of the world still do exclude, women from equal consideration. Indeed, women have been and still are more often defined as property than as property holders. Similarly, definitions of justice and "doing what is right" often mirror male traditions of obligations and social norms, such as family honor and filial duty.

The experience of acknowledging oneself as a lesbian often requires women to step outside the bounds of commonly accepted and familiar social relationships with which they have been raised. Even if their immediate families are accepting and understanding of their sexual identity, there are strong social messages of disapproval, condemnation, hatred, and fear. Finding one's own strength and self-acceptance in this milieu is challenging, at best. These common experiences fueled the emergence and articulation of lesbian ethics, which champions truly liberated choice.

Self-understanding is the natural starting place for lesbian ethics, suggests philosopher Sarah Hoagland, because as women fully understand themselves and their relations with others, they open the door to their own agency. One important role for such agency is social transformation. As with all feminist ethics, lesbian ethics expresses a strong commitment to work to create a society that fully supports women's rights. However, lesbian ethics go beyond liberal feminist arguments in seeking a moral revolution to replace patriarchal social structures rather than simply amending them. Lesbian ethics advocate not merely broader support for women but a community in which women, inclusive of lesbians, fully control and shape their lives.

Lesbian ethics are sometimes criticized for spending more time discussing what they aren't and what they are in rebellion against than what they are. There is little discussion of whether the society aspired to by lesbian ethics is one that has room for both hetero- and homosexual relations. In this way, the visions of lesbian ethics are perhaps utopian and incomplete. However, given the reality of heterosexual dominated society, the contribution of lesbian ethics provides a unique opportunity to explore the potential of women's creativity and choice apart from the man-made world.

—Robbin Derry

See also Diversity in the Workplace; Feminist Ethics; Feminist Theory; Gay Rights; Patriarchy

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Leveraged Buyouts

A leveraged buyout (LBO) is an acquisition strategy whereby a company is purchased by another company (typically an investment firm) using borrowed money (bonds or loan). LBOs have played an important role in the restructuring of corporate America in the 1980s.

In numerous cases, LBOs have been used by managers to buy out shareholders (a process then called MBO, management buyout) to gain control over the company (both ownership and decision making), which raises ethical problems of conflicts of interest.

Of the many firms associated with LBOs (such as The Carlyle Group, The Blackstone Group, Forstmann Little & Company, Hicks, Muse, Tate & Furst), the New York City–based private equity firm Kohlberg Kravis Roberts & Co (KKR) is the most well known for two reasons: First, KKR pioneered the LBO approach to buyouts, and second, the most famous LBO in American history was the takeover of RJR Nabisco by KKR in 1988 (for the record amount of $25 billion). The story was later chronicled and popularized in a 1990 book by award-winning journalists Bryan Burrough and John Helyar (*Barbarians at the Gate: The Fall of RJR Nabisco*) and in a 1993 film (starring James Garner), which introduced many readers and viewers to the world of hostile takeovers and financial speculations in corporate America.

Empirical evidence shows that many LBOs, like other types of buyouts, have resulted in significant improvements in firms' performance (using a range of indicators from cash flow to return on investment), which can be explained by a combination of factors including tax benefits, strengthened management, internal reorganization, and change in corporate culture. On the other hand, LBOs, because of the leverage aspect, are controversial because they may cause disruptions and economic hardship in the company purchased: Its assets serve as collateral for the borrowed money, the purchasing company (often a holding whose only purpose is corporate ownership and control) intending to repay the loan by using the future profits and cash flows from the purchased company or, failing that, by selling its assets (i.e., dismantling the company). Besides, LBOs have represented a moral hazard: In the context of the savings and loan debacle of the 1980s, their investors' gains (through junk bonds) were eventually paid by taxpayers. LBOs also raise further issues of ethics, notably about conflicts of interest between managers or acquirers and shareholders, insider trading, stockholders' welfare, excessive fees to intermediaries, and squeeze-outs of minority shareholders (who may well receive a good price for their shares, an average of 30% to 40% more than the market price, but do not eventually benefit from the massive financial rewards of shrewd postbuyout strategies).

The use of LBOs started to decline in the late 1980s for two reasons: First, companies started to develop preventive strategies and defensive tactics (with "poison pills" meant to deter hostile bids, typically giving current shareholders particular rights to buy additional shares or to sell shares with severe economic penalties on the hostile LBO acquirer); second, changes in the legislation made such takeovers more difficult (e.g., with Delaware's merger moratorium law or Ohio's control share acquisition law). The rise of litigations against leveraged bids (for instance with allegations of violations of antitrust and securities laws) also contributed to the dearth of LBOs. At the start of the 21st century, there have been some LBOs again, especially in the high-technology sector, with cable and software companies becoming the targets of private equity firms; if some scholars and specialists predict a new wave of LBOs, it is nonetheless unlikely to be accompanied by the greed and aggressiveness of the 1980s.

—Loykie L. Lominé

See also Corporate Accountability; Corporate Governance; Mergers, Acquisitions, and Takeovers; Savings and Loan Scandal

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Liability Theory

Theories of liability are intended to explicate the conditions under which a party can be held legally responsible for harms to others caused by said party's activities. Harms for which a party can be held liable include personal injury, property damages, and certain intangible harms such as mental anguish and loss of future earnings. Questions of liability occur in many business contexts, including most prominently cases in which a distinct harm is brought about to an individual through the use of a company's product. Theories of product liability provide guidelines for determining the extent and level of redress available to injured persons. By providing consumers with a means of seeking redress for harms caused by unsafe products and companies with an incentive to produce safe products, product liability law can be seen as providing a socially efficient means of addressing issues of product safety. In the United States, the law of product liability generally falls under civil law and is governed by the common law of torts as well as the Uniform Commercial Code. While different theories of product liability have governed the law of product liability in the United States historically, the theory of strict liability is currently applicable to cases involving product liability claims in most jurisdictions.

The theory of strict liability holds that the manufacturer of a product can be held liable for harms caused by the defective nature of that product even if the manufacturer was not negligent in the production of that product. Thus, for instance, under the doctrine of strict liability, a person injured by a defective product need not prove that the company had knowledge of or was at fault for the defect that resulted in the harm in question. According to the standard of strict liability, if the product was defective in a manner that created an unreasonable danger, and this was the cause of the injury at issue, the manufacturers can be held responsible even if they exercised due care in producing the product. Under some circumstances, assemblers, distributors, and retailers of products may also be held strictly liable for damages caused by defective products.

Proponents of the theory of strict liability have offered a number of justifications for the doctrine. On utilitarian grounds, proponents argue that holding manufacturers strictly liable provides them with an incentive to produce safer and more reliable products than they would otherwise. Similarly, proponents of strict liability often maintain that even when neither party is morally at fault for the harms caused by defective products, businesses are better able to bear the costs of injuries than are the harmed individuals. Furthermore, some proponents of the theory have argued that since proving negligence is extremely difficult in cases of product defects, requiring such proof in cases of product liability places an unreasonable burden of proof on the harmed individuals. In this vein, they often argue that when standards of negligence were the rule, a large number of individuals went uncompensated for their injuries.

On the other hand, opponents of the theory argue that the application of the doctrine of strict liability is unfair as well as harmful to the economy. Such critics hold that it is unfair to hold manufacturers responsible for defects in products even when they followed all reasonable precautions in producing those products. Furthermore, opponents claim that the application of the standard of strict liability inhibits product innovation and places a stifling economic burden on businesses as well. In regard to the latter claim, many of these critics point to the increasing costs of litigation and insurance premiums for business firms in the United States over the course of decades, since standards of strict liability became the norm, as illustrative of this problem. As such, in recent years, there has been a push by opponents of strict liability for tort reform in many jurisdictions that includes a return to standards of due care and negligence in cases of product liability.

Though the notion of strict liability is often conflated with that of absolute liability, it is important to note that the two concepts are not equivalent. Whereas the idea of absolute liability precludes all defenses for a resultant injury, the notion of strict liability does not imply that manufacturers must compensate for any injury brought about through the use of their products. For one, as noted above, in order for strict liability to apply, the injury in question must be caused by a product defect, either of manufacture, design, or warranty. Second, claims of strict liability can generally be avoided if it can be shown that the product was substantially altered or used by the injured party in an unintended and unanticipated way. Finally, it is important to accent that the burden of proof clearly rests with the plaintiff in cases of strict liability, as it is up to the plaintiff to demonstrate that the product in question was in fact defective in the manner claimed.

While the theory of strict liability applies by and large to issues concerning the responsibility of businesses for the products they produce, the concept of limited liability is generally used to refer to the liability that the owners of a business have in relationship to the activities of the business itself. The doctrine of limited liability states that the owners of a business are liable only to the extent that they have contributed to the business. A limited liability entity is, thus, one in which the contributing investors or partners can only be held responsible for the obligations of the business to the extent of the value of their investment in that business. Thus, under a limited liability structure, the investors or partners are not held personally responsible for the debts or obligations of the business, and their personal assets are thereby protected. Proponents of the doctrine of limited liability argue that by limiting the risk to individual investors, the limited liability structure encourages investment in business, which is conducive to an efficient economy. In this regard, the rise of the modern limited liability corporation has been seen by many as an essential element in the development and expansion of capitalist economies.

—Daniel E. Palmer

See also Business Law; Common Law; Compensatory Damages; Consumer Product Safety Commission; Consumer Protection Legislation; Corporate Social Responsibility (CSR) and Corporate Social

Performance (CSP); Due Care Theory; Litigation, Civil; Negligence; Product Liability; Shareholders; Tort Reform; Torts

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LIBERALISM

Liberalism is a philosophy, a political theory, a theory of education, an idea in economics, and a religious idea, all of which ultimately are grounded in the liberty of individuals and the free associations they create. Fundamentally, what liberalism values is the liberation of humanity from what liberalism holds are coercive elements of customs and traditions, as well as the authority of class privilege, aristocracy, and coercive ecclesiastical or political power, so that ethical, social, economic, and theological progress is possible. To serve the goal of progress in these areas, liberalism promotes political/legal systems that preserve the liberty and equal dignity of individuals while otherwise limiting governmental restraint, so that individuals and their voluntary associations are free to pursue ends that they hold will contribute to making a better future. Liberalism is a major philosophical, political, and religious current in Western thought and has been, and continues to be, foundational to the West's public institutions as well as many of its social institutions.

The Idea of Liberalism

The idea of liberalism antedates the use of the term *liberalism.* It developed in the philosophical and religious traditions of the West, specifically in one trend in Christian theology and political philosophy, as well as in the humanism of Enlightenment philosophy, which had its roots in Europe's Renaissance and was very influential in 18th-century political thought. Underlying these theological, philosophical, and humanistic trends is the belief that human beings' basic nature is good and that human beings have a tremendous capacity for knowledge and reason, even though that nature and capacity can be corrupted by power or by coercive elements in government and society. When liberated, however, human beings are able to improve themselves and their world continually as they reach toward, even if never ultimately reaching, perfection.

Thus, liberalism's focus is the good that is possible in this world and not the salvation of souls for the eternity of the next. That is, liberalism is a "secular" mode of thought in the original meaning of the word "secular." Originally, "secular" did not mean "nonreligious," as it does in popular discourse today. Rather, "secular" pertained to those things that are time bound and, therefore, not of that other eternal world but are of importance to the "this-worldly" pursuits of the here and now. Consequently, secularism in this sense does not oppose religion, but rather emphasizes the "this-worldly" pursuits of religion and other endeavors. Nevertheless, because liberalism involves liberation of the people and their free associations from governmental constraints and the coercive elements of custom and tradition (including religious traditions and their institutions), liberalism emphasizes the need for government to remain unentangled with religion and vice versa.

Consequently, liberalism holds that government's role is not to constrain human beings in order to limit their potential to sin. That had been the traditional Christian political theory's justification for government's domination of the people in coordination with ecclesiastical authorities. Rather, liberalism promoted the revolutionary notion that human beings can be trusted with liberty. The idea is that even though there may be missteps along the way, when human beings are free, they naturally and ultimately, through experience and reasoned reflection, progress toward human flourishing. This leads in turn to greater and greater degrees of happiness in this world, and ultimately to an unfolding revelation of the true and the good. Hence, change is possible and is good as it can lead to progress toward that better world of tomorrow; that is, the "golden age" is in the future and not in the past.

Theological Liberalism

Although its impulses can be found elsewhere, theological liberalism's first impulse in the West was the liberation of the individual to question the constraints of religious doctrine and authority. Here, religious inquiry, free from outward constraints, turns to inner motivations and the ascendancy of humanity as thinking beings. Thus, human beings use reason as they challenge and are challenged by religious dogma in an effort to discover the essence of faith, an understanding of ultimate reality, and human beings' relationship to God—all with the potential to realize a more authentic faith than that offered by tradition taken only on faith. Accordingly, theological liberalism holds that religion should be interpreted in light of experience as well as the best contemporary reasonable thought.

Although the concept of progress was implicit in these early developments, theological liberalism's later acceptance of scientific developments, such as Darwin's theory of evolution, and the influences of the Industrial Revolution resulted in theological liberalism's more explicit embrace of the notion of progress in the realm of religion. The idea is that through a continuing process of taking account of experience and submitting that to reasoned reflection, human beings produce new understandings and profound experiences. As a consequence, human beings' potential to move ever closer toward God is increased.

Liberalism as a Political Tradition

Although liberalism seeks to free individuals and their free associations from the constraints of tradition, liberalism did not wholly reject tradition. Rather, it spoke from within it to the future where a better world is possible. Therefore, liberalism itself can be thought of as a tradition. One of the first to articulate that tradition in the arena of government was John Locke (1632–1704), a British philosopher who wrote about the potential for human understanding through empirical observation and about the foundations of a governmental structure and political ethic that would ensure the freedom of the people.

Locke's works reveal that it is difficult, if not impossible, to divorce political liberalism from its roots in theological liberalism. In fact, Locke held that reason itself is "natural revelation." Accordingly, Locke's political philosophy begins with basic beliefs about humanity's state of being in the "state of nature." Locke held that human beings are, by nature, free and equal because they are created that way by God. They are free in that their actions are not predetermined; that is, they have free will. They are equal, not in their talents or abilities, but because they have equal dignity before God as God's highest creations. Locke concludes therefore that this natural, God-given state of humanity should be respected to the greatest degree possible when societies and governments are formed. That is, government should not thwart the essential nature of humanity, as God intended, by unduly limiting human beings' ability to exercise their free will or by disregarding the inherent worthiness of all human beings.

Central to Locke's approach was the idea that society cannot fulfill its potential to foster human flourishing and happiness, and ultimately the search for the true and the good in the world, if the people are not free to pursue their own religious beliefs. Each human being is, then, his or her own moral agent responsible directly to God. Hence, although Locke did not advocate tolerance of atheists, religious tolerance for people of all faiths (even Catholics, Muslims, Jews, highly controversial Protestant sects, heretics, and heathens, all of whom were deemed highly suspect by others) was foundational to Locke's articulation of liberalism. This is consistent with liberalism's "secular," that is, this-worldly, focus on improving the political and social conditions through which the true and the good can be pursued.

In turn, Locke emphasized a free and open public forum where, as he stated, "truth" is "left to shift for herself." The idea was that in the process of exchanges in the public forum, the participants, presenting and considering a variety of perspectives, would arrive at new understandings. These then would be tested again as the conversation would progress continually toward better and better ideas about how human beings can flourish as they engage in the search for ultimate truth and goodness in their pursuits for happiness in the world. And if ultimate truth and goodness do not result, at the very least there would be a sort of equilibrium of competing views, thus limiting the potential for any one view to dominate the others.

This "natural law" political philosophy led Locke to conclude that there are two fundamental principles for a government of a free people whose equal dignity is served. The first is that no one may harm another in his or her life, liberty, or property. The second is that the laws of society should be consistent as to every member of society and therefore not be based on the hypocrisy of any custom or tradition that privileges some of the people over others. That is, no one may deny to others what one is not willing to deny oneself—Locke's reversed statement of the golden rule—at least not through the instrumentalities of the state.

Accordingly, Locke held that government should be limited, its purposes being to preserve the people's natural rights, to provide a fair and unbiased judge of disputes (i.e., a political and legal system that serves the people's natural rights), and to ensure the general welfare of the people in a way that does not infringe on the people's natural rights. In this regard, Locke was an early proponent of trade, a free press, and, as already stated, religious toleration, as well as the "just bounds" between government and individual conscience.

Locke's works are the classic statement of liberalism, which became the foundation for political liberation in the West, but were especially influential as a basis for the popular cry for liberty that led to the American Revolution, the Declaration of Independence, and the United States Constitution.

In addition to Lockean "natural rights" liberalism, liberalism developed what is known as "utilitarianism." The general idea is that the moral worth of actions and practices should be determined solely by reference to whether their consequences are "good," which has been defined variously over time. That is, this general idea, known as the principle of "utility," is that the good should be maximized, while the bad should be minimized to the extent possible in any given circumstance. Utilitarianism's early proponents include Jeremy Bentham (1748–1832), James Mill (1773–1836), and John Stuart Mill (1806–1873). The original basic concepts include Bentham's commitment to individualism ("everybody to count for one, nobody for more than one") and the greatest happiness principle (that morality should be based on what produces general happiness or pleasure). In this regard, John Stuart Mill offered the general rule that "actions are right in proportion as they tend to promote happiness, wrong as they tend to produce the reverse of happiness."

These ideas also found their voice in politics and political economy, no less so than in John Stuart Mill's own pivotal and still influential work, *On Liberty*. That work emphasized the sovereignty of the individual over authority (including the authority of the majority) because, he believed, respect for individual autonomy would lead to utility. Although Mill later favored democratic socialism, his work and that of other utilitarian thinkers continue to inspire those who espouse the idea that the greatest degree of social benefits (i.e., social utility) and economic benefits (i.e., economic utility) can be achieved through an ongoing process of exchange among free but interdependent individuals.

As liberalism developed, it became as much a method and a process as an ideal. In other words, it became at once the means to liberation of oneself and one's community from the limitations and coercions of tradition, custom, privilege, aristocracy, and unwarranted governmental restraints, and at the same time the goal of liberation itself.

Liberalism's Schism

Liberal politics gradually took hold in the West. Government was to be reformed so as to ensure the liberty of each individual to as great a degree as possible while at the same time providing the circumstances for respecting the freedom of others. Fundamentally, political liberalism came to emphasize individual liberty, adherence to the rule of law (as opposed to reliance only or primarily on the judgment of designated leaders), representative democracy (with popular sovereignty checked by adherence to individual rights), checks and balances of governmental power, and private property. Individual liberty led, in turn, to the demand for universal suffrage so as to free disenfranchised citizens (e.g., the unpropertied, women, and minorities), so that they too could become full participants in the progression of society. Liberalism also led to the call for universal education so that ordinary people would be capable of exercising their right of popular sovereignty, free from unexamined assumptions, customs, and traditions. Such education was to ensure that the people would have the knowledge needed for them to remain free from the coercive power of a state aligned with society's powerful aristocrats, plutocrats, and religious authorities.

However, liberalism developed a schism in response to some of the effects of the booms and busts of the 19th century's economy and the Industrial Revolution, both of which were believed by the vast majority to have produced severe hardships on masses of people, while the profits of a few grew exponentially. On one hand, there were those who argued that the effects of a political system based on liberty must not only ensure a method and process for the continual enhancement of liberty of action and belief but also be cognizant of the goal of liberty. On the other hand, there were those who held that government's role is to ensure individual liberty but that government should be very limited otherwise. That is, the liberal process should unfold without making corrections to outcomes.

Those who focused on the goal of liberty held that if the method for liberty results in outcomes that are liberty-limiting, then adjustments must be made, and government can be effective in making such adjustments. That is, liberty should not entail only "negative rights," which involve what government may *not* do in order that liberty can be ensured, but should also consist of "positive rights," which involve what government *can* do to promote liberty. Consequently, this thrust in politics led to the call for democratic reforms and "progressive" legislation that would promote not only political reforms, but also economic reforms, as well as reforms in education. John Dewey (1859–1952), who helped organize the American Civil Liberties Union and promoted liberal public education, among other things, was a prominent figure in this movement.

Many argued for a safety net of welfare programs that seek to provide basic economic security because economic security and stability were held to be essential for the exercise of liberty. This view also led to the support of trade unions to balance the relative powerlessness of a nominally "free" laborer with the superior power of a free employer. Overall, those holding this view promoted a stronger government to address such liberty-limiting outcomes.

These trends in "liberal" politics became amplified in a significant American religious movement in the late 19th century and early 20th century: the "social gospel movement." Social gospel movement proponents, in particular their main spokesman Walter Rauschenbusch (1861–1918), held that unrestrained capitalism, which had arisen in the wake of free market economics, thwarts the ability of the masses to prosper through their own labor and, therefore, is unjust. As a result of these social forces, the people are led to despair, and they are steered toward sinful behavior, such as alcoholism, thievery, and prostitution. Consequently, the social gospelers argued in favor of "social salvation" to augment individual responsibility. This took the form of social reforms, which proponents believed would help usher in the Kingdom of God on Earth.

A complementary trend from another direction came from the famed economist John Maynard Keynes (1883–1946) in the early 20th century. Keynes provided an economic theory that challenged the prevailing free market economics of the time. He advocated government intervention at the "macroeconomic" level to address economic anomalies in the market, which he held had produced the economic insecurities of recessions and depressions. Keynes's work was a significant influence on the Great Depression era (1930s) "New Deal" economic policies of Franklin Delano Roosevelt. These economic policies, among other things, resulted in the Social Security system, the Securities and Exchange Commission, and a series of programs designed to provide relief to those most negatively affected by what were widely viewed as abuses by big business in an unregulated market economy.

In addition to concern over potential liberty-limiting outcomes of an unregulated market economy, another complementary trend developed midcentury regarding "distributive justice." Proponents rejected a concept of liberty that favors those fortunate in the distribution of chance characteristics (such as one's innate talents or abilities) or chance social circumstances (such as being born to well-educated and wealthy parents). John Rawls (1921–2002), a main proponent of this trend in liberalism, argued that an economic system that favors the lucky and disadvantages the unlucky is ultimately unjust. In any event, it is not one the people would choose if they considered the matter from the perspective (which he called the "original position") of all others, especially the least fortunate or, in his terms, least advantaged. He argued that distributive justice demands that inequalities in the distribution of society's social goods should favor the least advantaged in society. Another to contribute to this trend is Ronald Dworkin (b. 1931), who has argued that liberty must be framed in terms of the equal concern for individuals who are in unfortunate social circumstances due to no fault of their own.

Conversely, those liberals who focused on a free process (without regard to ends) contended that examinations or corrections of outcomes and limitations on private institutions involve governmental encroachments that limit freedom. That is, liberty was held to be primarily a method, a way to ensure liberty of action and belief, rather than a goal. This approach stands in the tradition of economic liberalism.

Economic Liberalism

Economic liberalism is grounded in the classical statement of liberalism where government is to be limited so as to preserve the people's natural rights, thus ensuring that the people remain free from governmental restraints. Consequently, economic liberalism developed the idea of liberal, that is, free, trade, which further developed into liberal, that is, free, market capitalism.

Economic liberalism, perhaps better termed *liberal political economy*, has its own original proponent: Adam Smith (1723–1790), known as the "father of economics." Smith provided the classic articulation of liberal economics. Smith's idea was as much a moral approach to economic activity as it was a practical one:

Everyone should pursue his or her own self-interest in a competitive environment to produce the greatest good in terms of the wealth maximization of individuals and nations. Smith contended that economic interactions in a free market (which can be viewed as analogous to Lockean liberalism's free and open debate) would lead to overall public welfare. The reason is that it would involve an equitable distribution of wealth, based on the merits of effort, ability, and talent, thus producing an equilibrium of competing interests. The then current system had sustained an entrenched aristocracy of wealth and privilege, which in turn made the poverty of the masses inevitable and unrelenting. The consequence of economic liberalism, however, was believed to be decreased poverty with the result that the masses would not have to resort to immoral behavior (i.e., thievery and prostitution) to survive. Others, such as David Ricardo (1772–1823), later built on this tradition, which has become the prominent approach to economic activity in the West, albeit with modifications of various kinds and degrees in various countries.

The ideas undergirding economic liberalism antedate Smith, however, in that the impulse for economic liberty developed with the rise of the bourgeoisie in Europe. The bourgeoisie were the trader and merchant class that developed a middle way of obtaining material sustenance as against medieval feudal society's serfdom on the one side and aristocracy on the other. Just as many sought reforms that would free individuals from political and religious constraints, the rising business class sought freedom from governmental economic restraints, which severely encroached on the ability to develop economic viability and stability that would not be dependent on others' inherited positions or wealth.

As a consequence, economic liberalism developed as a major component of liberalism. However, when the schism of liberal thought referenced above developed, economic liberalism was in alignment with the view that liberalism is a method for liberation whose wealth-maximizing outcomes are intrinsically fair, and, therefore, adjustments of outcomes are not warranted and ultimately involve an unjust redistribution of wealth. Accordingly, economic liberalism emphasizes individual rights to private property and freedom of contract (regardless of power differentials between bargaining parties) and holds that a loss of economic freedom ultimately leads to a loss of political freedom. From this perspective, governmental interventions for social reasons that promote "positive rights" are inherently counter to liberty and, moreover, have the potential to lead to an authoritarian governmental system.

Friedrich A. Hayek (1899–1992), a main proponent of economic liberalism, argued that attempts to ensure a measure of economic equality through governmental social programs would lead down a "road to serfdom," which liberalism originally had been designed to counter. As a consequence, such attempts would thwart the potential of natural economic exchanges to produce the wealth of nations that liberal economics promised to yield. Following this line of thinking, another main proponent, Milton Friedman (1912–2006), with his wife Rose D. Friedman (b. 1910), argued against government intervention in economic concerns. Among other things, the Friedmans are famous for the argument that the Great Depression was caused by government intervention rather than by the failure of the free market and also for their advocacy of free market approaches to social issues, such as access to adequate K–12 schools. Robert Nozick (1938–2002), who also wrote in this vein, countered John Rawls's ideas about "distributive justice," specifically. Nozick argued that redistribution of wealth is inherently unjust and that an economics of free exchange within a context of equitable laws is just, even if it produces wide disparities in the distribution of wealth.

Liberalism and Education

Although "liberal arts" education may be construed as the means for transmitting the customs and traditions of society, education in the tradition of liberalism, in its strict sense, is education for freedom. First, it is a method that involves free inquiry that questions existing, entrenched modes of thinking and societal institutions whose foundations usually lie in the often blindly accepted "truths" of society's dominant traditions. Liberal education in this sense is not education focused merely on transmitting the learning and information of such traditions, be they philosophical, political, religious, or otherwise. Rather, the goal of liberal education is to use critical inquiry based on reason and experience to examine the prior assumptions and outcomes of such traditions. This is not only to unravel those prior assumptions and outcomes to determine whether they serve the search for the true and the good and ultimately human happiness in this world but also to build on whatever is found there that serves that goal. Second, liberal education goes beyond servile functional education that involves "how-to" mechanical, technical, or professional training for vocational purposes, such as for law or business. Rather, liberal education serves to prepare individuals for full participation in the free and open debate that a liberal society framed by liberal governing institutions ensures.

Liberalism Today

In the West, those referred to as "liberals" and those referred to as "conservatives" include many who are inheritors of the tradition of liberalism. The current struggle between these "liberal" and "conservative" inheritors can be understood as an argument involving two opposing views about the best way to promote the ideals of liberalism. On one hand, "conservative" inheritors of the tradition of liberalism (which includes libertarians in its strictest form) contend that governmental interventions should be severely limited because they always encroach on liberty. This view, which includes economic liberalism, has a tendency toward anarchism. While some hold that tending toward anarchism produces a greater potential to ensure liberty, others argue that such an approach leads inevitably to the rise of a powerful force or forces, for example a new aristocracy of wealth and monopoly or of religious ideology, which inevitably results in the limitation of the liberty of others.

On the other hand, "liberal" inheritors of the tradition of liberalism contend that the role of government is to preserve liberty, which requires government to take corrective action as regards outcomes that limit liberty, such as severe economic inequities. That is, state measures are needed to ensure that social and economic freedoms are available to all. This view has a tendency toward socialism. Some hold that tending toward socialism produces a greater potential to ensure liberty. However, others argue that such an approach leads inevitably to an ever-expanding government, which ultimately limits the liberty of the people as it encroaches on many aspects of people's lives in the exercise of governmental privileges.

Furthermore, the challenges of the liberalism of the mid- and late 20th century to entrenched modes of thought, customs, and traditions, particularly in the realm of education, have resulted in an anomaly. Critics argue that liberal ideology's conclusions regarding things such as the relativity (as opposed to the absolutism) of morality, the virtues of religious pluralism, multiculturalism, secularism, and liberal redistributive economic policies have become entrenched in the ivory towers of our first and finest institutions of learning. The charge comes interestingly from conservative traditionalists, among others, who argue that liberalism has become so ingrained and ensconced in many places in the academy that it has closed the door to open debate, which it originally was designed to ensure. Critics further contend that a significant strain of liberalism has turned its method of critical inquiry on everything, including the philosophical and moral bases of liberalism. This has resulted in the deconstruction of liberalism's own foundations without a counterbalancing reconstruction—to the point where it has begun to undermine its own tradition and, therefore, liberty itself.

In the meantime, conservative traditionalism has rushed to fill what it perceives to be the moral vacuum bequeathed by liberal liberalism. Consequently, conservative traditionalism in turn challenges many assumptions of liberal liberalism. These include the assumptions that religious pluralism, multiculturalism, and secularism equate with liberty and that human beings are inherently good (as opposed to sinful). Accordingly, conservative traditionalism endeavors to stem the tide of what it views as the libertine tendencies of liberal politics, public policy, and education, which do not address what conservative traditionalists hold are fundamental social values in such areas as sexual behavior, marriage, and the beginning and end of human life. In so doing, conservative traditionalism invokes traditional Christian theological justifications for the promotion of public policies, thus challenging liberalism's traditional secular roots and, in turn, the separation of church and state. To confuse matters more, in the United States conservative traditionalism has joined with conservative economic liberalism in a political alliance that some find anomalous in that the ultimate assumptions, methods, and goals of each are at odds.

In the meantime, theological liberalism appears to have lost its voice. Although a new religious "left" has arisen, it bears little resemblance to the original tradition of theological liberalism. Instead, it promotes theological, generally biblical, justifications for a more magnified socialist-trending liberal liberalism. In so doing, it evokes and expands on the social gospel movement of an earlier era, while it, too, strains the "just bounds" between church and state.

All these trends call into question whether the terms *liberal* and *conservative* hold any meaning of substance in today's economic, religious, and political debates.

Overall, it remains to be seen whether liberalism's championing of individual liberty (as against the centralizing tendencies of governmental institutions) can be counterbalanced with public policies that thwart potential liberty-limiting abuses by private institutions (such as powerful and potentially dominating business enterprises, which themselves have centralizing, i.e., monopolizing, tendencies) without undermining liberalism's original "secular" aspirations. Those aspirations were to produce a society that frees human beings to promote human flourishing, seek happiness in this world, and participate in the search for the true and the good to make possible a better world for tomorrow.

—Barbara A. McGraw

See also Absolutism, Ethical; Anarchism; Autonomy; Bentham, Jeremy; Capitalism; Coercion; Communitarianism; Dignity; Freedom and Liberty; Free Market; Free Will; Friedman, Milton; Hayek, Friedrich A.; Individualism; Invisible Hand; Justice, Distributive; Libertarianism; Locke, John; Mandeville, Bernard; Market Socialism; Mill, John Stuart; Natural Law Ethical Theory; Neoconservatism; Nozick, Robert; Nozick's Theory of Justice; Political Theory; Property and Property Rights; Rawls, John; Rawls's Theory of Justice; Relativism, Moral; Smith, Adam; Socialism; Spencer, Herbert; Spontaneous Order; Utilitarianism

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LIBERTARIANISM

Libertarianism is a social and political philosophy in the Western liberal tradition committed to the advancement of personal liberty. It is distinguished from egalitarianism by its views on property rights and the use of force. Although the term *libertarianism* first appeared in political discourse in the 1950s, its conceptual framework was firmly established in the 18th and 19th centuries by political economists and philosophers in the "classical liberal" tradition, most notably John Locke and John Stuart Mill. Despite marginal theoretical disagreement, most libertarians agree that the principles of self-ownership and nonaggression are foundational.

The most influential 20th-century libertarian theorists are in the Lockean deontological (rights-based) moral tradition. Robert Nozick and Murray Rothbard defend liberty via rights, independent of utilitarian considerations. Other recent scholars are in the teleological (consequentialist) moral tradition of John Stuart Mill. Milton Friedman and F. A. Hayek argue that increased personal liberty also produces greater individual happiness and social utility than highly centralized government. In the 20th century, libertarian theory was also shaped by outside influences such as Ayn Rand's objectivist philosophy.

Self-Ownership

For Lockean libertarians, all rights are property rights rooted in John Locke's principle of self-ownership, or the idea that we own ourselves in the same sense that we may own property (natural resources and/or artifacts). Self-ownership limits what others can do to our selves and our property without our consent. Entitlement to property is based on historical principles or how that property was originally acquired. Lockeans argue that initial ownership of natural resources results from a person mixing his or her labor with that unowned resource. So, if we own our selves, then we have a right to the fruits of our labor. The institution of involuntary slavery, for example, is universally morally wrong because it violates the principle of self-ownership and involuntarily deprives individuals of their natural right to what they produce.

Once natural resources come under initial ownership, entitlement to those natural resources and the subsequently created artifacts may be transferred to others, if and only if the contract is informed and consensual. Once legitimate ownership is established, neither other individuals nor the government may coercively seize that property. Most libertarians reject all governmental policies that coercively redistribute property based on some patterned, or preferred, end state such as merit, need, equality, or utility.

Recent debate concerning the original status of natural resources has spawned a form of libertarianism known as "left libertarianism," which, in contrast to "right libertarianism," argues that natural resources are not initially unowned, but owned collectively by society in some egalitarian manner as public property. Therefore, those who want to acquire natural resources must secure consent or reimburse society for their use. Despite scholarly disagreement between left and right, libertarians remain committed to both self-ownership and nonaggression.

Nonaggression

Libertarians argue that nonaggression provides the universal foundation for morality and legality. Unprovoked physical aggression is construed as a violation of property rights via self-ownership. Libertarians follow John Stuart Mill and distinguish between other-regarding acts, which violate the rights of others without their consent, and self-regarding acts, which do not. The inviolable bounds of personal liberty lie within the sphere of self-regarding actions. Self-defense is the only justification for violation of the nonaggression axiom.

Rights impose duties not to kill others or to deprive them of their liberty or property. According to libertarianism, the nonaggression axiom imposes a negative right to life, which posits a duty not to kill others or deprive them of their liberty or their property. There are no positive rights that obligate us to assist others and therefore, there is no "positive right to life." If there were a positive right to life, as some left libertarians suggest, both left and right would agree that it would be more efficiently secured by individual charity and nongovernmental organizations than by tax-supported redistributive welfare.

The nonaggression axiom applies to both individuals and governments. Libertarians disagree over the implications of the nonaggression axiom for the nature and scope of the state as it limits government's ability to raise revenue via coercive taxation or raise an army via involuntary conscription. Most libertarians today are "minarchists," who support limited government that protects citizens (via an all-volunteer army) from external threats posed by aggressive nations and from internal threats (via a criminal justice system) posed by murderers and thieves. Some radical libertarians are "anarchists" or "anarcho-capitalists," who argue that all governments invariably violate the nonaggression axiom or that all governmental functions can be more efficiently served by private individuals, voluntary, nongovernmental associations, and the free market.

Libertarianism, Social Issues, and Global Affairs

Libertarians hold that most social problems are caused by intrusive government and therefore prefer to empower individuals to make their own decisions and solve their own problems. Most are free market capitalists opposed to any government redistributive programs intended to serve the public good, such as urban planning, social welfare, socialized medicine, affirmative action, minimum wage laws, or public schools.

Libertarians resist any attempt by individuals or governmental central planners to coercively impose any one moral or religious view as a legal obligation. Therefore, they stand opposed to restrictive governmental policies toward marriage, birth control, pornography, and recreational drugs. Views on abortion, stem cell research, and cloning are contingent on whether one can reasonably extend self-ownership to zygotes, fetuses, and clones.

In terms of foreign policy, libertarians hold firm to the nonaggression axiom and therefore declare war only in self-defense. In global economic affairs, right libertarians embrace free market economic policies and laissez-faire government, which limits the role of government (national and international) to protecting consumers against theft and fraud. Most are against governmentally enforced monetary policy, protective tariffs, and antisweatshop legislation. Most libertarians say that foreign aid, when appropriate, is best provided by individuals and private nongovernmental organizations rather than by government.

On the contemporary political landscape, libertarians are classified as "social liberals" and "economic conservatives." Their primary critics are communitarians, egalitarians, and utilitarians. Left libertarians hope to bridge the gap between right libertarianism and egalitarianism via a collectivist natural resource policy and, therefore, draw fire from both sides.

—Ronald F. White

See also Anarchism; Egalitarianism; Friedman, Milton; Hayek, Friedrich A.; Liberalism; Nozick, Robert; Self-Ownership; Shareholder Model of Corporate Governance; Statism

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Life Settlements

A life settlement represents the sale of an existing insurance policy to a third party. In a life settlement, as contrasted with other relationships, the third party does not have an insurable interest in the life of the insured: that is, the purchaser does not have an "interest" in the continuing life of the insured in the manner of a traditional beneficiary, who is usually related to the insured (spouse, sibling, child, etc.). Most types of life insurance can qualify in life settlement transactions.

The emergence of life settlements, particularly in light of newer variations that appear to treat insurance as an instrument for financial investment, has generated considerable controversy. On one hand, there is compassion for the types of individuals who have a legitimate need for cash, which they can get by selling their policies to third parties through life settlement transactions. At the same time, however, there is significant concern regarding the commodification of life insurance and the ripple effect across the industry caused by allowing investors to prey on the gap between the prices insurance companies can afford to pay to buy back policies and the value that policyholders seek for this exchange.

Life Insurance

Life insurance is a product of a special nature. Whereas individuals often invest in gifts for one another, life insurance in and of itself is a gift—not merely a product that becomes a gift through types of purchases. The purpose of life insurance is to enable individuals to provide dependents with financial protection on death. Public policies have developed to promote investment in life insurance. Tax benefits, for example, are promoted.

Insurable Interest

Traditionally, according to laws in the United States, an "insurable interest" has been considered a prerequisite for the purchase of life insurance. An insurable interest is an interest held by a beneficiary that offsets that individual's interest in the premature death of the insured, which would result in an early windfall for the beneficiary. In other words, by law, insurance is not sold to strangers, because of the risk that the beneficiary might choose to facilitate an early death in exchange for the financial benefits. It is believed that family members have a deterrent in their affection for their relatives, which is considered "insurable interest"—that is, an interest in keeping the insured alive. Insurable interest is a hedge against beneficiaries trying to cash in prematurely on the commercial value of the insurance.

Market Need

Opportunities for life settlements occur where the insured finds present-day cash more valuable than the anticipated death benefit in the future for the beneficiaries. Through a life settlement, the insured receives cash through the sale of the policy to a third party. Policies tend to include a specified cash surrender value, which represents the amount that the company will pay to buy back the policy. Life settlements are attractive because the value the insured receives through the transaction, while less than the anticipated death benefit, is more than the company's cash surrender value.

Viaticals

A distinction is usually made between a life settlement and a viatical. The latter is traditionally used to refer to financial transactions involving the sale of an insurance policy by an insured who is chronically or terminally ill. Life settlements are typically used to refer to the sale of a policy by an individual who is not ill.

Viaticals are considered the predecessor of life settlements. This instrument emerged in the 1990s as an option for terminal patients, such as victims of AIDS. Through a viatical settlement, the insured is permitted to engage in a sale transaction absent an insurable interest. The reason for viaticals stemmed from the recognized need of these sorts of individuals to be able to access cash, for their investment in life insurance generally antedated their knowledge of their own special medical needs. Providing for their last days supersedes their desire to invest in the future of their loved ones.

Consequences

After the insured sells the policy, the proceeds are the insured's to disperse as he or she deems appropriate. The proceeds of the insurance policy are tax deductible up to the amount already paid in premiums. The remainder of the proceeds are taxed at the individual's normal rate. After completion of the sale, the insured loses all rights and obligations connected with the policy. While the insured is no longer responsible for the premiums, his or her beneficiaries will not receive any disbursement of income from this policy at the death of the insured. The third party—often a firm of some sort—now becomes the beneficiary of the insurance policy.

Concerns arise in that the insured remains connected to the third party through the policy. The third party can require the insured to undergo medical examinations, and that third party can gain access to information about the insured's medical condition and other personal information through ownership of the policy. This raises multiple challenges to personal freedom and privacy.

Controversy

There are several reasons why an insured would be interested in selling his or her insurance policy. These reasons can range anywhere from the belief that the policy is no longer needed or desired to the need for liquid capital to pay for unforeseen costs. Some insured people claim that their premium payments have become too much of a burden or that their estate planning needs have changed since they purchased the policies.

Some people are concerned with the recent increase in life settlements. These people believe that selling a life insurance policy to an individual or institution who lacks an "insurable interest" in the insured results in a challenge to the essential purpose of life insurance and the important role that this financial instrument plays in society. This role has grown increasingly important in this time of declining trust in the pension funds provided by the government and private employers and in the future of social security. Simply put, the purpose of life insurance was to provide financially for the insured's dependents in the event of his or her death. In this way, the purchase and maintenance of a life insurance policy is considered an altruistic act. Resources that the insured could have spent during his or her own lifetime are instead put away to secure the future of loved ones.

Life settlements arguably distort the essential purpose of life insurance when what begins as an altruistic act is turned into a vehicle for investment. This investment becomes particularly attractive since it leverages the tax benefits that the government bestows on life insurance to encourage more people to purchase life insurance. These tax benefits were designed to incentivize actions to relieve the public of the burden of taking care of dependents left destitute by the death of their primary financial support. Life settlements thus jeopardize the tax benefits on which these investments rely.

At the same time, life settlements do fill a need in society that the companies are not able to address efficiently. The fact of the matter is that life settlement firms can afford to pay more than the companies that issued the policies. In many ways, life settlements represent a sort of win-win situation.

The real problem is linked to related instruments that further the distance between the ultimate beneficiaries and insurable interest. Recent years, in particular, have witnessed the proliferation of new instruments that turn insurance into a financial investment instrument. An array of related products exists, all of which share in common eventual stranger ownership of life insurance polices. They are known by acronyms, that is, COLI (company-owned life insurance), IOLI (investor-owned life insurance), STOLI (stranger-owned life insurance), and so on. These are becoming increasingly controversial as their lack of a relationship to insurable interest is challenged.

This is not to say that the only legitimate policyholder is a blood relative. On the contrary, companies have for many years protected their investment in senior executives through what is known as "key man" policies. It is believed that the reliance of the companies on these top executives creates a sort of acceptable insurable interest. What about companies who want to insure janitors? Clearly, janitors do not influence business in the ways that senior executives do.

Conclusion

The future of life settlements remains uncertain. Life settlements continue to serve as an attractive alternative, particularly for aging policyholders. Although companies initially balked at the emergence of this new market, many are finding that life settlements do not represent a significant challenge to how they do business. While concerns are increasing regarding other forms of stranger-owned life insurance, many insurance companies are turning the emergence of this new life settlements market into an opportunity to streamline how they do business. While they are not willing or able to pay policyholders more than the cash surrender value, many appreciate the willingness of settlement firms to step in and assist their customers where they are not in a position to do so. The financial services industry is one that remains committed to customers.

—Tara J. Radin and Julie Anne Ragatz

See also AIDS, Social and Ethical Implications for Business

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Litigation, Civil

Civil litigation, more commonly called a "lawsuit" or "civil action," describes the formal process of resolving disputes between individuals, businesses, governments, and other groups through the court system. It would most likely translate from its Latin roots as "to carry on a lawsuit between citizens." Civil litigation is initiated by one party, called the plaintiff, to protect particular personal or property rights (guarantees enforceable under the law) against another party, called the defendant, who allegedly violated said rights in contradiction of a duty. Litigation seeks to enforce rights by obtaining a court order that precludes violation of said right, in the form of an injunction prohibiting such behavior, or by winning a judgment that compensates one for injury to said rights, in the form of monetary damages. Civil actions commonly involve breach of contracts or harm to personal or real property by an intentional or negligent act. Although other specialized areas of law like bankruptcy, divorce, probate, and tax may technically fall outside the precise definition of civil litigation, they are all considered to be included within it. The previous distinction between actions at law and actions in equity, traced to the separate courts used in England on which U.S. law is based, have been essentially eliminated. Conversely, a criminal action varies from a civil action in that it is brought by government on behalf of the rights of all society (and the victim) that have been violated through the commission of a crime and punishes the perpetrator via fines, incarceration, or even death in some states. Rules of civil procedure regulate the lawsuit process.

Social and Ethical Implications

The costs associated with civil litigation raise serious concerns about its role in society and in business.

Attorney fees, costs for experts and other expenses, and the final monetary judgment, which is sometimes in the millions, even billions, of dollars can have a crippling effect on a business. Lawsuits distract attention from productivity, invade privacy, and harm reputations and relationships. Yet civil litigation appears essential to protect the rights of consumers and businesses alike. Tort reform has been proposed as a tool to limit high judgments that might devastate a business. Adversaries to such reform claim that it will diminish consumer protection rights since without the threat of severe penalties, businesses will not be as conscientious and cautious because they will be able to more easily pass on these lower court judgments to the consumer in the form of higher product prices.

Civil litigation attempts to resolve differences in a manner that protects and promotes business and social relationships. For both to operate effectively, there must be some confidence that personal and economic rights and interests will be protected. Law is a critical component of business since almost every aspect of production is regulated in some fashion. In civil litigation, the courts apply the law, the official designations of the enforceable rights and duties, to the specific circumstances between the parties in coming to a decision or judgment. The term *common law* refers to the judge-made law in written reported decisions. These previous judicial decisions are followed as precedent in guiding current and future decisions under the doctrine of *stare decisis* (let the decision stand). Thus, the litigation process and the law provide a predictability and consistency on which business and social relationships can depend and strategize.

Law, although distinct from ethics, often encompasses social morality within its enforceable legal principles. The protection of rights and enforcement of duties is at the basis of law and of certain deontological ethical systems. In these ways, law is a major influence on and reflection of society's ethics and values. Without the enforcement of morality in the form of lawsuits, many rights would arguably go unprotected and duties unperformed. Law facilitates that moral minimum that society deems necessary to adequately function. Alternative dispute resolution (ADR) is a system to resolve disputes outside the usual judicial system and includes arbitration and mediation, among other components.

The civil litigation (or lawsuit) process includes three different stages that help the court to accurately resolve the disagreement in a fair and impartial manner. These three stages of a lawsuit are generally referred to as pretrial, trial, and posttrial, with very distinct actions occurring during each stage. All are designed, in part, to administer justice, fairly and impartially. A major limitation to such fairness is the access to resources that the different parties have for preparation of their respective cases.

Stages of a Lawsuit

Pretrial

The pretrial stage of civil litigation involves the following activities: consultation with an attorney, filing of pleadings and pretrial motions with the court, discovery of relevant information from the opposing party, and conferences with the judge. Although one may initiate litigation without the representation of an attorney (called pro se), it is uncommon beyond some of the small claims courts. Thus, the party seeking protection of or redress for injury to a particular right usually seeks legal representation from a lawyer (also called an attorney), as will the opposing party in the action. The attorney and client discuss the circumstances giving rise to the dispute and methods to resolve it, including the pros and cons of availing themselves of the court system. If litigation is chosen, the party determines which court system would be both available and advantageous to the lawsuit. The federal and state court systems are the two options. Each court system generally has three levels (some smaller states only have two), although additional courts may be added for special types of cases. For every state, there exist the trial courts (where lawsuits initially begin), the intermediate appellate courts, and the highest or state supreme courts, although a different designation may be used in a few states (e.g., in New York and Maryland, the highest court is called the court of appeals). Meanwhile, the federal court system has U.S. district courts (at least one within every state), 13 U.S. circuit courts of appeals, and one U.S. Supreme Court.

A court must have *jurisdiction* over a dispute (i.e., the authority to render a legally binding judgment) for it to be considered properly before that court. Courts need both *subject matter jurisdiction* (over the type of dispute) and *territorial jurisdiction* (over the person or property involved). *Concurrent jurisdiction* means that both the federal and state courts have the authority to hear and resolve said dispute, which exists when a federal question is at issue or a dispute over $75,000 involves people from different states (diversity of citizenship).

Once the appropriate court has been determined, the plaintiff, the party with standing (i.e., the protected right at stake), initiates the case by filing the necessary written documents with the court, called pleadings. The *complaint* or *petition,* the initial pleading that begins the lawsuit, puts forth why the court has jurisdiction, the facts surrounding the controversy, and the request for a remedy. The court, through a *service of process* and *summons,* then notifies the defendant that he or she is a party sued and named in the lawsuit. The defendant will then file a pleading called an *answer* that responds to the allegations in the complaint, and possibly a *counterclaim* that would list any allegations that the defendant has against the plaintiff. A variety of *motions* (i.e., written or oral requests for the judge to do something in connection with the case) are presented during the pretrial, trial, and posttrail stages of a lawsuit. Motions to dismiss the case for judgment on the pleadings or for summary judgment are the most common at the pretrial stage. The court either grants or denies said motions after allowing both parties to submit their arguments.

As the pretrial stage continues, the plaintiff and defendant use different methods of *discovery* to obtain information about the case from each other. Depositions (oral questions and answers to parties and witnesses that are officially recorded as sworn testimony), interrogatories (written questions to parties that are similarly answered), requests for documents, for objects, or for entry upon land, requests for admissions (to agreed-on facts), and requests for a physical or psychological exam are the primary forms of discovery. The information and method used for discovery needs to be relevant to the dispute and not overly burdensome. For example, requests for examinations would only be appropriate when the physical or mental condition of one of the parties is in question. Pretrial conferences between the judge and parties also occur to simplify the case, to set a trial schedule, to review and rule on any motions, and even to discuss a possible settlement. If the lawsuit is not dismissed in accordance with any motion or settlement, the case will then proceed to the trial stage.

Trial

The trial stage of civil litigation begins with jury selection and ends with a judgment, with opening statements, the presentation of evidence and witnesses, and closing arguments occurring in between. The Seventh Amendment provides the right to a jury trial in a civil case worth more than $20 in the federal court system. The right to a jury can be waived by both parties, resulting in the lawsuit being heard and decided solely by the judge. Jury selection (or voir dire, which means "to speak the truth") involves the questioning of potential jurors by each party's attorney to gauge their adequacy and impartiality for service on the jury. Potential jurors may be challenged and dismissed for cause with the approval of the judge or peremptorily without a reason (these latter challenges are limited in number). For instance, a potential juror who could not be impartial because he or she was a relative of one of the parties could be challenged for cause. The number of jurors required varies from 6 to 12 with additional alternates, depending on the rules and requirements of the particular court.

Once the jury has been seated, the attorneys for each party have the opportunity to give *opening statements,* which provide a limited statement of the facts they intend to establish, evidence to be presented, some reference to the law, and the ultimate remedy that they seek. The plaintiff puts on his case first by calling witnesses to testify in open court, along with any type of documentary evidence or expert witnesses. The courts have rules of evidence that govern what type of information may be presented and how. Even the questioning of witnesses is governed by rules as to the type of testimony (no hearsay, e.g., unless an exception) and the type of questioning (no leading questions to your own witnesses). One party may challenge by objection the admissibility of a question, testimony, or evidence presented by either party. The court either sustains or overrules said objections. The questioning by an attorney of one party's own witness is called direct examination. Opposing counsel then has the opportunity to ask questions during cross-examination. A second round of questioning occurs in the same order: redirect examination followed by re-cross-examination. When the plaintiff is done putting forth the case, the defendant's attorney has the chance to move for a directed verdict (or judgment as matter of law in federal courts) on the argument that not enough evidence was presented to support the plaintiff's case, even though such motions are rarely granted. The lawsuit moves forward with the defendant's attorney similarly presenting witnesses and evidence in support of the defendant's position. After both parties have rested their initial cases, the plaintiff is given an opportunity to offer a rebuttal, and then the defendant receives the chance to dispute new evidence in a rejoinder. *Closing arguments* are then made by each attorney in a manner that highlights essential facts, critical evidence, applicable law, and the reasons for receiving a verdict or judgment in their favor.

In a jury trial, the jury is given *jury instructions* with charges as to the relevant law and facts. The jury's role is to determine the facts and then to apply the law as given by the judge to said facts in coming to a verdict. The jury goes to a separate jury room to deliberate the case. The plaintiff needs to prove his or her case by a preponderance of the evidence, which is the standard of proof in civil litigation (as opposed to the beyond-a-reasonable-doubt standard of criminal cases). There are a few civil cases that require clear and convincing evidence. The jury determines the verdict in favor of the plaintiff or defendant by unanimous vote, unless otherwise allowed by the courts. The jury's failure to reach the required consensus is called a hung jury, which results in a mistrial. The court then prepares to enter a judgment in accordance with the jury's decision. The litigation now moves from the formal trial stage into posttrial activity.

Posttrial

Before the judge enters the final trial judgment, the losing party is entitled to file posttrial motions for a new trial or for judgment n.o.v. (notwithstanding the verdict). The judge may rule in favor of the motion if convinced of error by the jury. A new trial may be awarded due to misconduct by the jury or attorneys, newly discovered evidence, or judicial mistake. In a judgment n.o.v., the judge's decision replaces the jury's verdict based on the judge's determination that the jury's conclusion was unreasonable in light of all the evidence.

The plaintiff or defendant is entitled to appeal (challenge) the judgment or rulings on any pretrial, trial, or posttrial motions. The party appealing the trial court's decision must first file a notice of appeal with the trial court, which then sends all the relevant materials to the appellate court that has jurisdiction over such reviews. Written briefs are filed by each party, by the appellant or petitioner who filed the appeal, and by the appellee or respondent, arguing their respective positions about alleged error of laws made at the trial level (but not about facts or other evidence). Oral arguments by each party's attorney are given before a panel of judges (often three at the intermediate appellate level). After considering the record on appeal, the briefs, and oral arguments, the appellate court issues a written opinion affirming, reversing, or modifying the trial court's decision in accordance with the majority of the court panel. They may also remand the case to the trial court for further proceedings in light of their decision. The written decision may include majority, dissenting, and concurring opinions. There also exists the possibility of appealing the case another time to the next level of courts: the state or U.S. Supreme Court (or even another time from the state supreme court to the U.S. Supreme Court). However, these appeals are discretionary, meaning completely up to the court based on importance and other factors. The losing party appeals to this higher appellate court for a *writ of certiorari* or other similar order, which when issued brings the case up to the court with all its relevant materials. This court then allows new briefs and oral arguments to be presented before rendering its judgment.

Once all possible appeals have been exhausted, the lawsuit is prohibited from being relitigated under the doctrine of res judicata. This allows the successful party to move toward *enforcement* of the litigation judgment. The different remedies include monetary damages (money award), specific performance of a contract obligation, or a temporary or permanent injunction (court order requiring or prohibiting a certain type of activity). Damages may be compensatory, punitive, or nominal. The losing party would pay out of available assets. If the losing party does not pay, then the winning party may need to go back to court to get a *writ of execution,* which directs the sheriff or other authority to seize property in satisfaction of the unpaid judgment.

Conclusion

Civil litigation is essential to the stability of business relationships and social interaction. Without the ability to rely on and enforce certain personal and property rights, such professional and personal relations would be stilted or insecure. Law is also the primary expression of society's ethical and moral values. Although law may only provide society with a moral minimum, its reach into all facets of business and social relationships is extensive. Thus, law informs and influences the behavior of business and of the many stakeholders that constitute society.

—Mark R. Bandsuch

See also Alternative Dispute Resolution (ADR); Business Law; Common Law; Compensatory Damages; Due Process; Negligence; Product Liability; Punitive Damages; Tort Reform; Torts

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Living Wage

A living wage refers to the amount of money a full-time employee needs to either afford the basic necessities in life or exceed the poverty threshold. It is based on the principle that people working full-time should make enough money to financially support their families. Most living wage initiatives are local municipal ordinances lobbied by the American Federation of Labor–Congress of Industrial Organizations and the Association of Community Organizations for Reform Now (ACORN). As of January 2006, 134 municipalities in the United States have legislated living wage ordinances.

Living wage proponents maintain that the minimum wage should lift people out of poverty; but that is not the case in the United States. In 2005, a full-time worker paid the minimum wage of $5.15 an hour would have annual earnings of $10,712. The poverty threshold, determined by the federal government, for an adult with two children was $16,090, equivalent to an hourly living wage of $7.74. More than 30 million Americans working full-time, representing more than 20% of the labor force, earn below-poverty-level wages. Women account for nearly 60% of the total.

Source of the Problem

During the late 1800s, labor unions, socialists, and progressive religious leaders began lobbying the federal government to establish a minimum living wage rate for employees. When President Franklin Roosevelt proposed the first federal minimum wage law in 1938, the guiding principle was a fair day's pay for a fair day's work. His administration initially recommended a minimum wage of 40 cents an hour, but that was reduced to 25 cents an hour to achieve congressional approval. The minimum wage was not indexed to inflation or to a poverty threshold.

The minimum wage's purchasing power peaked in the mid- to late 1960s and has since declined steadily. The current federal minimum hourly wage of $5.15 would be $8.88, had it been indexed to inflation in 1968. Proponents of a higher minimum wage, frustrated with opposition from federal and state politicians, focused their lobbying efforts at the level of local municipalities and particular employers, such as school boards, colleges, and universities.

Advocates invoked the term *living wage* rather than *minimum wage*, because it highlighted the inadequacy of the current minimum wage and had greater moral resonance with the public. Living wage advocates argued that it was unethical for people working full-time to be paid a wage that kept them entrenched in poverty. A full-time job should be a ticket out of poverty, they argued.

Opposition to a Living Wage

Neoclassical economists and many business owners oppose a legally mandated living wage. Arguments against the living wage are very similar to those against increasing the minimum wage. The most common arguments are the following:

- Wages should be determined by labor market supply and demand, not by politicians, government bureaucrats, or voters.
- Cities will lose the valued services of businesses that choose not to pay a living wage.
- Some small businesses cannot maintain profitability with higher labor costs.
- Businesses will have to raise prices for products and services to compensate for the higher wages, leading to local inflation.
- Cities will have to raise taxes to pay for the higher-priced services.
- Businesses will hire fewer low-skilled employees due to the higher wage rates.
- City businesses will relocate just beyond the ordinance's jurisdiction to avoid paying the higher wages, which would reduce the city's or county's tax

base, result in higher taxes for those that remain, and increase local unemployment.

- Businesses within a city paying high wages are at a competitive disadvantage to businesses operating just beyond the ordinance's jurisdiction due to higher labor costs.
- Artificially high wages will encourage some people to drop out of school because of the better short-term economic opportunities.

The latest research has shown that a modest increase in minimum wages does not negatively affect employment levels. However, many of the living wage amounts recently approved by local municipalities, such as Santa Fe's 2006 $9.50 citywide living wage, are substantially higher than the $5.15 federally mandated minimum wage.

Calculating a Living Wage

Living wage proponents typically recommend indexing the minimum wage to the poverty threshold. Some advocates argue that the federal poverty threshold is currently underestimated, so the index should be more than 100%.

In the 1960s, food accounted for approximately one third of an average family's budget, and this became the benchmark for the poverty threshold formula. The federal government annually determines the poverty threshold by multiplying the cost of the minimal amount of food needed to sustain different household sizes by a factor of 3. This formula continues to be used, even though food now accounts for only one fifth of an average family's budget due to increases in health care, child care, and other basic living expenses. If the 2005 poverty threshold for an adult with two children were adjusted accordingly—multiplying food cost by a factor of 5 rather than a factor of 3—a living wage would be $12.89 hourly ($26,811 annually) rather than the current $7.74 hourly calculation ($16,090 annually).

Growth of the Living Wage Movement

The living wage movement originated in 1994 when a coalition of churches and labor unions successfully lobbied the Baltimore city council to pass a living wage that was more than one dollar higher than the federal or state minimum wage. The coalition pursued what they considered to be a politically winnable strategy by limiting living wage requirements to private companies providing city services rather than all city government employees or all employees within the city. They argued that the city government should not contract services from private employers who pay below-poverty-level wages.

Baltimore's living wage, which took effect in 1996, benefited more than 2,000 employees. All private service contractors doing business with the Baltimore city government—firms providing food, health care, maintenance, security, and so on—were required to pay their workers a wage equivalent to the poverty threshold for a family of four, which at the time was $6.10. The Baltimore policy spread quickly to other local municipalities. Milwaukee, Wisconsin, passed a living wage ordinance in 1995, followed by Jersey City, New Jersey, Portland, Oregon, and New York City in 1996.

In 2002, New Orleans residents overwhelmingly approved the first-ever citywide living wage, which was $1 above the federal minimum wage. Exempted from this legislation were city employees and businesses with less than $500,000 in annual revenue. Seven months later, the local ordinance was voided by the Louisiana Supreme Court on the grounds that only states and the federal government had the constitutional right to establish minimum wage laws. By 2006, 134 jurisdictions had enacted living wage ordinances and another 115 were considering them.

Living Wage Ordinance Differences

Living wage advocates have focused on influencing the smallest political unit—namely, local municipalities. In 2005, living wage amounts ranged from $7.73 an hour in Philadelphia to $13.20 in Sonoma, California. The wage differentials are a function of a variety of factors, including regional cost-of-living estimates, what it is indexed against, and health care considerations. Living wage ordinances also differ according to the range of businesses or employees covered.

Range of Businesses or Employees

Most living wage ordinances are aimed at city or county government service contractors. Some ordinances cover all service contractors, while others cover only particular types of service contractors. Exemptions are also made based on the size of the contract (less than $25,000 in Brookline, Massachusetts) or number of employees (less than 10 in Bloomington, Indiana).

Some municipalities have extended the living wage to a contractor's subcontractors (Fairfax, California; Syracuse, New York), nonprofit organizations (Philadelphia; Sonoma, California), and businesses with city leases (Sebastopol, California). Lakewood, Ohio's living wage ordinance applies to any business receiving tax incentives, loans, or other forms of city assistance worth at least $75,000.

Some living wage ordinances also cover city government employees, such as those in Cincinnati, Orlando, Philadelphia, and Sacramento. Efforts are being made to cover a broader range of employers residing within a city's jurisdiction. The Santa Monica, California, city council passed a living wage ordinance in 2001 that applied to all employers in the city's coastal tourist district with annual revenues of more than $5 million.

Indexing Considerations

Local municipalities have indexed living wage rates to minimum wage rates (Philadelphia), the Consumer Price Index (Sonoma, California; Syracuse, New York), and the federal poverty level (Durham County, North Carolina; Lawrence, Kansas; Lincoln, Nebraska). Philadelphia's living wage is indexed at 150% of the minimum wage. In Lawrence, Kansas, the living wage is indexed at 130% of the federal poverty threshold.

Health Care Considerations

Some municipalities establish two living wage rates: one for employers who provide health care benefits and another for those who do not. In Port Hueneme, California, the living wage is $9 an hour if health care benefits are provided and $11.50 if not. In Bloomington, Indiana, employers covered by the ordinance may deduct up to 15% of the $10 hourly living wage if they provide health care benefits. Private contractors hired by Orlando, Florida's city government must either provide a bona fide health program or pay 20% more than the living wage.

Other Employee Benefits

Some living wage ordinances address other employee policies. City service contractors in Oxnard, California, must provide employees 96 hours of paid leave annually. Those in Sonoma, California, must provide 12 compensated days off and 10 uncompensated days off.

Living Wage Expansions and Setbacks

Living wage advocates initially focused on local municipal ordinances because many state and federal legislators opposed increasing the minimum wage. City governments also tended to be dominated by Democrats, rather than Republicans, who were more prone to accept government intervention in the free market system. Initially, local politicians would only support the ordinances if city employees and other key business constituencies were excluded. As a result, living wage advocates limited the scope of local ordinances to companies that had contracts to provide city services. After these initial political victories, advocates lobbied to extend the living wage citywide.

In 2002, Santa Fe, New Mexico's city council enacted a living wage for all service contractors and city employees. The following election cycle, the Santa Fe city council extended its living wage to every business in the city with at least 25 employees, with the wage gradually increasing from $8.50 in 2004 to $10.50 in 2008. Opponents challenged the law's legal standing, but it was upheld by both a state court and an appeals court. In 2003, San Francisco also mandated a living wage for all city businesses with at least 10 employees.

Living wage opponents have lobbied state legislatures and filed lawsuits to overturn these local initiatives. In Wisconsin, the city of Madison passed a citywide minimum hourly wage of $5.70 in 2004. The following year three other cities in the state—Milwaukee, Eau Claire, and La Crosse—did likewise. Each Wisconsin city intended to gradually increase its minimum wage to that of a living wage. However, in 2005, the Wisconsin legislature repealed all four citywide minimum wage laws for violating the state's constitutional right to establish minimum wage laws within its jurisdiction.

ACORN has responded by directing more effort to lobbying federal and state governments. In 2004, voters in Florida passed a ballot initiative to increase the state's minimum wage by $1 to $6.15, an amount still below the poverty threshold. Living wage advocates are choosing hourly wage amounts that they believe to be winnable in elections, though their eventual aim is to index minimum wages to the poverty threshold.

—Denis Collins

See also Association of Community Organizations for Reform Now (ACORN); Capitalism; Just Wage; Minimum Wage; Poverty

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Locke, John (1632–1704)

John Locke was a British philosopher who stands foremost among the founders of what we now call "classical liberalism." His most important teachings on government and economics are set forth in his *Second Treatise of Civil Government,* and they begin from the view that the individual is naturally free, equal, and sovereign and possesses rights to life, liberty, and "estate." From such a beginning Locke concludes that the just powers of governments are limited and derive from the consent of the governed; that labor naturally constitutes a claim to ownership; and that the natural world, without labor, has very little value.

Locke is well known to Americans for having first made the philosophic case for a number of the doctrines that were later presented in the Declaration of Independence as "self-evident truths," and his *Letters on Toleration* advanced the case for religious toleration. In showing what knowledge is, and both its possibility and its limits, Locke's *Essay Concerning Human Understanding* also prepares the way for a fresh look at reigning moral and political opinions.

Whereas many in the West now tend to take Locke's core positions for granted, he faced the challenge of establishing them against once-powerful rivals. He had first, for example, to bury the view that political authority descends by divine right, which he did in his *First Treatise of Civil Government.* With this task accomplished, Locke turned in his *Second Treatise* to argue that people have rights by nature and that they authorize governments only to protect these rights. The individual is clearly prior to civil government, not vice versa.

Like Hobbes before him, Locke began by imagining people in a prepolitical condition, "the state of nature," as a way of exploring and highlighting the relationship between human nature and civil society. Unlike Hobbes, Locke appears to teach that this original anarchic condition is not a state of war, but he nevertheless joins "the justly descried Hobbes" in presenting civil government as the "the proper remedy for the inconveniences of the state of nature." He traces these "inconveniences" especially to the lack of any consistent enforcement of law (for one can possess rights even in circumstances in which they are not likely to be respected) and to the stinginess of nature prior to its transformation by human labor.

Locke makes it unmistakably clear that he cannot abide Hobbes's defense of absolute monarchy, which he calls "no form of civil government at all." Since people create government to escape the perils of the state of nature, they cannot be supposed to consent to the establishment of governments that, granting them no rights or protections, put them in a condition even more perilous than the state of nature. From Locke's emphasis on limiting government to protect the individual, it was but a short step to Montesquieu's defense of the separation of powers as a way of securing these limits.

One of Locke's most novel and influential doctrines is his teaching that there is no private property in the state of nature until someone mixes his or her own labor with something natural: When no one owns something, it is labor that constitutes the decisive claim to possession. Part of this teaching argues that without labor, nature is very stingy indeed, so our original condition was harsh and insecure. The key to a more comfortable existence is to encourage labor, which contains the potential of transmuting nature's stinginess into limitless abundance. Above all, it is the invention of money that makes this possible. Only after people consent to value something imperishable, like gold, does it become reasonable for people to work for more than they need in the short term: No one would farm much land, for example, without the prospect of trading the produce for some durable good. Money liberates human productivity and thus fuels the transformation of our impoverished natural condition. It does so, at least, if people are granted the right to possess money in unequal amounts, and Locke argues that their very consent to give value to money implies consent to the unequal wealth that is its natural consequence.

—*Wayne Ambler*

See also Capitalism; Hobbes, Thomas; Individualism; Natural Law Ethical Theory; Rights, Theories of; Rousseau, Jean-Jacques; Social Contract Theory

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Long-Term Capital Management

Long-Term Capital Management (LTCM) was a hedge fund founded in 1994 by John Meriwether. Meriwether was a well-known bond trader and the former vice chairman at Salomon Brothers. After leaving the firm in 1991 following its Treasury bond scandal, he assembled a group of LTCM principals who were both academics and noted traders. Two such academicians, Myron Scholes and Robert C. Merton, were top economic theorists. In 1997, Scholes and Merton received the Nobel Memorial Prize in Economics for their work in stock options. LTCM began trading after it had received minimum investments from 80 initial investors, approximately $1.3 billion of investor capital. The fund experienced unprecedented growth, with returns as high as 40%, until its demise in 1998.

LTCM used complex quantitative models to determine the timing and estimated return of domestic and foreign bond trades. Also called convergence trades, LTCM sought bonds that were not priced accurately relative to one another. Each transaction realized a very small profit, so LTCM significantly leveraged its trades to make a profit. It would conduct a series of financial transactions that purchased lower priced bonds with long positions while selling short the more expensive, liquid bonds. LTCM used this arbitrage technique to achieve aggressive rates of return.

The Demise of LTCM

At the beginning of 1998, LTCM had equity of $5.0 billion and assets of approximately $129 billion, and it had borrowed $125 billion. In May and June of 1998, LTCM's net returns fell to −6.42% and −10.14%, respectively, reducing its capital by $461 million. In addition, Salomon Brothers, a large stakeholder in LTCM, withdrew from the arbitrage business in July 1998. When the Russian government defaulted on its government bonds in August and September that same year, investors began to panic. By the end of August, the fund had lost $1.85 billion in capital. As a result, LTCM and its investors experienced a "flight to liquidity." In an attempt to transfer assets from a risky market into more secure instruments, they began to purchase U.S. treasury bonds. The Federal Reserve Bank of New York organized a bailout of $3.5 billion to avoid a collapse of the entire financial market. The total losses were estimated at $4.6 billion.

Conclusion

LTCM was responsible for one of the biggest financial disasters of its kind. The founders began amassing investors without thoroughly testing their investment practices in actual market conditions. Liquidity issues were immense, to the extent that without a bailout of some sort, a systemic market crisis affecting all investors would have resulted. The societal implications would have been significant. Before opening the fund to investors, LTCM had an ethical obligation to business and society to test its theories in the markets and to more accurately estimate the liquidity, leverage, and volatility risks.

—*Pamela C. Jones*

See also Arbitrage; Economic Efficiency; Finance, Ethics of; Financial Derivatives; Hedge Funds

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LOVE CANAL

Love Canal, a small community near Niagara Falls, New York, entered into our national memory starting with a front-page story in the *New York Times* on August 1, 1978. In that story, it was noted that Hooker Chemical Company had dumped toxic wastes into the ground up until 1953. The article addressed the incidence of birth defects in children in the area. Lois Gibbs, a resident, became a national spokesperson for all those who lived in Love Canal.

Love Canal was named after a Mr. William Love, who attempted to build a canal connecting two levels of Niagara Falls in 1890. His plan ultimately failed, and the only actual accomplishment was the building of a canal about 1 mile long, 15 feet wide, and 10 feet deep. The City of Niagara Falls began using it to dump chemical wastes as early as 1920, and the U.S. Army used the site to bury wastes from chemical warfare experiments. In 1942, Hooker Chemical Company (an arm of Occidental Petroleum) expanded the use of the site and, in 1947, bought the land for its own use. By 1952, the site was filled to capacity with approximately 21,800 tons of toxic wastes.

The local school board was seeking out new land for school buildings as a consequence of population growth. The school board pressed Hooker for the property and the firm refused on several occasions. The community threatened to take over the land by eminent domain and the firm finally agreed to sell the property for $1. The company warned the community of the dangers of the site, of the risks involved with the toxic wastes, and included a 17-line explanation in the agreement outlining the dangers and transferring all liability for the site to the City of Niagara Falls. This transfer of liability has often been ignored in public comment and debate. In the building of the school, the cap directly on top of the waste site was broken through (several drill bits were broken in the process). This breaking of the cap allowed water to seep into the site and toxic chemicals to leach out into the surrounding area.

Starting in 1978, Lois Gibbs, the then president of the Love Canal Homeowners' Association, led the community effort to obtain information about health concerns and to get redress for the situation. The association was opposed by Occidental and by government at all levels. Eventually, in 1980, as a result of extraordinary publicity, President Jimmy Carter declared it a federal emergency and had the residents evacuated from Love Canal. More than 800 families were eventually relocated and reimbursed for their residences. Occidental Petroleum spent more than $200 million on the cleanup.

This incident was used to further national public interest in hazardous waste sites and led to the passage of federal legislation, commonly referred to as the Superfund, to clean up toxic and hazardous waste sites nationwide.

—John F. Mahon

See also Corporate Issues Management; Corporate Public Affairs; Corporate Social Responsiveness; Crisis Management; Hazardous Waste; Reputation Management

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LOYALTY

Loyalty is a prominent concept in business literature and practice. Discussions of loyalty most often center on employee loyalty to organizations but also include loyalty to particular persons and groups within organizations, customer loyalty to products and brands, and investor loyalty to corporations. Loyalty is generally understood as devotion to a person, group, cause, or ideal. Accounts differ, however, regarding which ethical framework best characterizes loyalty, who is (or should be) loyal to whom, and loyalty's relationship to whistle-blowing, self-interest, and reciprocity. Also of critical concern are situations when one loyalty conflicts with another, and the impact that has on personal integrity.

Loyalty and Ethical Theory

In ethical analyses, loyalty has been characterized as a duty, a virtue, and a complex of virtues. Because it is recognized as devotion to some object, loyalty has also been characterized as a passion—even a type of love—often in combination with duty or virtue. While the designation of its theoretical home may be unsettled, loyalty is arguably linked to all these concepts in that it involves a complex of passions, and loyal persons will perform certain duties and possess certain virtues.

When understood as a duty, loyalty is conceived as an obligation that a person owes to another person, group, or cause. For example, loyalty might be reflected in an employee's duty to maintain trade secrets or a customer's duty to continue purchasing a certain brand. In the business context, the obligation is rooted in such things as reciprocity for pay and other benefits provided by an employer or supervisor; oaths, often in the form of written contracts, in which a person pledges fidelity to an organization; and expectations built over time based on a person's continuing service to an organization or a customer's continuing practice of purchases. For an apparently loyal action truly to be an act of loyalty, however, it must proceed from loyal motives. If loyalty itself is a duty, then it requires an obligation to act from feelings of devotion, not just an obligation to act in certain ways that serve the object of loyalty, and to avoid acting in other ways that fail to serve it. For example, honoring a nondisclosure agreement would not reflect loyalty if it was motivated by fear of reprisal rather than devotion to an organization or particular members of it, and continuing to purchase a particular brand would not reflect loyalty if the customer planned to change as soon as an alternative became available.

The importance of motive in discerning whether actions are truly loyal leads many scholars to view loyalty as a virtue rather than as a duty. Loyalty can be found in various contemporary catalogs of virtues, in which it is often described in Aristotelian fashion as the golden mean between the extremes of disloyalty and blind loyalty. Some virtue theorists, however, contend that loyalty is not a typical virtue, because it involves more than one character trait, unlike classic virtues such as courage or temperance. A loyal person would need to be courageous, trustworthy, and cooperative, among other things, and so need to possess several virtues. Thus, these scholars view loyalty as deserving special classification as a "super virtue"—distinct but necessarily working closely with several "standard" virtues.

Even the "super virtue" designation may be insufficient, however. Focusing on motive leads some scholars to describe loyalty as a passion in relation to corresponding virtues and duties but not as a virtue or duty in itself. Rather than the traditional one-to-one correspondence between passions and virtues (or vices), loyalty contributes to multiple virtues (and possibly vices) and obviously to a multitude of ends. Because loyalty extends beyond the self to some object of devotion, it is a social passion, and even a type of love. It is this passion that motivates people, shaping their characters and leading them to engage in certain actions.

Self and Other

Whether understood as a duty, virtue, or passion, loyalty extends beyond the self to some object of loyalty, creating a strong attachment between the self and this other. These attachments, in many respects, define individuals and their own sense of self. In interpersonal loyalties, such as might be seen between coworkers or between an employee and a manager, attachments can take the form of personal relationships and become quite strong. When considering attachments to larger groups, the level of intimacy is less and clearly decreases in relation to a group's size. In these cases, the attachment is a more general sense of membership rather than relationship, and it is this sense of membership that provides the basis for loyalty, linking individual identity with that of the group. To be loyal, an employee would need to feel like a part of the organization through a matrix of relationships and identify himself or herself with the organization, typically with a positive association. A sense of membership minimizes the psychological compartmentalization or segmentation that often happens when there is a profound separation of the workplace from the rest of one's life. Within very large organizations, however, the sense of attachment necessary for loyalty may be more readily achieved among smaller groups and, even then, only for a limited period of time (e.g., the duration of a shared project). Organizational size, thus, may diminish the possibility for loyalty to corporations as a whole but not necessarily to individuals and smaller groups within them. There are, of course, different possible levels of membership in terms of commitment and identification (not necessarily in terms of job status), and the degree of loyalty would vary with them. Other types of business loyalties would also be based on relationships with individuals or some sense of attachment to the larger organization or its products. For example, customers may develop affective ties with particular sales managers or associate a particular brand with their own sense of identity.

This emphasis on attachments to others stands in stark contrast to the common focus on self-interest in business because loyalty apparently calls for individuals to sacrifice their interests for the sake of others, as opposed to seeking their own good. It is a mistake, however, to associate loyalty primarily with self-sacrifice, because the objects of loyalty are a critical part of a person's self-identity. While loyal people often do sacrifice various interests, their time, and sometimes even their lives to serve some person, group, or cause, loyalty is not strictly altruistic. The loyal person's self-interest is tied up with that of the object of loyalty. Something is not strictly in the interests of a company, boss, or coworker, but also in one's own interests. Loyalty is not simply a matter of sacrifice for others, although loyal individuals may make sacrifices. They do so, however, for themselves and their interests in conjunction with the interests shared with others, not strictly for others and interests that are external to the self. Personal investment gives individuals a stake in the object of loyalty. The necessary dichotomy between loyalty and self-interest is a false one as long as self-interest is not narrowly construed. Loyalty involves self-interest, broadly conceived. Nonetheless, it does not necessarily involve reciprocity. The loyal person may not necessarily receive any benefits directly. Instead, he or she may simply be satisfied with serving a group or cause and contributing to its success.

Objects of Loyalty

Loyalty is devotion to a particular object; but it is arguably a duty, virtue, or positive passion only if its object is worthy of such devotion. If the object is unworthy, then devotion to it is a form of blind loyalty and so is a vice or a negative passion. A knowingly corrupt colleague, boss, or organization would be unworthy of loyalty, and so devotion to such objects would receive negative moral evaluation. Loyalty thus requires good judgment. This crucial judgment about objects is a different sort of judgment from what is usually associated with virtues. Typically, the possessor of certain virtues, for example, courage and temperance, does not judge whether or not to be courageous or tempered. Rather, he or she judges how best to display courage or temperance in particular contexts. Here, the individual must decide whether or not to be loyal. Even after judging the end as good and worthy of loyalty, however, one must still consider the particular means by which one demonstrates loyalty. The second form of blind loyalty is using unethical means to serve good ends. Recognizing an end as worthy of loyalty does not license any means of serving it. Furthermore, one can sometimes remain loyal to the object by rejecting the typical means of being loyal. For example, raising objections to, or refusing to follow, a boss's directive because it would be detrimental to a project or to the organization could indicate loyalty to a larger goal or group.

Of particular interest in the business ethics literature is whether corporations are ever proper objects of loyalty and so whether employee loyalty is ethical or even prudent. The answer to this question very much depends on one's understanding of corporations. Viewing the corporation as essentially an instrument or bureaucratic institution focused solely on financial performance generally leads to finding loyalty inappropriate. Viewing corporations, at least potentially, as teams or communities where there is a sense of membership and shared values leads to discerning whether a particular corporation is worthy of loyalty. Some corporations may be worthy whereas others would not.

Loyalty and Personal Integrity

The business context is not, of course, the only place where loyalty can be found. People are loyal to other persons, groups, and causes, and these loyalties are also part of their identities. Loyalties to family, friends, religion, town, country, coworkers, and corporation, among others, may happily coexist with one another but likely will compete, at least periodically if not more often. When they do compete, one is forced either to balance the competing loyalties in some fashion or, in extreme cases, to choose between them. In extreme cases where one or more other loyalties outweigh loyalty to coworkers, boss, or corporation, whistleblowing can be an appropriate response.

Integrity, a personal sense of wholeness, is important to the task of balancing one's loyalties and the potentially painful task of choosing between them. That is not to say that all loyalties are equal and so must receive identical treatment; some undoubtedly are more important than others. Generally speaking, business loyalties should be less than some loyalties, but perhaps more than some others. This balancing must be worked out in concrete cases, however. It is only then that a person of integrity can discern which loyalty takes priority.

While the need for such balancing or choosing may cause one to question the desirability of loyalty in business, the inability to have loyalty in the business context itself can damage a person's integrity. The impossibility of loyalty would make for a divided self and could potentially compromise one's other loyalties to religion, family, friends, and so forth.

—George D. Randels Jr.

See also Altruism; Fidelity; Integrity; Reciprocity; Self-Interest; Stakeholder Responsibility; Virtue; Whistle-Blowing

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M

MACHIAVELLIANISM

Machiavellianism refers in common parlance to the ready and systematic seizing of every advantage for oneself without regard to the rights or claims of other individuals or of the larger society. The Machiavellian is scornful of claims of conscience or morality and is restrained only by the need to be careful about breaking laws and violating mores, lest one get caught, not by any belief that a profitable action can be wrong. In the business world, the Machiavellian is prepared, as needed, to cook the books, advertise falsely, cut corners on product quality, sell pirated goods, and—where possible—cheat employees or damage the environment. In politics, the Machiavellian will add military force to weapons used in the quest for every advantage, fair or unfair.

Machiavellianism gets its name by association with the most notorious of the chief maxims associated with the Florentine philosopher, Nicolò Machiavelli (1469–1527). Machiavelli was the author of plays, poems, a sweeping history of his native city, a dialogue on warfare, and two of the most arresting works of political philosophy ever written. As happens with most "-isms" added to the name of a great thinker, Machiavellianism inevitably entails a dilution and distortion of his thought.

Machiavelli stated quite openly that his moral and political teachings were radical, and he even likened the novelty of his discoveries to those of the explorers who were in his day discovering unknown seas and continents. What he discovered, as he put it in *The Prince*, is to base thoughts and actions not on how people ought to live but on how they actually do live. His stated reason for so changing the foundation of ethics is that otherwise one achieves ruin rather than preservation. Machiavelli here presents himself as the ultimate realist in a world populated by naïfs, so it is no surprise that the naïfs would counterattack and denounce him as an enemy of morality: Machiavellianism is a pejorative term.

Machiavelli contributed to the emergence of Machiavellianism by cultivating the art of expressing shocking propositions in very crisp phrases (such as "Men are quicker to forget the death of a father than the loss of a patrimony," "It is better to be feared than loved," or "A prince never lacks legitimate reasons to justify breaking his word"). Furthermore, he often amplified such memorable maxims by illustrations, and this helped solidify his reputation as a teacher of evil. A favorite example is that of Cesare Borgia, whom Machiavelli describes as first appointing a certain thug to terrify a turbulent part of his domain and then, once his henchman's severe punishments have brought the population into submission, having him chopped into pieces in the town square. Machiavelli's apparent enthusiasm for Cesare Borgia's stunning use of treachery and murder not surprisingly helps cast Machiavellianism as the ultimate in the cynical rejection of moral decency for political gain.

Since people commonly turn their moral outrage against those still alive and threatening, however, the term as commonly used has become diluted: It is applied in newspaper pieces to annoying political opponents who strike one as unscrupulous. Standards have slipped even here. William Shakespeare's Richard III would be a better example of what Machiavellianism requires, for he did not scruple to kill, deceive, or otherwise dispose of all those who stood between him and the throne, young children included. And yet he failed. Machiavelli wrote not to encourage evil but to foster success.

Although Machiavelli himself never quite used the phrase, and although variants of it were used well before him, "The end justifies the means" is the maxim most associated with Machiavellianism. When taken somewhat literally and used defensively, this maxim is invoked to suggest that an important result or end excuses an action one would otherwise condemn. It is true, one might say, that deceit is reprehensible, but political necessities can be pressing. Perhaps a little lie is needed to defend against an expected attack. In this case, the legitimate end of defense is thought to justify the lie that secures it. When Machiavelli is defended, he is so especially on the grounds that he knew well what it took to secure political stability and republican government. After a millennium with little of the former and none of the latter, such knowledge was precious.

But Machiavellianism implies strong disapprobation, and when "the end justifies the means" is used as an attack, it implies the charge that someone holds *any and every means* to be justified by his or her ends, that someone shows no hesitation to employ means that are outrageously shocking and does so for an end that is simply unworthy. Perhaps all governments sometimes must cut some moral corners, but the so-called Machiavellian ruler is not scrupulous about minimizing such occasions. True, the non-Machiavellian ruler admits: Defense and order cannot always be secured by, say, the principles of the Sermon on the Mount. But should all ethical restraint therefore be abandoned? And if exceptions must sometimes be granted for national defense, must they be granted as well for imperial aggrandizement or for the advancement of a party or individual?

It is partly its generality that makes "The end justifies the means" a blunt instrument for moral analysis, for it is important to distinguish among different ends and means. But it is also important to ask whether certain actions can properly be considered to be means at all. Is compassion, generosity, or honesty properly considered a "means"? Does the anti-Machiavellian not consider these to be characteristics or virtues that are good in and of themselves?

However much a vulgarization of Machiavelli's thought, Machiavellianism does help identify these important questions: Should actions be judged by some intrinsic quality, or by their effect? Is honesty, for example, a virtue or a policy? Should it be encouraged because it is useful or because it is admirable? And if there are virtues that deserve our admiration as ends in themselves, what is their relation to the requirement of success in business or politics?

—Wayne Ambler

See also Human Nature; Individualism; Virtue; Virtue and Leadership; Virtue Ethics

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MacIntyre, Alasdair (1929–)

Alasdair MacIntyre, whose work revived virtue ethics, placing it in the mainstream of contemporary philosophical discussion, was born in Glasgow and received his M.A. from the University of Manchester. He has held a number of university appointments in both the United Kingdom and the United States, including Oxford, Vanderbilt, and Duke, and is currently Senior Research Professor of Philosophy at the University of Notre Dame.

MacIntyre's philosophical work encompasses a broad spectrum, but he is primarily known for his work in ethics. He believes that the study of ethics must be interdisciplinary, using the insights of the social sciences, since morality cannot be adequately understood in isolation from particular societies. His most influential work is *After Virtue,* in which he argues that morality in the modern world consists of a series of fragments from disparate and often contradictory traditions. MacIntyre calls for a return to an earlier understanding of morality based on the virtues. Virtues are stable character traits, such as courage and integrity, that help a person to live a life that promotes human flourishing. People develop virtues in the context of particular practices. A practice is a cooperative human activity (such as chess, farming, or medicine) through which human beings gain goods internal to the practice. Internal goods, as opposed to external goods such as money or status, can only be gained from participating in a practice, and are discovered by identifying the ends essential to that practice. In medicine, for example, an internal good is helping a sick person in need.

Practices have histories that form various traditions. At the broad level of societal practice, morality makes sense only within a particular tradition with its own view of the proper ends of the good human life. There can be no coherent tradition-independent morality. MacIntyre denies that this leads to relativism. In *Whose Justice? Which Rationality?* he argues that although there is no tradition-independent rationality, there are criteria through which individuals can compare their own tradition with another to determine which one is superior. MacIntyre believes that the tradition arising from Aristotle and Thomas Aquinas is better than the alternatives, a view he develops in *Three Rival Versions of Moral Inquiry.*

MacIntyre's views on business ethics reflect the position that modern corporate culture has helped fragment human life into multiple, often self-contradictory, roles. For example, business managers must necessarily focus on efficiency in running a corporation, but these same managers would not have such a focus in their family lives. An emphasis on efficiency may also conflict with long-term goods for society (e.g., a clean environment).

Despite MacIntyre's skepticism about corporate culture, ethicists such as Robert Solomon who hold a positive view of corporate culture have applied virtue ethics to contemporary business. Solomon understands business to be a practice in the MacIntyrean sense, and discusses the way virtues, such as friendliness, loyalty, and shame, can help stakeholders gain what he terms the goals internal to business.

—Michael Potts

See also Aristotle; Virtue; Virtue and Leadership; Virtue Ethics

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MAJORITARIANISM

Majoritarianism is the advocacy of the idea that the majority of the population should have the final say in determining the outcome of public policy (e.g., there is a movement aimed at making the English language not only the national language of the United States but the only language used in public). There are, of course, various ways of "slicing up" the population that would give different identities to the majority.

Majoritarianism must be distinguished from majority rule. In a political system that operates through majority rule, the ultimate power on matters of public policy resides with the vote cast by more than half of those eligible to vote. The majority of those eligible to vote is not identical with the majority of residents in a country. It is conceivable that the views of the majority of the population may be expressed in some instances by other institutional arrangements or persons designated to speak on behalf of the majority.

From the time of classical Greek philosophers such as Plato and Aristotle down through the 18th century, including the founders of the United States such as James Madison, majoritarianism has had a pejorative connotation. It was routinely presumed that the majority of the population was constituted by the poor and the ignorant. It was also presumed that the majority, when given the power and opportunity to do so, would tyrannize over any and all minorities. The latter view was of great concern in the 19th century to J. S. Mill and Alexis Tocqueville, the latter of whom coined the phrase *tyranny of the majority.*

Starting in the 18th century, majoritarianism began to acquire a positive connotation. To begin with, it was argued that any individual or group less than the majority was also capable of tyranny. The classical view that only some individuals had the intellectual and moral virtue that enabled them to determine the common good as opposed to the interests of a particular faction was challenged by the Enlightenment view expressed by Jean-Jacques Rousseau and others that through proper education everyone is capable of making that kind of decision.

There are four important issues raised by majoritarianism. First, is the purpose of majority rule a negative formality to block tyranny by one faction or is it a positive way of arriving at an objective social truth? That is, is the social good a set of procedural norms for protecting the independent interests of individuals (Madison) or is there a social good that substantively encompasses all individual goods (Rousseau's "General Will")? Second, can the interests or rights of minorities (including individuals) be protected through formal legal and political structures (e.g., a constitution) or can they be protected only through some shared cultural values at some other level? Third, is majoritarianism a concept that applies only on the political level or does it permeate every institution? For example, should religious organizations have authoritarian structures or should they have democratic structures? Is the purpose of a business firm to produce a product or service that is ultimately profitable to shareholders or should a firm be organized to give voice to all stakeholders? Should these decisions be left to the individual institutions or should they be made democratically by society as a whole? There are paradoxes connected with voting as noted by Kenneth Arrow. Finally, do the terms *majority* and *minority* capture some important conceptual distinction or are they merely a political rhetoric?

—*Nicholas Capaldi*

See also Arrow, Kenneth; Egalitarianism; Multiculturalism; Political Legitimacy; Political Theory

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Managed Competition

Managed competition is a relatively new organizational paradigm for the provision of medical services that tries to capture the benefits, while avoiding the limitations, of both competitive and cooperative models. To best understand this concept, five main topics will be addressed. They include (1) defining managed competition, (2) contextualizing managed competition in the health services industry, (3) origins of managed competition, (4) advantages of managed competition, and (5) disadvantages of managed competition.

Defining Managed Competition

Managed competition is a marketing and management strategy used to obtain maximum value for consumers and employers. It relies on competitive rules that were established through macroanalysis of interactions among consumers/employees, employers, health service providers, and public and private funding agencies.

The sponsor of a managed competition scheme develops a planned system that requires establishing rules of equity, as well as efficiency. Participating plans are selected and enrollment processes are regulated. This strives to achieve a balance between demand, cost, and risk considerations within fixed comprehensive health insurance service packages for consumers.

Managed competition offers employees a choice of several different health insurance plans or delivery systems. The employer contributes a set fixed-monetary amount established by sponsors set at or below the price of the low-cost plan. Employees then make their choice from among the plans offered that best meets their needs and pay any price differential with pretax dollars. This creates incentives for employees to make tough economic choices and introduces price competition among insurance providers.

Contextualizing Managed Competition in the Health Services Industry

In the 1970s, the American federal government developed the Medicare and Medicaid programs as limited entitlement plans intended primarily for retirees and the indigent. These systems essentially comprised government-funded social medical insurance. The more affluent obtained employer-provided private insurance programs, for the most part. Both of these approaches to improving medical coverage have benefits, as well as limitations.

One advantage of the single-payer government medical insurance model lies in its ability to spread or "socialize" the risk of the occasional high-cost procedure over a relatively large contributor base. Another benefit is that the single government payer gives the consumer considerable leverage in price and service negotiations with prospective medical care providers and systems.

The single-payer social insurance health care approach does have potential deficiencies. It poses a "moral hazard" that consumers may be tempted to overuse nominally "free" medical services paid for by the government as a universal social entitlement. Scarce tax dollars could be wasted, thereby undermining the financial soundness of the social insurance fund for all. The question is this: Should health care be regarded as a public good freely available to all citizens? Or, is it a private consumer good that can most efficiently and effectively be provided by private entities responding to price mechanisms and profit incentives?

Conversely, private or free market medical insurance delivers services to those with the means to afford them. It is relatively expensive, since competing, duplicative insurance providers lose potential economies of scale in purchasing and medical administration. It can also be portrayed as restrictive and inequitable, since comparative wealth allocates the quality and quantity of medical services provided. In 2006, an estimated 45 million Americans lacked any or meaningful health coverage; yet Americans paid twice as much per capita as Canadians and the French for health service. Some private health insurers, driven by the profit motive, tend to cherry-pick healthy clients and exclude high-risk customers with preexistent conditions.

Origins of Managed Competition

Alain C. Enthoven, Ph.D., is recognized as the father of managed competition. He was the Marriner S. Eccles Professor of Public and Private Management, Emeritus, at Stanford University. He was also a core faculty member at the Center for Health/Center for Primary Care and Outcomes Research, also at Stanford.

Enthoven was one of the original founders of the Jackson Hole Group, a think tank focusing on human resource action, community relations, and health care policy reform. His academic research in public policy administration targeted the financing and delivery of health care. Enthoven's goal was a health care delivery system using market-based incentives to create medical costs efficiencies, promote accountability, and better guarantee the quality of health care for consumers.

Advantages of Managed Competition

Under managed competition, patients with illnesses would choose plans that focus on their specific ailments, while healthy patients might instead seek out the plan that provides the best primary care services. Plans would be encouraged to form partnerships with others to create the best possible array of services. Becoming more efficient with fewer errors, achieving modernization, and eliminating waste are primary goals in managed competition.

When using a managed competition system, employers offer many different plans and employees can choose the one that best suits them individually. This is a major advantage for cash-strapped employers insuring their employees on a budget.

Government regulation plays an important role in managed competition plans. Regulations convey specific guidance and motivation for health care plans to provide the best care possible. However, governmental presence is relatively modest in this market-driven medical insurance system.

Disadvantages of Managed Competition

Managed competition may not be best suited to providing health care to people with illnesses that are expensive to treat. Because medical practices would try to greatly decrease costs to be the lowest-priced plan, they will be more selective about which consumers they wish to cover in an effort to provide the cheapest rates.

Managed competition encourages plans to specialize in one area of the medical field. The problem with specialization is that there is no incentive for physicians to focus on costly, undersupported illnesses. If health insurance plans attracted a large number of people needing expensive treatments, they might lose money and end up exiting the market. Also, there would be an incentive to underserve the indigent sick and overserve the healthy and wealthy. In addition, this concept puts patients with chronic illnesses at risk because of the high costs of multiple treatments and long-term care.

There is concern that managed competition pits service providers against one another to provide the least expensive coverage. When budgets are cut to reduce cost (a typical competitive tactic), the quality of services could potentially deteriorate as well, since decreased funds would be available for medical care. A hybrid approach that combines government-supported social insurance coverage to socialize the risk of catastrophic illnesses, as well as support indigent and elderly patients, with managed competition to provide gap coverage for the normally healthy may offer the best combination of fairness and cost effectiveness in the provision of medical services.

—Dirk C. Gibson, Miranda Evjen, and Jennifer Lin Roberts

See also Competition; Health Maintenance Organizations (HMOs)

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Management, Ethics of

When discussing management ethics, it is natural to focus on the management of business as many schools of management have done. However, nearly all organizations need managers-universities, not-for-profits, sports teams, and government agencies. Thus, management ethics covers a wider terrain than business ethics. Although the emphasis in this entry will be on the ethical management of a business, many of the comments here are generalizable to ethical management in general.

Managing for Shareholder Wealth

The starting point for ethical management should be role morality. Role morality is the morality of one's station and its duties. The duties of one's station are determined by the purpose of the organization. Suppose we take the traditional starting point for the purpose of a corporation. Milton Friedman's position is the standard: that business has only one responsibility, which is to use its resources to increase its profits, engaging in free and open competition without deception or fraud. Under this view the manager is the agent of the stockholders who are the owners of the firm. As an agent of the stockholders the ethical obligation of the manager is to do the bidding of the stockholders, which normally is to make as much money as possible while following the basic rules of society, according to both the law and ethical custom. Many people do not see making money for stockholders as a *moral* obligation, and professors of finance seldom teach it as a moral obligation, but Friedman's position is a moral position nonetheless.

It should also be pointed out that violation of this simple moral requirement is behind many of the scandals that have afflicted business and behind many of the criticisms of business with respect to corporate governance. Excessive executive compensation and lavish executive perks are a violation of the ethical obligation of managers to increase the profits of stockholders. Many of the accounting scandals of the 1990s and 2000s were the result of managers manipulating earnings so that they could get their stock options or bonuses. These managers were not working for the stockholders and violating the law and ethics on behalf of the stockholders. Rather they were violating the law and ethical custom for their own selfish gain.

The qualifications that Friedman makes to the obligation of managers to increase shareholder wealth are significant, however. Even if the manager is the agent of the stockholders, he or she cannot be asked to make profits in a way that the law deems illegal or that violates ethical custom. The term *ethical custom* can have narrow or a broad application. Friedman specifically rules out anticompetitive practices and deception and fraud. However, some in Friedman's camp do allow bluffing. Albert Carr pointed out that the ethics of business is more like the ethics of poker than the ethics of ordinary morality. There is still no consensus as to what should be included under Friedman's term *ethical custom*.

One item that is not included in ethical custom for Friedman is philanthropic giving from profits or the use of profits to help solve social problems: that is, using profits for social responsibility. If a manager uses the profits for philanthropy or social responsibility, he or she is taking the money that belongs to the stockholders and using it for other purposes without their permission. Friedman characterizes this as a kind of taxation without representation. However, Friedman is assuming that the stockholders do not want corporations to engage in philanthropy or help solve social problems. However, the stance of individual corporations with respect to philanthropy and social responsibility is well known. For example, the stockholders of the Target Corporation are well aware or reasonably should be aware of the fact that Target is one of the more generous companies with respect to corporate giving. Target stockholders either are willing to sacrifice some of their profits for the public good or, more likely, believe that Target's record of charitable giving will result in a competitive advantage that yields even more profit in the long run.

An Alternative to the Stockholder View: Sustainable Management Practice

It is important to realize that Friedman's view of the obligations of managers has a particularly American flavor to it. There is a consensus in capitalist countries that increasing shareholder or owner wealth is a moral obligation of managers; however, American managers focus on that one obligation while the consensus in other capitalist countries is that there is more to the purpose of a corporation than lawfully and ethically making money. The European Union has as its official policy that the corporation must practice sustainable management. (A term that is often used synonymously with "sustainable management" is Corporate Social Responsibility Europe or CSR Europe. This latter terminology seems to be giving way to the former, however.) Sustainable management or management in accord with Corporate Social Responsibility broadens the duties of the manager. On the European view, sustainable management requires financial success but it also requires obligations to protect the environment and to be socially responsible. In Europe, "social responsibility" is not understood in terms of philanthropy but rather is understood in terms of respecting human rights. The Europeans have even come up with the notion of triple bottom line accounting that broadens the traditional accounting determination of financial success to include measurements of environmental responsibility and social responsibility. Triple bottom line accounting is still in its early stages of development, and it is unclear how successfully quantitative triple bottom line accounting can become.

The position of the European Union on the ethical responsibilities of managers is similar to that taken by the United Nations in its United Nations Global Compact. An international effort affiliated with the United Nations Global Compact is the Global Reporting Initiative that is designed to present common international principles for bottom line accounting.

The philosophy that will govern capitalist countries in Asia is still evolving. The Japanese are moving away from a more collective and paternalistic set of management practices, but in doing so, they seem to prefer the model of sustainability rather than Friedman's maximization of profit model. Academicians in China are working with a notion of corporate social responsibility for their society.

There is now a debate regarding the eventual financial viability of the two models. Many Americans believe that the more narrowly focused emphasis on stockholder wealth is ultimately the more successful model. Much of the rest of the world seems to disagree. One implication of this debate is that when one specifies the ethical obligations of managers one must be clear what one takes the primary function or purpose of the firm to be.

Stakeholder Management

Whether one is an adherent of Friedman's increase shareholder wealth philosophy or an adherent of the sustainability philosophy, one will hear many references to stakeholder management. To fully understand management ethics, we need to be clear about the obligations that managers have to corporate stakeholders. In the U.S. academic literature, stakeholder management is often positioned as an alternative to Friedman's stockholder theory. As an alternative to Friedman, the theory requires that the moral obligation of the manager is to balance the interests of the legitimate stakeholders of the business. (It should be noted that any organization such as a university or charity can use stakeholder analysis.) On a narrow definition of stakeholder, a stakeholder, or more accurately stakeholder group, is defined as a group that can affect the firm's survival. On a broader definition, a stakeholder is a group or individual that is affected by the behavior of the firm. On the narrow definition, the traditional stakeholders are stockholders, customers, employees, suppliers, managers, and the local community. Some add government, media, and nongovernmental organizations (NGOs) to the list.

Stakeholder theory is still a work in progress. It is not a moral theory in its own right. The range of legitimate stakeholders is still a matter of controversy, and there is no acceptable methodology for balancing the interests of stakeholders. However, when taken as an alternative to Friedman's stockholder view, each legitimate stakeholder has the right to have its interests taken into account, and it is the obligation of the manager to do so.

It is not enough to consider the interests of the stakeholders simply to increase the wealth of the stockholders. To do so would simply use a stakeholder as a means to the wealth of another. Each stakeholder has legitimate interests of its own, which deserve ethical treatment in their own right.

It should be noted that nearly all companies, including American ones, use stakeholder language. In Europe, the discussion centers on stakeholder dialogues. Such dialogues are a device that managers use to achieve sustainability. Despite the difficulty faced in determining stakeholder interests and in balancing them, a number of the largest companies in the world, such as BP and Shell, use a rather broad definition of stakeholder analysis to guide management practice.

Stakeholder theory has important heuristic uses as one considers management ethics. Every organization has stakeholders, and one effective way of looking at the ethical obligations of managers is to do a stakeholder analysis. In this way, there is a generic principle of management ethics that applies to all types of management. That is, management has an obligation to consider the interests of legitimate stakeholders and to achieve a balance in honoring those interests. At that point, management ethics becomes specific to the organization. A major research university has a different function and a different set of stakeholders than that of a major corporation. Thus, the obligations of a university president are different from the obligations of a typical business CEO. Even within business, management ethics may require different obligations depending on the kind of business one is engaged in. For example, an entrepreneurial firm that is dependent on venture capital has a broader range and perhaps a more stringent set of obligations to the provider of venture capital than a manager has to stockholders in a Fortune 500 company. Both the amount of risk to capital and the magnitude of the risk to the venture capitalist are usually sufficient to distinguish the venture capitalist from the ordinary stockholder.

Of course, some stakeholders are common to almost any organization. Nearly all organizations have employees as well as clients. In the university, the clients are students and in business the clients are customers. All but self-sufficient organizations have suppliers. Universities, corporations, and not-for-profit medical facilities all depend on suppliers. And all organizations exist in the natural environment and in a local community. Organizations also have different stakeholders, that is, stakeholders of one organization may not be stakeholders for another organization. Public companies are unique from both partnerships and single proprietorships and from other nonbusiness organizations in the fact that public companies have stockholders as stakeholders. Discussion of the obligations of business managers to these basic stakeholders follow.

The Ethical Grounding of a Manager's Role Obligations

The fact the stakeholder theory is a theory of management and not an ethical theory should be emphasized. Even our general principle of ethical stakeholder management described above needs to be justified. In other words, it is not enough to limit management ethics to my station and its duties. Role obligations need to be consistent with and justified by higher-order or more universal moral concepts. Otherwise, the role obligations of a mafia don becomes an example of management ethics. Effectiveness in carrying out one's role is not sufficient to establish the morality of one's carrying it out.

Organizations are made up of persons. Respect for persons is a central moral principle both in the world at large and in moral theory. Management ethics requires that those managed are treated with respect. Given this universal, the moral task of the managers is to implement respect for persons in the organizational setting in which they find themselves.

Since organizations are collectivities, ethical managers must consider the good of the entire organization. This requires that the individuals within an organization function as a team. One of the great challenges to ethical managers results when he or she needs to sacrifice the need of an individual for the good of the organization. Coaches of athletic teams often face this dilemma. But corporate CEOs do as well. Sometimes the survival of the business requires layoffs. Ethical management requires that when an individual interest is sacrificed for the organizational good, the individual must be treated with respect. Even when layoffs are justified and necessary, there is a right way (respectful way) and a wrong way (disrespectful way) of laying someone off.

Ethical management also involves certain attitudes and dispositions. Let us refer to these as the virtues of ethical management. What is to count as the appropriate virtues of the ethical manager is a matter of great controversy. Some managers believe that employees are basically self-motivated and trustworthy and thus should be mentored rather than bossed. Others believe that employees present agency problems, that is, they will always loaf and take other actions to advance their own interests rather than the interest of the organization. Such managers think that free riding on the part of employees is a serious problem. In the context of employee conduct in the real world, it is hard to say which attitude toward managing employees is the correct one. It may be that a mentoring relationship is morally appropriate in some business contexts and that a monitoring relationship is the morally appropriate attitude to take in other contexts.

At this point we can say that management ethics involves respecting the persons whom one manages, taking into account the good of the collective entity that one manages for and cultivating those managerial virtues that increase the likelihood that the manager will indeed respect persons and promote the good of the organization. A general ethical principle for ethical management is that managers consider the interests of legitimate stakeholders in management decisions.

The Ethical Treatment of Employees

Respect for persons is the fundamental moral principle for managing people. What does that entail in the typical business? Many would argue that respect for persons requires some participation and voice on the part of the employee. Certain laws and managerial norms stand in the way of employee participation and voice. One is the legal doctrine of employment at will. Employment at will indicates that in the absence of a contract and in the absence of illegal discrimination, both the employer and the employee are free to sever the employment relationship at any time for any reason—good reason, bad reason, or reason immoral. Some defenders of employment at will point out that since both the employer and the employee can exercise employment at will, any ethical issues are eliminated or at least greatly lessened. Critics of employment at will point out that it is easier for the manager to find another employee than for the employee to find another job. As a legal matter, the relationship may be symmetrical, but as a matter of fact it is not symmetrical. Critics also point out that severing a relationship for a bad reason or reason immoral is always prima facie wrong. Even the courts have gone part way to recognizing the critics' point by allowing a public good exception to the employment at will doctrine.

Another danger to the ethical treatment of employees is created by paying excessive attention to hierarchies within the organization. Hierarchies are often represented in organization flowcharts that show who reports to whom. As devices to show reporting relationships they may raise no ethical red flags. However, when they reflect how decisions are made in the organization, they can become morally problematic. If one is lower in the hierarchy, that should not mean that he or she should simply follow orders and have no voice in the decision-making process. There is also a danger that those at a higher position will hoard information and keep subordinates in the dark. Indeed not only will subordinates be kept in the dark, but they will be deceived as well.

There are a number of management practices that counteract these dangers. Labor unions and employment contracts serve as an antidote to employment at will. It should be noted in passing that the United States is fairly unique among industrialized countries in subscribing to employment at will. With respect to hierarchies, a number of enlightened management practices are designed to undermine hierarchies. Quality circles, team building, and participative management all represent steps in the direction of participation and voice for employees. One of the more comprehensive practices is open book management. Open book management eliminates information asymmetry by providing all financial information to all employees. In so doing, each employee will see how the business runs;

in other words, the employees will think like owners. And from the perspective of management ethics, they will take more responsibility and thus exercise participation and voice.

Employees have a right to be concerned with an important change in the marketplace. By the mid-20th century, employees believed that they had a social contract with management that, when honored, justified loyalty to management and the business firm. Even within the doctrine of employment at will, it was assumed that a good worker would continue with the firm until retirement. In some industries, as many as three generations within the same family would have worked in the firm. As well as a living wage employees would receive health insurance and a pension. In other words, an element of corporate paternalism was expected even though the United States had nothing like the Japanese system of guaranteed lifetime employment. As the 20th century came to an end, there had been massive upheaval in labor markets in part caused by global competition. Downsizing became all the rage. Others lost their jobs due to outsourcing. Some layoffs were also caused by efforts to please the short-term traders on Wall Street. Too often, employees were seen simply as a cost rather than human capital. Where layoffs from the impacts of globalization are probably morally justified, layoffs to please Wall Street are ethically suspect. These layoffs are simply using some as a means for the financial ends of others. In some industries, the layoffs were in the tens of thousands. In addition, the paternalism disappeared. Early into the 21st century, employees were asked to contribute much more to their health insurance if they were fortunate enough to receive employer subsidized insurance at all. Defined pensions were dropped and workers had to save for their retirement from their salaries. The fortunate ones received a percentage of their salaries as a benefit although the individual employee was responsible for investing the funds. The size of the pension a worker was to receive was not guaranteed. Employers referred to this change as the "New Social Contract." It was hardly a contract since the employees had no say in its terms. The terms of the contract are also perceived by many to be unfair.

As a result of these changes employees need to change their expectations. Employees should not expect lifetime employment or paternalistic benefits; they need to manage their careers and make their own financial decisions. They also need to take more responsibility for managing their health care and their retirement. However, as a result of these changed expectations, the old notion of loyalty has practically disappeared. To many it seems that market considerations are now the only determinant of what employees receive in terms of salary and benefits. Ethical notions such as past promises, fair distribution from the gains of productivity, and loyalty seem far less relevant that they were a few years ago. Many ethicists believe that this change in expectations is patently unfair to employees.

Managing Ethical Obligations to Customers

Since customers are so essential to the success of a business enterprise, you might think that managers would consider their obligations to customers to be paramount. On occasion a company, especially in advertisements, will talk that way, such as proclaiming that "the customer is number one." For instance, the Johnson & Johnson Credo ranks the customer first among its stakeholders. Despite this endorsement of the importance of the customer, there are a number of important issues regarding the treatment of customers that deserve the attention of the ethical manager.

Customers are often in a situation of high information asymmetry with respect to the products they buy. That is, the seller of the product knows much more about the product than the customer. In such situations, there is always a temptation for the salesperson to sell the customer something more expensive than is needed. This temptation is especially acute when the sales staff is on commission. What are the obligations of the sales manager with respect to how his or her sales staff should deal with situations of high information asymmetry?

One might argue that the customer has the obligation to search out the information that will close the information gap. In its most extreme form, this is the philosophy of "Let the buyer beware." That philosophy is neither legally nor ethically suited to a world where the products are so complex. On the other hand, a moral requirement that sales managers operate under a principle that provides the customer with whatever information he or she would want is much too broad. There is no obligation for a sales manager to tell a customer that a competitor has the same product on sale at a lower price. Some middle ground is the ethically appropriate answer here.

Surely sales people should not lie or deceive. If a customer asks if a 32″ flat panel TV will work in an apartment, the sales person should not try to sell him a 58″ TV on the grounds that the 32″ one is too small.

To help define the ethically appropriate line in providing information to customers, two things need to be considered. First, how are salespeople compensated? An overemphasis on commissions will tempt salespeople to sell the most expensive product even if it is not needed. Second, would finding the ethical solution to this dilemma be more likely if salespeople thought of themselves as professionals rather than traditional salespeople? Putting salespeople exclusively on salary and expecting them to behave like professionals might go far in overcoming the problem of customer information asymmetry.

Vulnerable consumers ethically require more help in overcoming information asymmetry. Unfortunately, this ethical obligation is breached by the unscrupulous, who play on the information asymmetry you find in the elderly and in the uneducated. It is common to find senior citizens paying for sealed driveways or roofs they do not need. However, the ethical issues here involve more than deception. Target marketing is an accepted and even essential way of doing business. However, when a vulnerable population is targeted, ethical issues arise. The beer industry was rightly criticized for targeting inner city blacks with ads for malt liquor. Marketing managers need to be especially sensitive when their customers might be considered vulnerable and thus harmed by the product being marketed.

Other ethical issues in the treatment of customers concern fairness. Does being a good customer permit special treatment? Often it does. We seem to accept the fact that frequent flyers are entitled to special perks. However, it is alleged that good customers get special treatment when they call a credit card company or a bank regarding a problem. That is, these customers get a live person quickly or have a shorter wait time. Is that fair? Indeed, the whole system of automated phone answering devices is highly unpopular with customers. It seems to take forever to get to the option that applies to you and even when you get there you might not be able to resolve the problem. Automated check-out lines in grocery stores and discount stores as well as automatic check-in lines that the airlines have introduced shift the transaction costs from the seller to the buyer. What is the fair burden for dividing the transaction costs? These and similar issues deserve the attention of the ethical sales and marketing manager.

The Ethical Management of the Supply Chain

Managers have always had ethical obligations to their suppliers. However, recently there have been demands in some industries that managers have an ethical responsibility for their suppliers. This distinction can be illustrated by some examples.

With respect to ethical obligations to suppliers, it seems as if managers have an obligation to keep their word, for example, by honoring their contracts. Many would argue that faithful suppliers with a long history of supplying high-quality products at a reasonable price deserve loyalty and should not be instantly dropped when the manager can get a competitive product for a slightly lower price. Unfortunately, the real world is departing rather sharply from the ethical ideal. Suppliers are always being pressured to lower their price and to "renegotiate" contracts in order to keep the business. Loyalty to suppliers seems to be a thing of the past as long-term suppliers are instantly dropped if a competitor comes in at a slightly lower price. The ethical manager has a difficult balancing act to perform—on the one hand, responding to the demands of the market and on the other being fair to faithful suppliers with a long and good track record with the company.

Recently, the ethical manager has been required to take responsibility for ensuring that their suppliers behave ethically. This has been particularly true in the apparel and sportswear industry where the distributors of these products such as Nike and the Gap were criticized because of the sweatshop conditions that had existed at a number of their suppliers. Activists and nongovernmental agencies have demanded that the distributors of these products require their suppliers to provide safe working conditions and a living wage. They have demanded that distributors provide the names of their suppliers so that those suppliers could be subjected to independent inspections.

This demand that managers police their suppliers and require certain forms of behavior is controversial. There is no question that working conditions in the sweatshops are bad—indeed very bad—when compared with manufacturing facilities in industrialized countries. On the other hand, some economists have argued that sweatshops are a necessary step in economic development and that well-intentioned steps to improve sweatshops only make the economic situation worse. Beyond the debate about economics, there is also an ethical issue about responsibility.

Normally, we are only held responsible for our conduct; we are not held responsible for the conduct of others. But this is not always the case. In theory, the managers of bars and taverns are required by law and ethics not to serve or continue to serve obviously drunk customers. Indeed, on occasion these managers have been sued when a drunk customer has driven away only to be involved in an accident that injures or kills another. Some states and municipalities have passed laws holding gun manufacturers responsible in certain cases when gun owners commit a crime, especially a crime in which the victim is killed by a gun. Opponents of extending responsibility in this way are trying to pass a national law that would invalidate such attempts by states and municipalities to hold gun manufacturers liable.

Despite the controversy surrounding these cases, the public has accepted without much debate a moral requirement on sportswear and apparel distributors to take responsibility for their suppliers. Perhaps part of the reason for the willingness to extend responsibility here is because the sweatshop issue has been construed as a human rights issue; the sweatshop manufacturers are seen to be violating internationally accepted human rights. If that allegation is correct, then a serious moral wrong is taking place because the violation of human rights is a serious moral wrong. The argument then goes that major international corporations in the apparel and sportswear industry should not take advantage of the victims of human rights violations to make a profit. Indeed, under the European Union model of corporate social responsibility, managing a business consistent with human rights and in a way that supports human rights is a moral requirement. When framed in that way, the leap to taking responsibility for your suppliers does not seem like such a great leap.

Management's Obligations to the Community and the Environment

Business does not take place in a vacuum. It is contextually located in a community or communities, which in turn are located in the natural environment. There are those who say that a business provides jobs—the very lifeblood of a community. It also usually pays taxes to the community just as individuals do. As a result, there is no further obligation to the community—in the form of charitable giving or in the form of helping to resolve social problems. Indeed, those who follow the view of Milton Friedman believe that it is morally wrong for managers to assist in these ways.

Despite the view of the Friedmanites, some form of corporate social responsibility is accepted as an obligation—at least on the part of the large companies. But is such an obligation justified? Some have argued for such an obligation on the basis of the great financial resources that these large companies possess. Others have made an argument on the great power that large corporations have. With great power and great resources goes great responsibility, and part of that responsibility involves philanthropy and other activities that benefit the public good.

Another way to establish a managerial obligation to the community is to challenge the "we provide jobs and pay taxes" argument. The "pay taxes" piece is especially vulnerable since many companies get states or localities to compete for the business and the most common way that states and localities compete is to give tax breaks. Even the "create jobs" piece of the argument has been recently challenged. Wal-Mart, for example, has been criticized for paying such low wages and providing so few benefits that many of its employees need Medicaid or other forms of public assistance. The business press has taken notice and now refers to the pushing of health and pension costs on the public as another form of corporate outsourcing. To the extent that these arguments are correct, the firm has an obligation to the community on grounds of fairness.

However the theoretical arguments play out, most companies at least make gestures to a responsibility to the community. Small businesses support charitable events in their communities and large companies have foundations or designated programs for charitable giving and community service.

Concern with the effects of business activity on the environment is now a focus of managerial ethics. The first step in environmental stewardship occurred when businesses realized that there were huge cost savings in waste and energy reduction. Although great progress has been made here, the international traveler cannot help but notice that the United States is behind other industrialized countries in taking easy steps to reduce stress on the environment. In Europe and Japan, for example, sheets in hotels are not changed every day unless requested, escalators do not run day and night even when no one is using them, and lights in hallways and elevators turn off automatically when no one is there. Also when you leave your hotel room and take your key, the lights go out.

The real challenge for managerial ethics involves business decisions that help the environment and perhaps even profits in the long run but that hurt profits in the short run. The most acute example here is in the automobile industry. Car makers, especially GM and Ford, make the best profit margins on SUVs and have marketed these cars very successfully. However, these vehicles have low gas mileage and other problems. Should GM have even produced the Hummer—a monster gas guzzler? Do the automobile companies have a duty to educate consumers about the cost to the environment when purchasing SUVs? One of the great challenges for managerial ethics is in developing a business strategy that is both profitable and environmentally responsible.

Ethical Leadership

One of the tests of management ethics is whether one is both an effective manager and an ethical manager. Management ethics is more than effective management. This moral fact has important consequences in any discussion of leadership. Ethical leadership is more than effective leadership and thus not everyone who manages a company successfully can be considered a moral leader. Just what that something else besides effectiveness entails is a matter of great controversy in leadership study and practice.

Honoring the role obligations that fall on all managers such as putting the good of the organization above their own interests as well as honoring the obligations of managers to the various stakeholders are key parts of management ethics. So is moral imagination. Moral imagination involves looking at business decisions and strategy from different points of view. It involves creative attempts to be profitable and ethical. This is the challenge that faces the automobile industry as well as many other industries. In the long run being effective is not sufficient; being effective while being ethical is what successful management is all about.

—Norman E. Bowie

See also Agency, Theory of; Asymmetric Information; Business, Purpose of; Business Ethics; Conflict of Interest; Corporate Accountability; Corporate Citizenship; Corporate Ethics and Compliance Programs; Corporate Governance; Corporate Issues Management; Corporate Philanthropy; Corporate Social Responsibility (CSR) and Corporate Social Performance (CSP); Corporate Social Responsiveness; Employment Contracts; Ethical Role of the Manager; Moral Leadership; Open-Book Management; Roles and Role Morality; Scandals, Corporate; Shareholder Model of Corporate Governance; Shareholder Wealth Maximization; Social Audits; Stakeholder Theory; Strategic Corporate Social Responsibility; Strategic Philanthropy; Sustainability; Transparency; Triple Bottom Line; Trust; Working Conditions

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Mandeville, Bernard (1670–1733)

Bernard Mandeville was Dutch and English. One of the first modern thinkers to address the relationship between morals and economics, Mandeville is renown for his claim that a prosperous society could be brought about only by self-interested, not virtuous, individuals. Born in or near Rotterdam and trained in medicine at the University of Leiden, Mandeville emigrated to England in the last decade of the 17th century. His thesis, that private vices generate public benefits, first appeared in his poem, “The Grumbling

Hive: Or Knaves Turn'd Honest," published in 1705. The poem was reissued, in 1714, as *The Fable of the Bees* and included an essay on the origin of morals and a series of additional remarks on the poem. With another edition of 1723, Mandeville became famous, if not notorious; subsequent editions of the *Fable* included a second volume with six dialogues. He published a variety of other works, including, in 1732, *An Enquiry into the Origin of Honour.*

In "The Grumbling Hive," Mandeville depicts a society of self-interested bees whose trade generates a large and bustling commercial society. In the early 18th century, the reigning opinion held that self-denying virtue—entailing action contrary to a natural passion and in accordance with reason—was essential to the public good. Mandeville contended, in the poem and in the extended editions of the *Fable*, that we are motivated by self-interested passions, not reason. Through the division of labor, we pursue material gain. Our desires for goods and finery (condemned by some as luxury) provide employment and our trades generate wealth. The standard of living rises, the population grows, and the poor enjoy a better life than did the wealthy of previous generations. Note that Mandeville does not claim that any instance of vice is beneficial, only that which is consonant with a rule of law establishing justice. It is the duty of the politician to secure a legal framework that will serve as the foundation for commercial interaction.

Mandeville's provocative claims provide the basis of much of the 18th-century discussion of morals and society, influencing and challenging David Hume, Jean-Jacques Rousseau, and Adam Smith, among others. Today his writing raises a variety of significant issues for ethicists. Not only does his thought raise the question of whether business and self-denying ethics occupy distinct spheres, it also includes an evolutionary account of how norms might emerge out of social interaction. In his attempt to puncture hypocrisy, he also suggests that one must keep in mind both the practical consequences of ideals and whether some goods (such as self-denying virtue) are compatible with others (such as the benefits of commercial growth). Finally, Mandeville is among the first to move away from an anthropomorphic conception of society, according to which all social order must result from someone's intention. The idea of unintended emergence reminds the ethicist that society is complex, that the empirical application of principles demands careful attention, that our reason may be limited, and that good intentions are not sufficient for beneficial outcomes.

—F. Eugene Heath

See also Hayek, Friedrich A.; Individualism; Invisible Hand; Liberalism; Libertarianism; Self-Interest; Smith, Adam; Spontaneous Order

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Manipulation, Financial

The financial manipulation of stock market quotations consists in the altering of the ordinary course of supply and demand. This is done through devices that stimulate or depress stock prices, thus seriously distorting the market by not letting share prices be fixed naturally in free market exchange. In manipulation, something, or someone, intervenes in the mechanism of price setting, thereby taking unfair advantage at the expense of the rest of the investors.

Manipulation is an extremely serious action because it causes prejudice to the integrity of the financial markets and, in a particular manner, that of the stock market itself. The damage is done both by hindering clean play and by simultaneously blocking the meeting of institutional goals. In the case of the financial markets, manipulation obstructs the effective mass ordering of shares on a totally equal basis, reducing in this way the financial market's goal of being a source of financing. As for the stock market, objective and impersonal price setting breaks down, thus frustrating the market goal of being a privileged indicator of the pace of the economy. When this happens, justice suffers and market efficiency is cut down.

Different ways of manipulating stock market quotations exist, but the most commonly used methods come to three: manipulation through quasi-monopoly, manipulation brought on by falsehoods, and manipulation by placing shares on the market above their real value. Following are a few relevant examples.

Suppose that a large bank controls several portfolio companies and it decides to use an important part of its own shares and a substantial amount of money in cash to dictate the quotation price of its shares. When market control has been obtained, the bank would be in favored position to buy back its own shares at a cut-rate price by going through its subsidiaries. Once the price had gone up, they would sell them, making high profits at the cost of the investing public. This would be a case of manipulation by quasi-monopoly.

Another example along the same line is "muscle play," which basically consists of taking advantage of a false oligopolistic position at a concrete moment. This muscle play aims at the creation of such a considerable price change that the losses resulting from creating this movement are less than the profits generated by the end result. There have been cases in which, in the last minutes of taking orders at a specific stock market, and at a moment of clear euphoria and a rising trend, a single operator made the index drop by more than 2%, with a large-scale operation. Although considerable losses occurred, the motive behind this apparently peculiar behavior became clear: A powerful institutional investor forced the index to drop so as not to face payments caused by the expiry of certain contracts made with another entity on the aforementioned index.

Manipulation through falsehoods can take a number of forms: false rumors; unfounded news of the impending crisis of a specific listed company; imaginary appointments, resignations, or contributions; false financial documents such as general balance sheets and past or future profit and loss accounts; supposedly expected profits or dividends; the discovery of mines, or granting of nonexistent patents for unreal inventions; and effective quotations. This last is the most efficient "rumor." While it is assumed by the investing public that the publishable share price is correct, in reality it is the result of imaginary sales and purchases, of washed and matched sales. The motive behind this falsehood is to modify or produce changes with a frequency that in reality should not exist, but which benefit the image of the share in question.

With respect to the third group of manipulative practices, special mention should be made of sales made under high-pressure methods. This is usually done by dealing with low price shares or those quoted on a parallel market. Investors receive telephone calls with persuasion methods that are frequently accompanied by swindle, fraud, deceit, or the inexact presentation of facts. This type of manipulation causes incautious investors to lose considerable amounts of money.

The manipulation of share quotations is a type of dishonest speculation because the manipulator is not taking advantage of price fluctuations, he or she is causing them. For this reason, if the manipulation consists of the voluntary alteration of fair share pricing, it must be considered, in general terms, not only as illegal but also as an immoral practice. And the manipulator is taking part in an unethical practice if he or she knows the fair price of a financial asset and modifies it without reason, causing the share quotation to be far from its true value.

However, a case could be made of certain "manipulation" being ethically correct if, for example, someone initially forecasts the potential of a share following the logic that the price will move in a foreseen direction. The investor does not take the future into direct account but, in this way, effectively accelerates the change in the share quotation. In this example, the shares have not been manipulated, and the share quotation will have taken longer to rise or fall. Here, then, the investors are not manipulators and would be helping the market to correctly evaluate the fair price. The ethically wrong action would be to use unfair means or to place a value on quotation levels much higher or much lower than the share's base price.

What is in play in the world of finance has enormous importance, not only because of the resulting negative economic consequences, but above all because, if market abuses are not counteracted, the investing public risks giving up on the system for loss of confidence. Adverse effects on the economy and the common good would soon be noted.

Evidently, authorities and regulators should continue their attempts to suppress these bad practices by all legal means. But at the same time the financial community should accept self-regulation in line with accepted ethical standards and binding professional practice.

—José-Luis Fernández-Fernández

See also Insider Trading; Sarbanes-Oxley Act of 2002; Scandals, Corporate; Speculation and Speculator; Transparency

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MAQUILADORAS

A maquiladora is an assembly or manufacturing plant, in most cases along the border between two countries, which receives imported materials and equipment duty-free, assembles the product, and then exports the product back to the originating country with very low or no tariffs. The word *maquiladora* comes from the Spanish word *maquilar*, which means *to assemble*, and was first used to describe plants established under a special program on the Mexican side of the U.S.-Mexican border. The term and concept have since spread to areas in other countries where trade barriers are reduced on imported materials to assemble goods for export.

Mexico's maquiladora program was established in 1965 to create jobs for Mexican workers after the end of the Bracero program, which had allowed Mexican workers to find temporary agricultural-based employment in the United States during and after World War II. When that program was terminated in 1964, Mexico designed the maquiladora program to encourage manufacturing along its northern border and thus provide jobs for Bracero workers and the rural poor. In the beginning, maquiladoras could only locate within approximately 12 miles of the U.S. border and only served the purpose of labor-intensive job creation and foreign currency flow.

In the 1970s, U.S. companies began to develop the concept of the "twin plant," where they would locate capital-intensive operations on the U.S. side of the border and labor-intensive operations on the Mexico side of the border to capitalize on the low-priced labor. Well-known city pairs include El Paso, Texas, and Ciudad Juarez, Mexico; San Diego, California, and Tijuana, Mexico; and McAllen, Texas, and Reynosa, Mexico.

In 1986, Mexico joined the General Agreement for Tariffs and Trade, which changed the country's complex import policies and tariffs. Over the next 4 years, Mexico's tariffs dropped by 45%, which attracted a new wave of foreign investors and pushed maquiladora employment up to a growth rate of nearly 20% per year. Later, in 1994 with the initiation of the North American Free Trade Agreement (NAFTA) with Canada and the United States and the severe peso devaluation, maquiladora operations continued to expand to take advantage of even cheaper labor as well as more favorable trade terms.

As competition increased, some international firms began to increase the technical sophistication of work that took place within their maquiladora operations. While labor-intensive tasks remained the norm, maquiladora operations expanded to incorporate research and design along with high-tech assembly and manufacturing. By 2001, maquiladora exports represented almost half of Mexico's exports, and maquiladora employment had increased to employ 3% of the country's total workforce.

Since 2001, Mexico's maquiladora sector has struggled to remain competitive due to the U.S. recession in 2001, a stronger peso, and increased global competition. Between 2001 and 2002, 420 maquiladora plants closed in Mexico, and nearly 229,000 jobs were eliminated. A "permanent establishment" clause, added to Mexican tax laws in 1998 when limits on domestic consumption of maquiladora production were phased out, meant that these plants now had to pay taxes on assets and income in Mexico. The maquiladoras also lost their duty-free privileges with non-NAFTA countries in 2001 with the onset of NAFTA Article 303. The Mexican government created sectoral promotion programs to protect duty-free benefits of non-NAFTA component imports, but extensive paperwork makes participation difficult. The Mexican maquiladora industry also faces increasing competition from low-cost operations in China, the Caribbean, and Latin America.

Supporters of maquiladora programs point out the economic benefits of job creation in poor countries and the increase in consumer welfare because the cost of goods is lower. Critics of maquiladora programs are concerned about moving jobs from higher-cost developed countries and then exploiting workers in developing countries by paying low wages and exposing them to dangerous working conditions. Air and water pollution and other types of environmental degradation are more prevalent in maquiladora areas because environmental regulations are often not enforced and because low tax revenue cannot support municipal treatment facilities.

—Jeanne M. Logsdon and Phoenix Forsythe

See also Economic Growth; Free Trade, Free Trade Agreements, Free Trade Zones; North American Free Trade Agreement (NAFTA); Tariffs and Quotas

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Marginal Utility

In economics, marginal utility refers to the additional utility derived by a consumer from the purchase of one more unit of a good. More formally, it is the rate of change of utility with respect to changes in the quantity of goods purchased (the first derivative). The concept is crucial in economic theory because decisions about how much of a given good to purchase are thought to be made *on the margin*; that is, the agent asks himself or herself, with respect to each additional unit of any good (whether oranges in the grocery bag or dollars of life-insurance coverage), whether his or her expected utility from purchasing it is sufficient to justify its cost. He or she may also consider whether a substitute expenditure elsewhere, on a different good, would produce superior benefits in terms of utility.

Over a wide range of goods, marginal utility is *diminishing*. That is, the utility gained from each additional unit is less than that gained from the previous unit. Mary, for example, may get considerable utility from owning one bicycle. She is apt to get some, but less, utility out of purchasing a second. It is not as vital to her transportation or recreational needs as the first, but could add convenience because, for example, it could be used as a backup when the first bicycle breaks down or could be lent to visiting friends. But the marginal utility of Mary's acquiring a third bicycle is apt to be rather small. When the cost to Mary of buying another bicycle exceeds her expected utility from it, she will stop buying bicycles. (Up until that point, Mary has actually gained something from each transaction, since her marginal utility in each case has exceeded the price she's had to pay. The amount by which a consumer's marginal utility exceeds the price is known as consumer surplus.)

Money, too, has diminishing marginal utility. The move from being penniless to having 10 dollars entails a much more significant increase in utility than the move from having a million dollars to having a million and 10 dollars, even though 10 dollars are added in each case.

Diminishing marginal utility is used by some ethicists to justify wealth redistribution, especially via progressive income taxation. The argument is that any transfer of X dollars from a rich person to a poor person will increase overall social welfare. This is because the diminishing marginal utility of money guarantees that the decrease in welfare experienced by a wealthy person losing X is smaller than the increase in welfare experienced by a poor one gaining X. This argument is not fully persuasive, however, since the price-distortion brought about by taxation may result in deadweight loss—loss of social productivity—that offsets the welfare gain from the transfer.

—Stephen R. Latham

See also Deadweight Loss; Justice, Distributive; Property and Property Rights; Redistribution of Wealth; Rights, Theories of; Surplus, Consumer and Producer; Utilitarianism

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Market Bubbles

In a *market bubble*, a term that came into common use during the South Sea Bubble of 1720, the price of a commodity rises far higher than estimates of a commodity's difficult-to-specify "real value." The rise is not like a sharp inflationary increase, in that the price of the commodity does not move with the market, but, rather, in response to extraordinary demand. This rise usually occurs after a new product or technology or social opportunity appears and slopes upward rapidly under a demand that appears more like a social contagion than a market exchange. The commodity is perceived by buyers as unique, scarce, and nonsubstitutable. The price rises to a level far higher than that at which the commodity was recently and/or customarily sold. Purchases of higher-valued types of the commodity expand to lower-valued types as the market becomes less discriminating in order to supply the huge demand for the commodity.

The possibility of growth in the commodity's value is overestimated, partly due to lack of experience with the newly sought-after commodity. Demand is fed by speculation, as the possibility of quick wealth draws new participants into the market. The bubble generates social excitement, which spreads from investor to investor via personal contacts. Wealth floods into the market for the commodity, being drawn typically out of other investments perceived in comparison with the bubble commodity as underperforming. Investment in the bubble slows as fungible wealth is exhausted, and the costs of extracting wealth to purchase the bubble commodity begin to accelerate.

Events Leading to Bursting a Bubble

The bubble bursts when one or more of several possible events occur: First, wealth available to purchase the bubble may become relatively unavailable, whether due to actual availability or to extraction cost, so that demand slackens from potential purchasers. Because the run-up occurs over such a relatively short period, there is little chance for the market itself to expand. Although in the initial, slower run-up many new entrants may arrive, in the bubble's later stages, the market participants who are present and would invest are already fully engaged in the bubble. At least from the perspective of the practical limits seen in historical contexts, it is not feasible to bring in more distant participants to replace those who are "topped out." Thus, as the capital supply slackens or becomes too costly, demand plummets and the bubble collapses.

Second, qualities of the commodity may be shown as not unique, not scarce, and/or substitutable. Or the commodity itself may be revealed as different in character from its social perception, or even to be false or nonexistent, as in a scam. Indeed, the commodity's market may be revealed publicly as a bubble, sparking immediate divestiture of holdings and market collapse. Thus, the bubble may collapse if the special, demand-producing character of the commodity changes.

Third, natural or scheduled deadlines may cause investment to slacken as the deadlines near; market investors begin to exit to capture their gains, demand evaporates, and the price goes into free fall. This was one reason for the collapse of Tulipomania (see below).

Fourth, market intervention by government or other powerful actors may establish coercively backed rules that slow price increases, increase the costs of market exchange, or exclude certain actors from the market (e.g., purchasers using essentially borrowed funds in extreme margin purchases).

As the price falls, holders of the commodity quickly perceive that the peak price is past and rush to sell in order to recover as much profit as possible. The commodity price falls very rapidly as buyers leave the market. Paper gains are wiped out, and the commodity falls to levels far below that at which most participants entered the market, given that it was the rapid rise that drew in most participants. As a result, most purchasers of the commodity suffer high losses. It is possible for prices of the commodity to recover, however, to near prebubble levels.

Bubbles are a form of market failure and have been subject to considerable debate in economics because of their apparent violation of what would be expected in efficient markets. There have been attempts to reconcile bubble behavior with efficient markets (see, e.g., Peter

Garber's work), but most scholars argue that more than traditional economic theory is needed to adequately explain them.

Contingencies of a Bubble

Note that bubbles require several unusual circumstances to hold: First, the commodity's value is determined by socially reinforced perceptions of its special character, whether or not such character can be objectively measured in some way. Buyers perceive a shortage, whether or not the commodity is in short supply, and their judgments are reinforced by personal contacts with others who share this view. In other words, the market is driven entirely by perceptions reinforced by personal contacts, rather than by signals that accurately feed back commodity and market statuses.

Second, attempts to purchase the commodity grow in a frantic, panic-stricken fashion. The dynamic is not only rapid, but accelerating. Buyers act as in a mania, driven by fear of shortage, fear of losing the profit from the quick price run-up, fear of being left behind, or fear of having to face remorse at losing the opportunity for great wealth. Thus, actors behave with what may be termed *emotional biases*, as well as with the cognitive biases that defined the special characters of the commodity and its apparent scarcity in supply.

Third, the success of the bubble depends on the availability of wealth to drive the expansion into the commodity. This means that a substantial amount of disposable, convertible, or otherwise fungible wealth must be available at low cost to market entrants.

Fourth, the bubble draws in many market newcomers who seek quick wealth from the rapid price rise. These market neophytes do not have experience in evaluating market signals properly, and many have entered as a result of information transmitted by acquaintances. As a result, the new participants are ill informed about commodity characteristics. Indeed, they may care little about what they are buying because they entered the market to make a quick buck, not to acquire and hold the commodity. Thus, driven by greed, they hold the commodity too long before converting their profit, and get caught in, and contribute to, the fall.

Fifth, the dynamics of the bubble as well as the nature of many entrants raise issues about the ethical character of such markets. Some bubbles, such as the South Sea Bubble of 1720, were chiefly manipulations, having little or no value behind their securities. Others featured scams, product misrepresentations, and/or questionable marketing practices. In essence, the run-up was fueled by widespread deceit. Markets are considered normatively desirable at least partly because they respond to consumer choice—they feature *consumer sovereignty*. But how can markets be considered normatively acceptable if they treat consumers not as sovereigns whose choices must be respected, but as duped and deluded "fools" whose choices may be driven by contagion, shaped by market timing, and reflecting not commodity choice but a mindless greed that proceeds ignorant of the commodity's actual characteristics? Indeed, Edward Chancellor explicitly compares the speculation inherent in market bubbles with the behavior of carnival fools. Thus, the existence of bubbles raises important normative questions about the performance of markets.

Market bubbles have occurred periodically for centuries. Examples include the Tulipomania in the Netherlands in the 1630s, the South Sea Bubble in England in the early 18th century, the technology bubble in the United States in the 1990s, and the real estate or housing bubble in the United States in the early 21st century. Because all market bubbles burst, the suggestion by government policy makers that a bubble is under way can be sufficient to cause sudden stock market drops or even to collapse the bubble, potentially with disastrous effects. Thus, Alan Greenspan, chairman of the board of governors of the Federal Reserve in the United States, famously described market conditions in a 1996 dinner speech as a case of "irrational exuberance." Stock markets all over the world plummeted several percentage points after his speech. Thus, economic policy makers refrain from suggesting that markets seem to be becoming bubbles. As the real estate bubble of the early 21st century grew, it was common for analysts to instead decry the level of "froth" in the market, a description that avoided an outright labeling of the market as a bubble.

Tulipomania

As an illustration of a market bubble, consider the case of Tulipomania. Introduced from Turkey, tulips were a novel, colorful flower well-suited to the low lands of Holland. Interest in them grew steadily in the early 17th century. Growers had succeeded in producing enough of the flower to create expanding markets, with prices of common bulbs falling to levels that made them accessible to tradesmen, farmers, and laborers. The flower bulbs could be divided to generate more of highly desirable types, although the most desirable varieties, which we now understand to have been produced by a plant virus, remained scarce.

Holland was then at the end of a long recession, which turned into an economic boom by the early 1630s. Incomes in the country were the highest in Europe. While wealthy individuals continued to invest in joint stock trading companies and other vehicles focused on steady appreciation of wealth, the less well-off looked to quicker means of becoming rich. Banks were not used for savings by those with smaller amounts to invest, so other outlets for appreciation became attractive. Thus, the availability of savings for investment coincided with the rising interest in tulips. In addition, the bubonic plague was rampant in Holland during the peak period of the bubble—for example, it killed one eighth of the population of Haarlem in less than 2 years. This produced a labor shortage and, consequently, rising wages, making even more funds available for investment in tulips. Mike Dash, in his chronicle of the bubble, *Tulipomania*, suggests that an attitude of "fatalism and desperation" may have also contributed to the extreme behavior of the tulip traders.

Traditionally, tulip traders had traded only from June to September, as the flowers themselves could be seen in bloom. The bulbs were then traded, "lifted," and, eventually, as the season determined, planted again. As demand grew, this sequence was abandoned. By the fall of 1635, an active futures market, called the *windhandel*, or wind trade, in tulip bulbs had developed. Bulbs were traded on paper, rather than in physical form. In addition, personal credit agreements based on the future deliveries were made. Trades were turned over many times, and prices skyrocketed. Tulip dealers set contracts for bulb delivery in the spring that featured promises by purchasers to pay at a certain price at a certain date. A purchaser assumed that he could buy tulips at already high prices, paying a deposit to guarantee that price, to be paid when the bulbs were lifted in the spring. He assumed that the price would at that time be much higher, so that the bulbs could be sold, the dealer paid off, and the purchaser pocket the difference (or be compensated for the new, higher price). Although the tulip futures market was outlawed, being considered dangerous and even, according to Dash, immoral, it continued to flourish.

During 1636, the soaring market drew many new and inexperienced entrants, whose investments continued to fuel the futures market. One estimate is that the tulip trade between 1633 and 1637 totaled about 40 million guilders at a time when the whole Dutch East India Company was valued at 6.5 million. A single high-quality tulip bulb could sell for several thousand guilders. At the time, 3,000 guilders could purchase all of the following: 8 fat pigs, 4 fat oxen, 12 fat sheep, 24 tons of wheat, 48 tons of rye, 2 hogsheads of wine, 4 barrels of eight-guilder beer, 2 tons of butter, 1,000 pounds of cheese, a silver drinking cup, a pack of clothes, a bed with mattress and bedding, and a ship.

The tulip bubble burst in February 1637. Tulips fell suddenly in value to 5% and even 1% of their former trading level, and many markets simply ceased to function. Demand for bulbs had outstripped the supply—only low-quality bulbs, with absurdly high prices, were new to the market. At the same time, prices had exceeded the availability of capital to meet those levels. And chains of futures purchases meant that buyers were unable to meet their obligations by selling their contracted purchases at higher prices, so that the chains collapsed. The collapse occurred in advance of, and partly also in anticipation of, the lifting of the bulbs in the spring, as traders realized that the settlements that would be necessary then would be impossible.

Thus, the tulip bubble reflected many of the characteristic features of bubbles: The bubble in this novel commodity grew rapidly, drawing in novice participants who had funds available to invest. In this case, regulation of the futures market was ineffective. As quality tulips became less available, the commodity being sold became less unique. The huge existing investments left fewer funds available to purchase less desirable tulips. The looming deadline of the spring lifting in 1637 helped trigger an early collapse.

Of high interest in today's economy is the fact that such bubbles, if not in tulips, then in some other commodity, may be expected in the future.

—Barry M. Mitnick

See also Contracts; Economic Rationality; Economics, Behavioral; Efficient Markets, Theory of; Manipulation, Financial; Market Failure; Opportunism; Perfect Markets and Market Imperfections; Pricing, Ethical Issues in; Self-Interest

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Market Failure

The concept of market failure refers to the numerous ways in which real markets fail to display the characteristics and performances of theoretical or perfect markets and/or to generate social outcomes that are analytically superior to those produced by other means of societal allocation. The modern conception of ideal market exchange and its perceived benefits dates at least to the classic work of Adam Smith in *The Wealth of Nations* (1776).

Characteristics of a Perfect Market

The concept of a "perfect market" is an abstraction. A perfect market is an exchange system featuring many buyers and sellers; actors who pursue rational self-interest with completely free choice and stable preferences; perfect information held by all the actors; goods that are all private in character in that their consumption can be excluded from consumption by other potential consumers; exchange among the buyers and sellers that is costless; actors who begin their market exchanges with resource endowments that can neither increase nor change in quality or capability over time nor have any special characters or values (but can be used only to fund the exchanges); actors who are solitary and self-contained in that they act as atomistic, disconnected entities with no internal complexity and no external, dependent relationships such as stakeholder ties; no technology effects such as those that would cause markets of different sizes to behave differently so that trading in goods at different scales produces different behaviors; no by-product costs or impacts from the exchange, so the market itself is self-contained and has no memory or history, among other characteristics.

In contrast, real-world markets can violate any of these conditions. They can have few sellers and/or few buyers; consumers can be inconsistent in their choices and be influenced by other actors and historical patterns; false or incomplete product information can flood the market; buyers can collude with one another; the supply of goods can be joint, not private, in that once supplied to one consumer they are at the same time consumable by other consumers; there are many, and many kinds of, transactions costs in the market; actors can possess widely varying endowments of resources that can be transformed in quality and value by innovation and technology, yet for some actors may be too little or of such type or quality as to prevent those actors from using them to conduct any market exchanges or participate meaningfully in the market; production in the market produces unintended by-product effects not priced in the market; technology can cause rational market actors to collude and/or combine so that the market itself collapses into a single actor; information about all aspects of the market and its actors can be unevenly distributed and costly to elicit; market actors are often internally complex, as in firms, and intricately interdependent with stakeholders who affect or are affected by the actor, that is, the firm; and so on.

Pareto Optimality

Perfect markets are held to be desirable because they can produce the exchange condition that economists label *Pareto optimality*, after the Italian economist Vilfredo Pareto (1848–1923). In the exchanges leading to Pareto optimality, market participants have employed their endowments to make exchanges with other participants in response to their self-interest and their perfect knowledge of available exchanges. Participants are driven by the benefits of each exchange to continue to trade until they can no longer—either they have exhausted their endowment or, what is equivalent, there is no available trade that will make them better off. In other words, there is no trade available that will make at least one actor better off while leaving the other actors indifferent to the exchange. Such a condition is, in essence, the best of all possible worlds available to market participants at that position in the sense that they cannot move to any state where they would be better off. Movement toward that condition is also desirable—any trade that makes at least one actor better off while no other actor is harmed is a *Pareto efficient* transaction.

Now, being at a Pareto optimum does not mean that every actor is at his or her own optimum possible through market trade, that is, that the result is globally optimal—there can be many possible positions of the market in which no further trades are possible without making at least one actor worse off. In other words, trade could have brought the actors to other, perhaps better positions that would also have been Pareto optimal in that no further exchange would be rational. An abstract, perfectly competitive market can produce a Pareto optimum, but cannot guarantee that each and every actor in that market will be in a globally optimal position when that optimum is reached.

The obvious problem is that, just as perfect markets are an abstraction that the real world can only approximate in rare instances, so would a perfect market that has traded its way to Pareto optimality be more abstract than real. Although one can easily think of situations in real market exchange that would be Pareto efficient, and perhaps see trading systems that trade their way to an end point in which no further trades are volitionally possible, one cannot consider the result Pareto optimal in any global sense. The absence of trading opportunities does not mean that the cessation of trade has resulted in the best of all possible worlds for all actors, especially given that the market in which trading occurred was not perfect. And trading to a Pareto end means only that in available trades market actors took maximal benefit from the endowment with which they began trading, not that the condition of the world at the end of the trade was in any larger sense optimal.

To the extent to which the normative defense of markets rests on the perfect market's display of Pareto optimal outcomes, the judgment of market success or failure depends on an essentially procedural criterion. The optimal end point has value only in the way it was reached and in the absence of possibility of actor benefits beyond the end point. Nothing whatsoever is said regarding the relative desirability of actual end states. Nothing matters about which actors are benefited in what ways, but only that no further enhancement of those benefits will be chosen by the market actors. Thus, markets fail in the sense of being unable to function in ways that produce outcomes that in and of themselves may be recognized as invariably more desirable than those produced by other societal means of allocation.

The Stakeholder Paradox

Setting aside the notion of whether markets produce desirable outcomes, one can examine whether the essential characteristics of markets by themselves provide support for the value of markets. One such characteristic is *consumer sovereignty.* Under consumer sovereignty, markets are understood to be driven by the choices made by market participants, consumers. No authority dictates market exchange or exchange values, that is, prices. In essence, markets are decentralized exchange systems that defer to the freely expressed judgments of market actors. Normative value may be attached to consumer sovereignty to the extent that any principle of freedom of choice has normative content. Thus, no matter their outcomes, markets may be judged desirable simply because they are economic systems that permit free choice.

But market participants are not all individuals. In the modern economic world, many economic actors are, of course, corporate actors. The criterion for the success of such an actor is typically given as the maximization of its value. That is, the firm as corporate "person" is operated in the market so as to provide maximal benefit to its owners by maximizing the value of their holdings in the firm.

A paradox, here called the *stakeholder paradox*, follows: Markets are held desirable because they permit free choice to their participants (consumer sovereignty) and because they permit the unfettered pursuit of shareholder value. But the two principles—consumer sovereignty and maximization of shareholder value, in essence, shareholder sovereignty—do not necessarily coincide. The unregulated pursuit of one can be invidious to the realization of the other.

Consider, for example, the case of the diabetes drug Rezulin, which was marketed by Warner-Lambert (later acquired by Pfizer). Rezulin's side effects led to the deaths of more than 60 people who took the drug—all, of course, quite literally, consumers. Warner-Lambert kept the drug on the market well past the time at which the lethal side effects were recognized, and it kept the drug on the market because it was extremely profitable. Warner-Lambert earned more than $1 billion from the drug until it was finally obliged to withdraw it, less its costs from the legal actions of surviving family members. Even after subtracting the costs of the civil actions, the drug provided an enormous profit to Warner-Lambert and, of course, ultimately, value to its shareholders and those of its corporate heir, Pfizer.

Thus, the interests of consumers and of shareholders do not necessarily coincide. In other words, the normative world of markets is not the same as the normative world of firms. Nor would the general argument be in essentials different if one were to substitute other stakeholders, such as employees or the local community, for consumers. The stakeholder paradox prescribes that normative principles that are generated in support of one stakeholder cannot be sustained in preference to those generated in support of any other. One cannot necessarily apply a moral principle derived from and/or applied to market behavior to the behavior of any other stakeholder, and vice versa. Thus, the performances of markets, and of their corporate participants, firms, fail to generate support for any overarching normative principle or principles that would support the general desirability of markets.

Some Forms of Market Failure

There are a number of ways in which the behavior of empirical markets diverges from that expected in perfect markets. In example, three classes of such failure are identified below: market failures related to the characteristics of goods traded in markets, market failures related to the characters of market participants, and market failures related to market structures and performances.

Characteristics of Goods

Pure *public or collective goods* are goods such that their consumption is joint or "nonrival," and "nonexcludable". Thus, once provided to one consumer, they are provided to others, without diminution due to the consumption of others (i.e., their consumption is nonrival). National defense is one example. Furthermore, the good cannot be excluded from consumption by others. An example is air pollution—once provided to one consumer, it is provided to all, and it is not feasible to exclude some from consuming it. Goods vary in their degrees of jointness/nonrivalness and excludability. As the economist Mancur Olson described, public policies act like public goods—once the benefit of the policy is available to one citizen, it is available to all. Markets fail to provide optimal levels of public goods, because potential contributors to the supply of such goods judge that they can be *free riders* on the contributions of others—they will enjoy the good whether or not they contribute because of its public character. Hence, positively valued public goods will be inappropriately priced, or priced not at all, and be in chronic undersupply. And negatively valued public goods, such as air pollution, will not be part of market exchange.

The demand for public goods, particularly in view of their artificially low apparent market price, can generate *congestion* effects. Congestion can mimic the effects of rivalry or exclusion, as high demand for the good interferes with consumption of the public good.

Goods also vary in the extent to which consumers can evaluate their characteristics, including their quality. Markets will fail to perform adequately because the normal forces of supply and demand will fail to operate if consumers cannot make choices based on full or correct information regarding the goods they are purchasing. *Search goods* are goods that require consumers to invest in their detection or evaluation in advance of purchase. Absent payment of search costs, consumers will either fail to purchase goods or purchase goods that may not have the characteristics that the consumers would prefer. Or they may rely on simplifying and economizing heuristics, such as brand, product reputation, or ratings or product referrals. These may not, however, actually direct the consumer to the optimal purchase.

Experience goods can only be evaluated after purchase. But postpurchase evaluation increases the chances for consumer error. Because consumers essentially precommit to a particular good before being able to make their own judgment of how well it meets their preferences, it becomes more difficult for consumers to acquire more highly preferred goods. If the good does not measure up, consumers are faced with paying the perhaps considerable costs of exchange or replacement of the good. Consumers can attempt to deal with the issue by seeking out reports of the experiences of others, such as product ratings, or purchase warranties as a form of insurance against products that turn out to be of low quality.

Credence or *trust* or *postexperience* goods are those goods whose qualities are not evident even after consumption. In essence, the consumer must trust in their performance. Prescription drugs that have long-term negative side effects fall into the category of credence goods, as do those prescribed by physicians when the patient is unable to detect either the illness or its resolution. An example is medication against high blood pressure or against high cholesterol. The problems may have been detectable only by the physician; while taking the drugs, the patient feels no different than before. Markets cannot provide the appropriate evaluations to consumers; consumers must often seek out skilled agents to interpret their need for the goods as well as the performance of the good.

Characteristics of Market Participants

Markets can be unable to provide appropriate judgments of the performance of agents in agent-principal relationships; flows of information can be asymmetric. In *adverse selection*, the principal can observe the agent's behavior, but is unable to judge whether that behavior is optimal in the agency relationship, that is, whether the agent is serving the principal with the quality expected. The context often offered is that of employment, in which an agent has expertise not shared by the principal who engaged him or her. The principal is consequently unable to judge whether the agent is doing work of highest quality, because he or she cannot evaluate it directly. Kenneth Arrow termed the problem of being unable to judge quality, the problem of *hidden information.* According to Barry Mitnick, the problem of adverse selection actually conflates two kinds of problems. One, *adverse claims*, relates to the difficulty encountered by principals in trying to evaluate the qualities of prospective agents. The second, *adverse performance*, relates to the different problem of evaluating an agent's performance when he or she is being supervised within an agency relationship, such as an employment relation. The methods and measures used by the principal are different across these cases.

A second general agent-principal problem, termed *moral hazard*, occurs when the principal could judge the optimality of the agent's behavior, but cannot observe it so as to be able to apply that expertise. The most common examples are taken from insurance contexts. The existence of insurance leads agents to reduce the care with which they treat insured objects. Insurers can tell the difference between careful and careless behavior, but cannot observe the insured to see if his or her actions are consistent with good care. Arrow thus terms the problem of being unable to observe, a problem of *hidden action.*

In general, market participants may be unable to appropriately evaluate the risks of market actions or may display any of a number of biases of social cognition in evaluating their market participation and/or the qualities of the goods they seek in the market (see, e.g., the work of such scholars as Amos Tversky, Daniel Kahneman, and Baruch Fischhoff). The market by itself cannot compensate for these effects.

Characteristics of Market Structure or Performance

Markets often cannot take account of the production of goods or effects that are generated as unintended by-products of the primary task of producers. These goods are termed *externalities.* Often these goods have negative impacts, and so escape market pricing—no one wants to purchase them. The most common example is environmental pollution. Positive externalities can also be produced and can experience problems with market inclusion because their origin may be unplanned and unstructured. Thus, creation of a public park may have the unintended by-product effect of increasing the value of nearby houses. But the market has no means of capturing that added value, other than in the increased selling price of the houses. In that case, the benefit of the park is transferred to increased income for the sellers of the house. The municipality cannot recover the benefit bestowed on the homeowners from the placement of the park (except, perhaps indirectly, via house transfer taxes tied to selling price and increased property taxes).

A second structural problem for markets stems from the transaction, information, and bargaining costs attending market interactions. Market participants may make suboptimal choices because of the costs of extracting information from the market; it may not be rational for such participants to pay the cost of getting complete information because the costs of extracting information and assuring its quality exceed the benefits of doing that.

A third problem for markets that comes from structural or performance characteristics arises when buyers or sellers combine so that markets collapse into monopsony (one buyer) or monopoly (one seller). Such market structure problems can, of course, be the result of deliberate manipulation unrelated to underlying market defects, as when entrepreneurs create cartels to control pricing and reap monopoly profits. A condition of *natural monopoly* occurs when average cost declines with increasing demand for the product or service. In essence, producers can economize by combining their production, reducing the average cost of producing a unit of the product or service. The rationale for public utility regulation rests on fears that unregulated utility markets will collapse to natural monopolies as producers see the advantages of building only a single distribution network rather than several, parallel, competing ones. It is the technical characteristic of the product or service that structures cost so that only one system makes economic sense. As a result, the market cannot be sustained, and, indeed, rational market exchanges will result in collapsing the market to a monopoly. The resulting single producer can then extract monopoly profits from consumers with no alternative market choices.

A fourth market problem is reflected in business cycles, as the economy cycles between boom and recession. Markets cannot manage such cycling on their own. Such cycles require the intervention of central banks and other economic policy actions to shape the cycling in ways that produce healthy, sustained market competition.

General Issues in Market Failure

In general, markets have no mechanisms for incorporating public or community interests; they are good in attending to the wants of consumers but poor in balancing interests across society. Markets ignore disparities in original endowments; they have no means of redistributing society's wealth to aid the least advantaged. Markets have no mechanisms for resolving disputes or conflicts of interest other than the raw application of economic power. Indeed, one prerequisite to a successful market system is a government that can establish, operate, and defend a legal system that protects private property and establishes limited liability for corporate investors. Finally, markets cannot protect employees lacking market power from exploitation. After all, one rationale for government regulation is to create a governmental protector or agent to serve interests who have no ability to protect themselves.

Thus, although markets are the centerpiece of Western economic systems, and are commonly valued for their mimicking of the democratic values of free choice, both their normative principles and their behavioral characteristics can fail to provide the satisfactory rationales as well as performances that are essential in a modern, complex society.

—Barry M. Mitnick

See also Adverse Selection; Arrow, Kenneth; Asymmetric Information; Cartels; Collective Choice; Externalities; Free Market; Information Costs; Market Bubbles; Monopolies, Duopolies, and Oligopolies; Monopsony; Moral Hazard; Pareto, Vilfredo; Pareto Efficiency; Pollution Externalities, Socially Efficient Regulation of; Public Goods; Public Utilities and Their Regulation

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Market for Corporate Control

The market for corporate control (MFCC) is a market in which one or a set of investors may attempt, and sometimes succeed, in securing management control of a firm from another set of investors through the trading of shares. This may be done, for example, by friendly or hostile takeovers by means of a tender offer, or by mergers or acquisitions negotiated by the board. It is mainly relevant for public listed corporations; shareholders in unlisted corporations often have restrictions on how they may dispose of those shares (such as a veto power by other shareholders).

The MFCC serves as an external corporate governance mechanism by ensuring that management acts to maximize shareholder value through efficient use of a corporation's resources irrespective of whether current shareholders are satisfied with management's performance. If shareholder value is not being maximized, new investors can, in theory, create value for themselves by taking control and putting in place managers who they believe can maximize shareholder value, or by one organization taking over or merging with another to create value through, for example, transfer of core competencies or increased market power. Although, in general, the MFCC creates shareholder value, the evidence suggests that the shareholders of the target company often gain a larger portion of this value than the shareholders of the acquiring company.

All public corporations are subject to the MFCC, including those that are efficiently and ethically managed: It is not just a mechanism for disciplining ineffective management. As the MFCC encourages managers to do what they should already be doing, control does not have to be transferred for the mechanism to be effective: The threat of the transfer is an equally effective, and in some cases a more effective, corporate governance mechanism.

The MFCC is more effective as a corporate governance mechanism in countries where shareholdings are dispersed and there is high liquidity, such as in the United States and the United Kingdom, but generally less effective in countries where there is often a controlling shareholder, such as in Germany, or a controlling group of interconnected shareholders, such as the Japanese *keiretsu*. In such instances, the role of the MFCC is replaced by direct monitoring of management. Even where the Anglo-American model of corporate governance is entrenched, the MFCC may not be effective; in Kenya, for example, there has not been a single hostile takeover since the stock exchange was founded in 1954, and in 2005 the turnover ratio was only 7.9%.

There are three broad groups of ethical issues raised by the MFCC. The first group relates to the social consequences of changes of control. The MFCC effectively forces managers to maximize shareholder value even when this is at the expense of other stakeholders. For example, if a firm pays wage rates above those of its competitors, or engages in activities such as education or health care, protecting the environment above regulatory minima, or philanthropy, then it is effectively transferring value from shareholders to other stakeholders. Although this may be ethical business practice, the MFCC punishes such behavior: Those taking control of the firm do so to increase shareholder value not by creating additional value but by transferring value back to shareholders through reducing wages and cutting programs. Changes of control may also result in relocation or rationalization of operations, which may have devastating impacts on local communities. An even larger impact may result from especially Western corporations using their advantages in, for example, technology and access to cheaper financing to take control of corporations in developing countries and then expatriating profits, thereby undermining the economic development of such countries.

The second group of ethical issues relates to the tactics used in the MFCC, especially those used to thwart it, as they may have negative side effects. To make changes of control more difficult, a corporation may, for example, (1) incorporate in a jurisdiction in which legislation makes hostile takeovers more difficult; (2) put in place the so-called shark repellents such as poison pills (e.g., a conditional rights issue) and golden parachutes (massive severance packages for directors and senior managers in the event of a takeover); (3) take over a competitor to make the merged corporation too large for the potential acquirer, or if the potential acquirer is a competitor, make antimonopoly regulator approval more difficult; (4) act to artificially inflate the share price through market failures such as the exploitation of information asymmetries, making it more difficult for outsiders to finance the purchase; (5) use different share classes, for example, a family-owned corporation may give family members (or any corporation may give as remuneration to current directors and managers) shares with voting but not economic rights; (6) have large, but not controlling, shareholders act together to effectively control the corporation, which in some jurisdictions is illegal; or (7) sell the corporation to a friendly suitor (the "white knight" defense). There are also opportunities for unethical behavior on the part of the outsiders, especially for "greenmail," in which a raider begins purchasing shares and threatens a takeover, and then offers to sell the shares to other shareholders or management at a premium if they wish to retain control.

The third group of ethical issues relates to the fiduciary duties of managers in change-of-control situations. The managers of a corporation have an obligation to act in the corporation's best interests. Some changes of control are in a corporation's best interest, and managers have a duty to facilitate them even if it means that they will personally suffer negative consequences, including loss of employment. In other instances, the change is not in the corporation's best interests, and managers must try to prevent it even though, for example, they may have personally profited from it such as by a golden parachute. It is unethical for managers to acquire another corporation simply to increase their own prestige and remuneration if it does not increase their own corporation's value. Hostile takeovers raise ethical issues if proper due diligence cannot be undertaken, because in that case the shareholders of a company cannot properly evaluate the risk that is involved.

Although the MFCC is useful as a corporate governance mechanism in only a small number of countries, and even in those countries appears to be more effective as a threat than when effected, it plays an important corporate governance role in those countries by helping to ensure that managers consistently act to maximize shareholder value. Nevertheless, it raises many ethical issues that need to be addressed through legislation and regulation, listing rules, corporations' constitutions, and shareholder activism.

—Royston Gustavson

See also Leveraged Buyouts; Mergers, Acquisitions, and Takeovers

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Market for Lemons

George Akerlof developed the idea of the market for lemons to explain problems related to information asymmetries in markets. "Lemons" refer to used cars that are of poor quality. If there are two types of cars on the market—those of high quality ("cherries") and those of low quality ("lemons")—and the buyers and sellers can easily determine which category a cars falls into, then both types of cars will be sold and high-quality cars will sell for a higher price than low-quality cars. In the real used-car market, however, there is an information asymmetry problem because the sellers of cars know more about the quality of cars than the potential buyers. Because the quality of a used car may be difficult and costly for the buyer to determine (and the seller may still have an information advantage due to actual experience with the car), the buyer will want to avoid the risk of paying a high price for a low-quality car. To do this, the buyer will assume that all cars are of an average quality. This assumption will cause the demand curve for high-quality cars to shift down (decreasing the supply of high-quality cars), but cause the demand curve for low-quality cars to shift upward (increasing the supply of low-quality cars). Over time, this shifting of the demand curves will continue to occur until only low-quality cars are sold. This is a market failure because there is no longer a choice of cars of various quality levels for the consumer to choose from. Instead, only sellers of "lemons" will be participating in the market.

The above analysis can also apply to the markets for health insurance, financial credit, and other markets with information asymmetry problems. In health insurance, for example, the buyers of insurance will have an advantage over sellers with respect to information on the quality of the buyer's health. As a result, unhealthy buyers purchase insurance at the price of an "average" buyer, which then forces up the price of insurance and causes healthy buyers to choose not to be insured (which further increases the proportion of unhealthy buyers as holders of insurance). Over time, the market fails. This problem is referred to as adverse selection.

Potential solutions to the lemons problem include signaling and developing a positive reputation. Signaling involves actions that allow sellers to distinguish their high-quality products from sellers of low-quality products, although buyers cannot determine the level of quality until after they make a purchase. For example, sellers of high-quality cars could offer a warranty or money-back guarantee on their car because they know that buyers will rarely need to use the warranty or guarantee after a purchase. Sellers of low-quality cars, on the other hand, could not afford to offer such warranties, because buyers would exercise those rights and create additional costs for the seller. Thus, the presence of a warranty may provide a useful signal to buyers as to the true quality of the car and they will no longer make the assumption that all cars are of average quality. Likewise, if the seller develops a positive reputation, then buyers may be willing to trust the seller's statements as to the quality of the car and avoid the market for lemons problem.

—David Hess

See also Adverse Selection; Asymmetric Information; Free Market; Perfect Markets and Market Imperfections; Signaling

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MARKETING, ETHICS OF

Marketing ethics is the systematic study of how moral standards are applied to marketing decisions, behaviors, and institutions. Because marketing is a process inherent to most organizations, marketing ethics should be viewed as a subset of business ethics; thus, much of what is written about business ethics applies to marketing ethics as well. At the outset, it is also useful to distinguish between *positive* and *normative* marketing ethics. Positive marketing ethics looks at marketing practices from the standpoint of "what is." For example, specifying the percentage of organizations that have codes of ethical marketing practice or tracking the number of violations that deal with *deceptive advertising* would be examples of positive marketing ethics. In contrast, normative marketing ethics deals with how marketing *ought* to operate according to some moral standard or theory. The sort of moral standards (or theories) applied to marketing situations involve the usual moral frameworks commonly applied when evaluating business ethics (e.g., utilitarianism, duty-based theories, virtue ethics). When the words "marketing ethics" appear in the general media or business press, the reports typically describe a marketing strategy, tactic, or policy that some constituency feels is "unfair" or "exploitive" or "deceptive." Often, the subsequent discussion turns to how marketing practices might become more consumer-friendly, socially compatible, or put in philosophical terms, how marketing might be *normatively* improved.

Normative marketing practices might be defined as those that emphasize transparent, trustworthy, and responsible personal and/or organizational marketing policies and actions, and exhibit integrity as well as fairness to consumers and other stakeholders. In the true spirit of normative ethical standards, this definition provides certain virtues and values (e.g., trust, fairness) to which marketing practitioners ought to aspire. However, the definition also raises myriad questions. What do we mean by transparent? Does that mean no trade secrets are ever allowed? What is the essential nature of integrity? Does it mostly involve keeping organizational promises to customers or is it broader than that? What is the nature of fairness, and who decides what standard of fairness is to be applied? Should it be consumers, the company at focus, regulatory agencies, or a broader cross-section of society? What stakeholder interests should be taken into consideration, and how should they be weighted? As one can see from these questions, the area of normative marketing ethics is likely to generate considerable controversy because there are differing views among various parties about what constitutes "proper" behavior in marketing.

General Perspectives

Because marketing is the organizational process focused directly on exchange, ethical issues in marketing have existed since the inception of trade. The Roman philosopher Cicero counseled merchants to avoid raising prices too high in times of shortage, lest they alienate their customers, who might shun them when supplies were more abundant. However, the analysis of marketing ethics from a more systematic and analytical standpoint has only begun to develop in the past 40 years. Since the mid-1960s, the literature on marketing ethics has grown substantially. A recent 2005 ABI/Inform literature search using the term *marketing ethics* as its search query generated a list of more than 400 citations to the literature—all of which presumably addressed marketing ethics in some scholarly form or fashion. While cynics view the term *marketing ethics* as an oxymoron, no doubt due partly to the frequent questionable activities of some used car dealers, advertising copyrighters, and telemarketers, there exist clear and articulated standards of proper behavior that are "peer endorsed" by marketing practitioners. In other words, marketing managers themselves have expressed their opinions as to the ideal obligations inherent in the honest and forthright conduct of marketing. Perhaps the best known of these codes of conduct is the American Marketing Association's (AMA's) "Statement of Ethical Norms and Values for Marketers." This document—endorsed by the largest professional organization of marketing practitioners in the world—and available for review at www.marketpower.com (search: code of ethics) specifically states that marketers serve not only their company enterprises but also act as stewards of society in creating, facilitating, and executing the efficient and effective exchange transactions that are part of a greater economy. The AMA statement recognizes the duties that marketers have to all stakeholders (e.g., customers, employees, investors, channel members, regulators, and the host community) as they discharge their job responsibilities. This document explicitly warns that marketers must not knowingly do harm in executing their selling responsibilities, that marketers have a duty to foster trust in the marketing system, and that they should embrace basic marketplace values, including truth telling, genuine service to customers, avoidance of practices acclaimed to be unfair, and an adherence to honest and open communications with clients. Significantly, it states that marketing organizations have responsibilities of "citizenship" just as individuals do. Documents such as the AMA Statement represent hard evidence that there are bedrock ethical standards and values that have been agreed on by numerous marketing practitioners.

Of course, the extent of practitioner compliance with these values is another issue. Over the years, surveys of marketing managers report that the vast majority of practitioners discharge their job responsibilities in a lawful and meritorious manner. Nonetheless, every year brings its share of horrific and controversial marketing blunders. Current issues in the news involving marketing practices have to do with price-gouging when gasoline shortages occur (as they did in the wake of Hurricane Katrina) and stealth marketing techniques such as surreptitiously gathering information about consumer patterns when they surf shopping sites on the Web. In general, national opinion polls of the public suggest that marketers have plenty of room to improve their ethical performance before it conforms to public expectations. Perhaps the "truth" about marketing lies somewhere between the practitioners view that marketers are predominantly "good guys" and the public perception of marketers as suspect purveyors of sometimes dubious goods and services.

While the above-mentioned statement of AMA of "norms and values" is partly inspirational in nature, there has also been substantial effort expended by marketing academics and ethics scholars to develop pragmatic models of marketing behavior that delineate the factors that shape and affect ethical (or unethical) marketing decisions. An example of such a work (*positive* marketing ethics) would be the Hunt-Vitell model of marketing ethics—a framework that has been subjected to extensive empirical testing. This complex model takes into account various factors such as (1) environmental dimensions in industry and the organization influencing ethical actions, (2) the recognition by decision makers of an ethical problem and its likely consequences, (3) the teleological and deontological norms used by marketing decision makers that might affect their selection of various alternative choices, (4) the type of ethical judgments made in various situations, (5) the formation of any intentions attributable to the marketing practitioners at focus, and (6) a measure of the outcomes of actual behavior. The purpose of weighing the myriad factors involved in real-world marketing decisions associated with ethical questions is that it helps specify the gaps between what the actual behavior of marketing practitioners *is* versus how far managers need to go in order to be in conformance with various marketing ideals. Empirical studies, using models such as Hunt-Vitell, have suggested, for example, that the standards managers use to address ethical questions vary considerably (e.g., some are utilitarian; some derive their perspectives from religious traditions). Moreover, the response to ethical issues by managers depends on the issue being addressed. For instance, the majority of managers might be very concerned that clandestine competitive intelligence gathering is growing in their industry but most may not be bothered by "puffery" (advertising exaggeration). Yet both practices are subject to ethical debate in the public realm. It is in the conduct of such systematic *ethics research* that the positive and normative aspects of marketing come together because marketers can learn what to "fix" based on what is actually going on.

Marketing Practice

At the heart of marketing ethics are decisions that marketing practitioners make about ethical questions. Ethical questions most often arise in marketing when a stakeholder group or some segment of the public feels that the actions taken by some (or many) marketers might be judged to be morally inappropriate. Currently, for instance, many consumers feel that *spam* advertising over the Internet is far too prevalent and/or that product rebates have too often been intentionally made to be difficult to redeem. Similarly, other ethical questions occur when marketing managers believe that they might be compromising their own personal values in the quest for increased organizational profit. In such situations, marketers are often evaluating whether they should take *business* actions that they feel ought *not* to be done from the standpoint of *personal* ethics that they hold—the essence of an ethical dilemma. Most managers cannot avoid facing such tough issues because the majority of marketing professionals report confronting such ethical questions at some point in their careers. These "ethical" branch points can pertain to a host of marketing issues such as selling cigarettes to teenagers, the promotion of violence-oriented video games, pricing products at a level that exploits unsuspecting consumers, bluffing in negotiations with long-time suppliers, writing intentionally misleading ad copy, and so on. If the marketing actions that are taken happen to be in violation of the law, these are also typically characterized as unethical. However, our focus in this entry is particularly on actions that are *not* illegal but that are criticized as "improper" according to some ethical value or norm. Therefore, marketing ethics is mostly focused on marketing behaviors that are not prohibited by the law but perhaps should not be indulged due to certain moral considerations. And thus, marketing ethics is often concerned with actions that are currently legal but still might be judged improper according to some invoked moral standard. For instance, NASCAR has every legal right to have their automobiles sponsored by and festooned with the logos of brewers, distillers, and other alcoholic beverage makers. Whether it is ethical to link speeding race cars to alcohol beverages given the significant "driving while intoxicated" problem that exists in the United States is a matter for debate.

Most generic areas of marketing practice provoke substantial ethical comment and discussion. These areas include marketing segmentation, marketing research, product development, pricing, distribution, personal selling, and advertising. In the paragraphs below, a sampling of marketing issues, often suggesting ethical questions from these areas of marketing practice, is briefly reviewed to illustrate both the nature and the scope of marketing ethics in the conduct of business operations.

Market Segmentation

One of the basic strategies of marketing campaigns involves the division of the mass market into "segments" followed by the development of specific offerings to appeal to the selected "target market." Ethical questions especially surround the target marketing of segments that include potentially vulnerable populations such as children, the elderly, the impoverished, and marketing illiterates. The "ethical issue" at focus here centers on whether marketers have too much "power" over certain groups who are not prepared to independently participate in the marketplace.

For example, children are a $25+ billion market in the United States alone for products such as toys, sugared cereal, DVDs, and video games. One major ethical question involves the extent to which marketers can freely treat children as "consumers in training" (mini adults) subject to pretty much the same promotions as the rest of the (adult) market. For young children (less than 8 years old), there is the issue of whether they even understand the difference between (for instance) television advertising and the programming itself. For older kids, the ethical issues might focus more on the appropriateness of certain products (violent video games), or the degree to which young teenagers might be susceptible to particular kinds of provocative fashion or lifestyle advertising. The key issue involved in targeting children turns on whether marketers should be held to a higher standard care and caution when marketing to children. One illustration of emergent constraints when approaching children involves the passage of the Children's On-line Privacy Protection Act of 1998 that was promulgated because of significant parental concerns regarding the collection of market research information data over the Internet from children younger than 13. Essentially, this federal legislation, inspired by numerous ethical questions raised by the general public, prohibits the collection of any personal information by market researchers from "under 13s" without verifiable permission from parents allowing it.

Similar questions about vulnerability to marketing scams occur with regard to older consumers—especially those more than 80 years of age. Such seniors are living longer, and as they grow older, they become less confident in their decision-making ability and become potential targets for the fraudulent sales of financial services, vacation packages, insurance annuities, and prescription drug plans—to name only a few product categories. As the baby boomers grow older and make up a larger percentage of the population, the focus on the appropriateness of marketing practices to this senior segment will only increase in prominence. Various scams that exploit seniors (e.g., sweepstakes that promise winnings but are designed only to sell magazines) are reported in the press almost weekly.

Marketing Research

Since marketing decisions are often data driven, market research techniques and outputs are frequently used by marketing practitioners. Market researchers themselves often have considerable training in methodological and statistical techniques, and one might surmise that because of their greater education, they exhibit a higher degree of ethical professionalism than other marketing practitioners. Certainly, it is true that various professional organizations related to the practice of marketing research such as the Council for Survey Research, the Market Research Society and the European Society of Marketing and Opinion Research have developed detailed codes of ethics addressing common conflicts that occur in the execution of marketing research. These "conduct codes" of these professional organizations can be accessed at their Web sites and provide a modicum of guidance for marketing researchers when facing common situations that occur as part of the research process. These codes stress that tactics such as protecting respondent confidentiality when it is promised, not misrepresenting the identity of the research sponsor, properly disclosing research procedures, and many other professional practices should be adhered to.

Additional ethical issues arise owing to the fact that marketing research often involves contact with the general public, usually through the use of surveys that are increasingly being conducted online. Because marketing research activity relies heavily on publicly submitted information, some of which is personally sensitive, marketing research is ripe for ethical abuse or misuse. As survey research has become digitized, researchers have gathered substantial records about consumer product and service usage as well as their satisfaction. As a result, the issue of *consumer privacy* is at the forefront of marketing research ethics. It is hoped that the coming decade will yield definitive answers about the extent of privacy protection that consumers can expect when shopping online. Second, most marketing research is conducted by for-profit organizations to aid decision making within corporations. As a result, the profit motive may cause researchers or their clients to compromise the objectivity and precision of the research that is undertaken. Researchers inherently want to provide support for the outcomes their sponsors hope to find. Clients basically want the research they conduct to tell the best possible story about their company and their products. It should not be surprising then that marketers sometimes fall to the temptation of misusing market research information by manipulating or exaggerating the results.

Product Management Ethics

Ethical issues surrounding the management of products are central to marketing because the marketing process generally begins with a product (broadly defined to include goods, services, or ideas). The most common ethical concerns in this area pertain to the safety of products. Earlier, in the brief discussion concerning the AMA practitioner norms and values, the notion of "never knowingly doing harm" was introduced as a central ethical percept. Certainly, this prescription directly applies to the area of products. That products are safe "for their use as intended" is a basic consumer expectation and is embodied in common law within the concept of "implied warranty." While the sale of safe products is a fundamental marketing expectation, many consumers remain skeptical as to whether they are likely to receive this protection. A 2005 Yankelovich/MONITOR poll of consumers found that 61% agreed that even long-established companies cannot be trusted to make safe, durable products without the government setting basic industry standards. Indeed, a minimal base line of consumer protection in this area is assured via regulation by the U.S. Consumer Product Safety Commission, which has the general mandate to oversee product safety in the United States. Other government agencies also oversee specialized areas of product category such as the U.S. Department of Agriculture, the Food and Drug Administration, and the U.S. Department of Justice, which has specific jurisdiction for alcohol, tobacco, and firearms.

Despite all these protections, perennial ethical questions about product safety continue to be asked: How safe should products be? How safe is safe enough? When products harm consumers in the course of normal usage, who should be held liable? Too often marketers fail the safety test. For example, each Christmas season various consumer advocacy groups identify and publicize toys that are potentially dangerous to young children unless used with extreme care and under adult supervision. And, exactly where to draw the line in automobile safety is a never-ending debate. Should SUVs, which American consumers both love and demand, roll over as often as they do? Should side air bags, which consumers generally are reluctant to pay for as "add-ons," be mandatory because they can prevent serious injuries?

Another growing area of concern is product counterfeiting. Product counterfeiting involves the unauthorized copy of patented products, inventions, and trademarks or the violation of registered copyrights (often for the purposes of making a particular product look like a more popular branded leader). Common examples of product counterfeiting include fake Rolex watches, knockoff Levi jeans, and illegally pirated video and audio tapes of popular movies and music. It is estimated that product counterfeiting costs American companies $450 billion in sales each year. Product counterfeiting is unethical and, in most markets around the world, illegal as well. Counterfeiting is unethical because it involves an attempt to unfairly capture the "goodwill" created by one company's brand equity and unfairly transfer it to a knockoff product without royalty payment to the originating party. Simply put, counterfeiting is a form of intellectual theft. Interestingly, the majority of college students in the United States find "downloading" music from the Internet without paying to be a mostly harmless and ethical practice. With the expansion of China's economy and the many knockoff products that seem to originate there, product counterfeiting will be a major ethical issue for organizations in the early part of the 21st century.

Another instance of common ethical concern involves products that create problems for the physical or natural environment. Examples would include product packaging that is not biodegradable; products that use inordinate scarce resources such as large sports utility vehicles (e.g., the Hummer) along with their unusually low fuel mileage; various chemicals and detergents that pollute the land, air, and groundwater when improperly disposed of; and medical wastes that are sometimes dumped into oceans or lakes because the proper disposal of such material is burdensome for the user. Contributing further to all this is an increasingly "disposable lifestyle" in many developed countries that generates waste-handling problems, a residue of the convenience-oriented mentality—fueled by marketing. For example, the average American generates approximately 4 pounds of garbage a day of which 30% represents product packaging. The fundamental ethical issue connecting all these ecological examples is that of *externalities.* Basically, externalities are costs that are imposed on the society as a whole that are not paid for by the original producer or consumer. To take an obvious example, when beer bottles and soft drink cans are littered in public parks or recreational areas, the cleanup of that packaging represents an "externality." As a response to all this, a "green marketing" movement has developed, which puts a premium on product marketing and programs being compatible with environmentally protective principles. To this end, some organizations have embraced the Coalition for Environmentally Responsible Economies (CERES) principles—some of which speak directly to marketing-connected issues. In general, these principles involve adhering to an environmental ethic of strong commitment to ecological excellence as well as human health and safety. The CERES principles, which can be accessed online, are yet another normative code of conduct to help guide marketing actions in particular areas of operations.

Pricing

Perhaps no area of managerial activity is more difficult to assess fairly and to prescribe normatively in terms of morality than the area of pricing. The given price of a product or service commonly results from the confluence of three factors: *demand*, *competition*, and *cost.* Each of these factors can be central to ethical questions about pricing fairness. For example, when high demand puts pressure on supply, such as the desperate need for construction materials after a natural disaster, there may be a temptation for sellers to price-gouge. Or in an attempt to gain dominant market share, strong competitors may use predatory pricing (below cost pricing) to drive economically challenged sellers from the marketplace. In a business-to-business setting, a vendor may simply mislead a client concerning what "actual costs" have been incurred especially if they are operating under a "cost plus" pricing contract. While there is agreement that sellers are entitled to some profit margin above their full cost, how high prices can be and still be "fair" has been debated since medieval times. According to theologians such as Thomas Aquinas, the "just price" was often conceived of as the (debatable) amount above cost that the merchant needed to charge in order to maintain his or her business and to provide for his or her family. Charging more than that was to commit the grievous sin of avarice.

There is presently considerable regulation that helps establish some minimum behaviors for "fair pricing" (e.g., *price-fixing* by sellers, sometimes called "collusion," is illegal; similarly, "price discrimination" to different distributors by sellers without economic justification is also contrary to commercial law). Nevertheless, the concept of ethical pricing seems destined for considerable future debate. One current practice in the news has to do with the pricing strategy engaged in by the so-called pay day loan stores (i.e., those lending businesses that provide instant cash advances in lieu of unpaid, but earned, wages). These operations charge extremely high interest rates mostly to the impoverished segment of the market. A second dubious pricing instance involves some forms of adjustable rate mortgages that can often trigger significantly higher repayment rates for a variety of dubious reasons. And, a third questionable pricing scheme centers on “rent-to-own” furniture/appliance stores whose cumulative rate schemes often translate to payment totals far in excess of the total cost of the items rented. In each of these instances, it is argued that the pricing is “exploitive” because the high rates take advantage of certain unwary or desperate consumers.

Distribution

The distribution element of marketing involves the entire supply chain from manufacturer through wholesalers and distributors (including retailers) on to the final consumer. At each point in the supply chain, because there are economic interactions between these various parties, the potential for ethical issues to occur is quite common. Perhaps the most overarching issue within the channel of distribution supply chain has to do with the question of *power and responsibility* within the channel itself. Often one organization within the channel has greater economic leverage than other channel members, and with that economic leadership comes a potential for ethical abuse. A current example of this situation might be the enormous economic power that Wal-Mart possesses over its suppliers. Due to their dependence on Wal-Mart’s access to the market, suppliers must conform to Wal-Mart’s various contract requests or face losing a distribution outlet that serves tens of millions of customers. One perhaps encouraging lesson of marketing history is that channel members who abuse their power eventually lose it, often through the enactment of new government regulations that restrict and constrain certain competitive practices.

Another common concern within channel relationships has to do with “gift giving” that sometimes mutates into bribery. A long-standing business custom is to entertain clients and to give modest gifts to business associates. Such practices can cement important economic relationships. The pervading ethical question, of course, is, “When does a gift become a bribe?” Historically, for example, pharmaceutical companies have offered medical doctors lavish entertainment and gifts. The drug companies have argued that these amenities are not being provided to influence physician prescription decisions, but rather simply to inform them of the availability of new branded drugs. Consumer advocates contend that such practices are forcing consumers away from less-expensive generic drug alternatives and contribute directly to escalating health care costs. Not surprisingly, one of the best ways for channel members to deal with such potential ethical questions is to develop clear guidelines that address some of the typically questioned practices that exist within their particular industry. For instance, some companies restrict their employees from giving or accepting anything worth more than $20 in a given year when dealing with a business partner. In this manner, managers are given at least minimal guidance as to what constitutes acceptable and nonacceptable gift-giving practices.

Personal Selling and Sales Management

Sales positions are among the most typical marketing jobs. Ethical conflicts and choices are inherent in the personal selling process because sales reps constantly try to balance the interests of the seller they represent with the buyers that they presumptively serve. Moreover, sales reps seldom have the luxury of thoughtfully contemplating the ethical propriety of their actions. This is because sales reps operate in relative isolation and in circumstances that are dynamic with their business transactions frequently conducted under great time pressures. Even when sales reps electronically submit real-time sales reports of their client calls, such “outcome-oriented” paper evaluations contribute to a perceived clinical distance between sales managers and their representatives. Business case history tells us that sales people seem to be most prone to acting unethically if one (or more) of the following circumstances exist: when competition is particularly intense; when economic times are difficult placing their vendor organization under revenue pressure; when sales representative compensation is based mostly on commission; when questionable dealings such as gifting or quasi-bribes are a common part of industry practice; when sales training is nonexistent or abbreviated; or when the sales rep has limited selling experience.

Sales managers in particular bear a special responsibility for questionable selling practices because they are in a position both to oversee their sales staff and to influence content and implementation of sales policies. Ethically enlightened sales managers should regularly review their sales literature before distribution to minimize the possibility that inflammatory (to competitors) material is inadvertently circulated. They should counsel their sales people not to repeat unconfirmed trade gossip. They should strive to maintain a sales environment free of sexual harassment. They ought to encourage their sales people never to make unfair or inaccurate comparisons about competitive products and avoid claiming the superiority of their own product/service offerings unless it is supported by scientific facts or statistical evidence documented or prepared by an independent research firm. Despite best efforts of marketers, the area of sales will continue to have its share of ethical controversies. Sales are the most common entry-level position into the field of marketing and also the job position in marketing about which the general public feels most suspicious.

Advertising

Advertising is a significant economic force in the world economy, with global ad spending projected to be well over $300 billion in calendar year 2005. The visibility and marketplace influence of advertising is so great that many consumers think of advertising as synonymous with marketing. Various critics charge that advertising is biased, needlessly provocative, intrusive, and often offensive. Yet most surveys suggest that the majority of consumers, on the balance, find advertising both entertaining and informative. While some types of advertising involve outright transgressions of the law (e.g., deceptive advertising containing intentional errors of fact), a great deal of advertising controversy involves practices that are perfectly legal but still raise moral questions. For example, promoting handguns in magazines with a substantial teenage readership, the featuring of bikini-clad Paris Hilton suggestively soaping down a car in an ad campaign for hamburgers, and implied health claims for products that may not be especially healthy (e.g., low-carb beer) are instances of controversial (but legal) advertising approaches. Over the years, many lists of citizen concerns about the ethics of advertising have been put together. Often included on those lists are questions about the appropriateness of tobacco and alcohol advertising, the use of stereotypical images in advertising (e.g., Hispanic gardeners, hysterical housewives), the increased amount of negative (i.e., attack) political advertising, and various attempts to exploit children as buyers. The last issue is particularly sensitive to the public and, since the early 1970s, the Children's Advertising Review Unit, established by the Better Business Bureau, has monitored advertising directed to children less than 12 years and has sought the modification or discontinuance of ads that were found to be inaccurate or unfair in some fashion.

One of the more curious features of ethics in advertising is that the involvement of several parties (i.e., ad sponsor, ad agency, and the media) in the creation of advertising has probably led to a *lower* ethical standard in the practice of advertising than one might expect. The presence of multiple parties, none of whom has full responsibility, has created the default position of "leaving it to the others" to articulate and enforce an appropriate ethical standard.

Implementing Marketing Ethics

Of course, at the heart of marketing ethics is the issue of how to improve the ethical behaviors of organizations as they discharge their marketing tasks and responsibilities. There are several elements of successful implementation that have been regularly articulated in the business ethics literature and successfully applied to marketing. Good ethics begins with a chief marketing officer (CMO) who must not only publicly embrace core ethical values but also live them. It is often said that the organization is but a lengthened shadow of the person at the top; this is no less true of the marketing organization. Implied also, then, is that the CMO is supported in the endeavor to maintain strong ethical values in marketing operations by the chief executive officer (CEO) of the corporation. Put another way, a key role of the leadership of any company wanting to travel the high ethical road is to keep publicly voicing the importance of ethical conduct in the discharge of their business affairs. Such ethical exhortations involve espousing the core ethical values identified in the corporate mission statement. These values should be made operational in a code of conduct that addresses the specific ethical issues that are most common to a particular company or industry sector. For instance, the Internet sellers must explicitly address privacy policies for their shoppers, vintners should comment on the question of responsible drinking, and so forth. Furthermore, it is important that any such marketing code be dynamic and periodically revised. Caterpillar Corporation, a manufacturer of heavy construction equipment, has revised its code of conduct five times since the mid-1970s. Moreover, any organizational code or statement of norms must also be communicated well enough that all employees can verbalize its essential values. It is equally important that managerial and employee behavior in the organization be monitored, including that of the CMO, so that conformance to company values is checked on in a pragmatic way. One tool for doing this is the usage of a periodic *marketing ethics audit* to systematically check company compliance with ethics policies and procedures. When ethical violations occur, proportionate punishment must be meted out. Similarly, when organizational managers perform in an ethically exemplary fashion, appropriate rewards also should be provided. This last step testifies to something beyond financial results leading to recognition in the organization. Details of executing all these steps have been exhaustively treated in the business ethics literature and modified for a marketing context. Johnson & Johnson and Ford are examples of organizations that conduct audits of their social performance that includes the evaluation of multiple marketing dimensions.

Conclusion

At the end of the day, the most vexing ingredient in the recipe for better ethical behavior by marketers remains the force of will to always keep ethics at the heart of a company's purpose. The pressure on individual organizations to maintain and improve their profitability and to grow revenues is incessant. The nature of marketing management is to provide needed consumer goods and services by undertaking risk that, if calculated properly, is rewarded with financial profit. Ethical operations, at least in the short run, can be detrimental to that profitability because they often include some economic cost. Keeping ethical marketing at the forefront of operations is an exceedingly difficult challenge given the constant pressures on marketing managers to remain financially successful and growing.

—Gene Laczniak

See also Advertising Ethics; Brands; Children, Marketing to; Consumer Fraud; Consumerism; Consumer Rights; Deceptive Advertising; Green Marketing; Just Price; Pricing, Ethical Issues in; Trademarks

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Market Power

Market power describes the capability of either a buyer or a seller to negotiate, bargain, and make exchanges that are more aligned to their own preferences than to the preferences of the other. A market, where goods and services are bought and sold, is a social institution where benefits and costs are distributed. Market power is the means for market participants to appropriate more benefits for themselves while providing less benefit and transferring more cost to others.

Buyers and sellers negotiate, bargain, and make their exchanges in the market. In a free market, where each exchange is a voluntary transaction between a self-interested buyer and a self-interested seller, buyers or sellers can demonstrate their market power by making credible threats to abandon, or "walk away from," a bargaining or negotiating interaction. When buyers and sellers can choose whether to enter into agreements, successful exchanges depend on their ability to negotiate terms that satisfy their individual needs.

Explicit communication of a threat to walk away from the exchange is not necessary if one party to the negotiation can recognize the presence of market power without being told. Such recognition, or tacit communication, can arise from patterns in the economic relationships among sellers and buyers. A market relationship in which the seller is dominant may arise from a single, large organization that has a monopoly over supply, or from interorganizational cartel relationships in which several suppliers coordinate their activities to exercise power over smaller and more fragmented buyers. Conversely, a single buyer may be a monopsony or a large organization that accounts for almost all demand. In the absence of monopsony, many smaller buyers may form cooperative relationships to pool their demand and achieve market power over sellers.

Sometimes, market power may be explicitly exercised outside of the direct exchange process. For example, buyers may apply activist techniques that mobilize media, popular opinion, public policy, and other stakeholders to influence the market behavior of suppliers.

For sellers with a surplus of goods and services, unsold products are a cost burden—costs to store the inventory, costs of production equipment not generating revenue, and costs of aging products that may spoil or become obsolete. In this situation, buyers may not need to explicitly threaten sellers in order to exercise market power in negotiations. The relationship of supply and demand motivates sellers to give up their bargaining power so that they can attract relatively scarce buyers for their relatively abundant supply.

Reaching an agreement on a fair price when supply exceeds demand may be an interesting ethical dilemma. If the supplier knows that supply exceeds demand, does honesty require that they inform the potential buyer? If buyers know, is it fair for them to use their market power to demand a price so low that the seller risks going bankrupt? Interestingly, the principle of economic efficiency is *yes* to both questions. The laws of supply and demand are fundamental engines of free markets, but the engine only works as intended when buyers and sellers have accurate and timely information. Furthermore, society is most productive over the long term when inefficient businesses stop operating and their resources are redeployed to other productive activities. The exercise of market power to serve long-term social progress, however, imposes responsibilities to care for the welfare of those sellers without market power in the short term. Typical examples of such short-term care include public unemployment and retraining insurance.

When demand exceeds supply, there is a shortage of goods and services. In this situation, sellers do not have the capacity to satisfy all potential customers, and they can trade with customers willing to pay a high price, while refusing to sell to buyers not willing to pay the seller's preferred price. Some events such as natural disasters or terrorist attacks can cause demand in some local areas to far exceed available supply for short periods of time. Most societies think it highly unethical and unfair for sellers to use their market power to charge high prices in these emergency situations. Many governments have outlawed the use of such market power.

There are macroeconomic circumstances in which the use of bargaining power in free markets usually is considered fair. For example, if the macroeconomic business cycle is in a period of declining sales, then each customer is precious and sellers must give more and more net benefit to customers in order to capture a potential sale. Conversely, if the macroeconomic business cycle is in a period of increasing sales, then sellers are more likely to abandon negotiations with customers who are too demanding.

Free market advocates consider it fair for buyers and sellers to exercise their market power, as long as the power is exercised honestly and in accordance with law. Milton Friedman, an American economist and Nobel Prize winner, wrote in the tradition of Adam Smith (*Wealth of Nations*, 1776) that the exercise of honest and voluntary exercise of market power is the only socially responsible business behavior. Advocates of more planned economies, however, often consider the mismatched market power among buyers and sellers conducive to fraud, abuse, and chaotic distribution of goods and services throughout society. Also, advocates for poor people, such as Dr. Martin Luther King Jr. during the 1960s in the United States, are concerned that the lack of market power means an unfair distribution of goods and services that perpetuates conditions of poverty from generation to generation. Public policy may respond to such concerns with socialism, the ownership of industry by government to control market power for equitable distribution of goods and services throughout society.

In addition to micro- and macroeconomic conditions, there are unique characteristics of buyers and sellers that may give rise to market power in negotiations and bargaining. If a large portion of a seller's total wealth is the outcome of a potential agreement with just one buyer, then the seller must comply with the preferences of that one customer or risk the loss of significant wealth. If the buyer has a choice of many sellers from whom to purchase, then each seller must be very responsive to the buyer's preferences or risk losing the sale. Buyers also gain power if they can switch from one seller to another with little or no cost, such as a customer who can buy this year from a different clothing store than last year at the same shopping mall. In all these situations, the buyer has more market power in the relationship with the seller. Sellers, almost like a hostage, depend on the buyer's integrity for their welfare.

Conversely, a seller has market power in a relationship with a buyer if the goods and services provided by that seller are not available from alternative sources. In this situation, the buyer must acquiesce to the seller's preferences or risk having no supply. Buyers must depend on a virtuous seller who will not abandon them for a better deal elsewhere.

—Greg Young

See also Cartels; Consumer Activism; Contracts; Cost-Benefit Analysis; Laissez-Faire; Monopolies, Duopolies, and Oligopolies; Negotiation and Bargaining; Regulation and Regulatory Agencies; Self-Interest; Socialism; Stakeholder Economy; Utility

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Market Socialism

Socialism is an economic philosophy developed in 19th-century Europe that diagnosed many social ills—poverty, inequality, injustice, and unemployment—as consequences of the capitalist system's private ownership of the means of production. There are many forms of socialism, all of which eliminate private ownership of capital and replace it with collective ownership. These many forms, all focused on advancing distributive justice for long-term social welfare, can be divided into two broad types of socialism: nonmarket and market.

The historical collapse of nonmarket socialism in the 20th-century history of the Soviet Union, Eastern Europe, and China was due, in part, to their inefficiencies caused by information problems of centrally planned complex economies, motivational problems of self-interested people in societies purporting to transcend individualism, innovation problems of change-resistant bureaucracies, and social problems of individual liberty subordinated to coercive, repressive, and corrupt central planning. After the rise and fall of these nonmarket socialist systems, some who remain committed to the ideals of socialism believe that it may be revitalized as a feasible alternative to capitalism if they are perceived to be more accepting of democratic institutions and successful market economies. The proponents of market socialism claim that it is such a viable alternative.

Market socialism has its emphasis on workers' rights and distributive justice for long-term social welfare that is true to socialism's ideals. Rather than central planning, however, production and exchange decision making is located in worker-owned enterprises that transact with local buyers and profit-seeking sellers whose negotiations are informed by the market's prices for goods and services.

In practice, the implementation of market socialism replaces private ownership with worker collectives and profit sharing. Collectives are vested with business decision-making authority that workers exercise in a democratic process. In small firms, decision making might be "one worker-one vote." In large complex businesses, there may be a general manager appointed by elected representatives of the workers. Market socialism is sometimes called economic democracy because of this style of decision making.

Market socialism claims to resolve the flaws of capitalism that motivated original socialist philosophers to seek a better alternative. These flaws include alienation of the worker class, wealth disparities, and unequal distribution of critical goods to the poor who cannot afford market prices. It is not clear, however, what enterprise-level mechanisms will resolve these issues and introduce a compassion for community without the need for some social intervention. Workers must still satisfy their tasked performance objectives whether the business is owned by a workers' collective seeking profit from its investment in labor or owned by private shareholders seeking profit from their investment in labor. Similarly, profit under market socialism remains vulnerable to the forces of market competition, and businesses need to adjust their costs and capacity to fit with these forces. Employees may lose their jobs in times of adjustment and need to apply for new employment with other profit-seeking businesses. In these circumstances, market socialism applies democratic social institutions to guide industrial policy when social needs are not satisfied by enterprise-level decision making. For example, socially owned banking institutions allocate capital funds to worker collectives in areas needing stimulus and growth, even while worker collectives plan and operate production according to the incentives of market-based prices.

Socialist philosophy argues that the goal of production is to serve the community and not to create profit for private interests. Market socialism calls for government at all levels to play a major role in resolving these issues. For example, the national government creates and controls a social investment fund that distributes funds to regional government entities. Each region makes decisions concerning the appropriate level of funding for its constituent community governments; each local community government transfers these funds to public banks; and each public bank makes commercial investments to worker-owned businesses in the local community to increase employment and entrepreneurship. These businesses remain free to use their market power to maximize their profits legally.

Market socialism is premised on a moral philosophy grounded in positive utilitarianism. It assumes that the greater good for a society is knowable, and an economic structure can be designed to create greater good than social harm. This is opposed to institutional social philosophies that argue that institutions (such as capitalism) are embedded in the richness of a society's culture as it unfolds over time. Hayek argued that not all the antecedents and consequences of such embedded systems can be known, and there are unintended consequences when social engineers change institutions. A principle of caution suggests that societywide economic change should not be undertaken when the consequences are largely uncertain. The comparative historical experiences of economic transformation in the former Soviet Union and China provide evidence both for the likelihood of serious unintended consequences and for the advantages of caution.

Israeli kibbutzim are examples of market socialism in modern Western society. Kibbutzim are collectively owned communities that operate modern enterprises and sell their products in both domestic and export markets. Another successful experience with market socialism is found in the system of land-grant universities of the United States. State governments provide these institutions of higher learning with financial and land capital in order for them to educate citizens for productive participation in the community. At the same time, as they are capitalized by government, land-grant universities still must respond to market forces of supply and demand for professors, students, and economically valuable skills and knowledge. These institutions are important public mechanisms that, nevertheless, must work closely with the free market to create and distribute social welfare throughout segments of society that purely private universities cannot serve.

Market socialism blends ethical principles just as it combines different economic philosophies. It starts with a compassion for building just communities and then, because of the need for operational viability, allows for business to be governed by self-interested economic efficiency. Its roots remain in a socialism that has historically been antagonistic to the market system. The moral travel of market socialism to embrace the economic behavior of markets is a reaction to the historical failure of the central planning forms of socialism. Still, market socialism seeks to remedy the deficiencies that many see arise in capitalist systems—disparate wealth, unjust distribution, unemployment, shortages of social services, and alienation.

—Greg Young

See also Capitalism; Communism; Economics, Behavioral; Hayek, Friedrich A.; Human Rights; Industrial Policy; Justice, Distributive; Marxism; Socialism; Unintended Consequences, Law of; Utilitarianism

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Marx, Karl (1818–1883)

Karl Marx applied historical and scientific analysis to economic history and concluded that class struggle would lead to a dictatorship of the proletariat as a transition to the development of a classless society governed by the principles of communism. Marx responded to the suffering and injustices he observed and experienced during adulthood by participating in subversive political activities aimed at overthrowing existing political and economic power structures.

The Formation of a Radical

Karl Marx grew up as the second son of nine children in Trier, Prussia, a city now in the western part of Germany. His paternal and maternal grandfathers were both Jewish rabbis. His father converted the entire family to Lutheranism, the state's dominant religion, when Marx was 6 years old, to continue practicing law in the civil service. Marx studied law at the University of Bonn and philosophy at the University of Berlin, where he became attracted to the writings of Kant and Hegel. He obtained his doctorate from the University of Jena in 1841.

Although a brilliant philosophy student, Marx was denied a teaching position because of his Jewish heritage and atheistic religious beliefs. He became a journalist for a liberal newspaper in Cologne and attended socialist meetings. His articles criticized the Prussian monarchy, proposed the abolishment of private property, and encouraged a working class revolution. Marx and his wife, the daughter of Prussian nobility, moved to Paris after the Prussian government threatened to arrest him for treason. There Marx helped create a political journal in exile.

Marx and Engels

In 1844, Marx declared himself a communist and formed a lifetime friendship with Friedrich Engels, another Prussian writer living in Paris. Engels, an heir to a business fortune, published *The Condition of the Working Class in England* in 1845, a seething critique of the negative impacts of the Industrial Revolution on individuals and society. That same year, Marx and Engels published *The Holy Family*, a critique of the Young Hegelians. Marx began writing *Economic and Philosophic Manuscripts*, about the communist solution to capitalist alienation, and *The German Ideology*, about his materialist conception of history, although neither would be published until after his death.

Marx was expelled from France in 1845 for his revolutionary writings. Jobless, he relocated his family to Belgium, where they lived in poverty. Marx joined the revolutionary Communist League whose goals included violently overthrowing capitalism. In February 1848, he and Engels published *The Communist Manifesto* as the political organization's statement of faith. In their call to arms, Marx and Engels argued that capitalism inevitably would be replaced by socialism and then communism.

Marx was arrested and expelled from Belgium in 1848 for supplying revolutionaries with money to purchase weapons. He and Engels reentered Germany as it experimented with democratic reform. They were arrested for inciting a revolt, acquitted, but then deported. Marx went back to Paris to participate in revolutionary activities but was expelled from France again. In 1849, Marx settled in London, England. He lived in slum conditions with his wife and children. Only three of his seven children survived to adulthood.

Engels accepted a job with his father's Manchester, England, textile firm and subsidized Marx's living expenses and revolutionary writings. Marx earned minimal income as the international reporter for an American newspaper and spent most of his days reading and writing in the British Museum's Reading Room. With Marx and his wife in continual ill health, his mother-in-law sent a servant to assist them. The maid gave birth to his illegitimate son, whom he abandoned. In 1859, Marx published *A Contribution to the Critique of Political Economy*, which outlined how economic forces influenced the law, politics, religion, art, and philosophy. After nearly two decades of living in poverty, Marx inherited money and moved his family into a mansion.

In 1867, Marx published the first volume of *Das Kapital*, his economic magnum opus that integrated his economic, philosophic, historical, and scientific thoughts. Three years later Engels sold his portion of the family business and paid Marx a generous annual pension. Marx continued to study, argue with intellectuals, write, and struggle with his many illnesses until his death in 1883 at the age of 65. Engels published the long-awaited second volume of *Das Kapital* 2 years later and the third and final volume in 1894, a year before his own death. The three volumes served as the intellectual foundation for Marxist thought over the next century.

—*Denis Collins*

See also Communism; Industrial Revolution; Liberalism; Marxism; Socialism

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Marxism

Essentially, Marxism replaces the private pursuit of capital with the collective ownership of production and distribution of goods and services. German philosopher and political economist Karl Marx (1818–1883) developed this revolutionary theory of socioeconomic power relations based on his radical socialist critique of capitalism. Communism is considered inevitable as the only way for the majority to completely rid itself from what is regarded as the essentially exploitative nature of capitalism.

While he was deeply influenced by German idealist philosopher G. W. F. Hegel and Scottish political economist Adam Smith, Marx rejected as much of their thinking as he embraced. He replaced Hegel's theory of human history, as an evolving dialogue between opposing ideas (dialectical idealism), with his own "dialectical materialism," whereby ideas are shaped by material and social forces instead of the other way around. He thus followed Smith in analyzing the material implications of the free flow of capital, while rejecting Smith's view of human nature as essentially acquisitive. For Marx, human nature is much more malleable and dependent on prevailing socioeconomic frameworks. Accordingly, Marxists hold that capitalism encourages people to become individualistically competitive and profit seeking, while socialism encourages them to become more cooperative and less selfish. Marx held that capitalism was politically and economically unsustainable and would inevitably lead to a more equitable and beneficent socialism, in which the means of production are controlled by the democratic state. And ultimately, this socialism would lead to a worker-controlled communism in which all property is collectively owned.

Although capitalism is still growing on a global scale, it has been tempered in many ways that Marx predicted. Indeed, no successful economy today is anything close to pure laissez-faire capitalism, and several of the world's largest economies remain semisocialist, for example, France, Germany, Italy, and Canada. China is a notable exception since it is not democratic. History has shown that while every socialist economy has privatized its markets to a certain degree, every successful capitalist economy has regulated them to a certain degree. Thus, each of the world's top 10 economies has sought to find its own ideal mix of capitalist and socialist elements. For example, all the dominant capitalist nations have instituted a minimum wage, antitrust legislation, union rights, graduated income tax, social security, unemployment insurance, public education, and so on. These are initiatives that Marxism endorses and predicts.

Conspicuously absent in the United States is universal medical coverage—present in all the other nine largest economies, and Marxists would expect it to arise here as well. Interestingly, globalization has resulted in some U.S. companies losing competitive edge partly as a consequence of bearing most of the health care costs of their employees. And some foreign job importers such as Toyota have publicly stated that they chose Canada over the United States to save on health care costs even when most of their sales are in the U.S. market.

There are many other examples of Marxist principles that arguably benefit business, and we will consider a few examples of U.S. corporations successfully implementing them, often without relying on government. But first we must understand the essential elements of the Marxist critique of capitalism itself.

Marxist Critique of Capitalism

Although Marx was deeply influenced by Adam Smith's economic analysis of human behavior and society, he rejected three of his central claims:

1. Human acquisitiveness is the driving force of economic development.
2. When individuals are left to pursue their own economic interests, they unwittingly produce the greatest good for all.
3. Employer and employee benefit equally from the invisible hand of the free market.

Marx deconstructs the capitalist framework to expose what he sees as the fatal flaws of these guiding assumptions. Addressing the third, Marx attempts to show that the capitalist employer exploits and alienates the employee from the value of the work itself. Concerning the second, Marx holds that unbridled profit seeking leads to oppressive oligopolies, that is, corporate rule of the state. And it is these systems that, according to Marx, artificially promote and reinforce self-interested attitudes, especially in the ruling classes. Thus, Marxism in general sees capitalism as a self-propagating value system, paradoxically containing the seeds of its own destruction at the hands of the inevitable working-class revolt. Whereas capitalism sees capital as a means of liberation, Marxism sees it as a tool of oppression. Marxism thereby examines the function of capital from a dialectical materialist point of view, that is, as an evolving power struggle between the working and upper classes.

Exploitation and Alienation

According to Marx, employer and employee in a capitalist system never meet on equal terms. Employers always possess sufficient capital to dictate the terms of the contract to their advantage. Most often, the workers need jobs to merely survive, while the employer-capitalists are not in such desperate need, as they usually possesses enough capital to offer employment and can thus wait longer than the workers to shape the terms of the contract to their advantage. This creates a power struggle between the bourgeoisie (capitalist upper class) and the proletariat (workers). Essentially, the bourgeoisie owns capital, while the proletariat has little to sell but its own labor.

Although Smith similarly acknowledged that employer and employee do not meet on equal terms, he nevertheless held that a laissez-faire economy continually stimulates new and competitive demand for labor, thus supplying improved working conditions throughout society. In this way, only the fewest possible number of workers are ever forced to remain in exploitive positions, as the free market systematically provides myriad employment alternatives for the greatest number of workers. Smith also predicted that worker unions would form to help combat corporate trusts intended to lower pay and benefits to workers across industries.

But Marx held that a dynamic free market combined with unionization is insufficient to dispel widespread exploitation. For Marx, capitalism is itself essentially exploitive to the worker. According to his analysis, the employer-capitalists are always able to exploit workers by paying them less than the true value of their labor. In fact, it is only through such an arrangement, he argued, that profits may accrue. And as the capitalists increase their profits, the more they can exploit the workers. Thus, the goal for the capitalists is to cheapen labor, while the goal for the workers is to increase its value. This establishes a hostile and dysfunctional relationship in which each party works against the interests of the other.

The consequence of this paradigm for the worker is that the work itself becomes fundamentally dehumanizing or alienating—as Marx puts it. As workers become debased through an exploitive relationship, they begin to see the product of their labor as an external objective, standing over and above their own interests. Thus, the worker receives less and less intrinsic satisfaction through the work, seeing it only as a means to satisfying other needs. Work thereby becomes unrewarding. As Marx puts it in the *1844 Manuscripts*, "Its alien character is clearly shown by the fact that as soon as there is no physical or other compulsion it is avoided like the plague. External labor, labor in which man alienates himself, is a labor of self-sacrifice." Indeed, the "American dream" for many is to eventually obtain a life of leisure through the self-sacrifice of long hard years of work, be it fulfilling or not. The reality, of course, Marxists claim, is that few ever achieve this goal. As wealth becomes concentrated in the hands of the bourgeoisie, the median household income barely keeps up with inflation. Although American workers once enjoyed the world's highest median standard of living, they are now far behind most of the developed world with respect to wages, benefits, health insurance, pensions, paid vacation days, and educational opportunities.

For Marx, fulfilling work is a basic human right, which should be protected by all civilized societies. And so long as workers remain alienated, they cannot be truly free. Citizens may have the political and social freedoms of speech, religion, and governance, but remain economically exploited and alienated. A full and good life is one that includes a profession that one can thrive in by exerting a significant degree of control over both the product itself and the act of production. Essentially, it is control over the means and ends of production that makes work intrinsically fulfilling as an instrument of freedom and self-actualization. And without intrinsically fulfilling work, Marxists believe that life lacks real meaning, and true happiness is thus never achieved. Hence, Marxists hold that even very well-paid workers remain self-alienated in a capitalist context since they have little or no say in what gets produced or how it gets produced. Since production is entirely motivated extrinsically by competition for profit, intrinsic motivation is hence systematically undermined as workers become demoralized by a routinized alienation of what they may not even be fully aware. This is the paradigm of "false consciousness," in which workers are ignorant of their own exploitation or alienation as a result of living in a stultifying capitalist culture and ideology. Marxists often see religion as facilitating this false consciousness by lulling workers to accept their bleak fate as determined by God. For as Marx famously put it, "Religion is the sigh of the oppressed creature, the heart of a heartless world, just as it is the spirit of a spiritless situation. It is the opium of the people" (*Critique of Hegel's Philosophy of Right*). Incidentally, Marx would have found it telling that a large majority of today's U.S. citizens espouse some form of religion.

Criticisms of Marxist Political Economy

Although many of Marx's concepts retain contemporary relevance, much of his theory of political economy is thought to have become dated, even by mainstream contemporary Marxists. Perhaps the clearest example is his notion that labor is the only force that can create surplus value. This seems false as mechanization has created much more value by actually minimizing labor. Furthermore, Marxists tend to overlook the fact that capitalists take on substantial risk via investment, thereby also creating value. Thus, the capitalist would seem to have a natural right to the fruits of investment independent of the labor employed.

Another strong criticism is that of the inefficiency (or impossibility) of socialist price setting. There is now empirical evidence that as an economy grows and diversifies it becomes nearly impossible to determine appropriate prices. Indeed, doing so tends to stifle productivity by creating artificial barriers to competition. If, for example, all four-door sedans are set at a certain retail price, this stifles ingenuity by making it unnecessary for manufacturers to seek ways to lower production costs and increase efficiency. Furthermore, as the number of products increases, it becomes increasingly difficult and ultimately impossible for a government to both track and determine the prices of all goods and services. Setting certain prices too high or too low could have disastrous effects on supply and demand, ultimately causing major shortages of consumer goods.

Another criticism of Marxism is the prediction that capitalism would lead to social democracy, which would ultimately lead to communism. Although we have indeed seen evidence of the first trend, we have not seen any of the second. A crucial intermediate step for this to occur might be for unions themselves to purchase companies. Yet this has not occurred. This is a difficult phenomenon for the Marxist to explain beyond pointing out that unions do not usually own enough capital to purchase their own companies and that purchasing other smaller companies would go beyond their role as negotiators between workers and owners. Still, it would seem that if widespread communist revolt is inevitable, this would be an obvious way to achieve it. While there are only a small number of large American cooperatives such as Recreational Equipment Inc. (REI), they can indeed demonstrate superior productivity. For example, REI boasts extremely low employee theft rates even without using security cameras. This would seem to indicate increased worker loyalty at a time when employee theft has become a major burden in most American retail companies.

Recent Marxist Thought

Prominent contemporary Marxists such as Seymour Melman maintain that U.S. capitalism fosters two basic types of alienation:

1. Alienation by design
2. Unpremeditated alienation

Alienation by design describes practices intended to accumulate managerial profits and power at the expense of workers. For example, production is shut down as facilities are offshored to underdeveloped countries, where a more compliant nonunion labor force may be secured. This creates anxiety in the American labor force and makes workers less likely to seek increased compensation and control. Furthermore, there is a declining interest in capital goods production, often referred to as deindustrialization. As American managers increasingly seek profits either outside manufacturing or by offshoring, a paucity of capital goods is created. This produces unintended consequences that Marxists refer to as "unpremeditated alienation." For example, as the U.S. population increased over the latter half of the 20th century, the number of U.S. factories declined dramatically, while dependency on imports increased proportionally. Marxists contend that the result is large labor forces and communities increasingly dependant on narrowly focused government projects such as military-industrial facilities, which when closed leave their labor forces with useless skills and ruined communities. Furthermore, corporate welfare generally becomes rampant, thus helping shut out smaller competitors.

Still, many critics argue that Marxism has become irrelevant in the United States, pointing to a rise in "worker capitalism" now that close to half of households own stock or mutual funds. This increase is largely the effect of employee stock options and 401(k) retirement plans widely introduced at American corporations. Such critics claim the result is that today's American workers have a stake in a new "ownership society" via a greater orientation toward the future. According to this view, workers are now more likely to support lower taxes and cuts in capital gains taxes, while sharing a rising skepticism of unions and government entitlement programs. This ownership society, they argue, causes workers to get more involved in managing their own accounts and more educated about the global marketplace.

Marxists agree that stock options and 401(k) plans can benefit workers. However, they counter that these trends are not truly "disalienating," nor do they dispel the specter of exploitation. Since the great majority of stocks are tied up in retirement plans, workers generally cannot access them to become genuine capitalists—that is, deriving most of their income from invested capital. And employee stock options are rarely significant enough to turn workers into genuine capitalists, although a few exceptions have occurred, which have enabled some workers to retire at a young age. Marxists would hold that if a company gave workers majority control of its stock, it would make all the difference. But unless that occurs, workers do not have genuine control over the means and ends of production. Until then, they remain alienated and perhaps even exploited.

Marxists would reject the very notions of "worker capitalism" and "ownership society" for the reasons stated above. The only ownership society possible for Marxists is one in which the means and ends of production are held in common. So long as control of production is in the hands of the genuine capitalists, workers remain merely externally motivated and lacking freedom. They are primarily oriented toward a possible future of increased wealth, and thus not toward the present and more immediate and certain future. Of course, this increased focus on obtaining a wealthy future is seen as a virtue for free market advocates whose ideas tend to encourage acquisitiveness. But since Marxists view human nature as malleable, they maintain that stock option programs can actually exacerbate alienation by reinforcing acquisitiveness and selfishness while adding only the illusion of control over production via a modicum of stockholder participation.

Furthermore, Marxists argue that exploitation can also be exacerbated by stock options since low-paid workers, say, at retail giants, which already supply relatively low wages and benefits, are effectively providing workers with a stake in keeping costs down, thereby deepening their own exploitation. Hence, workers in a capitalist society may be duped into considering themselves liberated, when in fact they are reinforcing the nature of their own labor as an external and alien autonomous power.

Whether this paradigm will continue to stifle union membership or eventually stimulate revolt is an open question. Marx did not foresee the degree to which consumerism might be fueled by the mass media and a marketplace flooded by goods derived from cheap foreign labor and migrant workers. The result of these trends is that Americans are empowered much more as consumers than as workers. However, companies focused on the longer term may increasingly discover that, as Marxists have long held, disalienating employment practices can improve quality and increase profits in the long run. There are much data to support this, which will be discussed in the following section.

Contemporary Disalienating Business Practices

Certain companies have launched novel and creative two-tiered investment plans Marxists would praise. One example is Google giving greater voting rights to employee and managerial shareholders, say, 10 to 1. Hence, all external shareholders possess only one tenth of full voting rights per share enjoyed by the internal shareholders. A small yet growing number of U.S. corporations continue to implement similar disalienating policies that promote productivity and efficiency.

Some give employees a significant share of decision-making power. For example, at Saturn, a division of General Motors, productivity is measured as a group or "work unit" instead of individually. Workers are hence responsible for managing major functions, including designing, timing, and scheduling of tasks, record keeping, budget analysis, developing and delivering production, training, repairing, and cleaning. In most other corporations, employees can make recommendations but managers are exclusively responsible for decisions. However, when employees are given significant authority and responsibility, companies can often yield consistently high productivity.

Another common disalienating practice, instituted at Whole Foods Market, is giving each new worker in each division a trial period after which the other employees and supervisor collectively determine whether that worker should stay. Such examples have consistently shown that, when implemented effectively, disalienating practices can significantly and continually boost motivation, loyalty, efficiency, and productivity, while decreasing absenteeism and turnover. A pioneering federal government study at the Hawthorne Electric Company in the early 1920s initially demonstrated this phenomenon, which is now commonly referred to as the "Hawthorne effect." Subsequent studies corroborate and deepen the Hawthorne results.

Conclusion

Marx's central thesis that capitalism fosters worker exploitation and alienation via a fundamentally hostile relationship with owner-capitalists may not be inescapable. Indeed, contemporary examples abound in which workers in a capitalist system have become significantly disalienated, thereby helping to obtain increased competitiveness and sustained profitability for their companies. Although such examples are still very much in the minority, it is perhaps not inconceivable that they may become more common if the field of business ethics continues to grow. After all, Marx's theory of human history as an evolving dialogue between the bourgeoisie and proletariat views human nature as shaped by this dialogue. Thus, the peoples of capitalist nations such as the United States may gradually become somewhat less acquisitive and self-interested as the socioeconomic benefits of collaboration and disalienation become increasingly difficult to ignore. If this occurs, Marx will be at once vindicated and refuted.

—Julian Friedland

See also AFL-CIO; Antitrust Laws; Arendt, Hannah; Boycotts; Capitalism; Communism; Communitarianism; Consumerism; Downsizing; Economics and Ethics; Executive Compensation; Exploitation; Individualism; Informed Consent; International Labour Organization (ILO); Invisible Hand; Justice, Compensatory; Justice, Distributive; Labor Unions; Laissez-Faire; Marx, Karl; Meaningful Work; Outsourcing; Smith, Adam; Socialism; Stakeholder Theory; Sweatshops; Triple Bottom Line

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Maternal Ethics

Maternal ethics are an approach to formulating ethical theory by holding the mother-child relationship to be central. The paradigm for understanding ethical conduct is thus a relationship between unequals who are vested in each other's well-being rather than that of two autonomous self-interested males. Maternal ethics advocate replacing the economic man of rational choice theory with a mothering person. The mothering person may be either a man or a woman, the term being ostensibly as gender neutral as economic man.

Feminist philosopher Virginia Held acknowledges without apology that her development of maternal ethics relies on an idealized view of mothering, explaining its use as parallel to the practice of relying on an idealized view of rational contractors. The concept of rational contractors was in itself a major step forward from the patriarchal household, which was once seen as the model for society. Thus, to sufficiently understand and apply the concept of the mothering person, one must look to the postpatriarchal family as a model of the noncontractual society. Held explicitly contrasts her work with that of John Rawls and David Gauthier whose influential theories are premised on the assumption of mutual noninterest between contracting parties. In the postpatriarchal family, women and men both take an active role in mothering and are freed from the traditional stereotypes of gendered roles and expectations.

The unique relationships between mothers and children are characterized as natural, that is, occurring in nature, nonvoluntary, mutually interested, mutually supportive but not always equally so, expressing a willingness to care for each other in times of need and dependence, gradually facilitating independence, irreplaceable, and permanent. In this type of relationship, the parties are vulnerable to each other's demands just as mothering persons are vulnerable to the needs and demands of their children. By this vulnerability they become practitioners and teachers of a morality of caring that would serve well, Held argues, if we could broaden the lessons of home to the marketplace and society at large.

Of course, not all relationships are like mother-child relationships. Indeed, critics argue that the mother-child relationship is completely unique, and few mothers or children long for the same obligations to be replicated in public spheres. Other types of relationships with greater parity may offer more apt paradigmatic characteristics. Held anticipates this criticism, readily admitting that no one relationship is likely to fit all instances. Indeed, maternal ethics need not be seen merely as a substitute for other ethical conceptions, but can also be adopted as a supplement or corrective to other narrow views. Considering the mother-child relationship as paradigmatic is one approach to facilitate thinking about a different, more caring, more mutually invested way of building our society and creating the future. The contrast with current assumptions of how two people will interact, assumptions that underlie contemporary economic theories and policies, is dramatic. The exercise of this contrast is one of the goals of maternal ethics. It encourages people to ask the questions: How would I act differently if I cared about this other person as I care for my daughter? How would I act differently if I felt a need to provide for this person as I do for my mother? The answers to such questions could lead to radical reconsideration of behavioral, economic, and ethical theory.

The concepts underlying maternal ethics fit readily with the values of sustainability and are particularly relevant to business from this perspective. Holding mothering relationships as paradigmatic leads to an assumption of long-term responsibility, to decisions made with an awareness of their impact on multiple generations, and weighing the sustenance of the "other" as much if not more than the immediate benefits to oneself. While these precepts are not the ones routinely associated with profit-maximizing behavior, they lead to business conduct that has been recognized as supportive of consumers, employees, and communities, as well as laying the ground work for an ecofriendly business. A business basing its ethical norms on maternal ethics would rely less on the model of disinterested rational contractors than is currently popular in Western capitalism. Although a market mechanism could still be embraced, its form would likely be shaped by participating members' expectations of longer mutual commitments and the internalization of many of the externalities of business processes.

Another arena ripe for maternal practice is world politics. It is not a coincidence, points out Sara Ruddick, that women who have been so fully responsible for bearing and raising children are drawn to peace activism. Women's role in protecting life extends naturally to resisting the practice of war. Peaceful women are also a myth, paralleling the myth of violent men, containing both truth and misrepresentation. The claim that women are by nature peaceful is too facile a generalization, acknowledges Ruddick, given an abundance of historical examples of women supporting and contributing to the waging of war. But mothers, the custodians of the promise of birth, know a unique hope for the life they have created. The work of mothering, whether it is done by men or women, the caring, nursing, protecting, guiding into the world that is required to support human life, is work that is designed to sustain our race. It is inherently peace making. As such, it holds the potential for transforming global politics of war and peace. Women and men have been drawn into war, sometimes willingly, sometimes in the name of peace. Indeed mothering is often interwoven with the hatreds and loyalties fostering militarism, as Ruddick thoroughly presents. But a feminist maternal practice of peace could be an essentially moral voice in the ongoing struggle to end war.

Recognizing mothering work as essential in our society is a feminist effort, in that it valorizes the role of mothers. However, it is not an effort that all feminists support, in that it contributes to the image of women as quintessentially caring, nurturing, and devoting their lives to the raising of children.

Critics of maternal ethics theory argue that focusing on and idealizing women's role as mothers is subversive to the feminist goal of freeing women from gender stereotypes. Emphasizing maternity as caring practice is to put women back into an essentialist box of feminine abilities and will only result in further limiting a broad social acceptance of women as equal to men in leadership skills and intellectual capacity. Advocates of maternal ethics maintain that recognizing and valuing the mothering work that women have long been responsible for is a means of liberating both men and women to make independent choices about their contributions in the private and public arenas.

—Robbin Derry

See also Ethics of Care; Feminist Ethics; Feminist Theory; Gender Inequality and Discrimination; Patriarchy; Work and Family

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Maximum Sustainable Yield

In economics, agriculture, and the study of ecosystems, the maximum sustainable yield (MSY) typically denotes the maximum amount of a resource that can be used or removed from a system without affecting the system's ability to maintain itself and replenish or renew the resource at current levels in a sustainable manner. In economics, MSY refers to the theoretical equilibrium yield or the amount that may be harvested at a steady equilibrium state without significantly affecting the reproduction processes. It is calculated using the intrinsic growth rate of the resource stock and the environmental carrying capacity. MSY can be estimated from surplus production models such as the Gordon-Schaefer production function.

H. Scott Gordon argued in 1954 that economic rent from a common resource, such as open-access fishing waters, could not be captured by society. A common resource was prone to overharvesting because no one owner sets limits to maximize the long-term average yield. These concerns in the 1950s and 1960s led to changes in the international law of the sea and the development of exclusive economic zones.

Usually used in reference to fisheries or other aquaculture, MSY is the largest catch, long-term average yield, of fish or other resource that can be harvested under given ecological conditions without weakening the ecosystem's ability to maintain that level of species. For a situation where the population of the resource fluctuates over time, the amount of resource that can be harvested varies. MSY is also called maximum equilibrium catch, maximum sustained yield, sustainable catch, long-term potential catch, or potential yield.

The United Nations Convention on the Law of the Sea of 10 December 1982 referred to MSY in the conservation and management of stocks (Article 61 Conservation of the living resources, Section 3). The European Environment Agency recommends using MSY as a quality indicator for fisheries and aquaculture. MSY can also be used for evaluating strategies to rebuild a resource; for example, stocks can be rebuilt to a level that will produce at least MSY for prevailing environmental conditions. MSY can be confused with optimum sustainable yield (OSY), where OSY is the level of effort that maximizes the difference between total revenue and total cost. This level of effort maximizes the economic profit, or rent, of the resource being used. It usually corresponds to an effort level lower than that of MSY.

MSY as an indicator of the sustainable use of renewable resources has been important in the development of sustainable business practices, balancing economic and ecological factors. Beyond applications in fisheries and aquaculture, MSY is considered in sustainable business practices from the procurement of resources, to the production, use, and disposal of resources. Although MSY usually addresses one species within a system and a specific carrying capacity and does not incorporate economic or social values and balances, it is a useful concept to study common resources in terms of production costs and environmental carrying capacity.

Sustainable agriculture is the concept of plant and animal production practices considered in an integrated system according to the U.S. Food, Agriculture, Conservation, and Trade Act of 1990. Addressing the natural environment, economic health, and social equity, sustainable agriculture has a systems perspective, involves interdisciplinary research and education, and contends with stewardship of natural and human resources.

—Virginia W. Gerde

See also Agriculture, Ethics of; Carrying Capacity; Commons, The; Economic Efficiency; Environmentalism; Natural Resources; Rents, Economic; Supply-Side Economics; Sustainability

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Meaningful Work

It is commonly said that there are some people who work to live and others who live to work. The first category is purported to include those who work for material survival as well as those for whom work is a means to other meaningful ends. The second category is purported to include those for whom work itself is a meaningful end, although it might also include those who are seemingly compelled by forces beyond their control to be so-called "workaholics." In many periods of history, including in our contemporary industrialized societies, more of the average worker's waking hours have been spent at work than anywhere else. The topic of meaningful work explores the importance of spending that time well, including the aims of and influences on meaningful work, the forms of meaningful and meaningless work, and the value of meaningful work among other meaningful ends.

The Meaning of "Meaningful"

Meaningful work signifies something of value. We may have varying opinions of the value of meaningful work relative to other valuable things, but we can agree that something in the work itself is obviously valuable to one who desires it and that it is also valuable to one who claims to have it (if it were not, it would be meaningless to claim to have it). Alternatively, work can have meaning without signifying something of value. All work signifies something (or many things); for example, submitting a trade order signifies the intent to trade, drawing a blueprint signifies the plan of a building that may be built, hauling away waste in a dump truck signifies that that waste will rest someplace else, and so on. Work means something in the life of every worker (an unpleasant necessity, a pleasant distraction, a way to earn a living, a chance to be productive), but not every meaning signifies something meaningful. The trader may have a passion for playing the bond market game, derive satisfaction from forging relationships with customers, or regard work as instrumental to the intrinsically important role of financially supporting a family; the architect may appreciate design, construction, or the interplay of art and engineering; the truck driver may enjoy working with a team, accomplishing a complex and socially beneficial cleanup task, or operating heavy machinery. Which of these meanings is meaningful is at least partially a matter of an individual's will and ability to make work meaningful regarding that individual's self-interest and perception. Nozick associates meaningful work with individual self-esteem and says it includes the chance to apply our abilities to a project we consider to be valuable to an overall objective that we consider in carrying out our particular tasks. According to this subjective conception, the aim of meaningful work is individual fulfillment, or self-realization.

Of course, work that is subjectively meaningful is not often wholly within the control of the individual. The capability to engage in work that satisfies our individual objectives and talents, at least for any sustained period of time, depends in part on market conditions and associated demand for such work, as well as the organizational conditions under which we work. To the extent that our ability to pursue self-realization through work can be promoted or impaired by social institutions, whether of the public or private sector, we may ask whether there are practical, moral requirements on those institutions to provide conditions within which meaningful work can be meaningfully pursued and practiced—for example, free choice to enter, honest communication, fair and respectful treatment, intellectual challenge, considerable independence to determine work methods, democratic participation in decision making, moral development, due process and justice, nonpaternalism, and fair compensation. This conception of meaningful work thus concerns the alleged objective obligations of institutions to preserve conditions under which meaningful work is possible, that is, where individuals are reasonably capable of pursuing their meaningful work interests.

Although as individuals we may value having a choice about the kind of work we do, as members of society we have no choice but to work, or for at least some of us to work. The idea of a work ethic—that *any* commitment to hard work is morally good—is associated with the necessity of work to life. As Nozick's characterization and the examples above suggest, some workers may find seemingly ordinary tasks meaningful insofar as they contribute to a perceived greater or necessary good. On this view, whether or not social institutions have a moral obligation to support individuals' pursuit of meaningful work, individuals may perceive a moral duty to perform work that meaningfully promotes social well-being. According to this conception of meaningful work, the value of it may be instrumental, in terms of service to others. Some individuals who have the capability of performing meaningful work knowingly or unwittingly squander the opportunity in favor of something else—slothfulness, leisure, whiling away the time, or even doing work they perhaps perceive to be fun but ultimately meaningless, as if it were a cheap toy. Failure to seize the opportunity for meaningful work may be considered a moral failure to live up to one's own potential (self-realization) and to contribute according to one's ability (service to others).

Tying meaningfulness to service, of course, raises the further complication of measuring social benefit. One way in which to determine what work is most socially beneficial is to look to indicators of economic value in the free market. The perfect market would not only tell us via market demand what work was needed but would also reward workers in proportion to their market contribution. However, the economic fact of market imperfection renders the market a subjectively arbitrary measure of social value, meaning that the most meaningful work, by other, nonmarket measures, is not always rewarded as such. Part of the challenge of reconciling the value of meaningful work with other forms of value lies in the various uses of "meaningful" to characterize meaningful work. What is meaningful may aim at individual self-realization or at service to others, while the achievement of either aim through work is affected by institutional conditions and potentially distorted by market measures. Moreover, these aims are intertwined, sometimes in harmony and sometimes in cacophony. For example, if we neglected social needs to pursue our subjective interests, we might either starve ourselves or enslave others to do the "dirty work" for us—outcomes that are not unfamiliar in human history. Performing work that meaningfully responds to society's needs may support our objective conception of meaningful work while distracting us from pursuing our own interests. Much work that is seemingly necessary is potentially dull and dangerous, rendering it potentially impossible to provide basic institutional conditions for meaningful work. Leaving such work to others may seem to advance our own chances for meaningful work while negatively affecting the opportunities of others. Although it is clear that meaningful work is something of value, it is also clear that there is no uniform conception of precisely what that value is.

The Meaning of "Work"

Self-realization and service to others are not always competing objectives. Adam Smith's familiar ideal would be for the individual pursuit of self-interest to result in what is good for the society. Karl Marx' associated concern about division of labor suggests that more efficient forms of institutional production can detract from individual fulfillment when workers are alienated from the products of their labor. Achieving some degree of coincidence between what an individual perceives to be meaningful and what society demands generally requires some compromise, and thus work that optimizes this coincidence is often referred to with the religiously mystical terms "calling" and "vocation." With a calling (or vocation), an individual seems to be made for precisely the work that society needs to have done. A calling is intrinsically meaningful to the worker while being also instrumentally meaningful to others, so much so that individuals have found callings in the direst of working conditions, amid war, disease, and injustice (examples might include Anne Frank, Mother Teresa, and Martin Luther King Jr.).

Whereas a calling may be considered the highest form of work, "labor" is the term used by Hannah Arendt and others to characterize the lowest form of work, in which the institution fails to satisfy the objective conditions that make possible the pursuit of meaningful work. When work is done for someone else, particularly someone else who is higher on the institutional pyramid, and according to prescribed methods that prioritize economic productivity over individual moral autonomy, it is actually, in Arendt's estimation, unproductive. By her claim that labor leaves nothing behind, she means that the product of unproductive labor is made to be consumed but not to sustain human flourishing of the individual worker or of society in general (e.g., beyond dire working conditions, another problem with sweatshops may be that the outcomes of labor may not allow for any sense of pride in the worker for nonperfunctory participation in the creation of a valuable, well-made product).

Much work seemingly falls between these two extremes and has been termed, by various theorists, "workmanship," "profession," or "career." Such work may as often as not be exciting and fulfilling or dull and unfulfilling, but it may nonetheless be done out of choice, for years on end, because it offers such instrumental benefits as reliable compensation as well as such other job satisfactions as career advancement, perfection of a skill that may further enable discretionary choice as to how work is done, and a sense of belonging to a work community. In fact, the labor-workmanship-calling distinctions are often blurry, but the hierarchy provides a useful way of thinking about the various ways in which workers relate to their work and to the social institutions within which and/or in the interest of which they work.

The Value of Meaningful Work

There is more to the importance of meaningful work than to say that we each ought to pursue our callings. If we all pursued what we perceived to be our callings, much necessary work might be left undone. (Would enough people claim waste collection as a calling to keep our streets and sidewalks clean? When the World Trade Center fell after the September 11 terrorist attacks, many contractors were well compensated for their waste collection efforts, but many others came from around the country to offer their services for free.) That is, we may be biased and/or mistaken about what is our calling, vulnerable to the belief that we may be more suited to work activities that we happen to enjoy when our services may in fact be better spent elsewhere. The fact that one person's labor can be another person's calling leads back to the common assumption that meaningful work is first and foremost about subjective preferences for work that seems intrinsically valuable and/or valuable in relation to an individual's other meaningful ends. However, it is important not to discount the importance of instrumental social benefits to a well-rounded definition of meaningful work.

Even in the absence of a standard definition of meaningful work, there are nevertheless practically important reasons to understand the general ways in which the aims of meaningful work are conceptualized, in terms of self-realization or of service to others, and how institutional and market factors influence these aims. One incentive for managers to gain an understanding of the idea of meaningful work is to permit them to improve employee motivation. Work motivation theory contributes to personnel strategies for attracting and retaining talented and productive workers who might otherwise leave their employers in pursuit of better work. By understanding workers' motivations—whether they focus principally on skills used, compensation, work-life flexibility, meaningfulness, or other features of a job—employers can influence employees' job satisfaction through job design, promotion and compensation structures, goal-setting, recognition, and other means. In other words, work motivation theory provides an instrumental incentive for institutions to care about what individuals perceive to be meaningful work. In parallel, workers who work for reasons other than the intrinsic meaningfulness of work often perceive work as an instrument to enable them to pursue other meaningful ends (e.g., paying for an education or taking family vacations).

Another reason to understand meaningful work is that policy makers can appreciate the relationship between the economic value of work and other forms of value. The familiar economic goal of job creation does not by itself fulfill the ethical goal of *meaningful* job creation. Moreover, laborers' opportunity for self-realization is not well served when meaningful work merely refers to minimum standards for working conditions. In comparison, subjectively meaningful work is a luxury item. The view that meaningful work promotes self-realization is often the privilege of only those in contemporary affluent economies who are comparatively materially well-off and have the opportunity to search for something more than material satisfaction from work.

Finally, understanding meaningful work can help individuals achieve balance in their lives and the lives of others. We define work in terms of its opposite, nonwork. Contemporary notions of work-life balance are predicated on the belief that there are other goods in life that cannot be pursued at work. Even in affluent societies, workers ironically work very hard to develop new technologies and initiatives in order to work less. The more we perceive the value of our own work to coincide with other meaningful ends, and the more we make that coincidence possible in the work of others who work for us, the less the "work to live, live to work" distinction seems out of balance.

—Christopher Michaelson

See also Arendt, Hannah; Instrumental Value; Intrinsic Value; Marx, Karl; Protestant Work Ethic; Self-Realization; Smith, Adam; Sweatshops; Work and Family; Work Ethic; Working Conditions; Work-Life Balance

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Media and Violence

"Violence" and "media" are familiar elements of modern life. Because the perception of violence is somewhat subjective and the universe of media is quite broad, definitions for each will establish parameters for the ensuing discussion. *Violence* is the use of illegal, unjustified, unnecessary, or extreme force to injure a person or damage something. *Media* are the various means of mass communication, including television, radio, print publications, video games, music videos, films, and the Internet together with the people involved in their production, distribution, and sales as a business sector and commercial market. While the specific genres of violence and media technology may have changed over time, public concerns about representational violence, particularly as a form of entertainment, are long standing. Ethical concerns focus on the possible link between media violence and aggressive behavior, its social impact, the impact of media regulation on free speech rights, and the locus of responsibility for moderating media violence in the interest of social order.

Violence in the media has been a subject of active public debate for generations. When novels were first introduced, concerned husbands and parents worried that young women would be corrupted by the dramatic portrayals of romance, adventure, and transgressive behavior. The introduction of each new media technology has been accompanied by publicly voiced fears about its effect on people who misuse it. These fears are met with equally insistent proponents of free speech contending that media violence is more a reflection of society's violence than a cause of it. The controversy over media and violence reveals a deep cultural ambivalence about violence and uncertainty about the ethics of freedom.

Critics of media portrayals of violence point to hundreds of research studies in claiming that exposure to television, video games, the Internet, and other media violence leads to aggressive behavior in children, both in the short term and throughout their lives. Others question the quality of the research findings, the conclusions, and the assertion that American society is dangerously violent. This ongoing debate over media violence has involved the U.S. Congress, the American Academy of Pediatrics, the Federal Trade Commission, and a host of other high-profile organizations in the United States and the world. Although the primary focus of this concern is on children, a general anxiety about violence and its impact on society is prevalent as a theme of public discourse.

Violence and Representation

Human beings are a violent species—perhaps no more so than other creatures, but humans are uniquely capable of thinking and reflecting about the violence in their lives. As far as we know, cockroaches, prairie dogs, and snakefish do not lose sleep over the suffering they cause by asserting their dominance in the food chain. Humans, on the other hand, are disturbed by violence and by the fact that they depend on violence for their survival. Part of the human reflection on violence is its representation in ritual and art. It could be argued that modern movies, video games, and television are to the 20th century what sacrificial rituals, gladiator games, and tragic drama were to ancient peoples. Aristotle examined the role of *catharsis* in ancient drama as a means of cleansing or purifying the soul through representation of conflict. Modern anthropologists have observed that humans seem inclined to ritualize the suffering they cause and endure through representation. Bettelheim has examined the role of fairy tale representational violence in the development of young children. In these respects, modern media violence may be functionally similar to other forms of representational and ritual violence. Perhaps modern media violence is more unsettling and provocative because it lacks the authoritative context of religion or tradition. It may also be disturbing that representational violence appears to be entertaining. However troubling, cultural representation of violence is more likely to be experienced by modern people, especially the young, through mass media than through traditional forms such as religion or classical art.

Consider an ordinary day in the life of an American child or teenager. It might, for example, begin with a media music wake-up call—rap, hip hop, or pop music with themes of sexualized violence against women, drug trafficking, and street violence. Breakfast is accompanied by seemingly innocuous cartoons—the Road Runner or Looney Tunes with repeated incidents of gratuitous violence complete with sound effects—or perhaps music videos depicting surreal images of sexual violence, gang warfare, or milder forms of degradation. The schoolbus or carpool ride may involve an iPod soundtrack of more pop, hip hop, and rap. Despite the best attempts of school officials to control Internet surfing, the school computer lab and library offer opportunities to explore Web sites featuring pornography, weapons, and Internet game sites simulating war, gang violence, sexual predators, and a host of violent themes. Media entertainment continues to fill the ride home, homework time, and hanging out in the family room. Researchers estimate that by the time the average American child graduates from high school, he or she has witnessed 18,000 homicides and thousands more assaults, rapes, bombings, explosions, car wrecks, and fights. Media entertainment saturates the lives of children with representational violence.

It may be useful to consider the unique qualities of representational violence and its impact on the human brain. Cognitive scientists have discovered that the human brain uses two information processing systems operating in tandem to manage the continuous stream of environmental data. One system is rational, analytical, deliberative, and slow—best suited for nonthreatening situations in which there is plenty of time to develop accuracy and clarity. The other system works fast and reflexively using automatic emotionally driven response mechanisms triggered by unusual environmental cues (harsh noise, sudden movement, attractive or repugnant objects) to identify perceived threats and opportunities. Representational media focus on the emotionally stimulating triggers to attract and sustain attention. The speed, erratic pace, noise, and visual "pop" of violence (and sex and food) immediately engage the brain's emotional response. In traditional cultures, representational violence is staged through episodic drama and ritual events understood as marked off from everyday life by boundaries of time and space. The emotional responses triggered by religious rites, transitional rituals—and even bedtime stories or going to the movies—are contained within boundaries that the human brain quickly learns to distinguish from normal life. Psychologists and anthropologists argue the positive benefits of these activities that help people manage the cumulative weight of anxieties and fears that plague human consciousness.

In a media-saturated society, people become habituated to their brains functioning in crisis mode for several hours a day for years and years. Some researchers are understandably concerned about the impact of this phenomenon, particularly on young children. Much of the focus of the attention has been on the impact of sex and violence in the media. More recently, some attention has shifted to the relationship between media culture and obesity. Although some concern has been expressed about the "dumbing down" of media culture, little of this attention is actually focused on the problem of emotionally habituated brain function. Most of the public's concern about media violence is focused on its possible correlation with aggression, violence, and crime and on the need to control its presumed social impact.

The Social Impact of Media Violence

What is the relationship between media violence and everyday life? Does exposure to media violence make people more violent? Does media violence create a more violent society? Should media violence be a public safety concern? Some groups of parents, researchers, and child protection advocates, insisting that there must be some effect from the thousands of murders that American children see over a lifetime of daily television and media exposure, propose censorship strategies. Some researchers counter with arguments that modern society is comparatively less violent than previous historical periods. Public interest groups have raised first amendment concerns about initiatives to restrict free expression. Media and communications experts promote media literacy rather than censorship as the key to developing a healthy adaptation to a media culture. The media industry advocates self-regulation as the best means of achieving a balance between free speech rights and child protection. Given the speed with which media technologies have been developed, it will take time to develop public policy consensus among these groups of competing interests.

Thousands of studies have been conducted to determine the link between television violence and aggression, particularly among children. One of the first studies of children and media violence, initiated in the 1960s by Leonard Eron in Hudson, New York, concluded that children who watched violent television programs were more aggressive at school. Since that time, media technologies have expanded to music videos, video games, Internet browsing, and iPods that could consume almost every moment of waking time in a person's day with content frequently described as violent, immoral, and degrading. Critics of media violence cite the homicide and rising male teenage arrest rates in the United States—dramatically higher than most First World nations—as evidence that American children, who watch more television than any other children in the world, are being incited to violence by television.

Public concern about violence escalated during the 1990s after a number of high-profile mass murders in American schools. In each instance, the perpetrators were middle-class boys in middle-class schools, prompting investigators to search for causal factors for violence in an environment thought to be free of the poverty, crime, and drugs associated with urban ghetto violence. Alarmed parents, educators, health providers, and child welfare advocates were quick to explore alienation, isolation, personality disorders, and family dynamics as possible contributors to the sudden outburst of violence. Media violence was also an obvious environmental factor seized by some as a corrupting influence.

The American Academy of Pediatrics (AAP) has been active in publishing statistics and developing guidelines for physicians and parents in addressing the issue of media violence for children in their care. The AAP identified several negative consequences of media violence for children: increased aggressiveness and antisocial behavior, increased fear of becoming victimized by violence, desensitization to violence, and increased appetite for violence. Parents were urged to limit and monitor media violence exposure and help children develop media literacy skills by talking with them critically about what they were seeing and experiencing.

In response to concerns voiced by members of Congress and Clinton Administration officials, the Federal Trade Commission conducted a study of the media entertainment industry in the1990s and issued a report in 2000, concluding that there was little effort on the part of film, recording, and electronic game producers to restrict access to violent material. While the media and entertainment industry was able to identify content inappropriate for children, the rating systems and parental warnings failed to reflect the industry's own assessment of appropriateness, and in fact, the industry actively promoted and marketed inappropriate products to children. While the report recommended self-regulatory efforts by the entertainment industry, it did not include specific legislative or governmental action to address the problem. Since the 2000 report was issued, however, the FTC has continued to monitor the media and entertainment industry, reporting some progress toward improved self-regulation. Focus for action has since shifted to coalitions of national child welfare organizations aimed at developing local and state initiatives.

In 2001, Bushman and Anderson published their meta-analysis of media violence and its impact on society, finding that the results of over a thousand studies, including those of major professional societies such as the AAP and the American Psychiatric Association, pointed to a causal connection between media violence and aggressive behavior in some children. Acknowledging the importance of the qualifier "some children," they compared the effect of media violence with the link between smoking and lung cancer: Not everyone who smokes gets cancer and there are other factors that cause cancer; the short-term effects are relatively innocuous, but the cumulative effects can be extremely severe; the tobacco industry has historically denied scientific evidence supporting claims of tobacco's harmful effects; and new media have been influential in shaping public opinion on the dangers of smoking. Drawing on these parallels, Bushman and Anderson linked analysis of scientific findings about media violence to news reporting of it and found that as the scientific community began clarifying and documenting the significance of the association between media violence and aggressive behavior, media reports and public concern became measurably weaker on the issue. When public opinion is not galvanized around an issue it is difficult to organize public policy initiatives with enough traction to have an impact. In a more recent publication, Anderson and Bushman suggest that results of ongoing studies of human aggression would support two effective approaches to reducing media-related aggression: reducing exposure to media violence and changing attitudes toward media violence. The second approach aligns with a growing initiative to promote media literacy as a means of teaching children to understand and critically evaluate the role of media in their lives, its functional dynamics, and its influence on their choices and behavior.

First Amendment Considerations

Despite a general consensus that media violence is an issue of undeniable public concern, first amendment rights advocates in the United States have taken a dim view of censorship as a viable means of protecting the public from media violence. Commitment to first amendment rights of free press, artistic expression, and speech have spurred legal scholars' involvement in the media violence debate, although some members of the legal community can be found on both sides of the issue of censorship for the protection of youth. First amendment advocates have cited the opinions of Supreme Court justices and legal rulings that declare the primacy of first amendment rights as the foundation of democratic systems of government. Librarians, writers, and artists have joined lawyers and jurists in claiming that the roots of violence reached far beyond the media, exhorting Americans to find solutions to the problem of community violence that would not erode the constitutional rights of expression so cherished as fundamental values for a free, democratic society. First amendment protection is a guarantee that the broadest range of perspectives, positions, and experiences will be included in the deliberative process of building public opinion and political will.

First amendment principles applied to media violence echo similar constitutional struggles of the past. First amendment advocates point out that censorship may seem to be an easy answer to an immediate perceived problem of media violence, but it does not address its complex root causes. In fact, it may enhance the appeal of violence for people with a distorted attraction to the "forbidden." Furthermore, it is not the role of the government to evaluate the merits of free expression, that is, the right and duty of each citizen in a free society. This responsibility of citizenship is framed as a recognition that value judgments are inherently subjective; rather than define a standard of value for the society, individuals in a free society are capable of defining for themselves what constitutes good or bad portrayals of violence in the media and exercising their power of choice accordingly in purchasing or using media products. It is also a fact that violence is a troubling reality in the world of human experience; censoring its portrayal in the media to "sanitize" it does not make it go away or render it less real for those who cannot escape it. Part of citizenship in a free, democratic society is taking responsibility for knowledge about the world and the way it is constructed; if violence is a problem, then perhaps it is incumbent on citizens who understand it to find ways to ameliorate it. Finally, it is individuals, as adult consumers and parents of children, who have a responsibility for decisions about what media are appropriate for themselves and their children. It is especially not the role of government to reduce the normative standard of acceptable media violence to that appropriate for a child. From a first amendment perspective, all the preceding arguments militate against media censorship and for an alternative approach to addressing the problem of media violence.

Media Literacy

One approach to media violence is a movement advocating "media literacy." The concept of media literacy was introduced in school systems in the 1970s. Media literacy empowers people—especially children—to understand and evaluate the media messages that surround them. When children possess the critical thinking skills to question advertising images or news reports, they are able to free themselves from being passive consumers to become active participants in a media culture. Media literacy projects have demonstrated that when they understand that media representations are constructed to "hook" them with a quick rush so that someone can sell an idea, product, or image, even children are able to challenge the message and exercise the power of alternative choice.

Despite its vigorous support, media literacy proponents do not agree about its primary purpose. Some media literacy experts propose an "inoculationist" approach to media education as a means of protecting children from destructive messages. Critics of this approach charge that it creates a hierarchy of privilege among media representations and products with someone inevitably determining what is "safe" or "not safe." They suggest a more rigorously nuanced approach to media that equips young people with the skills for establishing their own value judgments based on critically applied standards drawn from the context of their own communities, life experience, and values. Several states, local governments, school systems, and community organizations have been involved in media literacy projects that have developed a common body of concepts.

The Association for Media Literacy, formed in the 1970s by Canadian and American media literacy educators, defines several basic concepts of media literacy. First, all *media are constructions* that do not present reality but simulate it. Related to this concept is the observation that *media construct reality*; the constructed images, plots, and characters of the media are elements used by media consumers in the construction of their own reality. Also, *audiences negotiate meaning in media*; media engagement involves subjective interpretation and negotiation of its elements.

Because media producers constitute a major industry with collateral markets, *media have commercial implications.* There are no ideologically neutral media representations; *media contain ideological and value messages* that are not always obvious. People bring their experience with media into real life; *media have social and political implications.* The technology and material conditions of each media determine what makes it a viable product as a coherent media experience; *media form and content are closely related.* The material and technological elements of form and content, in turn, converge interactively with producers and consumers so that *each medium has a unique aesthetic form.* Media literacy offers some hope for an effective alternative to censorship in addressing the cultural problem of media violence.

—*Lindsay J. Thompson*

See also Free Speech in the Workplace; Paternalism

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MEDICAID

Medicaid, which became law in 1965 as part of the Social Security Act, is a social insurance program that pays for basic medical services for the nation's individuals and families who have the least income and resources. It is the biggest health safety net program in the United States, with more than 50 million people enrolled. It accounts for 16% of our nation's spending on health care, at an annual cost of over $300 billion. Unlike Medicare, which was enacted into law at the same time but is federally funded and administered, Medicaid is jointly financed by the federal and state governments. It is the third largest nondefense program in the federal budget after Medicare and Social Security, with 8% of federal outlays in 2004. At the state level, Medicaid is the second largest expenditure, after K–12 education, and it accounts for 16% of state own-source spending.

Medicaid enrollees must meet various financial criteria and belong to one of the "mandatory" eligibility groups, including pregnant women, children and teenagers, parents of dependent children, seniors, and people with disabilities. Private insurance is usually unavailable to Medicaid enrollees. Low-income workers and retirees might not have access to or cannot afford insurance through their current or previous employers. Many private insurance programs also exclude people with disabilities and chronic illnesses.

However, not all uninsured individuals qualify for Medicaid coverage, even if they are poor. Having assets in excess of a few thousand dollars may be enough to disqualify someone. Incidentally, although many immigrants meet various financial/asset criteria and mandatory categories, the Personal Responsibility and Work Opportunity Reconciliation Act of 1996, popularly known as "welfare reform," prevents new immigrants from applying for Medicaid during their first 5 years in the United States.

More than 7 million Medicaid beneficiaries, or 14% of Medicaid enrollees, are low-income seniors and people with disabilities who are also enrolled in Medicare. These "dual eligibles" usually have substantial health needs, comprising 42% of total Medicaid spending. They rely on Medicare to cover basic health services such as physician and hospital care, but depend on Medicaid to pay Medicare Part B premiums for the aforementioned services and copayments to cover prescription drugs and long-term care, which are not covered by Medicare. Now prescription drug coverage for dual eligibles is covered under Medicare Part D.

Federal statutes, regulations, and policies establish broad national guidelines for Medicaid. For example, state Medicaid programs are required to cover the following basic services for the mandatory groups of beneficiaries: (1) in- and outpatient hospital services; (2) physician, midwife, and certified nurse practitioner services; (3) laboratory and X-ray services; (4) nursing home and home health care for adults; (5) early and periodic screening, diagnosis, and treatment for children; (6) family planning; and (7) rural health clinic services. However, the scope and composition of Medicaid programs varies across states. States have substantial flexibility in administering their own program and setting their own guidelines regarding eligibility standards as well as types, amount, duration, and scope of services covered. They can also offer additional services such as prescription drugs and dental care for the mandatory beneficiary groups and other populations with significant needs. The majority of "optional" spending (86%) pays for services to the elderly and people with disabilities. Medicaid is the largest payer of long-term care, public mental health services, and AIDS treatment.

Funding for Medicaid is based on state spending and the statutory formula called Federal Medical Assistance Percentage. The federal government currently pays between 50% and 77% of all the state Medicaid spending with no predetermined limits, with higher matching rates for states with lower per capita incomes. The matching funds provide assistance for coverage of mandatory populations and services, as well as a wide range of optional services and broader population coverage. They also give incentives for states to invest in health care, since Medicaid is the largest source (44%) of all federal revenue to states. Reduction in state Medicaid spending will result in a substantial decrease in federal revenue.

Like private health insurance, Medicaid purchases services from hospitals, physicians, health maintenance organizations (HMOs), and other providers in the private health care marketplace. Each state sets its own reimbursement rates, which have historically been lower than those paid by other insurers. Some physicians are thus unwilling to serve Medicaid beneficiaries, and some HMOs have ended their participation in Medicaid.

While each state has a Medicaid Fraud Control Unit that monitors the safety net program, some of the largest and most complex state Medicaid programs (e.g., New York) have reported cases of service providers exaggerating their billings, charging for services that never occurred, and prescribing unnecessary but expensive drugs to "patients" who sell them on the black market. Such abuse is costing the programs billions of dollars and taking away resources from patients who depend on the programs.

In recent years, in addition to restricting provider payments and intensifying fraud control, many states have reduced services in response to sharp declines in state revenues and large budget shortfalls. In early 2004, the federal government, which faces an annual federal deficit of more than $400 billion, proposed to cap federal Medicaid matching payments and to enforce a state maintenance of effort requirement. Health and Human Services has also approved comprehensive waivers in the past few years that allow states to impose enrollment caps, enrollment fees, or higher copayments. Given that Medicaid is the primary source of health and long-term assistance for individuals with the most complex health care needs and the least amount of resources, some worry that any cost-cutting measure would further disadvantage the nation's most vulnerable population.

—Anita Ho

See also Health Maintenance Organizations (HMOs); Medicare

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Medicare

Medicare is a federally legislated program that provides low-cost hospitalization and medical insurance primarily for American seniors over the age of 65, who currently account for about one third of all health care dollars spent in the United States—more than $300 billion annually. Although a presidential committee considered creating a health insurance program for the elderly as early as 1934, it was not until 1965 that President Lyndon Johnson signed Medicare into law as part of the Social Security Act. Medicaid, a health safety net program for low-income Americans, was enacted the same year. Initially, both programs were the responsibility of the Social Security Administration. As the programs expanded and became more complex, the Health Care Financing Administration (HCFA) was created in 1977 to effectively coordinate and manage them. Further growth of the programs prompted the restructuring of HCFA in 2001, which was renamed the Centers for Medicare and Medicaid Services. This organization has three general divisions. First, the Center for Medicare Management focuses on traditional Medicare programs and government contracts with health care organizations. It sets up Medicare policies, determines reimbursement rates for service providers, and manages Medicare paperwork. Second, the Center for Beneficiary Choices codifies and regulates supplemental programs that provide coverage for services that traditional Medicare plans do not cover. Third, the Center for Medicaid and State Operations coordinates the Medicaid program with state governments.

In 2004, Medicare served approximately 42 million Americans, of which 35.4 million beneficiaries were people over the age of 65 who either paid into Medicare throughout their working lives or enrolled by paying an extra premium. Another 6.3 million beneficiaries were individuals who required dialysis due to end-stage renal disease and low-income people with disabilities who had received Social Security disability benefits for 2 years. In the fiscal year 2004, Medicare benefit payments totaled $295 billion, accounting for 17% of the nation's total health spending, or 2.8% of the gross domestic product. It is the second largest nondefense program in the federal budget (12%), after Social Security.

Five trustees, which include the secretary of the Treasury, the secretary of Labor, the secretary of Health and Human Services, and two private citizens, monitor the finances and report periodically on the economic health and sustainability of the two main Medicare funds. First, the Hospital Insurance program ("Part A" of Medicare) primarily covers inpatient hospital care, hospice care, and care in skilled nursing facilities. This "Part A" program is funded mainly through a payroll tax contributed by employers and employees, each paying 1.45% of the employees' income. Payments into the Hospital Insurance Fund are based on the number of workers paying into the system and are not adjusted each year, so the fund can become insolvent, that is, unable to meet all incurred debts. According to the 2005 Medicare Board of Trustees' projection, spending of Hospital Insurance trust fund assets might exceed income starting in 2012, and the fund's reserves might be exhausted in 2020.

Second, the Supplementary Medical Insurance program ("Part B"), which covers physician services, outpatient hospital care, laboratory tests, physical and occupational therapy, and most home health care, is financed by beneficiary-paid premiums ($78.20 per month in 2005) and general federal tax revenues, the latter of which makes up approximately three quarters of revenues for Part B. This fund is adjusted annually to cover the cost of Part B services and therefore cannot be overdrawn. These two plans do not cover custodial long-term care services, but low-income beneficiaries may also enroll in and receive such coverage from Medicaid ("dual eligibles"), a program that offers health services to Americans of all ages who have limited income and resources.

The majority of Medicare beneficiaries (88%) receive care through doctors and hospitals participating in the Medicare system, but some beneficiaries (12%) enroll in Medicare Advantage ("Part C"), which consists of private Medicare plans such as those offered by health maintenance organizations (HMOs). They stay within a network of doctors and hospitals in return for additional benefits not covered by the traditional fee-for-service Medicare system. The federal government pays a fixed fee to the HMO for each

Medicare beneficiary enrolled in the program. However, in recent years some HMOs have withdrawn from the program, claiming that they do not receive enough reimbursement from the federal government to cover the costs of providing care to Medicare patients.

Medicare paid less than half of the total medical expenses per beneficiary in 2002. Almost 90% of Medicare beneficiaries have some form of supplemental health insurance to help pay for health care services not covered by the Medicare program (e.g., dental services, hearing aids, podiatry services) and to ease the burden of Medicare's relatively high cost-sharing requirements. In addition to Medicare HMOs, beneficiaries often have other private coverage through retiree coverage from their former employer, veterans health benefits, supplemental private coverage (so-called Medigap plans), and Medicaid.

In 2003, the Medicare Prescription Drug, Improvement, and Modernization Act added an outpatient prescription drug benefit to Medicare ("Part D"). This new plan, which came into effect in January 2006, charges beneficiaries a premium set at 25.5% of the cost of the standard drug benefit. General revenues and state payments for dual eligibles contribute the rest of the cost.

The new drug plan, which is estimated to cost the federal government anywhere from $395 billion to $534 billion over the next 10 years, fuels the ongoing concern of the sustainability of Medicare. The Congressional Budget Office projects that Medicare spending will grow by an average of 9% annually between 2004 and 2014, a rate significantly higher than that of the overall economy. It is the fastest growing of all federal benefits programs and will continue to grow rapidly, affected not only by rising health care costs and benefit improvements but also by the eligibility of baby boomers beginning in 2011, longer life expectancy, and a decreasing ratio of workers to beneficiaries.

To maintain the federal government's financial stability while meeting the health care needs of an aging population, some have proposed increasing the role of private plans in Medicare. However, since the overhead costs of the traditional Medicare program (<3%) is substantially lower than that of HMOs (15% of revenues), and that private plans are demanding higher payments, many consumer and senior groups worry that privatization will further increase costs and lower choices for seniors.

—Anita Ho

See also Health Maintenance Organizations (HMOs); Medicaid

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Mentoring

Mentoring refers to the process by which a senior person (mentor) takes an active interest in sponsoring the career of a more junior person (protégé). Named for a fabled character in Homer's *The Odyssey* who tutored and looked after the title character's son, mentoring is a process that has been used for centuries as a means of handing down tradition, supporting talent, and securing future leadership. It flourished in the feudal system of the Renaissance as young men served apprentices to gain membership in guilds. Throughout history it is rare to study the career of highly successful individuals and not find the presence of a mentor. Aristotle mentored Alexander the Great, civil rights attorney Charles Hamilton mentored Thurgood Marshall, Gertrude Stein mentored Nobel Prize winning novelist Ernest Hemingway, and master salesman John Patterson mentored IBM founder Thomas Watson.

The popularity of mentoring reflects a confluence of interests of three different parties. Jobholders view mentoring as a means of meeting their career goals. Organizational officials are attracted to mentoring as an effective mechanism for extending their legacy and developing employees. And finally, individuals who are concerned with correcting injustices in existing career systems see mentoring as one tool for doing so. Advocates of mentoring have made it a widespread phenomenon touching the work lives of roughly two in five contemporary employees.

The outcomes of mentoring have been found to be generally positive but by no means equivalent for both partners. Protégés enjoy enhanced career mobility, compensation, and job satisfaction. Mentors are thought to accrue comparatively fewer and "softer" benefits such as career visibility, information acquisition, self-enhancement, and a sense of generativity. Even so, the experience of mentoring apparently makes these benefits more salient, since it makes them more willing to mentor others than individuals who have no mentoring experience.

In spite of these benefits, a number of ethical questions have been raised about the mentoring process. Some have criticized it for being too time-consuming. Others have indicted mentoring for resulting in favoritism and empire building. Along those lines, some have pointed out that mentoring tends to exclude women and people of color and that it is a conservative process that reinforces the status quo. Specific abuses in the mentoring partnership have also been reported. Mistreatment reported by protégés includes tyrannical and manipulative behavior such as revenge, political sabotage, and harassment. Similarly, some mentors report instances of dirty tricks and backstabbing by opportunistic protégés. Research has shown that such events are by no means rare within the mentoring relationship.

Mentor Duties

Based on a conception of mentor as a quasi-professional, Moberg and Velasquez derived the ethical responsibilities of the parties directly involved in the mentoring process. As a quasi-professional, the mentor's superior power implies a greater responsibility to ensure that the relationship not become abusive or otherwise dysfunctional. Specifically, the stringency of the ethical obligations that mentors have to their protégés varies in direct proportion to the power distance between themselves and their protégés. Within this formulation, mentors have seven prima facie ethical obligations: beneficence, nonmaleficence, autonomy, confidentiality, fairness, loyalty, and concern.

A mentor's duties of beneficence and nonmaleficence are consistent with utilitarianism. Beneficence is the obligation to be diligent in providing the goods of the mentoring relationship: knowledge, wisdom, and developmental support. As such, beneficence implies several corollary obligations. First, it implies that the mentor will ensure that he or she has the skills and information needed to provide these goods. Second, it implies that the mentor is duty-bound to be careful about the quality of advice provided. Nonmaleficence binds mentors to avoid exercising their role in a manner that might harm the protégé. This implies a duty to avoid any deleterious effect mentoring can produce. Obviously, this includes disregarding any temptations to engage in petty tyranny, manipulation, or deceit. It also includes disdain for comparatively minor transgressions that might distract the protégé from mastering intended lessons. Nonmaleficence also implies certain obligations that ethicists classify as positive duties, that is, duties to act rather than duties to restrain. One of them is the obligation to intervene and help out in instances when the protégé has followed the mentor's advice but it has turned out poorly. Such an obligation would not cover any situation that goes bad for a protégé. It would be restricted to situations in which the mentor's advice was followed but the results did not work out.

The mentor's duties to autonomy and confidentiality derive from fundamental notions of employee rights. Autonomy entails behaving in a way that enables rather than hinders the protégé's ability to exercise his or her own judgment and reasoning. Autonomy refers not merely to freedom from external constraint but to the development and exercise of a cognitive/volitional ability: the ability to think and act on one's own. The emphasis is on the protégé's ability to determine rationally what is best for himself or herself in the context of a community of others who are similarly disposed. This is a long-standing idea in professional ethics traceable to the work of Immanuel Kant. Respecting the autonomy of protégés translates to several specific mentor obligations. First, mentors should avoid any action that makes the mentoring relationship necessarily compulsory. Second, mentors should openly disclose and explain to protégés any information that they take into account as part of the mentoring process that protégés need to know. Third, mentors should assure that their communication represents education rather than propaganda. And finally, mentors should avoid establishing paternalistic relations with their protégés. Confidentiality implies that the mentor must maintain not only any confidences explicitly requested by the protégé but also anything that the protégé reveals about himself or herself in the course of their working together. Protégé self-revelations should always be assumed to be given with the expectation of confidentiality on the part of the mentor. Just as professionals are required to keep client information confidential except in those cases where it is certain that very serious harm to others will result, so too should mentors in their quasi-professional role.

The mentor's obligations of loyalty and fairness are based on the key requirement of justice—that a person should be given what is due to him or her. In mentoring, loyalty means, first and foremost, the avoidance of any conflict of interest. While mentors need not deny themselves the intrinsic benefits of their partnership, they should assiduously avoid the appearance that their commitment to the relationship is contingent on extrinsic favors or gratuities. Second, a mentor's obligation to be faithful to his or her protégés means making decisions about the relationship that ordinarily place the interests of the protégé in a paramount position. This does not imply that other commitments the mentor might have made are given no weight relative to the protégé's; it only means that ordinarily the protégé's ends are to be given greater weight. The requirement that mentors are fair in the allocation of benefits and burdens extends not only to their protégés but also to others who might otherwise be excluded or affected by the mentoring process. This implies that the problem of fair access is one for which mentors themselves should once again assume responsibility. Mentors ought to be open to mentoring protégés who have characteristics (social class, race, gender, interpersonal attractiveness, etc.) that make them less desirable to other mentors as protégé prospects. It also means that mentors should look for reasons to accept rather than reasons to reject such disadvantaged prospects. It is obvious that no one mentor can neutralize all access injustices by virtue of his or her own fair selection criteria; however, mentors who participate in mentoring relationships tarnished by unjust access are implicitly endorsing an indefensible, some might even say immoral, arrangement.

Concern is a mentor duty that draws from the moral requirement of care implicit in human relationships. Concern is the mentor obligation to exercise a caring but fair partiality toward protégés and their interests. It implies advocating on behalf of their interests and, more generally, providing them the kind of support that will contribute to their development. In these respects, the mentor exhibits a form of partiality toward the protégé, providing benefits and advantages for the protégé that the mentor does not provide for others. This obligation does not relieve the mentor of obligations to third parties and to the organization. The challenge is to be partial toward the protégé without simultaneously being unfair toward others.

Protégé Duties

It would be immoral for protégés to reap the benefits of mentoring without some correspondent obligations. Unless mentors are specifically rewarded by the organization for their actions as mentors, they are due reciprocity from their protégés. Such reciprocity ought to take the form of the duties of veracity, efficiency, and gratitude. Veracity obligates protégés not only be honest with their mentors so the advice and support they receive from them is built on accurate premises. It also binds them to be truthful about any observation they report about what is going on elsewhere in the organization. Among the few benefits mentors receive from mentoring is information from their protégé's network. For protégés to distort or withhold such information from mentors seems to accentuate what is already an inequitable situation. Thus, protégés ought to be forthcoming in all legitimate areas queried by a mentor. This includes frank information about the protégé's perceptions of whether the mentoring relationship is meeting his or her needs. In addition, protégés are obligated to be efficient in all encounters with their mentors. The reason is twofold. Once again, being efficient attenuates the inequity implicit in the relationship. In addition, it should be recognized that a mentor's time is typically at a premium. To reflect this, protégés acquire the duty to make every encounter as efficient as possible. This includes being prepared for each mentoring encounter, keeping the encounter moving, and in general respecting the mentor's time. The third protégé duty is gratitude. To the extent that protégés receive value in excess of the investments they make in the mentoring relationship, they owe their mentor a debt of gratitude.

The most important implication of this analysis is the impossibility of being a direct supervisor and an ethical mentor of the same person. As we have seen, the mentor role carries with it a special loyalty, partiality, and concern for one's protégés. This is contradicted by the moral obligations of the supervisory role to be impartial and fair to all one's subordinates. Therefore, unless one has only one subordinate, it is highly problematic to supervise and ethically mentor the same person. If the term *mentor* is used imprecisely to denote roles that involve only training, performance coaching, or career counseling, then holding both roles relative to the same person is feasible. Otherwise, they are morally contradictory.

Another key implication of this analysis is that some mentoring arrangements are more morally burdensome for mentors than others. Specifically, mentor duties are greatest if the power difference between them and their protégés is large, and this is exacerbated if the organization provides them with no rewards for their mentoring investments. If an organization has a formal mentoring program, it might be prudent to restrict especially burdensome mentoring assignments to those who are committed to high ethical standards.

—Dennis J. Moberg

See also Equal Opportunity; Ethical Decision Making; Networking; Preferential Treatment; Professional Ethics; Role Model

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MERCK & CO., INC.

Merck & Co. Inc., a large U.S. public pharmaceutical company, has faced several important ethical and social responsibility tests over the years. Established in 1891, Merck discovers, develops, manufactures, and markets vaccines and medicines in more than 20 therapeutic categories. The company has approximately 60,000 employees and sells products in approximately 150 countries. Worldwide sales in 2005 were more than $22 billion. The firm has always had a "patient first" approach to doing business as indicated by George Merck, the son of the founder, who stated that Merck tries never to forget that medicine is for the people, not for the profits. This view is currently reflected in the company's values, which states that Merck's business is preserving and improving human life. Although the firm has faced many challenges, two of the more significant ethical and social responsibility issues confronted by Merck include whether to produce and distribute a drug to help cure river blindness and whether to recall its arthritis drug Vioxx.

In terms of the first major issue faced by Merck, river blindness is an eye and skin disease caused by a worm that is transmitted to humans through the bite of a fly. The baby or larval worms then move through the body migrating in the skin and the eye causing itching, severe skin disease, and after repeated years of exposure, blindness. Merck researchers discovered that it was highly likely that by spending tens of millions of dollars they could develop the cure for river blindness. The problem was that the millions of people afflicted by the disease lived in parts of the world (primarily Africa) where they could not afford to pay for the drug. Other pharmaceutical companies, foundations, governments, and health organizations were not interested in paying for the development of the drug. Other concerns related to the risk of side effects for humans that might then affect the sales of Merck's animal drug, or that the human drug might be diverted into the black market, undercutting sales of the animal drug. The company also risked creating a precedent both internally among its researchers and externally among the public that might be difficult to meet in the future in terms of developing other important drugs with little or no financial return expected.

Despite the costs and the risks, Merck, through the leadership of its CEO Roy Vagelos, decided to spend the money. The drug, known as Mectizan, was not only developed but also distributed by Merck for free for years beginning in 1987. The decision did end up having indirect financial benefits for the firm, which according to Dr. Vagelos related primarily to the recruitment of top researchers. In December 2002, the World Health Organization declared river blindness virtually eradicated as a world disease, with the program reaching 40 million people annually in more than 30 countries.

The second major ethical and social responsibility issue places Merck in a potentially more negative light. The issue involves what has been perceived as Merck's delayed decision to recall its arthritis drug Vioxx, despite apparent knowledge of numerous deaths caused by the drug. Merck pulled its $2.5 billion-a-year drug off the market on September 30, 2004, when a study indicated that it doubled the risk of heart attack and stroke in patients who took the drug for more than 18 months. The issue appears similar to that faced by A. H. Robins Company, which was eventually forced into bankruptcy in the mid-1980s after facing lawsuits due to its allegedly defective "Dalkon Shield" intrauterine birth control device.

Plaintiffs claim that Merck knew of the additional risk of heart attacks based on previous clinical studies, but failed to warn doctors and consumers of the risk. From 1999 to 2004, more than 20 million Americans took Vioxx. By the end of 2005, Merck faced close to 10,000 lawsuits in the United States. The firm is also being sued in Europe, Australia, Brazil, Canada, Israel, and Turkey. As of April 2006, Merck had already spent hundreds of millions of dollars to defend four cases, with two wins and two losses (with judgments against Merck for $253 million in Texas and $13.5 million in New Jersey). The company continues to refuse to pursue a global settlement and is appealing the cases it has lost. Some estimate that the company may have to defend more than 100,000 Vioxx lawsuits leading to possible liability of up to $50 billion (U.S.) for Merck, since epidemiologists estimate that 100,000 people might have suffered heart attacks because of the drug. It is still unclear how Vioxx will ultimately affect the future prospects of Merck, and whether Merck will be able to withstand the current legal assault.

—Mark S. Schwartz

See also Corporate Social Responsibility (CSR) and Corporate Social Performance (CSP); Dalkon Shield

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Mergers, Acquisitions, and Takeovers

On a general level, merger, acquisition, and takeover refer to a combination of two organizations into one larger entity. Virtually every major public corporation—as a merger partner, acquirer, or target—has been involved in an attempted or realized organizational combination as mergers, acquisitions, and takeovers (MA&Ts) have become a basic staple of corporate strategy. The overarching reason why firms enter into a merger or decide to acquire another company is the belief that the combination will allow the new entity to attain its strategic goals more quickly and less expensively than if the firm attempted to do it by internal growth alone. While proponents argue that well-planned MA&Ts enhance both the value of the firm and the value of the firm to the larger society, critics respond that far too many of these combinations are undesirable and ill-conceived. In these latter instances, MA&Ts are suggested to create far more harm than benefit for an array of internal (e.g., shareholders, managers, employees) and external (e.g., customers, suppliers, unions, local communities) stakeholders, many of which are not directly considered in the decision-making process.

While the terms are often used interchangeably, there are some subtle differences. *Acquisition* refers to any transfer of ownership in which one organization is absorbed by another, *merger* is a combination in which two or more previously autonomous companies form a wholly new firm, and *takeover* refers to those situations where a company or an investment group gains enough shares of stock in a publicly traded company that it can control its governance via a plurality of votes for the board of directors. Merger typically reflects a sense of equality between the two organizations, whereas acquisition and takeover reflect the dominance of the acquiring organization over the target firm.

There are two fundamental sets of concerns raised about corporate MA&Ts: The first focuses on whether the combination will create economic value for shareholders; the second emphasizes the effect the combination will have on the companies' implicit contracts with other stakeholders and the larger society. These issues reflect both process and outcome considerations. From a process perspective, questions are typically raised about the appropriateness and fairness of the actions by the parties involved during combination planning, transaction, and implementation. In terms of outcomes, emphasis is placed on the combination's relative benefit or harm (direct and indirect) for all relevant stakeholders (including shareholders) and about the fairness and social desirability of these outcomes. Debate about these issues often comes down to questions about transparency, distributive justice, and the social role of the corporation and its responsibilities to a broader range of constituencies that go beyond shareholders per se.

Process and Outcome Considerations in Hostile Takeovers

A basic tenet of the free market is that organizational combinations intended to maximize the value of the firms for shareholders have long-term benefits for the larger society. The underlying market for corporate control, that is, the tendency of outside parties (often referred to as "raiders") to try to buy publicly traded companies, exerts a necessary discipline on managers, whose self-interests often diverge from those of the owners. Thus, even hostile takeovers, which imply change and restructuring that can have significant repercussions for the existing management, workforce, local community, and a host of other external stakeholders, can have beneficial effects in terms of stimulating improved economic performance and generating greater returns to shareholders. Many takeovers, for example, reflect the acquisition of underperforming or undervalued businesses that are unrelated to the strategic core of the parent company. The underlying argument is that managers, as agents of the owners, have a fiduciary responsibility to shareholders to sell off such assets and refocus the company on those areas that promise higher efficiency and return.

Critics argue that many takeovers are initiated for the simple purpose of liquidating the target company, especially when there is a gap between the market value of the firm and the breakup value of its assets. A basic proposition of free market capitalism is that market value represents the best estimate of net present value (a way of calculating the value of a net cash flow adjusted for the time value of money) of future cash flows. However, critics contend that beyond a short-term financial return for select shareholders, a liquidating takeover does not have any long-term benefit to other stakeholders or the larger society. These objections are especially directed at buyouts of successful and profitable companies, where the takeover may lead to layoffs and changes in management and can have a variety of negative effects on the firm's local community. Another argument is that the threat of corporate takeover compels managers to show evidence of continuous profitability that can precipitate a neglect of longer-term investments (e.g., in research and development). Although the extant research indicates that such causal dynamics are unclear, this pressure is suggested to undermine long-term capital formation and the competitiveness of the economy.

Takeovers and Defense Tactics

While ethical and social concerns typically focus on the acquirer's motives and actions, target firm management has also come under criticism for a series of questionable tactics intended to discourage unwanted takeovers. Based on an analogy to takeover specialists as "sharks," "shark repellent" refers to an exotic array of tactics that includes golden parachutes, poison pills, greenmail, sandbagging, and "pac-man" and "scorched earth" defenses. "Golden parachutes" promise lucrative benefits and severance payments to current management if they lose their jobs due to a takeover by another company. A related tactic that focuses on employees is referred to as "tin parachutes," which are suggested to be a better takeover defense than golden parachutes due to the fact that the greater numbers of employees can create a larger total payout, even if individual payments are less. "Poison pill" tactics are attempts to dilute the value of the shares held by the bidder by giving existing shareholders (except the bidding company) rights to buy shares of either the target company (referred to as "flip-in provisions") or the acquiring company ("flip-over provisions") at a significant discount, which are triggered by an attempted takeover.

As a spin-off of the term "blackmail," "greenmail" is when a target company repurchases a large block of its stock that is held by an unfriendly company or raider at a substantial premium to stop the takeover attempt. "Sandbagging" is when a target firm attempts to stall the process, often with the hope that a more favorable acquirer (a "white knight") will emerge. A "pac-man" defense is when a takeover target launches a tender offer for the company that was trying to acquire it. If successful, the target company ends up taking over the company that tried to buy it out. Finally, the "scorched earth" defense, which is sometimes referred to as a "suicide pill," involves selling off desirable assets or depleting the cash reserves of the target company by making extensive (and not necessarily profitable) acquisitions, possibly incurring large debt in the process.

While these various tactics may protect the target against an unwanted takeover, they render the company vulnerable to the vagaries of the business cycle, and they can significantly contribute to company debt. They also raise significant concern about the fiduciary duties of the target firm's management to its shareholders. From an agency theory perspective, the underlying question concerns the extent to which these tactics are being used to protect shareholder interests or to preserve the entrenched position of the target firm's executives.

Process and Outcome Considerations in Mergers and Acquisitions

Although criticism is typically placed on hostile takeovers, even "friendly" mergers and acquisitions (M&As) can raise an array of ethical and social concerns. Although M&As are often portrayed as carefully calculated, strategic acts, in practice they can be very costly with disappointing results. M&As typically disrupt organizations, often for years, diverting the time and energy of senior management and making organizational members feel stressed, angry, frustrated, disoriented, and frightened. Workplace ethics are especially vulnerable during such strategic transitions. According to a study by the Ethics Resource Center, employees in organizations undergoing mergers or acquisitions observe misconduct and feel pressure to engage in questionable business practices at rates that are nearly double those in more stable organizations.

Although many of the human problems associated with M&As—the fears and uncertainties, stresses and tensions experienced by employees—and the potentially negative repercussions for a range of external stakeholders cannot be totally eliminated, managers can exert favorable influence on both the integration process and consolidation outcomes. There are several concerns, each with a strong social and ethical component, that capture much of this tension.

Competing Claims and Conflicts of Interest

M&As involve multiple parties, each with separate interests and needs. Historically, this conflict has largely been framed in terms of the merger partners' or acquiring and acquired firms' shareholders. As such, legitimate competing claims have been viewed in terms of the interests of the two groups of shareholders. Accordingly, corporate officials were duty bound to define and pursue the best interests of these individuals. The stakeholder view, in contrast, emphasizes that firms have responsibilities to a broader array of groups that go beyond the immediate interests of shareholders—although the latter continue to occupy a place of prominence among stakeholders.

Although the stakeholder model suggests that a utilitarian orientation (i.e., the greatest good for the greatest number of stakeholders) should help resolve the difficulties posed by such competing claims, the "greatest" good in a merger or acquisition is difficult to determine. While shareholders have one set of concerns, other internal stakeholders such as senior managers and employees, and external stakeholders such as customers and local communities, typically have others. Simply put, what might be in the best interests of one particular stakeholder group might very well conflict with the interests of others.

Executive Compensation and Conflicts of Interest

A reality of MA&Ts is that nonexecutive employees and other stakeholders bear a disproportionate risk for poor corporate results, as senior-level executives often receive multimillion dollar payouts when a merger or acquisition is finalized. In most instances, senior-level executives are able to renegotiate their contracts, not only limiting their financial risk but creating significant remuneration in the process (e.g., golden parachutes). Such "change-in-control" provisions, which are often part of an executive's employment contract, may not be fully disclosed or understood by the company's compensation committee, and at times are added only weeks or even days before the finalization of the merger or acquisition. Due to the way in which such corporate reward structures are oriented, individual executives can be biased toward "doing a deal" rather than giving sound, unprejudicial advice to the board.

Culture Conflict as a Competing Claim

While the tensions between different interests can readily exacerbate combination-related decisions, the subtle nature of many competing claims further clouds the consolidation process. Cultural differences between organizations, for example, often create barriers to integration and consolidation, especially in mergers of "equals." Organizational members, an important internal stakeholder group, tend to feel that the culture of the merged organization should be closer to "their" culture (i.e., organizational philosophy, values and beliefs, ways of carrying out tasks) than that of their merger partner. In essence, such competing perceived rights and the resulting collision between different styles, orientations, and values create postcombination difficulties and can distract managers and employees from attending to critical business-related activities.

Secrecy Versus Deception

Tensions typically arise in communication between the managed release of information in an open, honest, and timely manner, and the controlled release of information to distort the truth and manipulate people. When faced with a merger or acquisition, managers are faced with difficult decisions concerning the nature and timing of communication to employees and other relevant publics. While Securities and Exchange Commission (SEC) rules limit what can be told and when it can be released (e.g., insider trading concerns), critics argue that executives often use such constraints to deceive and manipulate employees.

This issue raises concerns about information and property rights. Questions often focus on the extent to which the proposed transaction and its implementation have been carried out in a transparent and honest manner and whether parties with a legitimate right to information relating to the transaction have been given equal access to relevant and appropriate information in a timely manner. Open communication channels are an important factor in minimizing people's fears and creating an informed understanding of the organizational combination.

Insider Trading

Insider trading is when someone makes an investment decision based on information that is not available to the general public. Nonpublic information on an impending merger or acquisition gives "insiders" an unfair advantage to other investors who do not have access to such knowledge. Such illegal insider trading also includes providing others with nonpublic information, and company directors and executives, brokers, and even friends and family members acting on such information can be guilty. For the SEC to prosecute someone for insider trading, however, they must prove that the defendant had a fiduciary duty to the company and/or intended to personally gain from buying or selling shares based on this information. Insider trading is legal once the material information has been made public, at which time the insider has no direct advantage over other investors. The SEC still requires insiders to report all their transactions—and since insiders have insights into the workings of their company, investors often look at these reports to see how insiders are legally trading their stock.

Employee Participation and the Management of Grief, Loss, and Termination

M&As often differ in the extent to which organizational members are forced into accepting certain situations or provided a true opportunity to take part in discussions and decisions. In many instances, precombination planning and execution are tightly controlled by senior-level management, and the resulting change is typically done *to* organizational members rather than *by* them. The ways in which subsequent employee grief, loss, and termination are handled exert a significant impact on employee attitudes and behaviors.

During the initial stages of a merger or acquisition, employees typically experience conflicting emotions ranging from shock, anger, disbelief, and helplessness to hope, excitement, and raised expectations. Following a merger or acquisition, there is typically a "mourning" period, similar to when a member of an extended family dies, as the erosion of familiar work surroundings and the exit of colleagues and friends signals the "end of what was." From a managerial perspective, it is important to assist employees during this transition, helping them deal with such feelings and the new realities of the combined organization. The handling of employee terminations and staff reductions also sends signals about management's values to the employees. Yet research suggests that most people involved in a merger or acquisition feel that termination decisions are handled arbitrarily and ineffectively.

The Ethical and Social Impact of Mergers, Acquisitions, and Takeovers

The level of respect for organizational members and other key stakeholders as individuals is an important dimension of the MA&T process. Historically, the relationship between employer and employee has been governed by the employment-at-will doctrine: The employment contract can be terminated at will by either party at any time for any reason. Although this perspective has been challenged by public policy questions based on the greater good, it has led to the rather narrow view that employees only have those rights that they are able to negotiate with their employers. Employees and other key stakeholders, however, are not mere abstractions and, as individuals, have a moral right to be treated fairly, with respect and dignity.

To a large extent, the ethical and social impacts of MA&Ts are dependent on the extent to which these considerations are appropriately dealt with. While hostile takeovers, especially those characterized as liquidation strategies, are criticized for creating significant disruption and often fail to lead to the proposed level of efficiency and effectiveness, even friendly, collaborative combinations can precipitate disruption, dislocation, and upheaval. It is generally agreed that corporations are responsible for their actions and they have an implicit obligation to their relevant internal and external stakeholders. Thus, to minimize employee trauma and adverse effects on other relevant stakeholders (e.g., customers, local communities), organizations and their management should ensure fairness and due care throughout the M&A process, from precombination planning, through the transaction itself, to postcombination integration.

Such due care includes social impact analyses that present a coherent rationale for the combination, a 3- to 5-year business plan on how the combined business will be operated, and an assessment of the effects of the combination on key stakeholders. These analyses should explicitly address the underlying wealth creation strategies and their ramifications for primary stakeholders (e.g., employees, customers, suppliers) and their broader social impacts (e.g., the effect on the local community). Challenges include balancing costs and benefits across different social levels (e.g., local community vs. regional economic concerns) and time periods (e.g., near term vs. long term, current generation vs. future generations). Early planning and due diligence (i.e., the careful assessment a reasonable person should take before entering in an agreement or transaction with another party) should go beyond financial and legal analyses and include assessments of strategic compatibility, differences in corporate culture, operating style, organizational standards, and business practices. If companies do not address whether and how they will manage these inevitable differences from the outset, they will have to deal with conflict without agreed-on processes, tools, standards, or principles by which to guide smooth resolution.

Clearly, M&As can be risky strategies, but internal development can be just as risky and even more time-consuming. From an ethical and social vantage point, MA&Ts can favorably contribute to the firms involved, their stakeholders, and the larger society if all relevant stakeholders are considered and treated fairly and justly, ensuring that their rights are upheld. Focus should be placed on the extent to which the proposed combination will favorably affect the value of the firms and create more benefit than harm for the organizations' shareholders and other internal and external stakeholders and the larger society.

—Anthony F. Buono

See also Agency, Theory of; Conflict of Interest; Executive Compensation; Fiduciary Duty; Free Market; Golden Parachutes; Justice, Distributive; Market for Corporate Control; Securities and Exchange Commission (SEC); Shareholders; Stakeholder Responsibility; Transparency

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MERITOCRACY

The term *meritocracy* refers to the practice of rewarding or allocating according to those who are excellent or deserving. The etymology of the word comes from the Latin *merere*, which means to receive one's share as pay for work done. Thus, in its simplest form meritocracy can be seen as a way to reward producers. For example, it is often the case that some of the higher-compensated employees in a company are the top salespeople who are paid on commission. Most companies are happy to provide a competitive rate of commission to salespeople who produce for them. Given this incentive, there are many salespeople who are very talented and work very hard to earn handsome incomes—especially in such industries as financial services, real estate, and big-ticket manufacturing and services contracts.

On the next level, things become a little more difficult. How is it that we judge "merit" or "deserts"? This is the more difficult question and links the question of meritocracy with that of distributive justice. Three views will be examined: (1) the traditional position (represented by Daniel Bell), (2) a social welfare–based position (represented principally by John Rawls), and (3) a deserts-based position (represented principally by this author).

The Traditional Position

Daniel Bell says that meritocracy is made up of those who have earned their authority through individual achievement. This is a functionally based understanding. In a sales contest, a company might offer a vacation to Hawaii to anyone selling 50,000 widgets in the latest financial quarter. Under the traditional position, if Andy sells 50,000 widgets, then Andy merits or deserves the vacation. The traditional interpretation of meritocracy is behind much of American and global business assumptions. This is because of the strong link to classical models of capitalism. These models suggest a reward formula to each according to his valued work. Thus, within the rules of fair competition, a person is rewarded more if he produces tangible output that the society values. It is not the case that any means of production are allowable (since, at the extreme, one could kill another and snatch *his* output). Therefore, within the framework of rewarding according to work is a caveat that all the applicable rules of competition have been obeyed.

Implicit in classical models of capitalism is also a vision of useful synergy between various production engines within the society. Behind Andy's vacation reward, for example, is the notion that the company's functional standards should be seen in the context of larger interdependent markets. No single business can be accurately separated out. In macroeconomic terms, the traditional model supports distributing according to social usefulness (which fits the relatively unfettered operation of capitalism à la Friedrich A. Hayek or Milton Friedman). In theory, those who will acquire the most resources will be those who offer a social benefit to those who are able to compensate them for said benefit. In practice, the traditional understanding of meritocracy operates through a dynamic interaction between business and society.

The state steps in to establish fair rules and then acts as a referee only when someone breaks the rules. Apart from that, each person gets what she can with whatever resources she has at her disposal (such as her IQ or her hard work).

The Social Welfare–Based Position

For John Rawls, the question of distributive justice is rather different. He is not content to say that any person begins at some point in the process of acquisition and then is merely constrained by a set of rules and procedures to ensure fairness. Rather, the socioeconomic position of the agent is also considered.

Let's return to Andy and the sales contest. In the traditional position, the only thing we had to consider was whether there were clear rules and that these rules were being followed by everyone in the sales force. This is because what is important is whether someone sells 50,000 widgets or not. If you do, you get the trip. If you don't, you stay at home.

What Rawls wants to ask is *why* Andy is such a good salesman and whether there is some level on which justice might redistribute outcomes for others not as gifted as Andy. Rawls bases his query on *how* the agent is presented with her distribution of talents and social position. His conclusion is that these distributions are accidental and arbitrary. It is an accident that someone is born with whatever natural traits he may possess. For example, let us consider two traits only: being a fast runner and being a fast talker (meaning a persuasive salesman). Now if Sam is a fast runner, he is so because he was born with certain physical traits that made him that way, such as an efficient Krebs cycle in respiration, lung capacity, and so forth. If Jamal is a fast talker, this may also be due to certain natural attributes such as neural wiring that permits quick thinking and an ability to be single minded and not subject to hormonal interference (such as might cause anger or upset). Neither Sam nor Jamal can claim credit for their natural abilities that were given to them by parents in a natural genetic lottery. Thus, if these natural abilities are the basis of societal reward, then in a strong sense neither Sam nor Jamal *deserve* what they have achieved. In this case, the question is raised whether a meritocracy based on natural abilities is thus unfair. Some might contend, for example, that even if we do not deserve our natural abilities it is not unfair if we reap the rewards of those abilities because the system of reward is independent of the system of deserts.

However, Rawls makes the case that social position is also random and arbitrary. For example, if you put Sam the fast runner into a hunting society, he may garner the most goods because his speed makes him a better hunter. However, if you put him into the information-based service society, then speed is irrelevant. He will not be rewarded. The same may be said of Jamal in reverse order (viz., he would do poorly in the hunting society but would prosper in the information-based service society). Neither Sam nor Jamal could help growing up in the society in which they were born. It was an accident. Thus, the fact that their natural abilities may or may not be rewarded in that society is also an accident. To be rewarded based merely on an accident is not deserved. Thus, a meritocracy that is based on reward from undeserved social position is similarly unfair.

Therefore, both natural abilities and social position may not be the basis of distributive justice because they are unfair. The naturally advantaged are not to gain merely because they are more gifted. The rectification of these disparities in Rawls is his difference principle that makes all inequalities subject to the stipulation that the least advantaged will benefit from them.

There is some dispute on how Rawls's difference principle is supposed to work, but in our example of Andy, the salesman, Rawls might argue that part of the sales contest reward be distributed to the losers in the contest and to the secretaries and to the maintenance crew. Of course, if Andy now has to settle for a vacation to Long Island (say he lives in New Jersey) instead of a trip to Hawaii, he might not be so keen to work those extra weekends to sell the widgets. Thus, a probable outcome of Rawls's position is lower productivity since full merit reward is being modified for social welfare concerns.

The Debate Reconsidered

How do these two positions, the traditional approach and the social welfare–based approach, view each other? The traditional approach responds to Rawls that distributive justice does not require that each agent *deserve* everything she has obtained, merely that she has played by the rules (enforced by the government). As Robert Nozick once famously said, it need not be that the foundations underlying desert are themselves deserved, *all the way down.* Under this account, it is irrelevant to justice whether one deserves one's natural or social advantages. They are what one is given. So long as one goes forth from the starting point and obeys all the rules, then justice is upheld. However, Rawls would demur by claiming that natural talents are collectively held. If this is so, then the least advantaged has some claim on the goods possessed by those who are society's winners because of natural talent or social position.

Those evaluating the arguments supporting the above positions should note that much depends on the understanding of the agent and her role in society. If the agent is primarily seen as a largely separate, autonomous entity acting for herself as much as possible, then the traditional position will seem most appealing. The individual cannot help how she begins life. Why make her "pay" for her positive talents and advantages? If one begins at a fundamental position of a Lockean state of nature, then it is after all one's use of natural resources that would determine ownership. For Locke, the process of making a valid property claim depends on one actually using what is claimed. If one fails to use the land or ceases to use the land, then there is no valid claim. (This "use" principle is also behind the concept of adverse possession that entitles one to engage in a valid taking of another's property if the owner is not using it and does not defend it.) The "use" principle is based on a presupposition that it is individual effort that counts the most. Hobbes complicates the picture even further by suggesting that all agents are different but equal. If one person has natural advantage A to the *n*th degree then another will have a different but equally as effective natural advantage B to a degree such that both can compete on an equal footing. If one finds these depictions of the state of nature fundamentally correct, then the individualistic position again seems most plausible.

However, if one sees the individual as contextually linked in a kingdom of ends, then the story plays out differently. For the social welfare advocate to make her case, it is necessary to conceptualize society as radically interdependent. The ideas of John Donne in *Meditation XVII* or Martin Luther King Jr. in *Letter From a Birmingham Jail* describe a society in which there are no largely separate individuals. Each person in a society is connected to every other person such that the proposition that natural assets are collective is entirely plausible. Second, Rawls's difference principle can be seen as a response to the question of moral luck. How much should one's personal happiness depend on factors outside one's control? How much should our judgment of others depend on luck (natural talents or social position)? If it seems *wrong* for luck to be determinant without recompense from the community, then you are probably on the side of social welfare.

The Deserts-Based Position

Joel Feinberg has said that desert without a basis is simply not a desert. Feinberg then calls for some sort of basis so that if a person is deserving of some sort of treatment, he must, necessarily, be so in virtue of some possessed characteristic or prior activity.

The traditional position asserts that reward is based on merit and merit is based on achievement (as per Andy and the sales contest). The deserts position agrees with this in part. Both concur that merit is based on achievement, but the traditional position measures achievement as an outcome only. The deserts position measures achievement on the basis of work done by the individual without the advantage of any preferment. Thus, if you were a manager for the ABC Widget Corporation and your northeast sales staff was dominated by a producer named Andy who has family connections that allow him uniquely to always lead the company in sales, then if you wanted to have a sales contest that would motivate producers and increase production, you should make the sales contest based on bettering your last year's rolling average by some percentage. Such a sales contest would reward those who improve from where they are and mute the undeserved advantages Andy has due to family. Thus, in hiring and compensation practices, advocates of the deserts position strive to look at how far each individual has gone and strive to encourage and reward personal growth (and not just absolute outcomes).

In contrast to Rawls's social welfare conception, the deserts position judges merit on past actions and not on some sort of social, utopian goal. The traditional meritocracy model might ask, for example, "Who do you want doing your newly mandated Sarbanes-Oxley corporate audits each year—a person who has graduated from a top business school or someone who went to a midtier or lower-tier school and was probably admitted under Affirmative Action?" The assumption under the traditional model is that the former person has reached some higher level of technical competency and therefore merits the contract. Those advocating the deserts model would ask further questions about both candidates. It might be the case that the latter candidate has had to work very hard for everything he's gotten while the former candidate got into school because his family has always given a lot of money to the school. The former candidate's status of achievement may not be indicative of how well he might perform over the long haul. Since so much has been given to him, and since the latter candidate has already demonstrated an ability to overcome adversity, the deserts model would suggest hiring the mid- or lower-tier graduate (because of his previous degree in the school of hard knocks).

Obviously, this is a case at the extremes. However, it is put forth to make an abstract point about merit. Like the social welfare–based approach, the deserts model recognizes that some people have natural and environmental advantages that can include some or all of the following when it comes to the ability to compete for society's goods:

- Adequate food, clothing, shelter, and protection from unwarranted bodily harm
- Basic educational opportunity
- Being treated with dignity and love for who you are
- A nurturing home environment
- Parental models for patterning behavior (that the society views positively)
- Freedom from disabling disease whether it be mental or physical
- Inside connections affecting admission to universities and to the professions
- Affluence

Obviously, this list could go on and on. But when Mr. B speaks with hubris about how he has become a partner in the accounting firm, it may be important to know that Mr. B's father is the senior partner in the firm and got B his job in the first place (and has been holding B's hand all his life). This is the life of preferment that allows parents to present to their children an easy road. All the child has to do is not to screw up too badly and he's set for life.

This preferment list need not merely include socioeconomic factors. Race and gender may also be factors. According to the deserts-based model, this is *not* success by merit; it is success by unmerited preferment. Thus, the deserts-based approach contends that it combines the definition of merit (from the traditional model) with the concern for the distribution of natural and social advantage (the social welfare–based approach).

Conclusion

The question of how we are to think about meritocracy is an important one for business and society. Management strategies that follow one of the above approaches will be markedly different from those that adopt another model. Thus, it is important for businesspeople to come to terms with a particular model of meritocracy and make it their own. It will guide their worldview and management style. It is, of course, a separate question as to which model of meritocracy will most significantly increase the bottom line (since there are many ways to do that these days—including the so-called triple bottom line assessment that included ethics and environmental awareness as two additional categories that stand beside the standard depiction of monetary profit and loss). However, the question is an important one for everyone in society (including the business community) to assess in order to create the best systems of goods allocation (distributive justice).

—Michael Boylan

See also Affirmative Action; Aristotle; Collective Choice; Cowboy Capitalism; Deep Ecology; Entitlements; Ethics of Care; Existentialism; Fairness; Feminist Ethics; Hayek, Friedrich A.; Human Rights; Justice, Distributive; Just Wage; Marxism; Mill, John Stuart; Moral Luck; Moral Reasoning; Nozick, Robert; Rawls, John; Tax Ethics

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METAETHICS

The most inclusive way of understanding metaethics is as an investigation into the nature of moral judgments: judgments about the morality or immorality of actions, institutions, states of affairs, or whatever. What makes this formulation inclusive is that it describes both of the two areas of ethical inquiry that metaethics is generally understood as encompassing. These two areas are, first and most narrowly, the meaning of moral language; second and more broadly, the nature and possibility of moral knowledge. (Talk of "judgments" covers both because it can refer to both the words used in making a judgment and what is claimed in making that judgment.) Used to refer to the first area of ethical inquiry, metaethics is employed in what might be called its *linguistic* sense. (As it is still words and their meanings involved, for convenience, this description will apply even when, as sometimes occurs, the talk is of a "conceptual" or "logical" analysis rather than a linguistic one.) Used to refer to the second area, metaethics is employed in what might be called its *epistemological* sense (albeit that it covers ontological issues about *what* is known as well as more properly epistemological issues about *how* it is known). Used in either of these two senses, the prefixing of *meta* to *ethics* implies something above and beyond ethics as normally understood (*meta* being Greek for, among other things, "after").

As a term, *metaethics* entered the philosophic lexicon sometime in the 1950s or 1960s through the work of those philosophers, labeled "linguistic philosophers" by opponents, for whom an analysis of language was the first and most important recourse in solving philosophical problems. Fittingly enough then, in this its introductory stage, metaethics was used in only its linguistic sense. With the decline of linguistic philosophy after its 1950s and 1960s heyday, the epistemological sense came to be added to the linguistic. And today, although exclusively linguistic definitions can still be found, metaethics is more usually defined as a combination of its linguistic and epistemological senses.

Scope

Characterized in the linguistic sense, metaethics concerns what is meant when it is said that something is "good," "bad," "right," "wrong," and so on. Characterized in the epistemological sense, it concerns overlapping matters such as whether there is any sort of factual basis to moral judgments, whether moral judgments are capable of being true or false, whether we can ever know what is moral or immoral, and so on. On either characterization, in practice it is the same issues that emerge as metaethical with the only difference being whether, in terms of a purely linguistic definition, they are seen as problems of an entirely linguistic sort or whether, in terms of the now more usual combinatory definition, they are seen as both linguistic and epistemological in nature with the difference being simply a matter of the direction from which they are approached—that is to say, as a search for what is meant in uttering moral judgments or as a search for the epistemological basis to such judgments.

The resulting list of issues is best understood as a series of opposing standpoints stemming from differing views of the meaning and/or epistemological basis of moral judgments. They are, for the most part, standpoints that can be characterized in terms of an opposition between those who say there is some kind of "objective basis" to moral judgments and those who deny this by saying that they are in some sense or other "merely subjective." More particularly, we have on what can be called the "objectivist" side of the argument a position labeled "realism" (the claim that there are facts to make moral judgments true or false) from which follows another position labeled "cognitivism" (the claim that moral judgments can be known to be true or false). Contrariwise, on what can be called the "subjectivist" side, we have a denial of both these standpoints in the shape of positions labeled "irrealism" and "noncognitivism," respectively (with irrealism denying that there are facts that can make moral judgments true or false and noncognitivism denying that such judgments can be known to be true or false).

Consequent Distinctions

As was indicated in noting the meaning of the word *meta*, implicit in the idea of metaethics as a distinctive area of ethical inquiry is that, in terms of what is being examined and explained, it is the most fundamental area of such inquiry. Thus, a necessary accompaniment to the distinguishing of metaethics as an area is its distinguishing from other areas concerned with less fundamental matters demanding a lower level of explanation. And here two such areas have come to be recognized: one labeled "normative ethics" and the other "applied ethics."

As presently conceived of, normative ethics is about what it is that makes actions and arrangements moral or immoral and, as a consequence, judgments as to their morality or immorality, true or false. It is concerned with this in general rather than in particular circumstances or particular instances. It is concerned, therefore, with accounts of the nature of the ethical given by theories such as utilitarianism, which says that we should aim to optimize human welfare, and Kantianism, which says that we should do whatever duty dictates.

In contrast, and as the title would suggest, applied ethics is very much concerned with particular circumstances or instances. It comes in two forms: a broad form concerned with the ethics of particular sorts of activities and a narrower one focusing on particular issues. Thus, in its broader form, applied ethics denotes specialist subject areas such as business ethics, medical ethics, research ethics, and so on. While in its narrower form it denotes an inquiry conducted outside a specialist subject framework into contentious issues such as abortion, capital punishment, pornography, and so on.

Talk of applied ethics came after talk of normative ethics. As originally conceived of, normative ethics covered both theoretical accounts of the nature of the ethical such as utilitarianism, and so on, as well as what we now distinguish as applied ethics. This reflects the fact that what was seen as essentially distinguishing metaethics from other and less fundamental areas of ethical inquiry is that it is *non*normative. That is to say, an area of inquiry that is *not* about determining what is moral or immoral ("normative" being a word for just such a determining). In contrast, those less fundamental areas distinguished as normative ethics and applied ethics were both, in their different ways, seen as *normative.* So while metaethics was conceived of as a kind of value-free analysis and, therefore, neutral with regard to determining what is moral or immoral, normative ethics and applied ethics were not. Consequently, the role assigned to metaethics with respect to determining morality or immorality is as a necessary preliminary. Its role, in short, is to sort out ethical language and/or epistemological issues regarding objectivity and subjectivity *before* any such determining by normative ethics and applied ethics takes place: a demarcating of roles traditionally summed up by saying that metaethics concerns question *of* or *about* ethics, whereas the other two concern questions *in* ethics.

To this was generally added a demarcation of roles between normative and applied ethics based on the former determining morality or immorality in general, while the latter does so only in particular circumstances or instances. For what this difference suggested is a division of labor in which normative ethics supplies the criteria for deciding what is moral or immoral and the job of applied ethics (and the thing being "applied") is simply to bring those criteria to bear on particular circumstances and instances.

What emerges from this notion of metaethics as a distinctively nonnormative area of ethical inquiry functioning as a necessary preliminary to the two normative ones is, in terms of explanatory dependence, a decidedly hierarchical view of such inquiry. At the top is metaethics as an area that has to be sorted out before the other two areas are engaged in for otherwise they will be subject to all kinds of errors and confusions. In the middle is normative ethics as the area needing to be sorted out before it can be decided what to do in particular circumstances or instances. And at the bottom is applied ethics as the area dependent on normative ethics for the theories providing it with criteria for determining just what things are good or bad, right or wrong.

Criticisms

Well established though it is, this notion of metaethics as a specifically nonnormative area of ethical inquiry standing over and above normative areas is not without its critics. Their criticisms come in two main forms, one of which is more global in character than the other.

The less global is to question just how much of difference there is between metaethics and normative ethics. It can be argued, for instance, that the supposedly metaethical distinctions between realism and irrealism or cognitivism and noncognitivism are nothing more than a decision to (respectively) opt for or reject normative theories such as utilitarianism and Kantianism. And if so, then rather than constituting distinct areas of ethical inquiry, what has been distinguished as metaethics and normative ethics are merely parts of an interconnected theorizing about ethics for which the only heading needed is the very general one of "ethical theory."

Unlike the above, the more global criticisms do not just argue for a dissolving of the distinction between metaethics and normative ethics. They argue against the whole hierarchical and, in particular, top-down approach to ethical inquiry implied by the distinction. They do this by questioning the assumption of an explanatory dependence of normative ethics on metaethics and even, among the more radical of these critics, of applied ethics on normative ethics ("explanatory dependence" being the notion set out at the end of the previous section that explanations in normative ethics depend on metaethical ones and explanations in applied ethics on normative ones). Arguably, they say, dependence could also operate in the reverse direction. Thus, it is claimed that positions classified as "metaethical" can both arise from and be supported by stances on issues classified as belonging to normative ethics. And for some, the same is even true with respect to the relationship between normative ethics and what is classified as applied ethics, with applied ethics being both the test bed for theories of the nature of the ethical and their possible source. In short, although there are certainly different levels of generality with respect to explanations in ethics, there are not, at least not in any merely top-down way, different levels of explanatory dependence from theories of a high-level metaethical sort to those of a midlevel normative ethical sort and on to those of a bottom-level applied ethics sort. Not surprisingly then, these more global critiques of the concept of metaethics invariably come from those skeptical of the usefulness of the more abstract sort of theorizing about ethics and/or viewing applied ethics as the most potentially revealing way of approaching ethical issues.

Connections to Business Ethics

The way connections between metaethics and areas of applied ethics such as business ethics is viewed depends on whether, or to what extent, the top-down model of their relationship talked about above is accepted. For those who wholly accept the model, work in business ethics will be seen as predicated on theoretical assumptions provided by normative ethics and, ultimately, metaethics. Take, for instance, the much-discussed Ford Pinto case. Here it is said that a proposed solution to the problem of an unsafe design of motor car (the Ford Pinto) was to balance the monetary cost of changing to a new and safer design against actuarial estimates of the monetary cost of those deaths and injuries that were likely to result from staying with the existing and unsafe design. As it is being assumed that comparing the relative monetary cost of the two opposing options offers a definitive answer to the problem of what to do, then in terms of the top-down model this is a solution predicated on the metaethical assumption of an objectivist view of morality and, more specifically, a normative ethical theory of a utilitarian sort whereby right and wrong are determined by the extent to which there is an optimizing of human welfare (with, in this case, welfare being measured by a balance of relative monetary costs). So in these terms, a defense or rejection of that proposed solution would be by appeal to findings belonging to higher levels of ethical inquiry in the shape of normative ethics and metaethics that are beyond the purview of an applied area such as business ethics. Conversely, those skeptical of this top-down approach would have a less rigidly demarcated view of the situation. So while not denying the obvious truth that ethical inquiry can be conducted at different levels of generality with respect to the questions being asked, they would view ethical inquiry as a more or less integrated whole with fluid boundaries between different levels of generality and an explanatory dependence that is just as much from the less general to the more general as vice versa. Thus, for those skeptical of the notion of metaethics as a distinct and ultimate area of ethical inquiry, offering a solution to a problem within an area of applied ethics such as business ethics (be it the Ford Pinto case or anything else) is just as much a question of putting the perhaps overly abstract theories of normative ethics and metaethics to a practical test as it is of looking to those areas for theoretical guidance.

—John Kaler

See also Cognitivism and Ethics; Consequentialist Ethical Systems; Ethical Naturalism; Fact-Value Distinction; Ford Pinto; Is-Ought Problem; Kantian Ethics; Moral Realism; Naturalistic Fallacy; Noncognitivism; Normative Ethics; Relativism, Cultural; Relativism, Moral; Utilitarianism

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METALLGESELLSCHAFT

In the early 1990s, Metallgesellschaft AG, a German conglomerate that had evolved from a traditional metals company into a provider of risk management services, was one of Europe's most successful businesses with approximately $15 billion in annual sales. However, that success was marred when, in December 1993, MG Refining and Marketing Inc. (MGRM), a subsidiary of Metallgesellschaft AG, revealed that it had lost $1.5 billion from trading in energy derivatives.

The tale of MGRM's troubles starts with their marketing strategy. MGRM committed to sell to their customers set quantities of fixed-price petroleum products every month for up to 10 years. These contracts proved to be very popular. Each MGRM contract contained a sell-back option allowing MGRM's customers to terminate the contracts early if the next-to-expire (i.e., "front-month") New York Mercantile Exchange (NYMEX) futures contract was greater than the fixed price at which MGRM was selling the oil product.

To manage the risk from these contracts, MGRM established large futures and swap positions in gasoline, heating oil, and crude oil as hedges. These positions involved about 155 million barrels of underlying oil products. It is not clear that there was anything conceptually wrong with MGRM's hedging strategy. But it is clear that MGRM had not adequately communicated its intentions to its parent company and financial backers. In late 1993, MGRM's futures positions lost money as spot energy prices fell, requiring the immediate cash outflows to meet margin calls. Presumably, their other assets involved in the hedge were increasing in value in a way that offset those outflows, but these increasing values could not be turned into cash flows.

By the end of 1993, the heavy cash outflows required to maintain the hedge program, combined with concern about the credit risk taken on with the large swap position, caused MGRM's parent to change its assessment of the potential risks involved in its customer contracts. After reviewing the program in December 1993, MGRM's parent decided to end MGRM's participation in the hedge program, a decision that proved very costly to the firm.

Because the liquidation was publicly announced in advance, other traders were able to extract a large premium from MGRM. The net result is that MGRM lost on the futures and swap side of the transaction while failing to realize the offsetting gains they had reasonably anticipated. In total, MGRM lost $1.5 billion in the disaster.

—James A. Overdahl

See also Bankers' Trust; Barings Bank; Financial Derivatives; Long-Term Capital Management; Scandals, Corporate

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METHODOLOGICAL INDIVIDUALISM

Methodological individualism is the doctrine that large-scale social events and conditions, such as wars, social customs, economic recessions, the crime rate, and the state, should be explained or understood wholly in terms of the beliefs, intentions, attitudes, and actions of individual people. It is "methodological" in the sense that it indicates how social scientific inquiry ought to proceed; the "individualism" stems from its insistence that social scientific explanations should, at least ultimately, involve only facts about individual agents. Methodological collectivism or holism, in contrast, contends that at least some social phenomena can be explained only at a macroscopic or holistic level.

Methodological individualism was at issue in many high-profile disputes in sociology, psychology, economics, and the philosophy of history during the late 19th and 20th centuries. An early example is the so-called *Methodenstreit* controversy between members of the German Historical School and the Austrian

School in economics. More recently, Jon Elster has defended methodological individualism as a corrective to Marxists' fondness for functional explanations. Notable proponents of the doctrine include the sociologist Max Weber, the philosopher Karl Popper, and the economist Friedrich A. Hayek. The philosophers G. W. F. Hegel and Karl Marx and the sociologist Émile Durkheim are prominent collectivists. Although few social scientists today identify themselves as methodological collectivists or holists, methodological individualism is at odds with forms of explanation that remain widely used in the social sciences, such as structuralism, pure statistical analysis, and the explanations found in many kinds of sociobiology.

Although methodological individualism, at least as Weber initially formulated it, is an epistemological view about social scientific explanation, it is easily and often confused with other views, partly because it is often found together with other kinds of individualism and atomism. Popper and his student J. W. N. Watkins, for example, seem to defend methodological individualism out of a commitment to metaphysical or ontological individualism, the view that social entities are in reality nothing but aggregates of individual people and their behavior. One need not embrace this metaphysical thesis to be a methodological individualist, however, nor does embracing it commit one to the doctrine. So too, methodological individualism is distinct from political individualism, although Hayek and Popper espouse both doctrines and claim to find important connections between them. Although Thomas Hobbes is often characterized as a methodological individualist, his political individualism is better understood as related to his psychological atomism—his attempt to explain the possession of characteristic human capacities such as thinking and reasoning without appealing to people's relationships with others. Atomism of a different sort holds that social goods should be regarded as wholly constituted by interconnected individual goods, but this position too neither implies nor is implied by methodological individualism.

Weber acknowledges that we often speak of "social collectivities" such as corporations, associations, and states as though they were individual agents, but he contends that in social science research, collectivities should be treated as the product of individuals and their actions. This is because the actions of individuals are, in his words, "subjectively understandable." We can understand the motives and intentions of individuals that lead them to act as they do, and macrolevel social happenings and conditions are adequately explained only when given in these terms. Since the actual motivations of individuals may be unknown or unavailable to the sociologist or economist, however, social scientists must typically invoke a model of rational human action, which for Weber is his theory of ideal types.

Weber influenced Hayek and other members of the Austrian School who have been among the most ardent defenders of methodological individualism. But while Weber's theory of ideal types implies that social events and structures are rationally intended, Hayek in particular emphasizes that large-scale social phenomena are often the spontaneous and unintended effects of human action. What needs theoretical explanation, he argues, is how social order can be the result of individual action without having been designed by anyone. Explanations of money, markets, or the law, for instance, should be given in terms of how the relevant choices appear from the perspectives of individuals and in light of their beliefs, norms, and interests. This view leads Hayek to criticize the approach of the Keynesians whom he regards as attempting to explain macroeconomic conditions (such as total employment or the inflation rate), not in terms of the decisions of individual agents, but in terms of other macroeconomic conditions. Later in his career, however, Hayek apparently abandons his commitment to methodological individualism in favor of evolutionary explanations.

Many philosophers associate methodological individualism most closely with Popper and Watkins. While Weber and Hayek stress the differences between the natural and social sciences, Popper and Watkins stress the structural similarities between these two kinds of inquiry. Likening social science to mechanistic physics, Watkins writes that explaining the pressure inside a gas container in terms of other macro phenomena, such as the volume and temperature of the gas, would give merely a "halfway" or "unfinished" explanation. An appropriately "rock-bottom" account would explain the pressure in terms of the properties of gas molecules. Analogously, explanations of large-scale social phenomena are complete only when they reduce to facts about particular agents. Apparently, the reason why only such "finished" explanations are adequate, in Watkins's view, is that just as a gas is nothing apart from its constituent molecules, social collectives are nothing over and above their individual members.

Methodological individualism has been criticized on various grounds, but the success of these criticisms often depends on how the details of the doctrine are understood. Unfortunately, its proponents and critics have rarely agreed on what, exactly, they are disputing. Kenneth Arrow, for example, criticizes the doctrine on the grounds that economic production uses technical information, some of which is irreducibly social in character. Although this may be a cogent point against some of the economists Arrow has in mind, a methodological individualist need not deny the social nature of the information on which individuals sometimes act. In general, the doctrine is not committed to particular claims about the content or source of individuals' mental states. Many question, though, whether satisfactory social scientific explanations are always to be found at the intentional level. Consider Joseph Heath's example of a debate among social scientists as to why stepparents have a far greater propensity to kill very young children in their care than biological parents. The question is why one group is better able to inhibit aggression toward crying babies, for instance, than another. The answer may be that biological parents simply find their babies "cuter" than stepparents do, although they may be unable to articulate any meaningful basis for such judgments. An evolutionary account that explains parental affection in terms of inclusive fitness and sexual selection may be able to make sense of something that an account in terms of intentional states therefore cannot, insofar as the evolutionary account explains subintentional biases.

—Samuel V. Bruton

See also Austrian School of Economics; Hayek, Friedrich A.; Individualism; Marx, Karl; Weber, Max

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Methodologies of Business Ethics Research

The methodologies employed by business ethics scholars are extensively diverse, covering a wide range of theoretical foundations, data collection techniques, and analytical methods. Business ethics research may be characterized by theoretical discussions regarding the application of major ethical theories—utilitarian, justice, and rights, for example—to various knotty ethical dilemmas or situations found in business as well as the empirical exploration of decision-making processes and elements that influence an individual or organization's decisions or actions, such as personal traits, organizational influences, or the context of the ethical situation. In general, business ethics methodologies can be grouped into two analytical categories: normative and descriptive.

Normative Research

Normative business ethics scholarship focuses on assessing or prescribing behavior related to individuals, organizations, or societies from an underlying set of normative or ethical values that determines what is right or wrong. Normative research emphasizes what is right or ought to be. Normative business ethics scholars frame their research questions as abstracts or standards that should be held by all individuals or organizations in general. The methodologies employed emphasize the pursuit of an ethical ideal. This type of research gives rise to analytical frameworks that question basic assumptions, as well as seek resolutions to ethical questions. For example, a classic normative approach to ethical analysis might involve an analysis of the thesis (a particular point of view), antithesis (the opposite or contrasting point of view), with a resulting synthesis (a compromise or new, integrative point of view). Scholars taking this perspective are often trained in philosophy, theology, and other liberal arts disciplines where theoretical foundations provide a framework for interpreting information and framing the preferred outcome or prescribed behavior.

Descriptive Research

Descriptive business ethics scholarship concentrates on describing an individual or organization's actions to explain or even predict behavior. Applied social scientists often place greater emphasis on descriptive business ethics research. Their explorations are not theoretical but more often empirical in the collection of information about an individual or organization. These scholars tend to ground their research in social science theories that enable them to construct testable hypotheses, or questions, that will be answered by the results found in their study. The goal for descriptive research is to explain the behavior of individuals or organizations. Descriptive research might investigate business policies or practices and whether they are influential in organizational members' decisions or actions. Specific to business ethics research is the focus on decision making or behavior in the context of business organizations or business schools where future managers are being trained.

Descriptive research is more practical or pragmatic and less likely to frame the results derived from the data in terms of what ought to be done. *Ethical* is not understood as an "ought" or "should" but more in terms of an adjective describing the context of the behavior, that is, ethical behavior as opposed to marketing behavior. Descriptive business ethics research reports on what is done. For example, in an experimental research investigation, the question may be framed as a causal relationship question, whether X causes Y—that is, does having a code of conduct result in the organization's employees acting in a more compliant or ethical manner? Experiments can be conducted in a laboratory (controlled environment) or field setting. The two primary issues for evaluating experimental research are whether there is internal and external validity. If the experiment is internally valid, there is greater certainty that X caused Y. Internal validity may be higher in laboratory experiments since there can be greater control exerted over the exercise or study. However, there may be concern regarding the study's external validity. External validity has to do with the generalizability of the results, that is, will similar results leading to the same conclusions or proof be found if the study is conducted over and over again with different subjects or in a different setting? The artificiality of a laboratory experiment may reduce external validity, yet conducting the study in the real world, a field setting, might increase external validity.

Another descriptive research focus is on correlational approaches. Rather than being able to manipulate the variables to test a causal relationship, business ethics scholars may seek to discover a correlation between data. One example would be to assess whether there is a difference between experienced managers and inexperienced business school students. Two separate but identical surveys could be distributed to the two populations and the results could be compared to see if there is a correlation between the two groups, or if not, if the differences in their age and work experience might explain why different results were discovered.

Data Collection and Analyses Used

Influenced by whether the research is primarily normative or descriptive, the methodologies used by scholars in business ethics research can range from case studies, protocol interviews, or content analysis of secondary organizational documents to laboratory experimentation, assessment of databases, or survey work using ethical scenarios, statements, or demographic information to collect information. As implied above, applied social scientists would be more likely to use experimental designs or surveys and apply quantitative analysis to the data. The data could be analyzed using simply frequency analysis, *t* tests, or other basic statistical techniques. There is a trend toward more sophisticated data analysis techniques, such as regression analysis and other higher-order investigations, as the population of business ethics scholars become better trained in advanced statistical analysis.

Complimenting the applied social scientist and their quantitative data analysis approaches is a growing number of scholars seeking more in-depth answers to their investigations using qualitative analysis techniques based on data gathered through interviews or assessing information found in case study narratives. Ethnographic research, such as participant observation, may provide for a more in-depth understanding of an individual's decision-making process than quantitative techniques. While some believe that qualitative analysis provides richer, more in-depth analysis of information, there is concern that the data analysis is subject to researcher bias and interpretation. Thus, this methodology necessitates great care in ensuring that the results drawn from the data are reliable and valid.

—James Weber

See also Business Ethics; Descriptive Ethics; Normative/Descriptive Distinction; Normative Ethics

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MILKEN, MICHAEL ROBERT (1946–)

Michael Milken was an executive and a star trader at the now-defunct investment bank, Drexel Burnham Lambert. He received the nickname "junk bond king" for the role he played in making Drexel the leader in the junk bond market. Junk bonds are speculative investments that carry a higher than usual rate of interest (i.e., high yield) because they are associated with a greater risk of default. Junk bond financing fueled the takeover market of the 1980s by making it possible for smaller firms to mount a hostile takeover of much larger firms. Junk bonds and the role that Milken played in popularizing them have defenders and detractors, both of which are passionate. Critics blame junk bonds for the collapse of the savings and loan industry and the debt that mounted in the 1980s, leading to recession in the early 1990s. These critics claim that the 1980s became a decade of greed and that Milken and his junk bonds are responsible for the financial and emotional costs that were incurred. Milken's defenders say that his financial innovations fueled the U.S. economy's rapid growth by providing entrepreneurial firms with the financing they needed. They also argue that leveraged buyouts and mergers made possible by junk bond financing helped make the U.S. economy leaner and more competitive in a global marketplace. His defenders and detractors agree on one thing—junk bonds made Milken a very wealthy man.

In 1989, the then Manhattan U.S. District Attorney Rudy Giuliani charged Milken with 98 counts of racketeering and fraud: Milken was then indicted by a federal grand jury. Facing serious federal charges of insider trading, Michael Milken pled guilty to five lesser securities and reporting violations. He received a 10-year sentence, which was later reduced to 2 years. Milken paid a $200 million fine, paid another $400 million in settlements relating primarily to civil lawsuits, and was banned for life from the securities industry. In 1998, he admitted to acting inappropriately as a strategic business consultant by advising MCI and Revlon on deals. He was fined $47 million for violating his probation. Despite these fines, Milken remained a multimillionaire.

Since his release from prison in 1993, Milken has spent his time as an entrepreneur and a philanthropist. Along with his brother, Lowell, and Oracle Corporation CEO Larry Ellison, Milken formed Knowledge Universe (KU), a more than $1.5-billion holding company that supports a vast array of educational enterprises throughout the world. Since being diagnosed with prostate cancer in 1993, Milken has devoted his philanthropic endeavors to funding cancer research. Since its 1993 founding, Milken's Prostate Cancer Foundation (PCF—formerly named CaPCure) has raised more than $230 million, making it the world's largest private sponsor of prostate cancer research. Rather than relying on basic science, PCF focuses on reducing the wait time for grant funding and funding therapy-oriented solutions. PCF holds researchers accountable for results and requires collaboration among institutions, business, and academe: This businesslike approach to philanthropy is often called venture philanthropy.

—Ann Buchholtz

See also Corporate Philanthropy; Leveraged Buyouts; Market for Corporate Control; Mergers, Acquisitions, and Takeovers; Strategic Philanthropy

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Mill, John Stuart (1806–1873)

John Stuart Mill was born in Petonville, England, on May 20, 1806—the first son of James Mill and Harriet Barrow. John Stuart's intellectual journey commenced at an early age with his father as his primary instructor. A demanding and diverse educational process began with Mill grasping Greek and English at age 3 and Latin at age 8. By his middle teenage years, he had completed advanced studies in history, mathematics, and economics. Mill's education was enhanced by annual trips to the estate of Jeremy Bentham—a friend of James Mill—where John Stuart was immersed in Bentham's utilitarian ideas.

At the age of 17, John Stuart began what would become a 35-year career at the East India Company, starting as a clerk and rising to the second highest position in the company's London-based office. Mill enjoyed his career as it provided a sufficient amount of time for his true passion of learning, thinking, and writing. In his early 20s, Mill found himself suffering from a severe case of depression. Many scholars attribute this depression to the lack of social nurturing, as well as to the friendships that were sacrificed to complete his extensive home schooling. As he began to read the works of Wordsworth, Comte, and Coleridge, his emotional state strengthened, and he was able to set about his life's work of social reform and philosophy.

In 1830, Mill met Harriet Taylor and the two developed a close relationship. Over time, Taylor became an increasingly influential figure in Mill's life and, 2 years after the death of her husband, the two married. The couple collaborated on Mill's writing until her death in 1858. In 1865, Mill was elected to the House of Commons, but failed in his reelection run in 1868. Throughout his life and especially during his time as an elected official, Mill was a strong supporter of the rights of women and wrote a major work on the subject titled *The Subjection of Women* in 1869. John Stuart Mill died in 1873 and was buried next to Harriet Taylor Mill in Avignon.

Today, John Stuart Mill is best known for his writings on utilitarianism, the teleological theory that people are obligated to do those actions that produce both mental and physical happiness and/or avoid mental and physical pain. In 1843, he published his work titled *On Logic*—a well-accepted philosophical work on the use of logic in the field of social science. In 1848, he published *The Principles of Political Economy*—a piece dedicated to the social economic situation of his time. Mill's most famous pieces are *On Liberty* (1859)—a work of normative political theory that defends a principle of liberty—and *Utilitarianism* (1861)—Mill's most famous ethical statement. His *Autobiography* was published in the year of his death, and his only major work dealing with religion—titled *Three Essays on Religion*—was published 1 year later. Many of Mill's writings continue to be used in other areas such as economics, philosophy, political science, and religion.

—Corey A. Ciocchetti

See also Bentham, Jeremy; Dilemmas, Ethical; Freedom and Liberty; Moral Reasoning; Paternalism; Utilitarianism; Utility; Utility, Principle of

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Miller-Tydings Act of 1937

The Miller-Tydings Act of 1937 exempted retail price maintenance agreements (fair trade provisions) in interstate commerce from federal antitrust laws. Under fair trade laws, manufacturers created resale price contracts with distributors that required their retailers within a given state to sell "fair-traded" products at the same price. Specifically, the Miller-Tydings Act, in effect, amended Section 1 of the Sherman Act. Miller-Tydings made legal contracts or agreements prescribing minimum prices for the resale of commodity products sold and shipped in interstate commerce bearing a label, trademark, brand, or name of the producer or distributor when such products are in free competition under local state law.

During the 1930s, "mom-and-pop" druggists, hardware and appliance merchants, and grocery stores began to experience competition from large chain store operations throughout the United States. The chain stores benefited from economies of scale and were frequently able to sell at prices lower than that of their smaller rivals. In an effort to level the competitive playing field, a number of states passed fair trade laws that heavily taxed chain stores. At the federal level in 1936, Congress enacted the Robinson-Patman Act to prohibit price discrimination by suppliers to small businesses.

Before Miller-Tydings was enacted, various populists suggested that chain stores represented an assault on the economic backbone of American democracy, small businesses. They argued that small businesses needed protection from the predatory pricing practices of ruinous competition. Similarly, some economists and jurists opposed fair trade laws on the grounds that such laws significantly reduced or even eliminated competition (specifically small competitors) from the marketplace. President Franklin D. Roosevelt strongly objected to fair trade provisions on the grounds of potential resentment by consumers who would be faced with escalating prices.

Manufacturers and independent retailers were the main proponents of fair trade laws. Manufacturing firms supported the passage of fair trade laws because they worried that lower prices would negatively affect perceptions of quality by consumers, diminish the value of branded goods, and in turn, ultimately reduce sales. Small independent retailers supported retail price maintenance agreements because such agreements established floor prices that attenuated the bulk-purchasing advantage of large chains.

Congress passed the Miller-Tydings bill on August 17, 1937. The bill was designed to overrule the 1911 U.S. Supreme Court ruling in the Dr. Miles case (*Dr. Miles v. John D. Park & Sons*, 220 U.S. 373), in which the Court held that certain vertical resale price agreements substantially lessened competition as effectively as any horizontal agreement and were in violation of the Sherman Act. Subsequently, by June 30, 1938, resale price maintenance laws had been enacted in every state except Texas, Missouri, Vermont, Delaware, and Alabama.

A 1951 Supreme Court ruling (*Schwegmann Bros. v. Calvert Distillers*, 341 U.S. 384) invalidated nonsigner clauses to fair trade laws. Nonsigner clauses had allowed distributors to take action against parties with whom they had no contractual arrangements that limited fair trade laws. That Supreme Court ruling along with subsequent legislative lobbying efforts by various chain businesses led to the federal repeal of the Miller-Tydings Act of 1937 on January 1, 1976.

—Frank L. Winfrey

See also Capitalism; Just Price; Managed Competition; Perfect Markets and Market Imperfections; Predatory Pricing and Trading; Price-Fixing; Restraint of Trade; Unfair Competition

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Minimum Wage

The minimum wage refers to the lowest wage an employer can legally pay an employee. It is intended to protect the most vulnerable employees from excessive wage exploitation by establishing a wage higher than what the market would otherwise establish. The minimum wage arguably represents the amount of income needed by a full-time employee to maintain a minimally acceptable standard of living.

Some nations establish minimum wage laws for an entire country (Cuba, France, Russia, United Kingdom, United States), while others do so regionally (Canada) or based on industry collective bargaining agreements (Germany, Italy, Sweden). Many countries, including China and India, do not have a minimum wage law.

In these nations, the lowest wage is a function of either the laws of supply and demand or business interests.

Arguments Against the Minimum Wage

Economists are divided on the impact of a minimum wage on labor markets and the economy. Neoclassical economists oppose establishing minimum wage rates and, by extension, any increases to them. They report that artificially raising wages above the law of supply and demand hurts those it is intended to benefit by increasing unemployment, contributing to inflation, and discouraging business investment and growth. The extra labor costs force employers to hire fewer low-skilled employees and/or increase their prices. Some employers offset minimum wage increases by reducing other employee benefits. Minimum wage increases attract middle-class teenagers into the labor market, which creates more competition for low-skilled adults seeking employment.

In response, economists supportive of minimum wage increases report that higher hourly wages have little or no effect on unemployment rates and actually stimulate economic growth by increasing the purchasing power of low-income employees. At the same time, recipients of higher minimum wages reduce their dependence on financial assistance from the government.

Early History of the Minimum Wage

For most of recorded history, minimum wage laws did not exist. In *Wealth of Nations*, published in 1776, the Scottish philosopher and economist Adam Smith observed that employers naturally formed coalitions among themselves to offer low wages. Given the overabundance of low-skilled laborers, they possessed a superior bargaining position. Some employers paid below subsistence wages, an income level insufficient for an employee to purchase food and shelter. In 1845, Irish peasants working full time died of starvation because they did not earn enough money to purchase home-grown oats and grains stored on nearby British ships.

During the late 1800s, the idea of establishing a minimum living wage gained a wide spectrum of support among labor unions, socialists, and leaders of both the Catholic and Protestant social movements. Pope Leo XIII, in his 1891 encyclical *Rerum Novarum* ("On Capital and Labor"), tempered the right of capitalists to own private property with the sentiment that laborers who did not receive an income high enough to escape from poverty were victims of fraud and injustice.

The first minimum wage legislation was passed in New Zealand in 1894, followed by Australia 2 years later, and Great Britain in 1909. All three governments created wage boards to determine the minimum allowable wage in certain extremely low-paying industries.

United States' Legislative History

In the United States, early legislative efforts were aimed at providing minimum wages for women and children. In 1912, the Massachusetts legislature formed a council that requested voluntary compliance to minimum wage rates for women and children employed in certain industries. The following year, seven states enacted stronger minimum wage laws. But in 1923, national progress came to a halt when the U.S. Supreme Court ruled that state-imposed minimum wage laws violated the constitutional right of employers and employees to freely enter into contracts, including wage agreements.

In response to high levels of unemployment and poverty caused by the Great Depression, President Franklin Roosevelt created the National Industrial Recovery Act (NIRA) of 1933 to stimulate business activity. The NIRA encouraged companies to create industrywide codes of fair competition, which included agreements on appropriate prices and wages. The legislation also recommended that consumers purchase products only from businesses that paid their employees at least $12 a week for 35 hours of work. The Supreme Court ruled certain NIRA provisions unconstitutional, but quickly reversed itself in a subsequent ruling after considerable public pressure—including threats from President Roosevelt to restructure the Supreme Court itself.

The Roosevelt Administration issued the Fair Labor Standards Act of 1938, which federally regulated the length of the workweek, overtime rates, child labor, and minimum wages. One of the legislation's guiding principles was a fair day's pay for a fair day's work. The initial legislation proposed that several transportation and agriculture industries pay a minimum of 40 cents per hour. Republicans and Southern Democrats objected to the minimum wage provision until the amount was reduced to 25 cents an hour, or $11 a week. The federal minimum wage has since been extended to additional industries, including public schools, nursing homes, farms, domestic workers, and small retail businesses. Congress did not index the minimum wage to inflation or a poverty threshold and increases it periodically in response to political pressure.

Minimum Wage Features in the United States

In the United States, both states and the federal government have the constitutional right to create a minimum wage. An employee is entitled to whichever is higher. In 2005, the federal minimum wage was $5.15 an hour. Fifteen states had minimum wage rates higher than the federal amount. The state of Washington, which annually indexes its minimum wage to inflation, had the highest amount at $7.35 an hour in 2005.

Some employees are not entitled to the minimum wage. Those exempted from the federal minimum wage include workers with disabilities, full-time students, youth less than 20 years of age for the first 90 consecutive calendar days of employment, tipped employees, and student-learners. For instance, tipped employees can be paid as low as $2.13 an hour if the inclusion of tips at least equals the $5.15 hourly minimum wage rate. If not, then the minimum wage for tipped employees must be proportionately higher.

Approximately 10 million American wage earners—7% of the labor force—are paid a minimum wage. Two thirds of the minimum wage earners are adults, the remainder teenagers. Thirty-three percent are parents with children less than the age of 18. Approximately half work full-time. Fifty-eight percent are women, and 40% have less than a high school diploma.

Recent History of the Minimum Wage

During the 1960s, the federal government's "War on Poverty" established public assistance programs, such as welfare, for all adults living in poverty. In the process, the federal government de-emphasized the minimum wage as the primary means for ensuring that the working poor earned a subsistence income. The minimum wage was increased to $5.15 an hour in 1997 and has remained at that level. In 2005, congressional legislation proposing to gradually increase the minimum wage to $7 an hour failed to gain the necessary political support for passage. If the 1968 minimum wage of $1.60 an hour had been indexed to inflation, the current hourly rate would be $8.88.

Approximately 30 million Americans working full time earn an hourly wage below the poverty threshold. In 2005, the federal poverty threshold for a single parent with two children was $16,090. Annual earnings for a full-time employee paid a minimum hourly wage of $5.15 was only $10,712, insufficient to cover living expenses such as housing, food, health care, child care, and transportation. If the minimum wage was indexed to the federal poverty threshold it would be $7.74 an hour. Some local municipalities have approved a variety of "living wage" ordinances that enable the full-time working poor to earn enough income to maintain a minimally acceptable standard of living.

—Denis Collins

See also Capitalism; Exploitation; Great Depression; Just Wage; Living Wage; Poverty

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Minorities

Minorities can be defined depending on specific context, but generally minorities make up either a subgroup that does not form a majority of the total population, or a group that, while not necessarily a numerical minority, is disadvantaged or otherwise has less political or economic power than a dominant group. The most prevalent form of minority groups, that is, ethnic minorities, comprised less than 20% of the United States in 1980, and yet the projections are that by 2040, half of all Americans will be those now referred to as "minorities."

Minorities can also be classified by gender, disability, age, religion, sexual orientation, and other criteria. Although the ratio of men to women is balanced in most societies, given the lower economic status and lack of opportunities of the latter group has led some to equate them with minorities. Similarly, the elderly, while considered an influential group in many traditional societies, have been reduced to a minority role in terms of their economic and social contributions. Finally, the Disability rights movement has contributed to an understanding of people with disabilities as a minority group.

Minorities in the Workplace

Companies and governments are aggressively pursuing a strategy to ensure that minority groups do not continue to face unfair barriers to achievement in the workplace, in the labor market, and in education. Supportive diversity climates are maintained by providing realistic job previews and healthy work environments. Affirmative action, the idea that minorities should be given special privileges to facilitate equal access, is however a controversial issue. While proponents argue that a diversified environment is a desired positive outcome, critics argue that such actions result in reverse discrimination and a sense of victimization of the majority.

Marketing to Ethnic Minorities

In an increasingly global world, businesses are recognizing the need to reach out to minority groups. Companies such as AT&T, Sears Roebuck, and Coca Cola were some of the pioneers of such practices. The three major ethnic minority groups in the United States—Hispanics, African Americans, and Asians—currently account for almost 30% of the population, and they cumulatively account for 20% of the total spending power in the country. In 2004, corporate America did not effectively market to this segment of the market, since only 2% of the more than $200 billion spent on advertising was allocated to the ethnic media. In a study sponsored by the Association of National Advertisers (ANA) in 2004, an overwhelming 89% of the advertisers said that they were practicing multicultural marketing while 85% were involved in specifically creating separate ads for separate ethnic markets. The greatest challenge faced by the agencies cited in the study was the measurement of results (38%), funding (34%), and a lack of market research (13%).

The 2005 Yankelovich *MONITOR* Multicultural study found that 70% of blacks and 53% of Hispanics are very concerned about marketers' methods and motives. Furthermore, 50% concur that most marketing has no relevance for them and that they wanted marketers to be more attentive, in a sensitive and culturally appropriate manner. The results also suggested that for Hispanic consumers, marketers should use both Spanish and English to facilitate the infusion of the brand message with cultural familiarity and relevance. In many countries, companies such as L'Oreal, Alberto-Culver, and Proctor and Gamble–owned Wella have introduced several ethnic minority–specific products in categories such as cosmetics and hair care.

Drawing a Fine Line Between Patronizing and Targeting

While targeting minorities is encouraged to enable them as consumers to have greater access to products available to mainstream customers and to offer greater efficiencies to marketers, doing so has a sinister connotation, when minorities are perceived as "vulnerable." This has even a worse connotation if the products that are being targeted are potentially harmful. For example, many consumer activists and federal officials took action in the last decade when internal documents from R. J. Reynolds and Brown & Williamson Tobacco Corporation showed how these companies had targeted minority youths, particularly with their menthol brands. Similarly, C. Heilman Brewing drew fire when it extended its Colt 45 malt liquor line with Power master, a high-test malt, toward African American consumers. In other cases, politically incorrect marketing strategies have come under scrutiny, for example, when a high alcohol content malt liquor, "Crazy Horse," named after a famous Sioux Indian warrior, was marketed to Native Americans in the early 1990s.

On the contrary, avoiding minority groups, also known as "redlining," by denying bank loans and insurance policies primarily to minority households has also come under a lot of criticism. Retail redlining, when major firms do not serve customers in minority neighborhoods, because of unprofitable operations, has also been severely criticized by federal agencies and activist groups. Related research, as well as television newsmagazines such as *Dateline* and *20/20,* has shown that African Americans wait longer for customer service in the retail industry than customers of other races. Balancing the demands of hiring and treating minorities fairly, marketing customized products without patronizing or exploiting vulnerabilities, and providing attentive customer service are some of the major challenges that firms face today with regard to their minority stakeholders.

—Abhijit Roy

See also Advertising Ethics; Affirmative Action; Cross-Cultural Consumer Marketing; Diversity in the Workplace; Employment Discrimination; Gay Rights; Minority Shareholders; Racial Discrimination; Women in the Workplace

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Minority Shareholders

Minority shareholders are shareholders of a corporation who own less than 50% of the voting rights and who individually are unable to control the corporation. Minority shareholder status is related to the proportion of voting power held by a shareholder, not by the proportion of shares held: Some share classes may have no or limited or multiple voting rights.

The key ethical issue is that, because they are in the minority, they have an ineffective voice in corporate governance and those in the majority may operate the firm for the majority's advantage and to the unfair detriment of the minority. This acts as a disincentive for small shareholders to invest in equity markets. Minority shareholders themselves may also act unethically by acting as free riders—that is, they rely on majority shareholders to invest resources in monitoring management and benefit from that monitoring without making a proportionally similar investment.

The Organisation for Economic Co-operation and Development (OECD) Principles of Corporate Governance makes it clear that protection of minority shareholders from abuse is part of good corporate governance. Examples of abuse include transfer of value to companies owned by controlling shareholders through asset sales or unusually favorable supplier or customer contracts; new stock issues, especially of nonstandard share classes (shares with voting rights only are useless to minority shareholders); and for nonlisted companies, placing restrictions on the sale of shares, which prevents minority shareholders from liquidating their holdings. Minority shareholders who seek income from their investment may be harmed by the refusal of the majority to pay dividends.

Minority shareholder rights may be protected either *ex-ante* (prevention) or *ex-post* (cure or compensation). *Ex-ante* protections may be found in the legislative and regulatory framework for minority shareholder protection, a corporation's constitution, and stock exchange listing rules. Examples include whether shareholders can force the convening of a General Meeting, and, if so, whether this requires the signatures of a minimum number of shareholders, or shareholders with a minimum proportion of voting rights; whether proxy voting is permitted or personal attendance at General Meetings is required; whether a supermajority is required for specified resolutions; and whether controlling shareholders are required to buyout minority shareholders at an independently determined price in the event of delisting. *Ex-post* protection is provided mainly through the court system, either by means of court orders preventing certain actions or by means of tort action for compensation for wrongful harms; in extreme cases, a court may dissolve the corporation. The extent to which this is effective is related to whether regulatory bodies have sufficient resources to monitor and take action and whether litigants have ready and affordable access to corruption-free courts.

Minority shareholders are in a particularly vulnerable position in developing countries, where the agency problem (which results from the separation of ownership and control) has materialized as one between majority and minority shareholders rather than one between owners and managers. This often results from either a prevalence of family-owned businesses, typical in Asia, or foreign companies setting up majority-owned subsidiaries to meet government requirements. The outcome is poorly developed equity markets in many countries, including many in sub-Saharan Africa, which negatively affects the country's economy as a whole. Because the United States has a low ownership concentration and high *ex-post* protection compared with other countries, such issues have far less impact there; nevertheless, they remain a significant issue for some family-controlled businesses.

—Royston Gustavson

See also Agency, Theory of; Shareholder Activism; Shareholder Model of Corporate Governance; Shareholders; Shareholder Wealth Maximization

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Missions and Mission Statements

A mission guides a person or an organization in the direction that it wishes to proceed. A personal mission statement can help focus one's goals and life. A mission is generally best articulated in a formal, written mission statement. An organization's mission statement is designed as a broadly phrased statement of the firm's long-term goals; it distinguishes the firm from others in its industry and specifies the scope of the operations in terms of the firm's product or market. It spells out goals, is a statement of aspirations, and focuses one's actions. The mission expresses the vision of the firm's founders or strategic planners and also communicates the image that they seek to project. It often also indicates the principal customer or client needs that the firm will satisfy. Thus, the mission statement describes the firm's products, services, market, customers needs, and technology such that it also reflects the values and goals of the top managers, and ideally all the members of the firm. The mission statement defines the firm's overall plan in a succinct and engaging manner and with a tone that reflects the climate of the business itself.

A mission statement seeks to answer the following questions: What is the problem or the need that the organization is trying to address? What makes this organization unique? Who benefits from the work of the organization? Why does this organization exist? What customer or client needs do we fulfill? What sets our organization apart from our competitors? A mission statement should be brief, clear, and concise; it should be short enough that it can be easily remembered by the people in the organization. A mission statement should also be inspiring, free of jargon, and achievable. Members of the organization must be able to support the mission.

Through the mission statement, the managers and associates in the firm attempt to clearly articulate their long-term goals and what makes their organization special and worthy of people's attention. A mission statement thus expresses the values of the members of the organization. A mission statement focuses the efforts of all in the organization so that all are more likely to be "on the same page"; this better enables the firm to survive and to achieve long-term profitability and growth. This statement can then serve as a basis for shared expectations, long-range planning, deciding priorities, and performance evaluations.

A mission statement that is developed systematically and is comprehensive is an invaluable tool in directing and implementing policy. A mission statement thus serves as a guide to top managers when they make strategic decisions on the deployment of the organization's resources. Without it a manager may make decisions on the basis of one's biases and concern for "turf." A clearly stated mission statement enables a manager to focus on the long-range goals of the organization as a whole and not on the manager's particular priorities or preferences. Such a mission statement also provides a sense of shared expectations for people in the organization. It is important to give such guidance today, given global operations and people working in different countries and cultures. Thus, the mission statement specifies values and goals and provides a unity of direction that is intended to include many nations, peoples, and generations.

From outside the organization, one can view a mission statement as an instrument for learning about the goals of the organization, as well as its likely planning strategies. For a potential employee or customer, a mission statement may be a principal reason why one might seek or reject joining the firm as an employee or purchasing the firm's product or service. Thus, a mission statement communicates a description of the firm to prospective employees, customers, and other stakeholders, so that they may decide if they want to be involved with the firm.

Without a mission, a person or an organization risks wasting valuable time and resources by engaging in activities that do not contribute to attaining their goals. Indeed failing organizations often waste much of their time and effort on actions that have little long-term benefit for the organization. Once an organization grows beyond the few people who can have daily face-to-face contact, it becomes important to specify and write out the firm's mission and code of conduct.

Developing a mission statement for an organization forces the founders, top managers, and board of directors to articulate the goals of the firm in a clear, cohesive way. In a process that acknowledges the contribution of all people in the organization, these goals are then commented on by associates in the firm and are ultimately made clearer, more accurate, and more complete by an interactive process. Individuals in the organization also achieve a heightened sense of purpose when they reflect on and internalize the goals of the organization. The mission statement can be amplified by following it with important, more specific goals and objectives of the organization. Thus, the mission statement itself can be kept relatively brief—ideally, a few sentences that can be remembered—but additional important items can also be included.

More than 90% of large firms possess a mission statement and a code of business conduct. Formulating a mission statement can be a valuable experience for the members of the group that is seeking to clarify their goals, although it is not always easy. The completed mission statement might seem to be deceptively simple, since a mission statement can be as brief as a sentence or two. But to distill the meaning of the organization or the group into those concise, meaningful sentences requires discipline, insight, patience, and cooperation.

To develop a mission statement, leaders of the group often ask such questions: Who are we? What do we do? Why do we do it? What should we be doing? What do we stand for? Then someone takes the key points and attempts to draft a mission statement. The draft is sent back to the group for their comment in order to clarify the statement. It may then go through several rounds of revisions. Moreover, organizations generally update their mission statements periodically with a similar iterative process.

The process of coming to a consensus on the mission statement is generally a learning experience for the group. Some firms begin the drafting process during a retreat of the board. This is appropriate for a board, since the broad goals of the organization are a major responsibility of the board. But a group cannot efficiently write a mission statement together; quibbling over words can waste much time. The process will proceed better by circulating a draft written by one person, perhaps the founder, or a top manager who took notes during an initial group session. For the mission to be successful and for everyone in the organization to own that mission, it is essential that each person have some opportunity to participate in formulation. Conducting workshops, whereby all in the organization are able to comment on the mission, helps focus workers' efforts, gain cooperation, and build morale among the group.

There is not a clear distinction between a mission statement and a vision statement. A mission statement relates an organization's purpose, while some describe a vision statement as a "vision of the future." One attempt to distinguish is to call the vision the destination and the mission the journey.

Often a mission statement precedes a firm's ethics statement and sometimes the terms *mission statement, ethics statement*, and *code* are used interchangeably. Some firms, such as Johnson and Johnson (J&J), call their mission statement a Credo. J&J's Credo was the foundation that enabled top management to effectively deal with the tragedy of the poisoning of Tylenol pills. By the CEO James Burke's own account, he acted on J&J's Credo, which stated that their first responsibility was to the doctors, nurses, and patients, all those who used their products. They were open about the problem and mounted a costly and successful recall of all products. As a result, the firm and the product survived and prospered.

Some firms have set out their basic principles in a values statement, which sets forth the basic values on which the firm is based. The values statement often follows a firm's mission statement, and these values often make reference to the founder(s) actions and guiding principles that have made the firm a success.

A mission statement should be more than just a document posted on the wall or placed in orientation literature; it should be a living document that influences people in the organization in all their major decisions. As a living document, it should be revised and updated regularly. To demonstrate that the mission is not mere public relations, stories of how the mission has been achieved can be included as supplements.

Firms that have a clear and strong mission statement tend to outperform their competitors in the marketplace, according to empirical studies. Among those firms identified as strong on their mission are 3M, American Express, General Electric, IBM, J&J, Ford, Marriott, Nordstrom, Procter & Gamble, and Sony. Each of these firms has a clear mission statement. Each also is outstanding in its industry, is widely admired by businesspeople, has made an indelible imprint on the marketplace and the world, and was founded before 1950. Moreover, each of the firms that have a well-articulated mission tends to be more thorough in their orientation and various methods of communicating their vision and mission. Firms with a strong mission more carefully nurture and select senior managers and more often select their chief executives from within the firm.

Mission statements often stress the superior quality of the product or service offered. Mission statements also generally include elements such as the importance of integrity, respect for the individual worker, service to the customer, and responsibility to the community. It is important that the mission provide a foundation for the existing and desired ideology and that the members of the firm have integrity in acting out that mission. However, each mission is unique and thus reflects the industry, market, and values of the people within the firm.

In many cases, firms do not live up to their own stated mission. Mission statements are sometimes platitudes and public relations gestures, that is, statements that are designed to make the firm look reputable and responsible to its outside constituencies. If a mission is too general, it is ineffective because it does not describe the particular firm. Mission statements are sometimes too ideal; that is, since they are aspirational, they are not realistic. However, mission statements are statements of ambition, so it is not surprising if those aspirations are not always perfectly achieved.

Collections of some of the best business mission statements have been gathered and analyzed. These researchers have also provided some background on the individual firms and how those mission statements were developed. Organizations that are presented include AES, Bayer, Cadbury Schwepps, Caterpiller, Comerica, Cummins Engine, Donnelly, Ford, General Motors, Herman Miller, Hershey, Hewlett Packard, Hong Kong Ethics Development Center, Hyatt, J&J, Kroger, Levi Strauss, Marriott, Procter & Gamble, Sears, Starbucks, TRW, UNUM, and Whirlpool.

Nonprofit organizations (NGOs) are less likely to develop a mission statement, partially because members feel that their mission is already clear to stakeholders. In addition, funding agencies generally do not contribute to the general purpose of an NGO, but to specific projects, so there is less incentive to spend the time and energy to develop a mission statement. Moreover, a mission may seem to limit an NGO if a new project and funding is available. Nevertheless, the same rationale for a mission statement is true for

NGOs: to provide direction, coherence, and a goal by which to judge individual and organizational achievement and success. Moreover, since NGOs do not enjoy the automatic feedback of profit and loss, it is even more important to fashion a mission statement and to set goals.

—Gerald F. Cavanagh

See also Caux Principles; Codes of Conduct, Ethical and Professional; Global Codes of Conduct; Global Reporting Initiative; Social Accountability (SA); Strategic Planning; Transparency International; United Nations Global Compact

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Mixed Economy

A mixed economy is typically a market system of resource allocation, commerce, and trade in which the government intervenes to disrupt the "invisible hand" of free market forces. Examples of such intervention may include state-owned enterprises (such as public health or education systems), regulations, subsidies, tariffs, and tax policies. Alternatively, a mixed economy may emerge when a socialist government makes exceptions to the rule of state ownership to capture economic benefits from private ownership and free market incentives. In addition to a variety of forms, mixed economies have come about from a variety of motives and historical causes.

The British Corn Laws of the early 1800s, for example, were government interventions in the free market to protect native agricultural interests by limiting imports. The negative consequences of foreign protectionist responses and higher food and labor costs at home led to an invigorated laissez-faire and free trade movement. However, at roughly the same time, abuses of factory workers led to government intervention to reform child and female labor conditions.

In developed Western economies after the Industrial Revolution and before the Great Depression of 1929–1933, most political economists and governments believed that social prosperity progressed best in economic systems composed of free markets whose social and monetary order was protected by the actions of governmental and banking institutions. This belief was profoundly shaken by the system's twin catastrophic failures that we call the Great Depression—failing first to prevent the global economic collapse and then failing to recover communities from the horrendous human tragedies of unemployment and poverty wrought by the collapse. The New Deal, a series of interventionist legislation and government programs in the United States, was championed by President Franklin Delano Roosevelt to head off social unrest caused by the widespread unemployment of the Great Depression in the 1930s.

In the mid-20th century, many people agreed that the Great Depression arose from fundamental flaws in the free market theory of equilibrating supply and demand, and that this meant that the free market alone would be incapable of recovering from the Great Depression. In developed Western economies, the historical development of the mixed economy is the evolutionary change of the free market concept as it adapted to avoid the risks of widespread social unrest and potential revolutionary socialist or Marxist change. Social democratic programs that arose in continental Europe at this time created coalitions of business interests with major social groups to improve social welfare without jettisoning private property and the market economy. This mixed economic approach included economic planning, high tariffs, guarantees of group rights, and social welfare programs.

Mixed economies also arose in many countries that formerly had centrally planned and socialist economies. The mixed economies in modern China and Russia, for example, evolved from communist systems that were too inefficient to compete in the modern global economy. The recent social experience of the Chinese and Russian people is a profound testament to the personal difficulties and turmoil that people endure when a country makes a transition to a mixed economy.

As the historical examples above suggest, mixed economies have public, private, legislative, judicial, and regulatory components, but there is not a single ideal, standard, or typical set of economic features, and the mix may vary from country to country. Components in the mix may include government subsidies, fees, taxes, set-aside programs and regulations, state-owned enterprises, mandatory social security, or national health programs.

Common to all mixed economies is their combination of some free market principles of private contracting with some socialist principles of state ownership or planning, and some government-controlled economic incentives and disincentives that intervene with purely market-generated costs and benefits in individual calculations of rational utility.

Many economists and political philosophers have argued in favor of government action to enforce the ordinary rules of law in economic matters. For example, Adam Smith, and later Friedrich Hayek, noted the important role of government in assisting the functioning of markets by preventing violence and fraud, protecting property and public safety, enforcing contracts, and providing public infrastructure and utilities that would otherwise be unprofitable. In a mixed economy, however, there is a presumption that government must go beyond this limited role to improve distributive justice in society. Adam Smith wrote that intervention violated the ethical principle that indicates that economic efficiency is the best long-term path to social progress. Hayek also objected to such government intervention because he believed it to be economically inefficient, but even more important in his view is the inevitable tendency for the mixed economy to be politically abusive of individual liberty. Despite these philosophical and moral objections, almost all modern economic systems in the world today are mixed economies. While the modern global economy limits government intervention in free trade, it retains mechanisms for social welfare exceptions to the free market rule. At times, politicians have attempted to invoke such exceptions for reasons of parochial interest or political expediency.

Public policy making in mixed economies frequently must balance the concern for individual liberty with the need for a fair, equitable, and just society. Balancing these concerns with integrity and procedural justice requires the participation of diverse social segments as stakeholders in an ongoing and dynamic search for a fair and appropriate separation between utilitarianism and the tyranny of the majority. This is an extremely difficult public policy task that is made more challenging because the preferences of each social segment are based on individual and subjective definitions of utility that are often not easy to calculate, communicate, or compare across groups. For this reason, the success of the mixed economy depends on the integrity of governmental and social support for ethical principles of compassion, empathy, and respect for individual and minority rights. Without such support, the mixed economy can become a system of coercive government manipulated by powerful stakeholders.

—Greg Young

See also Cost-Benefit Analysis; Economic Incentives; Free Market; Great Depression; Hayek, Friedrich A.; Invisible Hand; Laissez-Faire; Marxism; Rational Choice Theory; Regulation and Regulatory Agencies; Resource Allocation; Smith, Adam; Socialism; Stakeholder Economy; Utilitarianism; Utility, Principle of

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Monetary Policy

Monetary policy is the control that a country's central bank or government exercises over the money supply and credit or, alternatively, over a short-term interest rate. Along with fiscal policy, it is the most important policy for achieving macroeconomic stability. Stability is usually taken to mean low and stable inflation, real interest rates compatible with reasonable levels of saving and investment, sufficient financing of economic activity, and a stable and competitive exchange rate.

Implementing monetary policy is the job of the central bank (such as the Federal Reserve in the United States, the European Central Bank in the euro zone, the Bank of England, and the Bank of Japan): a public financial institution that specializes in controlling the money supply, credit, and interest rates. Ultimate responsibility for deciding monetary policy objectives and strategy used to belong to government, although nowadays there is a broad consensus that it is better assigned to a central bank that is independent of the executive (the central banks mentioned above, and many others, are independent).

The goals of monetary policy may vary widely, but there is a broad consensus that its main objective should be to achieve and maintain a low, stable, and predictable rate of inflation for a sufficiently extended period. In many cases, there is a second objective: to maintain the real gross domestic product growth at a rate close to its potential rate or employment at a level close to full employment. The European Central Bank, for example, pursues only the first of those two goals, whereas the U.S. Federal Reserve System pursues both at once. The debate about which of the two strategies is preferable remains open, and the solution is likely to depend on each country's economic, social, historical, and institutional circumstances. In either case, monetary policy is a means for government to intervene in the economic system to enable its smooth functioning.

Important ethical issues for monetary policy relate to the short-term trade-off between employment and inflation. A decision to reduce inflation can result in higher unemployment. Many argue that this shifts burdens unfairly to the poor. In contrast, a loose monetary policy designed to stimulate employment may adversely affect those on fixed incomes, such as retirees. Thus, monetary policy has implications for social justice and welfare. Consequentialist ethical approaches are useful to understand and balance these implications. Distributive justice is a consequentialist approach that focuses attention on the fairness with which the impacts of monetary policy are distributed throughout the society. Utilitarian approaches focus on the amount of net benefit that monetary policy creates.

How Monetary Policy Works

A country's central bank is the provider of the most liquid of financial assets (the ones that can be converted into money most easily, at no cost), namely, cash (coin and notes in circulation) and the assets that banks use to meet their liabilities to the central bank and conduct transactions with one another (the so-called bank reserves, which tend to be mainly deposits held at the central bank). When the monetary authority creates those liquid assets and makes them available to banks, it is in effect encouraging them to extend more credit and thus is stimulating the growth of demand and prices: Monetary policy, in this case, is expansionary. Conversely, when the central bank withdraws liquidity, monetary policy is contractionary.

The central bank has at its disposal certain instruments for creating (and withdrawing) liquidity. The Federal Reserve, for example, conducts daily open market operations, which consist of buying (selling) public debt to the banks, which has the effect of increasing (decreasing) the liquidity available to them. The European Central Bank, meanwhile, grants loans to banks for weekly periods.

The monetary authorities also have other instruments at their disposal, such as the discount window in the United States (a way for banks to obtain additional liquidity when they need it), required reserves (whereby banks are forced to hold a certain proportion of their liabilities in the form of deposits at the central bank), or foreign market interventions (buying or selling foreign exchange, thus increasing or reducing the amount of liquidity in the economy).

What the monetary authority actually does, therefore, is modify the composition of banks' portfolios by changing a very short-term interest rate (such as the federal funds rate in the United States, or the refinancing rate in the euro zone). Banks react to that increase (reduction) of liquidity by extending more (less) credit to their customers, while lowering (raising) the interest rate on those loans. In doing so, they change the saving, consumption, investment, and borrowing decisions of households and companies: A drop in interest rates will encourage them to spend and borrow more, while the opposite will occur if interest rates increase. Ultimately, monetary policy will end up affecting the level of demand, production, and employment, as well as the price level. Eventually, through the inflows and outflows of capital, monetary policy also affects exchange rates and the country's balance of payments.

Monetary policy is not always an effective mechanism to change demand and production. The central bank may increase the liquidity available to financial institutions, but then find that the banks are unwilling to lend more to their customers, or that the banks' customers do not want to borrow more. As John Maynard Keynes put it, "You can lead a horse to water but you can't make him drink." In any case, for monetary policy to be effective banks should comply with, rather than evade, its restrictions.

Monetary policy may be used to achieve moderate and stable growth in prices, and over the long term it tends to be effective in controlling inflation. While the prices of goods and services may rise or fall for all sorts of reasons in the short term, over a longer period of time inflation is always a monetary phenomenon in the sense that prices can only increase overall if there is an increase in the money supply.

Design and Implementation of Monetary Policy

Monetary policy is a powerful instrument to influence demand, production, and employment. It also can have undesirable effects, including higher inflation, a bigger current account deficit, or financial instability. Like the Hippocratic Oath in medicine, monetary policy should not cause harm.

There is a passive and an active way of using monetary policy. Passive use of monetary policy is aimed at creating favorable conditions for the economy: sufficient growth in the money supply to finance the level of economic activity, without creating excess liquidity that might fuel inflation, while keeping interest rates stable and not too high and exchange rates competitive and likewise stable.

Some economists and politicians think that focusing monetary policy on a goal of low and stable inflation is damaging for the poor if it is likely to mean higher interest rates and lower job creation. Nevertheless, there is a broad consensus that there is not a long-term trade-off between an inflationary monetary policy and the permanent growth of gross domestic product and employment; and potential short-term trade-offs will be transitory. An approach to manage monetary policy that achieves a low and stable inflation rate complements the effectiveness of other policies to grow production and employment that over the long term are likely to improve public welfare and reduce poverty.

An active monetary policy intends to correct economic imbalances, such as high inflation, a serious current account deficit, a sudden capital flight, or a recession. In a country that has experienced rising prices for a long period, the monetary authorities may want to lower inflation expectations as quickly as possible. This risks a major impact on the value of assets and debts, and thus on the distribution of wealth and income. Monetary policies, therefore, must balance activism with fairness.

Monetary policy may be thought of as impersonal because it affects large sectors of society such as banks, companies, and households rather than specific agents. If the impact of monetary policy on a certain sector of society needs to be corrected, or if redistributive effects are intended, it is more efficient to use another mechanism, such as fiscal policy, that more directly allocates government financial resources and taxes.

Monetary policy acts through the financial markets by changing the expectations and decisions of the economic agents and influencing the value of their assets and liabilities. In recent years, monetary policy measures have tended to be announced in advance, so that the agents can anticipate the impending changes and adapt to them. It is desirable, therefore, that the central banks have a transparent communication policy.

The monetary policy of central banks needs to be credible and to inspire confidence even in politically volatile situations. There are several means to achieve this. One approach is to make the central bank an independent body whose mission is prescribed by a law or constitution that government cannot easily change. Another approach is to appoint central bank governors and boards, the monetary policy decision makers, for long terms of office that buffer them from political pressures. In these ways, monetary policy is more likely to be managed with integrity and to earn a reputation for responsible service to the public welfare.

—Antonio Argandoña

See also Accountability; Consequentialist Ethical Systems; Economic Growth; Federal Reserve System; Gross Domestic Product (GDP); Gross National Product (GNP); Inflation; Justice, Distributive; Poverty; Trust; Unemployment; Utilitarianism

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MONKEYWRENCHING

Monkeywrenching denotes nonviolent disobedience and sabotage carried out by environmental activists against those they perceive to be ecological exploiters. The term was made popular through its use by Edward Abbey in the novel *The Monkey Wrench Gang* of 1975, and has, since about 2000, very occasionally been used to indicate other forms of anticapitalist global activism, including culture jamming (see *Notes From Nowhere*). An equivalent term is *ecotage* and a contrasting term is *ecoterrorism.* The latter term is often a misnomer, properly applicable to rogue examples or individuals because monkeywrenching is typically motivated by a regard for preservation of life and is ordinarily restricted to two forms: either to nonviolent disobedience or to sabotage that does not directly endanger others.

Familiar civil disobedience scenarios include activists in vessels who place themselves between harpoon and whale or who chain themselves to earthmoving equipment, thus placing themselves at risk of injury if work activity should continue. Julia Butterfly Hill's tree-sitting effort is the most famous case. Hill remained for 738 days without pause in one prominent redwood tree in northern California beginning in December 1997. In collaboration with the protest organization Earth First!, Hill successfully secured the tree against logging by the Pacific Lumber Company until the parties reached a long-term preservation agreement.

The second approach for monkeywrenching involves destruction of unattended property by guerilla methods. Scuttling whaling vessels, cutting fishing nets, and contaminating the fuel of unattended earthmoving equipment are familiar examples. No annual value for damages can reasonably be estimated. Recent actions have greatly extended the category of environmental exploiter and the variety of targets. In August 2003, a San Diego condominium construction site was burned (damage valued at $20 million), and more than 100 energy-inefficient passenger automobiles were set ablaze at four Los Angeles dealerships in one night ($2 million). Arsonists left messages indicating alliance with the California-based Earth Liberation Front. The closely associated Animal Liberation Front engages in related actions against exploiters of animals; the independent Sea Shepherd Society focuses on the marine habitat.

Monkeywrenching broaches terrorism, as opposed to nuisance and economic harm, in some instances. A clear example is tree spiking, in which metal or ceramic spikes are driven deep within trees for the purpose of damaging chainsaws or blades at sawmills. Spiking has been credited with halting or delaying some U.S. Forest Service logging contracts, and with the serious injury of at least one sawmill worker. It has also been tried as a legal option for deterring illegal deforestation in Indonesia. Following a spiking, spikers usually mark trees or anonymously alert companies and government agencies of their activities. But markings on trees, along with the knowledge that a stand has been spiked, may be lost over the very many years that a forest stands. Consequently, any spiking is likely to pose significant irremediable long-term danger.

Monkeywrenchers have themselves suffered illegal sabotage and death. The most famous case is the 1985 bombing of the Greenpeace ship *Rainbow Warrior* in Auckland Harbor by members of the French Secret Service.

—Eric Palmer

See also Bureau of Land Management; Consumer Activism; Deep Ecology; Environmental Colonialism; Environmentalism; Global Business Environments; Natural Assets (Nonuse Values)

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MONOPOLIES, DUOPOLIES, AND OLIGOPOLIES

Monopolies, duopolies, and oligopolies all represent market structures that deviate from perfect competition and in which production decisions by any single firm directly affect the sales or selling price of other firms. In these types of markets, the limited number of sellers that exist maintain some control over the price of the goods or services sold, and these goods or services are either unique or significantly differentiated from other potential competitors in the market. As with all market structures that deviate from perfectly competitive markets, firms in these markets will tend to restrict output in their efforts to increase prices above marginal cost and thereby reduce the efficiency of the marketplace. The loss in efficiency in the markets is associated with a misallocation of society's resources and a deadweight economic loss.

Under monopoly, a single firm produces the entire market supply of a good or service. The effective market for a monopoly can either be localized or considerably broader. A number of factors can result in the barriers to entry that allow a single producer of a good or service to exist over time. Exclusive patents or licenses, the existence of large economies of scale, large start-up costs, and ownership of essential resources can all result in the establishment and maintenance of monopoly power in a market. Often these barriers to entry are classified as natural or artificial. Natural barriers to entry occur when technology or other cost structures make the minimum efficient size of the firm large relative to the market. Artificial barriers to entry exist by virtue of restraints that are imposed either by other firms already in the market, by government policies, or by a combination of these factors and are typified by circumstances such as exclusive patents or ownership of existing resources. Several monopolies or near-monopolies have existed or currently exist: U.S. Steel during the 1920s, Alcoa in the 1940s, United Shoe Machinery Company in the 1950s, AT&T through the 1980s, and Inco during most of the 20th century. More recent cases where firms have been argued to be monopolists or near-monopolists include Microsoft, De Beers, and the National Collegiate Athletic Association. Similarly, many local markets still exhibit local monopolies for cable television and many utilities.

Under conditions associated with natural monopoly, the average total cost of production is declining over the relevant range of production. Under such circumstances, a producer can always lower the average cost of a good by producing a larger quantity. As a result, the costs of production will not support the existence of more than one producer—whichever producer is capable of producing the greatest amount can afford to sell at a lower price than its competitors. For many years, conventional thinking regarded industries such as many utilities (e.g., telephone service, electricity, natural gas) and the U.S. Postal Service (with respect to delivery of first-class mail) as natural monopolies.

Regardless of whether a monopoly maintains its status through natural or artificial means, the effects of monopoly on key economic variables are essentially the same. Similar to competitive markets, a monopolist will produce output at the point where the marginal revenue from an additional sale will equal the marginal cost of producing an additional unit of output. However, unlike competitive markets where the market price of a good equates to the marginal revenue that the seller receives from an additional sale, in a monopoly market the marginal revenue is less than the price. (Graphically, the marginal revenue curve will be below the demand curve; see Figure 1.) Price exceeds marginal revenue in a monopoly market because when the seller lowers price to increase the quantity demanded, the seller must lower the price not only on the additional unit sold but also on all units sold by the firm.

Monopolists, by virtue of being the sole seller in a market, face a demand structure that is identical to the market demand for the good. (In competitive markets, individual sellers will face a demand structure that differs from the market demand for the good.) The supply schedule for monopolists is essentially nonexistent. Traditionally, the supply curve represents a schedule showing the quantities producers will supply at a given price. However, the pure monopolist will not face a supply curve because there is no unique relationship between price and quantity supplied. Instead, the price and quantity supplied will depend on demand. This is because the values in the demand schedule will determine the values in a marginal

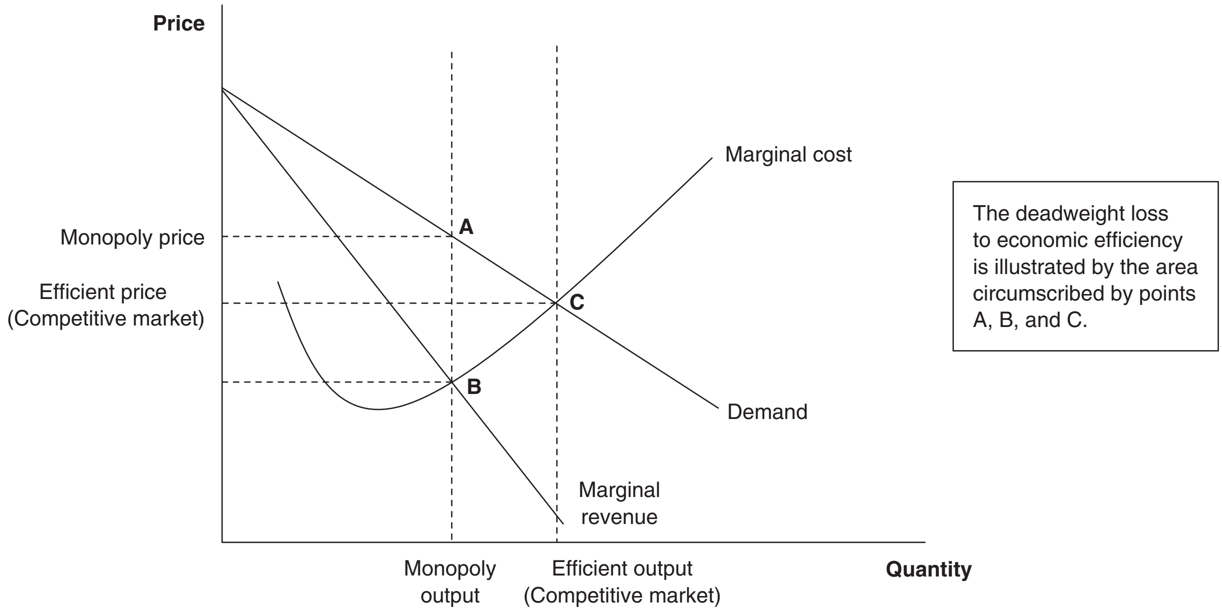

Figure 1 Monopoly and Perfect Competition Compared

revenue schedule and thus determine output. Because marginal cost and price are not equated by the monopolist when determining output, different demand conditions can result in the same quantity of output produced but sold at a different price. As a result, there is no unique price associated with a particular output decision and thus no supply curve for the monopoly firm.

As with competitive markets, the demand schedule will determine price in a monopoly setting. By virtue of being the only seller in the market and thus facing the market demand (to sell additional units the firm must lower price and face a downward sloping demand curve), the firm is a "price maker." The monopoly firm will thus have the power to set the price of the good in the market, and the price the monopolist will charge will be the market price that will result in all output being sold. Because the monopoly firm will produce at an output level where the marginal cost of production for the last unit equals the marginal revenue gained from selling that unit, and the marginal revenue schedule is less than the corresponding price on the demand schedule, the monopoly firm will produce a lower level of output and charge a higher price than a competitive firm.

Contrary to some popular beliefs, the monopoly firm does not charge the highest price possible. The goal of the monopoly firm, as well as competitive firms, is to maximize total profits. The monopoly firm will charge the highest price possible that will result in all output being sold, but there will be many possible prices above that level. A lower level of output would allow a higher price to be charged, but would result in the marginal revenue from the last unit of output exceeding the marginal cost and the firm could still generate additional profits by increasing output and lowering price.

Similarly, popular beliefs that monopolies seek to maximize per unit profits and are always guaranteed economic profits are not supportable. The monopoly firm will seek to maximize total profits, which occurs at the output level when marginal revenue equals marginal cost, rather than the maximum per unit profit, thus equating to the output when marginal cost is at a minimum. Depending on the cost structure involved, monopolists may operate in the short run at a loss. While the monopoly position of the firm does allow it to realize normal or better profits compared with a competitive firm, nothing is inherent in the structure of a monopoly market to guarantee economic profits, or even normal profits. In the long run, like a competitive firm, the monopolist will not operate if it persistently operates at a loss or is unable to cover its fixed costs.

A monopoly firm may also not realize maximum profits because of X-inefficiency, the situation where a firm fails to produce any given output at the lowest average cost. Firms in a monopolistic market are more able to pursue other goals, such as firm growth or avoidance of business risk, which may conflict with cost minimization, or to indulge in other activities that may not minimize costs, such as cronyism or nepotism. Because of the absence of competitive pressures, the monopoly firm may simply not remain vigilant about remaining internally efficient and monitoring costs. When these circumstances occur, the monopolist is likely to incur greater production costs than would be present in a competitive market, and while the monopolist would still enjoy some level of monopoly profits, the X-inefficiency will reduce those profits from levels suggested by cost-minimization strategies.

From a societywide perspective, the higher price and restricted output have an effect on the welfare of society. From the consumer standpoint, the monopoly situation is a loss, particularly compared with a competitive outcome, because they face both higher prices and less output. From the firm's perspective, the monopoly situation is superior to the competitive outcome, largely because of the existence of economic profits. However, the net of the two effects results in a loss to society as a whole.

Total surplus is used to determine the net effect of a monopoly on overall economic well-being. Consumer surplus, measured by the difference between what consumers would be willing to pay for a good minus the amount actually paid, and producer surplus, measured by the amount producers receive for a good minus the cost of producing it, are combined to measure total surplus. As a result, total surplus can be viewed as the value of the good to consumers minus the cost of producing it. Competitive markets allocate resources in a way that maximizes total surplus in an economy. However, because the monopoly firm restricts output below what would occur in a competitive market, the monopolist fails to produce an output and charge a price that maximizes total surplus. Contrary to some popular beliefs, the loss in welfare created by the monopoly situation does not result from the higher profits the monopoly receives, but from the reduced output associated with the monopoly decision. The economic profits of the monopoly do not represent an economic loss to the economy, but the misallocation of resources created by the restricted output does create such a loss.

Public policy toward monopoly is somewhat contradictory. The government serves to protect certain institutions that can be effective in creating barriers to entry. Government protection of ownership rights, particularly through patents and licenses, can be an effective barrier to entry in many markets. However, government policy has also recognized the economic loss from monopoly and has attempted to address some of its effects in various ways. Government policy has generally followed one of four courses of action: (1) attempts to make markets more competitive, (2) regulation of monopoly behavior, (3) turning monopolies into public enterprises, or (4) letting monopolies continue (doing nothing). Each of the first three courses of action can be, and have been, implemented through a variety of means. The most common approach for firms believed to exhibit the characteristics of natural monopoly has been price and output regulation. A general weakness of all three approaches has been the information demands necessary to determine or enforce the socially optimal price and output, particularly given that the firm controls the information or may not even have the necessary information available. Each approach has its relative strengths and weaknesses, and the need for and effectiveness of government action has been and will continue to be a subject of debate.

Price discrimination can alter the extent of any deadweight loss associated with monopoly behavior. Price discrimination exists when the seller is able to charge different buyers different prices for the same good. Perfect price discrimination is unlikely, because it requires the monopolist to know the amount of each consumer's willingness to pay and successfully charge that price to the consumer. However, when price discrimination is possible, the monopolist will generally increase output because selling additional units of the good no longer requires lowering the price received on other sales of the good. In perfect price discrimination, the monopolist could afford to produce at the level where price (demand) equaled marginal cost. From a total surplus perspective, the result would be the same as in a competitive market; however the distribution of the surplus would be changed—the seller would capture the entire surplus. To the extent that price discrimination occurs but is less than perfect, output is likely to be greater than under a monopoly with no price discrimination but less than under perfect competition. As such, the deadweight loss would be less and the monopoly would capture a smaller portion of consumer surplus, although total surplus would still be greater than under a monopoly without price discrimination.

Oligopoly is a market structure in which only a few sellers control most or all of the market and sell similar or identical products. Duopoly is a special case of oligopoly, where only two sellers exist. As with monopoly, oligopolies are essentially "price makers" rather than "price takers" and will attempt to restrict output and increase price above what would arise under perfect competition. However, the presence of other sellers tends to complicate the pursuit of monopoly prices, output, and profits. Oligopolies are sometimes classified as either pure (perfect) or differentiated (imperfect). In pure oligopolies, sellers produce identical products, while in differentiated oligopolies the products are essentially the same, but each firm's product has a unique "identity" to consumers. Regardless of whether the oligopoly is pure or differentiated, the production decisions of each firm affect all other firms and the market price of the product.

In an oligopoly, a firm's price and output not only depend on that firm's decisions but also on other firms' decisions. Game theory has been a particularly useful approach to modeling decisions under oligopoly. As with other market structures, the firm will choose to produce at an output where marginal revenue equals marginal cost, and, as under monopoly, the demand schedule will determine marginal revenue. However, the presence of competitors changes the nature of the marginal revenue schedule. If a firm lowers price in an effort to increase market share, competitors are likely to match the price change. However, if the firm increases prices in an effort to increase profits, rivals are unlikely to match the price changes and some of the firm's customers will choose to purchase from the rivals. This asymmetric behavior results in a discontinuity in the marginal revenue schedule.

The two primary effects of the marginal revenue and demand schedules facing a firm in an oligopoly are as follows: (1) Market prices tend to become somewhat rigid and (2) changes in the cost structure for a firm may have no impact on a firm's production decisions. The first effect stems from the dilemma that creates this discontinuity: Individual firms in an oligopoly cannot lower prices, primarily because of fears of retaliation from competitors, and they cannot increase prices for fear of losing sales. The second effect results from the discontinuity in the marginal revenue schedule because the discontinuity generates a range where marginal costs may vary but the optimal, profit-maximizing output remains the same.

The interdependence of firms in an oligopoly, combined with the goal of each firm to maximize profits and exert as much monopoly power as possible, creates strong incentives for individual producers to collude when making price and output decisions. Such collusion may either be overt (the Organization of Petroleum Exporting Countries [OPEC] is an example) or covert, depending on the presence of legal restrictions on collusion, and may be formal (complete with contracts or other written policies) or informal. A group of firms colluding in such a fashion is termed a *cartel*. Game theory demonstrates that under some conditions it can be very difficult to enforce collusive agreements, particularly if the decisions in the "game" are not repeated. A stable market outcome reached under an oligopoly is termed a *Nash equilibrium* and represents the outcome that occurs when individual firms interacting with each other each choose the best strategy given the strategies that the other firms have chosen.

Not surprisingly, the competitive forces in an oligopoly result in greater output and lower market prices than under a monopoly market, but the market concentration results in less output and higher prices than under a competitive market. As the number of firms in an oligopoly increase, the ability of each firm to influence the market declines and successful collusion between sellers becomes more difficult, causing market outcomes to more closely resemble those of a competitive market. As with monopoly markets, the more restricted the output becomes and the less flexible the pricing becomes, the greater is the deadweight loss to the economy from the oligopoly.

One distinguishing characteristic of oligopolistic markets is the extent of nonprice competition. Price changes, let alone price competition, are difficult if not outright counterproductive in a market characterized by oligopoly. As a result, firms frequently engage in nonprice competition meant to distinguish the firm's product from other goods in the market. To the extent that a firm in an oligopoly can create "uniqueness" for its product, the firm can behave more like a monopoly. Advertising and quality/design differences are the primary means by which firms in an oligopoly will attempt to distinguish their products from those of competitors. One of the key motivations for nonprice competition is that, unlike with price changes, competing firms can find it difficult to duplicate the actions of rivals. Oligopolistic markets are prevalent in a number of economic sectors. For example, according to the 2002 Economic Census, manufacturing of cigarettes, petrochemicals, house slippers, beer, light bulbs, household laundry equipment, and motor vehicles are all sectors where the four largest firms produce more than 80% (and in some cases more than 90%) of industry shipments in the United States. Many of these sectors have reflected this degree of concentration for decades. Similarly, on the retail side, the top four firms in sectors such as office supplies, discount department stores, warehouse clubs, and general book stores all account for nearly 80% or more of sales.

As with monopolies, public policy toward oligopolies varies, but a substantial framework exists to discourage cooperation. The Sherman Antitrust Act of 1890 and the Clayton Antitrust Act of 1914 have been used for more than a century to outlaw collusive activity and prohibit mergers that would lead to excessive market power or monopoly for a firm. The proper scope of these laws, particularly in the context of technological changes, international trade, or other business practices that may have legitimate purposes unrelated to the reduction of competition, has been and will continue to be a subject for debate.

—James E. Roper and David M. Zin

See also Antitrust Laws; Barriers to Entry and Exit; Brands; Cartels; Collusion; Competition; Copyrights; Deadweight Loss; Economic Efficiency; Economies of Scale; Game Theory; Market Failure; Market Power; Mergers, Acquisitions, and Takeovers; Nash Equilibrium; Patents; Price Discrimination; Productive Efficiency; Profits; Social Efficiency; Surplus, Consumer and Producer; Trademarks; Unfair Competition

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MONOPSONY

Monopsony is the "flip side" of monopoly. In monopoly, a firm is the sole seller of product to a group of consumers. Thus, the monopolist faces a downward sloping demand curve for its product. Every unit of output the firm produces reduces the market price for its good. This implies that the more goods the monopolist sells, the lower the monopolist's price. This in turn implies that selling an additional unit may be costly to the monopolist, and possibly result in a reduction of revenue at the margin (or "marginal revenue") to the monopolist. Thus, a monopolist will set output so that price is higher and quantity lower than the competitive outcome. This, in turn, creates deadweight loss, as not all the goods that could increase welfare in society will be sold.

In contrast, a monopsonist is the sole buyer of a particular input that it uses. For example, assume that trees are difficult to ship relative to milled wood. The only lumber mill in a geographic region might well have monopsony power over the foresters in this region. A monopsonist may well (and often does) face a perhaps perfectly elastic demand for its product in the outside world. But its market power over the relevant input that it purchases is similar to the power that a monopolist holds over the product that it monopolizes, as well as the deadweight loss generated by that market power.

Given this situation, what determines how much product (here trees) the miller will choose to purchase? Every tree the miller purchases raises the market price of trees. So purchasing one tree involves not only an additional payment to the owner of that tree but also more payments to the owners of other trees who sell to the monopsonist miller. So the miller will purchase trees so that the marginal cost of the purchase (which is above the market price) equals the marginal return, which (absent production costs) will equal the market price of milled wood from a particular tree in the "outside" market. As with the exercise of monopoly power, the exercise of monopsony power will reduce social welfare, as not all the inputs that could increase welfare in society will be sold.

Note that this story depends critically on a local input that has two conditions. First, there must be an upward sloping supply curve for the input. In other words, there needs to be an economic rent attached to the inputs used. Without this condition, there is no need to restrict purchases to stop the price of the product from rising. If the supply curve is perfectly elastic ("flat"), the monopsonist can have all the product it wants at the opportunity cost of the suppliers. Second, the input has to be more costly to transport in its "unfinished" state than in its "processed" state. Otherwise, the input suppliers could use transportation to reach downstream markets just as easily as the monopsonist.

By itself, monopsony does not violate Milton Friedman's ethical dictate that a firm should maximize its profits, subject to the rules of its society. At least in the United States, a "naturally occurring" monopoly (or monopsony) is not against the law. Broader ethical concerns can arise, however, from the monopsonist's ability to hold input prices below the competitive level. This monopsony harms the input suppliers, who are often small stakeholders in the relevant resource (say, forestry), to the benefit of the monopsonist, who is often a large corporation.

Monopsony Antitrust Cases

There are a series of monopsony antitrust cases, three of which are discussed here. *Mandeville Island Farms v. Crystal American Sugar,* 334 U.S. 219 (1948) appears to be the classic monopsony cartel case. Three and only three refiners in Northern California refined beets into sugar. These three refiners were found liable for colluding to lower the price they paid for beets. The monopsony power of the refiners stemmed from the fact that processed sugar is far easier to transport than unrefined beets. Also note that there is no assumption that the refiners have market power in the output market (here, for sugar).

A variant of the collusive purchasing story is bid rigging among potentially competitive buyers, as was present in *U.S. v. Portac,* 869 F. 2d 1288 (1989). In 1985, the U.S. Forest Service auctioned off approximately 8.1 million board feet of timber in Washington State. Three companies bid in the auction, with two of the companies submitting the minimum bid, and the third firm winning the auction with a bid $20.50 above the minimum. The three firms then split up the timber among themselves.

In *U.S. v. Rice Grower Association of California,* 1986 U.S. Dist. LEXIS 30507; 1986-2 Trade Cas. (CCH) P67, 288 (1986), the U.S. Justice Department successfully unraveled a merger between two rice millers in the central valley of California. The Justice Department was able to sustain its geographic market definition, as the only other rice millers in the United States were located in the southeast part of the country. The merger had created a firm with more than 50% of the relevant market and reduced the number of important competitive "players" from four to three, thus potentially increasing the monopsony power in the market.

In these monopsony antitrust cases, we see economic agents working to create monopsony power so that they can enrich themselves, while causing harm to input suppliers. This certainly violates Friedman's rule of ethics, as well as broader rules. Such action, by reducing purchases of socially valuable inputs, also acts to reduce total welfare in the economy. In addition, it may also have important distributional consequences.

Monopsonistic Labor Markets

Monopsonistic labor markets are a continuing topic in economic research. The basic theory is that a particular employer has a monopsony over labor in a specific region. The counterargument is that in the long run labor is mobile so that the employer must offer competitive wages to keep its employees. In some sense, this debate revolves around how long the "long term" must be.

Recent interest in this issue was spurred by the development of a new approach for addressing the issue. In this approach, search costs preclude workers from finding their optimal employment, generating monopsony power for employers. While firms also have search costs, they are able to offer recruits wages below those recruit's marginal products because it is more costly for the recruits to wait for another position than it is for the firm to wait for another valuable recruit to arrive in its labor pool. This phenomenon may be driven in part by recruits' liquidity constraints. Simply put, it can be very costly for an individual worker to wait for a further job offer to come about. The firm, on the other hand, may be able to do without the worker in the short run through a variety of substitutions available to it.

There are, however, some theoretic problems with this model. In particular, it assumes that the larger a firm becomes, the more costly at the margin recruiting becomes for this firm. Such a problem could in theory be alleviated by having decentralized hiring in large firms. In addition, the model does not consider issues of market concentration, which is central to issues of monopsonization (and monopolization) in input markets.

Here again, from the Friedman point of view, there is nothing particularly unethical going on, as firms are simply taking advantage of their position. In the longer run, however, firm's profits may suffer because they gain a reputation for "exploiting" their workforce. Once more, broader ethical concerns can arise, from the monopsonist's ability to hold input prices (here wage rates) below the competitive level. Indeed, what may be even more troubling is that firm's ability to do this depends on the employee's liquidity level, which in turn implies the less liquid an employee, the lower is his or her salary.

Monopsony in Athletic Markets

Perhaps the most famous issues of monopsony involve arrangements between various sports teams to limit the salaries of athletes. Leagues represented the only important purchaser of the labor of professional athletes. By using league rules to restrict competition for players between teams, leagues could generate monopsony power for themselves and their teams and capture economic rents from players.

Beginning in the 1970s with baseball, however, athletes and their unions have been able to reduce the degree of monopsony power held by franchise owners. Today, at least in the major U.S. sports, while many players draw large salaries, owners have managed to reach agreements with player unions that reduce player salaries by the means of salary caps and "taxes" on "excess" team payrolls. The rationale for these restraints is that they serve to protect league "competitive balance." Whether such restraints do have such a purpose, or are merely another way to exercise monopsony power, remains a difficult question to answer.

More clear, however, is the role of monopsony in highly popular collegiate sports (football and basketball) in the United States. For example, six or seven times each fall 109,000 people, after paying a significant amount of money for tickets, file into the football stadium on the author's campus to watch "student-athletes" perform on the gridiron. The athletes who perform, however, receive only a small fraction of the revenues (in terms of room, board, and academic scholarships that their coaches often make difficult to use fully) arising from their performance.

The lion's share of the revenues goes to the universities themselves. The universities are able to exercise monopsony power over the athletes through their membership in the National Collegiate Athletic Association (NCAA). The NCAA is able to effectively enforce monopsony power in cartel-like fashion by sanctioning universities that are caught violating the rules by giving more than scholarships to players.

The ethical implications of monopsony in professional sports markets are none too certain. It is difficult to take sides in the negotiations between billionaire owners and unions representing millionaire players over how the rents in professional sports should be distributed. The ethical implications of college sports monopsony, however, are far clearer.

The NCAA, acting to create monopsony for its member schools, takes rents away from 18- to 22-year-old athletes, many of whom come from poor backgrounds, and redistributes it to the member schools. This has all the negative ethical ramifications discussed above, with the perhaps further onus of taking advantage of young poor people.

It is in the NCAA's enforcement of these rules that the true ethical difficulties of monopsony arise. Given the rents at stake, it is not surprising that that many universities attempt to break the rules by giving athletes more support that the NCAA rules allow. Although such schools, when caught, are broadly thought of as "cheaters," from an economic point of view, it might be more accurate to describe these universities as "cartel breakers."

Perhaps it is easier to understand the ethical problems of the NCAA rules on a personal level. Consider the not atypical story of a not-terribly-well-compensated university assistant coach scouting a potential recruit in a small town who lives in deep poverty. It is only natural in those circumstances for the assistant coach to want to do something small for the recruit, such as buy him a good meal or a pair of sneakers out of the coach's own pocket. Yet, as the NCAA has made clear, any school whose coaches are caught engaging in such "unethical" behavior will face serious sanctions, including the loss of scholarships and perhaps important television revenues.

—Andrew Kleit

See also Antitrust Laws; Barriers to Entry and Exit; Cartels; Corporate Social Responsiveness; Deadweight Loss; Market Failure; Market Power; Monopolies, Duopolies, and Oligopolies; Price-Fixing; Reputation Management; U.S. Department of Justice

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Montreal Protocol

The Montreal Protocol on Substances That Deplete the Ozone Layer is an international treaty that has guided the gradual phaseout of production of chlorofluorocarbons (CFCs), halons, and other chemicals suspected of thinning the ozone layer. Restoration of the ozone layer is necessary to protect humans, animals, and plants from exposure to dangerous amounts of ultraviolet (UV) radiation. The Montreal Protocol was negotiated in 1987 and went into effect in January 1989. Revisions that have strengthened the Protocol have occurred regularly since 1990 as new scientific, environmental, and technical information has become available.

Each industrialized signatory nation agreed to reduce production of ozone-depleting substances (ODS) during the 1990s except for essential uses for which no substitutes could be found. Developing nations were given a longer timetable and financial assistance to phase out production. Each country created its own approach to achieving reductions. The United States relied on an accelerating tax on CFCs, while the European Union used regulations to restrict and then ban production, imports, and exports. By 2003, more than 90% of the production of certain ODS in industrialized countries was achieved, and more than 60% in developing countries.

The earth is protected from the sun's UV radiation by stratospheric ozone that screens out about 99% of UV. ODS do not wash out in the lower levels of the atmosphere, but drift up to higher levels of the stratosphere and eventually break down from UV exposure and release chlorine atoms that in turn cause ozone (O_3) to break down. The "hole" in the ozone layer over the Antarctic was documented in 1985, and other "holes" have subsequently been found over the Arctic, the Caribbean, and parts of Europe. Increased UV radiation is associated with greater incidences of skin cancer, cataracts, suppression of the immune system, and other health problems.

CFCs are the most widely known ODS to the general public for two reasons. First, CFCs were implicated as potential hazards in the mid-1970s, and their use in aerosol spray cans was banned in the United States in 1978. Second, CFCs were used in refrigeration systems, including air-conditioning in homes and vehicles, under brand names such as Freon, produced by DuPont Corporation. ODS are also used in foam insulation, industrial cleaning solvents, fire extinguishers, and some herbicides. Although ODS manufacturers opposed further restrictions in the early 1980s, by 1986 they reactivated research programs to find substitutes and supported the Montreal Protocol in 1987.

The United States began to regulate CFCs and other ODS in the 1990 revision to the Clean Air Act. The market incentive approach to environmental regulation was used to efficiently achieve the regulatory goal of eliminating ODS. Rather than taking a command-and-control approach by simply imposing a production ban by a certain date, the Environmental Protection Agency established an accelerating tax on CFC production. This escalating CFC tax sends clear price signals to consumers to look for alternatives and provides incentives to producers to create substitutes because the market for substitutes will become larger over time. At the same time, sales of CFCs were restricted to certified professionals who had to use prescribed equipment to capture and recycle the emissions. An early deadline for phasing out CFC production in the United States was set for 2000, but it was subsequently moved to 1996 because of the speed with which substitute products were developed and marketed. Some early substitutes were known to have lower levels of ozone-depleting potential or contribute to global warming, but these are being replaced by the next generation of substitutes.

Assistance to developing nations to meet the goals of the Montreal Protocol is provided by the Multilateral Fund for the Implementation of the Montreal Protocol. The fund received $2 billion from industrialized nations by 2003 to give grants for converting manufacturing processes, setting up national Ozone Offices, and supporting other tasks in developing nations. Two United Nations agencies and the World Bank administer the Fund.

The Montreal Protocol is widely viewed as a success in protecting the global commons. A few essential uses continue to require production of small quantities of ODS, for example, metered dose inhalers for asthma. However, estimates in 2003 indicate that the ozone layer will be restored between 2050 and 2065, depending on how quickly older ODS-using equipment is retired, and how quickly developing countries reduce ODS production and use.

The Montreal Protocol was used as a model for the Kyoto Protocol, which deals with increasing amounts of greenhouse gases that are purported to be causing global warming. The Montreal Protocol has been much more successful in meeting its goals and deadlines because of the nature of the problem, the costs of achieving ODS reduction targets, and the number of actors that would be significantly affected. Ozone depletion was assessed by scientists more quickly and with more certainty about the relationship between ODS and the thinning ozone layer. The aggregate costs of meeting Montreal Protocol targets were much lower per capita than for the Kyoto targets. Finally, ozone-depleting substances were largely produced by a few large corporations in a few industrialized countries, so cooperation and monitoring were more easily achieved.

—Jeanne M. Logsdon

See also Commons, The; Externalities; Kyoto Protocol; Ozone Depletion; Pollution Externalities, Socially Efficient Regulation of

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Moral Agency

Moral agency presumes that human beings are capable of choice and morally accountable for their actions, as well as the consequences of those actions. Closely related to the theory of self, moral agency embodies the ability to self-regulate and self-sanction one's behavior; it is part of living in community. Individuals have the capacity for making moral judgments and taking actions in keeping with a moral code. People who function as moral agents are able to consider the relationship between means and ends. They balance their intentions and actions with probable consequences and determine whether the ends justify the means. In general, theories of moral agency do not hold an individual responsible for the unintentional consequences of an action.

To some degree, moral agency is dependent on the social position or political representativeness of an individual. People who hold high social or political positions are often held to a higher moral standard than average community members might be. Whatever their status, though, all members of a community are expected to adopt the community's standards of right and wrong. They are expected to observe their own behavior, assess the degree to which the behavior adheres to the community's moral standards, and correct their conduct accordingly. Redemption, or forgiveness of a person's transgressions, is often contingent on the perpetrator's admission of guilt.

However, when a society's rules oppress, disenfranchise, or marginalize specific groups, individuals often step forward to challenge what they perceive to be the injustice or immorality of those standards. Sometimes, these individuals belong to the oppressed group; sometimes, they do not. These people question the status quo and assert the need for change. While they may be viewed initially as dissidents or trouble-makers, these people may become the leaders and agents of sweeping social change. In the Unites States, the Abolition, Women's Suffrage, and Civil Rights movements were founded when individuals or small groups of people called for change; although initially scorned, many of those early social change advocates are now viewed as heroes.

Moral standards are usually based on a combination of cultural, religious, and philosophical concepts and principles, which are used to determine whether a particular action is right or wrong. However, in the 20th century, Western culture individualized the definition of morally correct behavior, diminishing the hegemony of some established religions and other traditional moral authorities as the arbiters of morality.

To function as a moral agent, a person must understand the responsibility one has to behave morally. They must be able to feel shame, guilt, or remorse when they violate the moral code, proportionate to the magnitude of the violation. This requires a fairly well-developed sense of empathy and compassion: Moral agents are able to fully humanize their fellow citizens. They are also able to predict the probability of various outcomes of their actions and understand the relative desirability of each probable outcome. Under ideal circumstances, moral agents are able to postpone a decision long enough to consider the consequences before taking action. They operate free of coercion and are able to choose any possible course of action. They understand the potential outcomes of their actions. In addition, moral agents are able to exert the following pressures on their own behavior.

Rationality

Moral agents are able to reason and make self-interested decisions. This rationality is comparable with the legal concept of *mens rea*—moral agents know what they are doing; their choices are deliberate.

Trust

Moral agents occupy a position of trust that is recognized by their respective communities. However, there must be a rational basis for this trust. That is, the community must not have a sufficient reason to determine a person unable to function as a moral agent.

Moral agency is mitigated by social and personal constructs. For example, sleepers are not morally responsible because they are unaware of how their somnolent actions conflict with their moral beliefs. People with diminished mental capacity may not be able to control their own behavior, deliberate about possible courses of action, or understand the consequences of their behavior. Children can only be granted moral agency to the degree they are able to recognize the connection between cause and effect. They can only be held accountable to the degree of their understanding. In short, moral agency is imputed to people who are awake, sane, sanguine, sober, and possess either the knowledge or ability to acquire sufficient knowledge to assess a given situation, evaluate possible courses of action, and choose what they perceive to be the optimum course of action for all concerned.

Coercion may mitigate moral agency. People under the direct or perceived threat of death or significant harm may not be responsible for their own behavior, even if they would have moral agency in other situations. People in specific situations, such as war, or institutions, such as prison, may be more likely to behave in morally reprehensible ways; their culpability may be altered by their circumstances. In times when major catastrophes devastate a society's physical infrastructure, the norms that preserve social order may devolve to a state of nature, in which behaviors that would otherwise be considered immoral or criminal, such as stealing food, water, or medicine, become necessary to ensure survival. In this state of nature, it becomes proper to take what is necessary to preserve and protect one's life, while stealing obvious luxuries is still considered inappropriate.

The lack of sufficient, relevant, trustworthy information may also affect an individual's responsibility for the unintentional outcomes of their behavior. To function as moral agents, people must have both access to credible information and sufficient intellectual ability to digest that information and apply it to the situation at hand.

Moral agency imparts minimum obligations on individuals. It requires people to act as follows:

- Acknowledge the relationship between people, their actions, and the community's relative well-being
- Aid those in distress to the degree allowed by one's personal circumstances. The capacity to act determines the level of responsibility one has for taking action
- Choose between conflicting but equally important imperatives

- Comply with the laws of their communities and the professional standards of their occupations
- Disclose their limitations, conflicts of interest, and barriers to satisfactory performance
- Feel satisfaction at morally correct behavior for its own sake, with no need to be rewarded for doing the right thing
- Fight against consensus decision making when its effect is to push those with different points of view out of the public discourse
- Practice self-reflexivity. Moral agents are expected to analyze their own positions relative to a situation, balance objective and subjective ideas, and determine the course of action that would foster the greatest inclusivity and community building
- Prevent the suffering and death of others, the mistreatment of animals, and the wasteful or unnecessary depletion of scarce natural resources
- Reject moral disengagement—the rationalization of behavior that conflicts with moral standards of conduct by dehumanizing victims, or blaming them for their plight so that harmful actions become palatable
- Separate from otherwise righteous ideologies when those ideologies advocate morally reprehensible behavior in the name of their cause

Collectivization of moral agency is possible when individuals act in concert to achieve a specific goal. In this case, each member of the group is equally responsible for the outcomes of the group's behavior. Organizations are causally responsible for the coordinated actions of their members. Communities have a collective moral responsibility to care for people with disabilities, people who are elderly, widowed, orphaned, or poor, and people who are unable to care for themselves.

Moral agency follows individuals into their roles as employees, managers, and executives. Theoretically, the same rules would apply for granting moral agency to people inside corporations as outside their boundaries. In their roles as fiduciaries of their employers, however, sometimes socially responsible behavior contradicts the traditional definition of fiduciary responsibility as the maximization of shareholder wealth. In these instances, it is difficult to determine which duty rules: the duty of the individual to behave in the best interests of the company's shareholders or the duty to behave responsibly as a member of the larger community. The employee may feel coerced into acting in the interests of shareholders to the exclusion of larger community needs, especially if choosing in favor of the community cost the employee his or her job, or led to professional, economic, or other sanctions. Most communities acknowledge an employee's right to refuse any direction from a superior to indulge in lawbreaking or immoral conduct, but the fear of repercussions may force the employee to comply. The degree to which the employee perceives a threat may render the employee unable to function as a moral agent.

The corporation possesses moral agency. To the degree that it is a legal entity, corporations are certainly expected to obey all pertinent laws and regulations. When the corporation fails to follow the law, the responsibility for this failure rests on the individual members of the corporation, with special burdens placed on those with decision-making authority. Recent court cases in which CEOs and other corporate officers received heavy fines or prison sentences for their actions as officers certainly indicate that when corporations fail to execute moral agency, its leaders are held responsible.

—Cheryl Crozier Garcia

See also Absolutism, Ethical; Amorality; Aristotle; Autonomy; Business Ethics; Christian Ethics; Cognitive Moral Development; Commonsense Morality; Conscience; Corporate Moral Agency; Dilemmas, Ethical; Ethical Decision Making; Golden Rule, The; Integrative Social Contract Theory (ISCT); Moral Distress; Moral Education; Moral Hazard; Moral Imagination; Morality, Public and Private; Moral Luck; Moral Point of View; Moral Realism; Moral Reasoning; Moral Rules; Moral Sentimentalism; Moral Standing; Normative Ethics; Organizational Moral Distress; Relativism, Moral

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Moral Distress

Moral distress is the anguish and suffering caused when an individual's personal ethics conflicts with and, at times, is compromised by job requirements, administrative directives, managerial decisions, workplace policies, and so on. It is an issue that many face in today's workforce. While this notion was developed to explain a specific type of job-related stress and trauma experienced by health care workers, specifically nurses, psychologists, doctors, social workers, educators, and business professionals are now reporting similar experiences. There are related incidents also found in the area of family law and mediation regarding parents and child custody issues.

Definition and Characteristics

The notion of moral distress emerged in the early 1980s when Jameton, writing for nurses, drew a distinction between moral uncertainty, moral dilemmas, and moral distress. The first deals with instances when an individual is not sure what particular moral principle or value is applicable in the situation at hand. The second refers to problems when several moral principles or values are relevant, and the individual must choose between perspectives and their consequences. The third, moral distress, describes the reality of knowing the ethically correct action to take and feeling moral responsibility, but being unable to act in accordance with personal views due to organizational constraints. In such situations, individuals are faced with having to choose between their own integrity or participating in wrongdoing. Wilkinson expanded the understanding of this phenomenon by adding that there is a psychological dimension, a psychological disequilibrium created by disrespecting personal beliefs. First in 1995 and again in 2001, Corley published a Moral Distress Scale. It identified frequently occurring issues that were problematic for nurses, as well as severe morally distressing situations.

The ethics of care, among other ideas, has influenced the understanding of moral distress. In 1995, Liaschenko furthered the discussion of moral distress by describing nurses as "artificial persons" who find themselves in a stressful, complex situation. They are healing professionals and patient advocates who at times inflict pain against their will due to supervisory directives, institutional policies, and bureaucratic practices. In 2000, Penticuff and Waldren noted that the work setting, both actual and perceived, affects the ethical choices made by nurses.

Moral distress is a multidimensional phenomenon that can affect a person physically, emotionally, spiritually, and socially. Consciously knowing the appropriate action to take, but being unable to act, can damage a person's sense of integrity and authenticity. Long-term moral distress can result in the loss of moral integrity, causing the individual to not behave according to professed values and convictions, nor be able to effectively deal with moral conflicts.

During times of moral distress, frustration, anxiety, anger, and guilt are common emotions, because individuals often feel powerless, afraid of repercussions, or reluctant to act. These feelings occur during the period known as initial distress. Some individuals after identifying the divergence between their personal views or values, and those of the workplace, have the self-assurance, courage, and interpersonal skills to seek to resolve the difference. Others do not. The latter is referred to as reactive distress. If the distress becomes too acute, it can cause illness, relationship breakups, the loss of a job, and even the abandonment of a career. Moral distress is detrimental to the nursing profession because highly qualified individuals are leaving the profession or are not choosing to enter it.

Internal and external factors create morally distressing situations. Personal characteristics such as low self-esteem, religious views, lack of professional confidence, deficient interpersonal and conflict resolution skills, and fear are factors in an individual's ability to clarify and handle ethical differences. External reasons include industry standards, administrative directives, governmental regulations, managerial practices, inadequate time and human resources, legal ramifications, personal financial impact, and organizational culture and politics.

Moral Distress and the Workplace

Moral distress is an emerging concern beyond the health care field, because such stressful, anxiety-causing workplace situations are not isolated to medical and life science professions. Instances are coming to light in areas such as family law, business, and higher education. Some specific issues are as follows.

Family law and mediation experts are beginning to recognize the moral distress that some experience when children are mandated by the court to spend time with an unqualified parent. It is traumatic for a parent to routinely hand over a child to a parent who may not provide the level of care deemed necessary.

With the emphasis on ensuring ever-increasing higher profits, business and financial professionals sometimes find themselves faced with using questionable marketing, management, reporting, and accounting practices. Plus, repeated job redefining and layoffs are now standard methods used to reduce organizational operational costs. A growing number of companies are choosing to reduce their workforce, while increasing the workload of remaining employees. Staff reduction practices usually do not consider how repeated layoffs affect workers' health and careers. More and more managers are being charged with devising work assignments that are excessive and overwhelming. They are also being asked to conduct repeated layoffs in a "business-as-usual" manner while not considering an employee's loyalty, professional skills, economic condition, work history, and so on. These management professionals, when placed in this situation, sometimes feel that they must choose between personal integrity and retaining their jobs. While at times they may feel troubled and guilty about the ramifications these practices have on employees and their families, they usually rationalize the validity of these methods by believing that the required action is how profitable businesses are conducted.

In higher education, morally distressing issues can arise around the tenure process, admissions policies, and instructional quality. As institutions struggle to sustain themselves economically, enrollment standards and practices can become compromised. In some instances, department chairs are being requested to admit students who are not adequately qualified. Faculty members feel the burden to keep student retention high so that they are viewed as effective instructors committed to the university or college. Professors and staffs feel caught between enabling their university or college to stay financially viable and providing students honest feedback on their academic work so that they can receive a quality education.

The research conducted on the moral distress experienced by nurses has laid the groundwork for analyzing, understanding, and addressing this phenomenon in others areas of the workplace. Present scholarship verifies its existence, describes its basic nature, and outlines aspects of its devastating effects. Various professional organizations, such as the American Association of Critical-Care Nurses (AACN), recognize it as a serious issue, are beginning to educate their members about it, and are taking practical steps to address it. Future researchers can use this material to examine the following business sector–related questions: What moral conflicts do managers experience when they knowingly assign excessive workloads to cut costs and increase profits? What is the impact on managers' sense of moral integrity when they are required to repeatedly lay off employees without consideration of how this affects employees' well-being? What is the effect on employees when they have to routinely rationalize that work is more important than spending time at home with family and friends?

Reducing Workplace Moral Distress

Much still needs to be done to enable employees to consistently identify and handle the moral distress they experience. Four factors are critical in reducing workplace moral distress: organizational culture and values, leadership integrity, professional voice and code of ethic development, and professional association involvement. The development of an ethical organizational culture is vital in setting workplace expectations, instilling accepted values, devising appropriate policies, and supporting dialogue about divergent ethical views. More democratic work environments can provide employees avenues to discuss concerns about organizational practices, administrative policies, and supervisory directives without fear of negative repercussions. Professional associations can be effective vehicles for professional development of their members, as well as advocates for the creation of ethical work environments. Besides monitoring member behavior and articulating a code of ethics, they can provide leadership programs that enable the development of ethical decision-making skills, as well as training opportunities to enhance professional self-image, confidence, and conflict resolution skills. The latter service enables individuals to develop their self-esteem and professional voice to effectively discern moral distress situations, affirm their own feelings and values, and choose to take care of themselves by developing an appropriate action plan to resolve the stressful situation.

Thus, addressing workplace moral distress is about establishing and maintaining organizational integrity, and providing a safe and meaningful work environment for employees. It is about fostering professional voice and accountability so high-quality client and customer service is ensured. Last, it is about creating institutions and practices that do not harm the professional, the client, or the community in which they reside.

—Charles F. Piazza

See also Bioethics; Ethical Culture and Climate; Ethics of Care; Stress, Job; Virtue Ethics; Whistle-Blowing; Work Ethic; Work-Life Balance

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Moral Education

Moral education in a business and society context involves learning to make consistently correct moral judgments as a guide to behavior that is self-regulated instead of externally coerced in the realm of commerce. The literature on this enterprise is largely a product of scholarly projects in business degree programs at select universities and colleges. Moral education in this context is inextricably bound up with the mission of higher education in general and the university in particular. From its Greek origins, the university has been associated with the pursuit of knowledge for its own sake as well as the practical development of personal intellect and character. According to Darryl Reed, the medieval university extended this mission by preparing students for certain professions, most notably the clerical, medical, and legal, while emphasizing public service to the community or state. Business schools, shaped by both Greek and medieval traditions, typically require that students take liberal arts coursework as preparation for the more technical, professional education delivered in business degree programs. Given this tradition, it can be said that moral education involves three interrelated aspects: imparting knowledge that explains the nature of the business and society relationship, developing the personal intellect and character of students, and encouraging graduates of business schools to become socially useful practitioners.

The first aspect of moral education can be framed in terms of a social contract between business and society. A common interpretation of this contract derived from utilitarian ethics is that society grants legitimacy to business as an institution because of its potential to serve the greater good. According to William C. Frederick, this potential involves two major value processes: *economizing* or the ability of business organizations to convert inputs to outputs efficiently through competitive behaviors and *ecologizing* or the capability to forge symbiotic, integrative linkages between organizations and their communities that function adaptively to sustain life. Because business firms are embedded in communities, they are subject to various stakeholder expectations, also inherently value laden. For instance, social activists who pressure a firm for the proper disposal of toxic waste typically assert a community's right to a healthy environment that sustains life. At the same time, the costs of toxic waste disposal may adversely affect the economic performance of a firm, its ability to compete with other firms in the industry, and financial returns to its shareholders. As this example shows, ecologizing and economizing values can be in tension and subject to trade-offs. Historically, the government's role in business and society has been justified by the goal of ameliorating the negative spillover costs of business, such as toxic waste, with public policy that seeks to balance such value tensions. A moral education necessarily sheds light on these institutional roles in terms of the values and ethics at stake and the distribution of benefits and costs to various groups in society.

Ideally, the second aspect of moral education, the practical development of intellect and character, is enhanced by the first. That is, students who grasp the nature of the business and society relationship may also develop the potential to reason at higher levels of moral development or at least comprehend the decision-making models that incorporate such reasoning. In terms of Lawrence Kohlberg's widely applied theory, there are three levels of moral development, each embodying two sequential stages of learning. Specifically, the preconventional level involves a focus on self based on a reaction to punishment and seeking of rewards in Stages 1 and 2, respectively. If individuals learn to move beyond this self-centeredness to consider the expectations of others, then they are able to reason at the conventional level, conceptualized as Stage 3 or conformity to family and peer group conceptions of right and wrong and Stage 4 or an adherence to the rule of law and custom. In comparison, a person who can reason on the postconventional level of Stage 5 is able to focus on humankind in terms of moral principles, including human rights, social contract, and constitutional precepts, that are broader than those embodied in immediate referent groups or a particular society's customs and laws. Stage 6, the apex of moral reasoning in Kohlberg's framework, is denoted by an ability to define right and wrong in terms of principles of justice, fairness, and rights that can be generalized to the entire humankind. In terms of postconventional reasoning, moral education may help prepare students for the dilemmas in international business environments, where multinational corporations operate in developing countries that lack the legal or customary protections afforded to workers and consumers in more advanced industrial economies.

Another model of moral character has been developed by Carol Gilligan, who argues that boys and girls follow different paths to moral development, with girls valuing the quality of personal relationships and caring for others' well-being more than adhering to rules and principles. Differences notwithstanding, the common denominator of theories of moral development is the ability to advance from self-centered to other-regarding reasoning. Using Kohlberg's theory, James Rest found strong evidence that subjects tend to advance in cognitive processes of moral reasoning as long as they continue in formal education. Put differently, education has the potential to influence moral development and hence the personal intellect and character of students.

Finally, education that enhances moral reasoning should help produce socially useful practitioners who are able to factor values and ethics into their decisions while striving to economize, respond constructively to community concerns, and adhere to the law, public policy, and government regulation. According to Diane Swanson, it is particularly important that executive managers exhibit these abilities and require that other employees follow suit, given the power vested at the top of corporate hierarchy. Education meant to prepare practitioners for these inherently moral roles would incorporate corporate social responsibility in the curriculum, including topics such as the law, public policy, and governmental regulation; environmental sustainability; management and stakeholder relationships; value-based leadership and corporate culture; organizational ethics, compliance programs, and codes of conduct; moral reasoning; personal values and ethics; and the nature of ethical dilemmas or value trade-offs. Moreover, education aimed at encouraging students to reason at the highest level of moral development would emphasize the value-based utilitarianism that justifies the social contract between business and society as well as other ethical principles relevant to the good of humankind, including deontology or duty-based ethics, ethics of care, human rights, and justice and fairness.

—Diane L. Swanson

See also Business, Purpose of; Chief Executive Officer (CEO); Codes of Conduct, Ethical and Professional; Corporate Ethics and Compliance Programs; Corporate Social Responsibility (CSR) and Corporate Social Performance (CSP); Deontological Ethical Systems; Duty; Economics and Ethics; Ethical Culture and Climate; Ethics of Care; Human Rights; Integrity; Justice, Theories of; Kohlberg, Lawrence; Leadership; Moral Reasoning; Other-Regardingness; Teaching Business Ethics; Utilitarianism

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Moral Hazard

Moral hazard is the risk one party has when dependent on the virtuous, or moral, behavior of others. These risks increase when there is no effective way to control that behavior. To distinguish moral hazard from all cases in which people misbehave, moral hazard problems arise in situations in which two or more parties form an agreement or contractual relationship, and the arrangement itself creates the incentives for misbehavior. For example, for a person to have an incentive to exceed the posted speed limit so that he or she can be home in time to watch a favorite television show would not be an example of moral hazard. However, if one's employer agrees to pay all misdemeanor moving violations that he or she would incur when using a company car, then that would create a moral hazard problem by giving one an incentive to take an action (speeding) that harms the employer (paying for speeding violations). Because moral hazard problems arise within the context of agreements or contractual relationships, they are also a type of post-contractual information problem.

Suppose there is an arrangement between an individual and another person or entity, such as an organization, in which the individual agrees to behave in a certain way, perform a specified task, or provide a specific product. The potential for a moral hazard problem arises when the following conditions exist. First, there is uncertainty regarding the moral character of contracting parties. Second, the interests or objectives of the individual are not aligned with the interests or objectives of the person or organization with whom he or she made the agreement. Third, the agreement creates incentives for the individual to act in such a way so as to benefit himself at the expense of the person or organization he or she has agreed to help. Finally, it is costly, difficult, or impossible for the person or organization to fully monitor the activities of the individual. The problem of monitoring is critical. If contracting parties could effectively observe or monitor the activities of their partners, then moral hazard problems would be almost entirely eliminated.

Costly Monitoring

Monitoring is difficult because of contractual incompleteness and asymmetric information.

Contractual Incompleteness

A contract is incomplete if it does not specify an action for a potential contingency or if the action stated for a contingency is ambiguous. There are four reasons why contracts are incomplete: Some events cannot be identified or predicted at the time the contract is established; there might be too many contingencies to account for in the contract; it is often difficult to measure and evaluate the performance of contracting parties; and enforcing contractual compliance is costly. These problems are compounded when the contractual agreement is complex, exchange is infrequent, or the gains from trade are relatively small.

For example, suppose a person contracts with a carpenter to build a home. The contract might specify the style of home to build, the type and quality of materials to be used in construction, the date the home should be completed, and the payment the buyer will make to the builder. The contract might also stipulate what would happen if inclement weather makes it difficult for the builder to finish the home on time. However, there might be some events, unforeseen at the time the contract is established, that make it difficult for the builder to complete the project. For instance, a labor strike in another industry might make it impossible for the builder to obtain needed supplies. Incomplete contracts can create moral hazard problems if persons governed by the contract are able to exploit the deficiencies of the contract for their own personal gain. For instance, the builder could claim certain events, unverifiable to the buyer, have occurred that make it impossible for him or her to complete the project on time so that he or she can take time off for personal reasons. Or, the builder could use less costly materials because he or she knows the buyer is not able to distinguish perfectly between high- and low-quality materials.

Asymmetric Information

Asymmetric information means some people have relevant information not available to others. An example is the used car market. Sellers of used cars generally know more than buyers about the quality of the cars they sell. Asymmetric information is a problem if people have an incentive to use their private information to defraud others. Asymmetric information is manifested either before or after the exchange has been established. Asymmetric information problems arising before an exchange is formalized are known as adverse selection. Asymmetric information problems arising after an exchange is formalized are defined as moral hazard.

Moral hazard arising from asymmetric information is manifested as either hidden action or hidden information problems. In a hidden action problem, the person taking an action knows more than others about what he or she did or what the effect of his or her action is. Hidden action problems are the quintessential example of moral hazard problems, because moral hazard is most often thought about in terms of behavior. For instance, an insurance company might not know if persons with an insurance policy are taking precautions to avoid an insured mishap. An employer might not know if an employee is working hard or shirking. Citizens might not know if the trips their elected officials are taking are necessary for the discharge of their public duties. A person might drive a rented car more aggressively than a car he or she owns. In a hidden information problem, persons with private knowledge might not fully or truthfully disclose the information to others entitled to it, or they might use their private knowledge to benefit themselves at the expense of others. For example, an employee might not accurately disclose information requested by a superior, a corporate executive might not fully disclose the financial health of the company to employees or investors, a mechanic might report a car needs extensive repairs when in fact it requires only minor service, or a physician might order more medical tests than are necessary given the patient's expected medical condition.

Examples of Moral Hazard Problems

The problems of contractual incompleteness and asymmetric information are pervasive. Therefore, any transaction has the potential of creating a moral hazard problem. This means that most agreements and contractual relationships give rise to social and ethical problems for the people who enter into the agreements. Because monitoring is costly, an ethical problem for persons or organizations faced with the decision to monitor is whether they should tolerate some degree of waste, fraud, or abuse. Government regulation and trust can substitute for costly monitoring, although these are imperfect and costly to implement as well. For the person for whom the agreement creates an incentive for misbehavior, an ethical problem is whether to pursue one's own interest or subordinate it to the interest of the person creating the agreement. Social norms for behavior, such as "Do not lie, cheat, or steal" or "Don't bite the hand that feeds you," are often necessary to complement institutional and organizational solutions to moral hazard problems.

Insurance, employment, and professional (agency) relationships, as well as a case study of the savings and loan scandal of the 1980s, provide contexts for a more careful exploration of moral hazard problems and the ethical dilemmas they create.

Moral Hazard in Insurance Markets

The insurance industry provides the most effective illustration of the problem of moral hazard. In fact, the term *moral hazard* is thought to have originated in the insurance industry. People buy insurance to protect themselves from unseen or unanticipated risks. For instance, homeowners risk losing a home to a fire, and automobile owners face the risk of being in an accident that damages the car and causes injuries to themselves or others. Most people are risk averse, meaning they prefer not to face the risk but would rather transfer risk to others in exchange for a payment. Insurance companies are willing to take risk by providing insurance coverage because they can pool the risks of many individuals, assuming the risks are independent (meaning one person's risk of an accident does not affect another person's risk). In the absence of insurance coverage, most people will take some precautions to minimize the chance of an accident. The problem with insurance coverage is that once a buyer obtains insurance, he or she has an incentive to change his or her behavior because he or she knows someone else, in this case the insurance company, bears the risk of his or her behavior. For example, if people have an automobile insurance policy that pays for repairs in the event of an accident, then they have less incentive to drive carefully. They might, in fact, be reckless in their behavior because they know that they will not have to bear the cost of repairing their car. In the extreme case, people might have an incentive to cause accidents in order to collect insurance money. The insurance company thus faces the hazard it will have to pay out more in claims than originally expected. This problem becomes acute if, as is usually the case, the insurance company cannot fully monitor the insured to ensure their behavior is in accordance with policy guidelines.

A normative duty for those who are insured to resist the incentive to be reckless and to exercise adequate care in the actions they take will moderate the effects of moral hazard caused by insurance. Moreover, insurance companies can establish policies to reduce the incentives the insured face to engage in risky behaviors. For instance, deductibles and copays shift some of the cost of accidents to the insured. Also, some insurance companies have policies that do not pay if there is evidence that accidents are willfully caused or are caused by negligence on the part of the insured. Societies also create laws to prohibit the willful causing of accidents. For instance, people who are convicted of arson may have to pay fines or serve time in jail.

Moral Hazard in Employment and Organizational Settings

Moral hazard problems are pervasive in organizational settings, particularly in employment. One reason is that employment contracts are notoriously incomplete. Employment contracts offered to new hires often specify nothing more than a starting wage and date employment begins; contracts offered to supervisors or senior-level executives are usually more extensive, but even these contain boilerplate language. Work schedule and employment responsibilities are often negotiated later, and company policies are relegated to a company handbook. The incompleteness of employment contracts gives employers or even employees an incentive to take advantage of each other. For instance, an employer might shift work responsibilities to employees after they are hired or have worked for a period of time.

Another reason moral hazard is pervasive in employment is that it is impossible for firm owners or managers to fully monitor what workers do. Accordingly, workers have an incentive to shirk, that is, to give less than complete effort in their employment responsibilities and to free ride on the efforts of coworkers. Some workers might even steal from their employers by taking home office supplies, for instance. Furthermore, many employees bring specialized knowledge with them at the time they are employed. Other employees acquire specialized knowledge about the company, industry, production processes, activities, and competencies of coworkers as a result of their being employed. Because of the vast quantity and complexity of information created and available within organizations, it is not possible for owners or managers to know everything occurring within a company or everything relevant to making the organization function effectively. Thus, much information in organizations becomes private information. A hidden information problem arises when workers do not have an incentive to disclose relevant information to their superiors or when they have an incentive to distort information they do disclose.

There is a relationship between moral hazard and the nature of compensation within organizations. Ideally, workers are paid based on the effort they contribute to the company. Workers who contribute little ought to be paid little, while workers who work hard and contribute a lot ought to be paid a lot. In reality, firms do not usually pay workers based on their contributed efforts because of the difficulty managers have in determining precisely how hard workers work or what workers contribute. Thus, workers may shirk, or they may report a greater level of effort expended than they actually worked to increase their income.

Most firms have some form of incentive compensation or performance payments designed to align the interests of workers with those of the organization and to motivate workers to work hard. Because of the difficulty in observing and verifying individual efforts directly, so that pay can be tied to effort, most performance payments are tied to proxies of effort, such as number of units of output produced (piece rates in manufacturing), number of units sold or total sales (commissions for salespeople), stock prices, or productivity improvements.

Although incentive compensation is established to mitigate moral hazard problems, they can create new moral hazard problems. The motivation behind incentive plans is if workers perform well for the organization, then such efforts should affect the measurable indicators—sales would increase or stock prices might rise. However, incentive plans may work too well. Workers may focus too closely on the measurable indicators, taking actions to manipulate the indicators rather than benefit the company. For example, an executive paid in company stock might have an incentive to take actions that increase the stock price, at least in the short run. He could do this by reporting income to be earned in future periods as income earned in the current period, or by delaying the posting of expenses or failing to fully account for company expenses or liabilities. Most of the accounting scandals beginning with Enron Corporation in the late 1990s are examples of moral hazard problems writ large created by incentive compensation plans designed to mitigate moral hazard behavior of company leaders!

Moral Hazard in Professional, or Agency, Relationships

Moral hazard problems can arise when one person contracts with another to act in his or her behalf or to make decisions or recommendations for him or her. For example, a person might hire a lawyer to represent him in court, a person might visit a physician because she is sick, or someone might take a car to a mechanic or call a plumber to fix a leaky facet. These arrangements are collectively referred to as principal-agent or agency relationships. Specifically, an agency relationship exists when one person, the principal, contracts with another person, the agent, to take some action on the principal's behalf. In the examples cited above, the lawyer, physician, mechanic, and plumber would be an agent of the person hiring them.

People usually contract with professionals because of the expertise they possess. Moreover, once the agency relationship is established, the agent might also acquire knowledge relevant to the principal. Unless the interests of the principal and agent are perfectly aligned, which rarely happens, the agent might have an incentive to use his private information unethically to benefit himself at the expense of the principal and others. For example, if a physician wants to minimize the possibility of being subjected to a malpractice suit, she may order more medical tests, prescribe more prescriptions, or recommend more extensive or expensive procedures than are medically necessary, resulting in higher medical expenses for the patient and his insurance provider. Similarly, lawyers and accountants might overcharge their clients, or mechanics and plumbers might recommend unnecessary repairs. These problems could be eliminated if agents adhere to ethical principles of personal virtue, honesty, the golden rule of behaving toward others as you would have them behave toward you, respect for the rights of others, compassion, and commutative justice by rendering nothing less than the service expected by the client.

As with all cases of moral hazard, the root cause of moral hazard problems arising in agency relationships such as these is the difficulty a principal has in monitoring the agent. If the principal can know what the agent does or can obtain the private knowledge possessed by the agent, then most moral hazard problems could be solved. There are many organizational and institutional innovations that have evolved to help with the monitoring problem. For example, patients obtain second opinions before consenting to a medical procedure recommended by a doctor or dentist. Law enforcement personnel, government regulators, and even journalists routinely inspect and report on the services provided by mechanics, plumbers, and other service professionals. In addition, many clients seek referrals from friends and associates, suggesting reputations are a means of mitigating moral hazard behavior. Clients who are dissatisfied with services provided will usually tell others or make reports to local business bureaus.

Moral Hazard in the Savings and Loan Industry

Like a bank, a savings and loan association accepts deposits from patrons and makes loans and other investments with the money. Unlike banks, savings and loans are restricted in the types of investments they can make; they are limited to making loans primarily for residential mortgages and commercial real estate investments. To compete with banks, which could offer more attractive savings rates because of their greater flexibility in making investments, savings and loans during the 1980s sought riskier, higher-yielding investments by investing in high-risk commercial real estate projects as well as corporate "junk bonds." In other cases, managers at savings and loans committed outright fraud in their accounting of deposits and loans. When the real estate market collapsed in the late 1980s, savings and loan associations that had been overly aggressive in their investing and financial accounting were forced to declare bankruptcy.

The cause of the savings and loan scandal was moral hazard created by the combination of federal deposit insurance and lax oversight of the investment and accounting behavior of savings and loan associations. Bank deposits are insured by the government by the Federal Deposit Insurance Corporation, and until 1990, deposits at savings and loan associations were insured by the Federal Savings and Loan Insurance Corporation (FSLIC). Banks generally enjoyed greater federal regulation of their activities to reduce the likelihood banks would have to require a deposit insurance bailout. Savings and loan associations were not as heavily regulated as banks, however. Because savings and loan associations felt pressure to find riskier investment opportunities to remain competitive with traditional banks, the combination of lax oversight and the presence of insurance for deposit holders gave managers an incentive to be overly aggressive in their business activities. The result was a classic moral hazard problem creating the following ethical dilemma for managers: They could have operated their businesses according to sound lending practices but at the risk of losing market share to banks, or they could have gambled to remain profitable. The outcome is now history. More than 500 savings and loan associations declared bankruptcy and turned to the FSLIC for relief. The FSLIC did not have sufficient reserves to handle the billions of dollars of liabilities the bankruptcies created, forcing the government agency to turn to taxpayers for relief and damaging the savings and loan industry.

—Harvey S. James, Jr.

See also Accounting, Ethics of; Adverse Selection; Agency, Theory of; Asymmetric Information; Commutative Theory of Justice; Conflict of Interest; Contracts; Enron Corporation; Free Riders; Opportunism; Savings and Loan Scandal; Trust

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Moral Imagination

The moral imagination is the mental capacity to create or to use ideas, images, and metaphors, not derived from moral principles or immediate observation, to discern moral truths or develop moral responses. Some defenders of the idea also argue that ethical concepts, embedded in history, narrative, and circumstance, are apprehended best through metaphorical or literary frameworks. A variety of thinkers have invoked conceptions of the moral imagination, including 18th-century writers and philosophers, as well as contemporary philosophers and business ethicists.

In his *Theory of the Moral Sentiments*, first published in 1759, Adam Smith described an imaginative process essential not only to understanding the sentiments of others but also to moral judgment. Through an imaginative act one represents to oneself the situation, interests, and values of another, generating thereby a feeling or passion. If this passion were the same as that of the other person (a phenomenon Smith refers to as "sympathy"), then a pleasing sentiment would result, leading to moral approval. As individuals across society engage their imaginations, an imaginative point of view emerges that is uniform, general, and normative. This is the viewpoint of the impartial spectator, the standard perspective from which to issue moral judgments.

Edmund Burke was perhaps the first to use the phrase, "moral imagination." For Burke, moral concepts have particular manifestations in history, tradition, and circumstance. In a passage in *Reflections on the Revolution in France*, published in 1790, he suggests that the moral imagination has a central role in generating and recollecting the social and moral ideas that, when crystallized into custom and tradition, complete our human nature, stir the affections, and connect sentiment with understanding. In the early 20th century, and with a nod to Burke, Irving Babbitt proposed the moral imagination as the means of knowing—beyond perceptions of the moment—a universal and permanent moral law. Assuming a distinction between the one and the many, Babbitt contended that the absolutely real and universal unity could not be apprehended; rather, one must appeal to the conceptual imagination to develop insight into stable and permanent standards to guide one through constant change. That the conceptual imagination might be cultivated through poetry, myth, or fiction was an idea of Babbitt later taken up by the traditionalist social critic, Russell Kirk.

In recent years, philosophers and business ethicists have shown a renewed interest in the moral imagination. Mark Johnson contends that moral understanding uses metaphorical concepts embedded in larger narratives and requires ethical perception. For example, ethical deliberation is not the application of principles to specific cases but involves concepts whose adaptable structures represent types of situations and modes of affective response. Furthermore, moral conduct demands that one cultivate one's perception of the particularities of individuals and circumstances and develop one's empathetic abilities. To these ends, literature has an essential role. In business ethics, Patricia Werhane has suggested that the moral imagination is necessary to ethical management. Beginning with the recognition of the particularity of both individuals and circumstances, the moral imagination allows one to consider possibilities that extend beyond given circumstances, accepted moral principles, and commonplace assumptions.

In general, and despite its varying and sometimes vague elaboration, the moral imagination has relevance for business practice. An imaginative capacity allows for the consideration of the effects of actions on multiple stakeholders, attuning managers, for instance, to the particulars of individual experience in the workplace. More generally, the moral imagination may reveal that business practices do not reduce to bare principle or pure theory but are embedded in history and society. Nonetheless, critical questions remain. Is the moral imagination merely an instance of the general ability to form new images and concepts? Does the contemporary appeal to the moral imagination allow for ethical objectivity? And can the moral imagination be cultivated only by first defeating the human propensity to center one's concerns on the self?

—F. Eugene Heath

See also Commonsense Morality; Ethical Decision Making; Humanities and Business Ethics; Ideal Observer Theory; MacIntyre, Alasdair; Rationality and Ethics; Smith, Adam

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Morality, Public and Private

Contemporary scholars such as Linda Treviño and Al Gini have studied the relationship between the private moral behavior of managers and their ability to satisfy their public moral responsibilities. On the one hand, it seems natural to hold that the moral standards used to evaluate an individual's private behavior ought to be separated from the standards used to evaluate one's behavior in professional roles, representing organizations with public stakeholders. On the other hand, this tendency to separate private from public moral evaluations raises some problems associated with the ways in which private conduct can interfere with the satisfaction of public responsibilities.

There are two reasons that are cited to justify the separation of private moral standards from those that are public. First, it is sometimes said that private conduct should not affect our moral assessment of the actions of individuals in their public roles. This is so because what one does in private is not necessarily related to what one does at work or in professional life. Second, public standards of conduct are neither reducible to, nor expressive of, standards of private moral conduct. This reason is less practical and more conceptual; it maintains that the actual content of public moral standards is distinct from the content of private moral standards, which are more parochial and reflect individual choice or tradition.

Separating private from public standards of morality assumes that we can differentiate private roles from public ones. What one does at home, the nature of one's familial or personal relationships, and one's religious affiliation are matters relating to private moral choice. These choices not only represent an individual's sense of self but also reflect the norms that an individual has implicitly and explicitly endorsed. These norms, in turn, indicate an individual's attitudes toward conduct such as sexual relations, truth telling, child rearing, alcohol consumption, and charity. They also convey more comprehensive convictions regarding things such as religion and spirituality. One's public identity, in contrast, involves the roles and responsibilities one assumes in representing or working for organizations that serve a broad range of stakeholders with divergent interests. As a civil servant, elected representative, or a manager of a corporation, one inhabits a public sphere, composed of a plurality of individuals and groups with sometimes different private moral commitments.

The fact that the members of a public organization do not universally share private moral convictions provides advocates of the separation thesis with good reason to avoid using private moral norms to evaluate the conduct of individuals in public life. Private moral norms are controversial, subject to protracted disagreement, and either irrelevant or ineffectual in accomplishing the goals of public organizations. Moreover, what individuals do in private, as a matter of personal choice, often has little impact on their ability to serve the public in their professional lives. Thus, it is natural to advocate standards of public conduct that express broad-based, publicly acknowledged values, such as fairness, honesty, trustworthiness, autonomy, impartiality, and welfare, rather than more parochial moral norms that proscribe a range of behavior that is not always relevant to fulfilling the roles and responsibilities of a public figure. This way of distinguishing private from public moral norms also implies that public organizations should not require individuals to set aside or unduly sacrifice their private moral convictions in assuming public roles.

The separation of private from public morality is open to some important qualifications and objections, both practical and philosophical. First, there are numerous situations when private moral conduct can affect the morally relevant interests of stakeholders in a public organization. Consider some of the issues related to drug testing in the workplace. The use of marijuana can be a thoroughly private choice, reflecting an individual's endorsed norms of behavior. When its use, however, begins to impair performance at work or poses risks to other employees, it begins to affect an organization's ability to operate for the welfare of its stakeholders. Accordingly, some organizations have implemented drug testing procedures to detect drug use and, if need be, terminate employees whose private decisions interfere with the welfare of others. A drug testing program that administers tests with just cause and offers due process to employees is a good example of how public moral norms take priority when found to be in conflict with norms of private behavior.

Even private behavior that has less obvious impact on the welfare of stakeholders has been a source of controversy in business. Harry Stonecipher, former CEO of the aerospace giant Boeing Company, was forced to resign his post in 2005 after it was discovered that he had an extramarital affair with a female manager. Although this manager was not his direct subordinate, Boeing's board asked for Stonecipher's resignation because if such conduct were to be publicly uncovered, it would reflect poorly on Boeing's commitment to high moral standards. One might say that this should remain a case where private conduct should remain private and not affect the board's assessment of Stonecipher's professional conduct; however, to the extent that the affair was internal to Boeing and could have jeopardized an already tenuous public perception of Boeing's commitment to high moral standards, the board felt strongly that Stonecipher could not effectively fulfill his responsibilities as CEO. This case illustrates the deep connection between private moral choice and its public implications.

Second, and more fundamentally, some authors have noted that private conduct is never easy to disentangle from the attitudes and behaviors exhibited in public. Robert Solomon, for instance, has argued that moral conduct in business depends crucially on the virtue of integrity, a kind of holism that unifies one's moral commitments in both private and public roles. This Aristotelian position finds moral character to be more seamless than the separation thesis would suggest; the decisions made by individuals in their private lives reflect how they respond to situations in public settings. Who one is in private affects who one is in public. One need only consult cases such as that of former Tyco International CEO Dennis Kozlowski to find anecdotal evidence that an individual's tendency toward excess in private life can thwart the moral aim of public organizations to improve the welfare of its stakeholders. Managers who are inclined to steal or be deceitful in their private lives are those who are comfortable doing so in their roles as managers. There are times and places where private moral attitudes facilitate (or impede) the realization of public moral norms.

—*Jeffery Smith*

See also Aristotle; Codes of Conduct, Ethical and Professional; Privacy; Public Interest; Tyco International

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Moral Leadership

Moral leadership in a business and society context involves directing corporate activities toward socially responsible ends. The premise for this type of leadership is that corporations are granted power and status in society because of their ability to serve the greater good. William Frederick conceives of this ability broadly as economizing and ecologizing, the former referring to the ability to efficiently convert inputs to outputs through competitive behaviors and the latter to forging cooperative, collaborative linkages with society that function adaptively to sustain life. Because the economizing function of the firm is widely recognized, executive managers are sometimes referred to as stewards of society's scarce resources, which are transformed into goods and services in the business sector, subject to government regulation and social norms. Given this role, Archie Carroll proposes that firms should first and foremost fulfill their economic and legal obligations to society while also attending to various stakeholder expectations of ethical conduct over and above the letter of the law. Moreover, corporations are increasingly expected to give back to society in the form of philanthropy or programs targeted for the betterment of community. The enactment of these forms of corporate social responsibility, sometimes referred to as "corporate citizenship," and the balancing of their tensions and trade-offs is largely under the influence of the executive manager or chief executive officer who sets the moral tone for an organization's conduct in society through his or her span of control over the formal and informal organization. In both equally important realms, the executive has access to several mechanisms for directing organizational conduct toward constructive social ends, beginning with the formal or structural organization.

Morally Leading the Formal Organization

The chief executive officer can guide a firm toward responsible corporate conduct vis-à-vis the formal organization by directing other managers along the chain of command structure to attend to concerns expressed by internal and external stakeholders, the former including employees and investors and the latter consumers, suppliers, the media, government agencies, and other groups in society that can affect or are affected by the firm's activities. The issues raised by these groups are often articulated in terms of moral expectations, as when employees claim the right to fair treatment, investors expect honest and transparent financial statements, consumers assert entitlements to safe products, and social activists exert pressure for sustainable business practices. If the executive manager establishes formal policies that direct other managers, especially those in the office of external affairs, to listen to, document, and attend to these concerns in a timely way, then it is possible for the firm to develop collaborative relationships with stakeholders instead of adversarial or neglectful postures. From this point of view, it can be said that moral leaders seek to ensure that firms perform their economic function in society while also addressing stakeholder issues efficiently and effectively so that the benefits of corporate impacts are maximized while harmful outcomes are prevented or minimized.

Some advocates of business social responsibility hold that executives who seek to maximize the benefits of corporate actions will also give back to community in the form of corporate philanthropy whenever possible, perhaps in collaboration with not-for-profit organizations. For example, executives might encourage employees to give to the local United Way while also donating corporate funds to that agency. A moral leader might also set a personal example of donating his or her time to not-for-profit community endeavors while encouraging other employees to do the same, perhaps by providing them with organizational incentives. Increasingly, such philanthropy is deemed strategic if it contributes not only to broad social goals but also to firms' long-run economic performance by enhancing corporate reputations and increasing community goodwill.

An organization's ability to respond to internal and external expectations of responsibility also depends on the executive's ability to direct employee behavior toward other constructive purposes, notably compliance with the law and important ethical norms that go beyond the law. The formal mechanisms available to executives include soliciting oversight from an ethics committee made up of board members and other senior managers and the services of an ethics officer and his or her staff in formulating and implementing legal and ethics compliance programs, ethics codes of conduct, hiring procedures that screen potential employees for ethical standards, and ethics orientation and training sessions. Another formal mechanism for encouraging desirable employee conduct is the implementation of an anonymous reporting system or ethics hotline by which workers can disclose their concerns—such as suspicions of unsafe products, dangerous work conditions, sexual harassment, or questionable financial accounting—with anonymity or due protection. If managers follow through by rectifying questionable practices or situations in a timely manner, then it is possible that some legal and ethical problems can be avoided or ameliorated while, at the same time, employee commitment to high moral standards is strengthened. Employing the services of an ombudsperson is yet another formal mechanism by which executives can signal that employee concerns will be dealt with objectively and ideally before ethical issues escalate into legal problems. Moral leadership might also involve participating in industrywide "best practices forums" aimed at establishing and maintaining collective ethical self-governance among peer firms. In terms of evaluation and control, executives may institute an ethics audit as a means for assessing the effectiveness of ethics programs, policies, and procedures and identifying deviations from established standards.

Morally Leading the Informal Organization

Formal programs can be viewed as ineffective or as "window dressing" if employees are not convinced of upper management's commitment to moral leadership. Such commitment or lack of it can be evident in a firm's informal organization or culture. In fact, Edgar Schein asserts that the most important thing a leader does is to create and manage organizational culture, which he or she defines as a system of shared assumptions and beliefs, often taken for granted, and based on learned products of group experience. This learning ultimately reflects values or beliefs about what employees "ought to do." According to Schein, the organization's founder can significantly affect these beliefs by embedding certain values in the culture early on. Moreover, Schein identifies five primary mechanisms that the executive manager has access to for shaping and reinforcing culture on an ongoing basis: (1) what he or she pays attention to, measures, and controls; (2) how he or she reacts to critical incidents and crises; (3) his or her deliberate role modeling, teaching, and coaching; (4) his or her criteria for allocation of rewards and status; and (5) his or her criteria for recruitment, selection, promotion, retirement, and excommunication. While these mechanisms are often expressed formally, they can be more powerful informally in that employees ultimately learn what behavior is expected of them by what leaders do, not simply by what they say or endorse as formal statements, policies, programs, and procedures.

For example, if the formal corporate code of conduct stresses honesty, but the chief executive officer models unethical behavior or attends to, mentors, promotes, and rewards employees known for shady or nontransparent dealings, then the unspoken message to employees is that honesty is not really valued in the culture. Accordingly, formally espoused programs, policies, and procedures advocating honesty will likely be "decoupled" from actual behavior, meaning that the executive will actually encourage the development of a culture marked by dishonesty and a lack of transparency. The ideal scenario in terms of moral leadership is for executives to use mechanisms for shaping and reinforcing cultures that establish and maintain an organization's ability to respond affirmatively to stakeholder expectations of corporate social responsibility while directing employees to enact conduct befitting such an organization and providing them with a personal model or example of such behavior. Theoretically, the resulting type of organization can be described in terms of two ethical climates: benevolence or concern for others and integrity or adherence to principled rules and procedures.

Some Proposed Attributes of Moral Leadership

Although there is no one generally accepted theory of moral leadership, there is a preponderance of research suggesting that moral leaders inculcate or exhibit certain attributes. Some of this literature emphasizes the importance of other-regarding behavior in lieu of self-aggrandizement. For instance, decision making based on the felt sentiment of helping others first is the basis for servant leadership, which would seem to be a particularly fitting motivation for executives who lead corporations in philanthropic efforts aimed at the betterment of community. Another perspective based on Lawrence Kohlberg's model of moral development suggests that managers capable of articulating and defending their decisions in terms of what is good for society as a whole while applying principles of justice, rights, and social welfare universally to others exhibit the highest level of moral reasoning and, by extension, are capable of moral leadership in action. Virtue ethics implies that moral managers are those who have imbibed certain character traits, such as fairness, honesty, and benevolence, while the literature on integrity suggests that moral leaders are able to use such characteristics coherently to establish publicly their trustworthiness and ability to make balanced judgments in the face of moral complexity. According to a dialogic perspective, this ability depends partly on being able to respect, listen to, and give voice to various stakeholder concerns. In a similar vein, other research emphasizes that a necessary condition for moral leadership is the cognitive ability to factor values and ethics consciously into decision making.

—Diane L. Swanson

See also Business, Purpose of; Chief Executive Officer (CEO); Codes of Conduct, Ethical and Professional; Corporate Citizenship; Corporate Ethics and Compliance Programs; Corporate Philanthropy; Corporate Social Responsibility (CSR) and Corporate Social Performance (CSP); Corporate Social Responsiveness; Economics and Ethics; Employee Relations; Ethical Culture and Climate; Ethical Role of the Manager; Integrity; Kohlberg, Lawrence; Leadership; Management, Ethics of; Ombudsperson; Other-Regardingness; Servant Leadership; Stakeholder Responsibility; Virtue; Virtue and Leadership

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Moral Luck

Moral luck seems to appear when circumstances beyond a person's control influence our moral attributions of praise and blame. For example, consider the apparent role of moral luck in some of the worst failures in corporate history. If not for a run-up in resource prices, corrections for overpriced technology stocks, and the specter of terrorism, they might never have occurred. Deceptive accounting, employed to give the illusion of steadily increasing profitability, might have been unwound. It is possible, if not probable, that such improprieties occur with some regularity in more forgiving external circumstances, rendering them almost harmless. One executive, imprudent though fortunate, presides over relatively inconsequential misconduct. Is this executive any less blameworthy than another, whose similar inattentiveness is exacerbated by chance circumstances beyond the executive's control, resulting in corporate failure, unemployment, and loss of investor capital? Both executives may be held formally responsible for their action or inaction, but only the latter becomes the object of public disgrace and faces comparatively severe legal charges. How is it possible to reconcile the widely shared intuition that morality and moral judgments involve responsibility for our own actions with the undeniable fact that the moral life is vulnerable to luck for which we cannot be held responsible?

Types and Illustration

That there could be such a thing as moral luck challenges modern moral theory, which has tended to characterize morality as immune to luck. The claims that goodwill is independent of worldly contingencies, and that moral worth depends solely on the volition of an autonomous moral agent, have been attributed to Kant. The associated belief that moral value is wholly within our control, such that neither good fortune can augment it nor misfortune can take it away, is widely held among laypersons and moral theorists alike. Thus, when Bernard Williams coined the term *moral luck*, he expected it to be perceived as a contradiction in terms that threatened the modern conception of morality as a unique and supreme form of value. Aristotelian ethics, by comparison, has been characterized as more accommodating of the vulnerability of the good life to factors beyond our control, sensitive to the ways in which reversals of external fortune, and even internal human irrationality, may inhibit our ability to pursue the good life or to introduce conflicts of values that make a good choice impossible. Despite the perceived contrast between Kantian and Aristotelian ethics, it has been asserted that both theories recognize the problem of moral luck and the associated difficulty of reconciling attribution of moral responsibility with recognition of the influence of luck on human life.

Thomas Nagel distinguishes between four types of moral luck, none wholly within human control, which influence our own and others' judgments about persons' moral decisions and character. To illustrate them, consider the case of a pharmaceutical executive, deliberating whether and how to allocate resources to develop a potential cure for a disease whose victims may be unable to pay for it. Constitutive moral luck—who we are as a function of our natural makeup—arises in that the choice for this executive appears because it is in the natural makeup of a pharmaceutical company to have the capacity to produce treatments for disease. Circumstantial moral luck—the situations that chance introduces that bring about moral challenges—arises because the opportunity to develop a cure comes from the presence of the affliction and the chance that this company may have a research advantage on this type of disease. Causal moral luck—the antecedent circumstances that may determine who we are and the decisions we make—arises when an unexpected discovery in the research laboratory leads a research scientist to present the executive with the case for a possible cure. Finally, resultant moral luck— the consequences of our decisions and actions—will arise after a decision has been made about whether to go ahead with research and development. The outcomes subject the executive and the company to moral praise or blame, depending significantly on whether the drug is or might have been successful and accordingly how shareholders perceive the use of their capital.

The foregoing examples illuminate why the problem of moral luck may be particularly relevant in business. The moral judgments at issue are not purely about whether the executives are good or bad people or made good or bad choices. More salient to the professional environment, they are about whether the executives should be praised or blamed—and how their decisions should be justified, rewarded, or punished—if they cannot be held wholly responsible for the conditions that influenced their choices. How they are judged is critically important, in that success can bring benefits in the form of enhanced personal and company reputation and consequently shareholder value, whereas failure may potentially contribute to adverse market consequences and even formal sanctions. Business ethics is inevitably tied to monetary, legal, and other ramifications that involve judgments on the part of investors, legal officials, and other stakeholders about the degree to which a party should be held responsible for decisions and outcomes.

Responses to the Problem

On one hand, it would seem unfair to hold individuals fully responsible for their moral choices when they are not responsible for many of the conditions influencing those choices. On the other hand, some commentators have gone so far as to claim that accepting the existence of moral luck implies acceptance of determinism, in which case we could not hold individuals responsible for their moral choices at all. Williams and Nagel conclude that moral luck is an unresolved, and perhaps insoluble, problem for modern moral theory. We may want and expect our moral judgments to be unadulterated by seemingly irrelevant luck, and yet we cannot deny that almost nothing a person does, moral or otherwise, is wholly within that person's control.

Those unwilling to accept this conclusion have attempted to reject the problem by claiming the following:

- Our intuitions are philosophically mistaken: It is true that our moral judgments often fail to separate luck from that for which the moral agent is directly responsible. However, if we were sufficiently reflective, we would adjust our moral judgments to factor out luck.
- Our intuitions are psychologically mistaken: Our willingness to morally blame others for the bad outcomes of their negligence is based on an unjustifiable psychological bias that our own negligence will not produce similarly bad outcomes and that we are not similarly subject to moral blame. If we recognized and shed this bias, we would reject the problem.
- Moral luck is incoherent: It does not make sense to characterize our identity as subject to (constitutive) moral luck. To exempt individuals from moral praise or blame because they do not have control over some elements of who they are involves a category mistake, because those elements that may be outside of an individual's control are nevertheless a part of that individual's self as a moral agent subject to moral praise and blame.

Anticipating some of these challenges, Nagel says that our supposedly mistaken intuitions return involuntarily, again and again, despite our attempts to rationalize them away.

Why should we be content to leave the problem of moral luck unresolved? For Williams, part of the answer is that our very identity depends on a web of interaction between that which is within and outside of our control. Those who would wish to set aside moral value as a special kind of value that is uniquely immune to factors beyond our control are left with a sterile moral core that reflects none of the human variety arising from our chance of interactions with the world. Although luck can be an obstacle to the good life, Martha Nussbaum attributes to Aristotle the observation that features of the good life are also dependent on it: health, friends, loved ones, emotion, and compassion, among others. The existence of moral luck may complicate our capacity to make moral judgments, because we cannot separate morality from who we are, what we experience, and cause and effect. In short, moral luck challenges the supposed distinction between the moral and the nonmoral. But the problem of moral luck valuably teaches us to look at morality from the perspective of a long-term moral investor, who examines moral decision making in the particular context of its surrounding conditions while evaluating morality in the general context of the decision maker's complete life.

—Christopher Michaelson

See also Aristotle; Commonsense Morality; Enron Corporation; Kant, Immanuel; Merck & Co., Inc.

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Moral Point of View

The moral point of view is the impartial, universalizable perspective that each person is capable of assuming. Here the term *person* is used in a technical sense to denote rational, self-governing being. When we take the moral point of view, we seek to adjudicate disputes rationally, we assume that other persons are neither more nor less important than ourselves, and we assume that our own claims will be considered alongside those of others in an impartial manner. These three components of the moral point of view are respectively concerned with rationality, universalizability, and impartiality.

The moral point of view is *rational* in the sense that it involves the application of reason rather than feeling or mere inclination. Moral issues frequently invoke a strong emotional response in individuals. The attempt to justify a moral stance by appeal to reasons that may be considered and evaluated by other persons facilitates a process whereby individuals with distinctly different emotional responses to a moral issue may seek mutual understanding and, perhaps, agreement. In business, the fact that one person wields more economic power, for example, than another person cannot by itself outweigh the needs for both parties to offer a rational basis for their competing moral perspectives.

The moral point of view is *universal* in the sense that the principles or propositions ascertained therefrom apply to all persons and to all relevantly similar circumstances. Thus, if a moral principle or proposition is valid, no persons are exempt from its strictures. The notion of universalizability has particular relevance in the era of economic globalization. It requires that we regard all persons as equal in dignity and as such that we respect them in our business dealings wherever they may live or work.

The moral point of view is *impartial* in the sense that principles or propositions ascertained therefrom apply to persons irrespective of arbitrary considerations. This impartiality may involve the application of a specific principle that purposively ignores the circumstances of individual lives, or it may involve an unbiased evaluation of the particular reality of individual persons and an assessment of the needs and preferences of individual persons in light of the needs and preferences of others. In any case, it requires that characteristics such as a person's race, sex, nationality, and economic circumstances, for example, cannot be regarded as a legitimate basis for treating persons differently than other persons when there are no good reasons for thinking such considerations relevant. Impartiality is especially important in human resource management, where such considerations may interfere with the fair evaluation of employees and with their promotion or dismissal.

It is important to note that the moral point of view does not exclude partiality. Favoring the interests of one party over another is justified when there are overriding reasons for ranking the specific interests of one party over another. This is especially so when one has familial, professional, or contractual responsibilities. This point is of obvious relevance to business managers who have distinct moral and legal obligations to their employers. The challenge of the ethical manager is to determine when the interests of his or her employers trump those of other stakeholders and when the interests of those stakeholders override the interests of his or her employers.

The idea of the moral point of view may seem commonplace, but it is an idea with deep theoretical foundations. In the 18th century, Immanuel Kant, the great Enlightenment philosopher, argued that one should always treat other persons as an end unto themselves and never as a means only. Persons are free and rational creatures, and as such, argued Kant, all persons have intrinsic value that must be respected. This means that the desires, goals, and aspirations of persons other than ourselves must be given due consideration. Kant did not merely assert that persons are entitled to due consideration, but he provided a compelling argument for that conclusion. The interests of all persons ought to be given due consideration because persons have dignity. For Kant, a being that has dignity is beyond price. Persons have a dignity that mere objects lack. They have dignity because they are autonomous, responsible beings capable of rational activity; in other words, they are moral beings. Reason requires that any moral principle must be rational in the sense that it is universal. The fact that persons have this capability means that they possess dignity. As a matter of consistency, anyone who recognizes himself or herself as a moral being must ascribe dignity and accord due respect to anyone who, like himself or herself, is a moral being.

The capacity to act from the moral point of view differentiates persons from nonhuman animals and causes persons to be morally responsible for their actions. Anyone can forsake the moral point of view in the interest of the pursuit of profit. However, one who does so acts more like an animal than like a person. The ethical manager is one who makes a profit while acting from the moral point of view.

—Denis G. Arnold

See also Autonomy; Dignity; Duty; Ideal Observer Theory; Kantian Ethics; Moral Agency; Moral Imagination; Moral Reasoning; Universalizability, Principle of; Utilitarianism

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Moral Principle

Moral principles are general statements that provide guidance in evaluating the moral appropriateness of past or future actions, general categories of behavior, individual character, and social and political institutions. A distinctive feature of moral principles is their intended aim of providing *practical* guidance. Principles direct or obligate moral agents to *act* or *respond*, either in general ways or in concrete situations where certain circumstances obtain.

Moral principles take various forms and vary in the type of practical guidance that they provide. The principle that one should "do no harm to others" functions as a *general proscription* covering a wide range of activities from how one ought to treat their neighbor to how much a manufacturer should invest in product safety. Although formally similar, *general prescriptions* establish conduct or arrangements that ought to be pursued as opposed to avoided. The principle "negotiate in good faith" instructs agents to exhibit transparent intentions when they choose to engage in negotiated agreements. Other principles function less like general recommendations or prohibitions and more like *statements of conditional obligation.* The principle that "No one should profit from wrongdoing" is an example of a principle that specifies the conditions under which it is permissible to pursue certain activities, for example, profit seeking, and, implicitly, when it is unacceptable to do so. Finally, moral principles can also take a *procedural* form when they specify how individuals or organizations should go about responding to certain types of problems. The oft-cited *Principles of Stakeholder Management* authored by the Clarkson Centre of Business Ethics provides a good illustration of this approach to principled moral thinking. The Clarkson *Principles* put forth a number of practical recommendations that do not endorse or prohibit specific kinds of action but indicate the methods that managers ought to use to go about addressing moral problems. For instance, principles such as "Managers should openly communicate with stakeholders about their respective concerns and contributions" and "Managers should work cooperatively with other entities to ensure that harms arising from corporate activities are minimized" are essentially procedural in that they focus a manager's attention neither on specific outcomes nor types of behavior; rather, the principles recommend methods of responding that are intended to generate morally acceptable managerial decisions, whatever those may turn out to be.

The intended generality of moral principles makes their application in concrete circumstances a challenging task. To receive practical guidance from principles, agents need to engage in an elaborate process of judgment whereby the particularities of a specific circumstance are assessed in relation to the semantic content of a principle. The Clarkson *Principles* state that managers should distribute the benefits and burdens of corporate activity fairly among different stakeholders. To apply this principle in a specific circumstance, for example, in dealing with wage and benefit cuts for employees, an agent would need to address an array of pertinent questions. What are the unique burdens experienced by this group of employees? Are these risks in proportion to the benefits they have historically received? What trade-offs with other stakeholders need to be made if no wage and benefit cuts are made? What is a fair distribution of benefits and risks given that these employees have voluntarily accepted their position? Prior experience and sensitivity to all relevant facts help address these questions and, ultimately, enable a judgment about what changes to wage and benefit policies are called for by the principle.

Principles provide what some have called reasons to act in certain ways. Inevitably, however, principles may conflict with one another, specific circumstances may provide exceptions to the recommended course of action, and the principle itself may simply underdetermine possible responses in specific cases. The application of principles through the exercise of judgment is something that has prompted ethicists to emphasize that moral principles, while important in justifying particular moral decisions, do not determine with any precision what ought to be done in specific cases. This line of thought owes much of its history to the ancient Greek philosopher Aristotle who famously remarked in his *Nicomachean Ethics* that principles are only mostly true. Moral principles are therefore contrasted with moral rules that do purport to give exact, unambiguous guidance in specific circumstances.

—*Jeffery Smith*

See also Aristotle; Casuistry; Clarkson Principles for Business; Codes of Conduct, Ethical and Professional; Moral Imagination; Moral Reasoning; Moral Rules

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Moral Realism

Moral realism is the metaethical view that there are moral facts and moral properties and that the existence of these facts and instantiation of these properties is essentially independent of any subjective stance. This view commits moral realists to three logically independent theses. Moral antirealists deny one or more of these theses.

First, moral realism is a form of *cognitivism.* Cognitivism is the view that moral judgments express beliefs that are capable of being true or false. Realists see moral judgments as beliefs that are true or false depending on whether they accurately represent moral facts. In contrast, *noncognitivists* (expressivists) maintain that the function of moral discourse is either to express the affective states—such as the emotions or desires—of the speaker and to persuade others to share them (emotivism) or to prescribe universal rules of conduct (prescriptivism). Noncognitivists deny that there are moral facts against which the truth of moral judgments can be checked and that there are moral properties that determine the moral qualities of persons and actions. Moreover, since the noncognitive states that are expressed by moral judgments themselves have no truth-value, moral judgments are not capable of being true or false.

Second, realism is a *success theory.* Realists maintain not only that moral judgments are beliefs possessing truth-values but also that some of these beliefs are true in virtue of correctly reporting moral facts. Advocates of the so-called error-theories, such as J. L. Mackie, are cognitivists—they agree that moral judgments are beliefs possessing truth-values; however, they maintain that *all* moral beliefs are systematically and uniformly *false.* This is because they deny that there are moral facts or properties of the sort required to render our moral judgments true. Moral discourse, on this view, rests on a colossal error; it presumes the reality of certain facts and properties that simply do not exist.

Third, realism entails a form of *objectivism.* Objectivism here is the view that moral facts are essentially independent of any subjective stance and that moral properties such as goodness and rightness can be explained without any essential reference to what any (real or hypothetical) moral agent or agents approve of, desire, would assent to under certain conditions, and so on. Realists believe that moral judgments are true or false independent of what anybody thinks of them. *Moral constructivists*, in contrast, maintain that the moral domain *is* constructed out of the subjective stance of some (real or hypothetical) moral agent or agents, and, hence, the truth conditions of moral judgments *do* essentially depend on that subjective stance. Different normative and metaethical theories, each committed to a constructivist account of morality, hold opposing views about what the proper subjective stance is: Egoism claims that morality is constructed out of individual attitudes or preferences, contractarianism out of the principles endorsed by deliberators situated in special circumstances of choice, ideal observer theories out of the responses of a suitably characterized ideal observer, Kantianism out of the pronouncements of the rational will, relativism out of the conventions of social groups, and so forth. Realists and constructivists both endorse the reality of moral facts and properties; they disagree about whether these facts and properties are essentially independent of a subjective stance. *Moral nihilists* deny the existence of moral facts and properties altogether.

Realists disagree about whether the view is best construed as a form of ethical naturalism or nonnaturalism. *Naturalists* claim moral properties are natural properties—properties that figure in the natural or social sciences. Moral facts and properties, according to naturalists, fit within an ontology whose contents are fixed exclusively by the outcomes of scientific investigation. Reductive naturalists (e.g., Peter Railton) claim that moral properties are reducible to other natural properties that are the subject matter of the sciences. Nonreductive naturalists, such as the "Cornell realists" (e.g., Richard Boyd, David Brink, and Nicholas Sturgeon), deny that moral properties are reducible to any other natural properties, but argue that moral properties are natural properties in their own right.

Nonnaturalists (e.g., Jonathan Dancy, John McDowell, G. E. Moore, Russ Shafer-Landau, and David Wiggins) see moral facts and properties as different in kind from natural facts and properties. Nonnaturalists maintain that moral properties are irreducible and *sui generis.* This commits nonnaturalists to a more complex ontology, admitting (at least) two kinds of properties—natural and moral—and, hence, (at least) two kinds of facts.

Arguments for Realism

Realists employ three complementary strategies in defending their view: offering positive considerations on behalf of realism, offering criticisms of antirealist views, and responding to objections designed to undermine realism's plausibility. This section reviews two arguments employing the first and second strategies, the first directed against noncognitivism and the second against constructivism.

The Argument From Moral Phenomenology

Realists argue that their view comports well with commonsense moral phenomenology, whereas noncognitivism requires very serious revisions to our understanding of what occurs when moral agents engage in moral deliberation, argumentation, and judgment.

We ordinarily talk of moral truths, taking at face value judgments such as "It is true that deliberate cruelty is morally wrong," and we regularly attribute moral beliefs to agents. We issue moral judgments in the indicative mood, assuming that moral predicates are meaningful and can be used to describe the subjects of which they are predicated. We also think that we can err about our moral beliefs; hence, we engage in deliberation and argumentation about moral matters, which takes the same logical form as other kinds of argument and appears to be an attempt to determine a matter of fact. All this is in perfect accord with realism, but none of this would make sense if noncognitivism were true.

The Argument From Arbitrariness

Realists argue that fixing moral truths relative to a subjective stance makes morality arbitrary in an unacceptable way. Some metaethical views aligned with constuctivism (e.g., relativism) and some normative theories that are species of constructivism (e.g., egoism) maintain that moral truths are fixed by the *actual* attitudes of certain subjects. But these attitudes, realists point out, often conflict with deeply held moral convictions. Other normative theories that are species of constructivism (e.g., contractarianism, ideal observer theories, and Kantianism) sidestep this difficulty by requiring some form of idealization for the subjective attitudes that go toward fixing moral truths. But these theories, realists argue, face a dilemma: Either the conditions defining idealization are moralized or they are not. If they are moralized, then these theories really abandon constructivism, since they acknowledge the existence of moral principles that are conceptually and ontologically prior to the construction process. If they are not moralized, then, once again, it is unclear why the outcomes of the construction process should be definitive of morality.

Arguments Against Realism

Antirealists challenge realism on metaphysical, epistemological, and psychological grounds. This section rehearses a few classic antirealist arguments and indicates some lines of response developed by realists.

The Argument From Disagreement

The antirealist argument from disagreement is premised on the existence of widespread, intractable interpersonal and intercultural moral disagreement. Antirealists argue that moral disagreement is more readily explained by the hypothesis that moral judgments are subject dependent than by the hypothesis that they are attempts to express objective truths. Moral antirealists often contrast the degree of consensus within the natural sciences and moral inquiry. Scientific inquiry has generated a substantial degree of consensus, supporting the claim that there are scientific facts. Pervasive moral disagreement is good evidence for thinking that, in contrast, there are no such moral facts.

Some realists challenge the evidence as presented, pointing out that there really is significant moral consensus within and across societies and that the scientific community itself is deeply divided on certain matters. Realists also argue that a great deal of moral disagreement arises from disagreement about *non-moral* facts or errors in reasoning. Other realists accept the evidence as presented, but challenge the inference to antirealism. Many realists argue that there are salient differences between moral and scientific inquiry, which explain why there is more widespread disagreement in the former. For example, moral judgments, unlike scientific judgments, are overtly normative; consequently, they can threaten our self-interest and ideological commitments in ways that scientific judgments do not. Realists also note that moral disagreement is characteristic of the type of disagreement found in philosophy more generally, but this disagreement is not thought to imply that there are no facts of the matter about various philosophical issues. For example, persistent disagreement between theists and atheists is not thought to entail that there simply is no fact about whether God exists.

The Argument From Queerness

J. L. Mackie's antirealist argument from queerness has two parts: one metaphysical, the other epistemological. Mackie argues that if there were moral facts and properties, then they would be very queer things, utterly different from the ordinary facts and properties that we encounter in our everyday experience. Plato's Forms, Mackie suggests, give us a dramatic picture of what objective values would be. They would be sui generis entities: facts or properties such that the mere apprehension of them by a moral agent would necessarily supply both a reason for action and sufficient motivation to act. Ordinary facts are not intrinsically action guiding in this way, they are normatively inert.

Moral facts and properties would be so metaphysically anomalous, Mackie concludes, that we have good reason to reject realism. Mackie's corresponding epistemological worry is that if we were to be aware of moral facts and properties so construed, then it would have to be by way of some special faculty of moral perception or intuition, which, again, would be utterly different from our ordinary ways of knowing everything else.

Realists respond by challenging one or more of Mackie's assumptions about the nature of moral facts and properties. Naturalists reject the assumption that moral facts and properties would have to be sui generis*:* They claim either that moral properties are identical to certain natural properties or that moral properties supervene on certain natural properties. Both naturalists and nonnaturalists have denied Mackie's assumption that moral facts or properties must be intrinsically action guiding.

The Argument From Explanatory Necessity

Like Mackie, Gilbert Harman argues that we have good reason to exclude moral facts and properties from our ontology. Harman maintains that we are justified in postulating a type of fact or property to the extent that it is required to explain what occurs in the world. Scientific facts play just this sort of explanatory role. For example, consider a physicist who, seeing a vapor trail in a cloud chamber, immediately judges that a proton has passed by. The best explanation for the physicist's observation requires the assumption that a proton really did pass by; hence, we are justified in postulating proton facts. Harman asks us to contrast this case of scientific judgment with a case of moral judgment. Consider someone who, seeing a group of hoodlums pour gasoline on a cat and ignite it, immediately judges that the action is morally wrong. Harman argues that a full explanation of the appraiser's judgment does not require any assumptions about moral facts, such as that deliberate cruelty is really wrong: A complete explanation requires only assumptions about nonmoral facts—most important, natural facts about the appraiser's psychology. Harman concludes that moral facts and properties are explanatorily superfluous, so that, barring their reduction to respectable nonmoral, scientific facts and properties, there is simply no justification for postulating moral facts and properties.

Some realists reject Harman's methodological constraint, denying that explanatory necessity is the test of existence. Other realists accept this constraint, but argue that moral facts and properties *do* frequently play an ineliminable role in the explanation of actions and beliefs. For example, the fact that Hitler was morally depraved explains (in part) his actions. The realist argues that it is false that if Hitler were *not* morally depraved, then he still would have acted precisely as he did. That this counterfactual is false indicates that the putative moral fact does play an essential explanatory role.

The Argument From Moral Motivation

A long-standing objection to realism is that it cannot account for moral motivation. The argument underlying this objection runs, in short: Necessarily, moral judgments motivate; but beliefs by themselves cannot motivate; hence, moral judgments cannot be beliefs. The first premise expresses motivational judgment internalism—the view that, necessarily, if one sincerely judges an action to be right, then one is motivated (to some extent) to act in accordance with that judgment. The second premise is an implication of the Humean theory of motivation, which holds that motivation requires *both* beliefs and desires. The conclusion is a statement of noncognitivism and, hence, entails antirealism. Noncognitivists point out that their view can easily account for moral motivation, since they take moral judgments to be expressions of noncognitive states that are essentially motivating.

Realists reject one (or both) of the argument's premises. Realists rejecting internalism opt for externalism—the view that the connection between moral judgment and motivation is not conceptual and necessary but only contingent. These realists argue that the amoralist—an individual who endorses the rightness of an action without thereby being motivated to perform it—is conceptually possible. Realists advancing an anti-Humean theory of motivation reject the argument's second premise, arguing that some beliefs are sufficient by themselves to motivate.

—Michael B. Mathias

See also Cognitivism and Ethics; Ethical Naturalism; Ethical Nihilism; Intuitionism; Metaethics; Nihilism; Noncognitivism; Relativism, Moral

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Moral Reasoning

Moral reasoning is a form of practical reasoning wherein one attempts to give or find reasons for morally approving or disapproving actions. All reasoning involves premises that lead to a conclusion. A premise is a judgment, expressible in a statement, which contains two elements. The first is the subject, and the second is what logicians call a predicate. The predicate is what is asserted about the subject. There are two types of reasoning, practical and theoretical, and they each have their own characteristics. In theoretical reasoning one "argues" from two descriptive premises such as "All humans are mortal" and "Socrates is human" to a descriptive conclusion "Therefore, Socrates is mortal." However, the practical syllogism, as Aristotle noted, is an argument whose conclusion recommends an action or at least provides a judgment that a certain action ought to be performed. Furthermore, one of the premises is usually a value or attitudinal judgment (normative), while the other is a definitional or factual judgment. For example, Peter either pays Paul more or thinks he should pay Paul more (conclusion) because he thinks paying a pittance is unfair (value judgment), and he is paying Paul a pittance (definitional or factual depending on the criteria of pittance). So the practical reasoning either leads to the action of Peter paying Paul more or at least the assertion that Paul should be paid more.

Human Actions

The primary subject matter of our ethical judgments and hence of moral reasoning is deliberate human actions. While human actions are the subject of practical reasoning, not all human actions are subject to *moral* reasoning because some human actions lack ethical or moral import. One can deliberately decide to wear a red rather than a blue tie or to eat mashed potatoes with one's fingers, but these actions do not have ethical import. They do, however, involve aesthetic considerations about what kind of tie goes with what shirt or etiquette decisions about the propriety of eating potatoes with one's fingers. To have moral import, an action must involve harming or helping another person or oneself. This harm may be serious or not so serious as is recognized in religions with the distinction between mortal and venial sins and in law with the distinction between degrees of homicide or petty and grand larceny, or crimes and misdemeanors.

Moral reasoning in this framework is the activity of evaluating the moral rectitude of human actions. We perform the evaluation by giving reasons in support of or against the actions. Since moral judgments are normative, they involve dealing with values, emotions, desires, and subjective preferences. Because of these subjective and emotional elements many argue that ethical reasoning is personal and that each individual's judgment merely expresses one's feelings about certain actions and cannot be validated rationally (see subjectivism). However, it seems impossible for human beings not to judge, and sound judgment requires sound reasoning.

Justifying Reasons

Taking a commonsense point of view toward ethical reasoning provides a perfectly straightforward procedure for evaluating moral actions—investigate whether there are any *good reasons* in support of an action or whether there are reasons against such an action. Consider how one would usually handle a situation where someone on whom one was depending breaks his or her promise. For example, suppose one had a commitment from a subcontractor to do a job on a certain date and the contractor calls to say he or she won't be there. The normal response is, "You promised." Suppose they reply, "So? I just don't feel like keeping my promise." Not feeling like keeping a promise is not a *good reason* for breaking it. Promises after all are made precisely because people might not feel like doing what they promised to do. We expect promises to be kept, *unless there is a good reason not to.* If everyone always felt like doing what one promised we wouldn't need promises.

Suppose, however, that the subcontractor replies, "I can't be there because I was just in an accident." Since "ought" implies "can," that is a good reason for not keeping the promise. Another good reason for breaking the promise might be that he or she just discovered that to do the job would violate EPA regulations. Thus, the belief that he or she was not obliged under those circumstances to keep his or her promise may be justified. Furthermore, it may be the case that one is also obliged to release the subcontractor from his or her promise. Justification is the process of giving reasons for doing something. Moral reasons are used to justify moral judgments as observation is used to justify factual judgments.

The Moral Reasoning Process

Moral reasoning occurs when the following basic questions are asked about an action:

- Is the action beneficial for the actor or society? The primary rule of ethics is "Do good and avoid harm."
- Is the action fair or just? The principle of justice, which logical reasoning requires us to recognize, is that the same (equals) should be treated the same (equally). Of course, there is often disagreement about who and what are equal, but unless there is some relevant difference, all persons should be treated equally.
- Has an explicit or implicit commitment been made? This question asks if any promises to perform a proposed action have been made. Since any lasting relationship rests on implied promises and expectations of guaranteed behavior in spite of the contingencies of the future, that relationship contains an implied promise that should be kept. Since professional roles involve implied promises, this provides a ground for the obligation to fulfill one's role.

An example from a business context can show how this reasoning process operates. If an individual is planning to produce some commodity that brings a profit to the company, a commission to that person benefits society and doesn't in the process treat anyone unfairly or violate some promise or commitment, there are none but good reasons in support of it and it should be done. However, if that person is tempted to falsely declare profits in a financial statement developed for a merger, and he or she sees (1) that it is not beneficial to the company, its executives, or the general society; (2) that the action would be deceptive and hence unfair; and (3) that it would violate the relationship of trust that one's corporation has with the community, there are only reasons against performing the action.

This model of moral reasoning provides a decision procedure for determining what to do and what not to do. Ask the questions of common morality. If there are good reasons for performing the action such that it benefits an individual, and society, and does not violate justice or a commitment, do it. If on the other hand an action does not benefit society or an individual, is unfair, and requires breaking a commitment, then do not do it.

Moral Reasons and Ethical Theory

The reasons we have just examined not only constitute the common rules of morality, they underlie most of current ethical theory. Ethical theory is theory about which kinds of reasonings are definitive in the face of an ethical dilemma—a situation that arises when there is a good reason in support of the action and a good reason against the action. Ethical theories are the court of last resort, and each provides an overriding principle to be used in resolving a conflict of reasons. Hence, an *ethical theory prescribes* a principle that provides the overriding justifying reason for pursuing any course of action. In contemporary thought, there are two main theoretical approaches—consequentialist and principled.

Utilitarianism is a consequentialist approach that maintains that "those actions should be done that bring about the greatest good for the greatest number of people." Producing good is the basic reason for justifying an action or practice. The principled approach is called a "deontological" approach. Deontological theory gives precedence to considerations of fairness, rights, and commitment over consequentialist reasoning and claims that the "End (read consequences) doesn't justify the means."

In many situations, there is no conflict of reasons and what is good for an individual is also good for society while also being fair and in accord with one's commitments. At these times, we have every reason to perform an action and all the competing theories' principles would be fulfilled. But in cases where there are conflicting reasons, dilemmas can result and there can be dramatic disagreement about which principle to follow and which reason takes precedence.

Utilitarianism

The principle maxim of utilitarianism was best expressed by John Stuart Mill. "Actions are right in proportion as they tend to promote happiness, wrong as they tend to produce the reverse of happiness." In asserting this proposition, Mill was arguing against those who gave primacy to self-interest, the egoists (see Egoism). Mill claimed that "the happiness" is "not the agent's own greatest happiness, but the greatest amount of happiness all together." A recent formulation of utilitarianism reads, "Do that action that will bring about the greatest good for the greatest number of people," and in this and other formulations, utilitarianism uses a cost-benefit approach.

A major problem facing utilitarians is what counts as good. John Stuart Mill and Jeremy Bentham, the founders of utilitarianism, were hedonists who equated the good with happiness, and happiness with pleasure. But there is disagreement among utilitarians: "Pluralists" think there are a number of intrinsic goods; "eudaemonists" think happiness defined as well-being is the only intrinsic good; and finally "hedonists" think happiness is identical to pleasure. Others despair of identifying objective goods and appeal to individual preferences, or "satisficers," that is, whatever individual people prefer or think will satisfy them. In business and economics, the notion of an objective good has been dropped in favor of individual preferences, and those are judged by demand. But that assumes that what people prefer (want) is what they need (good). Anyone who does cost-benefit analysis will recognize that determining what will count as a cost and what will count as a benefit is a difficult matter. (For the other problems facing utilitarianism, see the entry on Utilitarianism.) Another difficulty with utilitarianism is that it seems to vindicate the principle that the end (consequence) justifies the means (the action).

The philosopher W. D. Ross raised a further, very important objection to utilitarianism, which he calls its "essential defect." Ross claims that utilitarianism ignores special commitments since it fails to recognize the highly personal character of duty. Utilitarianism, according to Ross, is indifferent concerning who is to benefit from the good that our actions create. With its emphasis on quantity of people experiencing "the good," Mill undermines the moral importance that human beings naturally place on relationships, for example, the almost universal importance of perceived obligation to benefit and look out for one's family.

Deontological Ethical Theory

This notion of relationships that Ross introduces raises the rational considerations of the deontologist and includes notions of fairness and commitment. Deontologist comes from the Greek word *deontos* meaning "what must be done" and sometimes translated as "obligation" or "duty." The foremost deontologist was the 18th-century philosopher Immanuel Kant, who offered several formulas to help decide in what one's duty consists: (1) "Act so that you can will the maxim of your action to become a universal law." (2) "Act so as never to treat another rational being merely as a means." In sum, he argues that one should be consistent in one's ethical reasoning and one should not use other people on account of their inherent dignity. Kant derives his moral imperatives from commonsense morality, so it is has been claimed that the principle that leads to Kant's position is the golden rule, "Do unto others as you would have them do unto you." The golden rule implies that everyone is fundamentally equal, and what is good for one should be good for all who are similar (the universalizability claim), and also recognizes that all rational beings are autonomous individuals and thus should be treated with equality and dignity (the ends not means claim).

Two major difficulties are raised with respect to Kant's theory. The first difficulty is that the application of the categorical imperative does not allow for exceptions. For example, if one were to universalize the maxim, "Everyone can lie if lying is in their self-interest," one would find that, when applied universally, this maxim involves the will in a contradiction. It is evident that for a lie to achieve the purpose of the liar, which is to be believed, it is necessary that the majority of statements people make are true. This is the case if the majority of statements people made were false, the liar's lie would not be believed. Thus, since no one tells the truth if everyone lies, the necessary condition for lying, truth telling, is impossible and hence to universalize lying is to make it impossible. Kant indicates that this is a will contradiction, that is, willing two impossible things at once, which is unreasonable and violates practical reason. Hence it follows that lying is never acceptable, nor is promise breaking or many other activities. However, there are times when great good can be done by lying, as Plato reminds us with his notion of the noble lie. The second difficulty is that Kant provides no solution for a situation in which there is a conflict of duties. This difficulty has been recognized by Ross and many other Kant scholars, and since one of the principal requirements of a moral theory is its ability to resolve moral dilemmas, Kant's silence on this point is especially problematic.

There is a claim that Aristotle has provided us with a third alternative for ethics called virtue ethics. But virtue ethics deals less with what actions should be performed than with what sorts of character human beings should possess. Ideal moral reasoning for Aristotle consists in practical wisdom that tells us how to do the right thing at the right time in the right way for the right reasons. But to determine the "right" actions and the "right" circumstances, it is necessary to reason about the nature of human persons and what constitutes the good life or human flourishing. Once these considerations have been completed, we are able to use a practical syllogism to achieve the good that we all seek.

Cognitive Moral Development Theory

An important contribution to the literature on moral reasoning has been made in the 20th century by moral psychologists such as Laurence Kohlberg who have argued that there is a process of cognitive moral development, wherein one develops through three stages of moral reasoning: (1) from a preconventional level where one is concerned with self-interest; (2) to a conventional level where societal norms and laws provide the moral guides for action; (3) to a postconventional level where one uses more general and abstract reasoning to make decisions beyond what are demanded by custom and law. Development to the postconventional stage is not guaranteed but comes about through the creation of disequilibrium about moral issues when one realizes that the conventional reasons need to be examined in light of the higher principles. Kohlberg identifies the principles used in higher reasoning by designating that an autonomous individual is an individual who reasons in such a way that he or she is looking at issues from either a utilitarian or deontological perspective.

—Ronald F. Duska

See also Aristotle; Bentham, Jeremy; Cognitive Moral Development; Cognitivism and Ethics; Consequentialist Ethical Systems; Deontological Ethical Systems; Dilemmas, Ethical; Egoism; Ethical Decision Making; Utilitarianism

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Moral Rules

Rules are statements that prescribe or proscribe any of the following: factual claims, inferences, decision procedures, courses of action, or behavior. Rules, thus, either form a normative standard for what we should believe or what we ought to do. There are rules in games, such as the rule governing the movement of the queen in chess; rules in mathematics, such as the process of multiplication; and rules in a host of practical matters, such as law and morality, that prescribe certain actions or responses depending on the particular circumstances that obtain.

Moral rules are rules that are designed to prescribe or proscribe well-defined actions or behavior in order to uphold some moral value. The rule "abide by the terms of a written contract" prescribes certain actions, that is, those demanded by the written terms and conditions of the contract, and implicitly proscribes certain actions, that is, those that are inconsistent with the written terms and conditions of the contract. This rule is a moral rule in virtue of the fact that it is designed to direct action so as to properly respect the moral values of honesty and trustworthiness. There are also examples of moral rules that describe what moral attitude we ought to take toward an individual under certain conditions. For instance, someone might hold that "she who neglects the terms of her written contract is dishonorable." As a matter of practice, however, moral rules typically take the form of statements that identify practical guidelines for appropriate and inappropriate conduct rather than guidelines about the moral qualities of someone's character.

One source of ongoing discussion among ethicists concerns the kind of practical direction that moral rules provide. A natural way of thinking about moral rules assumes that they are all-or-nothing in that they rigidly determine what one ought to do in all relevant circumstances. The rule "Abide by the terms of a written contract" compels obedience when certain conditions are met, wherever they obtain. When a contract with specific terms is signed by two parties, the rule would bind each party to act in very specific ways, simply in virtue of the meaning of the rule. There may be exceptions to such moral rules; however, these exceptions can be logically built into the content of the original rule. It may be said that someone ought to abide by the terms of a written contract so long as they have not been voluntarily released from those terms by the other party. This important exception would serve to clarify the rule in question by stipulating the conditions under which someone may permissibly not abide by the terms of a contract that they have signed. On this all-or-nothing conception, moral rules have a practical character similar to the rules of a game. Chess has very specific, context-sensitive rules regarding the movement of pieces based on all the contingencies that could transpire within a particular match. Similarly, an all-or-nothing moral rule stipulates all the relevant exceptions and conditions for its application and, as a matter of logic, will compel certain actions when an entire range of specific conditions are considered.

Many find this conception of moral rules unsatisfactory. First, viewing moral rules as game rules fails to acknowledge the inevitable indeterminacy of certain concepts contained within a rule. What would it mean to fail to abide by the terms of a contract? The temptation to articulate these terms in greater and greater detail would be strong; nevertheless, questions about the meaning of these new, detailed provisions would inevitably surface again. A comparable problem emerges even for games. Rules regarding balls and strikes in baseball assume forms of judgment on the part of the umpire regarding the strike zone as to whether a particular pitch has traveled through the zone. This problem suggests that all-or-nothing rules are not nearly as mechanical in their application as one might first think. The fact that judgment is involved in applying rules implies that not all rules function in the same way—some may be more mechanical than others. Moral rules are characteristically less mechanical than other rules because, as we will see below, they often include the use of contestable terms.

Even granting that complete precision could be reached; however, a second related problem surfaces. The moral guidelines that individuals and organizations use to direct their actions do not take the form of all-or-nothing, mechanical rules. It is very rarely the case that we look to rules to define the entire scope of permissible and impermissible conduct. This is what has led some to draw a distinction between moral *rules*, on the one hand, and moral *principles* on the other. In practice, this distinction is not always observed; however, philosophers have noted that while rules tend to be used in ways that formulaically determine action, principles articulate an underlying moral commitment that holds for the most part, without determining what ought to be done in particular circumstances. Principles neither admit of exception nor purport to give unambiguous direction in all relevant circumstances. Without necessitating actions or decision in any one direction, principles serve to call agents' attention to certain indeterminate norms that indirectly express an allegiance to abstract values such as fidelity, honesty, justice, and benevolence.

Principles such as "Respect the property of others," "Do no intentional harm," "No one should profit from wrongdoing," and "Stakeholders should receive benefits in proportion to their contributions" are examples of the kind of indeterminate, yet extremely important commitments that shape individual and organizational action. A few points of comparison with moral rules are instructive. First, as has been suggested, the commitments that principles express convey prima facie reasons to act in general ways (and refrain from acting in other ways) without necessitating any particular course of action. Rules, unlike principles, do not identify a general course of action under ideal conditions, but they are often intended to provide absolute, precise guidance. Second, principles require moral agents to assign comparative importance to principles when one or more principles are relevant in a particular case. One can imagine situations where two or more principles provide conflicting prima facie reasons. In such cases, the agent is forced to exercise judgment as to which principle is most salient and which principle is less important in the circumstances at hand. Mechanical rules do not suffer from this problem. An apparent conflict of rules is simply that—an *apparent* conflict. If the rules are truly formulaic, then one would expect such conflicts to dissolve once more nuanced sets of conditions or exceptions are uncovered and built into the rules. One rule would simply become inapplicable once these details emerge. Principles, however, never lose their applicability even if they are silenced by the circumstances or judged less important than another principle. Third, the boundary between moral rules and principles is not always sharp. Although there are clear logical differences between rules and principles along the lines already discussed, the substance and practical intention of a general moral statement can serve to qualify it as a rule, a principle, or simultaneously both. Consider the statement that "no prices should be set that unreasonably take advantage of the economic position of consumers." This statement could be treated as a moral rule pertaining to the general issue of fairness in pricing: Marketing managers are required to avoid prices that unreasonably take advantage of the economic position of consumers wherever and whenever these conditions exist. Note that the phrase "unreasonably take advantage of" is inherently less determinate than the rule requiring individuals to abide by the terms of a written contract. The pricing rule calls for a judgment regarding reasonableness in pricing given the economic situation of the relevant consumer group. Thus, even if we treat the prohibition on unreasonable pricing, logically speaking, as a rule, it functions more like a principle due to its reliance on a phrase that is substantively less determinate.

These considerations naturally lead to a final observation, which is that principles justify the validity of rules. Principles are the grounds on which rules are revised and sometimes criticized. A rule that requires the operations managers of multinational corporations to adhere to all local health and safety regulations may function well in establishing a specific, determinate guideline relating to the relative safety of its employees in foreign countries. Compliance with this rule, however, may still fall short of the corporation's principled commitment to protect the health and well-being of its employees. Some local health and safety regulations are simply inadequate for all technologies and production processes. In such circumstances, the principle may call for a revision to the rule or the implementation of different policies designed to uphold the spirit of the principle.

This priority relation between principles and rules has been implicitly endorsed by an array of different organizations and corporations. The American Institute of Certified Public Accountants' (AICPA's) Code of Conduct sharply differentiates the rules and principles governing the conduct of accountants. The Code directly states that rules (or technical standards) are to be exactly followed by their members, unless countervailing or ambiguous circumstances surface that make the application of the rule unclear. Where there have been questions regarding the meaning and applicability of a rule, the AICPA has offered interpretations to further clarify the scope and significance of the rules in order to enable the rules to have a more complete and determinate form. The AICPA acknowledges that its rules cannot anticipate every possible future circumstance; as a result, the rules are interpreted in light of more abstract principles regarding professionalism, public interest, integrity, objectivity, and due care. The rules regarding conflicts of interest, for instance, have been identified and developed as standards designed to compel action consistent with the principle of objectivity. Individual corporations have also developed comparable approaches. The casual clothing giant Levi Strauss & Co. has a statement of *Values and Vision* that sets out abstract, principled commitments to empathy, originality, integrity, and courage. It has also developed a document titled *Terms of Engagement* that outlines specific standards with regard to global sourcing and operations. This rule-based document prohibits the use of child labor, products made with forced labor, the formation of contracts with suppliers that pay subminimum wages, as well as other practices that undermine Levi Strauss's responsibility to the fair treatment of employees. Levi Strauss explicitly states that these *Terms of Engagement* are an attempt to specify actions that are consistent with the company's *Values and Vision.*

The application and implementation of principles raises a host of other practical complications. It should be clear from the preceding remarks that principles require moral judgment on two different levels. First, in evaluating past decisions, current problems, or existing practices, moral agents need to be able to identify and classify all the particular, relevant facts before understanding which principles are appropriate in evaluating moral performance. Many have argued that cultivating this kind of moral vision is necessary for principles to have any practical impact on the way that agents reason about what to do in any specific case. Principles provide only very general grounds on which particular moral decisions are inferred. For a principle advocating the fair distribution of benefits and burdens among stakeholders to be relevant, it requires that an agent be aware of the situational markers of unfairness. Following those who have been inspired in various ways by the moral thought of Aristotle, this necessitates sensitivity, care, experience, and training. Second, agents need to creatively explore the meaning and significance of a principle in determining what they will do in the future. What does a commitment to fairly share the benefits and burdens mean for wage, benefit, and compensation policies? How does this principle affect the way in which information is shared among stakeholders? What mechanisms are in place to monitor and assess the relative benefits and burdens of each stakeholder? These questions are part of an overall process of judgment that transforms an indeterminate principle into an action-guiding directive.

—*Jeffery Smith*

See also Aristotle; Casuistry; Caux Principles; Clarkson Principles for Business; Codes of Conduct, Ethical and Professional; Moral Imagination; Moral Principle; Moral Reasoning

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Moral Sentimentalism

Moral sentimentalism is the view that human sentiments—feelings, emotions, or other affective states—are fundamental to an account of moral evaluation, awareness, and motivation. According to sentimentalists, objects of moral evaluation—actions, motives, and character—are morally right or wrong (or virtuous or vicious) depending on whether we feel approval or disapproval toward them. (A weak form of sentimentalism maintains that the moral status of actions, motives, and character is determined *in part* by our sentiments but that other considerations are also relevant to fixing their moral status.) Many sentimentalists maintain that the moral evaluation of motives or character is prior to the moral evaluation of actions, but not all sentimentalists agree that this is the case. Sentimentalists do agree that our awareness of what morality requires is not primarily a matter of cognition—that is, a matter of knowing something—but is rather a matter of feeling something. These feelings of moral approval and disapproval, sentimentalists claim, are essential to moral motivation.

While all sentimentalists agree that moral evaluations depend on our sentiments, there is disagreement about the nature of this dependency relationship. The simplest form of sentimentalism maintains that to judge that a moral property applies to an object is just to feel the associated sentiment. A more sophisticated form of sentimentalism regards moral properties as dispositional properties. In this approach, to judge that a moral property applies to an object is to say that the object tends to produce a certain sentiment in normal human observers under normal conditions. Some sentimentalists modify this dispositionalist account by appealing to the affective responses of a hypothetical, ideal (fully informed and impartial) observer; they claim that to attribute a moral property to an object is to hold that an ideal observer would have a certain affective response to the object. The leading contemporary forms of sentimentalism are varieties of second-order sentimentalism. According to this type of sentimentalism, to judge that a moral property applies to an object is to deem it appropriate to feel an associated sentiment toward that object. For example, one might claim that an act is morally wrong if, and only if, it is appropriate for the agent who performed the action to feel guilt for having done it and for other people to feel anger or resentment at the agent for having done it.

Sentimentalism is opposed to moral rationalism (or intellectualism)—the view that moral evaluation, knowledge, and motivation are grounded in reason, as opposed to sentiment. According to rationalists, reason determines the proper ends of action, and moral knowledge is a matter of rational cognition. Moreover, rationalists typically maintain that moral knowledge taken by itself is capable of providing sufficient motivation for action. Traditional forms of rationalism include intuitionism, which sees moral truths as indemonstrable, self-evident principles, and Kantian approaches, which see moral precepts as grounded in a general theory of practical reasoning.

While sentimentalists maintain that morality is fundamentally a matter of feeling, they typically allow that reason plays some role in morality. This role is normally limited to reasoning related to ascertaining and discerning facts, and means-end (instrumental) reasoning: The ultimate ends of action are fixed by moral sentiments, and reason identifies the best means for achieving these ends given the circumstances at hand. Similarly, while rationalists deny that sentiments define morality, they usually do not entirely deny feeling a role in morality. Rationalists see moral feeling as the product or result of our cognitive awareness of the moral status of an object, and such resultant feeling can help move us to pursue (or avoid) that object. Again, according to the sentimentalist, an action is right, a motive is virtuous, or a character is admirable because we feel approval toward it, whereas according to the rationalist, we feel approval because we rationally recognize that the act is right, the motive virtuous, or the character admirable.

Sentimentalism is allied with certain other metaethical theses. It is a form of moral antirealism. This is because sentimentalism is a form of constructivism: It claims that the moral domain is constructed out of the subjective stance of some (real or hypothetical) moral agent(s), and hence, the truth conditions of moral judgments essentially depend on that subjective stance. Sentimentalism is also often characterized as a form of projectivism—the view that moral properties are not real or genuine properties of things in the world but are projections of our own sentiments or emotions onto the world. Some sentimentalists—the so-called expressivists—are noncognitivists; they maintain that the function of moral discourse is not to report or describe the feelings of agents but to express these feelings.

Sentimentalism is attractive to its adherents for several reasons. The view is historically and theoretically aligned with empirical and naturalistic approaches to moral theory and philosophy more generally. By grounding morality in human nature, sentimentalism promises to explain morality in a manner consistent with the scientific worldview. Sentimentalism accords with the increasingly common view that moral values essentially depend on human valuing, which is inextricably related to our affective states. Sentimentalism also provides a simple account of how moral judgments motivate us to act. Sentiments play a relatively straightforward motivational role; so, if moral judgments are grounded in sentiments, it is easy to see how these judgments move us to act. Sentimentalists have long argued that reason alone is motivationally impotent, and so it is unclear how moral judgments construed as rational principles could move us to act.

For their part, critics have raised a variety of problems for sentimentalist approaches to morality. Perhaps the most fundamental difficulty involves reconciling sentimentalism with the rational aspects of moral evaluation. Moral deliberation and argumentation are governed by norms of justification. We advance and defend our moral judgments with reasons, and we routinely argue about their correctness. It is unclear, however, how the purely affective states that supposedly fix morality can be rationally justified in the relevant way. Opponents of sentimentalism also typically argue that moral principles are, by nature, necessary and objective, while sentiments, even if universal, are contingent and subjective. Sentimentalism, critics charge, makes morality a wholly arbitrary matter.

Sentimentalism is compatible with a wide variety of approaches to normative and applied ethics, so sentimentalists can, and do, approach business ethics in many different ways. Generally speaking, those sentimentalists who think that actions—either specific instances or general types—are the fundamental objects of moral assessment maintain that business practices involving deception, cheating, exploitation, physical harm, and so forth, are morally wrong because of the disapprobation that we tend to feel toward these practices. Those sentimentalists who consider motives or character traits to be the fundamental objects of moral assessment claim that certain motives (e.g., the unconstrained pursuit of profit) and certain character traits (e.g., selfishness) are morally bad because of the disapprobation that we tend to feel toward them. In this general approach, the business practices mentioned above are morally wrong because they exemplify these motives or character traits.

Historical Development

Historically, moral sentimentalism is most closely associated with the moral sense school of ethics that flourished in Britain during the first half of the 18th century. Anthony Ashley Cooper, Third Earl of Shaftesbury (1671–1713), is typically regarded as the founder of this school—he was the first to use the term *moral sense*—although there are rationalistic elements to his moral philosophy that are not consistent with sentimentalism. The doctrine of the moral sense was systematically developed by Francis Hutcheson (1694–1746) and refined by David Hume (1711–1776). Although he rejected their idea of a moral sense, Adam Smith (1723–1790) was strongly influenced by Hutcheson and Hume, and his moral philosophy represents an important form of sentimentalism.

Thomas Hobbes (1588–1679) set the agenda for early-modern British moral philosophy, and both moral sentimentalism and rationalism originally developed in reaction to his views. In *Leviathan*, Hobbes defended a secular form of voluntarism: He maintained that moral distinctions are determined by the sovereign's will, and hence, in a state of nature—a situation prior to or without government—morality is nonexistent. He also maintained that good and evil are relative to the desires of individuals and that humans are motivated primarily by selfish desires.

The rationalist line of response to Hobbes was initiated by the Cambridge Platonists, Ralph Cudworth (1617–1688) and Henry More (1614–1687). Cudworth and More defended a traditional form of moral intuitionism—the view that moral truths, such as logical and mathematical truths, are grounded in an eternal and immutable order that is apprehended a priori through rational reflection. Hence, they rejected Hobbes's voluntarism, maintaining that morality is grounded in reason and not the will. Samuel Clarke (1675–1729) extended the Cambridge Platonists' analysis by adding the idea that what reason apprehends is a relationship of "fitness" or "unfitness" between circumstances and actions. According to Clarke, the right action in a given set of circumstances is the fitting one, and our knowledge that an action is fitting motivates us to do it. Early-modern British ethical rationalism culminated in the work of Richard Price (1723–1791). Price abandoned Clarke's idea that moral concepts are analyzable into something further such as fitness, arguing that moral concepts are simple and irreducible. Price did not think that one can know by direct rational intuition what one should do in specific circumstances; rather, he believed that what is self-evident to reason are general principles about what considerations are morally relevant—for example, it is self-evident that, other things being equal, one ought to be truthful. Many elements of Price's intuitionism reappear later in the moral philosophy of H. A. Prichard and W. D. Ross.

The sentimentalists employed a different strategy in responding to Hobbes, challenging in the first instance his characterization of humans as selfish, unsociable beings. Shaftesbury argued that experience teaches us that other-regarding (disinterested) sentiments, such as benevolence, sympathy, and gratitude, which move us to promote the good of others for their own sake, are just as fundamental to our nature as are self-regarding motives. Virtue, Shaftesbury thought, consists in achieving balance between one's self-regarding and other-regarding motives. What is more, we naturally approve of, or take pleasure in the contemplation of, virtue, and this pleasure induces us to pursue it. Where the rationalists saw a likeness between morality and mathematics, Shaftesbury—like many subsequent sentimentalists—saw moral judgment as analogous to aesthetic judgment. Shaftesbury occasionally referred to the faculty of moral judgment as the "moral sense," but he did not explain its origins or workings. Providing an account of the moral sense was the central aim of Hutcheson's moral philosophy.

Hutcheson firmly situated his sentimentalism in John Locke's (1632–1704) empiricist theory of knowledge. According to Locke, all our ideas originate in experience—reason itself cannot be the source of any new ideas—and experience is acquired through either sensation ("external sense") or reflection ("internal sense"). Locke attributed our ideas of colors, sounds, odors, and so on, to the external senses, and he attributed our ideas of mental operations and feelings to reflexive senses. Hutcheson argued that our moral ideas are unique and irreducible; hence, he concluded that they must originate in a distinct reflexive sense—a moral sense. Our moral ideas are feelings of approval and disapproval, and they are elicited by our observations of people acting from certain motives. When we observe someone act from the motive of benevolence, we naturally and spontaneously feel approval. A contrary feeling of disapproval arises when we observe someone acting selfishly. Our moral judgments are grounded in these feelings: We judge benevolence to be virtuous simply because we feel approval toward it. So, moral judgment, on Hutcheson's view, rests on an affective response to the world rather than a rational cognition of it.

Hutcheson leveled a number of fundamental objections against ethical rationalism, but Hume launched an all-out assault on rationalism that was remarkable for both its argumentative and rhetorical power. One of Hume's most forceful and influential arguments against ethical rationalism is premised on the view (generally referred to as "motivational judgment internalism") that there is an internal (semantic or conceptual) connection between moral judgments and motives for action such that, necessarily, one is motivated (to some extent) to act in accordance with one's sincerely held moral judgments. But, Hume argued, reason alone cannot move us to act. Reason can show us how to best satisfy our desires, but it cannot move us to action independent of these desires. Since reason is in this manner "the slave of the passions," moral judgments cannot be grounded in reason alone.

Like Hutcheson, Hume concluded that morality is "more properly felt than judged of," but he modified sentimentalism in several important ways. Where Hutcheson took the sentiments of moral approval and disapproval to be brute facts of human nature—and, hence, subject to no further explanation—Hume explained the moral sentiments in terms of sympathy, our natural propensity to feel what others are feeling. Spectators take sympathetic pleasure (or pain) in the happiness (or unhappiness) that certain character traits tend to produce for those possessing them or others, and this sympathetic pleasure (or pain) gives rise to the particular kind of pleasant (or unpleasant) feeling that constitutes moral approval (or disapproval). Genuine moral approval and disapproval occurs only when the spectator considers a person's character from a "general" or "common" point of view—that is, when the spectator considers how a person's character affects people in general, and independent of the spectator's own self-interest. By introducing the notion of a general point of view, Hume allows for a certain degree of objectivity in moral judgment: The general point of view provides a standard for correcting aberrant moral judgments.

Hutcheson thought that the object of moral approval is always some form of benevolence, but Hume distinguished between "natural" virtue (e.g., benevolence) and "artificial" virtue (e.g., justice). Explaining why we approve of justice is more difficult than explaining why we approve of benevolence, since sometimes justice demands that we act in ways that do less good than we otherwise could. Hume explained that the conventional rules of justice provide stability and security in conditions where goods are scarce and people are too often selfish. Maintaining the system of justice is necessary to the survival of society and, hence, to the well-being of every individual. Moral approval of justice, then, depends ultimately on sympathy with the happiness of society in general.

Hutcheson and Hume have long been regarded as forerunners of utilitarianism. Indeed, Hutcheson was the first to express the principle of utility—"That action is best which procures the greatest happiness for the greatest numbers," which was later developed by Jeremy Bentham (1748–1832) and John Stuart Mill (1806–1873). But it is important to note that both Hutcheson and Hume regarded moral judgments about motives and character to be prior to moral judgments about actions, and, moreover, these moral judgments depend on our natural and spontaneous affective reactions to these objects and not on thoughts about consequences.

Adam Smith took it for granted that Hutcheson and Hume had established that morality is a matter of sentiment. Like Hume, Smith took moral approval and disapproval to be grounded in the operation of sympathy. For Smith, sympathy involves imaginative identification—the ability to imagine oneself in another's situation so as to be able to consider whether the agent's motives are proper given the situation. Smith also follows Hume in maintaining that moral appraisal involves a disinterested point of view, which Smith refers to as the standpoint of the "impartial spectator." But Smith went beyond Hume in employing this idea to explain the origins and workings of conscience. Although he was committed to sentimentalism, Smith did reject certain aspects of the moral sense theory. Most fundamentally, where Hutcheson and Hume thought that moral approval (and disapproval) involves one particular type of feeling, Smith maintained that there is in fact a variety of moral sentiments. Among these different moral sentiments are the sense of propriety, the sense of virtue, the sense of merit, and the sense of duty.

Recent Developments

Sentimentalism waned in the late 18th and 19th centuries. Bentham and Mill stressed the utility of actions and social policies, and this supplanted the moral sense theorists' emphasis on our sentiments. Sentimentalism was revived in the 20th century, however, and some of today's most important projects in moral philosophy employ a sentimentalist approach.

A. J. Ayer developed the emotive theory of ethics as an adjunct of logical positivism. Emotivism is the view that moral judgments express, rather than describe, the speaker's sentiments of approval or disapproval. According to Ayer, moral judgments—like aesthetic judgments—are not statements but are exclamations, which are neither truth nor false; hence, emotivism is a form of noncognitivism (and antirealism). In Ayer's analysis, one's judging that eating meat is wrong is like one's shouting, "Boo to eating meat!" In so judging, one is not simply describing one's negative feelings toward eating meat; rather, one is evincing these feelings.

Criticisms of Ayer's emotivism led to the development of more sophisticated forms of expressivism. Like Ayer, Simon Blackburn and Allan Gibbard agree that moral judgments do not express beliefs but rather some noncognitive mental state. But where Ayer thought that moral judgments express our sentiments of approval and disapproval, Blackburn maintains that moral judgments express our dispositions toward our sentiments of approval and disapproval, and Gibbard maintains that moral judgments express our acceptance of a system of norms that governs feelings such as guilt, remorse, resentment, blame, and anger. For second-order sentimentalists such as Blackburn and Gibbard, making a moral judgment is not simply a matter of feeling a certain way toward an object; it is a matter of approving or endorsing the way that one feels. To judge that a moral property applies to an object is to regard as appropriate one's feelings toward that object. On Blackburn's projectivist account of morality, to say that honesty is a virtue is to express a stable, favorable disposition toward one's own (and others') feeling of approval toward honesty: It is to express a favorable "second-order" sentiment toward a "first-order" sentiment. According to Gibbard, to judge that stealing is wrong is just to say that it is rational for the agent who stole to feel guilt at having done so and for others to feel anger at the agent's having stole. But, on Gibbard's analysis, to say that it is rational for the agent and others to have these feelings is not to state a fact; rather, it is to express acceptance of a system of norms that warrants these feelings.

The revival of virtue ethics has been one of the most important trends in recent moral philosophy. Initially, contemporary virtue ethicists were encouraged primarily by the thought of Aristotle. However, modern-day virtue ethicists have increasingly looked for inspiration to the 18th-century British sentimentalists. A prime example is Michael Slote, whose "agent-based" moral theory grounds evaluations of actions in more fundamental evaluations of sentiments that reflect a general concern for humanity. On Sloate's analysis, an act is right if, and only if, it comes from a virtuous motivation involving benevolence or caring. These motives are virtuous just because they are admirable, and not because they are central to human flourishing or because they tend to generate happy consequences.

Another important trend in recent moral philosophy involves attempts to articulate a distinctively feminine morality, and many have argued that sentimentalism accords with the moral experience of women far better than rationalism. Annette Baier, for example, reads Hume as a protofeminist. She argues that his sentimentalism anticipated many of the central themes of the feminist ethics of care described by Carol Gilligan. Where rationalists such as Kant see emotions and feelings as subversive to morality, Hume recognized that they are indispensable to it. Like the ethics of care, Hume's sentimentalism grounds morality in other-regarding sentiments that are developed and exhibited primarily in interpersonal and social relations, and maintains that we are not guided by moral rules so much as by a natural and direct concern for the well-being of others. Baier's own ethics of trust builds on these Humean foundations.

—*Michael B. Mathias*

See also Cognitivism and Ethics; Ethical Naturalism; Feminist Ethics; Feminist Theory; Hume, David; Intuitionism; Metaethics; Moral Realism; Noncognitivism; Smith, Adam

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Moral Standing

Moral standing is a concept that relates to what ethicists call "moral considerability." Here, the moral status of an entity is determined by considering whether that entity deserves to have their well-being taken into account within the context of moral decision making. To ask if an entity has moral standing is to ask whether that entity should be considered in the moral judgments that people make and the moral decisions that they take, and whether that entity should count as a morally valued being and whether it can make moral claims on other moral beings. Hence, this concept has to do with the value or worth that is bestowed on an entity. Whether the entity under consideration is determined to have intrinsic or instrumental value will often play a role in how that entity is morally treated or regarded by people. The question of moral standing is one that has been raised primarily within the context of the philosophical debate about animal rights, although it has had a role to play in other ethically controversial areas (Does or should a fetus have moral standing?). The moral standing of animals is important to determine; if they don't have any moral standing or worth, then it would be permissible to treat them in whatever ways one wishes. If animals do have moral standing, though, then perhaps using them in medical experimentation or eating them may be ethically problematic.

Ethicists have taken several positions about how to determine the moral standing and inherent worth of an entity. Aristotle set a tone that still reverberates today with his teleological view of nature that sees the world as a hierarchy where the lower levels of plants and animals have value only in relation to the purposes of humans. Kant later held a similar view when he claimed that we have no moral duties to animals. This view has been called an "anthropocentric view" because it puts humans above all other entities and holds that all and only humans are morally considerable.

There are two kinds of anthropocentrism that ethicists have recognized. "Strong anthropocentrism" argues that only humans have intrinsic value and all nonhumans have only instrumental value as determined by human ends. "Weak anthropocentrism" holds that while humans count most in moral matters, nonhumans do have some moral status and humans do have certain duties to animals to reduce their suffering and treat them humanely.

Others have objected to anthropocentrism and have offered their own positions. It is often claimed that anthropocentrism commits "speciesism," a form of bias toward the human species that unfairly discriminates against other species. Some have appealed to the concept of sentience to determine which entities have or should not have moral standing. Sentience is often defined as having the quality of awareness or the state of consciousness and self-consciousness. Some define it as relating to sensation, perception, ideation, or feeling.

In this account, then, a sentient, self-aware being possesses and has moral value, while nonsentient ones do not. Still others suggest that a "biocentric view" is even more plausible in that it gives moral status to both human and nonhuman entities alike. Finally, "environmental holism" has been suggested by those who want to see moral standing granted to species and ecosystems such that it would be morally culpable to engage in activities that are environmentally degrading.

The concept of moral standing can be important in the area of environmental management and helpful in sorting out the obligations of businesses to the environment. It may be used to form the basis of a management philosophy or be useful to enlightened organizations that desire to understand what their moral duties might be in the environmental arena since determining the moral worth of entities, animals, species, and ecosystems might serve as a solid self-regulatory principle in ethical business decision making.

—*Peter Madsen*

See also Animal Rights; Animal Rights Movement; Environmental Ethics; Environmentalism; Instrumental Value; Self-Consciousness

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Most Favoured Nation Status

Most favoured nation (MFN) status provides that for all countries that are members of the World Trade Organization (WTO), all foreign suppliers should be treated equally and without discrimination in respect of all tariffs and other charges and the rules and formalities connected with imports and exports. In effect, MFN says that within the WTO, a member country cannot have any favorite countries for which it cuts a special trade deal.

Alternatively, a member country cannot punish another member country by giving it a worse trade deal. The basic premise is that a member country cannot treat any one member less favorably than any other member on the conditions of goods or services entering its country. MFN ensures that each member country is afforded the same terms of trade.

MFN is at the heart of the WTO's rules for international commerce and has been part of the modern world trade system since the inception of the General Agreement on Tariffs and Trade (GATT) in 1947. With the beginning of the WTO in 1994, member nations were bound by MFN commitments for goods (GATT, Article I), services (General Agreement on Trade in Services [GATS], Article II), and intellectual property (Trade-Related Aspects of Intellectual Property Rights [TRIPS], Article 4).

MFN has been a very powerful way of liberalizing the world trading system. It has two wide-ranging effects. First, in certain cases, it multilateralizes bilateral or "minilateral" (a few countries) negotiations. Generally, the toughest trade talks are between major supplier countries and major consumer countries. That is, if India is a major supplier of software and the European Union (EU) is a major consumer of such software, their negotiators will spend a long time considering the terms of trade, including other India-EU international commerce. Likewise, India may be a major importer of foods. Once a deal is struck, say the EU decides to cut its tariffs on imported software by 50% and to allow Indian software engineers (service providers) easier access into the EU, while in return, India lowers its tariff 20% on imported wheat, corn, and wine, all other members states of the WTO receive the benefits of the deal. In this case, other nations that export software, such as the United States, Israel, Japan, and others, now can enjoy a 50% reduction in the tariff levels into the EU. Likewise, countries such as Argentina and Brazil that export high quantities of grains and Australia, New Zealand, and the United States that export large volumes of wine now have the lower rate into India. These other nations in effect take a "free ride" from the hard work of the Indian and European negotiators and enjoy the outcome of the negotiations in the form of new opportunities for their country's products and services into these markets. So in effect, MFN takes something that is bilateral (India-EU) and makes it multilateral by extending the benefits to all member states.

There is a second element of MFN related to bilateral or minilateral negotiations. The starting point, here, is a multilateral negotiation among the 149 member states (as of December 2005) of the WTO. While it may be useful to get each country's input as to how to handle each product, service, intellectual property, foreign direct investment, labor, environmental, and other issues, it is very difficult for the 149 members to have such discussions on each item of trade. If inclusion was mandated, the sheer volume of work and number of items would more than likely grind the WTO to a stop. MFN simplifies matters by allowing those countries that have a big stake in a sector or in another trade area (say the general receipt of foreign direct investment or intellectual property rules over medicines for epidemic diseases) to come together in smaller-sized groups. There is much give and take in these smaller negotiations because trade negotiators generally have a mercantilist view that if they reduce a tariff they are "giving up something" and therefore must "get something in return" such as better access into the foreign market. That said these smaller negotiations generally have a greater chance to succeed than negotiations among all the countries together. MFN assures that every member state enjoys the fruits of these smaller-scale negotiations.

The existence of MFN eliminates the need to create rules of origin that are necessary in preferential trade arrangements such as free trade zones. Rules of origin are used to identify the country of origin of goods subject to tariff treatment. These rules are particularly complex for products with components from several countries. Without MFN, a country needs to maintain a tariff code indicating different rates for different countries. Indeed, many nations used to maintain such tariff schedules by product and by country. With MFN, any product or service originating in any of the 149 member states is subject to the same treatment. This is a major simplification for both national authorities and for businesses trying to make sales, purchase, and investment decisions.

There are some exceptions to MFN. Countries can enter into free trade or preferential trade arrangements such as customs unions and free trade areas that discriminate between their members and outsiders. For example, after the North American Free Trade Agreement, Mexican apparel producers enjoyed better market access into the United States than firms from El Salvador or the Dominican Republic. In addition, some developed countries administer programs called Generalized System of Preferences where they maintain low tariffs for certain products from certain developing nations. Countries may also grant special deals to certain nations for reasons of national security, public health, and safety and morals, contrary to the MFN. For instance, many countries disallow trade of certain technologies to certain countries for reasons of national security. For public health reasons, some countries practice differential treatment of foreign health care providers, depending on the country in which they studied or practiced medicine.

MFN simplifies the policy world of international trade tremendously for companies. First, the MFN world creates a single trade rule such as a tariff on a product for a given country, regardless of where it is made. This allows the company to manufacture in a particular location for reasons other than preferential tariff treatment by a national authority. Second, MFN makes it easier to focus political efforts for a company. The political activities generally follow the largest trading or investment relations so that companies can aim their political activities accordingly. For example, if a French pharmaceutical company has an intellectual property issue with the piracy and parallel importation of generic drugs, it needs to direct its political efforts toward the large producing and trading nations of generics such as India and Brazil.

—Doug Schuler

See also Free Trade, Free Trade Agreements, Free Trade Zones; International Trade; North American Free Trade Agreement (NAFTA); Piracy of Intellectual Property; World Trade Organization (WTO)

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Motives and Self-Interest

Voluntary human actions—those actions with which ethics is primarily concerned—typically arise as an agent seeks to satisfy a desire. Satisfying desires, moreover, is typically in an agent's interest. Thus, there seems to be a rather straightforward connection between identifying an action as voluntary and identifying that action's motivation (i.e., the desire for the sake of which the action is being pursued) as self-interested.

Additional support is lent to this line of thought by considering that human agents are, on the one hand, members of a species that seeks to secure its own survival and, on the other hand, social creatures. Insofar as humans seek to secure their own survival, they are motivated to act in ways to satisfy their desires for food, shelter, and security. Insofar as humans are social creatures, they are motivated to act in ways to secure their position within their group, primarily by engaging in behavior that others will regard as praiseworthy and by avoiding behavior that others will regard as shameful or otherwise blameworthy.

Sophisticated versions of this line of thought distinguish between agents' consideration of their short-term and long-term (or rational) self-interest. In terms of both what is introspectively available to each of us and how we best understand behavior we observe in others, the evidence suggests that voluntary agents often act out of a consideration of long-term self-interest. Thus, such agents often pursue courses of action that generate no immediate results, calculating that a short-term sacrifice is acceptable in the pursuit of some greater goal. For example, businesses invest significant capital in research and development, where the returns on these investments are realized later, if at all.

The strongest version of the line of thought that links action to the pursuit of self-interest claims that all human action is motivated by some consideration of what is in the agent's own best interest. This position, known as psychological egoism, asserts that every action—from the most obviously greedy act to the most apparently altruistic act—ultimately must be understood in terms of an agent's pursuit of self-interest. This is often cited in support of the normative position known as ethical egoism: If the only acts that are psychologically possible are selfish acts, then—given the plausible principle that *ought* implies *can*—the only acts that an agent ought to perform are selfish acts.

While the self-interested motivation of actions is clearest with respect to actions avowedly undertaken to satisfy the agent's desires, questions arise when attempting to identify the self-interested motivation of apparently selfless acts. For example, employees who blow the whistle on corruption within the firm often face significant harm: reputational losses, difficulties maintaining employment with the firm, and so on. Moreover, such employees often assert that their decision to blow the whistle was motivated simply out of a sense of duty (to shareholders, to the public).

When confronted with an agent who has just performed an apparently selfless act, and who insists that the act was done with absolutely no consideration of self-interest, psychological egoists often respond by positing some subconscious motivation for the act. In the case of a whistle-blower, for example, it might be suggested that the decision to act was motivated by a subconscious desire to be regarded as a hero, to secure a lucrative book deal, or even just to sleep contentedly, free of the pangs of conscience.

At this stage, what was supposed to provide a descriptive account of the actual operations of human psychology seems to become nothing more than an assertion of a putatively conceptual truth. Psychological egoism was supposed to gain its support from the empirical investigation of human psychology, perhaps buttressed by the findings of evolutionary psychology (e.g., explanations of apparently altruistic actions in terms of gene fitness, or kin selection). However, as a scientific theory, it should be responsive to all the evidence, including apparently falsifying evidence. To the extent that psychological egoism resists the evidence provided by apparently selfless acts, it risks credibility.

—David Levy

See also Altruism; Conscience; Darwinism and Ethics; Egoism; Evolutionary Psychology; Hobbes, Thomas; Ought Implies Can; Rand, Ayn; Rationality; Rationality and Ethics; Self-Interest

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Multiculturalism

Multiculturalism is understood as a term that stands for accommodation of diverse cultural groups and their practices within a mainstream culture and society.

Such accommodation is needed to make all minority cultures feel at home in a dominant culture that may at times be perceived by minority groups to be oppressive of or insensitive toward their cultural heritage and tradition. Because cultural diversity has come to be recognized as a value to be prized, making a society rich in ideas and options, multiculturalism is a goal actively pursued by all liberal societies. Besides cultural richness, commitment to the multicultural ideal is also seen as a sign of a liberal society's commitment to equality, including equality of all groups and cultures. Of course, problems crop up in implementing the policy of multiculturalism because it requires a nuanced balancing of several competing claims on several fronts. The claims of equality present both a conceptual challenge and practical problems of implementation as social policies.

Politics of Difference

The dominant liberal ideology in the West makes individuals the epicenter of justice and equality, not groups or cultures. Committed to individual autonomy, state neutrality, and procedural fairness, the liberal ideal finds it problematic to single out any group or culture for special rights or privileges. Yet minority groups and cultures are getting progressively vocal in demanding special recognition to establish a strong identity. One implication of this demand, for them, is to be granted special rights and recognition to make up for the discrimination and marginalization they encounter in the majority culture. They fear that if equality is understood as equal recognition, along with the same rights and entitlements for all individuals and groups regardless of their differences, then the majority norm in the guise of impartial standard for everybody would in effect reward the dominant groups and perpetuate the status quo, overlooking the significant differences that give minority cultures their distinct identity.

This "politics of difference" is rooted in the emerging identity politics of multiculturalism. To work out the nuanced balance between the twin fronts of egalitarianism and multiculturalism is the big challenge in today's liberal democracy. Egalitarianism is the idea that social justice should be based on the principle of equality and impartiality, without any special favor to any group or individuals. However, critics point out that multicultural accommodation in a pluralistic society may require giving minority cultures greater protection and more immunities in especially those areas where their religious and cultural commitments related to their identity may seem to be at stake. For instance, it may mean that government should avoid undue legal restrictions on the right of children in public schools to wear clothing symbolizing their religious identity, such as girls wearing head scarves as a part of their cultural or religious commitment. Defenders of multicultural accommodation argue that an impartial liberal theory is not incompatible with distinct principles of affirmative equality with regard to the members of marginalized groups. Thus, what may seem like partiality is not really partiality but a variation of the same liberal equality principle. Others try to defend this move with a slightly different argument. They claim that if there is a legitimate reason for partiality, then it can be justified on impartial grounds. Thus, even if granting special rights and immunities would seem like a form of partiality, this is still compatible with the principle of state neutrality. Accordingly, defenders of multiculturalism point out that the policy of special recognition in some exceptional cases is perhaps the only way to assure equality in practice, along with it being a good policy of promoting tolerance and diversity in our pluralistic society.

Conflicting Equalities

The issue of multicultural accommodation makes uneasy alliances and bitter divisions. The secular, cosmopolitan liberal ideology based on the principle of universal rights favors individual autonomy, whereas the nonliberal, communitarian segments of the liberal West value the situated identity of the individual understood as a member of a group or a community. Thus, the multicultural demands of special recognition create a tension of "conflicting equalities" between individual rights and group rights, which is a dilemma in liberalism itself. Liberal attitudes in America toward multiculturalism have varied from benign neglect or indifference to confusion and tension. Quite common was the liberal insensitivity toward religious and cultural differences among groups as well as a general lack of interest in global concerns. In reaction to such shortcomings, these attitudes have now been tempered by an acceptance of cultural rights and differences, although the problem of conflicting equalities between individual rights and group rights is a source of perpetual tension in liberalism. Nowhere is this uneasiness more pronounced than when liberalism is confronted by oppressive cultural practices of illiberal groups.

Feminism and Multiculturalism

Feminists too display the liberals' tension and confusion over the issue of multiculturalism. A broad base of feminist theorists questions the liberal premise of individuals as autonomous selves. Feminists claim that the idea of an embedded self in multiple networks of relations and dependence is closer to reality and a good starting point of understanding the feminist concerns about women's subjugation. Accordingly, they would, in general, favor the particularist identity of an individual over the liberal notion of a monadic self. This would seem to bring them closer to the defenders of multiculturalism in their understanding of and appreciation for the cultural rights and differences of minority groups. Yet, confronted by cultural practices oppressive to women, feminists tend to display the same dilemma as the liberals toward multiculturalism. Consequently, both feminists and liberals today are more challenged than ever to look at the dynamics of multiculturalism.

Both feminists and the liberals are divided on the issue. While both camps claim to be respectful of the autonomy of diverse cultures and still claim to be firmly committed to the idea that demands of multiculturalism should not override the dictates of certain fundamental rights, there are two broadly different approaches in both camps. Cosmopolitans among them, taking the individual as the yardstick of their measure for justice and rights, are guided by a universal human rights perspective. Citing empirical studies that seem to show that the claim is in fact overblown that there are incommensurable differences across cultures on issues of human rights, they are hopeful that the universal mandates of human rights would override the claims of oppressive practices in the name of cultural autonomy.

The other group points out that the issue cannot be resolved through mandates or directives from the top down but can be assuaged through public deliberation and negotiations at the grassroots level, especially within cultural and religious communities themselves. They emphasize the role of deliberative democracy in addressing the contending issues of egalitarian representation in a pluralistic society. Claiming themselves to be both feminists and liberals, they take cosmopolitan theorists to task by showing the limitations of what they call the a priori liberal approaches to the problem, manifested in a prepolitical commitment to certain nonnegotiable rights. They argue that the issue of democratic representation in a pluralistic world is essentially a political one, requiring a strategic response not a liberal normative resolution, because the conflict, regardless of its appearance, is not a clash of liberalism versus illiberalism. For them, an a priori normative framing at the foundational level tilts the discourse in favor of liberalism, resulting in the marginalization and alienation of minority groups (and individuals) that differ from the mainstream liberal ideology. So they try to offer a resolution to the liberal cosmopolitan dilemma of respecting individual rights and cultural pluralism by reframing the conflict through the lens of deliberative democracy.

Multiculturalism and Universal Human Rights

The debate on multiculturalism both within a pluralistic liberal society and on the global scene raises critical questions regarding the viability of the notion of universal human rights and of liberalism itself. The ideal of human rights guarantees certain basic liberties to all individuals regardless of their race, class, gender, and religious affiliations. The Universal Declaration of Human Rights enshrined in the United Nations' charter affirms this ideal. Nearly all nations have pledged to abide by the charter to promote and safeguard human rights for all their citizens. The gradual emergence of global human rights culture in the past 50 years has been one of the undeniable trends of modern globalization. Despite all this, the idea of human rights is a hotly contested and politicized concept in the world today. This raises the question whether the claim of universal human rights is a viable concept or whether the problem lies in the differences in interpretation and enforcement across nations and cultures. If it is the latter, then the issue is a practical problem in the application of rights, requiring a careful analysis of the rights, specific cultural practices and national traditions, forms of constitutional commitments in the democratic framework of countries, and the key provisions and treaties in international law. Along with the empirical investigation grounded in the global realities of politics, law, and culture, it would also require certain conceptual reframing of the human rights discourse to accommodate demands of human rights with tolerance for cultural and national practices.

One such attempt by theories of rights that provide for a cosmopolitan framework is to strive to make room for local variations consistent with alternative versions of democratic decision making. In view of the standard critique of abstract cosmopolitanism—that its message of universal egalitarianism is unrealistic and utopian in a fragmented world—this "situated" version of cosmopolitanism looks more credible. In fact, some rights-based cosmopolitan theorists have done promising work to find a middle ground between abstract universalism and cultural specificity to validate the contextuality of the egalitarian human rights ideal within a democratic setting. Appealing to realities of current global practice, they emphasize the actual vitality of cross-cultural discourse concerning human rights and the heterogeneity of religious and cultural communities that tend to be treated as uniformly committed to restrictive views. This is an approach whereby abstract cosmopolitanism committed to universal egalitarianism becomes situated and negotiable by adopting some version of deliberative democracy.

Another example to negotiate a middle path between mandates of rights and weight of culture and self-determination is the one proposed by the "capabilities approach." Initiated by Harvard economist Amartya Sen and developed by both Sen and the University of Chicago ethicist Martha Nussbaum, this approach is claimed as a better starting point for understanding fundamental constitutional entitlements than rights-based approaches have proven to be. This they consider a promising strategy for the task of exploring issues of social justice in a modern constitutional democracy as well as for respecting cultural pluralism. Implied in these various alternative nuances is the claim that endorsing cultural differences does not mean that cultural relativism is true.

But if the concept of universal human rights is claimed to be a flawed concept, then it would require a philosophical investigation into the nature of rights itself to decide whether shared human values in today's global world can be the basis of universal conceptions of human rights and whether basic human rights can be defended from a universal moral point of view that is neither imperialistic nor relativistic. Thus, the national discourse on multiculturalism and the international politics of cultural tolerance have certain features in common. Of course, the international arena is guided by international law based on the sanctity of national sovereignty that prohibits intrusion or intervention in the internal affairs of a country, but the gradual redefinition of national sovereignty due to the forces of an aggressive global economy, the changing global ecology, and the emergence of a human rights culture have increasingly called into question the moral relevance of a strictly construed national and cultural autonomy. Consequently, any undue restriction of rights in the name of local culture is difficult to sustain in a globally vigilant and interconnected world.

Conclusion

As economic globalization has built bridges through cultural differences, it has had problems in demarcating appropriate boundaries. The egalitarian commitment to justice and human rights and the democratic ideal of legitimacy through self-rule and autonomy are often manifested in the tension between individual rights and group rights. Because both rights are in a continual state of flux and readjustment due to the shifting nature of the forces of globalization, to work out the right balance in theory is not easy. Thus, although the debate on multiculturalism and democratic accommodation is on the forefront of the liberal consciousness, the problem of moral evaluations of cultural practices that may conflict with human rights concerns offers no easy resolution. Because the norms of cultural well-being may not always coincide with those of individual autonomy, today's global business cannot be too aggressive in promoting a consumer culture of self-gratification that may clash with cultural norms.

—Deen K. Chatterjee

See also Affirmative Action; Capabilities Approach to Distributive Justice; Cultural Imperialism; Egalitarianism; Feminist Ethics; Human Rights; National Origin Discrimination; Racial Discrimination; Religious Discrimination; Rights, Theories of

Further Readings

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Multinational Corporations (MNCs)

The term *multinational corporation* (MNC) can be defined and described from differing perspectives and on a number of various levels, including law, sociology, history, and strategy as well as from the perspectives of business ethics and society. Certain characteristics of MNCs should be identified at the start since they serve, in part, as their defining features. Often referred to as "multinational enterprises," and in some early documents of the United Nations they are called "transnational organizations," MNCs are usually very large corporate entities that while having their base of operations in one nation—the "home nation"—carry out and conduct business in at least one other, but usually many nations, in what are called the "host nations." MNCs are usually very large entities having a global presence and reach. Names and company logos such as those of Coca Cola, Exxon Mobil, Mitsubishi, and Royal Dutch Shell are good examples. Today, however, we are also witnessing a rapid growth of smaller- and medium-sized enterprises that also conduct business in multiple nations and also have a global presence and reach. Hence, MNCs can be understood as either large or smaller corporate entities that operate on a global scale even though most people think of the MNC as a huge conglomerate with business offices, plants, or facilities worldwide.

MNCs have also undergone great structural changes over the years and they engage in many different and varied kinds of businesses. In addition to the basics of the production, manufacturing, and trading of goods, today MNCs can be found working within a host of business activities that include the delivery of services such as banking or communications both locally and globally, knowledge-based industries, foreign investment and currency exchange, maintaining branch offices or feeder plants in host countries, the extracting of natural resources, the assembly of products in one region (e.g., the maquiladora program in Mexico and elsewhere) for sale in another region, and various forms of technology transfer, among quite a few others. Hence, a picture of the typical MNC is difficult to draw, since there are so many variables and characteristics that can be depicted in the contemporary version of the MNC.

The First MNC

The first publicly held MNC is generally recognized to have been the *Verenigde Oostindische Compagnie* or VOC, which was chartered in 1602. The Dutch East Indian Company was a venture that risked the capital of not only Dutch citizens but also "Zuid-Nedelanders," who are now Belgians, and Germans as well. What these first shareholders had invested their money in was an enterprise formed from the merger of a set of Dutch spice trading and marketing companies that came together in the late 16th century. Competing primarily with traders from Spain and Portugal, these individual groups needed to establish a corporate entity, and this organization was based primarily on diverse geographic "chambers" of the Netherlands that included the geographical areas of Amsterdam, Rotterdam, Delft, and Zeeland, among others. Each chamber had a set of "directors" that selected a "board of directors," which in turn then chose a set of "executive directors."

The company established or took over many trading routes and managed the commerce between the east and the west by establishing its East Indian headquarters at Batavia on Java (now Jakarta, Indonesia). Trading beachheads were set up on the Moluccas, the Banda Islands, Ceylon (now Sri Lanka), Japan, and China. In 1652, the first white colony on African soil was founded by the company as a resupply camp at the Cape of Good Hope, which eventually became Cape Town, South Africa. Various spices such as nutmeg, cloves, cinnamon, and pepper, and tea, silk, foodstuffs, and Chinese porcelain were among the goods shipped from the far-off lands to be sold to wealthy Europeans who could afford the exotic offerings from the Orient.

The growth and development of the Dutch East Indian Company was not accomplished overnight and was not without its corporate ups and downs. Not only did it have to outmanage its European competitors from Spain, Portugal, and later England, it had to overcome losses thanks to its battles with pirates, the extremes of ocean weather, and deadly diseases. To meet its numerous financial obligations, it was necessary to issue both short- and long-term bonds in order to raise enough working capital to stay afloat, as it were. In the end, though, the Dutch East Indian Company flourished for nearly 200 years and became the world's richest and most powerful company.

It amassed quite a few assets, including 150 trading vessels and 50 warships that it needed to protect its sea routes and, at one point, it saw its shares rise 1,200% in value. It was granted many special privileges such as the ability to enter into treaties and alliances on behalf of the Netherlands government, to build forts, and even to mint its own coin. In short, the world's first MNC seems to have been something of a standard setter for all such organizations, at least when it comes to accumulating great power that rivals nation-states and in setting the tone for the process of what we now call globalization.

Unfortunately, the VOC set lower standards for itself when it came to management practices. While it had a long history, it was not so illustrious. The VOC actively leveled competitors sometimes by sheer force, and it became a monopoly in the world spice market until 1799, when it was liquidated due to mismanagement. As a result of its unethical practices, the Dutch called VOC's experiment in international business *V(ergaan) O(nder) C(orruptie)*, which roughly translates as "sunk under corruption."

The Benefits of MNCs

Although they had such beginnings, one thing is clear about MNCs—the world would be quite a different place without them and the major contributions to global progress that they have made over the course of time since the Dutch East Indian Company. Successful worldwide distribution of goods and services; the expansion of employment opportunities, especially for the world's poorest people; pronounced economic growth through concerted foreign direct investment; and the creation of pure and practical knowledge through research and development and the global implementation of technological breakthroughs—these and other advances are often cited as concrete examples of the many benefits of MNC business expansion. On the global economic scene, MNCs have expended some $66 billion per year since 1990 on direct foreign investments. It is claimed such MNC economic activities have done much to spur economic growth as measured by increases in gross domestic product (GDP) especially in Western economies, to provide higher levels of material well-being worldwide, thereby generally raising standards of living. While it is the case that the less economically developed nations do not have percentage increases in per capita incomes at the same rates as the more economically developed nations, it is the case that there are income increases worldwide and these are projected to continue barring unforeseen or calamitous events. Indeed, empirical studies by the World Bank and others have shown that as more openness to international trade increases, so too does per capita income and the income of the most poor.

There have been many contemporary social commentators and many ethicists over the course of the history of ethics that have claimed that strong international commerce leads to conditions of peace and security. The interlocking of national economies through free and fair trade made possible largely by MNC business activities makes large-scale war a less likely option for nation-states. As a result, many nations now pursue a general policy of open trade that has led to the establishment of several international free trade conventions and the creation of the World Trade Organization (WTO), which serves as an international regulatory body. The WTO has been embraced by many as a prime example of global cooperation, although there are others who see it as something of a threat to the idea of national sovereignty.

It is also clear that MNCs provide the context within which major strides in industrial research and development take place. MNCs have done much to further advances in pure and applied science, for example. This can be witnessed in several major industries. One of the more prevalent forms that this takes is in the area of information technology (IT), and IT serves as a good example of how MNC practices can benefit many in the world. It is often said that today is the Age of Information, and this depiction is due to the fact that IT has become so prevalent and far-reaching in modern life. It would likely be a very different world if some of the major MNCs did not stimulate applied research in IT and support its development. Another good example of how MNC capital investment has changed the world for the better is in the area of medical research. Basic medical research into the causes of diseases, pharmaceutical practices that provide safe remedies for so many medical ills, and the invention of miraculous life-saving medical devises—these would likely not have become realities today, if it were not for the initial push in these areas provided by large MNCs. There is little doubt that life expectancies have been increased thanks to MNC-sponsored medical research, for example. In short, MNCs can be credited with having changed the nature of human life through their concerted efforts in the areas of research and development, a change that only they could likely accomplish, given their business activities of turning profits into capital available for investments geared to the progressive improvement of the human condition.

MNCs, Power, and Globalization

While many reap the tangible benefits of large MNCs and are literally alive today only because of the reinvestment of capital by MNCs that made such benefits possible, there are some who nonetheless find it necessary to raise important questions of an ethical nature about how MNCs operate. For example, the question of MNC power is a very pressing one, and it is closely related to the concerns that have arisen in reaction to "globalization." The governments of the European Union and the United States (among others) and a number of nongovernmental organizations (NGOs) along with an array of amorphous groups—some radical and some not—have expressed alarm about the way in which multinational corporate organizations have grown and about the threats posed by global multinational capitalism. Many of the more radical groups have demonstrated their anger at the accumulated power of MNCs by taking their concerns to the streets in the form of violent demonstrations in cities around the world. A brief survey of the reaction to the role that MNCs have played in the globalization process is thus useful.

According to the advocates of "critical theory" and other postmodern social critics, globalization should be seen as something like a world-historic process in which a great transformation and dismantling of cultures, institutions, and nation-states is unfolding. In these accounts, we can take note of at least three kinds of "globalization." First, an "international" conception of the idea of globalization can be identified where the nation-state is still the central focus of analysis, and so globalization in this first sense is measured by the basic alterations of or to nation-states and their power. Second, the "transnational" idea of globalization points to an array of practices and institutions that have become or are becoming transnational. In this account, the contemporary MNC would be taken as a major "transnational institution." Here, such institutions gain prominence and share the focus of the theoretical constructs that deal with the process of globalization.

Finally, there is what has been called the "globalist" conception where the nation-state is seen as a weak, if not a nonexisting, force in the world and where other institutions, such as MNCs, have supplanted them. In these critical accounts, then, of the processes of globalization, capitalism in the form of the spread of the MNC is a major—for some it is *the* major—force in the unfolding of the globalization process. The antiglobalization movement holds that the transnational power of MNCs is supplanting the power that formerly was seated in the nation-state and transforming the globe thereby.

The power of capital is rapidly displacing political power, and the ongoing unfolding of this displacement is a defining feature of globalization according to this movement. Indeed, for many in the movement, this displacement is just one among many that goes into the creation of the postmodern experience. So the antiglobalization movement is essentially a call for reform—in some cases radical reform—which wants a reining in of the accumulated power now being exercised by MNCs around the planet. The recent protests in major world cities by the divergent groups that make up the antiglobalization movement are primarily protests against corporate power and a call for its moderation that may be brought about by policies regulating the behavior of MNCs at the international level. But such reform policies and regulations face various hurdles before they might become a reality. Not the least of these has to do with a theoretical consideration of the ethical legitimization of these international regulatory policies, and today many business ethicists who specialize in the field of "international corporate responsibility" (ICR) have been working to provide a theoretical foundation to such policies.

The MNC, Business Ethics, and Society: International Corporate Responsibility

From the perspective of business ethics and society, the MNC often becomes an object of scrutiny by academic specialists who teach and write about business ethics and business and society issues. As alluded to above, various practices of MNC have been pointed to as questionable or even unethical because of the harms they perpetrate on society. There are a number of ethical issues, problems, and dilemmas that have to do with MNC practices, and several classic case studies involving specific MNCs have been analyzed and discussed in the literature of business ethics. As a result of this academic attention, a branch of business ethics has emerged in which the ethics of MNCs and the ethics of international business practices are central. Again, this subdiscipline has been called the international corporate responsibility (ICR).

ICR, taken as a conceptual movement, explores whether MNCs have been cognizant of and have included the rights of stakeholders, and their responsibilities and their obligations to them, in their business strategizing. Questions that an ICR specialist might address include whether international businesses have conscientiously monitored their labor practices, respected the integrity of local cultures and the basic human rights of the individuals within those cultures, carefully measured and reported the environmental impact that they might have, or contributed fairly to the well-being of their "host countries." ICR takes many forms, and those interested in it have much work both in the conceptual clarification of the main ideas of ICR and in continuing empirical studies of how organizational responsibility is or is not fulfilled by MNCs.

Bribery, Business Gifts, and the Foreign Corrupt Practices Act (FCPA)

One of the more recurring ethical issues that can be found in the area of ICR has to do with the question of bribery and gift giving in international business. This issue presents managers in MNCs with difficult business decisions based on the uncertainties of cultural relativism. It may be the case that in their home country the exchange of gifts between business associates is considered unethical and, in some cases, such exchanges may be construed as illegal bribes. However, in many host countries business gift giving is a culturally expected part of doing business and business relationship building. In fact, in some countries the failure to give gifts may lead to the loss of business transactions since the host may take the absence of a gift as an insult and in some contexts the value of a gift is expected to be high.

Gift giving in international business transactions is thus a problem of relativism and is often expressed in the precept "When in Rome, do as the Romans do." This old adage suggests that the phenomenon of cultural relativism is real and that there may be more than one ethical standard according to which people need to gauge their actions. Moreover, it suggests to managers in MNCs that they need to be mindful of any differences in host country business practices that depart from their own and that sometimes these might conflict with their own home country business ethics and basic values. In this case, gift giving may appear to be a form of bribery that corrupts the level playing field of business or it may just appear to be an accepted and normal part of business relationships—it all depends on your view from the host or the home country and the respective values that stand behind that view.

In the United States, the Foreign Corrupt Practices Act (FCPA) was adopted as a regulatory law to address the question of whether or when business payments should be considered a bribe and, therefore, a form of illegal corruption. According to the Department of Justice, in the mid-1970s, the Securities and Exchange Commission found that more than 400 U.S.-based companies had made questionable payments in excess of $300 million to foreign government officials, politicians, and political parties. The FCPA now makes it illegal to make such payments to high-level foreign officials for the purpose of obtaining or retaining business. Past MNC practices included the bribery of highly placed foreign officials to secure some type of favorable action by their foreign government as well as the so-called "facilitating" or "grease" payments that were made to ensure that governmental functionaries discharged certain "ministerial or clerical duties." These would include, again according to the Justice Department, routine bureaucratic tasks, such as obtaining permits or licenses; processing papers, such as visas and work orders, providing phone service, power, or water supply; the approval of the loading and unloading of cargo; and inspections associated with the performance of a contract or the transit of goods.

The FCPA does not prohibit U.S. MNCs from making such facilitating payments, and for many this continues to make the issue of bribery murky. Many ethicists and others concerned with matters of corruption have argued that the FCPA exception granted to facilitating payments that "grease the wheels of industry" is based on the recognition that other countries are not prohibiting their MNCs from making such payments and that this would give them an unfair business advantage over U.S.-based MNCs. Even so, goes one argument, such payments are bribes by any other name and are unethical and questionable per se regardless of how many countries fail to prohibit them. Just because many do it, it does not follow that it is morally right to do it. This "grease payment" controversy has swirled around the FCPA for quite some time, and there is no end to this debate in sight.

Nonetheless, the effects of the FCPA on the way American firms do business have been far reaching. Once again, according to the Justice Department, several firms that paid bribes to foreign officials have been the subjects of criminal and civil enforcement actions, resulting in large fines and suspension and debarment from federal procurement contracting, and in some cases, their employees and officers have gone to jail. To avoid such consequences, many MNCs have implemented internal policies, codes of international business ethics, and detailed compliance training programs intended to prevent and to detect illegal international business payments.

Host Country Obligations

Another problem with MNCs that is often cited centers on the role that they sometimes play in their host countries, which also happen to be developing nations, or less economically developed countries. Here the MNC is often thought of as a large hulking intruder that exploits both natural and human host country resources for its own monetary interests and profit by turning the public goods of the poorer nations into private gain for its shareholders. These concerns about the presence of MNC in the less economically developed countries were underscored with the unfolding of a number of highly publicized international events that are now classic case studies used by business ethicists in their research and writings about MNCs. For example, one such event was the 1984 Union Carbide (now part of Dow Chemical Company) toxic gas leak of methyl isocyanate (MIC), a highly toxic substance used in making the widely used pesticide Sevin, at Bhopal, India. To this day, the pictures of Indian women and children who were killed or left alive with crippling injuries continue to grip people who visit the numerous Web sites dedicated to the victims of Bhopal.

The tragedy at Bhopal remains the world's single worst industrial accident. Although the estimated numbers fluctuate widely depending on the source, some estimates are that of the 520,000 people exposed to MIC, 3,800 died immediately and more than half a million people were seriously injured. Some have held that the accident was due to a negligent attitude on the part of Union Carbide toward its Indian subsidiary, in general, and toward its facility at Bhopal, in particular. There were six major accidents at this site in the previous 6 years, for example. Moreover, many claim that Union Carbide was reluctant to meet its obligations to the victims of Bhopal as it engaged in what seemed like a legal standoff with the Indian government (which itself came under great criticism for its distribution of compensation to the citizens of Bhopal). As of 1994, Union Carbide had only fulfilled $3.1 of its $470 million legal obligation to the victims of Bhopal. This case has become a lesson in reputation management for MNCs on how not to respond to accidents that they are perceived to have caused.

Another case example occurred in 1995, when there was reaction from around the world to the hangings of Ken Saro-Wiwa and eight other Ogoni activist leaders in Nigeria. The Netherlands-based Royal Dutch Shell (and British Petroleum to a lesser extent) was alleged to have been a major supporter of Nigeria's military dictatorship and its attempts to silence the Ogoni people. The Ogoni had protested what it called an "ecological war" being waged against its homelands in the Niger River delta by the large MNC oil companies that were operating oil wells, gas flares, and pipelines that the Ogoni found offensive and destructive. While Shell and other MNCs were making large profits by sending crude to the oil-thirsty West, the Ogoni people remained stuck in their cycle of poverty and misery. It appeared that their land was being exploited against their will without any compensation being given to them. In reaction, they mounted a large demonstration in January 1993, organizing 300,000 people to gather and march in a country that had banned all forms of political free speech. This protest movement ultimately led to the November 1995 hangings of Saro-Wiwa and the other Ogoni leaders. Shell was criticized as an accomplice to these hangings given that it seemed to be propping up the military dictatorship with its economic largess. In response to the critical worldwide outpouring of voices raised against them after the death of Saro-Wiwa, Shell mounted a major ethics overhaul by reexamining its corporate policies and strategies with respect to its obligations to the people of less economically developed countries.

Also in 1995, Shell's *Brent Spar* controversy burst on the scene, creating yet another public relations and reputation nightmare for the MNC. *Brent Spar* was an old and decaying oil storage platform in the North Sea. Greenpeace and other vocal NGOs protested Shell's plan to disassemble the platform and dispose the parts and the oil still contained in the platform directly into the ocean. Greenpeace wanted Shell to consider a reclamation plan by bring the platform to shore and dismantling it there. Shell thought this recycling effort was much too expensive. As a result of the standoff, Shell was condemned globally for putting economic values ahead of environmental ones. After there was some violence at Shell gas stations in Germany and after Greenpeace had occupied the rig twice, Shell reconsidered its decision and towed the platform to Norway, where it was recycled for use in the construction of a ferry terminal. But, in a twist to this case, Greenpeace was forced to admit it had made a mistake about the amount of waste oil that the platform contained and was thought to be damaging to the ocean environment, if dumped in the North Atlantic per Shell's plans. As a result, about 6 months after the platform had been moved to Norway, Greenpeace sent Shell a formal letter in which they apologized for this mistaken calculation. Brent Spar is a good MNC case to demonstrate that NGOs aren't always correct in their critiques of MNCs and that the careful observer of the dance that goes on between NGOs and MNCs should keep in mind that all groups, like all humans, are fallible.

Another event that brought the issues of ICR home to many U.S. citizens was the numerous allegations of child labor and sweatshop conditions that were attributed to international business concerns and large MNCs in the apparel industry such as Nike, Adidas, Reebok, Benneton, Disney, Gap, and Levi Strauss. One of the most publicized cases was that of Kathie Lee Gifford's line of sportswear, which was shown to have been produced in sweatshops both abroad and in the United States. For example, at Global Fashions, a Honduran factory that made her clothing, it was alleged that 5-year-old girls earned 31 cents an hour and worked 75 hours per week.

A representative list of case studies of the questionable practices of MNCs could become rather long. In addition to many documented cases of sex discrimination, instances of fraud, and other financial improprieties, this list would include publicized examples such as the Nestlé infant food formula controversy; the Mitsubishi salt factory and the gray whales habitat incident at Laguna San Ignacio, Mexico; the intellectual property rights controversy of pharmaceutical MNCs and AIDS drugs produced in Africa; MNCs such as Wal-Mart (in 2005 it was the world's largest MNC) and Levi Strauss and the propriety of business dealings with China given its human rights record; the French-based MNC Total and Unocal oil pipeline built with forced labor provided by the military dictatorship in Myanmar; former president of Mexico Raul Salinas and alleged money laundering at Citibank; and so on.

What these case examples seem to demonstrate and thematize is the recurring exploitation of developing countries in which a giant and powerful MNC seemingly engages in self-serving activities that use and/or misuse the human or natural resources of the countries that had hosted them. They raise the question of how MNCs should determine their moral obligations to their host countries. Critics have argued that such practices are not only immediately damaging to the environment or harmful to people but that they also lead to a kind of geopolitical condition that has been labeled the "dependency theory," a political position that is often framed as the "development of underdevelopment." The intent and the claim here are to demonstrate that the more economically developed countries have kept the less economically developed countries of the world in a perpetual state of reliance or dependence on them. According to this account, the less economically developed nations have had the surplus of their productive efforts siphoned off by the greed and profit-taking activities of MNCs and, because of this, they have no ability to reinvest into their own economic development, thereby stifling any potential economic growth and continuing the cycle of misery and poverty in these nations.

These cases raise the question about the bona fide duties and obligations that MNC have to host countries and how these should be carried out. Answers to this responsibility question have been formulated by individuals such as business ethicists who are interested in the crafting of an answer based on particular ethical theories. Other individuals have a more practical concern and wish to see MNCs take concrete action to implement responsible behaviors. These latter individuals often form NGOs that have set as their mission the promotion and spotlighting of issues having to do with ICR. This movement has grown dramatically over the course of the past several years, and in addition to the previously mentioned Greenpeace, one can cite several leading NGOs that have made MNC watching and critiquing the main part of their trade. A shortlist would include Social Accountability International (the United States), CSR Europe (Belgium), International Business Leaders Forum (the United Kingdom), the Global Reporting Initiative (the Netherlands), The Copenhagen Centre (Denmark), and SustainAbility (the United Kingdom).

Cultural Imperialism

Those who have been critical of the process of globalization as outlined above often also criticize MNCs for their role in that process, which they refer to as "cultural imperialism." Cultural imperialism can be defined as the imposition, supplanting or erosion of one culture and its characteristic practices—language, customs, mores, values, and so on—by another culture that is considered the dominating one, because it is the culture of a larger and more powerful nation or region that can easily make such impositions on other cultures.

In the area of communications studies, "cultural imperialism theory" has sprung up as an academic specialty and it includes the study, analysis, and discussion of central concepts such as "media imperialism," "cultural dependency and domination," "cultural synchronization," and "electronic colonialism." Herbert Schiller, who is often cited in this field, may have been among the first to establish the term *cultural imperialism*. He meant for it to describe and explain the way in which MNCs, especially those in the media industry and based in the more economically developed countries, have dominated the less economically developed countries.

In general, the term has been used more often than not in a derisive manner. Most theorists seem to hold that the effects of cultural imperialism are deleterious. They claim that history has many examples to demonstrate how cultural imperialism operates and that the cultural imperialism of today's globalization will result in the same kind of destruction that befell past cultures. The examples most used in this context are those of empire-building cultures that spread through the ancient world and the more recent effort to colonize the "New World" by the Western European powers. The argument goes that just as the past dominant cultures supplanted and replaced the cultures of the lands that they "conquered" (sometimes to the point of extinction), so too today is there such a replacement of cultures being affected by "multinational capitalism" that is transforming the globe into one primary culture, namely, Western culture as defined by the customs, practices, and values of the United States and Western Europe. Soon all the people of the world will be in the same culture that is typified by the drinking of Coca Cola, the eating of McDonald's hamburgers, and the watching of movies made in Hollywood.

It should be noted, though, that theories of cultural imperialism are not without their detractors. Many find that as a theory it is lacking on epistemological grounds, because it relies on pure descriptive analysis and has no genuine explanatory import or power of predictability that are characteristics of a good scientific theory. Others have argued that the "discipline" lacks conceptual precision and that its main ideas are more like assumptions than actualities. Finally, critics have held that the theory is primarily motivated by the ideological leanings of its proponents and should be readily dismissed as a form of political rhetoric and polemic.

But in any case, the term has become a fairly common one outside of academia, and it can be found as having a certain cachet in newspaper editorials, magazines, blogs, and the popular literature of the day. In this context, too, the meaning is clear that what is meant is a globalizing, ethnocentric movement where market capitalism that is exported by the large MNCs primarily from the United States and Western Europe is hard at work in the dismantling and disassembly of the cultures of the world and replacing them with new and different customs, mores, and values. But, there has been a movement in some countries to resist the leveling effects of cultural imperialism (even in the West, France stands out as such an example), and there are many who reject the basic assumption of cultural imperialism and the thesis that what globalization and market capitalism have to offer is inherently corrosive or undermining of culture. These counter-critics argue that due to the efforts of MNCs and globalization, the standard of living of most people around the world has improved since World War II. Moreover, they say that many "modern miracles"—communication technology, the global distribution of goods, and ongoing increases in the longevity of the lives of people as well as their basic medical and health conditions—would not have been possible without the economies of scale that MNC can bring. In short, for this group, MNCs have been a boon to the world and not a burden. There is little doubt that this debate between the advocates and the detractors of MNCs over the relative merits of these organizations will continue well on into the foreseeable future.

Monitoring MNCs

Given the kinds of ethical issues and problems generated by MNC practices, it is not surprising that there have been a number of attempts to monitor MNC behavior and to establish measures that might serve as counters to the power that MNCs seem to have accumulated as major geopolitical players on the world's stage. A survey of these monitoring attempts would include the establishment of voluntary codes of conduct by MNCs, the movement to institute a system of measuring and reporting the responsibility of an MNC with respect to the environmental and social impacts of its practices in host countries, and the pressure of different groups that has been brought to bear on MNCs over the years to take stock of their practices and include and institutionalize more ethical awareness. This last item also refers to the activities of such world-renowned organizations as the Organisation for Economic Co-operation and Development (OECD) and the United Nations that have introduced influential programs called the "Guidelines for Multinational Corporations" and "The Global Compact," respectively.

Among the first and earliest attempts to monitor and bridle the power of MNCs was a self-regulatory effort on the part of MNCs themselves to set up codes of corporate conduct and compliance training programs. In the 1970s, only some MNCs had designed and adopted such codes, but today nearly all the Fortune 500 companies have them. The overall goal of these tools is to institutionalize ethics, to alert managers and employees of their obligations as associates in an MNC, and to create a climate of compliance with the requirements of the code. Many organizations go one step further and have mandatory training programs for managers and employees that familiarize them with code content and other aspects of their work, especially if they will become expatriate employees.

Most MNC voluntary codes of conduct contain typical planks or provisions dealing with host country operations that include or cover areas such as

- respect for the traditions, customs, and values of the host country;
- obeying host country laws and regulations;
- noninterference in the domestic affairs of the host country;
- institution of fair labor and employment standards;
- establishment of environmental obligations to the host country;
- a commitment to transparency in business dealings;
- pledges to avoid corrupting behavior (bribery or gift giving);
- the avoidance of tax evasion by price-transferring practices;
- expressions to enter into fair contracts and to renegotiate any existing unfair arrangements; and
- statements of philanthropic intent where the social and economic goals of the host country are recognized and promises to contribute to them are made.

In addition to the institutionalization of MNC ethics through code enforcement undertaken by individual MNCs themselves, there have been other forms of self-regulation that have been implemented and offered by industry trade groups or associations. For example, the Chemical Manufacturing Association—the chemical industry trade association now named the American Chemistry Council—set up several initiatives dealing with ways to alert the public to potential threats and to create safeguards within the industry especially after the Bhopal incident. Community Awareness and Emergency Response (CAER) programs give the public access to important information on hazardous chemicals, and the Responsible Care program attempts to reduce workplace accidents and increase health and safety awareness as well as to promote good environmental practices. This latter program likewise standardizes performance and improvement measures on the part of MNCs in the chemical industry.

Measuring and reporting performance and impact is another major monitoring area in which MNCs have been active, sometimes at the behest of groups external to them. A set of NGOs and academic research centers in the field of international business ethics have been quite vocal in expressing their views that MNCs should be engaging in the public reporting of their practices that have an effect not only on bottom-line results but also on society and the environment. One of the more prominent academic groups that is active in this area is the Centre for Social and Environmental Accounting Research (CSEAR) that is housed at the University of Glasgow. According to its mission and working with the general assumption that accounting and accountability should go hand in hand, some of the topics covered in research reports, discussion papers, and scholarly treatises at CSEAR deal with issues such as the economics of sustainability; environmental management; the actual process of social, ethical, and environmental reporting by MNCs; social and environmental cost internalization by markets and organizations; the relationship between social and environmental disclosure and share price performance; and the articulation of the standards for social and environmental reports.

The Global Reporting Initiative (GRI), housed in Amsterdam, is a good example of an international sustainability reporting institution from the ranks of NGOs. It is affiliated with the United Nations serving as one of the United Nations Environment Programme (UNEP) Collaborating Centres. Its stated mission is to develop and disseminate globally applicable sustainability reporting guidelines. These Guidelines are for voluntary use by organizations in their reporting on the economic, environmental, and social dimensions of their activities, products, and services. The GRI incorporates the active participation of representatives from business, accountancy, investment, environmental, human rights, research, and labor organizations from around the world. The GRI guidelines

- present reporting principles and specific content to guide the preparation of organization-level sustainability reports;
- assist organizations in presenting a balanced and reasonable picture of their economic, environmental, and social performance;
- promote comparability of sustainability reports, while taking into account the practical considerations related to disclosing information across a diverse range of organizations, many with extensive and geographically dispersed operations;
- support benchmarking and assessment of sustainability performance with respect to codes, performance standards, and voluntary initiatives; and
- serve as an instrument to facilitate stakeholder engagement.

A final monitoring activity that should be highlighted is provided by major groups external to MNCs. One such group is the OECD. The OECD is an international agency that supports programs designed to facilitate trade and development. Established in 1961 to replace the Organization for European Economic Co-operation, the OECD is composed of 30 member countries and has active relationships with 70 additional countries, civil society organizations, and NGOs. The OECD member countries produce two thirds of the world's goods and services, and the agency is designed to craft international conventions and agreements, decisions, and recommendations that promote a global economy. The OECD "Guidelines for Multinational Enterprises" was finalized and agreed to by the member countries in June 2000.

These Guidelines are considered recommendations to MNCs made by OECD governments; they are addressed to companies and not to their governments. Hence, these provisions cannot be taken as binding international law, but rather as a voluntary code of conduct to guide MNC practices. The document contains provisions to address some of the ethical and legal concerns that OECD member nations had in response to the kinds of behavior on the part of MNCs that are outlined above. Comprised of various planks, the Guidelines have the overall goal to encourage the positive contributions that multinational enterprises can make to economic and social progress worldwide. The Guidelines themselves are divided into eight chapters and each deals in detail with typical sorts of MNC practices. These chapters are arranged according to the following categories: general policies, information disclosure, competition, financing, taxation, employment and industrial relations, environment, and science and technology.

Similar in nature, if not in scope, to the OECD Guidelines are the 1977 "Tripartite Declaration of Principles Concerning Multinational Enterprises and Social Policy" from the International Labour Organization (ILO). The ILO devised a set of principles regarding the social aspects of multinational enterprises, for the use of governments, employee organizations, and MNCs themselves. The main scope and focus of this document is employment: safe working conditions, job security, equal opportunity in employment, and fairness in industrial relations between labor and management. Again, the provisions of the ILO principles are voluntary in nature.

A last organizational monitoring system to note is the United Nation's "Global Compact" that became an international reality in 1999. The Global Compact begins with 10 principles that deal with human rights, labor, the environment, and anticorruption and are based on other documents taken from both within and outside of the United Nations such as "The Universal Declaration of Human Rights," The ILO's "Declaration on Fundamental Principles and Rights at Work" and the United Nation's "Convention Against Corruption." The Global Compact asks MNC (as well as domestic companies) to embrace, support, and enact, within their sphere of influence, the several values found in the 10 principles. Now, many hundreds of companies from all over the world and international labor and civil society organizations are participants in the Global Compact. The Global Compact Office is supported by six UN agencies.

Although, the Global Compact is yet another voluntary program, there was a recent policy announcement at the United Nations requiring corporate participants in the Global Compact to disclose to their stakeholders the progress that they are achieving in implementing the 10 principles. Hence, this program may transform itself into a hybrid that will combine the performance and measurement approach with an effort to entice MNCs to engage in ethical practices voluntarily. It can be hoped that such a new approach to an old problem might be successful to further the aims of MNC business ethics and be of some beneficence to the global society.

—Peter Madsen

See also AIDS, Social and Ethical Implications for Business; Bhopal; Corporate Citizenship; Corporate Social Responsibility (CSR) and Corporate Social Performance (CSP); Cultural Imperialism; Developing Countries, Business Ethics in; Developing World; Foreign Corrupt Practices Act of 1977 (FCPA); Global Business Citizenship; Global Codes of Conduct; Globalization; Global Reporting Initiative; International Business Ethics; International Labour Organization (ILO); International Trade; Maquiladoras; Multinational Marketing; Nike, Inc.; Organisation for Economic Co-operation and Development (OECD); Postmodernism and Business Ethics; Sweatshops; Transparency; Transparency International; United Nations Global Compact

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Multinational Marketing

Multinational marketing involves the domestic firm extending its products into multiple foreign markets. Multinational marketing examines the discrete differences between domestic and foreign markets. These foreign markets in many cases operate differently than the domestic markets. Firms have to account for another tier of marketing attributes to understand the foreign market. Several factors make the environment for multinational marketing more complex. The marketer has to initially recognize that each country is a sovereign entity. Basically, the country decides how it is to be run without any direct intervention from another country. The country is run in a manner that accommodates the government's political interest. The government has an overbearing influence over the environmental factors that affect a firm marketing in a foreign country. First and foremost, a firm must obtain permission from the government to either produce and/or sell a good in the country. So for a firm to be engaged in multinational marketing, it must know how to operate within another type of framework. The factors that shape this new framework can be broken down into categories that involve but are not limited to social, political, legal, economic, governmental, cultural, language, customs, and topological factors. These factors help institutionalize the characteristics of the country, and the firm must adapt to these principles by learning how these factors affect the delivery of marketing goods to consumers.

In many ways, marketing products globally is the same as marketing them at home. Regardless of which part of the world the firm sells in, the marketing program must be centered on a sound product or service that is properly priced, promoted, and distributed to a carefully selected target market. In other words, the marketing manager has the same controllable decision variables in both domestic and nondomestic markets. Although the development of a multinational marketing program may be the same in either domestic or nondomestic markets, special problems are encountered during the implementation of marketing programs in nondomestic markets. These problems often arise because of the environmental differences that exist among various countries that marketing managers may be unfamiliar with.

In examining the differences between countries, the marketer must focus on how the consumer buying behavior is affected by the environmental forces. Many of these factors create distance between how the firm currently markets versus what can be done in the new environment. The environmental factors change the buying behavior and pressure the firm into revisiting its strategy for marketing in a new market. Sometimes the market changes so much that the firm has to rethink its entire strategic approach to entering the market. Although the traditional marketing mix factors of price, place, promotion, and product still reign as the most important factors in marketing, their emphasis changes when engaging in multinational marketing. The global factors actually affect how these marketing mix elements are used by the marketer. The global factors in most cases change the good that is delivered to the consumer. This directly limits the firm from being able to extend its goodwill previously established in the good's original form.

For these reasons, most firms tend to establish separate marketing plans for doing business in different countries. This is the essence of what multinational marketing is all about. Creating a separate marketing approach requires the firm to come up with unique strategies to enter heterogeneous foreign markets. The marketer must integrate the marketing mix factors with the global environmental factors to cultivate an effective approach to market in a country. The firm must conduct an extensive analysis of the global factors to determine the strategy for entering the country. In most cases, it is difficult for a firm to standardize the market attributes found in each country. This occurs because each factor is so unique to the country that it creates problems for the firm. The firm has to make a key decision early on in the process whether it is going to be an importer or an exporter. Importers make the good in another location and sell it around the world. Of course, they are subject to tariffs, quotas, duties, and sometimes, licensing restrictions that might alter the good even more. Conversely, they can choose to be an exporter, which means that they produce a good in a country and sell it in that country. A firm that directly invests in a country takes on the highest level of risk associated with multinational marketing. They are subject to potential loss of assets and stringent rules for doing business in the country. If there is a high degree of uncertainty surrounding the country, a firm might decide to be an importer to mitigate the risk.

Language

Distance barriers are created by language or labeling requirements when products are produced using a certain language in advertising the good. Although these changes may be subtle in nature, they can have a huge effect on a good. Firms have to consider what language barriers exist and how they can modify a good's image and goodwill. Firms don't want to lose value that they have created in a product. Although language is a significant barrier, the firm has to find a way to work within new guidelines to maintain value and satisfy country requirements. Also, language barriers can affect the manner in which a firm advertises in foreign markets. Depending on the advertising method, language may limit the effectiveness of the medium of communication. Sometimes the meaning of words changes when put into another language. So the firm has to figure out how to preserve the integrity of the meaning, while using a different language to communicate the message.

Culture

Another factor that the firm has to contend with is culture. Globalization has made accessing foreign markets easier. Culture is a problematic issue for many marketers since it is inherently nebulous and often difficult to understand. One may violate the cultural norms of another country without being informed of this, and people from different cultures may feel uncomfortable in each other's presence without knowing exactly why. For example, McDonald's prided itself on selling standardized hamburgers to a mass market of consumers. When they wanted to expand into the market in India, they would have a problem because beef is not an acceptable food for this culture. The Indian culture views the cow as a sacred animal and, therefore, Indians don't consume beef as a staple daily food as people do in the United States.

In some other cultures, what you see is what you get, and the speaker is expected to make his or her points clear and limit ambiguity. This is the case in the United States—if you have something on your mind, you are expected to say it directly, subject to some reasonable standards of diplomacy. In Japan, in contrast, facial expressions and what is *not* said may be an important clue to understanding a speaker's meaning. Thus, it may be very difficult for Japanese speakers to understand another's written communication. The nature of languages may exacerbate this phenomenon—while the German language is very precise, Chinese lacks many grammatical features, and the meaning of words may be somewhat less precise. English ranks somewhere in the middle of this continuum.

However, the culture that awaits the firms has not drastically changed. The firm must understand the cultural dimensions that exist and determine how differences can affect buying behavior. Culture is the pattern of behavior and thinking that people living in social groups learn, create, and share. Culture distinguishes one human group from another. Foreign culture includes beliefs, rules of behavior, language, rituals, art, technology, styles of dress, ways of producing and cooking food, religion, and political and economic systems. The firm must analyze these traits and compare them with their host country standards. This helps the firm have a better understanding of consumers from that market. Some products are far more vulnerable to cultural differences than others.

For instance, products that are nondurable ("perishable") are extremely sensitive to cultural changes. Some examples of these products include fresh foods, vegetables, clothing, carbonated drinks, dairy products, wines, meats, and other forms of textiles. On the other hand, durable products are less sensitive to cultural changes but may be affected by environmental factors. In European countries, there is a different standard for electricity, which means that the voltage on most consumer electronic devices is different. There are two basic standards for voltage and frequency in the world. One is the North American standard of 110 to 120 volts at 60 Hz, which uses plugs A and B, and the other is the European standard of 220 to 240 volts at 50 Hz, which uses plugs C through M. This environmental change in electricity forces the firm to change the electrical connection to meet the requirements in different countries. Also, automobiles have a different standard because of the various environmental factors pertaining to emission standards.

Political

Understanding the political environment of a country is essential to obtaining permission to access a country to sell goods. Given the sovereign nature of most countries, they have a high degree of discretion in deciding how they choose to be governed. Thus, the political environment of countries is a critical concern for the international marketer, and they should examine the salient political features of global markets they plan to enter. A nation's sovereignty from an international law's point of view is independent and free from external control; enjoys full legal equality; governs its own territory; selects its own political, social, and economic systems; and has the power to enter into agreements with other nations. It is in the extension of national laws beyond a country's borders that much of the conflict in international business arises. Nations can and do abridge specific aspects of their sovereign rights in order to coexist with other countries. The European Union, North American Free Trade Agreement (NAFTA), and MERCOSUR are examples of nations voluntarily agreeing to give up some of their sovereign rights in order to participate with member nations for common, mutually beneficial goals. The ideal political climate for a multinational firm is a stable and friendly environment, but often that is not present. Since foreign businesses are judged by standards as variable as there are nations, the friendliness and stability of the government in each country must be assessed as an ongoing business practice. For example, the European Union limited Chiquita Banana from selling large quantities of bananas there and placed tariffs on the banana as well. By limiting supply and increasing the price the European Union made Chiquita's banana unattractive compared with other bananas in the marketplace.

The most important of the political conditions that concern an international business is the stability or instability of the prevailing government policies. Political parties may change or get reelected, but the main concern for firms is the continuity of the set rules or code of behavior regardless of the party in power. A change in the government does not always mean change in the level of political risks. In Italy, the political parties have changed 50 times since the end of World War II, but business continues to go on as usual in spite of the political turmoil.

The most severe political risk is confiscation, which is the seizing of a company's assets without payment. Less severe is expropriation, which requires reimbursement, for the government-seized investment. A third type of risk is domestication, which occurs when the host country takes steps to transfer foreign investments to national control and ownership through a series of government decrees. A change in the government's attitudes, policies, economic plans, and philosophies toward the role of foreign investment is the reason behind the decision to confiscate, expropriate, or domesticate existing foreign assets. Some products are more politically vulnerable than others, in that they receive more government attention. This special attention may result in positive or negative actions toward the company. Unfortunately, there are no absolute guidelines for marketers to follow whether the product will receive government attention or not.

There are some generalizations that help identify the tendency for products to be politically sensitive. Products that have an effect on the environment exchange rates, national and economic security, and the welfare of the people are more apt to be politically sensitive. For instance, the United States has banned the use of lead-based paint in homes. The Japanese government banned imports of beef from the United States after the discovery of the first case of mad cow disease in Washington State. For products judged nonessential, the risk would be greater, but for those thought to be making an important contribution, encouragement and special considerations could be available.

Economic

The marketer must develop an understanding of the economic factors that will influence the environment. The economic factors involve the size of the economy, the purchasing power parity that exists in the market, stability of the currency, foreign exchange rate, rate of inflation, rate of interest, disposable income in the economy, and the rate of unemployment. These factors determine whether the market is suitable for the firm to enter in order to sell a product. The marketer wants to enter markets that are stable and growing. The factors contribute to explaining the business cycle in a country. The marketer has to look at the current stage of economic development the country is in. It may not be an attractive market for the marketers if they have to allocate a large sum of resources and time to develop the market. The marketer should be able to measure the return from investing in a country.

Ultimately, the firm wants to remove its profits from the country. So looking at forward contracts to guarantee a stable return is essential for multinational firms that decide to invest in a country. This directly ties back to the stability of the country in terms of ensuring that its foreign exchange rate is not undervalued. The marketer should have a good idea of how many months they should take with a forward contract. The more unstable the environment, the longer the contract should be to mitigate risk.

For example, in 2002 when Dell Computer decided to sell computers in China, it found out that the per capita income was some $1,000 compared with $36,000 in the United States. Also, less than 1% of the population had a credit card. The Chinese government controlled the content that was permitted on the Internet as well. So Dell had to revise its strategy for selling its computers over the Internet in the Chinese market.

Legal

One of the greatest areas of concern for the marketer is in the legal area. The marketer wants to protect its intellectual property rights and must look at how developed the rules are in protecting a foreign firm's intellectual property rights. If the country does not allow the firm to enforce its rights effectively in the country, the firm stands the chance of losing a great deal of goodwill in their products. The marketer must examine the rules for advertising as well in the country. Sometimes a country may have specific limits on speech and the manner in which the firm can communicate a message. The country may have rules that limit guest workers and the type of workers that can be used in a country. Understanding the country's laws will help the marketer develop a multinational marketing strategy that works. In most countries, the biggest problem that firms run into is illegal use of their intellectual property rights (i.e., copyright, trademark, trade secret, and patents). Some countries don't have sophisticated rules in place to protect foreign intellectual property rights and thus their infringement is likely. For example, Yaqing, a Shanghai-based soft drink maker, lost a lawsuit last January against Coca Cola and its local bottler over the naming of a new beverage. Yaqing claimed the characters for Coke's Qoo fruit drink—"Ku-er" in Chinese—were too close to those of Yaqing's Kuhai drink. Yet a Shanghai court ruled that the two names were different enough for consumers not to confuse them.

Customs

The firm must examine the role of technology in the foreign country. Technology has allowed marketers to overcome certain barriers that in the past prevented them from entering certain markets. Technology has afforded many firms the ability to operate more efficiently over the long term. So an examination of the role of technologies in the multinational marketing plan is essential in today's environment. The multinational marketing firm pursues different strategies in each of its foreign markets. They could have as many different product variations, brand names, and advertising campaigns as countries in which they operate. Each overseas subsidiary is autonomous. Local marketers are given the authority to make the necessary decisions and are held accountable for their results. In effect, the multinational marketer competes on a market-by-market basis.

Topological

Last, in the process of marketing products in multiple countries, the firm must recognize the subtle differences in the topology of the country. In other words, the terrain and climate of the country will have a great impact on how the firm distributes its products. It might not be conducive to sell products in a similar manner as the United States based on the structure of the environment. In some countries, it is not common to see large shopping malls. It is more common to see smaller stores that sell a broad range of products. Also, the mechanism for reaching customers will be affected by the topology of the country. In some countries, because of the mountains and steep hills it is difficult to reach customers with traditional methods of advertising. For example, using the radio, television, and cable television may be limited in some foreign markets. So this is yet another challenge that the marketer has to consider in developing their marketing plan for each country.

Conclusion

Multinational marketing is a process that firms recognize they need to grasp in order to market in other countries. A continual evaluation of environmental factors is key to understanding these new markets. Firms must develop a careful and detailed approach for reaching consumers in various markets. They must work with the people in each country and find their unique differences to avoid alienating themselves from the market. Firms should not take an ethnocentric approach to examining each market but rather selectively choose a market and examine the environmental factors. After determining the core differences, the firm should establish a strategy for entering the market. These elements are mandatory for a firm to be successful in another country. Unfortunately, there are no shortcuts in learning about another country. But there is enough history available to learn about the country and develop a strategy for doing business in the environment.

—Sylvester E. Williams, IV

See also Consumer Goods; Consumer Preferences; Cross-Cultural Consumer Marketing; Global Business Environments; Multinational Corporations (MNCs)

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N

Nash Equilibrium

Named after its inventor, John Nash (1928–), a Nash equilibrium is a combination of strategies—one for each player—such that each individual's strategy maximizes their payoff against the strategies of the other players.

For example, the game in Figure 1 represents the barroom scene occurring during the "eureka" moment in Nash's biographical film, *A Beautiful Mind.* John and a rival can either approach a blonde or one of her friends. If both approach the blonde, they block each other; each receives a payoff of 0, as illustrated in the northwest cell. If John approaches the blonde and his rival a friend, John's payoff is 3 and his rival's is 1 (the northeast cell). The payoffs in this cell are circled because blonde maximizes John's payoff against the rival's strategy of friend (3 > 2), and friend maximizes the rival's payoff against John's strategy of blonde (1 > 0). Consequently, the strategy combination (blonde, friend) is a Nash equilibrium.

		Rival	
		Blonde	Friend
John	Blonde	0, 0	3, 1
	Friend	1, 3	2, 2

Figure 1 Beautiful Mind Game

Note: John's payoff is listed first; his rival's is listed second.

Equivalently, any collection of strategies is a Nash equilibrium if they are *mutual best replies.* For example, the payoffs in the southwest cell of this game are also circled because friend is John's *best reply* to the rival's strategy of blonde (1 > 0). Similarly, blonde is the rival's best reply—against John's strategy of friend—because 3 > 2.

It is useful to compare Nash equilibrium with an ethical norm, one that is incorrectly identified as the Nash equilibrium in the film itself. According to the golden rule John should approach a friend (doing what he would like his rival to do). Similarly, the rival should approach a friend (because this is what he would like John to do). Yet this outcome—corresponding to the southeast cell—is *not* a Nash equilibrium. Either would approach the blonde if the other approaches a friend.

Nash equilibrium is the predominant solution concept for noncooperative games because one always exists under very general conditions (e.g., irrespective of the number of players or the number of strategies each player possesses). Finding Nash equilibria may require the use of *mixed* (probabilistic) strategies. For example, in a principal-agent game the principal (manager) monitors the agent (worker) at random intervals rather than continuously standing over his or her shoulder. The two most common interpretations of mixed strategy Nash equilibria are epistemic and mass action. The epistemic interpretation treats Nash equilibrium as the prediction of the likelihood of behavior by rational players who have common knowledge about the game. In the mass action interpretation, a Nash equilibrium is the average frequency of behavior within a population of players randomly matched to play the game. This latter interpretation links Nash equilibrium to the biological solution concept of evolutionary stable strategy.

Nash equilibrium has proven to be an essential concept for auction design, such as the Federal Communication Commission's auctioning of spectrum licenses or eBay's initial public offering. The understanding of Nash behavior in competitive price setting is fundamental for detecting cartel behavior and in assessing the credibility of entry-deterring strategies such as predatory and limit pricing. Finally, in principal-agent relationships a fundamental trade-off exists between Nash equilibrium, Pareto efficiency, and budget balancing of managerial incentives and revenues, thereby identifying a further role for ethics in corporate governance.

—Daniel Arce

See also Agency, Theory of; Commons, The; Game Theory; Incentive Compatibility; Moral Hazard; Pareto Efficiency; Prisoner's Dilemma; Tragedy of the Commons

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National Ambient Air Quality Standards (NAAQS)

To control ambient air quality, the Clean Air Act, which was last amended in 1990, requires the Environmental Protection Agency (EPA) to set NAAQS for pollutants that are considered to be harmful to public health and the environment. The Clean Air Act established two types of standards for ambient air quality. Primary standards concern the minimum level of air quality necessary to keep people from becoming ill and are aimed at protecting public health. These primary standards are intended to provide an adequate margin of safety for the public, which has been defined to include a representative sample of so-called sensitive populations such as the elderly, children, and asthmatics. The secondary standards are aimed at the promotion of public welfare and the prevention of damage to animals, plant life, and property generally.

These standards have been set for six principal pollutants known as criteria pollutants. These are carbon monoxide, lead, nitrogen dioxide, particulate matter, ozone, and sulfur oxides. It should be noted that ozone is not directly emitted into the air but is formed by sunlight acting on emissions of nitrogen oxides and volatile organic compounds. There are also two categories of particulate matter: those that are of dimensions 10 μ or less and those of 2.5 μ or less. Each of these has different primary standards. These standards are performance rather than design standards; that is, they set the performance levels to be achieved rather than specifying the equipment that needs to be installed to clean up air pollution.

Because air pollution problems vary from place to place throughout the country, a regional concept was adopted for air pollution control through the establishment of air quality control regions. These air quality control regions are useful units for management and control because each region has individual problems and individual characteristics of pollution control. An air quality control region is defined by the EPA as an area with definite pollution problems, common pollution sources, and characteristic weather. States were given responsibility for drawing up plans called "state implementation plans" to attain the standards for the air quality regions within their boundaries. Individual states may have stronger pollution controls, but none can have weaker pollution controls than those set for the country as a whole.

Ambient air quality is measured by using a pollutant standards index (PSI), which provides the EPA with a uniform system of measuring pollution levels for the major regulated air pollutants. Once these levels are determined, the PSI figures are reported in all metropolitan areas of the country where the population exceeds 200,000 people. These index figures enable the public to determine whether air pollution levels in a particular location are good, moderate, unhealthful, or worse. The PSI places maximum emphasis on acute health effects occurring over very short periods of 24 hours or less rather than on chronic effects occurring over months or years.

The ethical and social issues for business revolve around the inability of the market system to respond to air pollution problems. In most cases, there is no incentive for business to control its air pollution emissions. Air pollution control equipment costs money, and if one company voluntarily incurs these costs, it puts that company at a competitive disadvantage. The quality of the air we breathe is a public good, and when goods such as clean air are indivisible among large numbers of people, the market will not allow for their provision. A system of regulation must be created that makes all businesses adhere to the same standards thus leaving them in the same competitive position as before the regulations were issued.

—Rogene A. Buchholz

See also Pollution; Regulation and Regulatory Agencies

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National Association of Securities Dealers (NASD)

The National Association of Securities Dealers (NASD) is a private, nonprofit, self-regulatory organization to which nearly all brokerage firms doing business in the United States are required to belong. Including more than 5,200 firms with almost half a million employees, NASD's board largely comes from member securities firms. Its purpose is to enforce practices that protect investor rights and help maintain efficient and fair markets. As such, NASD is the largest self-regulatory organization in the country. NASD regulatory activities include supervising and disciplining broker-dealers, analysis and oversight of over-the-counter market activities, and providing arbitration and mediation for most of the disputes in the industry. The NASD is empowered to take disciplinary actions such as imposing fines and even revoking licenses against firms and registered representatives that violate its rules.

Stock market manipulation was a major issue that Franklin D. Roosevelt emphasized in the 1932 election campaign. The Securities and Exchange Act of 1934 then established the legal foundation for self-regulation of the exchange markets. A system was set up under which the New York Stock Exchange, the American Stock Exchange, and other organized exchanges, and through them their member seat holders, would act as self-regulators for the newly created government body, the Securities and Exchange Commission (SEC).

NASD's formation in 1938 resulted from the Maloney Act that amended the Securities Exchange Act and provided for self-regulation of the over-the-counter market. The NASD acts as the enforcer for federal laws and SEC regulations and is in charge of surveillance and oversight of NASDAQ securities trading, formal review of arrangements for underwriting publicly issued securities, and complex requirements for submission of monthly financial statements. Its compliance program includes such safeguards as on-site inspections of member firms, review of advertising to protect investors from inaccurate claims, and testing to ensure that member firm personnel are qualified. NASD members also subscribe to the internal Rules of Fair Practice that proscribe ethics violations, such as recommending speculative securities to customers whose financial status does not warrant it or excessive trading ("churning") intended to generate more commissions.

The NASD is well funded by firm membership fees and assessments of registered representatives and applicants in addition to fines that it levies. In 1968, NASD initiated the electronic automated quote system that grew into the electronic stock market known as the NASDAQ, which eventually outstripped the NYSE in volume. In response to veiled criticism from the SEC that such commission generating activity posed a potential conflict of interest for NASD itself, NASD elected in January 2000 to restructure and exit the trading business. By 2003, NASD had sold its holdings in the NASDAQ operation as well as in the AMEX to private investors. It remains, however, under contract to regulate those markets.

A persistent criticism of NASD is that its enforcement actions hit smaller firms for relatively minor abuses hard while ignoring major problems throughout the industry. Critics suggest that this lukewarm enforcement is emblematic of self-regulatory bodies in which the interests of the consumer become secondary to those of the supposedly regulated industry. In response to this criticism, NASD has stepped up its market surveillance activities in the past few years. At the same time, growing discord between small and large firms within the NASD has led to increasingly contentious board elections. These internal controversies coupled with growing public concern about abuses in the financial market suggest more contentious times for the NASD in the future.

—Anthony D. Branch

See also Commodity Futures Trading Commission; Great Depression; Prudent Investor Rule; Securities Industry Association

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National Federation of Independent Business

The National Federation of Independent Business (NFIB) is the largest political advocacy organization in the United States that represents small and independent businesses. The purpose of the organization is to provide resources to assist small business owners and managers, particularly through its effort to influence public policy at the national and state levels.

The NFIB has a membership of about 650,000. Although smaller than the Chamber of Commerce's membership of 3 million, the NFIB has a reputation in the last decade as being the most influential or powerful of all business lobbying organizations. The NFIB was founded by Wilson Harder in 1943, and he had a major goal then of trying to give small and independent businesses a voice in government decision making. Jack Faris, as the current president and CEO of the NFIB, has led the organization since 1992. Under the leadership of Faris and through an emphasis on grassroots lobbying, the NFIB has been given substantial credit for early and effective actions that helped defeat the Clinton Administration's plans for health care a decade ago.

Since the NFIB has a membership that crosses many business sectors and industries, it pursues a broad set, but limited number, of legislative goals for which consensus of its members is possible. The NFIB assumes a much more conservative political stance on most issues than several much smaller organizations dedicated to lobbying for and addressing small business interests. The National Small Business United created in 1937 is less partisan in its lobbying connections. The even smaller American Small Business Alliance, established in the mid-1990s with the involvement of Silicon Valley and other entrepreneurs, has endorsed more liberal policy alternatives than either the NFIB or National Small Business United. The American Small Business Alliance's support for issues such as a national minimum-wage hike and employer-sponsored day care places it in sharp contrast to typical NFIB positions. Among the NFIB's recent public policy priorities have been tax reduction/simplification, tort reforms and caps for medical liability, changes in health care emphasizing reduced cost, and reduction of unnecessary, excessive, and intrusive regulations.

The NFIB offers its members a variety of information sources and services. Among these benefits are reports on monthly economic trends and business-related forecasts, a ballot on public policy issues that members receive three times a year, a magazine called *MyBusiness* that is published six times each year, and its Web site informing members of its political and legislative priorities and outcomes. The NFIB actively seeks partnerships with business firms that can provide discounted products and services for its members. It has also formed alliances with other political advocacy organizations. One example is its alliance with the Moms in Business Network in 2005.

—Stephen L. Payne

See also Corporate Political Advocacy; Interest Groups

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National Highway Traffic Safety Administration (NHTSA)

The National Highway Traffic Safety Administration (NHTSA) was created by the National Traffic and Motor Vehicle Safety Act of 1966 to set safety standards for motor vehicles and motor vehicle equipment. The Energy Policy and Conservation Act and Clean Air Act Amendments of 1970 also gave the agency the authority to set standards for fuel economy and emissions. This agency is located within the Department of Transportation with the general purpose of protecting the public from unreasonable risk of injury resulting from the usage of motor vehicles and is responsible for developing programs to reduce deaths and injuries as well as economic losses resulting from motor vehicle crashes.

The specific responsibilities of the agency include (1) setting and enforcing mandatory average fuel economy standards for new motor vehicles; (2) regulating the safety performance of new and used motor vehicles and their equipment such as tires; (3) investigating auto safety defects not covered by standards and requiring manufacturers to remedy such defects; (4) setting standards for auto bumpers, auto ratings (e.g., for crashes), and diagnostic auto inspections; and (5) administering the federal odometer law to prevent odometer fraud.

Other responsibilities include helping state and local governments conduct effective local highway safety programs as well as helping them reduce the threat of drunk drivers to local communities; establishing and enforcing regulations related to vehicles and antitheft devices; providing information to consumers on topics related to motor vehicle safety; and encouraging the use of air bags, child safety seats, and seat belts in motor vehicles. The agency also maintains a toll-free hotline where consumers can register complaints about safety, request information about recalls, report alleged defects in auto vehicles, and request publications dealing with highway and traffic safety.

The agency conducts research on traffic safety and the behavior of drivers so that improvements in safety can be accomplished in the most efficient and effective manner. It maintains a research and development program that supports the agency's goal to reduce motor vehicle injuries and fatalities. This program engages in extensive research, development, testing, crash investigation, and data collection and analysis activities. With regard to the latter, it maintains a National Center for Statistics and Analysis that helps gain an understanding of the nature, causes, and injury outcomes of crashes and the strategies and interventions that will reduce crashes and their consequences. NHTSA has also created a Fatality Analysis Reporting System to help interested parties identify safety problems and evaluate initiatives in motor vehicle safety standards and highway safety.

NHTSA began to evaluate its Federal Motor Vehicle Safety Standards in 1975 and, by October 2004, had evaluated the effectiveness of practically all the life-saving technologies that had been introduced in passenger cars, pickup trucks, vans, and sports utility vehicles from approximately the year 1960 through the later 1990s. A statistical model was used that combined these life-saving technologies to estimate the number of lives saved from 1960 to 2002, and, based on this model, the agency estimated that during this time period these technologies saved 328,551 lives. The annual number of lives saved grew steadily from 115 in 1960 to 24,561 in 2002. During the early years, a small number of people used seat belts, while in later years, seat belt usage stood at 75 percent and most cars and trucks were equipped with numerous other safety technologies that helped improve the figures.

—Rogene A. Buchholz

See also Regulation and Regulatory Agencies

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National Industrial Recovery Act

Passed by Congress in 1933, the National Industrial Recovery Act (NIRA) was one of several measures that were passed by Congress and supported by the Roosevelt administration that were aimed at helping the nation recover from the Great Depression. The NIRA was a unique experiment in U.S. history as it suspended the antitrust laws that were passed to root out conspiracies and combinations in restraint of trade and sanctioned and supported an alliance of industries. Under the law, companies were required to write industrywide codes of fair competition that effectively fixed wages and prices, established production quotas, and placed restrictions on the entry of other companies into the alliances. These codes were a form of industry self-regulation and represented an attempt to regulate and plan the entire economy to promote stable growth and prevent another depression.

Under the act, employees were given the right to organize unions and could not be required, as a condition of employment, to join or to refrain from joining a labor organization. Prior to this act, the courts upheld the right of employers to do just about anything to prevent the formation of unions. Companies could fire workers for joining unions, force them to sign a pledge not to join a union as a condition of employment, require them to belong to company unions, and spy on them to stop unionism before it got started. Attempts to form unions without government help were thus not very successful, and before the Great Depression, interest in unionism was waning. The NIRA rekindled this interest.

The law created a National Recovery Administration (NRA) to promote compliance with the act on the part of corporations. This administration was chiefly engaged in drawing up industrial codes for companies to adopt and was empowered to make voluntary agreements with companies regarding hours of work, rates of pay, and prices to charge for their products. More than 500 such codes were adopted by various industries, and patriotic appeals were made to the public to encourage wider compliance. Companies that voluntarily complied could display the Blue Eagle emblem in their facilities, signifying NRA participation.

According to most historians, these codes did little to help economic recovery and, by raising prices, actually made the economy worse. Under criticism from all sides, the NRA did not last long enough to fully implement its policies. In a case called the *Schechter Poultry Corporation v. The United States* decided in May 1935, the Supreme Court declared the NIRA unconstitutional because it assigned lawmaking powers to the NRA, which violated the Constitution's allocation of such powers to Congress, and said that the provisions of the poultry code (the case in question) did not constitute a valid regulation of interstate commerce and thus unreasonably stretched the Commerce Clause. Many of the labor provisions in the NIRA, however, were reenacted in later legislation.

—Rogene A. Buchholz

See also Antitrust Laws; Great Depression; Regulation and Regulatory Agencies

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Nationalization

Nationalization is the involuntary transfer of private property to government ownership through confiscation, expropriation, or seizure, often with no compensation paid to the private owner. If the asset is transferred through a forced sale, the price is usually nonnegotiable and often set below the fair market value. In rare cases, an asset is confiscated by one level of government from another, as might be the case when a national entity seizes municipal property, for example, to consolidate an industry under national control.

The classic argument for nationalization stems from the idea that some essential services and commodities are so critical to citizen's lives that they cannot be entrusted to private enterprises, with motives (usually profit) that may be at odds with ensuring the general welfare. By nationalizing these assets, the government then assures the protection of key resources and revenue for use in meeting national objectives.

Governments have historically provided a number of specific reasons for engaging in nationalization: closing the gap between extreme wealth and poverty through income redistribution; environmental protection through nationalization of land and water resources; avoidance of wasteful competition by nationalizing and joining enterprises operating in natural monopoly sectors of the economy—such as utility companies—to promote reduced costs; protecting critical national security assets, such as airports, railroads, and telecommunications; and leveraging assets for economically strategic reasons, in the construction industries, for example, and even in commercial development to generate revenue for states or localities.

History of Nationalization

Nationalization is a 20th-century phenomenon that has often occurred when less developed countries decide to assume control of foreign-owned assets deemed strategic. In 1938, for example, the Mexican government expropriated all oil properties belonging to North American corporations, while in 1951 the Iranian parliament voted to take over all assets belonging to the Anglo-Iranian Oil Company. In the latter instance, Britain froze Iranian assets in England and brought a case against Iran to the International Court of Justice at The Hague; the court ruled in favor of Iran by arguing that a contract between a state and a private foreign corporation does not fall under international jurisdiction and that private foreign investors are therefore not protected by international law and must assume the risk of nationalization. The oil nationalization trend started by Mexico and Iran was followed by Venezuela, Saudi Arabia, Iraq, and Kuwait, and by the close of the century, most world oil had been nationalized.

Examples of nationalization in other industries include the nationalization of logistically important sectors (coal, gas, petroleum, railroads, airlines, communications) by the Labour Party in Britain after the Second World War; the Egyptian takeover of Suez Canal operations and infrastructure in 1956 in exchange for compensation to major French and British stockholders; the nationalization of foreign-owned copper mining enterprises in Chile in 1971; and most recently, the confiscation of white-owned farms by President Mugabe's government in Zimbabwe in the late 1990s.

The most dramatic nationalization trend occurred during the period of communist expansion starting early in the 20th century with the Russian revolution, where all industries, down to the retail level, suffered mass nationalization and conversion to state-run enterprises. With a few exceptions, such as Cuba and North Korea, this communist-induced trend had been reversed by the end of the century.

In the United States, nationalization has not been a significant issue, but it does appear periodically. For example, during the Korean War, President Harry S. Truman attempted, unsuccessfully, to seize the steel industry when it appeared that a nationwide strike was imminent.

Ethics and Nationalization

One can approach the ethics of nationalization by considering whether preserving the rights of individual property owners jeopardizes the collective rights of the citizens. In Iran, for example, governments had negotiated agreements (oil concessions) with foreign investors that subsequent administrations determined were unfairly tilted in favor of private interests, keeping valuable national resources in foreign hands, thus threatening Iranian sovereignty in matters of economic and welfare policy. A nationalization decision in this case was justified as the only way to eliminate this threat.

On the other hand, private property owners involved in nationalization cases have typically expended considerable capital and have too much to lose as a result of a government takeover. It seems reasonable that these owners should be compensated at a level commensurate with their investment.

A problem that often arises, however, is that by the time a country is ready for nationalization, it may argue that the owners have already enjoyed a more than adequate return on their investment, that the original contracts and concessions were null and void because they were negotiated by corrupt or otherwise illegitimate regimes, or that, as in the Iranian oil case, the concessions themselves were not legitimate since they bargained over national assets that rightly belonged to the citizenry and were, therefore, not for sale.

Depending on the extent to which owners are perceived, justly or unjustly, as having made exaggerated profits, a government may choose to conduct nationalization as a forced sale appropriation or may opt for outright confiscation. To complicate matters, nationalized assets usually provide a platform for future development and gains on the part of the country, a platform that might not have been available without the capital and effort of the owners. In some cases, the private investment is so extensive that a country cannot afford to pay fair market value without risking bankruptcy, recession, and unmanageable debt. Nevertheless, and difficult as it may be to realize in practice, a nationalization resolution will not be ethically satisfactory unless governments make every effort to provide fair and just compensation to the owners.

The Future

Nationalization can backfire. When a country nationalizes a foreign-owned industry, it increases the expropriation risk to all investors for many years, staunching the flow of capital without which a country can remain underdeveloped regardless of their bounty in natural resources. As the expropriation risk increases, the required return on foreign investments can become unreasonable, and governments with a history of nationalization should expect to be required to negotiate very attractive incentives with new investors to mitigate their risk.

—Sousan Urroz-Korori

See also Business Law; Coercion; Colonialism; Communism; Corporate Citizenship; Cultural Imperialism; Developing Countries, Business Ethics in; Developing World; Development Economics; Eminent Domain; Externalities; Foreign Direct Investment (FDI); Free Trade, Free Trade Agreements, Free Trade Zones; Globalization; International Business Ethics; Just Price; Multinational Corporations (MNCs); Natural Resources; Newly Industrialized Countries (NICs); Political Risk; Public Goods; Public Interest; Socialism; Statism

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National Labor Relations Board

The National Labor Relations Board (NLRB; referred to here as the Board) was established by the National Labor Relations Act (1935) as its administrative body of three members. The 1947 amendment expanded the NLRB to its present membership of five, appointed by the president and confirmed by the Senate. Functionally, the NLRB comprises several bodies with different roles: The 50 Regional and Area Offices handle routine information requests and initial contacts with labor and management officials; these offices receive requests for elections as well as unfair labor practice (ULP) charges; they conduct representation elections and certify the election outcomes.

The Office of the General Counsel offers general supervisory oversight of the 50 Regional and Area Offices. In addition, it investigates ULP charges and issues complaints where such is warranted. The full Board establishes general policies for the General Counsel and the 50 Offices. In addition, it oversees the administrative law judges, who hold elections under the act. In disputed ULP cases, the General Counsel acts as prosecutor and the Board acts as a judge. However, if either party in the dispute declines to obey the order of the Board, the General Counsel shall go before the U.S. Circuit Court of Appeals seeking an enforcement order, after another hearing. This potentially long delay is one of the complaints about the act and its enforcement, thus allowing the employer to use the act as a chilling effect on employees' actions.

The membership is naturally politically oriented as it collectively attempts to interpret and implement the provisions of the three statutes it administers. Over time, the Board's philosophy has changed from an emphasis on employee rights to employer rights, and decisions of a particular Board have reversed the decisions of previous Boards.

Statutory Coverage

Three statutes, collectively known as The National Labor Relations Act, as amended, were a logical expansion of the principles laid down in the Norris-LaGuardia Act (1932) and the National Industrial Recovery Act (1933). The National Labor Relations Act, 1935 (Wagner Act) primarily set forth rights of employees to join labor organizations and the responsibility of employers to bargain collectively with the employees' chosen labor organization. The Labor-Management Relations Act, 1947 (Taft-Hartley Act) primarily laid down some restrictions on employee rights as had been exceeded in the preceding 12 years. The Labor Management Reporting and Disclosure Act, 1959 (Landrum-Griffin Act) has been generally viewed as a law to protect individual employee rights and addressed some charges of corruption within the unions. Thus, the purview of the NLRB is large.

Overall Assessment of Effectiveness

Naturally labor and management will be critical when they do not win cases with the Board. However, the foremost academic authority on the act, Professor James A. Gross, has charged that the national labor policy favors and protects the powerful to the detriment of the less powerful and maintains that the current national labor policy is a failure, based largely on the administration of the act as well as the lack of enforcement power. Few academicians have written about successes of the Board or the act.

—Jerald F. Robinson

See also AFL-CIO; Labor Unions

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National Origin Discrimination

National origin discrimination is discrimination based on the country from which an individual (or his or her ancestors) comes, or his or her accent, customs, or native language. These factors are also collectively referred to as an individual's ethnicity. The Civil Rights Act of 1964 prohibits discrimination in education, public accommodations, receipt of federal funds, and employment by employers with 15 or more employees on the basis of race, color, religion, gender, and national origin. The legislative history of the Civil Rights Act indicates that it was enacted primarily to address racial discrimination, but discrimination on the basis of national origin or ethnicity has become an increasingly important part of the law and is used with increasing frequency.

Title VII of the Civil Rights Act, which has been the basis of most of the national origin discrimination claims and court cases, prohibits discrimination in employment. Cases have involved discrimination claims based on speaking a language other than English in the workplace, refusal to hire applicants from a certain country or of a certain ethnicity, refusal to promote otherwise qualified employees based on the employee's accent, or harassment based on ethnicity or national origin.

Using national origin or related criteria as the sole basis for failure to hire, promote, or train, or to unnecessarily discipline, harass, or terminate an employee is illegal. Those who have been discriminated against on the basis of national origin may file claims with the Equal Employment Opportunity Commission, the federal agency responsible for enforcing the Civil Rights Act. Evidence of discrimination may be direct or indirect. Direct evidence may involve the employer saying those of a certain national origin or ethnicity will not be hired. Indirect evidence may involve the employer having a neutral policy, which has the impact of excluding employees of a particular national origin at a higher than normal rate, such as a height and weight requirement that disproportionately excludes those of a national origin statistically slighter and/or smaller than the requirement, without there being a business necessity for the requirement.

The prohibition against discrimination on the basis of national origin or ethnicity does not entitle an applicant or employee to a job if not qualified; however, national origin or related issues cannot be the sole basis for refusal to allow a qualified employee to be hired and treated like any other employee. This prohibition also applies to housing, education, public accommodations, and receipt of federal funds.

There has recently been an increase in national origin claims for at least three reasons: (1) after the terrorist attacks of September 11, 2001, on the Pentagon, New York's Twin Towers, and the forced plane crash in Pennsylvania for which Islamic extremists claimed responsibility, there was a backlash in the United States against Middle Easterners and Muslims; (2) the increased influx of immigrants and the negative response to them; and (3) the increased willingness of immigrants to use U.S. law and policies that can protect them. Closely related to this issue after the terrorist attacks on September 11, 2001, is discrimination on the basis of religion, particularly against those who, or whose ancestors, are from the Middle East. In the wake of a dramatic increase in negative and discriminatory actions toward Muslims and Middle Easterners after 9/11, the Equal Employment Opportunity Commission issued cautions reiterating its commitment to vigorously enforcing antidiscrimination laws against Muslims and Middle Easterners.

—*Dawn D. Bennett-Alexander*

See also Affirmative Action; Civil Rights; Equal Employment Opportunity; Equality; Equal Opportunity; Glass Ceiling; Racial Discrimination

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National Traffic and Motor Vehicle Safety Act

The National Traffic and Motor Vehicle Safety Act was passed by an overwhelmingly Democratic Congress and signed by President Lyndon Johnson in 1966. It required automobile manufacturers to institute safety standards to protect the public from unreasonable risk of accidents occurring as a result of the design, construction, or operation of automobiles. It also included nonoperational safety factors, such as highway design, and it empowered a new agency, the National Highway Traffic Safety Administration (NHTSA) to mandate uniform safety standards.

Although automobile accidents were by 1965 the leading cause of death of Americans under 44, both government and manufacturers had largely ignored the issue. A series of events would unfold that focused national attention on automobile safety and culminated in litigation and automobile recalls in the years following the establishment of the NHTSA. A relatively obscure lawyer named Ralph Nader emphasized the issue of automobile safety in his 1965 book *Unsafe at Any Speed*, which focused on the alleged defects of the Chevrolet Corvair. Extensive congressional automobile safety hearings the following year chaired by Senator Robert Kennedy grabbed the spotlight when they revealed that General Motors secretly employed detectives in an unsuccessful attempt to find personal "dirt" on Ralph Nader. These well-publicized hearings helped instill the idea among consumers that the "caveat emptor" rule no longer sufficed for highly technological products. These hearings created the necessary popular support to pass a federal law that made automobile manufacturers responsible for the safety of their products.

During the next decade, life-saving shoulder-lap belts, collapsible steering columns, strengthened door latches, shatterproof windshields, and protective dashboards became the mandated standard. These new legal requirements led to a record number of product safety lawsuits and many product recalls and, ultimately, to significantly lower traffic death rates. Additional regulation was added in 1975 with a 10-year schedule of required increases in the fuel efficiency of all new cars. Critics from the automobile industry and many free market advocates decried such requirements as overly bureaucratic edicts that restricted consumer freedom and were far too costly for industry.

A 1985 article by Ralph Nader in the *New York Times* asserted that these regulations had already saved more than 150,000 lives and cited a government report that motorists had also saved "a cumulative $90 billion in transportation costs since 1975 from improvements in fuel economy." Many consumer advocates believed that these savings largely resulted from design and engineering changes that Detroit auto makers would never have done without pressure from the NHTSA. Even Henry Ford II in 1977 allowed that the first wave of NHTSA standards had advanced car and highway safety, fuel efficiency, and pollution controls. By 1998, reliable sources estimated that seat belts alone saved at least 10,000 lives a year.

After the heady early years of its existence, NHTSA's regulatory programs slowed considerably, beginning in the late 1970s. Mandates for the second wave of engineering advances such as the air bag were stalled for more than a decade by successive congresses that were increasingly skeptical about regulation and more susceptible to the auto industry's very extensive lobbying activities. There were signs by the middle of the first decade of the 21st century that this might shift again. Significant increases in fuel prices coupled with large numbers of fuel inefficient SUVs prompted a renewal of congressional mandates for increased fuel standards.

—Anthony D. Branch

See also CAFE Standards; Ford Pinto; National Highway Traffic Safety Administration (NHTSA); National Transportation Safety Board (NTSB)

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National Transportation Safety Board (NTSB)

The National Transportation Safety Board (NTSB) is an independent federal agency responsible for investigating all civil aviation accidents and other significant accidents in railroad, highway, marine, and pipeline transportation. The NTSB's mission is to improve transportation safety. Its accident investigation findings are used to make safety recommendations and improvements that will make transportation safer.

The NTSB was established by Congress and began operation on April 1, 1967. It became a completely independent agency on April 1, 1975. To maintain impartiality, it is not affiliated with any other agency or organization, although it works with other agencies and organizations in accident investigations. Since its founding, the NTSB has investigated more than 124,000 aviation accidents and more than 10,000 surface transportation accidents. The NTSB does not have regulatory or enforcement powers. It makes recommendations based on the facts arising from investigations. Recommendations from accident investigations are based on thorough investigation and may address deficiencies that do not directly pertain to what is ultimately determined to be the cause of the accident. To maintain impartiality, the board's analysis of facts and determination of probable cause cannot be used as evidence in a court of law nor can persons in legal or litigation positions be assigned to accident investigation teams.

The NTSB is governed by a five-person board of directors, who are each nominated by the president and confirmed by the Senate. They serve 5-year terms. One member is designated by the president as chair and another as vice chair for 2 years. The chair requires separate Senate confirmation.

Accident investigations are carried out by the NTSB's "Go Team." The team's goal is to begin investigating major accidents at the scene as quickly as possible. A team consists of anywhere from three to more than a dozen specialists from the board's headquarters staff in Washington, D.C. Each team is supervised by an Investigator-in-Charge and made up of separate investigators who are specialists in each clearly defined portion of the accident investigation. In aviation, these areas include operations, structures, powerplants, systems, air traffic control, weather, human performance, and survival factors.

If it is determined that an investigation involves criminal activity, the attorney general, in consultation with the chair of the NTSB, will notify the board. The NTSB will then surrender lead status on a transportation accident to another agency such as the FBI or the Justice Department.

Since 1990, the NTSB has maintained a "most wanted" list of safety improvements. Because of the agency's reputation for impartiality and thoroughness, more than 82% of its recommendations have been adopted by those in a position to effect change. Examples of items on the current list include improving child occupant protection in automobiles, eliminating hard core drinking and driving, reducing dangers to aircraft flying in icing conditions, and improving audio and data recorders in aircraft.

—Patrice Luoma

See also Consumer Protection Legislation; Consumer Rights; National Highway Traffic Safety Administration (NHTSA); National Traffic and Motor Vehicle Safety Act; Regulation and Regulatory Agencies

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Natural Assets (Nonuse Values)

Natural assets are the various forms of wealth originating within the natural world. Land, water, the atmosphere, animals, and plants are all examples of natural assets. Natural assets can have both a use value and a nonuse value. The nonuse value of natural assets lies in their intrinsic value apart from any instrumental use as a mere means to other human ends. If, for instance, the Everglades were to be obliterated, this would be understood as a loss not simply because tourism would falter but because something of intrinsic value would have been lost. Tourism would represent one use value of the Everglades, but the Everglades also has a nonuse value, an intrinsic value. Recognizing the intrinsic value of natural assets is crucial to the appreciation of natural beauty, spiritual and moral development, and understanding the place of humans in the world.

Although natural resources are often thought of as publicly available natural assets, in practice, this does not always hold true. Natural resources are not defined as natural assets for an individual unless one also has a right to them. Clean water, for instance, may be a natural resource, but many have no access to clean water and are not necessarily thought to have a right to clean water that they may claim against those who privately own local water rights. So if someone owned the water rights to a local spring, the clean water from the spring would be both a natural resource and a natural asset for the owner. The spring water would be a natural resource but not a natural asset for a neighbor with no rights to the water.

Natural assets serve two crucial functions: providing the raw materials of economic production and serving as the natural sinks needed to maintain ecological homeostasis. As natural sinks, the air, water, and soil absorb and decompose waste. Forests, for example, play a crucial role in carbon sequestration. When wood is burned for fuel, carbon is released into the atmosphere contributing to climatic changes that often have a negative impact on the global ecosystem.

Traditionally, economists have not accounted for nonuse values assigned to natural assets in terms of either intrinsic value or their value as natural sinks. Instead, economists have held that natural assets are just another factor of production for which human-made capital can be substituted indefinitely. Ecological economists try to account for the nonuse value of natural assets by assigning replacement cost values required to make up for the economic benefits otherwise yielded by intact natural sinks. While it is impossible to assign dollar values to the intrinsic value of natural assets, ecological economists argue that assigning economic value to natural assets, such as natural sinks, can go some of the way toward a more accurate assessment. Ecological economists, for example, would assign value to the oysters of Chesapeake bay as the kidneys of the bay that help to prevent algae blooms, rather than assuming that the monetary value of the oysters for the fishing industry is exhaustive.

—Mary Lyn Stoll

See also Biocentrism; Intrinsic Value; Land Ethic; Natural Capital; Natural Resources

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NATURAL BUSINESS ETHICS

Natural business ethics is the use of theories, concepts, and research from the natural sciences that provide insights into the ethical dilemmas, problems, and issues that occur in business organizations. The natural sciences most frequently involved are ecology, evolutionary biology, evolutionary psychology, cognitive neuroscience, and genetics, with thermodynamics, paleontology, primatology, and related anthropological sciences sometimes being used. In this approach, human behavior is understood to be the outcome of natural evolutionary forces that have produced behavioral traits, cognitive modules, and genetic systems that are positively and adaptively responsive to environmental challenges and opportunities of the earth's ecosystems. Business behavior, including that found in the large-scale business corporation, is a variant of naturally evolved human behavior and subject to the same natural forces, constraints, and opportunities. Going beyond simple descriptive accounts of nature-based business behavior, natural business ethicists draw normative inferences about the moral issues that occur in the corporate workplace, such as fair pricing, discriminatory treatment of employees, stakeholder claims, organizational justice, breach of social contracts, environmental pollution, and so forth.

A broad base of Darwinian evolutionary theory and confirming empirical research constitutes the conceptual foundation of natural business ethics. It includes the following features:

- Organic life evolves within its host environment, with adaptive success dependent on the organism's physical traits and behavioral routines.
- Organic traits and behavioral patterns are the outcome of an organism's genome, that is, its total set of genes, interacting with the host environment.
- Natural selection describes the organism–environment linkage wherein those traits and routines that enable the organism to survive and adapt are favored and conserved, while nonadaptive features are discarded or become adaptively nonfunctional.
- Life-supporting ecosystems consist of a great diversity of cellular forms, plants, animals, and humans, and are affected by meteorological, astronomical, chemical/physical, geological, and oceanic forces. Symbiotic, mutually supportive linkages between diverse organisms occur throughout ecosystems, enhancing the adaptive prospects of ecosystem inhabitants.
- Modern human beings (*Homo sapiens*) and their hominid predecessors (several *Homo* variants) have evolved subject to the organic, genetic, natural selection, and ecosystem processes that have shaped and conditioned all organic life on earth.
- Cognitive neuroscience, paleoanthropology, and comparative primatology describe the evolution of a distinctive human brain capable of forming, using, transmitting, and self-correcting cognitive symbols as adaptive tools for interacting successfully with environmental forces.
- Human cognitive symbols are the basic building blocks of human culture, capable of assuming diverse forms and patterns within geophysical environments of great variety. These sociocultural symbols, also known as memes, are transmitted through learning by being copied from brain to brain over generational time, thus establishing cultural traditions and customs.
- A reciprocal relationship exists between sociocultural symbols and the natural evolutionary processes that gave rise to them, with each dependent on the other. Hence, the nature-nurture, culture-gene interface blends and harmonizes human learning and inherited biological traits, rather than separating and opposing them to one another.

Building on this Darwinian theoretical base, natural business ethicists have proposed that moral issues in business are a mixture of biological and cultural traits, best understood and dealt with by recognizing the natural components involved. Four examples give a flavor of this approach. William Frederick has argued that two nature-based value systems—economic production and a quest for power—drive the behavior of corporate managers toward goals that defeat and contradict the moral needs of employees and their communities by disrupting ecological systems and diminishing social justice. Paul Lawrence posits the presence of four biological drives—to acquire, to bond, to learn, and to defend—underlying all human behavior, which taken together constitute an innate moral system. The resultant moral sense can be used as a template to evaluate the ethical and unethical actions of companies like Enron. Timothy Fort draws on cognitive neuroscience research that shows an upper limit on the number of meaningful relationships that people can have with others, arguing that a person's moral identity therefore depends on working within relatively small-size groups. Large-scale, hierarchical organization that is typical of business corporations can, and often does, diminish the ability of business practitioners to distinguish right from wrong. Evolutionary psychologists Leda Cosmides' and John Tooby's research reveals the presence of ancestral neural modules that favor the formation and enforcement of social contracts; David Wasieleski and William Frederick subsequently developed a model of evolutionary social contracts that demonstrates the moral responsibility of business firms when they contract with employees and host communities.

These recent studies of natural business ethics are a historical extension of much older traditions reaching back to Adam Smith and David Hume, who believed that nature-induced moral sentiments mediate much economic behavior, an idea echoed by contemporary political scientist James Q. Wilson's notion of an innate moral sense for fair play. Related theory and research in organizational ecology, population ecology, organizational complexity, and economic sustainability provide supplemental support for the basic ideas and approaches of natural business ethics.

—William C. Frederick

See also Biodiversity; Bioethics; Corporate Ecology; Environmental Ethics; Evolutionary Psychology; Genetics and Ethics; Human Nature; Natural Capital; Reciprocal Altruism

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Natural Capital

Natural capital refers to the ecological resources that are used in economic production and consumption, such as fertile land, elements from the earth's crust, atmospheric gases, bodies of water, and plant and animal species. The concept of natural capital has been developed by advocates of sustainable development to emphasize the dependence of all economic activity on these naturally occurring resources and the ecological systems of life that they support. Natural capital has quantifiable economic value either in terms of its potential to enable the production of goods and services or its ability to be traded as a commodity; however, unlike traditional capital, natural capital is thought to have a kind of primary importance in that its conservation and protection is a necessary condition for the continued availability of other forms of capital and, thereby, economic activity.

Natural Capital and Other Forms of Capital

Economists of the modern period, ranging from Adam Smith, David Ricardo, and Karl Marx, have historically identified three central elements in the production process: land, labor, and capital. Capital in these contexts refers to items such as buildings, plants, tools, and machinery that are used to produce other tradable goods. The ability of firms to produce valuable goods for trade depends on capital maintaining its value over time as an instrument of ongoing production. Capital, in this sense, refers to *manufacturing capital* or capital that is created by humans to engage in production. The origins of the term underscore that capital is centrally an object of human creation, as opposed to something found in nature.

Contemporary economists and management theorists have implicitly maintained that capital should be more broadly understood as those resources that can produce additional market value or competitive advantage. *Financial capital* is perhaps the most common form of capital discussed in contemporary settings, especially as businesses transition from a manufacturing to a service orientation. All financial capital can, in principle, be liquidated for money. Whether such capital takes the form of cash, equity stock, bond notes, or other financial instruments, financial capital enables either the direct use of money for business operation or the acquisition of money through leveraged agreements. Business leaders are also aware of the importance of new ideas and innovative practices in remaining competitive. Such *intellectual capital* can result in valuable patents and responsive product lines or services. Information technology firms have operated under the principle that innovative ideas and the integration of resultant technologies hold the key to developing new service platforms that make timely information available to a range of customers. *Social capital* refers to the advantages made available to organizations through the trust, commitment, and skill offered by its stakeholders.

Whether manufactured, financial, intellectual, or social, capital is intended to be maintained rather than depleted. Indeed, the sound growth of business traditionally takes place only under the assumption that the firm's stock of capital is enhanced rather than diminished. *Natural capital* has traditionally escaped a comparable analysis. A number of observers within economics and business have emphasized that an economy exists only as a part of a larger ecological system. This ecological context of commerce requires that market actors acknowledge both the natural environmental inputs in the production process as well as the ways in which their activities can adversely affect the health and viability of the ecosystem in which they operate. Natural capital, such as water, air, minerals, energy sources, and plant and animal life, are depleted by business; however, like other forms of capital, the continued depletion of these resources threatens the ability of market actors to create value in the future. Where traditional economic analyses have disregarded the natural environmental limitations to market activity, ecological economists have put forth arguments as to why natural resources are, in a fundamental sense, capital that cannot be spent without significant adverse social and economic impacts to human well-being. Global climate change, such as greenhouse gas emissions, deforestation, groundwater toxicity, and destruction of essential wetlands are but a few examples of the social and environmental problems associated with the continued depletion of natural capital.

Natural Capital and Sustainable Enterprise Management

More recent discussions involving natural capital have centered on the ways in which economic activity can be made *sustainable* and thereby preserve the stock of natural capital. Sustainable development implies an elimination of the very idea of economic growth as it has been traditionally understood. As natural resources are extracted, used, and depleted, the balance between ecosystems and the economy is thought to become less stable. The use of naturally occurring energy sources creates by-products that are often rendered unusable for economic or natural purposes. Production processes create waste that transforms naturally beneficial or benign substances into ecologically harmful pollutants. Certain resources, such as trees and fisheries, are used commercially at much higher rates than natural, regenerative mechanisms can create new supplies. Advocates of sustainable development maintain that these problems illustrate why the expansion of markets without accounting for natural capital is ultimately unsustainable. As long as markets operate without regard to environmental scale, that is, the biophysical capacity of the natural environment, growth potentially outstrips the environment's ability to support continued life and, thereby, economic activity.

Sustainable development, hence, is economic activity that continually improves human well-being while remaining at a level that can be indefinitely maintained by the natural environment, thereby permitting future generations to achieve similar levels of well-being. This position requires that market actors think differently about the use of natural capital. First, it requires that natural resources be used as productively as possible to eliminate inefficient or careless use of natural capital. Second, since economic activity has historically produced harmful wastes, it is incumbent on economic actors to minimize such wastes or, as some have argued, do away with the very concept of waste. Third, sustainable development requires the beneficiaries of economic development to reinvest in natural capital. Just as firms and governments need to reinvest in fixed capital from time to time, enhancing the value of natural capital through ecological preservation is a basic tenet of sustainable development.

These principles have shaped the emergence of sustainable enterprise management. While advocates of sustainable development tend to analyze economic trends at an institutional or global level, organizational leaders who take the goals of sustainable development seriously have articulated an array of frameworks that managers can use to change their operations to satisfy the ends of productivity, waste minimization, and reinvestment in natural capital. The nonprofit consultancy The Natural Step, for instance, works with businesses to encourage managers to see how the ends of environmental sustainability and profitability are not only compatible but mutually supportive. The Natural Step puts forth four "system conditions" that are necessary for the sustainable development of market economies. These four conditions are novel, in part, because they also simultaneously serve as guidelines for enterprise management; the patterns of economic activity at the organizational level are thought by The Natural Step to determine the systemwide carrying capacity of the economy. The system conditions are the following: (1) eliminate contributions within the biosphere to increases in concentrations of substances from the Earth's crust (e.g., minerals and metals); (2) eliminate contributions within the biosphere to increases in substances produced by society (e.g., chemicals and air pollutants); (3) eliminate contributions to the physical degradation of the biosphere (e.g., deforestation and overfishing); and (4) eliminate activity that undermines humans' ability to meet their needs worldwide. The first two of these system conditions are designed to address the issues of productivity and waste minimization. The third system condition emphasizes the commitment not to engage in activity that disrupts the normal, regenerative processes that take place in nature. The fourth underscores how sustainable development occurs when economic activity improves well-being for all who make productive contributions.

The catalog retailer Norm Thompson has merged the Natural Step's four system conditions with the goals of environmental protection to guide the development of their Sustainability Action Plan. This strategic vision requires that the managers of Norm Thompson not only consider the impacts of their direct retailing on natural resources and ecologically sensitive processes but also direct their relationships with suppliers and peer organizations. Consequently, Norm Thompson has set goals of a net zero impact on greenhouse gas emissions, elimination of toxic substances from its catalog production and the products it sells, a net zero negative impact on forests (given its reliance on paper for its catalogs), and the achievement of zero waste in its facilities.

These commitments have led to practices ranging from partnerships with the Alliance for Environmental Innovation to use fully recycled (and recyclable) catalog paper of sufficiently high quality to new incentives and timelines for suppliers to use organic, chemical-free cotton. Subsidies are provided to employees to use public transportation. Norm Thompson provides noteworthy leadership among industry associations to reform the practices of clothing manufacturers and catalog retailers. As part of its action plan, Norm Thompson hired a sustainability manager that coordinates all efforts (product development, packaging, publishing, transportation, and outside influence) aimed at environmental sustainability. Management is centrally focused on accounting for the impact of Norm Thompson's business on natural capital; energy consumption is tracked, trends in waste are monitored, changes in product materials are assessed, and suppliers are questioned on their environmental practices.

The Rocky Mountain Institute (RMI) is another organization that has stressed the business case for the proper accounting of natural capital. Several elements have been introduced by RMI founder Amory Lovins and his contributor, Paul Hawken, in their framework, *natural capitalism.* The first is natural resource productivity, or the pledge to make the most efficient use of available natural resources in the development of new products and services. Lovins and Hawken cite the textile firm Interface Corporation as an exemplar in this regard. Interface's steadfast commitment to radical ecoefficiency led the firm to design its production facilities for modular floor covering so that use of electricity would be minimized. The size and shape of cooling pipes, placement of machines, and use of daylight-sensitive lamps were part of systemwide design changes that reduced power requirements by more than 90%. The German chocolate manufacturer Ritter Sport has adopted a similar stance; energy-saving technologies are deployed as long as they do not increase operational costs by more than 10%. This has resulted in an array of unique changes including the ability to control the climate in office buildings from the heat produced by a cogeneration plant adjacent to their chocolate production facilities.

Lovins and Hawken also stress that natural capitalism is committed to adopting biological models of production. In nature nothing is wasted. All by-products are used by other organisms and systems. Biological models of production, thus, emphasize production techniques that are naturally benign; that is, they can be used by the ecosystem without harm, eliminate waste altogether, or are closed-loop, in that they involve partnerships with organizations that can use what would otherwise remain unused waste. It is important to note that the call to eliminate waste is primarily, although not exclusively, a call to eliminate waste that cannot be reintegrated into natural ecological processes. Waste that is toxic or waste that ends up on landfills are wastes that are biologically harmful because they either destroy the ecological purpose, or *telos,* of certain ecosystems or circumvent the reintegration of resources into the natural environment for future use. Nature exhibits waste in some other senses of the term: For example, a bird may drop twigs to the ground in constructing a nest. This simple sense of "waste," however, neither harms other ecosystems nor thwarts the use of any resources by other available natural processes. This is quite different from human activity that, while wasteful in this simple sense of the term, is also wasteful in that it sometimes undermines the ability of natural systems to function according to their ecological purpose.

Natureworks, LLC has made significant headway in developing biopolymers, manufactured from corn and rice, which can be used in place of petroleum-based plastics in food packaging, bottles, and even clothing. Apart from lowering reliance on fossil fuels, Natureworks' biopolymers are more likely to biodegrade, thereby eliminating the inevitable waste that accompanies the best plastic recycling programs. Interface Corporation has made innovative use of flooring made from solenium that has enabled managers to meet their goal of developing flooring that is 100% recyclable into a new product. RMI is a strong advocate of business models that lease services as opposed to selling tangible goods. Efforts by companies like Xerox to lease office equipment that is made with the intention of reusing parts in later models is an example of how leasing products creates incentives to improve their quality and longevity while promoting the goal of making fully recyclable products. These efforts are encouraged by recent efforts to implement frameworks to account for the entire life cycle of products that are bought, made, and sold by businesses.

Lovins and Hawken stress, too, that the protection of natural capital requires that market actors reinvest in the stock of natural capital. This is perhaps the most challenging aspect of sustainable enterprise management, as it moves beyond the intermediate-term competitive advantages obtained through such things as energy efficiency and reduced costs associated with the handling of waste. It requires that individual firms recognize that preserving natural capital is part of the larger preservation of the ecological infrastructure on which economic activity is built. Ritter Sport continues to work very closely with agricultural cooperatives in Central America that train cocoa farmers in tilling and planting techniques that minimize soil erosion or deforestation. This notion of reinvesting in natural capital is centered on improving the long-term viability of market strategies that rely on the use of natural resources for profitable business activity.

Prospects and Challenges

The preservation and reinvestment in natural capital demonstrates how financial, intellectual, and social forms of capital are linked in complicated ways. Efficiency and cost reduction have an impact on the availability of financial capital for future ventures. Both the Natural Step and RMI have pursued enterprise management strategies that emphasize innovation. The three goals of efficiency, waste reduction, and preservation are enabled through regular investment in new, environmentally sustainable technologies. Such technologies can represent novel ways of accomplishing old tasks, for example, the use of solar panels to produce electricity, or can serve as new tools in achieving the goals of resource efficiency, for example, the use of geographic information systems to optimize the location of distribution facilities to reduce the fossil fuel consumption that inevitably accompanies transportation. Serious efforts to protect natural capital also require long-term, creative relationships with an array of stakeholders. This is especially true in situations where novel uses of waste need to be uncovered or competitors within the same industry can work together to find mutually advantageous solutions to common resource use problems. Interface has a long track record of working with municipalities and nongovernmental organizations to "offset" the carbon emitted through their businesses' operation by capping methane gas released from landfills to reuse as a substitute for natural gas; by participating in the construction of new, low-energy housing developments through high-tech building design; and, more simply, by planting trees.

One common and reoccurring objection to sustainable enterprise management is that inadequate assessment tools and incentives exist for businesses to take the steps necessary to protect natural capital. The assessment problem has resulted in a number of elaborate frameworks to monitor and measure a company's net impact on the ecosystems it affects. So, for instance, more companies are seeking the guidance of organizations such as the United States Green Building Council to certify that their building designs meet certain levels of environmental protection, measured in terms of water use, energy consumption, and impact on surrounding ecosystems. Life cycle accounting is a technique that is designed to provide an accurate snapshot of a product's true environmental impact from the beginning to the end of its life cycle. This includes the materials and energy that go into making the product to its impact on, say, the groundwater once it ends up in a landfill. Companies like Interface measure their environmental impact in much the same way in which other companies measure any other expense. All carbon emissions, whether from production facilities, company automobile fleets, or the trucks driven by suppliers to Interface's distribution centers, are monitored and recorded. This helps Interface managers make decisions about where carbon can be trimmed and how much offsetting they must do to meet their goals of being a carbon neutral company. The Global Environment Management Initiative is a nongovernmental organization that has taken the lead in developing both guidelines and metrics for these and other techniques for assessing the impact of more sustainable business management.

The incentives problem is more difficult to the extent that it requires action by more than just business leaders. As Lovins and Hawken admit, there are many good reasons why, from a business perspective, natural capital is not protected. Companies in the United States are rewarded for resource consumption in that raw materials and production inputs purchased from suppliers are treated as expenses for traditional accounting and tax purposes. Moreover, until the market prices reflect the true costs associated with environmental degradation, there is little reason for businesses to voluntarily take on the increased costs associated with sustainable enterprise management when other competitors do not. These facts point to the need for changes in policy that begin to account for the long-term economic value of natural capital and accordingly create mechanisms that direct businesses to adjust their activities to preserve this source of value, just as they would any other form of capital. This may include credits for alternative energy use, tax advantages for comparative reductions in raw materials use, and research and development grants for the use of certain technologies.

—Jeffery Smith

See also Capitalism; Economic Growth; Environmental Ethics; Intellectual Capital; Natural Resources; Social Capital; Socially Responsible Investing (SRI); Stakeholder Engagement; Sustainability; Triple Bottom Line

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Naturalistic Fallacy

The naturalistic fallacy was identified by G. E. Moore (1873–1958) in *Principia Ethica,* where it provides the grounds for his rejection of evolutionary and hedonistic ethics. The fallacy is important to consider in business ethics since evolutionary and hedonist positions are still endorsed by some contemporary theorists in this area.

The fallacy includes a failure to distinguish between identifying a property that good things have in common and providing a general account of moral goodness. This failure prompts a fallacious assumption that by identifying a property shared by good things, one has succeeded in providing an account of goodness. For example, good things may have in common that they are desired or natural. Being desired or being natural, then, would be properties shared by good things. The fallacy is committed in accepting that because good things share either of these properties, *good* means the same as *desired* or *natural*.

The naturalistic fallacy is often conflated with the is-ought fallacy. The is-ought fallacy arises on assuming that a claim concerning what should or ought to be the case follows directly from a claim about what is the case. For example, one would commit the fallacy in assuming that because a business does or can make a profit by price-gouging, a business should or ought to make a profit by price-gouging. While the naturalistic fallacy is related to the is-ought fallacy in that it concerns a faulty assumption that prescriptive claims follow directly from descriptive claims, it is more specific in its focus. The naturalistic fallacy includes only those cases in which it is assumed that because good things all have a certain property in common, the property is the same as goodness.

As its name indicates, the naturalistic fallacy is usually identified in cases in which the property in question is a natural property. However, the same conflation may occur concerning nonnatural properties. For example, the fallacy would be committed in reasoning that since businesses that are good are also those that make a profit, *making a profit* or *profit making* means the same as *good*. While it may well be that businesses having the property of being profit making also have the property of being good, to assume that *profit making* means the same as *good* is to commit the fallacy.

Moore uses his well-known *open-question argument* to support the claim that this is a fallacy. This argument brings into relief a finer point about the linguistic source of the conflation occurring in the fallacy. Assuming that a single property, such as in the example of being profit making above, is the same as being good commits one to claiming that the words *profit making* and *good* have the same meaning. But if two words have the same meaning, then in any claim stating that profit making and goodness are the same, the *is* must assert their identity. For example, the *is* in the statement "profit making is profit making" asserts that profit making is identical with profit making. This statement is uninteresting because it is not informative. In contrast, in the statement "profit making is good," the *is* works to attribute a quality or property of goodness to profit making. This claim is informative, indicating that the word *is* is that of predication rather than identity. As Moore explains this difference, we can see that the *is* in "profit making is good" is not the *is* of identity, because we can ask a significant question about this assertion that we cannot of the other. While it is not a significant question to ask whether profit making is, after all, profit making, to ask whether profit making is, after all, good is to ask a significant question. But this question must remain open; the question always has significance because profit making is not the same as goodness.

Moore argues that evolutionary and hedonistic ethicists fall prey to the naturalistic fallacy. In his heated response to evolutionary ethicists—Herbert Spencer in particular—he points out that the fallacy is committed by Spencer in his attempt to associate ethics with natural selection. Spencer commits the fallacy by assuming that being natural or being evolved is the same as being better or being good. In response to hedonistic ethicists, both egoists and utilitarians, Moore charges that the fallacy arises in their foundational assumption that pleasure is the same as good and their understanding of the *is* in this claim as the *is* of identity rather than of predication.

—E. D. Kort

See also Fact-Value Distinction; Hedonism, Ethical; Hedonism, Psychological; Hobbes, Thomas; Is-Ought Problem; Mill, John Stuart; Spencer, Herbert

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Natural Law Ethical Theory

This is an ethical theory that holds one or more of the following three claims: (1) moral claims are not social conventions but are based on the objective nature of things; (2) moral right and wrong depend on facts of human nature; and (3) an immoral rule cannot be a valid law.

All three of these claims are found in the writings of ancient and early medieval Greek and Roman thinkers. The view that moral claims are not conventional but are based on the objective nature of things is stated by Aristotle, who notes in the *Nicomachean Ethics* (Book V, Chapter 7) that natural justice consists of moral claims that are "unchangeable and equally valid everywhere and do not depend on whether or not we accept them," while merely legal justice consists of social norms that "have been laid down by rule [and] differ from place to place." The view that moral right and wrong depend on the facts of human nature was advanced by ancient Greek and Roman Stoics, such as Cicero, who claims in *On the Laws* that "the nature of justice must be sought for in the nature of man." And the view that an unjust or immoral rule cannot be a valid law is famously stated by the early medieval bishop St. Augustine who declares in various writings that "an unjust law is not a law."

The medieval theologian St. Thomas Aquinas drew together all three of these claims into a comprehensive natural law theory that is commonly taken as the paradigm example of a natural law theory. Aquinas characterized what he called the "Eternal Law" as the regularities that are exhibited in the behaviors of the things that make up the universe that God created. These regularities, he claimed, are the products of the natures that God instilled in things when he created them. In particular, the regular lawful behaviors of things in the universe are the outcome of the "inclinations" that are built into the nature of each thing and that move each thing toward its proper ends. The "natural law," according to Aquinas, is the eternal law as it applies to human beings. Like all other things in the universe, human beings have inclinations toward their own proper ends, and these inclinations are part of their human nature. Unlike other things, however, the inclinations that orient human beings toward their ends are inclinations that are exhibited in their reasoning processes. In particular, human practical reason is inclined to seek what is good and to avoid what is evil. Aquinas identifies four specific goods that reason perceives as part of the human good and, therefore, as goods that human practical reason is inclined to seek and whose destruction practical reason perceives as evil and, therefore, is inclined to avoid. These four goods are human life, the procreation and care of the young, knowledge of God, and social order. The "precepts" of the natural law, then, consist of the moral claims that derive from the recognition of each of these ends as part of the human good: Human life ought to be sought and its destruction avoided; the procreation and care of the young ought to be sought and its destruction avoided; knowledge of God ought to be sought and its destruction avoided; social order ought to be sought and its destruction avoided. Human laws—that is, the rules promulgated by a ruler—can have the binding force of a valid law, he claimed, only to the extent that they are consistent with the moral precepts of the natural law. A rule that contravenes any of these moral precepts lacks one of the defining characteristics of law and so is not a valid law and has no moral claim on our obedience.

Aquinas's theory clearly embodies all three of the claims of natural law theory. First, moral claims, in his view, are not social conventions but derive from the eternal law that constitutes the objective nature of things. Second, in his theory, moral right and wrong are based on human nature, in particular on the inclinations that constitute human nature. And third, he claims that a valid law, by definition, cannot contravene one of these moral claims. During the centuries that succeeded Aquinas, however, the three strands that he wove together into an integrated natural law theory often came unraveled, and each has been independently developed by various thinkers.

The first strand of natural law theory, that is, the view that morality is not conventional but based on an objective natural order, has been a staple of Western moral theory. Thomas Hobbes, for example, who saw himself as articulating a natural law theory, argued that the laws of nature that constitute the "true moral philosophy" are binding on all men and precede any human social conventions, in particular all political conventions. The laws of nature, Hobbes claimed, command men to seek their self-preservation by entering a social contract through which they submit themselves to a sovereign and thereby create a government. Subsequently, John Locke, who also saw himself as articulating a natural law theory, agreed that the laws of nature consist of moral laws that govern humans prior to the construction of any political institutions. Locke, however, argued that the laws of nature endowed all men with natural rights to "life, liberty, and property" and so these natural rights preceded all political conventions. Contemporary human rights theories, which also claim that moral rights are not conventional but are based on an objective moral order, continue to echo the natural rights claims of Locke. It has been argued that Kantian theory and even utilitarian theory can be considered natural law theories insofar as they advocate the view that morality is not based on conventions but on objective principles.

The second strand of natural law theory—the claim that a valid law, by definition, must be consistent with morality—has also had a long history of discussion. John Austin in his treatise on law, *The Province of Jurisprudence Determined*, notably denied the claim when he argued that the concept of a law, which he defined as the sanctioned command of the sovereign, is distinct from the concept of morality. Austin's view, however, was repudiated by William Blackstone who claimed that laws that "are valid derive all their force, and all their authority" from the natural law. The question of whether the concept of morality "overlaps" the concept of law continues to be a key issue in contemporary jurisprudential debates. The so-called positivist theories of law reject the view that there is a necessary "overlap" between morality and law, while "conceptual naturalist" theories of law accept the overlap thesis. Among contemporary philosophers, John Finnis has recently defended a version of the overlap thesis, arguing that the obligatory force of the law derives from the principles of morality, and so a law that contravenes those principles cannot be obligatory "in the fullest sense" and, therefore, is not fully a law. Ronald Dworkin, who also defends a version of the overlap thesis, has argued that when "hard cases" require judges to interpret the law, the best interpretation will be one that is based on or consistent with the moral principles that best justify society's legal practices.

The third strand of natural law theory, the view that morality is based on human nature—particularly on the orientation of our human nature toward certain human goods—has been developed in numerous versions since Aquinas, particularly by Catholic thinkers. Prominent among these was the 16th-century group of Spanish theologians known as the "School of Salamanca" (including Francisco Suarez and Francisco de Vitoria) who, while acknowledging that the natural law is based on human nature, argued that the natural law obligates only because God commands it, thereby introducing a voluntaristic note into natural law theory. Among contemporary philosophers, Germain Grisez, John Finnis, and Joseph Boyle have defended a "new" natural law theory of ethics that is largely an adaptation of Aquinas's theory of morality. Finnis and Grisez, for example, define the natural law in terms of what human reason perceives is required to achieve those "basic goods" toward which humans are naturally inclined. However, whereas Aquinas suggested that there were four basic goods, Finnis and Grisez have argued in favor of seven basic human goods: life, knowledge, work, aesthetic experience, sociability, practical reasonableness, and religion. An action is morally wrong, they claim, when it directly destroys a concrete instance of these basic human goods. Finnis and Grisez specify several "requirements of reason" to which human beings must adhere in their pursuit of the basic goods: requirements that emerge as the virtues of integrity, fairness, readiness to forgive, cooperation, enthusiasm, fortitude, self-control, and faithfulness.

Although a few natural law thinkers have recently addressed business ethics issues, natural law theory has not been part of the mainstream of contemporary business ethics theory. In fact, apart from a few scattered articles, there have been virtually no attempts to apply natural law theory to issues in business ethics during the past two decades. This was not always the case. Throughout the medieval and early modern periods, natural law theorists discussed the ethical issues encountered in commercial exchanges, including fair pricing, buyer ignorance, fair profits, contracts, and money lending. More recently, several natural law ethicists, including John Ryan during the 1940s, Johannes Messner during the 1950s, and Thomas Garrett and Henry Wirtenberger in the 1960s, wrote several important treatises on the implications of natural law theory for business. Messner, an economist, provided detailed moral analyses of banking, of the modern corporation, and of the price and wage mechanisms of contemporary capitalism, while Ryan addressed the obligations of the employer to the employee. Garrett and Wirtenberger focused their analyses on the everyday issues encountered by the contemporary businessperson. More recently, Manuel Velasquez and Niel Brady have used natural law theory to analyze several contemporary business issues and have argued that natural law theory provides a more useful and more insightful basis for evaluating the ethics of business practices than do other more popular deontological and consequentialist theories.

Perhaps because of its long history, natural law theory has accumulated a significant number of troubling criticisms. First, both relativist theories and subjectivist theories have contested the claim that morality is objective. The diversity of moral views among different cultures and individuals suggests that morality does not have an objective basis. Second, critics have argued that natural law theory asserts that one can move from descriptive claims about human nature to normative claims about human obligations. But such a move, critics allege, is an instance of the is-ought fallacy and so must be rejected. Third, critics claim that natural law theory is committed to a teleological conception of human nature in its claim that morality is based on goods toward which human nature inclines. But evolutionary theory has shown, they argue, that a teleological conception of human nature is untenable. Fourth, critics contend that natural law theory wrongly implies a link between morality and the existence of God, both in its claim that religion is a basic human good and in its claim that moral obligation is a function of a God-given order or, more strongly, of a command of God. They conclude that natural law theory, therefore, wrongly implies that morality requires a commitment to belief in God. Fifth, critics argue that the view that an unjust rule cannot be a valid law is mistaken because the concept of law and its validity can be defined in morally neutral terms. If such a morally neutral definition of law is possible, then it is possible for a rule to count as a valid law and yet be unjust. Sixth, critics have criticized the claim that it is possible to specify a set of human goods whose pursuit is universally binding. As evidence against this claim, critics cite the fact that natural law philosophers have provided conflicting lists of these supposed "universal goods." Indeed, critics argue, given the immense variability in human desires, it is unlikely that one can construct a list of specific goods that would be universally acceptable.

—Manuel Velasquez

See also Absolutism, Ethical; Darwinism and Ethics; Doctrine of Double Effect; Human Nature; Is-Ought Problem; Naturalistic Fallacy

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Natural Resources

Natural resources refer to objects, relationships, or capacities of value that exist in a form or environment that originated without human intervention. Businesses, whether providing products or services, typically consume or otherwise rely on natural resources in their conversions from raw materials to finished goods. The value of natural resources derives from different modes of usage: direct consumption, indirect servicing, and/or enjoyment through nonuse. Traditional direct use or consumption of natural resources would include activities such as mining, forestry, and commercial fishing. Examples of indirect use, when natural resources provide a beneficial service, include flood mitigation by wetlands and fisheries production provided by free-flowing rivers. As many indirect-use services are enjoyed without direct cost, their value is generally only appreciated when the service is interrupted, such as when a reduction in fish stocks occurs as a result of restricting river flows through dams and irrigation infrastructure. Nonuse value derives from the personal utility gained through the simple existence of the resource such as a pristine old growth forest or specific charismatic megafauna like whales, elephants, and tigers. Natural resources, such as fresh water, forests, and solar energy, are also classified as renewable if the potential for regeneration exists within a time span relative to a human life span. From deforestation to food production to the global warming phenomenon, natural resource consumption and protection form the basis of some of the most contested social issues today. To thrive in the information age, where the actions of an international supplier can blunt sales at home literally overnight, businesses must be aware of and consciously address their use and treatment of "natural capital."

Externalities and the "Tragedy of the Commons"

An externality is an effect (negative or positive) on someone uninvolved in the action that created it. In a neighborhood park, second-hand cigarette smoke is generally considered a negative externality by non-smokers, while a neighbor who plants a garden that is casually enjoyed by others is an example of a positive externality. Hypothetically, "the commons" refers to those public goods that are not privately owned but that can be individually exploited, such as the neighborhood air in the above example. The concept that individual interests acting on a common resource will invariably lead to the degradation of those assets to the detriment of all is known as "the tragedy of the commons."

In regard to natural resources, pollution of various sorts is often the result of the negative externalities of industrial production and disposal of goods and services. One strategy of addressing this class of externality is to force the producer to internalize the cost of the pollution through financial penalties. By employing so-called pigouvian taxes, the producer would make an optimal or efficient production decision while accounting for the externalities. Theoretically, the resultant taxes would be used to clean up any resulting pollution or compensate those affected by it. Ronald Coase noted that in certain situations, pigouvian taxes would not result in economically efficient outcomes and the so-called Coase theorem posits that externalities can be eliminated if property rights are well-defined, people act rationally, and transactions costs are minimal. In essence, if all affected parties are brought into the transaction at a low cost and clear property rights allow those parties to agree on prices, externalities cease to exist by definition. While perhaps applicable to some situations, others, such as air pollution, fail the Coase theorem's requisite assumptions, and so governmental regulations are often invoked in an attempt to manage the resulting natural resource use and degradation.

Depletion and Sustainable Development

Depletion implies an unavoidable future reduction in natural resource consumption, which then naturally leads to the concepts of conservation and sustainability. The idea of conservation is rather straightforward: consume less today to provide for more consumption tomorrow while maximizing current nonuse and indirect-use value, if any. However, the concept of sustainability and sustainable development is less clearly developed. A widely accepted definition promulgated by the United Nations is as follows: "Sustainable development is development that meets the needs of the present without compromising the ability of future generations to meet their own needs" (*Our Common Future* by the World Commission on Environment and Development, 1987).

The difficulty in fulfilling this commitment lies in the twin unknowns of the needs and especially the abilities of future generations. Specifically, considering finite resources such as oil, any consumption today limits future generations from meeting similar needs at similar costs with current technologies. Sustainability concepts such as Natural Capitalism and The Natural Step advocate not conservation, but rather equivalent consumption while reducing natural resource use to remain within the carrying capacity of the ecosystem through greater efficiencies, waste reduction, reuse of existing resources, and increased use of renewable resources. Specifically, the sustainability concept of Natural Capitalism seeks to fairly value all types of capital including human capital and natural capital and advocates increased levels of economic activity with decreased overall resource degradation through the following:

- *Radical resource productivity:* The natural evolution of capitalist businesses in a competitive market is to increase production efficiencies thereby reducing costs and yielding higher profits. This results in increased resource productivity. Resource productivity is kept artificially low through the use of subsidies, especially those directly targeted at natural resources such as oil and timber, because the reduced prices inhibit the motivation for innovation and investments in efficiency gains.
- *Biomimicry:* Many production processes that we currently rely on, such as metal and glass production, are incredibly energy intensive and produce significant waste streams. Processes have been discovered in nature that accomplish similar things, such as the production of a pearl by an oyster, but that use significantly less energy and raw materials to do so. Exploring and imitating natural processes is one way to vastly increase resource productivity.

- *A service and flow economy:* A shift from production of goods to the sale of services would address many of the pollution and waste externalities currently borne by society. In essence, if ownership of all products was retained by the manufacturers and use was simply leased to customers, it is postulated that the manufacturers would be given incentives to minimize materials use, maximize durability, and design for maintainability and deconstruction; all of which are things that would result in enhanced resource productivity and reduced waste. This concept does not consider the possibility that products may suffer their own tragedy of the commons. That is, if a consumer does not own a product, there is little incentive to take care of it. Rather, the user would most likely attempt to derive maximum utility from the product with little regard to potential future users. This would likely result in premature product retirement or require products to be overengineered for durability: both situations that would reduce resource productivity.
- *Investing in natural capital:* This concept assumes that ecosystems that produce natural resources have been damaged by human activities and thus require investment to maintain output. On an individual scale with clear property rights, such as a family farm, the need for investment in natural capital is clear. If the soil cannot support the seed and the crops fail, the farm fails. On a broader scale, however, no clear framework is proposed for dealing with common resource issues such as air quality or ocean health. One potential mechanism could be to recognize the value of natural capital in the system of national accounts, as explored below, and charge governments with maintaining the balance.

Some argue that taking steps to actively reduce resource consumption in a capitalistic economic system is wholly unnecessary as prices themselves will regulate resource use. The classic energy example begins with whale oil—a common energy source in the 19th century. As whale stocks declined, whale oil became more and more expensive, which provided a market opportunity for entrepreneurs to develop new and cheaper energy sources. Coal and eventually petroleum-based products rapidly replaced whale oil, whose price plummeted and the industry largely collapsed. The same logic would predict that as (and not until) petroleum prices increase due to scarcity or increased demand, new energy technologies will be developed (perhaps fusion and the lauded hydrogen economy) that will eventually eclipse the old and become dominant.

This framework fails to deal with environmental degradation that is a result of short-term profit taking and a lack of human knowledge about the environment. The sardine markets around Monterey, California, in the mid-1950s did not experience an orderly increase in price due to scarcity, which might have led to innovation and the productive stewardship of the fishing grounds rather than the catastrophic collapse of an entire natural resource with long-lasting economic and environmental consequences. This framework also fails to address the issue of generational equity: that is, whether one generation of people should be able to drive a resource to scarcity and thereby prevent later generations from enjoying the same resource.

Representation in the System of National Accounts

The United Nations System of National Accounts, first published in 1953, aims to provide a standardized, systematic, and complete method of accounting for economic activities. Gross Domestic Product (GDP) attempts to capture the total value of final goods and services produced during a specific timeframe according to the formula

$$\begin{aligned}\text{GDP} = {} & \text{consumption} + \text{investment} \\ & + \text{exports} - \text{imports}.\end{aligned}$$

Investment, in this sense, refers to the acquisition of capital goods or goods that are not consumed today but rather used to produce additional goods in the future.

GDP is generally accepted as an indicator of overall health of an economy; yet it does not take into account environmental factors such as natural resource stocks or ecosystem health. For example, if the harvest of a certain fish is reduced to allow greater reproduction and hence larger harvests in the future (a classic investment), GDP is reduced due to the lower consumption today. Conversely, if the fishing harvest is increased, GDP is increased even though the long-term viability of the fishing grounds may be damaged. Proponents claim that by adding environmental factors into the System of National Accounts, a more accurate sense of true economic health can be gleaned from the resulting data. Since 1994, the London Group on Environmental Accounting, an international group operating under the guidance of the United Nations Statistic Division, has been researching and developing standards by which to value and report natural resource assets within the framework of the National System of Accounts. As this work becomes accepted, it is expected that natural resource stocks and general environmental health will be reported, valued, and managed like other capital assets.

Conclusion

All raw materials used in the world's economy are drawn from or rely on natural resources. Energy resources are particularly important fuels in the economic engine with oil, natural gas, and coal, all nonrenewable natural resources, providing for a vast majority of the world's energy consumption. Many of the social and ethical issues surrounding natural resource consumption and conservation are a result of externalities that businesses cannot, or choose not to, address. While the natural course of competitive commerce is to improve productivity and capital efficiency, externalities need to be proactively addressed by businesses to minimize negative environmental impacts and to avoid social reactions that tend to be expensive for all involved. Some natural resources like solar energy are clear, free, and virtually inexhaustible. However, most others are either scarce in occurrence or biologically complex or both and require thoughtful stewardship to ensure optimal and just use both today and in the future.

—Craig S. Lindqvist

See also Carrying Capacity; Externalities; Natural Capital; Pollution; Sustainability; Tragedy of the Commons

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Natural Resources Defense Council

The Natural Resources Defense Council (NRDC) is an environmental activist organization. While it is considered a special interest group that has an agenda, the depth and scope of the NRDC is far greater than that of most environmental activist groups. The NRDC has not only the support of 1.2 million members but also experts in law and science who work with many different groups to not merely criticize but to lend their expertise to these various groups in helping develop more efficient methods in such areas as renewable energy, coal technology, nuclear energy, and cleaner fuel burning cars. It is venues like this that give the NRDC credibility among various stakeholders in the United States and abroad. For example, the NRDC has partnered with Environmental Entrepreneurs, a national community of professionals and businesspeople who believe in protecting the environment while building economic prosperity. This has resulted in bringing together the business community, government, and the NRDC in bipartisan fashion to help shape state and national policy. Through collaborative efforts with companies like Environmental Entrepreneurs, the NRDC has been able to address issues such as energy, energy efficiency, and water purity, by publishing position papers that not only use NRDC sources but are often supported by the industries they are studying. For example, expanding the ethanol business would not only benefit farmers but also the auto, manufacturing, and trucking industries by providing a cheaper form of energy than gasoline or diesel fuel, as well as reducing U.S. greenhouse gas emissions.

This is not to say that the NRDC enjoys universal respect from the business community; it does not. Some in the business community look at the NRDC as a liability because more often than not their suggestions entail additional capital spending, thus reducing profits. Through its vast world membership, the NRDC mobilizes activists to assist in the protection of forests and marine ecosystems that may be threatened by industrialization or the extraction of natural resources from the areas. In addition, the NRDC has established itself as a legitimate watchdog agency in areas of environmental policy that are generated by our lawmakers. It maintains a legal presence in Washington, D.C., to examine all legislation being put forward that may have an impact on the environment or health of the United States and its citizens. NRDC lawyers have addressed various issues concerning the environment and its protection. They have worked collaboratively with various businesses, with government agencies, and with other special interest groups to monitor the types of environmental legislation introduced by the government and to react if certain legislation runs counter to what is considered prudent and safe. They maintain a comprehensive Web site, which covers a variety of environmental areas and also lists a number of reference links that will allow the user to get an "objective" picture of various environmental issues that the NRDC has chosen to challenge. The links give the user an opportunity to see how members of Congress vote on these issues. The Web site also provides information regarding national and international environmental law and their decisions. There is another link devoted exclusively to providing brief summaries of major federal environmental laws (with links to full text for each law) and related resources.

—Tom Marini

See also Environmental Ethics; Natural Resources

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Negligence

Negligence refers to an actor unintentionally causing harm to another due to the actor's failure to meet the requirements of the applicable standard of care. The standard of care is what an ordinary, reasonable person would have done in that situation. If an actor is found to be negligent, then that actor (the defendant) is liable for any harm that negligence caused the plaintiff. To prove that the defendant was negligent, the plaintiff must show (1) that the defendant owed a duty of care to the plaintiff, (2) that the defendant failed to meet the requirements of that duty, (3) that the breach of the duty was the cause of the harm, and (4) that the plaintiff suffered damages. In some cases, the defendant may be able to establish a defense that absolves him or her from liability to the plaintiff.

The Elements of a Negligence Claim

There are four elements to a negligence claim that the plaintiff must prove to hold the defendant responsible for the plaintiff's damages. First, the plaintiff must show that the defendant owed a duty of care to the plaintiff. A duty of care is the standard of behavior a reasonable, prudent person would follow to prevent causing harm to others. The defendant owes a duty of care to anyone that could foreseeably be harmed by the defendant's actions. For example, if the defendant is driving a car, then the defendant owes a duty to all other drivers on the road to drive in a reasonable manner (e.g., not driving too fast, staying within a lane on the road, obeying all traffic signals). In other situations, the defendant may not owe a duty to the plaintiff. For example, in most jurisdictions in the United States, a defendant that discovers someone in a dangerous situation—that was not caused by the defendant's actions—does not owe a duty to that person to help them. Although there is a duty not to cause harm to others by your actions, there generally is not a duty to provide a benefit to someone else. Thus, a defendant that ignores the pleas for help from a drowning plaintiff would not be liable for negligence because the defendant did not owe a duty to that plaintiff. An exception to this general rule, however, is when the defendant has a duty based on a special relationship with the plaintiff (e.g., the drowning plaintiff is the defendant's infant child).

Second, once it is established that the defendant owed a duty to the plaintiff, the plaintiff must prove that the defendant breached that duty of care. The duty of care is determined by considering what a reasonable person would do in that situation and can be very context specific. For example, although a reasonable person may drive her car at the maximum speed limit on a sunny day, that reasonable person would drive considerably slower on a day with low visibility due to fog. The reasonable person standard is an objective standard that applies to all people in that situation and does not depend on the defendant's actual, subjective beliefs. Professionals, however, typically have a higher standard than lay people. For example, a doctor performing a medical procedure must live up to the standards of a licensed doctor practicing in that area. If the defendant shows a reckless or willful disregard for the standard of care, then he or she may be said to be grossly negligent.

Third, the plaintiff must prove that their injuries were caused by the defendant's breach of the duty of care. This typically requires proof of two forms of causation: "but for" causation and proximate causation. "But for" causation means that the plaintiff's injuries would not have occurred "but for" the defendant's actions. That is, if we take away the defendant's action, would the accident still have occurred? For instance, in an automobile accident, we may ask, "Would the plaintiff still have driven his or her car into the telephone pole even if the defendant had not ignored the stop sign?" Proximate causation refers to the foreseeability of harm caused by the defendant's actions. In general, if the defendant's actions caused an unforeseeable type of harm, then the defendant was not the proximate cause of the injury. For example, in the classic 1928 case of *Palsgraf v. Long Island Railroad Company,* railroad employees attempted to pull a man onto a moving train. During that process, the man dropped an unmarked package containing explosives. The resulting explosion caused the platform to vibrate, which in turn caused a set of scales to fall on Palsgraf and injure her. Palsgraf sued the railroad company for negligence, but the court ruled that the defendant was not negligent because it was not foreseeable that pulling a man onto a moving train (the breach of duty) would cause such an explosion (i.e., there was no proximate causation).

Finally, the plaintiff must show that he or she suffered damages of some sort, including harm to the person or property. As long as the plaintiff was injured in a foreseeable manner (i.e., proximate causation), the defendant is liable for all damages even if the extent of the plaintiff's injuries were unforeseeable. It is commonly stated that the defendant takes her plaintiff as she finds him. For example, although most people would suffer only slight injuries from being knocked to the ground, if the plaintiff has a very rare and severe back condition that is aggravated by the accident, then the defendant is still liable for the full extent of the plaintiff's injuries.

Defenses to a Negligence Claim

Even if the plaintiff can establish all four elements of a negligence claim, the defendant can either reduce his or her liability or escape liability entirely by claiming a defense. In some situations, the defendant may claim that the plaintiff was aware of and assumed the risk of injury from the defendant's negligent conduct. In other situations, the defendant may claim either contributory negligence or comparative negligence (a jurisdiction will have one rule or the other). Under contributory negligence, if the plaintiff's own negligent conduct contributed to causing the accident, then the plaintiff cannot recover any damages from the defendant. Under comparative negligence, on the other hand, a negligent plaintiff can still recover from the defendant, but the plaintiff's recovery is reduced by the amount that her own negligence contributed to causing the accident (e.g., if the plaintiff's negligence was 10% of the cause of the accident, then the defendant will only pay for 90% of the plaintiff's damages).

—David Hess

See also Compensatory Damages; Due Care Theory; Reasonable Person Standard; Torts

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Negotiation and Bargaining

Negotiation is the process of conferring with others to reach an agreement. Bargaining occurs when there is a dispute over the terms involved. A straightforward allocation of adequate resources would involve negotiation, but if there is a shortage of time, money, or materials, then the parties will bargain over the exact distribution to promote their own best interests. Collective bargaining is a structured process where a group such as a union will negotiate with an employer as a single unit about terms of their employment contract.

The basic conditions for negotiation are that the parties are voluntary participants and there is a positive bargaining zone. Thus, there is no negotiation in mugging at gunpoint or when groceries are offered at a fixed price in the store and there are sufficient paying customers that the storekeeper has no incentive to lower the price. A bargaining zone is a range of exchange where one side is willing to offer and the other is willing to accept. If neither side is willing to extend the zone then there is no room for meaningful negotiation.

There are several other necessary elements for negotiations to be successful. Initially, the parties involved must have the power to settle. Second, all the parties involved need to be willing to take part in the negotiation. If critical parties are absent or if one party is not prepared to bargain in good faith, then there is little hope for a workable agreement. Moreover, the parties need to be psychologically prepared to negotiate; if there is high emotion, inadequate information, or failure to formulate a negotiation strategy, then the parties' negotiations are unlikely to be productive.

The parties must in some way be mutually dependent and have the ability to influence each other. Such influence can be seen as having something the other party desires or having the means to increase benefits for the other side (or conversely the ability to inflict distress). A negotiator needs some form of leverage to provide an incentive to the other side to alter their behavior. Where the power is completely disproportionate, meaningful negotiation with the other party is also unlikely to occur. Parties must also have some sense that delay will result in some adverse action. If only one side is under great time pressure, then the party with time to spare is likely to use that leverage to extract greater substantive gains from the party that is looking for a quick solution. The Paris peace talks to terminate the Vietnam War illustrate this: The Vietcong were able to procrastinate to the point where the Americans made substantive concessions to hasten the negotiation. On a more mundane level, the householder with leaking pipes needs a repair urgently and thus will be in no position to bargain with an available plumber.

If there is a better deal available elsewhere or the psychological stress is not worth the potential benefits, then people will break negotiations. Contemporary negotiation theorists often refer to the point at which someone will walk away by saying that any deal must improve on a party's "best alternative to a negotiated agreement."

Finally, participants must feel that there are settlement options available that will meet their needs. In some cases, one party will not want to create a precedent of compromise or will want to establish a principle, even at the risk of losing the case entirely. Thus, people charged with a criminal offense will often be unwilling to make a plea bargain in order that they can have a public hearing that they believe will lead to complete exoneration. Similarly, tort cases where one party is looking for definitive vindication may not be suitable for negotiation.

Types of Negotiation

In very broad terms, we can classify negotiation as belonging to either of two schools: the so-called positional negotiation and interest-based negotiation. *Positional bargaining* is a negotiation strategy in which the disputant takes a series of positions that represent alternate solutions. It is also referred to as *distributional bargaining* because its primary function is to allocate a limited resource. The positions are rank ordered by the negotiator according to his or her preferred outcomes. The initial position represents the maximum gain, and each subsequent one represents a compromise from that ideal. Each party will have at least two positions: the opening position and the "bottom line." Agreement is reached when the parties' positions converge and they enter an acceptable settlement range between these two extremes. An example of this sort of negotiation would be one between a car salesman and a potential customer. The dealer has a bottom line of $20,000 but feels that the completely naive customer would pay the sticker price of $25,000. The customer is unwilling to pay more than $22,000 but starts at $18,000 to give himself some flexibility in the negotiation. So the customer offers his $18,000 and the salesman demands $25,000, although they both know that they will make concessions toward the other: They subsequently try to concede in as small increments as possible without forsaking the deal. They may come to an agreement in the range of $20,000 to $22,000.

Positional bargaining occurs most typically when the parties are not significantly interdependent and when there is no value placed on a continuing relationship. It also comes into play when there are limits on the negotiation—for example, when there is restricted time or when the items or services are not fungible and are strictly finite. Therefore, at a flea market, for instance, positional bargaining would be the standard way of reaching a settlement on the price of items for sale. The goal of each party is to win as much as possible, where a win for one side is thought of as a loss for the other. A distinct disadvantage of this approach is that it is difficult to alter position while saving face: If a car dealer says that his "bottom line" is $25,000, then it becomes hard for him to subsequently make concessions or justify a new, lower price. Moreover, if prices are somewhat arbitrary, as they are at a flea market, then argument over two proposed prices for a good can quickly descend into a contest of wills, which itself can sabotage a possible settlement. The adoption of positional bargaining fosters gambits, bluffing, extreme posturing, and game-playing in that it is driven mainly by the best individual payoff, however that may be accomplished.

Positional bargaining may be contrasted with *interest-based bargaining*, which focuses on satisfying as many interests or needs as possible for all negotiators (alternatively named *principled bargaining* or *integrative bargaining*). It does this by using a problem-solving approach, which tries not to distribute rewards in a win/lose manner. It has different initial assumptions from positional bargaining in that it recognizes that each party has multiple interests—a concern not only for the substance of the agreement but also for how the way in which settlement is reached affects the parties' feelings about the result. If one side feels railroaded, unheard, cheated, or bluffed, then the process is in some way tarnished and more likely to unravel whatever the substantive agreement may have been. Interests may be combined in a variety of ways, leading to a wide range of possible solutions. Since resources are not seen as limited to the monetary offers alone, more factors can be brought into the negotiation.

Interest-based bargaining is a process involving several stages. As it is still an unusual way of negotiating, parties initially have to learn about and accept the procedure and realize it requires a modicum of trust and disclosure. Then, they have to define what they see as the issues in the case. This might be done by finding out the reasons behind a stated claim that may go beyond getting the best substantive payoff; a person may have a strong interest in perceiving that she has not been cheated or need to feel that her concerns have been heard and attended to. The initial monetary offer may then be framed in terms of these interests, say, precedent in other deals, the maximum that someone can afford, the average price based on research on the Web, or similar reasons.

Each side openly discusses its needs, interests, and concerns. The parties then collaboratively generate options for settlement based on the interests that have been voiced and the criteria that are mutually acceptable. This level of abstraction allows the parties to generate multiple options for settlement. A key element is for the parties to find agreement in principle, for example, that a dealer is entitled to a fair profit or a customer should not pay more for a used car than the blue book value. Thus, parties may agree on, say, the principle of splitting assets equally in a divorce or that a reasonable price for real estate is the middle estimate from three assessors. Many assert that it is easier to argue rationally about the foundation principle than it is to haggle over positions. The various options are then assessed, and some final bargaining occurs.

Consider an example: A worker asks his boss for a raise, and his boss responds that he cannot afford it. In a positional framework, this negotiation is liable to end in stalemate or at least with a disgruntled employee. With an interest-based approach, the two sit down and discover each other's needs and concerns. It could be that the boss would like to pay more but cannot afford to do so on his present margins. The worker is actually looking for money largely as a symbol of recognition for what he perceives to be superior performance. Collaboratively, they generate options that will satisfy both their interests: perhaps some nonfinancial reward for the worker, a delayed bonus contingent on greater projected profits in the future, the opportunity for overtime, and so forth. The investigation into the reasons behind the positions allows both parties more flexibility and creativity in attempting to resolve their differences.

Appropriate Bargaining Styles

Interest-based bargaining has great potential for reaching lasting settlements that satisfy specific interests in a way that promotes trust and good relationships. Interest-based bargaining does seem to offer the best means for disputants to reach agreements that approach Pareto optimality. However, it is not suitable for all disputes; it takes time, a cooperative environment, and a willingness to disclose information that in positional bargaining would often be a closely held secret. It is also quite a complex process requiring trust, skill, creativity, and practice. We are all more familiar with positional negotiation because it is more typical of our everyday encounters; yet we should recognize that it tends to bruise relationships because of the lack of trust and the subterfuge that it encourages. It may also lead to a less than optimal agreement because the full range of interests and potential exchanges remain unstated.

Contemporary research in negotiation has looked at both the rational quantitative dimension of negotiation and the more qualitative issues brought into play by the psychological dynamics and motivations of the parties. It recognizes that it is appropriate for most negotiation to incorporate both distributive and integrative elements. There has also been considerable work dealing with the role of third-party intervention to facilitate optimal outcomes, the ethics of negotiation, and the nature of apparently intractable conflicts.

—Kevin Gibson

See also Alternative Dispute Resolution (ADR); Barter; Bluffing and Deception in Negotiations; Game Theory; Nash Equilibrium; Ombudsperson; Pareto Efficiency; Satisficing; Trust

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NEOCONSERVATISM

Neoconservatism was born when a group of liberal and radical New York intellectuals became disenchanted with the political left in the late 1960s. From the perspective of the left, which they attacked, they were conservative and were accused of so being, but because they retained an attachment to many of the liberal goals that had long attracted them and because they were rarely Christian, from the South, or inclined to romanticize the past, they were not traditional conservatives. They were inclined, for example, to praise FDR, but never Barry Goldwater or Russell Kirk. These neoconservatives (also referred to as neocons) agreed with the left that it was critical to end racially based injustice and the chronically disadvantaged position of the poor, but they broke with their leftist comrades over the way to achieve these goals. In general, they argued that in its impassioned pursuit of equality, the left had become blind to other worthy goals, such as a deference to democratic procedures, the liberty of the individual, and the complex social and educational requirements of stable government. In foreign policy, they charged liberals with having forgotten the need to remain strong against the Soviet threat. Neocons charged the liberals of the late 1960s and later with having forgotten the prudent legacy of their own past, so that they might more appropriately be called "paleolibs."

The early neocons agreed with liberals that poverty and racism were massive problems in the United States, for example. But they attacked the left for advancing state-supported affirmative action as a way of promoting these rights, for it would swell the state, limit liberty, and create resentment; similar concerns led them to oppose massive, state-run welfare programs. They agreed with libertarians that government enforcement of a more strict equality threatened individual liberty, and they agreed with fiscal conservatives that the Great Society welfare programs would place huge financial burdens on the economy. More than either of these groups, however, the neocons focused their writing on the indirect social and educational consequences of liberal approaches to solving the problems of racism and poverty. They stressed that it is a problem to encourage dependency on the state, rather than self-reliance, and they held that antipoverty programs sometimes weakened the family, an institution they considered important for society in general and especially important for the educational and economic progress of African Americans.

Early neoconservatives broke with their erstwhile liberal friends and allies over the radical assaults on the universities in the late 1960s as well. They denounced the students and professors who saw fit to protest racism and the war in Vietnam by disrupting classes and radicalizing the curricula. Education, the neocons argued, required a patient exploration of all serious alternatives and would suffer—or cease—if it came to be seen primarily as a means to advance the goals of a disadvantaged group. Hence neocons found themselves in quarrels with those favoring educational reform to advance the rights of women, Afro-Americans, and gays. They considered the "traditional" curricula to be intellectually liberating rather than the politically correct agenda that challenged it.

Free speech is another issue that helped give shape to neoconservatism. As the Supreme Court expanded the protections offered under the First Amendment, neocons argued on constitutional grounds that the Court was rewriting the Constitution, not interpreting it, and they argued on more political grounds that its new rules would be destructive. They maintained, for example, that protecting naked dancing as "speech" would only serve to devalue reasoned speech, and they argued as well that the resultant pornography was a distraction from education and an impediment to the formation of character. And is it consistent with a basically democratic Constitution that nine judges, or their majority of only five, determine such policies? On these issues, the largely secular neocons joined with religious conservatives and disagreed with libertarians. The principle of "consenting adults" is not their mantra, but their reservations are generally rooted in a view of the national interest, not the word of God.

It is common for neoconservatives to address the relationship between character and politics. Free and democratic politics, they argue, requires a responsible citizenry, and a responsible citizenry needs to be formed or encouraged, or at least not discouraged. Defenders of both liberty and equality, neocons worry that when taken to an extreme, one or the other of these principles can undermine the virtues needed in a free and democratic people. The goal of politics is not so simple as granting complete liberty to each person to choose to do what he or she may happen to want, the neocons argue, for what we want both influences and is influenced by the choices of others. They speak of a public culture and a "tone" of society, and they try to keep this in view as they analyze one policy or another. Although often not themselves religious, neocons tend to argue that religion can help form the character traits our nation needs and has long taken for granted.

Neoconservatives tend to support the war in Iraq and the policies of preemption and nation building that underlie it. Francis Fukuyama is an important and telling exception, but neocons are generally prepared to run risks in the hope of building democracies, at least in strategically important locations. They expect these democratic regimes to be more decent and more friendly to the United States than the tyrannies they are expected to replace. In their eyes, the United States of the 1990s was like Hamlet, always finding excuses for inaction in the face of growing threats, and like Gulliver, allowing itself to be tied down by a multitude of international sensitivities.

Neocons tend to be scornful of the opinion that today's UN is a source of wisdom, justice, or strength. While "internationalists" are often outraged at the readiness of neocons to call for U.S. unilateral action, which they see as undermining the UN, traditional conservatives consider neocons naïve for trying to force democracy into places it has never gone before. Neocons are prone to citing the remarkable spread of democracy over the last century, while paleocons are more inclined to note how few and unique are the examples of successful "nation building." Neocons must also face the charge that democratically elected governments may not always turn out to be so friendly to the United States, as the case of Hamas among the Palestinians now suggests.

To see contemporary neoconservatism in action, consult publications such as *The Weekly Standard, The National Interest, The Public Interest, The New Republic,* and *Commentary* and review the Web sites of such think tanks as the Project for the New American Century and The American Enterprise Institute. Neocons are far less numerous than traditional conservatives, libertarians, or liberals, but their influence extends well beyond their ranks. Powerful leaders such as Paul Wolfowitz, Jeanne Kirkpatrick, and Patrick Moynihan are or were neoconservatives, and Ronald Reagan and the two Bush presidents are among the many who have been influenced by them.

The first neoconservatives were left-leaning intellectuals from New York City, and they wrote especially for the journals mentioned above. The key figures in these early years included Irving Kristol (sometimes dubbed the godfather of neoconservatism), Gertrude Himmelfarb, and Norman Podhoretz. As neocons gained increased political influence, their center moved to Washington, D.C., where one now finds such prominent neocons as William Kristol, William Bennett, and Francis Fukuyama. A glance at both these earlier and later neocons suggests that they are defined by at least this one characteristic: They enjoy vigorous argument—even with each other.

—Wayne Ambler

See also Liberalism; Libertarianism

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Neo-Kantian Ethics

Neo-Kantian ethics refers to any philosophical work that derives from the work of Immanuel Kant. Contemporary scholars in this area seek to advance key insights of Kant with the tools of contemporary analytic philosophy while at the same time avoiding difficulties that may be found in some of Kant's original arguments. Such work is increasingly used to provide a theoretical foundation for business ethics.

There are many active areas of interest in this vibrant field. Regarding ethical motivation, neo-Kantians defend the view that such motivation properly originates within the self, and not from external sources such as God or other fear or concern for the opinions of others. In this view, agents who place profits ahead of moral duties are seen as not merely unethical but irrational. The question of how to understand the import of Kant's famous categorical imperative is another active area of study. The categorical imperative, in its primary formulation, holds that one ought only act on the principles that can be universalized. One prominent view holds that the categorical imperative ought to be properly understood as a side-constraint on action. Actions are permitted insofar as they do not violate such constraints. This view, most notably defended by Barbara Herman, has gained significant traction in recent years. The view is important insofar as it disarms many important, historical criticisms of the categorical imperative, such as the claim that Kantians must constantly apply the categorical imperative if they are to know how to act at any given moment.

Neo-Kantians also seek to better understand what duties are entailed by the Kantian doctrine of respect for persons, which constitutes the second formulation of the categorical imperative. One prominent view holds that a proper understanding of the duty to respect persons yields a core set of basic human rights that must be respected. Such a view has important implications for business ethics. In particular, such a view may indicate that corporate managers have specific duties to employees (including employees in contract factories) regarding health, safety, and working conditions, as well as to other stakeholders. Given this concern with human rights, neo-Kantians tend to associate with a cosmopolitan perspective regarding global justice. In the cosmopolitan view, a system of global socioeconomic justice must be grounded in universal ethical norms. Cosmopolitans see political institutions as a means to ensure respect for such core norms. Nation-states and multinational corporations that contribute to the violation of these norms, or merely tolerate the violations of such norms, are problems that must be overcome.

Kant's ethical philosophy is notorious for having given little weight to the moral status of nonhuman animals and to the natural environment. Some neo-Kantians who are persuaded by the merits of a Kantian perspective on ethical relations among persons are now seeking to provide perspectives on duties toward animals and natural environments. There are a variety of views in this emerging area. According to one such view, nonhuman animals have value in proportion to the extent that they exhibit agency. There is, however, little agreement among neo-Kantians on these questions.

Critics of neo-Kantian ethics argue that if theorists with Kantian sympathies have not yet been able to fully work out some of the most pressing difficulties of Kantian thought, then the Kantian project ought to be given up as untenable.

The aim of neo-Kantian ethics is to demonstrate that simple invocations of old objections to Kant's ethics cannot be a sufficient basis for dismissing Kantian ethics. Neo-Kantian ethicists believe that they provide a firm basis for ethical theorizing about business and about what it means to live a rational life as a businessperson.

—Denis G. Arnold

See also Deontological Ethical Systems; Human Rights; Kant, Immanuel; Kantian Ethics; Moral Agency; Moral Point of View; Moral Reasoning; Universalizability, Principle of

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Net Present Value

The net present value (NPV) of an investment project is the difference between the present value of the stream of future net (or free) cash flows generated by the project and its current investment costs. Thus, this concept represents an application of cost-benefit analysis to problems in financial economics where net revenues are the benefits. A typical example is the expansion of a firm's manufacturing facilities, which requires the firm to sacrifice funds in the present so that it may increase its sales in the future.

Importance in Financial Management

The fundamental importance of the NPV concept to the financial management of the firm lies in the fact that investment projects with positive NPV increase the wealth of the firm's shareholders by that amount, whereas projects with negative NPV reduce shareholder wealth. Because the paramount objective of the financial manager should be to maximize the wealth of the firm's current shareholders, it follows that management should undertake only investment projects with positive NPV. Unfortunately, sometimes the manager's own objectives may be in conflict with shareholders' wealth maximization, although this problem of diverging objectives may be mitigated by carefully designing the manager's compensation contract.

NPV Arithmetic

To illustrate the mechanics of the NPV technique, assume that the project requires an initial investment of I dollars, the free cash flow in any time period t is C_t, where $t = 1, 2, \ldots, n$, and the required rate of return (discount rate) on the project is r. Then, the NPV is obtained by using the following general formula:

$$\text{NPV} = -I + C_1/(1+r)^1 + C_2/(1+r)^2 + \ldots + C_n/(1+r)^n.$$

To take an example, consider an investment project with I = \$2,000, C_1 = \$1,100, C_2 = \$1,210, and C_3 = \$1,331. Assume, in addition, that the firm's investors require a rate of return of $r = 10\%$ per annum. Then, this project's NPV = $-2{,}000 + 1{,}100/(1 + 0.1)^1 + 1{,}210/(1 + 0.1)^2 + 1{,}331/(1 + 0.1)^3$ = \$1,000. Consequently, by undertaking this project, management is adding \$1,000 to the firm's wealth.

Potential Implementation Problems

Although NPV is an invaluable tool for the financial management of the firm, it may lead to faulty decisions if its implementation is incorrect. Indeed, note from the above general formula that the correct computation of the NPV technique critically depends on choosing an appropriate value for the discount rate (rate of return), r. The appropriate rate, in turn, depends on the risk level of the project. In practice, however, the risk level is often difficult to ascertain with precision. Because of this difficulty, an erroneous choice of discount rate may indicate that a project should be rejected when, in fact, it should be accepted. Of course, the converse may occur as well. These potential errors, if left unchecked, may have a deleterious effect on the value of the firm.

NPV Profile

A useful tool for checking the sensitivity of the NPV to the choice of discount rate, r, is the NPV profile, which provides a visual representation of the NPV of a project for a variety of discount rates. For the numerical example given above, the NPV profile has a downward-sloping shape. Indeed, substituting $r = 0$, 0.1, 0.2, 0.3, 0.4, and 0.5 in the general formula produces NPV = \$1,641, \$1,000, \$527.20, \$167.96, –\$111.88, and –\$334.52, respectively. Recall that the firm's required discount rate is $r = 0.10$, or 10%, so its estimated NPV is \$1,000. However, if the firm is unknowingly mistaken in choosing that value of r, then the NPV profile may visually reassure the firm that even a relatively large error in either direction may not be critical to the accept/reject decision. Indeed, based on the calculations just given, the project produces a positive NPV for any discount rate between $r = 0\%$ and at least $r = 30\%$.

In fact, by refining the discount rate values between $r = 30\%$ and $r = 40\%$, it can be verified that positive NPVs occur for all positive discount rates up to $r = 35.71\%$. Thus, if the correct but unidentified discount rate falls within this broad range, the firm can be confident that its decision to accept the project, based on its choice of a 10% discount rate, is likely to be correct. In this example, $r = 35.71\%$ determines the boundary between the accept/reject regions of the NPV profile. More generally, the discount rate at which a project achieves a zero NPV is known as the internal rate of return of the project and is an important financial concept in its own right.

—Ricardo J. Rodriguez

See also Cost-Benefit Analysis; Discounting the Future; Shareholder Model of Corporate Governance

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Networking

A network is a formation of individual agents or nodes where each is connected to one or more other nodes by a link. The individual nodes may be businesses, individuals, computers, or other units, and the links may be based on infrastructure, beneficial relationships, or collaboration. The term was first applied to social networks by J. A. Barnes in the 1950s. Networks can bring efficiency through the sharing of assets and pooling of competencies, and in the second half of the 20th century, networking became established as the preferred form of organization in many business sectors. Ethical aspects of networking include the requirement for openness, transparency, and trust if the networking is to be successful. Infrastructure networks such as airline route networks seldom involve ethical issues, although trust is an important element in some computer networks.

In networks where each link is undertaken for the benefit of the participants directly involved, such as supply chains, syndicated radio networks, or industry associations, ethical issues can arise in the course of the exchange between the individual members. One member may have, and abuse, market power or may seek to gain additional advantage by deceit, and the members of the network may join together to seek unfair advantage from a wider group with which the network deals.

Collaborative networks, sometimes called strategic alliances, replace a traditional contractual relationship between participants with a mutual commitment to apply one's resources toward the achievement of a shared goal. The essential feature is that the arrangements are entered into for mutual advantage but do not involve direct ownership by one party of the others, and extend beyond a simple contractual sale-and-purchase or design-and-construct agreement. Small- and medium-sized enterprises find alliances attractive as a means of enhancing competitiveness.

Collaborative networking promises the flexibility needed to succeed in complex, uncertain, and unforgiving business environments and the potential for increased innovation. Successful networking requires a level of openness, transparency, and tolerance of uncertainty beyond that required in a traditional business relationship, and collaborative networks will not achieve their promised benefits through the application of traditional management processes based on command and control. Trust and other unconventional management virtues, such as prudence, justice, and love, are essential to success in a situation where the individual units lose their independence yet remain separate. Issues can also arise in the apportionment of reward for the value added by each participant, as the extent to which each contributed to product or service improvement may be hard to determine.

Virtual networks, where the members do not make direct contact with each other, may be based on contractual or collaborative relationships. The absence of direct contact increases the opportunity for deceitful behavior, for instance, in the creation of false persona, as the very existence of each network member is taken on trust.

—Howard Harris

See also Spontaneous Order; Transaction Costs; Virtue Ethics

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Newly Industrialized Countries (NICs)

As the name implies, newly industrialized countries or NICs are generally understood to be those countries that have in the past few decades transitioned their economies from being primarily agricultural to newly industrialized. The economies of these countries are not as advanced as those of the developed countries such as the United States, Japan, and Western European states. However, they are more advanced than those of the so-called undeveloped or Third World countries. NIC is a socioeconomic term applied to countries that derive a significant portion of their national income from the goods-producing sector, which consists of industries associated with manufacturing, construction, and mining operations.

NICs began to be recognized in the 1970s when countries such as Hong Kong, South Korea, Singapore, and Taiwan underwent rapid industrial growth, most now having evolved beyond this status. Current examples are Turkey, Thailand, Malaysia, Mexico, Brazil, Argentina, South Africa, China, and India. Each of these countries is experiencing a general rise in per capita income, although a higher income does not necessarily reflect a higher development status. For example, India and China, due to large populations, are likely to have low per capita incomes even though they have experienced significant economic growth rates and have large manufacturing sectors. Industrialization and growth in NICs has been achieved through diverse means: for example, import-substitution in India, export-orientation in Taiwan and South Korea, investment in heavy industries in Russia, and attraction of inward foreign investment in China.

Yet there are some common features usually shared by NICs. These include recent political and economic reforms allowing for greater civil rights and market liberalization, strengthening of the legal and economic environment to foster privatization of ownership in industry and increased competition, and trade liberalization policies allowing increased exchange of goods and cross-border investment. In almost all NICs, greater industrialization has led to increased trade, participation in regional trading blocs, and attraction of foreign investment especially from developed countries.

However, NICs face certain problems that have ethical implications. Despite the attempt to decrease government regulation and increase market efficiency, governments continue to play a large role in artificially controlling currency exchange rates. Such controls have led to financial crises in countries such as Malaysia, Taiwan, South Korea, Mexico, Russia, and Argentina. To restructure their debt, these countries sought the assistance of the IMF, whose stringent conditions like raising taxes caused hardship to the local population, often creating controversy regarding the role played by the IMF. Furthermore, many of these countries follow an active industrial policy that encourages investment in certain sectors of the economy, and due to the considerable control exercised by the State, there is a great opportunity for corruption and bribery of public officials. Corruption in turn is a major detriment to further industrialization and contributes to an unfavorable business climate. Often, in NICs, rapid industrialization is not accompanied by the concurrent increase in investment in infrastructure, thereby creating unbalanced development in different regions of the country. Migration of labor from rural to urban areas often results in problems such as overcrowding in cities, pollution, environmental degradation, and water shortages. While laws exist on paper, they may be unenforceable due to lack of resources to fund adequate law enforcement or due to lack of political will, resulting in low labor standards reflected in low wages, unsafe and unhealthy working conditions, and use of child labor. Furthermore, wealth created by industrialization, more often than not, is unequally distributed among different sectors of society leading to huge disparities in incomes and standards of living. From an international perspective, corporations operating in NICs are frequently accused of cutting corners on wages, working conditions, and environmental protections, leading to a "race to the bottom" in terms of labor practices and contributing to global environmental problems. Others, however, argue that it would be unrealistic to expect the same wages, working conditions, and environmental protections in all countries no matter the stage of development, and to demand this would only serve to entrench the position of advantage of developed countries.

Despite these problems and controversies, NICs have huge potential for economic growth. They are currently showing growth rates double those of developed nations and hence continue to attract foreign investment.

—Manisha Singal and Richard E. Wokutch

See also Child Labor; Developing World; Globalization; International Monetary Fund (IMF); Sweatshops; World Bank

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Nihilism

In laymen's terms, nihilism refers to the experience of having lost a sense of meaning or purpose in life. It also relates to the belief that nothing is valuable or desirable. The philosophical understanding of the term, though related to its popular use, is somewhat more complex. Over past centuries, philosophers have debated the cause of the loss of meaning in life vigorously and have, therefore, come to define nihilism in many different ways. These philosophical nuances provide us with important insights into the manifestations of nihilism in the business realm.

One of the prominent distinctions that philosophers make when discussing nihilism is what may be described as the difference between explicit and implicit nihilism. Explicit nihilism could be defined as the absolute repudiation of worth, purpose, or desirability. It is often the result of the realization that the truth, values, or purposes that we as human beings use to give our lives structure or to legitimize our decisions and actions lack irrefutable ground. Ethical or moral nihilism is a certain type of explicit nihilism that is the result of the realization that values refer to nothing more than bias or taste. Another form of explicit nihilism that most closely resembles the popular use of the term *existential nihilism* refers to the feeling of emptiness or pointlessness, or the experience that "life has no meaning."

Implicit nihilism is quite different from explicit nihilism. Its main proponent, Nietzsche, argued that implicit nihilism is the most extreme form of nihilism—one that results from an uncritical acceptance of certain truth claims as irrefutable. In fact, implicit nihilism is the result of operating under the assumption that one's values and truth statements are rooted in a transcendental source, such as God or some ideology. Implicit nihilism often goes hand in hand with a devaluation of life and a negation of a mortal existence in favor of the pursuit of a spiritual realm, an afterlife, or realization of some ideological ideal. One can distinguish many forms of implicit nihilism: Transcendental nihilism is the nihilism of "absolute values" or "absolute spheres," that is, the belief that God, or its representative on earth, defines what is right or wrong. Nietzsche believed that this leads to a "slave morality" or "herd mentality," whereby human beings lose their ability to judge for themselves. After the rise of Modernity, the God's sanctioning of values and truths fell away because of the Enlightenment's emphasis on the use of reason and autonomous thinking. This, however, merely led to a new kind of nihilism: passive nihilism. Passive nihilists are so disillusioned by the dismantlement of their certainties that they tend to feel that they have neither the energy nor the right to create any truths or goals for themselves. However, a worse response, according to Nietzsche, is that of reactive nihilism, which entails replacing transcendent foundationalism with an alternative universal truth. An example of reactive nihilism is found in socialism, which replaced God with yet another "moral superstructure" and, in that sense, was merely an ironic reenactment of transcendental nihilism.

The experience of nihilism is not restricted to any specific sphere of life, and hence has implications for business organizations. The various manifestations of nihilism in business organizations can be described by addressing a few basic questions that come up in the work environment. First, "Why do we work?" Experiences of explicit nihilism may cause people to have no answer to this question, since no activity has any ultimate meaning and significance from the perspective of explicit nihilism. This may cause a lack of work ethic or low levels of staff motivation, which may undermine employees' sense of doing meaningful work. A second question may be, "Why be ethical if all values are relative and there are no absolute truths?" This form of moral nihilism makes it very difficult for corporations to foster a certain ethical climate and direct ethical behavior. A third question that relates to explicit nihilism in the corporate world is, "Who can we trust?" A form of explicit nihilism is found in the public's disillusionment in the wake of deceptive financial reporting among big corporations. The mistrust that was caused by collapses like Enron is a by-product of the explicit nihilism that sets in when "truth" is revealed as "fiction" and "falsity." Uncertainty about whom and what to trust in terms of representations of truth often leave stakeholders paralyzed, cynical, and without resolve. Being aware of the dangers of both implicit and explicit nihilism may serve to make stakeholders more creative and vigilant in their ongoing questioning of corporate practices.

To address the phenomenon of implicit relativism in business is more difficult, though no less important. In counteracting the dynamics of implicit nihilism in the corporate realm, we may have to pose a few rather radical questions: Why believe in the "truths" that capitalism advocates? If one considers the widening gaps between rich and poor globally, advocates of a simplistic belief in the success of the hidden hand may suffer from some form of implicit nihilism—that is, an inability to critically assess and reconsider certain commonly held conceptions. The alternative may not be to abolish capitalism or to replace capitalism with another ideology but rather to foster the ability of people to judge for themselves. This would challenge stakeholders to interrogate the "truth" that is presented to them in corporate marketing and reporting. If stakeholders want to be more than "herd-like" followers of corporate rhetoric, they would need to start asking meaningful questions—for instance, "Is triple bottom-line reporting merely 'smoke-and-mirrors'?" To be able to get rid of implicit nihilism, the critical and analytical capacities of a broad array of stakeholders may need to be developed.

—Mollie Painter-Morland

See also Enron Corporation; Ethical Nihilism; Meaningful Work; Relativism, Cultural; Relativism, Moral; Trust; Work Ethic

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Nike, Inc.

Nike, Inc. is a high-profile sporting goods and apparel company that engages in the design, development, and marketing of footwear, equipment, and accessory products worldwide under brand names such as NIKE, Cole Haan, Converse, Starter, Hurley, and Bauer. The company, which is headquartered in Beaverton, Oregon, sells its products through a mix of independent distributors, licensees, and subsidiaries in approximately 120 countries worldwide. Nike has experienced substantial financial and marketing success since its founding in the 1960s and is now the largest sporting goods company in the world (in terms of market capitalization). Despite its success, the company has been the target of much criticism in recent years for alleged abusive or "sweatshop" labor practices in its subcontractors.

Nike was founded as an athletic shoe company by Phil Knight and Bill Bowerman in 1962 under the name Blue Ribbon Sports. In 1972, the company changed its name to Nike, after the Greek goddess of victory. Knight had been a track athlete and business student at the University of Oregon, where Bowerman was his coach. While getting his MBA at Stanford, Knight devised a strategy for the manufacturing of athletic shoes overseas that would take advantage of lower-cost off-shore production capabilities. The plan was for Nike to be essentially a design, marketing, and distribution company with all the production performed by subcontractors operating overseas.

This strategy proved highly successful. Nike started subcontracting in Japan and then moved its sourcing operations to South Korea and Taiwan to take advantage of lower cost of production in these locations. As the economies of South Korea and Taiwan developed, Nike continued to move its sourcing operations to even cheaper locations such as China, Indonesia, and Vietnam.

In the fiscal year 2005, Nike had revenues of $13.7 billion and employed about 24,000 people directly and another 650,000 in more than 800 supplier factories worldwide. The company has operations in several locations including Oregon, Tennessee, North Carolina, and the Netherlands in addition to its Niketown and Nike Factory Store retail outlets. It has several subsidiaries: Cole Haan (casual luxury footwear and accessories), Bauer Nike Hockey (hockey equipment), Hurley International (teen-oriented sports apparel for surfing, skateboarding, and snowboarding), Converse (athletic footwear), Nike IHM, Inc. (cushioning components used in Nike footwear), and Exeter Brands Group, which includes Starter and licenses other Nike brands. Nike became a publicly traded company in 1980, and its New York Stock Exchange ticker symbol is NKE.

One of the key components of Nike's strategy has been the use of celebrity athletes as endorsers for its products. Its endorsers have included some of the biggest names in sports such as Michael Jordan (after whom the famed "Air Jordan" shoes were named), Lance Armstrong, Tiger Woods, Kobe Bryant, and Jerry Rice.

In the late 1980s, Nike found itself at the center of controversy brewing over alleged sweatshop labor working conditions in its subcontractor factories in developing countries. Critics alleged that a number of labor-oriented problems existed in these factories including (1) wage and salary concerns—both the payment of low wages and the use of various schemes to cheat workers out of the wages to which they were entitled, (2) unsafe/unhealthy working conditions, (3) excessive working hours and forced overtime, (4) harsh and abusive disciplinary tactics, (5) the use of child labor, and (6) active opposition to unionization efforts by the workers. According to some critics, such as labor activist Jeff Ballinger, the opposition to unionization was the key concern because, it was reasoned, with effective union representation the other issues could be resolved.

Several incidents contributed to the notoriety Nike quickly acquired on these issues. There were several worker fatalities reported in Nike subcontractor factories in the early 1990s. In addition, reports started circulating of Nike's involvement with the use of child labor in its subcontractor factories. A picture purported to be of a child worker in a Nike subcontractor factory in Pakistan sewing soccer balls appeared in *Life* magazine in 1996. It was later learned that the photo was staged (soccer balls are sewn before they are inflated but the ball the child was holding had already been inflated). Nevertheless, Nike was perceived by the general public as a leading culprit in the exploitation of child labor. The company was lampooned in comic strips such as Doonesbury and by late night talk show hosts such as Jay Leno and David Letterman (e.g., one of the top 10 signs you are at a bad summer camp: you spend all day sewing swooshes on Nike sneakers). Critics also parodied Nike's "Just Do It" slogan by suggesting that Nike "Just Stop It."

There are several ironies related to Nike's strategy that contributed to the publicity this controversy received. The fact that Nike's shoes were high-prestige luxury items sold to well-to-do children (and sometimes not-so-well-to-do children) in the United States and other western countries contrasted sharply with working conditions being portrayed in the media and the perceived exploitation of child labor.

In addition, Jeff Ballinger, who had been working to organize Nike subcontractor factories in Indonesia in the late 1980s and early 1990s, was able to point out the disparity in the money Nike paid celebrity endorsers versus what workers were paid to make Nike shoes. In the August 1992 issue of *Harper's* magazine, Ballinger was quoted as saying that an Indonesian worker making Nike shoes in Java would have to work 44,492 years to make what Nike paid Michael Jordan in one year. This criticism was an example of how Ballinger and other critics were able to use Nike's celebrity endorsement strategy against the company. Although Ballinger would later concede that Nike was no worse than other firms in the industry, Nike's name became synonymous with the term *sweatshop labor* in the eyes of much of the general public.

Labor-affiliated critics of Nike's overall strategy and labor practices were concerned both with the loss of jobs to overseas production and what they referred to as a "race to the bottom." According to this line of argument, the exploitation of low-paid workers overseas in harsh working conditions put downward pressure on wages and working conditions of workers in the United States. Thus, it was both a matter of labor solidarity and self-interest that led union activists to criticize Nike's labor practices and to call for reforms.

The criticisms of Nike got traction on the nation's college campuses where chapters of Students Against Sweatshops began to form. Students and faculty involved began demanding to know who was making the college-branded gear (e.g., hats, sweatshirts, T-shirts) being sold in the college bookstores and under what conditions they were being made. About the same time, mid-1990s, a boycott of Nike products over sweatshop labor concerns began to pick up steam.

Both critics and supporters of Nike concede that Nike's problems were exacerbated by its initial response to the criticism. This was to disavow any responsibility for labor problems in its subcontractor facilities on the grounds that it did not make the shoes—they are made by its subcontractors. Nike subsequently enlisted former Atlanta Mayor and UN Representative Andrew Young to investigate its subcontractor factory operations in Vietnam. When a generally upbeat report was issued, Young was criticized for bias and sloppy research methods.

In November 1997, the *New York Times* stated that in an inspection report that was prepared for the company's internal use only, Ernst & Young wrote that workers at the factory near Ho Chi Minh City were exposed to carcinogens that exceeded local legal standards by 177 times in parts of the plant and that 77% percent of the employees suffered from respiratory problems. The article leaked several excerpts from this report that detailed the unsafe and unhealthy working conditions in Nike's factories.

While Nike was at the center of the controversy over alleged sweatshop labor practices, other firms and parties became embroiled in it as well. When morning talk show host Kathie Lee Gifford's line of clothing was criticized for being made with abusive labor practices, she investigated the allegations herself and confirmed some of the charges. Ms. Gifford then became an advocate for improving working conditions in the apparel industry.

As the criticism mounted regarding the use of sweatshop labor in the apparel and footwear industries, the federal government got involved. During the Clinton Administration, the White House convened a meeting of industry, labor, and activist representatives to address issues of sweatshop labor in the apparel industry. Originally called the Apparel Industry Partnership, this group came to be known as the Fair Labor Association whose purpose was to promote adherence to international labor standards and improve working conditions worldwide.

A turning point in Nike's response to critics was Phil Knight's appearance at the National Press Club in May 1988. In his speech, Knight conceded that Nike bore responsibility for conditions in its subcontractors' factories and that many of the critics' complaints about those factories were valid. Furthermore, he pledged to reform Nike's labor practices with respect to child labor, worker development, and safe working conditions. More specifically, Knight promised to raise the minimum age of all sneaker workers to 18 and apparel workers to 16, adopt clean air standards, advance microloans to workers, and expand its monitoring program. Following this speech Nike undertook a number of institutional changes to carry out Knight's promises. Notably, Nike changed its response to this controversy from defensive to proactive and began to take the lead in efforts to reform working conditions in poor countries. In addition, Nike has become more proactive in addressing criticisms of the company. Nike representatives have participated in forums at professional associations such as the Academy of Management and the International Association of Business and Society. Nike has also welcomed researchers into its factories and it has hosted college study abroad groups visiting countries in which its subcontractors operate. How much of this response was due to a sincere belief that the company had acted wrongly in the treatment of its subcontractor workers and how much was due to business expediency to silence the critics is uncertain.

Nike is one of the first companies to publicly publish a list of its active subcontractors/suppliers in an effort to establish transparency and also to gain efficiency for monitoring and inspections by collaborating with other companies who use the same subcontractors. As of May 2005, Nike is also recognized by four institutions that gauge according to their own specific criteria whether a company should be considered a socially responsible investment. These are *FTSE4 Good Index Series*, *Dow Jones Sustainability Index, Ethibel Investment Register*, and *KLD Broad Market Social*^SM^ *Index*.

Furthermore, Nike has also published a 113-page Corporate Responsibility Report FY 04 freely available on its Web site. While the company painstakingly details its efforts at engaging its five most important stakeholders, namely consumers, shareholders, business partners, employees, and the community, it recognizes that for the future they need to focus on the following priority issues with respect to workers and factories: freedom of association; harassment, abuse, and grievance procedures; payment of wages; hours of work; environment; and safety and health. The report notes that its biggest challenge is in China, which accounts for 180,000 contract workers in more than 110 factories. China accounts for 36% of its manufactured footwear and has a large and fast-growing domestic market for Nike goods. However, upholding its code of conduct in China is a difficult problem for Nike due to local laws that prevent independent labor organizing. Several other problems exist, such as the lack of clarity about the law and its monitoring, falsification of information related to wages by factories, and social problems caused by temporary migration of workers from rural China to manufacturing provinces. Nike believes that engagement with its stakeholders, including the Chinese government, and building partnerships in China is the long-term solution to improving labor conditions there.

Because Nike has been so closely tied to the sweatshop labor controversy, the underlying debate about the ethics of sweatshop labor is particularly relevant to the Nike case. Many critics have argued that companies like Nike have a responsibility to see to it that their subcontractors provide better than market-derived or legally mandated wages and working conditions in their operations in developing countries. Others though have argued that if such companies were to do so, there would be less incentive to invest in these developing countries and the benefits of economic growth would be forfeited.

As of this writing, critics and supporters of Nike are still very far apart on the quality of working conditions and the extent of labor abuses in Nike subcontractor factories. However, there does seem to be fairly widespread agreement that the criticisms leveled against the company have brought about an improvement in these conditions since the controversy started.

—Richard E. Wokutch and Manisha Singal

See also Developing World; Fair Labor Association (FLA); Global Codes of Conduct; Living Wage; Sweatshops; Worker Rights Consortium (WRC); Working Conditions

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NIMBY (Not in My Backyard) Phenomenon

NIMBY is an acronym for Not In My Back Yard. It has two distinct usages and categories of users. First, it connotes the selfish unwillingness of individuals to accept the construction by corporations of large-scale projects nearby, which might affect their quality of life and their properties' value. Project proponents, usually consisting of the sponsoring corporation, construction labor unions and contractors, and the like, use the term in this way. Second, it implies a lack of social conscience and a class, race, or disability-based opposition to the location of social service facilities in neighborhoods. Social service and environmental justice advocates use the term in this sense.

The phrase seems to have appeared first in the mid-1970s. It was used in the context of the last major effort by electric utilities to construct nuclear-power-fired generating stations, especially those in Seabrook, New Hampshire, and Midland, Michigan.

NIMBY's negative connotation comes from the fact that those opposing high-impact projects on environmental grounds tend to be of middle-class or lower-class origins. It is therefore a wedge issue used by project proponents.

The phrase has a double edge, which makes it difficult to cope with for people so labeled. It implies that project opponents want poor people and poor neighborhoods to bear the burdens of toxic waste facilities or quarries. Also, it hints that opponents are willing to sacrifice the blue-collar jobs that construction and operation of the facility would, arguably, generate.

Some environmentalists have tried to turn NIMBY into a positive. They have argued that the very basis of environmental awareness rests on caring about what happens in a person's own locale. They have also pointed out the logical discrepancy of a corporation's playing on social class in order to win its project.

While undoubtedly true, the "NIMBY as positive" argument has had little traction because in the 1990s environmental justice advocates and other social justice campaigners generally adopted a negative usage of the term and reinforced the class-based implication of NIMBY. Now, it applies particularly to the location of group homes for people with developmental disabilities or to drug-treatment facilities.

—Peter D. Kinder

See also Accountability; Conflict of Interest; Social Costs; Tragedy of the Commons

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Noncognitivism

Noncognitivists maintain that moral judgments are more appropriately viewed as *expressions* of attitudes, preferences, or desires rather than propositional claims about factual states of affairs. They typically subscribe to two related notions: First, moral statements are linguistically incapable of being true or false, and second, psychologically speaking, moral judgments are not reports of belief but indicators of other affective states of mind. Noncognitivism in ethics, thus, is a metaethical thesis regarding the truth aptness of moral judgments.

There are three principal forms of noncognitivism. *Emotivism* is the noncognitivist view that holds that moral utterances about good, bad, right, wrong, virtue, and vice (along with judgments concerning so-called thick moral concepts like justice, bravery, and beneficence) are emotional expressions of supportive or negative attitudes toward actions and individuals. So, for example, the moral judgment that "Charles was wrong to deceive her like that" is simply a complex speech act that expresses a brute attitude against Charles's deceptive act, much like "Charles's act of deception: terrible!" Even though moral judgments take the form of statements or assertions in many cases, *prescriptivism* maintains that judgments are actually imperatives: judgments like it is "dishonorable to deceive someone" amount to "do not deceive." More contemporary versions of *norm expressivism* begin from the premise that general norms or principles are, at bottom, expressions of some attitude toward an action or individual; however, norm expressivists also recognize how such attitudes can form the basis of a system of derived beliefs that are subject to the rational standards of semantic consistency.

There are at least two noteworthy philosophical motivations behind noncognitivism. The first centers on the nature of moral facts (if there are to be any) and the second concerns the underlying motivational force of moral judgments.

If moral statements are genuinely cognitive, that is, capable of reporting beliefs that are true or false, then there are presumably factual states that such statements identify and describe. Noncognitivists find this hard to accept, however, because such factual states would either have to be (1) naturally occurring states composed of moral properties or (2) nonnatural states or properties that are wholly different from anything in the natural world. Both these options lead to unacceptable conclusions for the noncognitivist. Option 1 is implausible for a reason famously identified by G. E. Moore in his open question argument. His argument was designed to show that for any naturalistic account of moral claims, someone can always intelligibly ask *why* the identified natural state of affairs has the moral characteristic identified with it. For instance, suppose that someone asserts that honesty is morally good because it produces greater states of happiness. Such a naturalist would find the question "Is happiness good?" unintelligible because he or she has already implicitly reduced the meaning of goodness to states of happiness. Moore believed, however, that such a question is quite intelligible and therefore demonstrates how moral appraisals cannot be reduced to the description of natural states of affairs. On the other hand, option 2 does not fare any better for many noncognitivists. To say that there are some nonnatural, intrinsically normative states that our ethical statements describe calls forth a deep skepticism about the existence of such metaphysically queer facts, especially when it is not clear how humans would come to know such facts.

Another motivation for noncognitivism stems from a prevailing view in moral psychology, often referred to as *internalism.* Internalism asserts that moral judgments necessarily give rise to the motivation to act in accord with the judgment. Cognitivists thus face a related difficulty; for if moral judgments are necessarily connected to motivational states of mind, it does not seem promising to reduce such judgments to beliefs about what is true or false. Factual beliefs are thought to be motivationally inert and incapable of motivating action. Thus, noncognitivists find it more plausible to characterize moral judgments as deeply connected to the expression of some affective state and, hence, are able to provide a coherent psychological explanation for why we are motivated to act in ways consistent with our moral convictions.

The implications of noncognitivism are subtle but nonetheless significant. Rejecting the truth aptness of moral claims implies that the supposed universality and objectivity of some claims, for example, those related to fundamental human rights, no longer have the validity that they are sometimes assumed to have. This worry holds equally well for the norms that govern the conduct of managers within business. There is a strong interest on the part of many observers of business to ground the validity of norms regarding fraud, honesty, and fairness in the objective nature of claims expressing those values. In response to this concern, noncognitivists have countered that the normative force of moral claims results from shared human attitudes and practices, independent of their ability to be true or false. Moreover, some noncognitivists, such as Simon Blackburn, are careful to note that while moral claims may not be literally true, the rich set of social commitments that form the basis of morality provide enough space for dialogue, criticism, and refinement of existing norms, thereby salvaging the objective "feel" of certain basic moral claims.

—*Jeffery Smith*

See also Cognitivism and Ethics; Metaethics; Moral Realism; Naturalistic Fallacy

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Nongovernmental Organizations (NGOs)

Nongovernmental organizations (NGOs) are nonprofit organizations that either deliver public services or advocate public policy, or both. Some observers also refer to them as civil society groups or third sector groups, as distinguished from the for-profit business sector and from government. They are also to be distinguished from intergovernmental organizations, such as the United Nations and the Organisation for Economic Co-operation and Development (OECD).

NGOs include a wide range of organizations—relief, humanitarian, development aid, and sustainable development—but the term more commonly refers to advocacy groups. The forerunner to the emergence of NGOs on the global scene was the rise of citizen groups and citizen activism within the United States. The proliferation of such groups occurred during the 1960s and 1970s and coincided with the rise of social regulation. The trend continues unabated in the new century and has given rise to global NGOs and international networks among citizen groups.

In the area of service delivery, there are domestic organizations that provide basic needs and social services, such as the Salvation Army, Goodwill Industries, and Habitat for Humanity. Some of these organizations provide services in the global arena as well, where they are joined by relief organizations such as the International Red Cross and Doctors Without Borders.

More central to this discussion are advocacy groups that promote change in corporate practices and public policy. These are the groups that have proliferated most rapidly over the past half century and that have promoted corporate responsibility and ethics concerns.

Before the strong wave of social regulation in the United States in the 1970s, the social movements of the 1960s transitioned into citizen groups in the following decade. What began as protest movements on civil rights, women's rights, consumer protection, and environmental protection in the 1960s transformed into more mainstream interest groups in the 1970s.

Political Tactics

The range of traditional political tactics used by citizen groups and NGOs has been broad and diverse and includes both traditional and nontraditional tactics.

Traditional Political Tactics

- Lobbying
- Campaign contributions
- Grassroots activism
- Issue advertising
- Litigation
- Research think tanks
- Ballot measures

Citizen groups hire political experts and experienced legislative staff from congressional offices to lobby legislators directly, a traditional function of Washington offices of all organizations. Along with labor unions and business, they also raise and channel campaign contributions to political candidates. The League of Conservation Voters, for instance, is the foremost political action committee of the environmental movement, while Emily's List has raised money for women congressional candidates.

NGOs have gone beyond direct lobbying to also organize grassroots campaigns to promote major public policy initiatives. They have done so by organizing their own members to write letters and contact legislators in key congressional districts while also reaching out to members of the general public who might be sympathetic to their cause. Such grassroots outreach campaigns often involve another tactic—that of issue advertising.

The 1970s also marked a time when NGOs began to make more sophisticated use of litigation and policy research. The Ford Foundation financed the development of a network of public interest law firms and legal foundations around the United States, which sponsored litigation in the areas of environmental rights, consumer rights, and civil rights. Also emerging around the same time were liberal think tanks, some of which were part of Ralph Nader's network, which produced policy research critical of corporations and of government policy.

NGOs also used the initiative process in several states to bypass legislatures and go directly to the people with ballot measures to promote their agenda. Such measures, since the 1970s, have included cigarette taxes, environmental and health disclosure standards for products, energy alternatives such as solar energy, and campaign finance reform.

Often, NGOs will be organized to use only one or two of the political tactics mentioned, such as the League of Conservation Voters on campaign contributions to candidates or the Center for Law and Social Policy to pursue litigation, or Consumers Union to provide consumer testing and research. More complex and sophisticated NGOs, meanwhile, might pursue a broader range of tactics and in essence be full-service political organizations. The Sierra Club is a good example. It engages in both direct and grassroots lobbying, produces policy research, and also sponsors litigation through the Sierra Club Legal Foundation. On a global scale, Greenpeace operates in a similar manner by lobbying, coalition building, and engaging in policy research. Meanwhile, it also pursues nontraditional and confrontational direct action campaigns against corporations, discussed in the next section.

Nontraditional Political Tactics

Beyond the range of traditional political tactics discussed, NGOs often use a range of nontraditional political tactics, as follows:

- Direct action
- Boycotts
- Shareholder activism and resolutions
- Cross-sector coalitions
- Corporate collaboration

While most of the traditional tactics are designed to influence corporations indirectly through public policy, the nontraditional tactics aim to influence corporations directly. NGOs often work with government, but they can also be cynical of their ability to force change through government policy. Hence, NGOs often advocate their positions by directly pressuring corporations. This may bring some interest groups back to their roots as social movements when they engaged in more confrontational tactics.

Protest marches and media events can bring enough adverse publicity to a corporation to cause embarrassment and possibly force change. The time-honored tactic of consumer boycotts can accomplish the same goal. The National Association for the Advancement of Colored People sponsored boycotts during the civil rights era of the 1960s, and civil rights activist Jesse Jackson threatened such boycotts against specific companies like Nike and Coca-Cola in the 1990s. Through Operation PUSH and the Rainbow Coalition, he sought to bring pressure for corporate covenants to increase minority representation in senior management and on corporate boards and to increase economic participation with minority businesses. The Internet has also become a key organizing tool, especially in attracting protesters from around the world to meetings of the World Trade Organization. Shareholder resolutions, explained more fully in another section of this encyclopedia, are another nontraditional tactic that NGOs have used to bring pressure for change in corporate policies.

Building coalitions between NGOs has often been used as a way to multiply the strength of group pressure on any issue. Environmental groups often bring concerted efforts to bear in coalition lobbying campaigns, for example. What are becoming even more common are cross-sector coalitions, where NGOs with very different agendas and interests coordinate their efforts to target a corporation or an issue. Religious groups, consumer groups, and health groups, for instance, combined forces to boycott Nestlé for its aggressive marketing of infant formula in Third World countries. Religious groups and civil rights groups joined in protesting apartheid in South Africa in the 1970s.

Often, these coalitions evolve into global networks of NGOs. Religious groups, farm worker groups, health groups, consumer groups, and environmental groups all pooled their efforts to form an antipesticides coalition, since pesticides endanger the interests of all their constituencies. Such broad coalitions may both symbolize the importance of an issue and maximize the range of tactics available in any conflict as some groups may have policy or scientific expertise, while other groups may have large and dispersed memberships to bring pressure against a corporation or against governments in different regions or the world.

Finally, as NGOs mature and moderate, they are sometimes willing to dialogue and collaborate with their corporate adversaries, perhaps even in a structured and formalized manner. This has been particularly true of dialogues among environmental groups, corporations, and government on such sweeping issues as global warming. Through such collaborative efforts, different interests can discover common ground and avert further conflict, litigation, or regulation. The World Wildlife Fund, the Institute for Resource Management, and the Keystone Center for Science and Technology have all convened dialogue groups. While studies show their recommendations have not often been formulated as public policy, the communication and collaboration they foster build the foundation for future consensus.

Impact of NGOs

Change promoted by NGOs may be either positive or negative depending on the intended and unintended consequences. Some critics also maintain that the proliferation of groups and greater amount of participation in the public policy process create gridlock and paralysis in decision making. With too many interests to accommodate, legislatures may never arrive at a consensus, and that may be viewed as positive or negative as well, depending on one's perspective.

There are two other lesser known but important impacts of NGOs. First, as groups of different views and ideologies proliferate, one can observe a countercyclical political phenomenon. Success tends to breed failure, and vice versa. When one constellation of groups has won a major public policy victory or has elected its supporters to office, it tends to grow complacent and retrench. Meanwhile, its ideological opponents may feel threatened and work that much harder to regain lost ground, leading the political pendulum to swing back in their direction. Environmental groups, for instance, experienced large gains in memberships in the 1980s after President Reagan was elected, but they have won more policy victories with less work during Democratic administrations.

Second, as the numbers of NGOs grow within a particular policy sector, inevitably, splintering occurs, as within the environmental and health sectors. Disagreements arise among the groups on both tactics and policy positions. Typically, grassroots, localized groups take more extreme positions and use more militant tactics, while groups headquartered in national capitals are more prone to compromise and resort to more conventional and moderate political tactics. Such splintering poses both a strategic opportunity and threat to corporations. The splintering makes it more likely that a corporation may find at least some groups willing to negotiate and take a market-friendly approach, as with Environmental Defense or the National Wildlife Federation. Meanwhile, it is also inevitable that groups taking an extreme position will be more intractable and will remain steadfast opponents to business.

Global Aspects

Ironically, even though the United States gave rise to citizen activism and other countries followed suit, some European countries may have surpassed the United States on certain items in the activist agenda. Global NGOs have criticized globalization as corporatization of the world economy and have emphasized human rights and environmental sustainability over other issues such as consumerism. Other issues on the NGO agenda include conflict resolution, peace keeping and nation building, refugee resettlement, and a ban on land mines. Groups have also fought for the alleviation of poverty, hunger, and diseases such as AIDS and have combated violence against women and sexual slavery.

NGOs such as Transparency International have also demonstrated a real concern for governmental process issues, and the latter has led efforts to monitor and fight bribery and corruption. Amnesty International has campaigned for political freedom and rights globally, while Freedom House has tracked and promoted the spread of democracy. NGOs have also monitored the projects of multilateral institutions such as the World Bank to ensure it respects human rights and guards against corruption.

Beyond the networking that occurs among global NGOs, facilitated by the Internet, international organizations also provide important forums for the participation of NGOs in global policy making, at least in an advisory capacity. The UN Global Compact, for instance, has many NGOs as members and enjoys the support of major corporations as well.

Critique of NGOs

One of the early criticisms of American citizen groups—lack of accountability—is also applicable to global NGOs. Studies of citizen groups going back to the 1970s found that most had no members at all, had been founded by social policy entrepreneurs, were staff dominated and undemocratic in their internal decision making, and were accountable primarily to wealthy donors and foundations. Even when they have members, NGOs do not take policy direction from them, and their staff are often insulated from their own board members in setting the agenda of the organization. Critics of NGOs see them as highly educated self-appointed elites that are closer to donors and governments than to the poor and powerless and also as too prone to compromise with economic and political elites.

Another criticism going back to the 1970s has also been applied to NGOs today: that they are really anticapitalist and antigrowth. Many international economists and advocates of globalization especially take this view. Related to the accountability problem, critics of NGOs also see them as controlled by Western nations, especially the United States; as having a pro-Western bias; and as self-appointed guardians of Third World nations and of indigenous peoples and tribes, to whom they are not accountable. Others, meanwhile, point to growth of NGOs based in Third World countries and the linkages developed with Western NGOs as indications that NGOs are becoming more mature and broadly based.

Values and NGOs

While NGOs in the United States run the gamut from liberal and communitarian groups to libertarian and conservative groups, most of the global NGOs focus on human rights and sustainability and adhere to values of social justice, equality, and communitarian values. Since most corporations are more concerned with liberty and efficiency, and find fewer allies with those values among NGOs on the global scene, relating to global NGOs is a larger challenge for corporations than relating to domestic NGOs and citizen groups. The culture clash that corporations experience in dealing with global NGOs, especially those in Europe, surpasses the distance they feel from the values of a more ideologically diverse array of groups in the United States. The NGO infrastructure in the United

States reflects its history of individual rights and freedom and of a plurality of interests, while NGOs in Europe and other areas of the world reflect a political culture more concerned about economic security and equality.

—John M. Holcomb

See also American Civil Liberties Union (ACLU); Association of Community Organizations for Reform Now (ACORN); Boycotts; Cato Institute; Coalition for Environmentally Responsible Economies (CERES); Consumer Federation of America; Council on Foreign Relations; Interest Groups; Nonprofit Organizations; People for the Ethical Treatment of Animals (PETA); Shareholder Activism; Shareholder Resolutions; Stakeholder Theory; Transparency International; World Resources Institute (WRI)

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Nonprofit Organizations

What do the following organizations have in common—the Ford Foundation, the Carnegie Endowment for International Peace, National Organization for Women, U.S. Chamber of Commerce, American Red Cross, and the YMCA? They are all nonprofit organizations. Nonprofit organizations may be generally defined as tax-exempt organizations created for the purpose of serving the public interest. The public interest may be reflected in categories such as charitable, educational, scientific, literary, or religious.

Nonprofit Sector

Nonprofit organizations, taken collectively, are referred to as part of the nonprofit sector. This is a general name given to the institutions and organizations in society that are not businesses or governments. The nonprofit sector is sometimes referred to by other names, such as the not-for-profit sector, the independent sector, the third sector, the philanthropic sector, or the voluntary sector. Nonprofits are typically referred to as nongovernmental organizations (NGOs) outside the United States. It has been estimated that the nonprofit sector in the United States represents about 6% of all organizations and that roughly 1 in every 15 U.S. citizens is employed in a nonprofit organization. It has been estimated that more than a million nonprofit organizations spend in excess of $500 billion each year. In short, nonprofit organizations are pervasive and touch each of us every day. Collectively, the nonprofit sector composed of these nonprofit organizations represents a significant segment of society that affects the total citizenry. All estimates seem to indicate that the nonprofit sector is growing in size.

What Is a Nonprofit Organization?

As their name implies, the primary characteristic of nonprofit organizations is that they cannot pay profits to owners. Nonprofit organizations have no owners in the traditional business sense. As compared to business organizations that can generate profits and distribute these profits to investors, owners, or shareholders, nonprofit organizations, frequently referred to simply as "nonprofits," cannot distribute any income that represents revenues in excess of costs. Nonprofits have stakeholders, not stockholders. These stakeholders include the clientele that benefit from their services or programs and the community, in general, that receive indirect benefits from their presence. This does not mean that nonprofits cannot make any profit. It simply means that whatever profit is made must be retained and reinvested into the organization's budget and programs.

Most nonprofit organizations are created for the purpose of providing some public benefit or service. Having a public service purpose or mission is a key identifying characteristic of nonprofit organizations as they are generally thought of in society today. They are created by interested parties for the purpose of serving society, generally, or particular issues, topics, or clientele groups, specifically.

Nonprofit organizations are private, in the sense that they are not a part of government. They are typically incorporated as legal entities, and they are self-governed by their boards of directors, who are usually volunteers committed to the nonprofit's mission. In terms of daily operations, depending on their size and budget, they could be composed of all nonpaid volunteers or could have paid staff, including paid executives and managers. Frequently, most nonprofits have at least a small core of employees who are paid but accomplish much of their work with volunteers.

Many nonprofit organizations receive their funds from private contributions. However, many other nonprofits generate revenue by charging fees for their services, earning interest on their investments, or producing and selling goods and services. In short, there are many different varieties of nonprofits and they are funded in a variety of ways.

When people think about nonprofit organizations, they often think they are all tax-exempt. Many nonprofits do organize in such a way that they can receive tax-exempt status by the Internal Revenue Service (IRS) and state tax agencies, but not all of them are tax-exempt. Those most frequently known for receiving tax-exempt status are known as 501(c)(3) organizations. Many nonprofits organize in this way because they depend on private funding and contributions, and they want to organize in such a way that donors may receive tax deductions for their contributions.

Thomas Wolf has asserted that there are five distinguishing characteristics of nonprofit organizations: They must have a public service mission; they must be organized as a not-for-profit or charitable corporation; their governance structure must preclude self-interest and private financial gain; they must be exempt from paying federal taxes; and they must possess special legal status that permits gifts made to them to be tax deductible. These characteristics do describe most nonprofit organizations, but there may be some exceptions to these characteristics.

Different Types of Nonprofit Organizations

There are a number of different types of nonprofit organizations. Section 501(c) of the tax code details the types of organizations that are permitted to have tax-exempt status. The tax code distinguishes more than 25 different classifications of nonprofit organizations. BoardSource, a nonprofit association, formerly known as the National Center for Nonprofit Boards, summarizes that there are four major categories of nonprofit organizations: charities, foundations, social welfare organizations, and professional and trade associations. These four categories help us appreciate the different types of nonprofit organizations existing today.

Charities

Most of the nonprofit organizations in the United States are classified as public charities. Examples include organizations that provide, without charge, care and services to the needy, hospitals, museums, and public television and radio. At a local community level, there are many charities that provide such services. Homeless shelters and food banks would be local examples. At the state and national level, there are charities that operate more broadly. Most of these charitable organizations have 501(c)(3) or some other type of tax-exempt status. A distinguishing feature of a public charity is that it is able to demonstrate broad public support as compared to funding from one source.

Foundations

Foundations are also 501(c)(3) tax-exempt nonprofit organizations. A foundation is a charitable institution, often constituting a permanent fund or endowment that is founded or created by individuals, families, businesses, or communities as a vehicle through which they support causes and programs that benefit society. Foundations are generally thought to be more complex than simple charities, and they are regulated more closely by government and have more strict reporting requirements than other nonprofits.

There are different types of foundations. The most common types of foundations include those which are private, operating, or community based. A *private foundation* typically has a single source of funding from an individual, family, or business, and it uses income from its investments to give grants to nonprofit organizations.

Well-known examples of private foundations include the Kellogg Foundation, the Carnegie Corporation, and the Ford Foundation. Some companies set up their own foundations as vehicles through which they make contributions. The American Express Foundation and the Bill and Melinda Gates Foundation are examples. Many companies choose to create in-house giving programs rather than operating through a foundation.

An *operating foundation* is one that uses the majority of its resources to carry out its own programs rather than making grants to others. Local hospitals and colleges or universities are examples of operating foundations. *Community foundations* collect resources representing particular cities, regions, or geographical locales. They usually focus on quality-of-life issues in particular areas.

Social Welfare Organizations

Social welfare organizations represent another category of nonprofit organizations recognized by the IRS. Social welfare organizations may not be organized for profit and must be operated exclusively to promote social welfare. Examples of social welfare organizations include the National Rifle Association, the National Association for the Advancement of Colored People, and the National Organization of Women. Many social welfare organizations are tax-exempt through IRS section 501(c)4. Some social welfare organizations participate more in legislative advocacy, lobbying, or political campaign activities and are not afforded tax-exempt status.

Professional and Trade Associations

Professional and trade associations are nonprofit organizations representing the business or professional interests of specific groups. Examples include chambers of commerce, business leagues, and organizations that promote the professional interests of an industry (e.g., manufacturing) or a profession (e.g., licensed engineers). These organizations generally qualify for tax-exemption under Section 501(c)(6) of the tax code. Contributions to these organizations are not tax deductible but membership dues may be deductible by the members as a business expense.

Causes Represented by Nonprofits

There are a number of different allowable purposes for nonprofit organizations according to the IRS tax code. A listing of them provides a useful overview of the different purposes for which nonprofits are created.

Arts, Culture, and Humanities

Examples of these nonprofits would include museums, concert halls, art, history, and genealogy appreciation, halls of fame, historic preservation, and organizations of writers, artists, and performers.

Education

Examples here would illustrate the broad range of formally constituted educational organizations. This would include both public and private schools and colleges and libraries, continuing education centers, literacy programs, and so on.

Health

Health-related causes embrace a wide range of different nonprofits. Examples include nonprofits related to hospitals, blood banks, outpatient clinics, mental health facilities, and medical research.

Human Services

Human services are more broad based than health-related nonprofits. Included here would be nonprofits related to protecting the public from crime, services for prisoners, job development and training, services for the unemployed, food services, children and youth services, homeless shelters, and services for senior citizens.

Others

Other causes or purposes for nonprofits might include religious-based organizations, environmentally focused organizations, and those related to animal welfare.

Three Stages of Nonprofits: Starting, Governing, Managing

There are three major stages in creating and managing nonprofit organizations that represent different levels of activities regarding their operations: (1) starting a nonprofit, (2) governing a nonprofit, and (3) managing a nonprofit.

Starting a Nonprofit Organization

Individuals and/or groups start nonprofit organizations because they believe the nonprofit status is the most appropriate way to organize their efforts toward providing a service to the public. To begin with, starting a nonprofit organization requires a statement of purpose answering the following questions: Why will this organization exist? What will it do? Although this process of stating organizational purpose may start with a few sentences or a brief paragraph, eventually it must be formulated into a mission statement. A *mission statement* is a statement of organizational purpose that serves as the guiding document in all that is done later. The mission statement should include the nonprofit's general purpose, a statement of the primary benefits and services provided to clients, groups of clients who will benefit from the services, and values that may guide the nonprofit organization. Whole books and numerous articles have been written on mission statements and their purposes, so we will not discuss this crucial step further.

At about the same time as the drafting of a mission statement, a *board of directors* needs to be recruited and formed. If there are plans to incorporate in a particular state, the founders should refer to state law as to how many board members are necessary to meet state requirements. Typically, the board members of a newly forming nonprofit organization will be individuals who have a passion for the cause or purpose of the nonprofit. The board provides *governance* of the nonprofit, the second stage of the process being discussed in this section. The subject of governance will be discussed further under governing the nonprofit.

Assuming the nonprofit organization desires to operate formally, the next step in the process is the creation of a legal entity by filing *articles of incorporation* that might require a lawyer and the submission of an application to the IRS if *tax-exempt status* is desired. In addition, *bylaws* may be needed that outline how the board will operate and how the staff will be configured. Depending on the proposed size of the nonprofit, a lawyer, banker, and accountant may need to be retained. Once federal tax-exempt status is achieved, other legal steps might include filing for state tax-exemption, property tax–exemption from the city, getting a solicitation license to solicit funds, and a mail permit for bulk mailings. Once employees are hired, insurance and other implications must be addressed.

Many Web pages dedicated to the forming of nonprofit organizations are available. The above steps generally outline what is involved in starting the nonprofit.

Governing a Nonprofit Organization

After a nonprofit has been started and a board of directors has been formed, the process of governance of the nonprofit becomes a central issue. In strategic management terms, governance refers to the overall exercise of authority provided by the board of the organization. It involves the creation and administration of policies and affairs of the nonprofit. The governing board becomes the strategic leaders who provide direction and vision for the nonprofit. The board has responsibility for refining the nonprofit's mission statement and for ensuring that the organization stays "on mission" in a responsible way.

There are a number of different lists that could be developed describing the steps involved in governing a nonprofit organization. BoardSource, formerly the National Center for Nonprofit Boards, a nonprofit organization that is in the business of providing educational materials for nonprofits, summarizes what it considers to be the "Ten Basic Responsibilities of Nonprofit Boards." The governance responsibilities of the board may be subsumed under these 10 items:

1. Determine the organization's mission and purpose.
2. Select the chief executive.
3. Support the chief executive and review his or her performance.
4. Ensure effective organizational planning.
5. Ensure adequate resources.
6. Manage resources effectively.
7. Determine and monitor the organization's programs and services.
8. Enhance the organization's public image.
9. Serve as a court of appeal.
10. Assess its (the board's) own performance.

While each of these 10 responsibilities define what boards do in the process of governance, BoardSource takes governance more seriously by suggesting a dozen governance principles that help to make boards exceptional performers. Many of these principles overlap with the 10 responsibilities named. Each of these 12 principles is worthy of summary.

1. *Constructive partnership:* Boards must form constructive partnerships with the chief executive of the nonprofit. Their two roles are interdependent.

2. *Mission driven:* Boards must effectively decide on and sustain mission, vision, and core values.
3. *Strategic thinking:* Operational and daily activities must be aligned with strategic goals and objectives to ensure maximum effectiveness. Boards must constantly think strategically to make sure this happens.
4. *Culture of inquiry:* Sound decision making requires that boards implement a culture of inquiry so that all points of view are heard and considered in the governance process.
5. *Independent-mindedness:* Boards must ensure that their members place the interests of the organization above personal interests. Part of this requires careful conflict-of-interest policies. Another part of this is for board members to express their legitimate concerns independent of the views of or loyalty toward the chief executive.
6. *Ethos of transparency:* Boards must ensure that all stakeholders and the public have access to information about the nonprofit's operations, finances, and policies.
7. *Compliance with integrity:* The promotion of strong ethical values and practices is an obligation of exceptional boards.
8. *Sustaining resources:* Exceptional boards will make sure that resources are available to support missions, goals, programs, and services.
9. *Result oriented:* Boards have a responsibility to measure and evaluate the nonprofit's results. These results may be expressed in terms of effectiveness, efficiency, and impacts. Other legitimate results relate to timeliness and costs.
10. *Intentional board practices:* Effective governance does not accidentally happen. Boards must intentionally put in place practices, policies, and structures that ensure optimization.
11. *Continuous learning:* Effective boards evaluate their own activities and performance to ensure that they are learning from past experience and integrating these lessons into future plans.
12. *Revitalization:* Effective boards revitalize themselves through continuous improvements involving planned turnover, careful recruitment, and inclusiveness.

In summary, board governance is the most comprehensive level of attention that may be given to providing direction for nonprofit organizations. Many of these same responsibilities will need to be carried out at the management stage, but they originate with careful boards of directors. Their focus is on achieving exceptional levels of performance.

Managing the Nonprofit Organization

The third stage in implementing nonprofit organizations entails their actual management. Management, of course, is a broad term that encompasses to some extent the previous stages discussed. In fact, according to the "constructive partnership" principle mentioned above, a close working relationship must be established and maintained between the board and the management group of the nonprofit. Indeed, a number of the activities required to run a successful nonprofit will require effective action at both the board and the management level. Two key examples where collaboration will be required include planning, especially strategic planning, and fund raising.

Depending on the size and funding of the nonprofit, the management group of the nonprofit organization may be many or few, paid or unpaid. A large nonprofit might have management and staff paid comparably to for-profit organizations. They might also have several layers of management. Examples of this type of nonprofit might include the American Red Cross or Habitat for Humanity. Often, these large nonprofits have offices located at state and local levels. In contrast, many nonprofits are medium or small in size, and their managers and staff receive modest compensation. Many of them have management groups and staff that are unpaid volunteers.

Without going into details, important management aspects of nonprofits involve getting the work done with paid staff and volunteers. Key management responsibilities in nonprofits include working with volunteers, creating programs and budgets, and fund raising. Management responsibilities embrace planning, organizing, motivating, and controlling—the same that are relevant in for-profit organizations.

One aspect of managing nonprofits that is different for for-profit organizations is the use of volunteers in getting much of the nonprofit's work done. Nonprofit boards and management groups must attract, motivate, retain, and replace volunteers.

It has frequently been observed that working with volunteers is the lifeblood of nonprofit organizations. Working with volunteers requires the board and management to undertake ventures such as understanding why people volunteer, determining the nonprofit's needs for volunteers, and designing a volunteer program. A volunteer program involves finding, recruiting, motivating, scheduling, and training of volunteers. Quite frequently, the volunteers work in the form of committees, so logical and coherent committee structures must also be put in place.

Dealing with volunteers typically brings the board and the management group into a close working relationship. Board members, themselves, are typically volunteers, and they play key roles both in terms of their own volunteerism and the management of other volunteers. To illustrate all the kinds of activities that are involved in working with volunteers, M. A. Hager and Jeffrey Brudney have identified a list of practices that they have used to gather information from nonprofits about their volunteers' activities. This list includes the following topics:

- Regular supervision and communication with volunteers
- Liability coverage or insurance protection for volunteers
- Regular collection of information on volunteer numbers and hours
- Screening procedures to identify suitable volunteers
- Written policies and job descriptions for volunteer involvement
- Recognition activities for volunteers
- Annual measurement of the impacts of volunteers
- Training and professional development opportunities for volunteers
- Training paid staff in working with volunteers

It should be apparent from this list of topics that working with volunteers is an awesome management and board responsibility that gets into many details regarding the volunteers and their activities.

Summary

There are so many nonprofit organizations in existence today that their presence is even referred to as the nonprofit sector of society or the economy. Nonprofit organizations are created for the purpose of providing some public benefit or service. Different types of nonprofits include charities, foundations, social welfare organizations, and professional and trade associations. The different causes for which nonprofits have been formed include (1) arts, culture, and humanities; (2) education; (3) health; (4) human services; and (5) other, which includes religious organizations, environmental organizations, and those related to animal welfare. There are three major stages in creating and managing nonprofit organizations that represent different levels of discussion regarding their operations: (1) starting a nonprofit, (2) governing a nonprofit, and (3) managing a nonprofit. Each of these stages embraces a wealth of information necessary for effective completion. Nonprofit organizations increase in number each year, and there is every belief that the nonprofit sector is growing in importance in society and in the economy.

—Archie B. Carroll

See also Nongovernmental Organizations (NGOs); Stakeholder Engagement; Strategic Philanthropy; Volunteerism

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Normative/Descriptive Distinction

The categories of "the normative" and "the descriptive" correspond to moral and factual statements, respectively. In the first case, normative assertions about values and "what should be" are traditionally investigated as the subject matter of moral philosophy. In the second case, propositions about facts or "what is" are typically examined in the descriptive realm of the natural and social sciences.

The methodological issues raised by the distinction are long standing. Notably, Hume's characterization of the difference between *ought* and *is* prompted the question of whether normative statements can be derived from factual descriptions. Moore addressed this question by asserting that defining *good* in terms of natural objects commits the naturalistic fallacy. On the other hand, social scientists have long expressed uneasiness about collapsing normative and descriptive categories, fearing that doing so would render facts too arbitrary and relativistic for objective analysis.

The partitioning of the normative and the descriptive in business research is also due to the influence of conventional economics, which, in the tradition of social science, tends to relegate normative considerations to the arena of ethics while limiting positivistic economics to factual, testable hypotheses. This separation prompts different approaches to the same subject matter. Consider poverty, for example. An ethicist would likely consider the rights claims of the poor, possibly as a justification for ameliorating disparities of income and wealth. In comparison, a positivistic economist would tend to focus on describing or documenting various indicators of poverty and wealth. When the distinction between the normative and the descriptive is followed rigidly, the resulting tendency is to partition ethical inquiry couched in traditional notions of right and wrong from the factual analysis of social issues.

Despite the influence of conventional economics, the distinction between the normative and the descriptive is more often blurred than not in business and society research, due to the cross-fertilization of ethics and social science in the field. For instance, it is common for business and society scholars to document both the facts and moral dimensions of issues such as consumer safety, employment conditions, business and community relations, and ecological sustainability. This coexistence of the normative and the descriptive results from a symbiotic relationship in which one approach informs the other in setting research agendas and influencing applications of research findings.

—Diane L. Swanson

See also Descriptive Ethics; Economics and Ethics; Ethical Naturalism; Fact-Value Distinction; Is-Ought Problem; Naturalistic Fallacy; Normative Ethics; Normative Theory Versus Positive Theory; Ought Implies Can; Positivism

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Normative Ethics

Normative ethics comprises the study of those actions that moral agents *ought* to perform. In emphasizing moral obligation, normative ethics is distinguished from more descriptive ethical theories that view ethics primarily as illuminating the way in which moral agents actually do act. While normative ethics may use the tools of descriptive ethics, it seeks to articulate a set of standards that are binding on all moral agents.

Normative ethical theories are commonly divided into three broad categories described as "deontological," "teleological," and "ethological." However, useful as this typology may be, in practice, moral action may make use of elements of all three.

Deontological Ethical Theories

The term *deontology* comes from the Greek word *deon* or duty. Deontological theories are primarily based on appeals to duty or some kind of unconditional obligation on the part of the moral agent. Different theories offer a variety of possible sources for this obligation. For some, it is rooted in the will of God or some other divine mandate, while for others it is rooted in the dictates of nature or reason.

Divine command theories of morality are common in theistic religious traditions, which assert some form of a personal God or gods. According to these theories, the nature of morality is prescribed by what God or the gods will to be done. Something is thus good if it accords with God's will and evil if it contradicts God's will. This idea was given a classic treatment in Plato's *Euthyphro,* where he seeks to demonstrate that the Good must be something independent of the will of God. However, this tradition has persisted and been given particularly vigorous defense in the reformed tradition of Christianity—for example, in the work of John Calvin and Karl Barth. Versions of divine command theories can be found in Judaism and Islam as well.

Kantian ethics, in contrast, seeks to root moral principles not in the external authority of a divine being, but in the autonomous exercise of human reason. Kant's theory is encapsulated in his Categorical Imperative. The first version of this theory states that one should always act in a way in which one thinks people should always act. By rooting his theory in the moral and logical consistency of the individual human will, Kant seeks an unassailable foundation from which to provide moral guidance. If the human will can consistently will a moral principle as universally binding, then it can be trusted to be a reliable principle for action.

Kant's second formulation of the Categorical Imperative puts its emphasis not on the universal validity of human reason but on the inviolability of the human person. The third formulation puts its emphasis on the autonomy of the human reason as a *legislating* will, calling on moral agents to act as autonomous legislators in a universal kingdom of ends.

The force of these three formulations, as Kant proposes them, is to offer a comprehensive conception of the nature of morality as rooted in human freedom and reason. Yet he believes that the moral law arrived at in this fashion is universally binding since all rational beings are capable of reaching the same conclusions. However, Kant's moral stringency is such that he does not allow for the possibility of contradictions among different moral principles. On the contrary, he believes that all duties are equally binding on moral agents and none can override another.

Other philosophers have sought to overcome some of the difficulties that Kant's inflexibility on this issue has produced. W. D. Ross offers perhaps one of the best examples in his theory of prima facie moral duties. Ross argues that there are moral duties that are properly described as "basic," in the sense that they cannot be reduced to other, prior duties. This includes, but is not limited to, duties such as fidelity, beneficence, nonmalificence, gratitude, and justice. Ross acknowledges that conflicts among these duties may exist and argues that it is only through a careful examination of the situation in question that one can arrive at a conditional determination of what one's "duty proper" must be in a given situation.

Another approach, which is more akin to Kant's second formulation of the Categorical Imperative, involves appeals to the idea of individual rights as constitutive of one's moral obligations. Of particular concern for business ethics is Robert Nozick's "Theory of Entitlement," which posits a natural right to the possession of certain entitlements of which one may not be deprived without one's consent. John Rawls, alternatively, offers a rights-based theory rooted in the idea of justice as fairness. This theory differs from Nozick's in a number of key respects, but most notably in that it offers a vigorous defense of a theory, rejected by Nozick, of distributive justice.

Deontological moral systems are appealing from a normative standpoint due to their clarity with regard to the nature of moral action and the source of moral authority. Most deontological moral theories are nonconsequentialist in the sense that one's duty is considered to be binding regardless of the results. This is easiest to understand in those cases where the consequences fall directly on the moral agent (e.g., if one accepts jail rather than lie or betray a confidence). Obedience to duty in such cases is seen to be a higher obligation than personal advantage. Such approaches become more problematic, however, when the consequences fall not on oneself but on others (e.g., letting an innocent person be harmed rather than lie or betray a confidence).

Deontological theories are often criticized precisely for being universal in those circumstances where they should allow for contingency. It's not immediately obvious that obedience to duty is of a higher moral value than protecting innocent life or preventing other negative consequences.

Teleological Moral Theories

The major theoretical alternative to deontological ethics is found in teleological, or ends-based, moral theories. These theories find normative guidance in the pursuit of particular goals or outcomes, though they often differ with regard to the nature of the goals to be pursued.

Catholic moral theology is based on a teleological conception of the moral life. Although, due to its reliance on a theory of natural law it is often taken to be deontological, the natural law is itself teleologically oriented toward the fulfillment of particular human and divine ends. Unlike a divine command theory, in which the moral good is solely defined by the will of God (irrespective of other concerns), Catholic moral theology understands the good in terms of that which fulfills the purpose for which it was created. This perspective was given its classic formulation in the work of St. Thomas Aquinas. Human beings, in this theory, are created as creatures to fulfill certain ends; for example, within society, humans have the goal of bringing about justice. In sexual relationships, the goal is to create further life. The interference with the specified goals of human activity represents a disruption or perversion of their created purposes. The consequences of actions are important in this approach insofar as those consequences correspond to the desired ends of human life.

Consequentialism, on the other hand, analyzes the morality of action in terms of whether it harms or benefits morally relevant subjects. Various consequentialist moral theories exist, differing both in terms of what is considered to be harm or benefit and in terms of who constitutes a morally relevant subject.

In Jeremy Bentham's version of utilitarianism, he advocates what he calls the greatest happiness principle. Happiness in this case is defined strictly in terms of pleasure. Those actions that produce the greater pleasure are good and those that produce greater pain are harmful. Similar theories were developed by James Mill and John Stuart Mill. Bentham offers a number of criteria to enable one to evaluate whether any particular action would produce a greater net amount of pleasure over pain, such as whether one pleasure is more intense than another or whether it is likely to be followed by similar pleasure in the future. Using these criteria, he developed a "hedonic calculus" on which one could calculate the likely morality of a particular course of action.

Others have criticized this analysis by arguing that defining utility in terms of pleasure leads to morally undesirable conclusions. These thinkers have offered alternative theories of utility, some arguing that utility should be understood in terms of, for example, one's interests and some arguing that utility should be defined not in terms of what individuals believe to be good for them but according to external moral criteria of what actually can be shown to be good for them.

The other key question for consequentialist theories has to do with who or what constitutes a relevant moral subject—one to whom consideration is owed in determining one's actions. The two major alternatives within consequentialist theory are identified with utilitarianism and egoism, respectively.

Utilitarianism, as noted above, is based on some version of the greatest happiness principle, which states that what is moral is that which produces the greatest amount of net happiness (however defined). This is often described as seeking the greatest good for the greatest number. According to this theory, one's own happiness is not of greater value than anyone else's, and therefore, when calculating the morality of one's action, one should not weight one's own good higher than the good of others. Egoistic theories, on the other hand, argue that one's own interest is morally paramount in deciding what action to take. That which is good for oneself takes predominance over the good of others. Some egoists would argue that one's own good should be considered *primary* and the good of others *secondary,* while others would argue that we have no moral obligations to others and each individual is solely responsible for achieving one's own good. Note that this is a *normative* egoistic ethical theory. Some thinkers, for example Adam Smith, have argued *descriptively* that human beings by nature place their own interests above others, but they do not endorse this as an ethical good. Normative egoism argues that human beings *ought* to act in their own self-interest and, at their most radical, that taking the interests of others into account is immoral. This perspective was most prominently advocated in the 20th century by Ayn Rand, who, in both her novels and her philosophical treatises, defended the virtue of selfishness.

There are a number of attractive features to teleological ethical systems from a normative point of view, particularly its consequentialist forms. It seems to conform to our ordinary moral sensibilities that the consequences of our actions ought to matter. At the same time, certain interpretations of teleological ethics, particularly utilitarianism, seem to lead to conclusions that shock the moral conscience. For example, does the principle of the greatest good for the greatest number imply that we may sacrifice the good of a minority for the sake of the rest of the population? It is difficult to derive such an interpretation from John Stuart Mill, whose own writing emphasized individual liberty in addition to the greatest happiness principle. However, other utilitarians have been less circumspect. These problems are only magnified in egoistic theories. More generally, it is not always clear that there can be said to be a moral *telos,* whether God or Good, toward which human beings are oriented.

Act-Based and Rule-Based Ethical Systems

A further distinction to be made among these theories is between those that are "rule-based" and those that are "act-based." Rule-based moral systems claim that moral norms must be understood in terms of rules that, once determined, are morally binding, while act-based systems claim that morality must be understood in terms of whether particular acts in particular circumstances correspond to relevant norms.

Deontological and consequentialist moral systems each have act and rule variants. Rule deontology claims that one's moral duty corresponds to the articulation of universally mandatory rules. Act-based deontology, on the contrary, claims that one's duty can only be discerned in light of particular circumstances.

Rule utilitarianism interprets the greatest happiness principle to be that set of general principles under which the greatest good for the greatest number is generally attained. Rule utilitarianism, unlike Kantian ethics, is not absolutist and allows for exceptions. Act utilitarianism claims that moral agents must decide, on a case-by-case basis, whether their actions will bring about a greater amount of good over harm, and act accordingly.

Ethological Ethical Theories

Ethology is a term that applies to those moral theories that are rooted in an evaluation of the appropriateness of particular actions or sensibilities in light of contexts or circumstances. Most prominent among ethologically oriented moral systems is virtue ethics. Virtue ethics is based on the pursuit of human excellence through the cultivation of good moral character. Most theories of virtue identify the cardinal virtues as wisdom, temperance, fortitude or courage, and justice. Although not all descriptions of these virtues are ethologically oriented (e.g., Plato), in large measure they describe these virtues as the product of an education in circumstance-appropriate behavior. Thus, no one is born knowing how to act courageously. Rather, one learns bravery as a result of being exposed to circumstances that require bravery and, through practice, learning the proper response. Moral education is thus experiential and circumstantial.

The classic expression of virtue ethics is found in Aristotle's *Nicomachean Ethics.* In this work, Aristotle describes morality as doing the right thing, at the right time, in the right way. That which is ethical is that which is appropriate to the circumstance, but only the well-cultivated character can properly identify and react to the circumstances. Virtue in Aristotle's *Ethics* is identified as the mean between two extremes: one of excess and one of deficiency. Thus, courage is not fearlessness; rather it is the proper degree of fear depending on circumstances. Thus, the brave man is one who has neither an excess of fear, that is, cowardice, nor a deficit, that is, foolhardiness.

In contemporary moral theory, virtue ethics has seen resurgence, in large measure as a result of Alasdair MacIntyre's seminal work *After Virtue.* MacIntyre argues that modern normative ethical theory, as understood primarily through the tradition that culminates with Kantian ethics, on one hand, and utilitarianism, on the other, is intellectually bankrupt largely because it has lost track of its own origins. The logical end product of modern ethics is the moral nihilism of Friedrich Nietzsche. It is as though a catastrophe has taken place in which we now possess nothing but the fragments of moral knowledge out of which we must cobble together partial and incoherent moral systems. In contrast to this modern day moral confusion, the tradition of the virtues offers a complete and coherent theory.

According to MacIntyre's interpretation, a virtue is an excellence in a particular practice that is cultivated within a community that is based on a particular tradition. Thus, to be excellent means to be excellent in the context of a particular understanding of human nature. In MacIntyre's framework, in contrast to that of Kant or Mill, there are no moral principles that can be detached from the history of a particular community.

Another approach to contextually based normative ethics is existentialism, particularly as articulated by Jean-Paul Sartre. The key element of this approach to morality is its emphasis on human freedom. Sartre writes that man has no nature. Rather, we are born free and as free individuals must choose how we will respond to the world in which we are "thrown." There are no universal and binding moral norms on which human beings can rely for moral guidance. Neither the Categorical Imperative nor the greatest happiness principle can absolve individuals from the obligation to choose their actions and the resultant consequences. There is no god to whom one can appeal either for guidance or for forgiveness. One must, therefore, take the entire weight of one's actions solely on oneself. However, rather than seeing this as a morally hopeless situation in which all paths are equally meaningless and, therefore, all choices equally pointless, Sartre argues that in the *act of choosing* we create a morality and by that act lend meaning to our existence.

In some ways similar to this are various pragmatic approaches to ethics—for example, those advocated by Richard Rorty and Jeffrey Stout. Pragmatic theories of morality differ markedly from one another, but what they share in common with existentialism as well as with one another is their rejection of a *foundationalist* approach to ethical normativity. Morality is rooted in social convention rather than in either a metaphysical system or a calculus of pleasure and pain. It is because we have agreed to value certain things that they have been rendered valuable, not because they have intrinsic value themselves.

Conclusion

The attempt to develop a coherent philosophical basis for normative moral action has been a preoccupation of ethical theory since its inception, and yet the conversation continues. One's normative framework often says as much about one's own ethical outlook as it does about the nature of moral action itself. It is not clear that any one moral theory is solely capable of accounting for the complexity of moral action, and so it may be necessary to abandon the search for one complete normative theory and seek to develop a mixture of different theories, which perhaps would not offer anything by way of completeness but would nevertheless satisfy our need for moral guidance in the particular times and places at which we find ourselves in need of moral guidance.

This is not a rejection of the idea that there may be such things as binding deontological principles or genuine human ends, nor is it a rejection of the importance of considering consequences in evaluating morality. It is to say, however, that our apparatus effectively determining which of these has precedence over the others is severely limited. Such a melding of different theories may rely to some degree on intuition but must also be based on the careful examination of the strengths and weaknesses of the variety of theories available and a recognition of when they do, and do not, give us an adequate picture of what is right, what is good, and what is fitting.

—Scott R. Paeth

See also Absolutism, Ethical; Aristotle; Bentham, Jeremy; Consequentialist Ethical Systems; Deontological Ethical Systems; Descriptive Ethics; Dilemmas, Ethical; Divine Command Theory; Duty; Egoism; Entitlements; Ethical Nihilism; Ethics, Theories of; Existentialism; Fairness; Hedonism, Ethical; Intuitionism; Justice, Distributive; Justice, Theories of; Kant, Immanuel; Kantian Ethics; Mill, John Stuart; Moral Agency; Moral Education; Moral Rules; Nihilism; Noncognitivism; Normative/Descriptive Distinction; Nozick, Robert; Nozick's Theory of Justice; Rawls, John; Rawls's Theory of Justice; Self-Interest; Smith, Adam; Universalizability, Principle of; Utilitarianism; Utility; Utility, Principle of; Virtue; Virtue Ethics

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Normative Theory Versus Positive Theory

In general, a positive theory is a theory that attempts to explain how the world works in a value-free way, while a normative theory provides a value-based view about what the world ought to be like or how it ought to work; positive theories express what *is*, while normative theories express what *ought to be*. Each of the social sciences, but particularly economics, has advanced both positive theories and normative theories. In economics, positive theories attempt to explain how the economy actually operates and include, for example, the basic supply and demand models of microeconomics as well as the macroeconomic theories of Keynesian economics and the theory of comparative advantage of David Ricardo. Normative economic theories typically propose a goal at which economies should aim. For example, early welfare economists (e.g., Alfred Marshall and Arthur C. Pigou) proposed the goal of maximizing utility, while their followers (e.g., John R. Hicks and Znicholas Kaldor) were forced by the problem of interpersonal comparisons of utility to retreat to the less ambitious goal of Pareto efficiency. Political science has also advanced both positive and normative theories, as has jurisprudence, psychology, sociology, anthropology, and business ethics. In business ethics, for example, stakeholder theory has developed both as a normative theory (a theory of the stakeholders businesses ought to take into account) and as a positive theory (a theory of the consequences business face if they do not take stakeholders into account). Positive and normative theories are often linked, particularly in discussions of public policy. For example, in the model of the perfectly competitive market, a positive theory played a key role in discussions of how antitrust law could achieve the normative goals of welfare economics. More generally, positive theories are said to show us the means to the public policy ends that normative theorists advance. A key discussion has centered on the question of whether the distinction between positive theory and normative theory is viable, a question that is closely related to whether the fact-value or is-ought dichotomy is viable. Some have argued that the selection of the questions that a positivistic social scientist will investigate, the methods the scientist will use, and assumptions about what counts as appropriate evidence and adequate measurements are all based on the background cultural and social values of the scientist, and so theories resulting from the investigation will be value laden and thus normative. Others have claimed that because theories must be expressed in language and language is value laden, even putatively positive theories must be normative. John Searle has argued, for example, that institutional concepts are inherently both descriptive and normative. If this is true, then allegedly positive social science theories that make use of institutional concepts—such as "money," "legal," "economy," "government," "property," and "marriage"— must also be normative. Several feminist philosophers of science have argued that many so-called positive theories in the sciences turn out, on inspection, to derive from assumptions that are subtly, or not so subtly, based on gendered values.

—Manuel Velasquez

See also Fact-Value Distinction; Is-Ought Problem; Normative/Descriptive Distinction; Positive Economics; Stakeholder Theory

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Norris-LaGuardia Act of 1932

The Norris-LaGuardia Act of 1932 was the first "pro-union" U.S. labor legislation. Previously, the legislative climate had not produced any encouragement of employee unionism. Furthermore, the judiciary had exhibited a pronounced negative reaction to union activity. The act was clearly a turning point in U.S. policy development and was quite unusual to have been passed in a period of national economic depression, and with both a Republican president and Congress.

Nature of the Courts in the Early 20th Century

In retrospect, judges tended to come from the ranks of attorneys. Prior to being appointed or elected to judgeships, these attorneys often had served the needs of the business community. Critics have argued that many judges owed their new positions to the business community since only persons who owned property were allowed to vote during the pre–Norris Act era. Workers normally were not members of the propertied class. Both the business and the political loyalty of judges of that era have been questioned by critics.

The Injunction Process

When a union organizing effort began, the employer's attorney could contact a "friendly" judge and seek an "injunction" to stop the union action. No union official need be advised of the "ex parte" hearing. A "temporary restraining order" would require the union (officials) to "cease and desist" specified actions in the order. If the actions being restrained continued, the union officials could be immediately jailed. Judges had the power to take appropriate action to enforce their temporary restraining order. This effectively stopped the union activists and chilled workers from joining the union. Such temporary orders could later be made permanent after formal hearings.

Impact on Injunction Processes

Under Norris-LaGuardia, federal courts were prohibited from issuing such "ex parte" restraining orders or injunctions. There now had to be a formal hearing with both parties present. The burden was on the employer to show that public officers were unable or unwilling to furnish adequate protection for the employer's property. Furthermore, the employer must also show that no other remedy at law exists and that the dispute had not been settled through a "committed effort" in collective bargaining.

The "Yellow Dog" Contract

Another major component of the Norris-LaGuardia Act dealt with the so-called yellow dog contract. Employers often required employees and prospective employees to affirm in writing that they were not union members, and should they join a union while employed by said employer, the employer had the right to discharge the employee, without recourse. Even though it was obvious on the surface that the contracts were negotiated under duress, the Courts had enforced such contracts until the 1932 act made them unenforceable in federal courts. While they were unenforceable, employers continued using the "yellow-dog" contracts for several years since most employees were not aware of this fact and employers, in using them, led employees to believe in their legality.

The Norris-LaGuardia Act was soon to be joined by still more positive labor relations legislation as the Presidency and the Congress changed political parties the next year.

—Jerald F. Robinson

See also Labor Unions; National Industrial Recovery Act

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North American Free Trade Agreement (NAFTA)

NAFTA, the North American Free Trade Agreement, is a trilateral agreement between Canada, Mexico, and the United States in which the three nations pledge to reduce trade barriers against each other to improve international trade and comity. Celebrating its 10th anniversary on January 1, 2004, NAFTA is an example of regional economic integration combining three sovereign nations. Although Canada, Mexico, and the United States are arguably at different levels of economic development, they came together in an agreement to develop a multilateral North American trading bloc. The NAFTA Agreement had its genesis in an earlier bilateral free trade agreement between the United States and Canada, the U.S./Canada Free Trade Agreement (1989).

Origins of NAFTA

While Canada and the United States were forging the U.S./Canada Free Trade Agreement, the government of Mexican President Miguel de la Madrid Hurtado opened Mexico to the international trade community by joining the General Agreement on Tariffs and Trade (GATT) in 1986. On joining GATT, Mexico reduced its trade barriers and came into compliance with the prevailing international trade regulations of the time. Combining its GATT compelled openness with a program of economic reforms instituted by President Madrid's successor, Carlos Salinas de Gortari, Mexico became ready to join Canada and the United States in establishing a multilateral trade agreement. On August 12, 1992, Canada, Mexico, and the United States announced their intentions to create a free trade zone—the NAFTA. Stretching from the Arctic Circle to Mexico's borders with Guatemala and Belize, NAFTA would be the largest trilateral trade relationship in the world.

Objectives of NAFTA

NAFTA combined the United States with its largest (Canada) and third-largest (Mexico) trading partners. Trade between the three countries was well established prior to NAFTA due to the U.S./Canada Free Trade Agreement and a new openness in Mexico to international trade. Under Article 102 of the NAFTA Agreement, Canada, Mexico, and the United States agreed to the following macro objectives: The countries pledged to work cooperatively to "eliminate barriers to trade in, and facilitate the cross border movement of, goods and services between the territories of the Parties; promote conditions of fair competition in the free trade area; increase substantially investment opportunities in their territories; provide adequate and effective protection and enforcement of intellectual property rights in each Party's territory; create effective procedures for the implementation and application of this Agreement, and for its joint administration and the resolution of disputes; and establish a framework for further trilateral, regional and multilateral cooperation to expand and enhance the benefits of this Agreement."

Trade Liberalization Under NAFTA

NAFTA liberalized trade in a variety of ways. Tariffs were either eliminated immediately or phased out over periods of up to 15 years. Limits on investments were removed, and investors from any of the three countries were treated equally, currency was freely transferred at market rates, and performance requirements such as maintaining export levels and trade balancing were eliminated. Trade in services was liberalized and equal treatment was expected for service providers and professionals in each country. The countries pledged to facilitate the licensing of professionals and, by 1996, to eliminate citizenship and permanent residency requirements for professionals. Transportation regulations were liberalized so that by 2000 commercial buses and trucks would have almost unlimited access to the NAFTA countries. Protection of intellectual properties was to be strengthened, including protection of literary works, recordings, computer programs, and product and process patents.

The NAFTA also provided various provisions to enhance the flow of trade among the three countries. A trilateral trade commission was established to resolve disputes, to review and prevent dumping of products across national markets, and to establish procedures for a country to reinstate pre-NAFTA duties for a period up to 3 years, on a one-time only basis, if domestic industries were injured as a result of an import surge from another NAFTA country.

NAFTA's Importance in Protecting and Stimulating U.S. Investment in Mexico

The passage of NAFTA was important for the United States due to significant investments by U.S. businesses in Mexico. The passage of NAFTA not only protected this investment but also stimulated additional investment. NAFTA also provided additional markets for U.S. products, increased jobs in the United States, and is an avenue to the larger Latin American market. NAFTA is also a building block for an even larger Free Trade Area of the Americas stretching from the Artic Circle to Tierra del Fuego, one of the megatrading blocs expected to emerge throughout the world in the 21st century.

NAFTA Today

NAFTA is administered by a Secretariat under Article 2002 of the agreement. The Secretariat, organized in three section offices located in Ottawa, Mexico City, and Washington, D.C., seeks to resolve trade disputes in a fair, impartial, and timely manner. Each section office is administered by a secretary appointed by the respective governments. Each country is responsible for the costs of operating its section office.

NAFTA's Supporters and Detractors

As with any form of economic integration, NAFTA has its supporters and its detractors. Supporters typically point to the volume of trade that flows freely between the three countries and the positive impact of such free-flowing trade on the economies of the three countries. Detractors typically point to the number of jobs lost due to NAFTA.

From an announcement of intentions by Canada, Mexico, and the United States on August 12, 1992, to undertake an experiment in regional economic integration, to NAFTA's enactment by the U.S. House of Representatives on November 17, 1993, and by the U.S. Senate on November 20, 1993, an interesting passage in regional economic integration is unfolding. In the larger realm of global economic integration, the World Trade Organization also finds detractors and supporters.

—William J. Kehoe

See also Development Economics; European Union; Export-Import Bank; Free Trade, Free Trade Agreements, Free Trade Zones; International Trade; Single European Act (SEA); Tariffs and Quotas; World Trade Organization (WTO)

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Nozick, Robert (1938–2002)

Robert Nozick, political philosopher and Pellegrino University Professor at Harvard, is best known in business ethics circles for his groundbreaking work in political philosophy, *Anarchy, State, and Utopia.* In this his first book, Nozick presents a rights-based approach to ethics and a systematized defense of free market capitalism. It is often juxtaposed with fellow Harvard philosopher John Rawls's *A Theory of Justice,* which was published just 3 years earlier.

In this seminal work, Nozick grounds his political theory in the argument that humans have a fundamental, natural right to be free from force and fraud. They are, therefore, entitled to property that is obtained without force or fraud, as long as they employ what he calls justice in acquisition, which involves the attainment of previously unowned goods, or justice in transfer, which includes all voluntary exchanges, including purchases, barter, gifts, and inheritance.

To discern the justice of a given distribution of wealth, Nozick argues that analysts should use a historical approach, tracing the various transfers that led up to the current holdings. If the entire history of a good consists of voluntary exchanges, the current owner has a moral entitlement to that item. Because ongoing transfers mean that these distributions are constantly in flux, he argues that the end result or snapshot approach to analyzing the justice of distributions is morally misguided. If force or fraud is discovered in the property's history, it is subject to rectification of the injustice.

Unlike the utilitarian, "efficiency" defense of free markets offered by most economists, Nozick argues that free market capitalism is moral because it is the only economic system that recognizes humans' fundamental right to be free from force and fraud. Governmental intervention in the market and redistribution of citizens' property can be accomplished only through the use of force and are therefore unethical. Unlike anarchists, however, Nozick argues that free people would agree to voluntarily support a minimal level of government. Citizens would institutionalize the legitimate use of force, such as that required to rectify injustice, into a "night-watchman" state controlled by checks and balances.

Nozick's rights theory has been criticized for its focus on freedom above all other considerations. According to the theory, actors are behaving morally as long as they refrain from using force or fraud: What they choose to do with their resulting freedom is subject only to individual choice. His entitlement theory has also been criticized for its impracticality. Observers note the difficulties inherent in going back through time to discern the validity of each current holding. Some have also noted that he has not offered a full argument for his strong conception of natural rights.

Along with Ayn Rand's objectivist theory, Nozick's work in political philosophy has helped shape the libertarian movement in the United States. His later works, in epistemology and metaphysics, were well received in philosophical circles but have generally had little impact on the field of business ethics.

—Lori Verstegen Ryan

See also Anarchism; Capitalism; Freedom and Liberty; Free Market; Individualism; Justice, Distributive; Libertarianism; Nozick's Theory of Justice; Property and Property Rights; Rawls, John; Rawls's Theory of Justice

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Nozick's Theory of Justice

In *Anarchy, State, and Utopia,* American philosopher Robert Nozick (1938–2002) develops an *entitlement theory of justice,* a libertarian theory of justice centered on individual inalienable rights (including, first and foremost, liberty). As an entitlement theory, it is concerned with the justice of what one has acquired. Nozick's entitlement theory has three elements—acquisition, transfers, and rectification—which are described in greater detail below.

Nozick's theory can be classified as historical and unpatterned. Broadly, Nozick constructs a typology of theories of justice in which he distinguishes between historical and unhistorical (i.e., end state or current time slice) principles of distributive justice, as well as patterned and unpatterned principles. All four combinations of principles of distributive justice are possible, but Nozick defends his own historical unpatterned theory against the other three conceptualizations (or combinations). By *history,* he refers to past transactions, choices, or actions among individuals that may create or transfer entitlements over resources (which Nozick calls "holdings"). By *pattern,* he means a systematic variation of a distribution according to some natural dimension, weighted sum of natural dimensions, or some other ordering of natural dimensions. For example, a patterned principle may demand that total distributive shares vary directly with moral merit, usefulness to society, or intelligence.

Although Nozick opposes historical-patterned and unhistorical-unpatterned (random allocation) distributions of holdings, his most explicit opposition is to unhistorical-patterned principles of justice, which are set out, for example, in John Rawls's *A Theory of Justice.* According to Nozick, liberty will necessarily upset any pattern of distribution of goods (e.g., egalitarianism). Vice versa, maintaining patterns in any distribution of holdings requires continuous interference with individuals' choices and actions. However, any such interference requires individuals' free consent. With this requirement, Nozick highlights the importance of procedural justice in which individuals agree on several principles of how holdings can be acquired and transferred and how any injustice can be rectified. Based on an individualistic, rights-centered moral philosophy, historical principles of resource allocation take priority over *end state* (also known as *end result* or *current time slice*) principles of justice, which focus on the distributive outcomes of resource allocations but do not examine how these distributions of holdings have actually come about. Nozick's deontological stance—that individuals have rights and that there are things that no one may do to them without violating their rights—does not allow for any position other than historical-unpatterned principles of distributive justice. Its three main elements—justice in transfers, justice in acquisition, and compensatory justice—are summarized in the following sections.

Justice in Transfers

In his proposition that whatever arises justly from a just situation is just, Nozick reaffirms his historical stance toward justice. Any voluntary, agreed-on exchange of goods—whether for money or by gift—satisfies the criterion of a just transfer, if the transferor in turn acquired the good through a just transfer. Although facts of nature, such as poor alternative choices, may constrain free choice, the resultant decisions are not by definition nonvoluntary or unjust. For example, it is conceivable that when workers in less developed countries agree to sweatshop working conditions (because there are no better employment alternatives), such voluntary employment contracts would be considered just in Nozick's theory.

However, Nozick also points out the limitations of free exchange between contracting parties. For example, Nozick regards various transfers as unjust: transfers that make one party a monopolist in a holding necessary to life, transfers that are fraudulent, or transfers that forcibly exclude a party from competing in exchanges. Broadly, exchanges are unjust if they, in one way or another, violate individual rights and diminish individual autonomy, which Nozick embraces as a primary moral value in his deontological ethical system.

Nozick's principle of just transfers implies that any given distributive pattern will be upset by individual choices. He uses the example of professional basketball player Wilt Chamberlain to show that patterned principles require, in Nozick's view, constant interference. Even if we assume that everyone starts out with equal shares of wealth, this distribution will shift as individuals pay voluntary fees to watch Chamberlain play basketball. Many small fees willingly paid by basketball fans will make Wilt Chamberlain very wealthy if a very large number of people pay those fees. The subsequent redistribution of wealth is not unjust, even though it is less egalitarian than the initial distribution. In short, to assess the justice of a given situation, we must examine the process through which such a situation has come about. Hence, a necessary but not sufficient condition for judging a transfer just is its voluntary nature.

In addition to the implications for business already mentioned above, the concept of just transfers implies, for business, that capitalist acts between consenting adults should not be prohibited. Community concerns over, let's say, obscenity or a range of other "irresponsible" acts cannot override the decision-making autonomy and liberty of consenting adults. Moreover, taxation of earnings is equivalent to forced labor or seizure of goods and time. To encourage the kind of justice exemplified in market-based free exchange, government must play a minimal role in individuals' and business affairs. The function of government is limited to the protection of individual rights and punishment of rights violators (including the imposition of compensation).

Several authors have criticized Nozick's theory of just transfers. One criticism points out that Nozick did not systematically delineate the rules of (and exceptions to) just transfers. Also, an accumulation of wealth typically leads to an accumulation of power, which in turn could restrict rather than manifest or express liberty. This second criticism of Nozick's theory claims that it is actually capitalism, not socialism, that restricts liberty. According to Nozick's critics, capitalism may give rise to exploitation of labor. However, Nozick would counter that some so-called exploitative capitalist contracts do not constitute any violation, or threatened violation, of natural rights (e.g., unfair wages). As long as these arrangements are voluntary, Nozick would not consider them unjust. Taking a patterned-justice view, some authors leaning to the political left do not agree with this conclusion.

Justice in Acquisition

Before a holding can be justly transferred, it must be justly acquired. Nozick does not develop a full-fledged theory of justice in acquisition but only sketches the essential elements of such a theory (as he had done with justice in transfers as well). Nozick builds on John Locke's theory of appropriation, according to which someone acquires property rights in an unowned object by mixing one's labor with it. Nozick changes Locke's proviso slightly, in that appropriation cannot be justified if the position of others no longer at liberty to use the thing would be worsened by that appropriation. So, for example, what is illegitimate under Nozick's proviso is (typically) the appropriation of the total supply of a holding necessary for life.

Nozick's proviso also has implications for his principle of just transfers. Just as someone cannot legitimately acquire the total supply of a particular good, one cannot purchase the total supply. One reason is moral: Such a purchase would violate the proviso that Nozick put on justice in acquisition. The second is economic: Over time, the rarer a good becomes, the higher will be its price and thus the less likely a person can purchase all of it. So, in many ways, market forces will prevent injustice in acquisition.

Although Locke's influence on Nozick is undeniable, Nozick also acknowledges limits on property rights. According to Nozick, these limits follow from the proviso. For example, someone may not acquire the total water supply and then charge monopoly prices on it. Nozick even disputes the morality of charging any price on an owner's exclusive holdings if some catastrophe destroys all other supplies of this good. Exorbitant monopoly pricing is proscribed by Nozick's version of the Lockean proviso. Nozick emphasizes that this restriction of property rights does not reflect some unhistorical end-state principle (which would be inconsistent with the deontological flavor of his theory), because the proviso is not about the structure of the resultant distribution of holdings but about the effect such illegitimate appropriation would have on others. However, some of Nozick's critics have pointed out that the proviso could, in fact, be regarded as a consequentialist (teleological) element of Nozick's otherwise firmly deontological theory of justice.

In general, though, Nozick affirms strong property rights in his principles of just appropriation, acquisition, and (by extension) transfer. In Nozick's view (contradicting Rawls), individuals are entitled to use or sell their natural endowments as they please. Thus, Nozick affirms strong property rights but is not quite clear on the foundation of these property rights. What is quite clear is that Nozick does not base them on a right to life. Nor do property rights emerge from a utilitarian calculus that justifies private property as the most efficient mode by which the rights to possess and use things can be arranged. Some critics of Nozick have argued that because of this lack of either a Lockean or utilitarian foundation, Nozick is unable to provide a persuasive, foundational justification of private property.

Compensatory Justice: Rectification of Injustice

The final element of Nozick's tripartite theory of justice addresses, in brief outline, how to rectify past violations of the principles of just transfers and acquisitions. Any process of rectification would compare actual situations that flowed from unjust actions (i.e., actions that violate the principles of just transfer and acquisition) with a best estimate of subjunctive (i.e., "what-if?") information about what would have occurred if the injustice had not taken place. Any gap between the two must be rectified.

Critics of this third principle of justice find fault in its impracticality. With exchanges spanning several generations, it is difficult to understand how rectification can be implemented in practice. Nozick, in fact, recognized this problem and suggested that patterned principles of distributive justice (e.g., those included in Rawls's theory of distributive justice) could, in fact, serve as temporary approximations of rectification, in the absence of historical information.

The Implications of Nozick's Theory of Justice

In general, Nozick's entitlement theory opposes the patterned principles of distributive justice espoused by John Rawls. Rawls's difference principle holds that inequalities are just only if they result in compensating benefits for everyone but, in particular, for the least advantaged groups of society. However, Nozick criticizes Rawls for proposing a redistributive state that tries to impose a patterned distribution on its citizens and, thus, interferes with individual autonomous decision making. He also claims that Rawls's difference principle is problematic because it inappropriately, in an *ad hoc* fashion, focuses on groups rather than individuals and, more generally, does not sufficiently take into account people's entitlements in holdings.

According to Nozick, Rawls failed to connect individual decision making to broader societal outcomes and structures. This criticism of Rawls's theory highlights Nozick's explanatory philosophical strategy, which has a number of interesting consequences for political theory. Nozick's insistence on sacrosanct individual autonomy and property rights leads to the recognition that the minimal state is the most extensive state that can be justified. Nozick's minimal state sits between a state of anarchy and Rawls's welfare state principles. As such, Nozick's theory was subject to criticism from both libertarians, charging that his minimal state goes too far, and contract theorists, charging that his minimal state does not go far enough. The controversy generated by *Anarchy, State, and Utopia* primarily lay in the latter perceived problem because Nozick likened taxation to forced labor and, thus, rejected government action to redistribute wealth.

Anarchy, State, and Utopia provides a compelling argument that underpins the tenets of libertarianism and free market capitalism. However, in his later work *The Examined Life*, Nozick has come to regard his theory as inadequate and too individualistic. In this book, Nozick argues that his earlier entitlement theory runs the risk of ignoring shared cultural values, identity, and solidarity. Despite Nozick's self-examination and self-consciousness (concerning his libertarian entitlement theory of justice), which are also apparent in his *Socratic Puzzles*, *Anarchy, State, and Utopia* stands as an important work affirming individualism, human dignity, and capitalism.

—Marc Orlitzky

See also Capitalism; Coercion; Consequentialist Ethical Systems; Deontological Ethical Systems; Libertarianism; Locke, John; Neo-Kantian Ethics; Nozick, Robert; Procedural Justice: Philosophical Perspectives; Procedural Justice: Social Science Perspectives; Property and Property Rights; Rawls, John; Rawls's Theory of Justice; Socialism

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Nuclear Power

Nuclear power is generated by nuclear fission when sufficient amounts of uranium-235 and/or plutonium are confined to a small space, often in the presence of a neutron moderator. The nuclear reactions produce heat, which is converted to kinetic energy by a steam turbine and then a generator for electricity. In 2005, the U.S. Energy Information Administration reported more than 440 commercial nuclear power plants in the world, generating approximately 365 GW. Nuclear power proponents highlight the amount of electricity that can be generated with a relatively smaller carbon footprint (amount of carbon emitted into the atmosphere) than coal or oil, but opponents argue that the uncertainties and risks associated with operating nuclear plants and disposing of spent nuclear material outweigh the benefits of nuclear-generated power.

In the United States, commercial nuclear power plants are regulated by the Nuclear Regulatory Commission (formerly the Atomic Energy Commission) and military nuclear power facilities by the Department of Energy. Other regulatory agencies and international organizations that address nuclear power are the International Atomic Energy Agency (IAEA) as an autonomous body within the United Nations and the Organisation for Economic Co-operation and Development (OECD) Nuclear Energy Agency. In several countries, more than one regulatory agency addresses nuclear power issues depending on the aspect, such as production, transportation, military use, and civilian or public use.

Nuclear power provides about 10% to 17% of the world's electricity, with the highest percentage in France with 83.4% of all electric power in 2004 generated by nuclear power plants. Popular movements against nuclear power led to the halt of construction of new U.S. nuclear power plants in the early 1980s and severely limit or prohibit the use of nuclear power in Austria, Sweden, and Italy. However, many countries use nuclear power: for example, France, Japan, Russia, and China. The use of nuclear power involves several ethical and social issues relevant to the business community: operations and costs, risks to the environment and communities, and the proliferation of nuclear weapons.

Economics

Across the world, the increase in the amount of electricity produced by nuclear power plants is fueled by increasing demand, expanding population, and rising fossil fuel costs. In the 1970s, a movement against the use of nuclear power began and spread primarily in the United States and Europe with concerns for plant safety and disposal of waste products. Two accidents resulting in a release of radioactive materials occurred at Three Mile Island in Pennsylvania in 1979 and at the Chernobyl plant, Russia, in 1986.

The relative costs of building and operating a nuclear power plant compared to a fossil fuel plant are high, and significant barriers to entry in the market exist. To overcome this obstacle, proponents of nuclear power plants have suggested subsidies and tax breaks to encourage new development and operation of nuclear facilities. As access to fossil fuels is more difficult and the price of fossil fuels and gas products increase, nuclear power may have a cost advantage over other forms of electricity generation.

Risks

Radioactive waste products from nuclear power present risks to the environment and people from production, through transportation, through disposal. Environmental and health risks are complicated by the different psychological factors that may increase the perception of risk: an "invisible" material, a loss of a sense of an individual's control (involuntary vs. voluntary like driving a car), and the time lag between possible exposure and potential surfacing of problems. However, the fields of risk management, risk mitigation, and emergency planning have been advanced by concentrated efforts in the nuclear power industry to reduce the risk of accidents and system failures.

Nuclear waste material is expected to remain radioactive for more than 10,000 years. In the United States, the Yucca Mountain Project in Nevada is a long-term storage facility for radioactive waste. Significant protests from the public continue to affect the design, construction, and operation of this facility; however, disposal operations will begin in 2010. In addition to the risks associated with normal operations and waste disposal, there are also concerns about accidental releases, advances for nuclear weapons, and the use of nuclear materials by terrorists.

Proliferation

In addition to electricity, nuclear power plants also produce plutonium that may be used for nuclear weapons. This is one reason why a country's ability to produce electricity from nuclear power raises fears about the potential nuclear weapons available in a country. Political and military strategy since the 1940s has had to address the use of nuclear weapons as a threat and uncertainty. Mutual (or mutually) assured destruction is a doctrine of military strategy that implies that any use of nuclear weapons against a party will result in retaliation with the use of nuclear weapons, and the only outcome is that both parties (and possibly more) will be destroyed by the effects of nuclear weapons. Based on the theory of deterrence, mutually assured destruction is also known as nuclear deterrence and is a form of the Nash equilibrium where both sides attempt to prevent the worst possible outcome.

After about 18 months of use, the fuel rods within the reactor are replaced. In countries other than the United States, the spent fuel rods may be reprocessed to recover uranium and plutonium that has been formed, which can then be reused as fuel. In the United States spent fuel rods are not reprocessed due to a political decision to try to minimize nuclear proliferation; however, other countries continue to reprocess due to significant economic advantages. Since the end of the Cold War, security concerns have focused more on the operation and safety of nuclear power plants and the potential use of nuclear material in terrorist operations.

As the concern about global warming and climate change grows, there are increased pressures on the energy industry to reduce the carbon footprint, or amount of carbon released per unit of energy produced, and maintain a clean and responsible nuclear power program. Once opposed to nuclear power in any form, the environmental movement is split in its support for nuclear energy. One group maintains that the historical uncertainty and risk associated with nuclear power outweighs any benefits, but a recent group supports the safe and responsible use of nuclear energy as it is a way of providing for the increasing energy demand, has less impact on the environment, and is more cost-effective. The U.S. Nuclear Power 2010 program is a joint effort with the U.S. Department of Energy and the nuclear power industry to identify sites for new nuclear power plants, improve nuclear plant technologies, and address economic issues of expansion. The global use of nuclear power faces technical, economic, social, environmental, and political challenges.

—Virginia W. Gerde

See also Chernobyl; Federal Energy Regulation; Hazardous Waste; Nash Equilibrium; Natural Resources; NIMBY (Not In My Backyard) Phenomenon; Nuclear Regulatory Commission; Pollution; Public Utilities and Their Regulation; Regulation and Regulatory Agencies; Rocky Flats; Silkwood, Karen; Toxic Waste; United Nations Environment Programme (UNEP)

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Nuclear Regulatory Commission

The Nuclear Regulatory Commission (NRC) is an independent U.S. government agency responsible for licensing and regulating civilian use of nuclear energy. Created by the Energy Reorganization Act of 1974, the NRC opened on January 9, 1975. The NRC took over the role of oversight of nuclear energy matters from the Atomic Energy Commission. Its mission is to regulate U.S. civilian use of by-products, sources, and special nuclear materials to ensure adequate protection of public health and safety, to promote the common defense and security, and to protect the environment.

The NRC has three basic responsibilities: (1) to oversee nuclear reactor safety, reactor licensing and renewal, material safety and licensing, and waste management including storage and disposal; (2) to license and regulate civilian use of nuclear energy to protect public health and safety and the environment; and (3) to conduct public hearings on nuclear and radiological safety and on environmental and antitrust issues relevant to nuclear energy. The NRC is capable of imposing civil penalties for violations of its regulations.

NRC-regulated civilian nuclear reactors include those for electric power generation, those for research, and other test reactors for research, development, training, and testing. Reactors are required to meet construction, licensing, security, and operational specifications. The NRC is authorized to shut down nuclear facilities until violations have been corrected. Military nuclear reactors and radiological material are regulated by the U.S. Department of Energy.

Radiological materials other than those used in reactors are also overseen by the NRC. The uses of nuclear materials in medical, industrial, and academic settings and facilities that produce nuclear fuel are regulated for proper acquisition, handling, use, and disposal. In the disposal processes, the NRC supervises the transportation, storage, and disposal of nuclear materials and waste, and the decommissioning of nuclear facilities from service.

The NRC is headed by a five-member commission, each appointed by the president and confirmed by the Senate for 5-year terms. With more than 2,900 employees in 2004, the NRC is headquartered in Rockville, Maryland. There are four regional offices designated to conduct inspections, investigate nuclear incidents, and conduct emergency response programs.

The NRC is important because it deals with "extreme scientific uncertainty, conflicting interests, and growing public fears," and there are problems with the development of feasible scientific knowledge and determining scientific estimates of safety (in the absence of certainty). Radiation exposure standards were developed, but because of the uncertainty and risk of radiation exposure, they are still debated. Reactor safety is still a controversial subject and a complex public policy issue as there are concerns over the reliability of emergency core cooling systems, vessel integrity, quality assurance, and the possibilities of a major accident or terrorist attack.

An accident at Three Mile Island in Pennsylvania on March 28, 1979, melted down the reactor's core. There was no major release of radiation to the community and no need for evacuation, but the accident manifested the public concern over nuclear power safety. Afterward, the NRC put more emphasis on operator training and the human factors, protection from natural disasters and equipment failures, and emergency planning among other issues.

The Department of Energy developed a high-level radioactive disposal site at Yucca Mountain, Nevada. The NRC provides oversight and regulation for this geologic repository for spent nuclear fuel and radioactive material, as well as for repository safety, performance confirmation, closure, and safety issues.

Opponents of the NRC's actions argue that it is unprepared or failing its mission in the areas of security, supporting use of alternative technologies, licensing fraud, disposal, and risk management. Security concerns include security of sources in transportation and transition among life cycle stages, security of physical facilities, and cooperation with other government agencies. Critics also contend that the NRC has required nuclear power plant operators to maintain only a minimum level of security capability. Unchanged in 25 years, the "design-basis threat" is not adequate to address terrorist threats or insider sabotage according to some citizen groups and other organizations.

The NRC has identified four strategic arenas based on its responsibilities: nuclear reactor safety, nuclear materials safety, nuclear waste safety, and international nuclear safety support. The first three are described above. In international nuclear safety support, the NRC is active in international nuclear policy formulation, export-import licensing, treaty implementation, nuclear proliferation deterrence, international safety assistance, and safeguards support and assistance. For example, the NRC worked with the International Atomic Energy Agency (IAEA) in developing a Code of Conduct for the Safety and Security of Radioactive Sources. The NRC also collaborates with other international organizations such as the Organisation for Economic Co-operation and Development (OECD) Nuclear Energy Agency.

The NRC is adapting to a changing social, political, and business environment as the demand for clean, responsible nuclear energy increases across the globe. Once opposed to nuclear power in any form, the environmental movement is now split in its support for nuclear energy. The traditional group maintains that the uncertainty and risk associated with it outweigh any benefits, but a more recent faction supports the safe and responsible use of nuclear energy because it is a way of providing for the increasing energy demand, has less impact on the environment, and is more cost-effective. With its role in regulation, research, and cooperation with the nuclear industry, the NRC continues its emphasis on safety for plant operations, waste material, international cooperation, research, trained personnel, and potential new providers on the supply side.

—Virginia W. Gerde

See also Environmentalism; Environmental Protection Legislation and Regulation; Nuclear Power; Regulation and Regulatory Agencies

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O

Objectivism

Objectivism is the name Ayn Rand gave to her philosophical system. Objectivism is in the Aristotelian tradition, agreeing with that tradition's naturalism in metaphysics, empirical reason in epistemology, and self-realization in ethics. Objectivist political and economic philosophy is robustly liberal, agreeing with the classical liberal tradition's emphasis on individual self-responsibility, freedom, and limiting government to the protection of individuals' rights to their lives, liberties, and property.

Rand's Objectivism adds a romantic and idealistic element to liberalism, most strikingly in its advocacy of business as a passionate calling on a par with art and science. This romantic idealism sets Objectivism apart from those philosophies on both the left and the right that view business either as an antisocial force to be restrained or as a force to be tolerated for its contributions to social welfare.

This conception of business as a potentially heroic enterprise depends on more basic philosophical premises. In the Objectivist view, a philosophy's stances on the power of reason and the morality of self-interest shape its ultimate attitudes toward business.

Objectivism and the Morality of Self-Interest

Most traditional ethical theories are suspicious of self-interest, praising selfless acts and calling self-interested acts amoral or immoral. In the traditional view, self-interest means ignoring or harming others' interests in the pursuit of one's own. Consequently, selflessness is urged as a means to encourage individuals to acknowledge and advance the interests of others.

Objectivism holds that the exact opposite is true: Self-interest, properly understood, is the standard of morality, and selflessness is immoral. The principle of self-interest means seeing individuals as *ends in themselves.* One's own life and happiness are one's highest values; one does not exist as a servant or slave to the interests of others. The corollary is recognizing that other people do not exist as servants or slaves to one's interests. Each person's own life and happiness is his or her ultimate end. The principle of self-interest also entails *self-responsibility:* One's life is one's own and so is the responsibility for sustaining it by methods appropriate to a rational being.

Objectivism's ethics leads to its political and economic liberalism. The morality of self-interest implies that individuals have rights to their lives, liberties, property, and the pursuit of their own happiness. Politically, a moral society will limit the power of government to protecting those individual rights. Economically, a moral society will leave individuals free to pursue their economic interests. This implies that a capitalist or free market system is moral: Free individuals will use their assets as they judge best and trade with others to mutual profit.

Objectivism on Reason and Ethics

Objectivism bases its advocacy of self-interest and liberalism on its view of the power of human reason. Reason is what enables humans to survive and flourish. We are not born with cognitive instincts that tell us what is good: Each of us must learn what is good. Nor are humans born with automatic action-instincts: Each of us must learn how to act successfully. It is by reason that we learn what to eat and what to avoid, which animals are useful or dangerous, how to make tools and devise strategies, and what forms of social organization are productive.

Thus, Objectivism advocates *rational* self-interest: One's interests are not whatever one happens to feel like; rather it is by reason that one identifies one's interests. Reason enables one to identify the relevant facts, project the consequences of potential courses of action, and adopt principled policies of action.

Objectivism calls *virtues* the principled policies individuals should adopt. A virtue is an acquired character trait; it results from identifying a policy as good and committing to acting consistently in terms of that policy.

One major virtue is *rationality:* Since the use of reason is fundamentally good, rationality is being committed to using one's reason. Another Objectivist virtue is *productiveness:* Since the values one needs to survive must be produced, productiveness means being committed to producing those values. Another is *honesty:* Life depends on knowing and acting in accordance with the facts, and honesty is being committed to awareness of those facts.

Independence and *integrity* are also core virtues. Given that one must think and act by one's own efforts, being committed to independent thought and action is a virtue. And given that one must both identify and *act* to achieve one's interests, being committed to acting on the basis of one's beliefs is the virtue of integrity. The opposite policy of believing one thing but doing another is the vice of hypocrisy.

Justice is another major self-interested virtue: Justice, on Objectivism's account, is the policy of judging people, including oneself, according to their value and acting accordingly. The opposite is injustice: Giving to people more or less than they deserve. The final major virtue on the Objectivist list is *pride,* the policy of "moral ambitiousness," as Rand phrased it. Pride is the commitment to making oneself be the best one can be, of shaping one's character to the highest level possible.

The moral person, in summary, is someone who acts and is committed to acting in his best self-interest—that is how one survives and flourishes.

The Objectivist account of self-interest is currently a minority position. The contrasting view typically pits self-interest against morality, holding that one is moral to the extent that one sacrifices for others or, more moderately, to the extent one acts primarily with regard to the interests of others. Some standard versions of morality will hold that one is moral when one sets aside one's interests to serve God, or the weak and the poor, or society as a whole. On these accounts, the interests of those others are of greater significance than one's own; accordingly, one's interests should be sacrificed when necessary. These ethics of selflessness thus advocate seeing oneself fundamentally as a servant, as existing primarily to serve others' interests and not one's own. "Selfless service to others" or "selfless sacrifice" are standard phrases indicating these accounts' view of appropriate motivation and action. The core difference between Objectivism's self-interest view and the selfless view can be seen in the reason why most advocates of selflessness think self-interest is dangerous: conflicts of interest.

Conflicts of Interest

Traditional ethical theories typically take conflicts of interest to be fundamental to the human condition and take ethics to be the solution: Ethical principles are to tell us whose interests should be sacrificed to resolve the conflicts. If, for example, a fundamental conflict exists between what God wants and what humans naturally want, then religious ethics will make fundamental the principle that human wants should be sacrificed for God's. If a fundamental conflict arises between social needs and an individual's desires, then some secular ethics will make fundamental the principle that the individual's wants should be sacrificed for society's.

Taking conflicts of interest to be fundamental generally stems from one of two beliefs: That human nature is fundamentally destructive or that economic resources are scarce. If human nature is fundamentally destructive, then humans are naturally in conflict with each other. Many ethics start from this premise—for example, Plato's myth of Gyges, biblical accounts of Original Sin, Hobbes's "solitary, poor, nasty, brutish, and short" conception of human life in the state of nature, and Freud's account of the Id. If individuals naturally want to steal, rape, and kill, then society must require that these individual desires be sacrificed. Consequently, a basic ethical principle will be to urge individuals to suppress their natural desires so that society can exist. In other words, self-interest is the enemy and must be sacrificed for others.

If economic resources are scarce, then basic human needs are in conflict: For one individual's need to be satisfied, another's must be sacrificed. Many ethical philosophies begin with this premise. Malthusian scarcity theorists argue that population growth outstrips growth in the food supply. Marxists argue that capitalism is driven by brutal competition for scarce resources that leads to the exploitation of some by others. So to lessen the destructive competition, a basic principle of ethics will urge that individuals sacrifice their interests in obtaining more so that others may obtain some and society can exist peacefully. In other words, scarcity implies that self-interest is the enemy and must be sacrificed for others.

Objectivism rejects both the scarce resources and destructive human nature premises. Human beings are not born in sin or with destructive desires; nor do they necessarily acquire them when growing to maturity. One is born with a set of physical and psychological capacities, and through one's choices and actions one develops one's beliefs, character traits, and habits. Chronic desires to steal, rape, or kill are the result of mistaken development and bad habits, just as are chronic laziness and the habit of eating unhealthily. And just as one is not born lazy but through one's choices develops oneself into an active or passive person, one is not born antisocial but through one's choices develops into a cooperative or an antagonistic person.

Objectivism also rejects the claim that resources are scarce in any fundamental way. From animals to wood to coal to oil to nuclear to solar, the power of reason has made possible the discovery and development of new energy resources, and there is no reason to believe that this progress has ended. The development of new resources and the production of an ever-expanding number of goods imply also that human interests do not fundamentally conflict. Instead, Objectivism holds that the opposite is true: Since humans can and should be productive, human interests are deeply in harmony. My producing more wheat is in harmony with your producing more chickens, for by mutual productivity and trade we are both better off. It is to your interest that I be successful in producing wheat, just as it is to my interest that you be successful in producing chickens—just as it is to both our interests that our neighbors be successful in producing automobiles, computers, and music.

Conflicts of interest do exist within a narrower scope. In the short term, available resources are more fixed. Consequently, competition for those resources results, and competition produces short-term winners and losers. Business competition, however, is a broader form of cooperation—a way to allocate resources socially without resorting to physical force and violence. Through competition, resources are allocated efficiently and peacefully, and in the long run more resources are produced. Thus, Objectivism concludes, a competitive business system is in the self-interest of all of us.

Critiques of Objectivism

Rand's Objectivism has been subjected to criticism from both the left and right ends of the traditional spectrum. From the conservative right come three broad criticisms: (1) that Objectivism's reason undermines religious faith; (2) that its individualism undermines communal ties; and (3) that by overemphasizing the power of reason and individual freedom, Objectivism encourages the weakening of traditions essential to social stability. The socialist left also makes three broad criticisms: (1) that Objectivism's idolizing of science and technology leads to an artificial world of dehumanizing machines and environmental degradation; (2) that Objectivism's competitive individualism and capitalism destroy community and lead to inequalities; and (3) that the combination of science, technology, and capitalism leads to a technocratic oppression of the have-nots by the haves.

Contemporary debates over the significance of Objectivism thus have a threefold character—between those who see it as a threat to an essentially religious-traditionalist vision; those who see it as a threat to an essentially left-egalitarian vision; and those who see it as a contribution to the achievements of the modern business, scientific, and liberal democratic world.

—Stephen R. C. Hicks

See also Aristotle; Cato Institute; Egoism; Freedom and Liberty; Free Market; Individualism; Laissez-Faire; Libertarianism; Locke, John; Rand, Ayn; Self-Interest; Smith, Adam

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Occupational Safety and Health Administration (OSHA)

The Occupational Safety and Health Act was passed by a bipartisan Congress in 1970 to respond to what was perceived to be a crisis in the workplace. Several studies had indicated that accidents and injuries on the job were increasing and that there were thousands of disabling diseases in the workplace caused by exposure to hazardous substances. It seemed that workers were not being adequately protected from hazards in the workplace and that federal regulation was needed. The act was passed "to assure so far as possible every working man and woman in the nation safe and healthful working conditions and to preserve our human resources." This act also created the Occupational Safety and Health Administration (OSHA) to administer this act. Congress specified several steps for OSHA to implement this mandate:

- Encourage employers and employees to reduce workplace hazards and to implement new or improve existing safety and health programs.
- Provide for research in occupational safety and health and develop innovative ways of dealing with occupational safety and health problems.
- Establish "separate but dependent responsibilities and rights" for employers and employees for the achievement of better safety and health conditions.
- Maintain a reporting and record-keeping system to monitor job-related injuries and illnesses.
- Establish training programs to increase the number and competence of occupational safety and health personnel.
- Develop mandatory job safety and health standards and enforce them effectively.
- Provide for the development, analysis, evaluation, and approval of state occupational safety and health programs.

OSHA is located in the Department of Labor and has legislative and executive functions with respect to the federal safety and health program. The mission of the agency is to ensure the safety and health of America's workers by setting and enforcing standards; providing training, outreach, and education; establishing partnerships; and encouraging continual improvement in workplace safety and health. OSHA and its state partners have about 2,100 inspectors to ensure compliance with standards, plus complaint discrimination investigators, engineers, physicians, educators, standards writers, and other technical and support personnel spread over more than 200 offices throughout the country. These people establish protective standards, enforce them in the workplace, and reach out to employers and employees through technical assistance and consultation programs.

The act encourages states to develop and operate their own job safety and health programs. These state programs are required to develop standards and enforcement procedures that are at least as effective as the federal program that prevents the states from "watering down" any part of federal requirements. OSHA approves and monitors these state programs to ensure that a state is effectively providing safety and health protection for its workers. As of June 15, 2005, 26 states were operating their own safety and health programs. Three of these state plans, however, covered only state and local government workers.

Two other agencies were established by the act to carry out certain aspects of the federal program. The National Institute for Occupational Safety and Health (NIOSH) is located in the Department of Health and Human Services and is the research arm of the safety and health program. NIOSH conducts research into safety and health-related problems and recommends criteria to OSHA for consideration in the setting of standards. Its objectives include (1) conducting research to reduce work-related illnesses and injuries; (2) promoting safe and healthy workplaces through interventions, recommendations, and capacity building; and (3) enhancing global workplace safety and health through international collaborations.

The Occupational Safety and Health Review Commission (OSHRC) is the judicial arm of the safety and health program and was established as an independent agency to promote objectivity and impartiality in its decisions. This commission handles appeals of employers on violations and penalties as a result of OSHA inspections. When an appeal is filed with OSHRC, an administrative law judge normally hears the case and makes a decision. This decision can be appealed to the full commission, and its decision can be further appealed to a U.S. court of appeals and possibly reach the Supreme Court if certiorari is granted.

OSHA does its work by setting standards related to workplace safety and health. There are two types of standards related to safety concerns: (1) horizontal standards that apply to all industries and (2) vertical standards that apply to particular industries. Health standards relate to particular substances that workers may come into contact with that are considered to be harmful. These standards are enforced through an inspection process where safety and health officers visit business facilities to check on compliance with the national safety and health standards that have been established. These inspectors are concerned with what standards apply to a given facility and whether employers and employees are in compliance with these standards. If violations of these standards are found, citations may be issued and civil penalties imposed.

OSHA has a number of programs designed to enhance safety and health in the workplace. Its consultation service is free to employers and is delivered by state governments using well-trained professional staff. Through using this service, employers can find out about potential hazards at the workplaces, improve their occupational safety and health management systems, and even qualify for a 1-year exemption from OSHA inspections. The Alliance Program, which started in March 2002, is a cooperative program that enables organizations committed to safety and health to work with OSHA to prevent injuries, illnesses, and fatalities in the workplace. Groups that can form an alliance with OSHA include trade or professional groups, educational institutions, labor unions, and employers.

The Safety and Health Achievement Recognition Program recognizes small employers who create and maintain an exemplary safety and health management system. The OSHA Strategic Partnership Program moves away from traditional enforcement methods and embraces collaborative agreements that are made with associations, unions and councils, and industries to affect multiple worksites or employers. Finally, the Voluntary Protection Program is designed to establish cooperative relationships at individual worksites that have implemented a comprehensive safety and health management system.

—Rogene A. Buchholz

See also Employee Protection and Workplace Safety Legislation; Regulation and Regulatory Agencies

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Ombudsperson

Ombudspersons serve as an informal resource for individuals who struggle with interpersonal conflict, violation of institutional policies, or the challenges caused by the increasing bureaucratization of organizations. Originally arising as a voice of the people for citizens to navigate claims against government, ombudspersons have been established through legislation or institutional policy in executive, legislative, advocate, or organizational roles in government, private corporations, not-for-profit organizations, and academic institutions. Organizational ombudspersons, the focus of this entry, are situated outside of regular management channels and possess no other formal or adjudicative role, but seek fair and just process. Established as an informal resource for employees, ombudspersons provide a safe place to investigate options, obtain information on policies, procedures, rights, and responsibilities, and learn about the resources necessary for satisfactory resolution of issues and disputes. Three critical marks define the organizational ombudsperson: neutrality, independence, and confidentiality.

As a designated neutral, the ombudsperson remains impartial and does not align with any party in a dispute or controversy within an institution. The ombudsperson has no power to adjudicate disputes or implement policy or decisions. The ombudsperson helps clarify policies, encourages peaceful dispute resolution, mediates, and explores all options for resolution. If an ombudsperson observes a trend that suggests the need for improvement of the entity or that violates institutional mission or policy, professional standards of practice permit systemic advocacy to encourage institutional change, so long as confidentiality is protected. To help minimize sources of conflict, ombudspersons frequently provide training on conflict management, mediation, and peacemaking.

As an independent, the ombudsperson is outside any formal reporting chains within an organization and has no other formal roles. The ombudsperson typically reports to the senior officer to ensure freedom from interference, control, or limitation on the ombudsperson's work. Although employed by the institution, the ombudsperson and the institution frequently draft charters to publicly set forth the necessary safeguards and procedures that guarantee the ombudsperson's independence, neutrality, and confidentiality.

Confidentiality remains the linchpin of the ombudsperson's responsibilities as parties seeking assistance are assured that conversations and identities will remain confidential. Confidentiality is held by the ombudsperson and cannot be waived unless the ombudsperson agrees or recognizes an imminent threat of serious harm. Unlike any other institutional officer, notice of an infraction or violation of policy or law to the ombudsperson is not notice to the organization. To protect the employee and serve justice, however, the ombudsperson may advise the individual how to give notice to the institution of violations of law or policy. Confidentiality serves a public purpose in encouraging individuals to come forward to discuss issues, explore the ramifications of giving notice to the organization or failing to give notice, inspire options, and seek resolution of problems without threat or fear of retaliation. The ombudsperson, therefore, seeks to increase workplace civility and emphasize respect for human dignity by helping individuals build confidence and hone the necessary skills to resolve conflict and pursue justice.

—Craig B. Mousin

See also Alternative Dispute Resolution (ADR); Sarbanes-Oxley Act of 2002; Whistle-Blowing

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Omnibus Trade and Competitiveness Act of 1988 (OTCA)

The Omnibus Trade and Competitiveness Act of 1988 (OTCA) seeks to bolster the competitiveness of American companies through changes in the substance and process of trade law. Although building on earlier legislation, this most recent major trade law addresses a far broader scope of issues, more forcefully asserts the interests of American firms, and provides executive branch officials with much less discretion in implementation.

Although the United States has championed the cause of free trade through multilateral agreements under the General Agreement on Tariffs and Trade (GATT) and the World Trade Organization (WTO), concerns about the competitiveness of American workers and companies mounted in the 1980s with the rapid emergence of Japan as an economic power, growing trade deficits, and job losses in manufacturing. Constituent pressures on Congress for protection against unfair foreign trade practices increased, and the OTCA was passed after lengthy deliberations and over some opposition by the Reagan administration.

Rising imports led to increasing complaints that foreign firms competed unfairly by predatory pricing or "dumping" and by export subsidies from their governments. The OTCA amended earlier legislation to improve the enforcement of antidumping provisions and facilitate the imposition of countervailing duties to combat foreign subsidies. Some criticize these efforts to defend domestic markets arguing that the costs to American firms and workers in the particular industry affected may be offset by benefits to other stakeholders, most notably consumers of the cheaper goods.

More central to the OTCA than the defense of domestic markets were efforts to enhance the competitiveness of American firms abroad. To this end, the Foreign Corrupt Practices Act of 1977 (FCPA) was amended to relax constraints on payments to secure the timely performance of routine governmental actions. American employees became legally liable only when they had "knowledge" rather than the "reason to know" of the illegal uses of their funds. Corporate liability for employees' actions was also reduced, thus creating the possibility of scapegoating midlevel managers. Some suggest that these changes may undermine the intent of the FCPA to align American officials' actions abroad to their home country standards.

The most controversial sections of the OTCA deal with efforts to combat unfair trading practices of foreign governments and firms that reduced the competitiveness of American firms abroad. Congress sought to ensure aggressive actions by the executive branch by transferring authority to retaliate against such practices, conferred under Section 301 of the Trade Act of 1974, to the U.S. Special Trade Representative and specifying in detail the procedures to be followed. What came to be known as Super 301 required the identification of nations engaged in egregiously unfair trade practices and the unilateral imposition of sanctions if necessary to end them. Of particular concern were barriers to the expansion of service industries not yet protected under the multilateral agreements. Even more critical were infringements on intellectual property rights that slowed the foreign penetration of high-technology industries considered essential to American economic growth. In response, a Special 301 clause was included in the OTCA requiring close monitoring of countries for violations of these rights, the public listing of violators, and the initiation of bilateral negotiations, backed by the threat of trade sanctions. In 2006, for example, although only one nation, Ukraine, was placed on the Priority Foreign Country list reserved for the most serious offenders, 13 countries appeared on a Priority Watch List for failing to provide adequate levels of protection, and a Watch List numbered 36, including the EU, China, and Canada.

These policies to combat practices hindering the access of American firms to foreign markets have been controversial. Some argue that they facilitate the transfer of wealth and jobs abroad and thus erode the incomes and welfare of American workers and communities. Others object that these actions by the U.S. government undermine the development of stronger multilateral agreements, international organizations, and a world community. Finally, many argue that rights to intellectual property, however important for innovation, often conflict with human rights, with the issue of poor people's access to drugs in developing nations frequently raised.

—J. Lawrence French

See also Developing Countries, Business Ethics in; Free Trade, Free Trade Agreements, Free Trade Zones; International Business Ethics; International Trade; Unfair Competition

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OPEC

See Organization of Petroleum Exporting Countries (OPEC)

Open-Book Management

Open-book management (OBM) refers to a system in which a company fully shares its financial status with its employees, who then become active partners in a synchronized effort to optimize future financial performance. The origins of OBM can be traced to Springfield ReManufacturing Corp. (SRC). Formerly a failing division of International Harvester, SRC was purchased in 1983 by its plant manager, Jack Stack, and 13 other executives. They paid $9 million for the plant, depositing $100,000 as a down payment and amassing a debt-to-equity ratio of 89:1. Recognizing that any financial error would cause bankruptcy, Stack decided to keep all employees informed about the company's ongoing financial status. John Case subsequently termed this approach "open-book management." Now a large and successful holding company, SRC calls its system—mirroring the title of Stack's first book—"The Great Game of Business."

Key steps in OBM include the following:

- Share with employees financial and operational information that supports optimizing business decisions. This should consist of critical numbers, highlighting the line-of-sight between employees' daily job performance and the firm's operating and financial results. OBM firms develop scoreboards—vehicles for regular communication of key numbers to the workforce.
- Enhance employee literacy in the basics of accounting and business. Simply giving financial statements to employees who don't understand them is a source of confusion and problems. Employees need to learn, for instance, about income statements, balance sheets, and cash flow statements.
- Empower people to make decisions based on what they know. Once the books are open, employees will want a voice. They should be given opportunities to self-manage and should be held responsible and accountable not just for scheduling their work and hitting quality targets but also for making their unit's budget or profit goals.
- Share the financial gains. While financial rewards take many forms in OBM firms, the key is to directly link those rewards to the "critical numbers" and profits.

However, OBM is more than a fixed series of steps. Rather, it is a process, a system, and even a philosophy.

The Case for OBM

In addition to SRC, OBM success stories include R. R. Donnelley, AES Corp., PSS World Medical, Manco, Inc., Foldcraft, and Whole Foods Market. Other firms, such as Saturn, while not referring to their efforts as OBM, employ the essential elements of the approach.

OBM combines a large number of currently popular concepts from organizational behavior and management, such as strategic planning, participation and involvement, education, empowerment, job enrichment, self-management, feedback, and goal setting. Furthermore, empowerment and aspects such as "playing the game"—short-term initiatives designed around a specific goal, with a low-cost reward if people "win"—should enhance intrinsic motivation, while directly linking performance to rewards should heighten extrinsic motivation. In addition, full implementation of OBM requires culture assessment and reinforcement or change. This set of characteristics should enhance intellectual capital, a critical resource in a knowledge economy, while fostering the sort of organic, flexible organizational structure required in complex, dynamic, uncertain environments.

Difficulties

Even staunch advocates of OBM emphasize potential difficulties associated with its implementation. They note, for instance, that some attempts to implement OBM failed because of unforeseen circumstances, changes in leadership, or unwillingness to make necessary changes in the compensation process. Some primary difficulties relating to OBM include the following:

- OBM is a major change effort, often involving even culture change, and will lead to redefinition of managerial roles, threats to status and power relationships, and uncertainty. As such, resistance is likely.
- OBM raises concerns about loss of information, including leaking of competitive secrets. Advocates respond that only critical numbers are provided to employees, not all financial information, and that most such information can already be found on the Internet and elsewhere. In addition, business law provides various protections—such as noncompete and nondisclosure agreements—against leaking trade secrets and company-specific information.
- For public companies, internal release of financial information may lead to scrutiny by the Securities and Exchange Commission. In some cases, such firms keep branch-level books open all the time but provide consolidated financials to employees only when they are released to the public. Others, such as AES Corporation, declare all their employees as insiders for stock-trading purposes.
- Implementation of OBM may be especially difficult in large organizations since the line-of-sight from individual employees' jobs to the organization's financial performance is harder to trace. In addition, political and cultural obstacles may be especially severe in larger firms.

Successful Implementation

As a major change effort, if implementation of OBM is to be successful, top management support must be strong, visible, and consistent. Probable sources of resistance to change should be identified and defused. Since OBM requires a substantial investment in people and systems, firms must be prepared to provide adequate resources. Furthermore, the organizational culture must be supportive and consistent with OBM tenets; OBM cannot survive in a command-and-control culture. In addition, the national culture must reinforce OBM; OBM may be unsuitable in national cultures favoring strong authority relationships and avoiding uncertainty. Finally, a long-term perspective and persistence are critical; as with other major change efforts, full implementation of OBM may take years.

Evidence

While OBM combines many features for which there is substantial theoretical and empirical support, evidence to date in support of OBM per se is almost entirely anecdotal. Several notable success stories are held up as exemplars. In contrast, companies that have failed to fully implement OBM or for which OBM was abandoned are typically cited just as examples of faulty implementation or unanticipated events. There may, though, have been other reasons for abandonment or failure of OBM efforts, including the desire to avoid escalation of commitment in the face of clearly intractable problems.

A study by the National Center for Employee Ownership concluded that firms implementing OBM, relative to competitors matched on SIC codes, number of employees, and sales volume, saw 3-year sales growths about 2% greater than would be expected without OBM and corresponding employment growth about 1.2% greater. While such findings are impressive, the study compared just firms that had been successful in implementing and sustaining OBM—not all firms undertaking OBM—to their competitors, and benefits may thus be overstated. On the other hand, a narrow focus on financial indicators—while certainly important—may fail to recognize other OBM benefits relating to trust building, equity perceptions, culture change, organizational commitment, and other "soft" outcomes, all of which may have long-term bottom-line impacts.

In sum, OBM combines many positive features, and its advocates can point to notable successes. However, additional research is needed to better understand OBM and provide solid evidence of its effectiveness.

—Ramon J. Aldag

See also Confidentiality Agreements; Empowerment; Fairness; Justice, Distributive; Meaningful Work; Participatory Management; Strategic Planning; Trust

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Opportunism

Opportunism is a foundational assumption of many economic theories that claims human beings are generally self-interested and will take advantage of others when possible. For example, some economic actors will take advantage of another party to advance their interests by making false promises, misrepresenting intentions, reneging on agreements, or changing the terms of a deal to benefit themselves. Other economic actors will be less deliberate by attempting to benefit from free riding. Such behavior, deliberate or otherwise, leaves the "honest" party to the exchange worse off.

Scholars assuming that people are opportunistic do not necessarily believe that everyone is perniciously self-seeking. Rather, they believe that the presence of *a few* opportunistic individuals means economic exchanges should be structured to protect against *potential* opportunism. Opportunism is thus a theory of exchange that assumes the worst about individuals and makes predictions as though the worst were reality. One influential economic theory based on the assumption of opportunism, transaction cost economics, claims market exchanges fail when a transaction becomes vulnerable to opportunistic behavior. When the threat of an exchange partner behaving opportunistically becomes particularly high (which is said to occur when the transaction is characterized by substantial uncertainty, small numbers, and irreversible investments to support just that transaction), economic exchange will shift to hierarchies such as firms, rather than occurring in spot markets. According to transaction cost economics, hierarchies have supervisory, monitoring, and incentive mechanisms that are able to detect and deter opportunism.

This view of human nature (which is ultimately what opportunism represents) has been vigorously challenged. Many sociologists, biologists, ethicists, and even economists and management scholars argue that humans consistently exhibit cooperative and altruistic behaviors, which belie an overreliance on the assumption of opportunism found in much economic literature. Moreover, they argue that opportunism is greatly reduced when individuals are part of an organization with a shared purpose, such as a firm. Indeed, some of the scholars who believe in the essential cooperative nature of economic agents claim that economic theories assuming opportunism invite managers and firms to inadvertently promote the very kind of opportunism that organizational hierarchy is assumed to lessen. In short, this side of the debate believes that people's cooperative and trustworthy tendencies should be highlighted and stressed in economic and management theories, instead of their opportunistic tendencies. And, as with many such debates, there is no widely agreed-on conclusion.

—Karen Schnietz and Ariff Kachra

See also Altruism; Bounded Rationality; Coase Theorem; Economic Rationality; Market Failure; Reciprocity; Transaction Costs; Trust

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Opportunity Cost

Opportunity cost is defined as the value given up by selecting one of a group of mutually exclusive alternatives. The fundamental economic problem is one of scarcity. Humans have virtually unlimited needs and wants for goods and services, but resources or inputs, such as land, labor, and capital, are limited. This combination of unlimited demand and scarce resources compels individuals and societies to make choices. When a choice is made, there is a trade-off and something must be given up. The value of the next best alternative that might have been chosen is called the opportunity cost. All decisions made by individuals and societies have an opportunity cost that may be thought of in monetary or nonmonetary terms. For example, the decision to take a walk means giving up time to read a book and the utility or satisfaction that goes along with reading the book.

The opportunity cost of a decision may exceed the out-of-pocket cost. An example often used to illustrate this point is the cost of a college education. The opportunity cost of attending college includes not only the monetary cost but also the costs associated with the foregone opportunities, such as earnings from full-time employment or the value of time spent training for the Olympics. If out-of-pocket expenses at a private university are $25,000 per year for tuition, fees, and textbooks and foregone earnings equal $18,000 per year, then the total cost of college attendance is $43,000 per year. A student must weigh this cost against the current and future benefits received to ensure that he or she is making the most efficient use of scarce resources.

Opportunity cost differs from accounting cost in that the latter does not include foregone opportunities. The financial statements of a business may show an accounting profit, while the business is sustaining an economic loss if opportunity cost is considered. Assume that a small advertising agency has a total revenue of $500,000 per year and accounting costs of $400,000, for an accounting profit of $100,000. If the small business owner could earn $150,000 per year working for a large advertising agency, then the total opportunity cost is $550,000, and the business is actually suffering a $50,000 annual loss. If the satisfaction (benefit) of self-employment does not equal at least $50,000 per year, the small business owner should shut down the operation and take the $150,000 position at the large advertising agency.

Business decisions are not always based on all-inclusive measures of opportunity cost. An example is a manufacturer who does not consider air and water pollution in the choice to adopt or not adopt a new manufacturing process. In a decision not to adopt a cleaner manufacturing process, the opportunity cost of the decision includes the costs of pollution that must be borne by local citizens. In the case of massive plant layoffs, the opportunity cost of dismissing all or part of a labor force may affect the long-term health of the company in the loss of valuable expertise and knowledge, future retraining costs of new workers, and the effects of unemployment on the local community. Community assistance resources may be strained. Local businesses may be affected when the community has less money to spend on goods and services.

In a market economy, an efficient allocation of resources requires that the marginal, or additional, benefit (or price) of each good or service be equal to its marginal opportunity cost. Often, market failures exist that prevent this efficiency condition from being met. The presence of negative externalities, such as air and water pollution, cause the marginal opportunity cost to society to exceed the marginal opportunity cost to the producer. In these instances, markets will underprice and overproduce the good or service. To ensure efficiency, the government may choose to impose regulations, taxes, or fines to ensure that the costs to the producer are equal to the costs imposed on society. Monopoly power is a market failure that results in the price of a good or service exceeding the marginal opportunity cost, resulting in less than the socially optimal level of output. In this situation, the government may regulate price and/or output. A third example of a market failure involves the provision of public goods. Private markets will fail to produce the efficient level of public goods because they are nonexcludable; that is, nonpaying users cannot be prevented from consuming the public goods. In this case, the marginal cost of additional users is zero, and it is not easily possible to charge a price. Therefore, private markets will not produce the goods, and the government becomes the provider of public goods.

Decisions concerning the efficient allocation of resources between the present and future are also based on opportunity cost. The opportunity cost of present consumption (i.e., lower future consumption) is reflected in the interest rate. When current consumption is valued over future consumption, savings will be low and interest rates will be high. The high interest rates reflect the fact that people require a high return to forego current consumption. On the other hand, if people value future consumption over current consumption, savings will increase as people put money aside to fund future consumption, and interest rates will be low. Since interest rates influence investment spending, the value of current versus future consumption affects the future productive capacity of the economy.

In practice, there are factors that may prevent the interest rate from correctly allocating current versus future consumption. First, interest rates are not completely market determined and are often manipulated by central banks to stabilize the economy. Second, some economists believe that humans are, by nature, shortsighted and undervalue future consumption. Third, prices of current goods and services do not reflect their true opportunity cost when negative externalities are present. Finally, current production will exceed the efficient level if some resources, such as rain forests, unspoiled deserts, and rare species of plants and animals, have a market price of zero.

The consideration of opportunity cost is necessary for sound economic decision making. However, in practice, determining the opportunity costs of alternatives may be difficult. This is a particular problem when public sector projects are evaluated and the cost-benefit analysis is subject to political control and the influence of special interest groups. Broadly speaking, opportunity costs include anything and everything that has any connection to or bearing on the decision. A decision that deliberately excludes the consideration of known social and economic factors raises questions about ethics in decision making.

—Rebecca Summary and Eleanor G. Henry

See also Cost-Benefit Analysis; Externalities; Market Failure; Perfect Markets and Market Imperfections; Public Goods

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Organisation for Economic Co-operation and Development (OECD)

The Organisation for Economic Co-operation and Development (OECD) is an international agency consisting of 30 member nations that are dedicated to economic growth and stability, democratic governance, and the economic development of the organization's less economically developed members and nonmember countries. In many ways, the OECD is unique. It provides numerous and varied services to its members including basic in-depth research on global matters, consultations on economic and social issues, and the diplomatic context in which various agreements and conventions have been entered into and observed. Moreover, the work done at the OECD is central and highly significant both in public policy formation in the member states and in terms of corporate governance given the emphasis that the agency has placed on the role that multinationals play in today's world. In short, the OECD can be called a "super organization," and in addition to having a unique mission and organizational design, the OECD also has a unique history that is a good point of departure in understanding the varied workings and reach of this international super organization.

OECD History

The OECD had its start in the transformation of the Organization for European Economic Co-operation (OEEC). The OEEC, established in 1948 through backing primarily from the United States and Canada, was designed to coordinate the Marshall Plan that had as its objective the reconstruction of Europe after the destructive effects of World War II. The OEEC had as its main mission the promotion of economic cooperation among its 16 member states so that the reconstruction of Europe might take place efficiently. There were several major economic measures that the OEEC introduced to achieve this goal including the development of trade within Europe by reducing obstacles to free trade practices between member states and the establishment of a new customs zone on the Continent. The OEEC also worked on European labor conditions and set up a permanent Committee on Manpower. In short, the OEEC was an economic development agency designed to restore Europe to some of its former stature as the geographic site of several leading economic powers before World War II.

Once the physical restoration of Europe was completed, the OEEC gave birth to the OECD on December 14, 1960. There were 20 original member countries that signed the convention establishing the OECD (Austria, Belgium, Canada, Denmark, France, Germany, Greece, Iceland, Ireland, Italy, Luxembourg, the Netherlands, Norway, Portugal, Spain, Sweden, Switzerland, Turkey, the United Kingdom, and the United States). For more than four decades the OECD has been a major player in the economic development of Europe, seeing its role expanded in several directions. It has also been the purveyor of several important international agreements and conventions that have helped shape the world economy. Today, the organization consists of 30 total member countries (added were Japan in 1964, Finland in 1969, Australia in 1971, New Zealand in 1973, Mexico in 1994, the Czech Republic in 1995, Hungary in 1996, Poland in 1996, South Korea in 1996, and the Slovak Republic in 2000). In 2004, a report titled "A Strategy for Enlargement and Outreach" suggested that the changing face of the world, thanks to the process of globalization, made it mandatory that the OECD think very seriously about even newer ways to expand and be a relevant presence in the world.

About the OECD

As an international super organization, just what does the OECD do? The founding mission of the organization says that its primary function is to work toward policies that will achieve (1) the highest sustainable economic growth and employment and (2) a rising standard of living in OECD, member countries. This was to become the main goal of the OECD, and at the same time, the policies that it would work on with its members were fashioned to maintain their financial stability and, thereby, contribute to the development of the world economy. In short, this organization set itself some very lofty local and global goals.

Since 1960, the OECD has been hard at work attempting to formulate and implement global economic development policies. Along the way, it has found it necessary to address and work on some noneconomic issues as well. The organization has taken it on itself to improve economic efficiency, groom markets and their systems, create the conditions under which to expand free trade, and contribute to development in the industrialized states as well as in less economically developed nations.

What makes the OECD not just an international organization, but an international super organization, is the fact that it engages in such a wide variety of activities that contribute both to the welfare of its member states and, thereby, to the continued progress of the world per se. It can be taken primarily as a center for the research, formation, and writing of international public policy. But more than that, it also serves to bring nation-states together in diplomatic ways and to create international conventions and agreements that have far-reaching consequences for the people of the OECD member states in particular and of the world in general. These various conventions and agreements often serve to fulfill the OECD's mission as an economic development program, but often they deal with other pressing tangential issues as well, such as education, social affairs, and development assistance to nations in need.

In addition to its 30 member states, 70 relationships with other countries and nongovernmental organizations are maintained, so the OECD can be labeled a very comprehensive organization. It also taps policy and consulting input from two major groups dealing with international business and labor, namely, the Business and Industry Advisory Committee established in 1962 and the Trade Union Advisory Committee founded in 1948 as an advisory committee to the Marshall Plan. With its major headquarters in Paris, a council that consists of representatives from its member nations governs the organization. The council has oversight authority of the various working committees that are established within the 18 OECD directorates that are devoted to a set of diverse topics. The council also sets the annual budget that is provided by member country contributions totaling around €330 million a year. A secretary-general serves as the executive of the organization.

The bulk of the work is done by the 2,000-plus employees of the OECD secretariat who are active in diverse projects through the committees that are divided among the directorates. The committees and their working parties, subgroups, and consultants perform the research and economic and statistical analysis, and they write the many publications that are used widely by officials both in and out of the member countries as well as by many academics who study and teach about globalization issues, economic development, and international public policy. And again, while the OECD is billed primarily as an organ for economic development, its work goes into areas such as social policies, environmental analysis, and the conduct of corporate practices the latter of which can be elaborated on under the general rubric of "corporate governance."

OECD and Corporate Governance

A topic of continuing interest and productive research at the OECD is that of corporate governance. Corporate governance is defined as the interplay between the rights and responsibilities of a company's management, its board of directors, the shareholders, and direct and indirect stakeholders who will likely be affected by management, and how well this interplay might contribute to a business organization's overall market performance. The *OECD Principles of Corporate Governance* represents the official statement about corporate governance at the OECD, and this document and the research that has gone into it have become widely recognized as a collection of some key corporate mechanisms for success in global business.

Originally devised in 1999 and revised in 2004, these Principles serve as a kind of benchmark by which to measure best business practices in the area of corporate governance and as a framework for discussion and dialogue about the need for good corporate governance between OECD member and nonmember states alike.

The Principles include reference to six central items that governments are asked to address and implement:

1. An effective institutional and legal framework to support good corporate governance practices

2. A corporate governance framework that protects and facilitates the exercise of shareholders' rights
3. Safeguards that support the equal treatment of all shareholders, including minority and foreign shareholders
4. Recognition of the importance of the role of stakeholders in corporate governance
5. Procedures that underscore the importance of timely, accurate, and transparent disclosure mechanisms
6. Clarity in setting up board structures, responsibilities, and procedures

If corporate governance can be bolstered by such mechanisms as are spelled out in the *OECD Principles of Corporate Governance,* then it is possible that the world may see fewer examples of corporate scandal. It could be argued that the recent surge in corporate malfeasance as witnessed at Enron, WorldCom, and Parmalat, may have been avoided, if stronger reins were in place at the top of these organizations and if their governance was stronger with more board involvement and the good exercise of controlling powers.

So the overall goal of the six principles is to urge nations, and, in turn, the international business organizations that they regulate, to be successful in the open market and to be so in a responsible way. In fact, corporate responsibility has been another major concern of the OECD over the years, and the OECD has engaged in a number of corporate-responsibility-based activities. Among the various initiatives undertaken by the OECD in the area of international corporate responsibility, there are two important programs that need to be highlighted and detailed: the Guidelines for Multinational Enterprises and the OECD Anti-Bribery Convention.

The OECD Guidelines for Multinational Enterprises

The OECD Guidelines for Multinational Enterprises can be taken as a set of well-defined recommendations made to international corporate organizations with respect to their actual business conduct and practices. Some point to the Guidelines as the only comprehensive, multilaterally endorsed, and voluntarily adopted corporate principles available that address international business conduct and are approved and "overseen" by governments through the OECD Convention that gave birth to them. Adhering countries consist of all 30 OECD member countries and 9 nonmember countries (Argentina, Brazil, Chile, Estonia, Israel, Latvia, Lithuania, Romania, and Slovenia). These governments have committed to promoting the Guidelines among corporations to which they are host or home. As such, the Guidelines serve as useful standards for multinational corporations as they develop their approach to international management issues and concerns.

Many of the major areas of international business ethics are addressed by the Guidelines, including labor relations, human rights, environmental obligations, information disclosure and transparency, the problem of bribing public officials, consumer interests, the business concerns around matters of science and technology, competition and antitrust issues, and taxation by host countries. The Guidelines are divided into three parts. The first section lays out and details the 10 guidelines themselves, and in this first part the business ethics areas mentioned are raised with attention to both general and specific recommendations on how multinational corporations can successfully address the given topic. This section is peppered with a number of "should" statements, that is, a set of 10 normative-type directives to multinational corporations that provide pointed language about their obligations and responsibilities in the global marketplace. More discussion of the provisions found in these 10 planks is provided in the third part of the Guidelines that consists of some extensive commentary and analysis.

The second section of the Guidelines is titled "Implementation Procedures of the OECD Guidelines for Multinational Enterprises." As the title suggests, the OECD has issued the Guidelines with suggestions to the governments adhering to them about how to apply, oversee, and manage the 10 recommendations. Although the provisions set out by the Guidelines are voluntary and exist without any recourse to legal enforcement, the OECD has set up "complaint mechanisms" whereby governments have clear implementation obligations, which include establishing a "national contact point" (NCP) to handle allegations of corporate misconduct. These NCPs may be senior governmental officials or government offices charged with promoting awareness of the Guidelines and handling inquiries about corporate behaviors that run counter to any one of them and violate the spirit of the Convention. The NCPs are designed to serve as a kind of international "Better Business Bureau" in the promotion of business ethics in the global marketplace and to provide a clearinghouse where affected parties can come and have their cases heard.

It almost goes without saying that the Guidelines are not free of critics who find fault with them for various and sundry reasons. Some claim that the specific content of the Guidelines is lacking in precision, while others criticize them because of the seeming lack of enforcement procedures that would give some teeth to the Guidelines. An example of such critical appraisal comes from OECD Watch, which promotes itself as an international network of civil society organizations promoting corporate accountability.

OECD Watch issued a 2005 report, "Five Years On: Review of the OECD Guidelines and National Contact Points," which was quite critical of the Guidelines and of the issue of their enforcement, in particular. The group claims that they cannot adequately curb corporate misconduct, since the NCP system is a failure. They concluded in their report that the NCPs rarely helped to resolve specific conflicts, and that after 5 years, the NCPs are failing to promote the Guidelines or to encourage adherence to them.

Nonetheless, and in spite of such criticisms, the OECD Guidelines for Multinational Enterprises might be taken as but only the first step toward something like the policing of multinational corporations. There are a number of obstacles as to why it is difficult to have international public policies that deal with the ethical conduct and misconduct of international firms. But without the introduction of the OECD program, there would be no movement in that direction at all. Moreover, there is still another example of an OECD initiative in international business ethics that remains to be detailed.

The OECD Antibribery Convention

In 1997, member countries, along with the assent of five additional nonmember countries (Argentina, Brazil, Bulgaria, Chile, and the Slovak Republic), entered into an OECD Convention titled "Combating Bribery of Foreign Public Officials in International Business Transactions." The OECD bills this convention as a one-of-a-kind international accord that provides for legally binding curbs on the behavior of multinational corporations. Adhering countries were expected to pass legislation that would criminalize acts of bribing public officials by executives of multinational corporations to further the business interests of their firms. According to the Convention, the bribery of a foreign public official should be punished by penalties. Also, the Convention requires that attempts to cover up such bribery or "launder money" having to do with the bribery of foreign public officials should also be criminalized by cooperating governments.

The fact that the United States had already passed such legislation with its Foreign Corrupt Practices Act (FCPA) was no doubt stimulation for the OECD to undertake such an antibribery convention. Simply put, U.S.-based multinational corporations felt themselves to be at an unfair competitive disadvantage to multinationals based in other major industrialized countries that did not have such legislation in place, and it was in the interests of the United States to foster a multilateral agreement such as the OECD Antibribery Convention. Hence, the Antibribery Convention can be taken as the expression of the will of adhering countries to match the United States in its lead against the bribery of public officials by international businesses.

The Convention has provisions for a monitoring system to be put into place and be managed by the OECD "Working Group on Bribery." This group, made up of representatives from the participating nations, was established in May 1994. It is implementing a system of review that is divided into two phases. The first phase was designed as an assessment process where a country's antibribery laws are compared with the Convention's recommendations and evaluated as being in compliance with them or not. The second phase requires that the Working Group on Bribery study the enforcement procedures for the antibribery laws that a country has adopted and implemented along with input on enforcement from stakeholder groups in labor and civil society as well as from governmental officials and business practitioners.

Progress reports on Phase 1 and Phase 2 are available on the OECD Web site. This monitoring process has resulted in some tangible changes on the international scene. Several countries have amended their laws dealing with bribery so that they can stand in compliance with what the OECD Convention has recommended. Among those countries that have enacted such amendments are Iceland, Japan, the Slovak Republic, Hungary, Sweden, Bulgaria, and Switzerland.

Conclusion

In addition to the OECD's work on management systems of corporate governance, supplying guidelines for ethical multinational conduct and providing leadership in combating bribery, this organization has also taken other steps to address the issues of international corporate responsibility in general. Among the many publications that the OECD furnishes each year, it has recently published "Corporate Responsibility: Private Initiatives and Public Goals," and this can serve as just one representative example of the work that the OECD does in this area. Attempting to clearly define what practices constitute corporate responsibility, this work on international business ethics topics takes place at the OECD through the Investment Committee of the Directorate for Financial and Enterprise Affairs. In summary, then, it can be said that what seems to make the OECD an international super organization is the expertise it is willing to expend on many important matters that have a bearing on economic development. By paying close attention to how businesses conduct themselves and their impact on society, the OECD demonstrates that its horizons are broad and broad enough for it to be called an international super organization.

—Peter Madsen

See also Corporate Governance; Corruption; Developing World; Directors, Corporate; Enron Corporation; Foreign Corrupt Practices Act of 1977 (FCPA); International Business Ethics; International Trade; Multinational Corporations (MNCs); Parmalat; WorldCom

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Organizational Moral Distress

Organizational moral distress is an extension of the concept of individual moral distress. Moral distress at the individual level is the anguish a person may experience when he or she is convinced he or she knows the right thing to do but is prevented from doing it. When applied at the level of organizations, it is a useful way to characterize and analyze conflicts or misalignment of values that can interfere with excellent organization function.

Organizations, like people, have goals and values. Organizations meet their goals by employing people to fill various roles, to take on responsibilities, and to function within the processes and systems that the organization creates. How the organization prioritizes its goals, how it designs its systems, structures, or processes to meet them, and whom it chooses to employ are a reflection of its values.

The values of an organization are generally stated in mission or vision statements and are sometimes referred to as "core values." These statements articulate the values the organization says it endorses. They are the values that the organization says it expects all its employees, including its leadership, to abide by. Moreover, these values can be perceived as a standard by which the organization can be judged. We judge individuals on whether or not they consistently live up to the values they say they endorse. So too we judge organizations on whether or not they consistently live up to the values they say they endorse.

Moral distress can arise when the organization says it values something other than what it actually values, or when the people it employs do not share the same values as the organization, or when the organization's internal stakeholders prioritize similar values differently. For instance, an organization might say that it values the quality of its product or service more than it does cost. But if the design of its processes produces outcomes that are very inexpensive, but of poor quality, then there may be a misalignment of values between what the organization says it values and what it actually values. Similarly, if an organization employs persons with radically different values or persons who share the same values but prioritize them differently, then there may be a misalignment of values between the organization and the people it has chosen to help fulfill its goals. An organization that values individual competitiveness and aggressiveness might find itself at odds with an individual whose highest priority is family time. Similarly, individuals who value competitiveness and aggressiveness would find themselves ill placed in roles that required teamwork and cooperation. Or leaders of different organizational divisions or with different responsibilities within the organization may have responsibilities that reflect different values, or that require prioritizing shared values differently. For instance, an organization might value both price and safety of a product or service, but a marketing function might value price over safety while an engineering function might value safety over price. In each instance, the situation is characterized by a values misalignment, and in each instance, the potential exists for organizational moral distress to arise.

Organizations operate in a context, the larger social environment, which can prevent them from doing what they perceive as the right thing to do. For instance, an organization might believe that it is in its best interests, as well as society's best interests, to pursue a certain type of research or product development but be prevented from doing so by legal or regulatory requirements. A good example of this is the refusal of the government to fund research associated with certain stem cell lines, resulting in individual and organizational dislocation. In these cases, the values within the organization may be in perfect alignment, with the obstacles to expressing these values being external to the organization.

Once organization moral distress develops from any of these possible misalignments of values, it can cause dislocations elsewhere. For instance, if organization leaders prioritize different values, they could inadvertently create processes that reflect these different values. Conflict is inevitable, and one form of organization moral distress can lead to another. Thus, in practice it may be hard to determine in an organization in distress where to look first for the misalignment of values.

Values misalignments are important because if they are not identified and corrected, the organization and its stakeholders will suffer. At best the organization's stakeholders will suffer confusion; at worst, organization moral distress might result in the organization's demise. Consider the expectations of customers and employees of an organization that says that it values quality over cost but that in fact does not. Customers might have expectations of the product or service that are unrealistic, and employees might be confused as to the decisions that they ought to make. Unrealistic expectations among customers might irretrievably harm market share, and confusion among employees might lead to conflict.

Or consider a situation in which employees' values are not similar to organization values. In this example, the organization expects employees to make decisions or pursue activities based on the values it endorses. If those decisions or activities are not forthcoming from employees, conflict will be inevitable. In this case, conflict might take the form of a strike or termination of certain employees. We can make the reasonable assumption that in all these situations morale is bad, that productivity is affected, and that the organization will be hurt in some way.

How does an organization prevent or cure organization moral distress? The mission and values of the organization often reflect the views of organization leadership, so it will be up to organization leadership to prevent or cure organization moral distress. Organization leaders may not be able to avoid distress that arises from the external environment, but they can prevent, mitigate, or cure organization moral distress arising from internal causes by revisiting the mission of the organization and the values that the organization says it endorses. In the same way that individuals ask whether or not they are living up to the values they say they endorse, organization leaders can ask if the organization is living up to the values it says it endorses. Organization leadership can take steps to reinforce the desired mission and values of the organization by aligning and embedding them in the strategies, processes, structures, and systems that the organization uses to fulfill its goals. Organization leaders should be clear about the organization's mission and values and communicate them to internal and external stakeholders. In this way, the organization leaders can seek to minimize gaps between what the organization does, what it says it wants to do, and how it does it. This is not a simple process, nor will it be effective if leaders of an organization do not share the same values and prioritize them similarly.

Organization moral distress results from a "values misalignment" and can take several forms, although they may easily implicate each other. Because organizations evolve over time and because organization moral distress can damage the organization, ongoing monitoring of values alignment within the organization and of the organization with its environment is critical. Preventing organization moral distress from occurring is best, but if it is already present, it needs to be identified, as a first step to curing it.

—Ann E. Mills, Mary V. Rorty, and Patricia H. Werhane

See also Corporate Ethics and Compliance Programs; Corporate Governance; Ethical Culture and Climate; Ethical Decision Making; Federal Sentencing Guidelines; Leadership; Management, Ethics of; Missions and Mission Statements; Moral Distress; Moral Imagination; Moral

Leadership; Role Model; Stakeholder Theory; Strategy and Ethics; Values, Personal; Virtue and Leadership

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Organization of Petroleum Exporting Countries (OPEC)

The Organization of Petroleum Exporting Countries (OPEC) was formally established in 1960 by Venezuela, Iran, Kuwait, Iraq, and Saudi Arabia at a conference in Baghdad. OPEC, which currently does not include Iraq, also includes Algeria, Indonesia, Libya, Nigeria, Qatar, and the United Arab Emirates, and since 1965 has been headquartered in Vienna, where it conducts its semiannual OPEC conferences. The 11 members produce 40% of the world's oil supply today, and, more important, they jointly hold 78% of the world's proven crude oil reserves (2003 estimates).

OPEC is a cartel whose principal objectives are to coordinate petroleum policies in the best interests of member countries, to stabilize prices, to provide a regular supply to consumer nations, and to provide a fair return on capital to investors. With these aims in mind, the oil ministers of the member countries meet at least twice per year to discuss policy and to allocate per-country supply quotas that are based on demand forecasts.

The exploration for oil and its drilling, production, transportation, refining, marketing, and distribution have historically been the concentrated activity of a few powerful global companies, at the head of which have been the "Seven Sisters" consisting of the three American Standard Oil companies, Texaco, Gulf, Royal Dutch Shell, and British Petroleum. On the other hand, the production of oil is dominated by relatively young nations, many of which made the transition from Western colonies to sovereign entities after the end of World War I and historically have had little international clout or bargaining power to apply when dealing with Western powers and their multinationals. It is the need to address this imbalance of power that OPEC members use as justification for their collusion in manipulating the world's oil supply.

Oil Prices

The nominal (unadjusted for inflation) price of oil went virtually unchanged from 1950 to 1972, settling at around $2 per barrel. With the oil embargo of 1973, the price suffered its first sharp hike since the end of World War II: Prices soared when OPEC member countries refused to ship oil to those countries that had supported Israel against Egypt and Syria during the Yom Kippur War. By the end of 1974, the price of crude reached $10 per barrel and helped unchain a cycle of inflation and unemployment (stagflation) in developed countries that had relied on cheap oil for decades. The next sharp rise in prices occurred when Iran significantly decreased its flow of oil following its 1979 revolution and subsequent war with Iraq. At the time the Shah left power Iran produced 6 million barrels of oil (about 20% of OPEC exports) per day, but by the end of 1980 the combined production of Iran and Iraq was in the neighborhood of just 1 million barrels.

In the mid-1980s, the price of oil began a precipitous decline: Not only did the nominal price of oil fall sharply, but by 1999 the real price (adjusted for inflation) returned to historically low levels. This drop in the price was caused by several elements, including overproduction by Saudi Arabia, which was in need of cash (to meet its obligation to fund the allies against

Iraq in 1991), the recession in Japan, and the peak of oil production from the North Sea.

OPEC's Impact

Oil provides energy and is also a fundamental raw material in many industries. As its cost rises, so does the cost of manufactured and agricultural products. Sharp price fluctuations affect the standard of living worldwide, most dramatically in those countries that both are net importers of goods and can count on few or no oil reserves of their own. Therefore, OPEC's ability to alter the supply is not taken lightly by most countries. Members of the United States Senate, for example, have argued that by acting as a cartel, OPEC fixes prices and as such violates the Sherman Antitrust Act—extended internationally—and have suggested taking corresponding suits to the International Court of Justice.

In defending itself, and after having weathered the crises of the last three decades of the 20th century, OPEC currently takes a less politicized approach to managing the supply and emphasizes that despite the significant increases in the nominal price of oil that began in 2000, the real price is still considerably below what it was as it peaked in the 1970s and 1980s. OPEC argues that oil as a raw material is not replaceable and that member countries must be permitted to generate adequate income for capitalization in other industries for long-term development that is independent of the oil industry. In justifying price increases, the OPEC countries directly link the purchasing power of generated revenue to its nominal worth; this is an argument that has become stronger in recent years when the dollar fell significantly relative to other hard currencies (the euro in particular). OPEC also argues that as a cartel, its aim is not to maximize revenue, but rather to ensure price stability and prevent volatility in oil prices. When charged with profiteering, OPEC also emphasizes that since 1976 it has helped many developing nations through its Fund for International Development, which has transferred some windfall profits to poor nations. It is also fair to point out that most short-term windfall profits from price increases don't necessarily increase revenue for OPEC members since their supply is typically presold in the futures markets; it is the traders who, in buying low and selling high to allocate their inventory, are the beneficiaries of sudden price fluctuations.

The Future

The new millennium saw a new dynamic in oil prices, which have steadily risen since 2000 as a result of geopolitical issues, including the War on Terror and the rise of China and India as rapidly growing economies. The war in Iraq and concerns about the stability of other Middle Eastern oil producing countries have contributed to a jittery market for oil, while the rapid growth in demand, especially from India and China, has pushed OPEC close to the limits of its current production capacity. Overlaying these issues are rising concerns for the environment and global warming and the increasing gap between rich and poor nations that is exacerbated by high oil prices. These considerations will tend to propel an increasingly serious search for alternative sources of energy, and OPEC will be challenged to find a balance between meeting rising demand over the near term and the specter of substantial oil independence by its current customers in the future.

—Sousan Urroz-Korori

See also Antitrust Laws; Boycotts; Cartels; International Business Ethics; International Trade; Multinational Corporations (MNCs); Natural Resources; World Resources Institute (WRI)

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Other-Regardingness

Other-regardingness concerns acts and virtues focused on benefiting other people rather than oneself. In its most narrow formulation, other-regardingness primarily means not harming other people (nonmaleficence). Its wider formulations also require the agent to consider, and be accountable for, the various positive and negative impacts of his or her actions on others. Its application also varies in that many ethical frameworks require giving equal weight to the interests of all people affected by one's actions, while other versions will give priority to particular others, such as family, friends, or fellow citizens. Other-regardingness is a key component of common morality and also major ethical theories such as deontology, utilitarianism, and virtue.

Besides concern for actions that affect others, other-regardingness can also refer to traits of character. Some virtues are considered to be other-regarding, while others are considered to be self-regarding, depending on whether the virtue concerns dispositions that focus on interaction with others or only on the self. Other-regarding virtues include benevolence, generosity, justice, and honesty. These virtues are often considered to be morally superior to the self-regarding virtues, such as courage, prudence, and temperance, because morality primarily concerns others.

Other-regardingness and self-regardingness are not necessarily mutually exclusive categories, however. While some philosophers contend that moral actions must strictly focus on the good of others and not at all on oneself, many philosophers find a convergence. Kant, for example, claims that certain self-regarding acts are moral duties because they are based on proper self-respect and provide the foundation for performing the rest of our moral duties, and several philosophers note that actions can have multiple motives and effects, serving the interests of both self and others. For them, pure other-regardingness is not required for moral action. Similarly, self-regarding virtues can serve the interests of others, and not focus strictly on the agent's interests and character. For example, courage can enable the agent to face danger for the sake of others, in addition to serving the agent's interests and preserving his or her integrity. While other-regardingness may sometimes require self-sacrifice, it is not necessarily equivalent to altruism. Other-regardingness does not even necessarily entail equal consideration of self and others, but only that others must be taken into account in some way.

Besides its role in common morality and ethical theory, other-regardingness also figures prominently in empirical descriptions of humanity. While some accounts describe humanity as primarily or even exclusively egoistic (e.g., as with the concept *homo economicus*), most scholars contend that other-regardingness is part of human nature. Whether that concern is a product of cultural or biological evolution, or some combination of the two, remains in dispute.

In business, the traditional focus has been on the self-interest of individuals and corporations. The role of other-regardingness was disputed, except insofar as it pertained to concern for stockholders and their financial interests. The business ethics, corporate social responsibility, and stakeholder movements have all contributed to a broader understanding of other-regardingness in the business context, and the need to take the interests of others into account as a regular part of business decision making.

—George D. Randels Jr.

See also Altruism; Corporate Social Responsibility (CSR) and Corporate Social Performance (CSP); Egoism; Kantian Ethics; Self-Regardingness; Stakeholder Theory; Virtue

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Ought Implies Can

The principle "ought implies can" asserts, roughly, that an agent ought to do something only if it is possible for that agent to do it. In other words, it's being possible for an agent to perform a certain action is a necessary condition on that agent's having an obligation to perform that action. In this way, the principle "ought implies can" is fruitfully understood not as a moral principle itself, but as a principle to which ethical theories must adhere. That is, for a candidate ethical theory or moral principle to be justifiable, it must not violate the principle that ought implies can; it must not require that agents perform actions they simply cannot perform. In this way, the principle itself recognizes that ethics is concerned with action, not simply with positing theoretical ideals in accordance with which no human agent can act.

Beginning with Immanuel Kant, most moral philosophers have found some version of this principle to be intuitively obvious, even if only because its denial gives rise to apparent absurdities. For example, to deny that ought implies can is to suggest that an agent (alone) could currently have an obligation to eradicate global poverty, even though that agent has no means currently available to do so. As Kant saw it, for the moral law to have any force over human agents, it must be possible for those agents to act in accordance with the duties that arise out of the moral law.

This principle is also useful in identifying unreasonable calls for businesses to reform their practices, such as demands that automakers radically (and immediately) decrease emissions and increase fuel efficiency, even when the necessary technology is not available. It might even be the case that, were the necessary technology available, nonetheless the demand could not reasonably be met; the implementation of the technology might be prohibitively expensive, forcing the automakers to ignore their prior obligations to shareholders (e.g., to provide a reasonable return on their investment) or to consumers (e.g., to provide goods and services at a fair price).

As the preceding example illustrates, for all its intuitive appeal, there are difficulties in identifying the relevant sense of "can" in the "ought implies can" principle. There are at least two leading candidates: (1) what the currently available (to the agent) resources and other means make possible and (2) what the laws of nature allow.

The first of these seems to be the operative sense of "can" when it is claimed, for example, that an individual agent has no moral obligation to repay a debt, absent the resources for doing so. This version, however, seems to ignore prior acts and/or omissions that make the current lack of resources itself morally blameworthy and insufficient to suspend the obligation to repay. Thus, even though the debtor currently is not able to repay the debt, it might nonetheless make sense to blame—and even punish—the debtor for the failure to fulfill the obligation to repay. Doing so would acknowledge that there were actions the debtor could have performed since incurring the debt that would have made repaying the debt now possible. (To return to the previous example, it might be that automakers are partly to blame for the lack of currently available, reasonably priced technologies that can control emissions and increase fuel efficiency. Perhaps they ought to have been pursuing such technology more aggressively before now.)

Understanding "can" as a function of the laws of nature recognizes that moral agents are limited in what they can do by facts about how the world works. Thus, given that no (unaided) person can leap to the top of a 20-story building in a single bound, it simply can never be the case that morality demands that a person do so.

An interesting subset of the laws of nature that would seem to have important implications for the identification of our moral obligations are laws of human psychology. Psychological egoists, for example, claim that all human action must arise from some consideration of the well-being of the agent. Thus, according to this theory, no altruistic actions (i.e., actions done exclusively for the sake of the well-being of those other than the agent) are psychologically possible, and so they cannot be morally obligatory.

—David Levy

See also Altruism; Dilemmas, Ethical; Egoism; Kantian Ethics; Motives and Self-Interest; Utilitarianism

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OUTSOURCING

Outsourcing may be defined as the practice of transferring production or services that were once performed in-house to an external source. The outsourcing organization is most commonly a for-profit enterprise, although governmental agencies are increasingly outsourcing services. Global offshoring refers to the practice of sourcing production or services to multiple offshore locations. While labor savings can be substantial, improvements in efficiency, productivity, and quality drive much of the demand for highly skilled, offshore workers. Typically, such globalizing strategies enable multinational corporations (MNCs) to meet increased demand and offer goods and services to customers at lower prices while enhancing profits.

Ethical issues regarding global outsourcing may be usefully separated into public policy questions concerning the establishment of a just regulatory policy and questions regarding the ethical management of outsourcing by organizations. This entry focuses primarily on the obligations of managers of for-profit enterprises regarding global outsourcing. Ethical issues regarding global outsourcing may be usefully divided between the treatment of domestic, or onshore, workers whose jobs are eliminated and the treatment of the offshore workers who are hired to replace them.

The offshore outsourcing of jobs is not ethically objectionable in and of itself. However, it is unethical if either the domestic workers who are laid off are treated as mere disposable tools, unworthy of dignity and respect, or if the workers who replace them in global supply chains are so treated. In cases where neither is the case, legal outsourcing is normally ethically permissible.

The Public Policy Dimension

In democracies, just corporate-governmental relations are reciprocal. Corporations exist because of the will of the people expressed via their elected representatives. Corporations enjoy a variety of privileges grounded in the political, economic, regulatory, and military power of the nation in which they are based. In the United States, for example, corporations enjoy benefits such as transportation infrastructure, police and judicial systems that protect corporate property rights, coercive military and economic influence, and representation in international trade negotiations. In return, public policy makers in the U.S. tax corporations require that they meet specific regulatory requirements. Ethical corporations meet these regulatory demands and refrain from coercing lawmakers into modifying such regulations.

Lawmakers who believe that MNCs have an ethical obligation to retain a specific percentage of domestic employees, to provide employees with severance packages when terminated, to provide employees with advance notice of termination, or to provide any other specific benefit to employees have the power to enact such legislation. When MNCs, or their representatives, exert coercive influence over lawmakers to prevent the enactment or enforcement of such laws, they undermine a core principle of modern democracy. This is the egalitarian principle that each citizen is entitled to one and only one vote. This principle makes it morally unacceptable for corporations to exert ideological and political power via the deployment of economic resources in ways that undermine the ability of individuals to make freely determined judgments about how best to govern themselves. However, MNCs can play a constructive and ethically permissible role regarding the creation of corporate law and labor law by providing lawmakers with information regarding the likely implications of that legislation for their business.

Onshore Corporate Obligations

The prima facie case for outsourcing is that it will improve shareholder wealth via increased profits and provide much needed jobs to workers in developing nations. Much of the controversy regarding outsourcing concerns the displacement of onshore, or domestic, workers. Critics of outsourcing argue that domestic workers are unfairly treated when their jobs are eliminated and tasks previously completed in the United States are sent offshore. In reply, supporters of outsourcing typically argue that no one in the United States has a moral right to a specific job. Furthermore, they argue that the doctrine of employment at will provides not merely a legal basis, but a moral basis, for the termination of expensive U.S. labor in favor of equally skilled, less expensive, and more efficient offshore labor. The doctrine of employment at will holds that, barring a contract that stipulates otherwise and excluding certain legal restrictions, employees may be hired or fired at will. By giving both employees and employers the opportunity to exit an employment relationship “at will,” this doctrine enhances efficiencies in labor markets and promotes the overall welfare of communities.

Patricia Werhane and Tara Radin develop a series of objections to the doctrine of employment at will that it will be useful to consider. They ground these criticisms in the claim that employees have a proprietary right to the fruits of their labor. From this proprietary interest, they derive three specific objections to the doctrine of employment at will. First, employees are entitled to be treated with respect by their employers. So, for example, employees are required to be given reasons that explain the actions of employers when employees are terminated. Second, the arbitrary treatment of employees by employers is said to be illegitimate because employees do not have the same prerogative. Thus, employers have an ethical obligation to refrain from terminating employees without explanation or for capricious reasons. Third, the relationships between employees and employers are required to be reciprocal. Thus, if there is an expectation of loyalty, trust, and respect on the part of employees toward employers, then employers must also exhibit loyalty, trust, and respect toward employees. As we have seen, Werhane and Radin ground these obligations in the proprietary rights of the employees. However, it is not clear how a worker's proprietary right to the product of his or her work entails any obligations on the part of an employer other than that of providing the agreed-on wages and benefits (if any) in exchange for the product of the employee's work. There is an alternative strategy that provides a basis for the claim that employers have duties to treat workers with respect, to treat them in a nonarbitrary manner, and to regard their relationship with employees as reciprocal. These duties may be grounded in the Kantian idea of respect for persons. To fully respect a person, one must actively treat his or her humanity as an end, and not merely as a means to an end. This means that it is impermissible to treat persons like disposable tools. The Kantian basis for this claim is well established.

Employment is of critical importance to the well-being and self-respect of persons. Nonetheless, it is difficult to imagine how an employer's duty to respect employees could entail a duty to refrain from firing them. However, Denis Arnold has argued that the duty to respect onshore employees *does* entail specific duties to at-will employees whose jobs are being outsourced overseas. First, there is an obligation to provide employees with appropriate notice regarding the elimination of their position. There is no clear formula for determining how much notice is appropriate. However, it is reasonable to maintain that loyal, diligent employees should be given advance notice of the elimination of their positions proportionately to the amount of time that they have been in service to their employers.

The second specific duty defended by Arnold of corporate managers to employees whose jobs have been outsourced concerns the long-term well-being of employees. Defenders of offshore outsourcing typically argue that domestic labor markets can accommodate displaced workers. Arnold points out that it is often the case that displaced workers are ignorant of high-demand areas of employment and that they are unqualified for those jobs. He argues that employers ought to provide significant guidance regarding job retraining to laid-off employees, both while they are still being paid by the corporation and afterward. Loyal, diligent employees should be given financial support for their retraining proportionately to the amount of time that they have been in service to their employers. In this way, employers properly reciprocate the loyalty and diligence of their employees.

Offshore Corporate Obligations

The offshore outsourcing of jobs may be ethically objectionable, even if the domestic workers who lose their jobs are treated with dignity and respect. It is ethically objectionable when the workers who are hired to replace the domestic workers, whether hired directly by the MNC or indirectly via a contractor, are treated disrespectfully in the interest of reducing labor costs. Arnold and Bowie and Arnold and Hartman have argued that on Kantian grounds MNC managers have duties in their offshore manufacturing facilities to respect the basic dignity of workers. In particular, they have argued that MNCs have duties to meet minimum safety standards, pay a carefully defined living wage, and adhere local labor laws.

Some MNCs, such as Motorola and Levi Strauss, have always sought to treat workers in their global supply chains with respect. Other MNCs, such as Adidas and Mattel, put in place policies and procedures to ensure the dignified treatment of workers more recently. Nonetheless, many MNCs continue to pay little attention to the welfare of workers in offshore factories. Such workers are, for example, frequently required to endure unsafe working conditions. Workplace hazards include exposure to toxic chemicals, exposure to airborne pollutants, noise pollution, malfunctioning machinery, and fire hazards. These hazards are attributable to a lack of appropriate safety equipment, poor or very harsh working conditions, and more generally to a lack of concern for the physical well-being of workers. These conditions frequently result in neurological damage, lung disease, and the loss of body parts such as fingers or arms.

Frequently, improvements in working conditions may be put in place for little cost. For example, at the suggestion of an employee at a large Nike factory in Vietnam, rubber scraps were used to deaden the sound of metal presses, thus significantly reducing noise pollution. However, MNCs and their contractors must sometimes expend considerable sums to provide improvements such as industrial quality exhaust systems, plumbing to provide water for the comfort use of workers, appropriate equipment for handling toxic chemicals, and health clinics for large factories. Many MNCs have accepted the cost of improving working conditions in their global factories as a necessary business expense. For example, in 1997, Mattel announced the creation of a global code of conduct for its production facilities and contract manufacturers. It has spent millions of dollars to upgrade its manufacturing facilities to improve worker safety and comfort. Furthermore, it has invited a team of academics to monitor its progress in complying with its self-imposed standards and to make their findings public.

One of the most controversial issues concerning global outsourcing is that involving wages and benefits. For services that require employees to have a college education, such call center technical support operators in India or China, the wages paid to employees often allow those employees to enjoy a middle-class lifestyle while earning a fraction of the wage formerly paid to U.S. or Canadian workers. However, factory workers typically earn much less than service workers and are among the most poorly paid employees in global supply chains. Arnold and Bowie have provided a Kantian defense of the claim that MNC managers and their contractors have a moral obligation to provide a living wage to employees working a 48-hour workweek, and they have provided a country-specific method for determining what that wage should be. They argue that for workers to be respected, MNCs must ensure that such a wage is paid even if the legally mandated minimum wage is less than this. In cases where the legally mandated wage is higher, they argue that paying that wage is sufficient.

It remains commonplace for MNCs, or contract factories over which they exhibit considerable influence, to violate local labor laws. Consider, for example, local labor laws relating to wages and benefits, forced overtime, health and safety, child labor, sexual harassment, collective bargaining, and discrimination. Typically, these laws are violated in the interest of economic efficiency, often with the knowledge of local authorities. Such violations of the law are typically permitted by local government authorities to prevent the MNC factory from shutting down and moving elsewhere. Many MNCs have yet to embrace a respect for the rule of law in those nations where their products are manufactured. Indeed, many government officials in the nations that host factories remain convinced that aggressive enforcement of existing labor laws will simply cause the factory to shut down and later reopen outside their jurisdiction.

Arnold and Bowie and Arnold and Hartman argue that the violation of host nation laws by MNCs and their contract factories, especially those that are not proactively seeking to ensure compliance, should be condemned. They argue that such violations are hypocritical in that MNCs rely on the rule of law to ensure, among other things, that their contracts are fulfilled, that their physical property is secure, and that their intellectual property rights are protected. They conclude that it is inconsistent for an MNC to demand that its own legal rights be protected while at the same time it violates the legal rights of others.

In response to these claims, some argue that local labor laws are cumbersome and expensive and that MNCs have good reason to seek out host nations where laws are not enforced or where there are few laws protecting workers. Furthermore, it is argued that any money spent to improve the working conditions of workers constitutes a sort of theft from shareholders. By seeking out the cheapest possible voluntary labor and by avoiding or ignoring local labor laws, it is argued, MNCs maximize profits and are thus in a better position to reward shareholders and executives.

—Denis G. Arnold

See also Coercion; Dignity; Employee Protection and Workplace Safety Legislation; Employee Rights Movement; Employment Contracts; Kantian Ethics; Sweatshops

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Ozone Depletion

Ozone is a relatively unstable form of molecular oxygen containing three oxygen atoms (0_3). Ozone near the earth's surface is the most noxious component of smog that is treated as an air pollutant in most industrial countries. The ozone layer in the stratosphere, however, shields the earth from ultraviolet radiation that is harmful to living organisms. This radiation comes from the sun, and too much of it can damage plant and animal cells, cause skin cancer and eye cataracts in humans, reduce crop yields, deplete marine fisheries, cause damage to materials of various kinds, and kill many smaller and more sensitive organisms.

Stratospheric ozone is found in a broad band, generally extending from about 15 to 35 km (9–22 miles) above the earth's surface. The amount and distribution of stratospheric ozone varies around the earth, but in general the layer of ozone is relatively thin when compared with the thickness of the stratosphere. Ozone is produced when upper-atmosphere oxygen molecules (0_2) are broken apart by ultraviolet light. Most of these freed oxygen atoms bond with ordinary oxygen molecules to form ozone. This ozone creation process is constantly at work producing more ozone.

However, ozone can also be destroyed by chemicals that react with it directly. One such destroyer was identified in 1974 by Molina and Rowland, two chemists at the University of California at Irvine, who theorized that chlorofluorocarbons (CFCs) could eventually drift up to the stratosphere to react chemically with ozone molecules in a destructive fashion. When CFCs reach the stratosphere, they are finally broken down by ultraviolet radiation to release chlorine atoms that act as a catalyst in a series of reactions that convert ozone into oxygen.

Because chlorine acts as a catalyst rather than as a reagent, a single molecule of chlorine can destroy thousands of ozone molecules before it eventually gets washed out of the atmosphere. CFCs can take as long as 6 to 8 years to reach the stratosphere to do their damage.

When first discovered, CFCs proved to be remarkable compounds with many uses. Since they were inert, they did not react with other chemicals with which they were mixed. They were neither toxic nor flammable at ground level. After their initial discovery, the number of CFC compounds grew quickly into the dozens and were used as a universal coolant; as a blowing agent in rigid insulation forms; as an aerosol propellant; as a solvent to remove glue, grease, and soldering residues from microchips and other electronic products; and as a component of foam packaging containers.

When Molina and Rowland first developed their theory, empirical validation was unavailable because of the difficulties involved in measuring actual levels of stratospheric ozone. No international action was taken to limit CFC usage until the discovery of the ozone hole over Antarctica. The British Antarctic survey conducted in 1983 found that concentrations of ozone in the stratosphere were dropping over Antarctica at a dramatic rate each austral spring to be replenished again by the end of the fall season. This discovery led to a $10 million scientific mission carried out by the United States under the combined sponsorship of NASA, the National Oceanic and Atmospheric Administration, and the Chemical Manufacturers Association to find out more about this phenomenon. By the spring of 1987, the average ozone concentration over the South Pole was discovered to be down about 50%, and in isolated spots it had actually disappeared entirely. Subsequent research showed that the ozone layer around the world was changing far more rapidly and in a different pattern than any model had predicted.

While the role of CFCs in ozone depletion had been hotly contested after the theory was first formulated in 1974, it didn't take long for these findings to be widely accepted and action taken. On September 16, 1987, after years of debate and heated negotiation, the Montreal Protocol on Substances that Deplete the Ozone Layer was signed by 24 countries, and by mid-November of 1988, that total had increased to 35 countries. The agreement included a freeze on CFC production at the 1986 levels starting in 1992, with extended deadlines for some countries, allowances to accommodate industry restructuring, and loose definitions of products that legitimately could be traded internationally. Developing countries were given a 10-year grace period past the deadline during which CFC production could be increased to meet basic domestic needs.

The cumulative effect of these loopholes meant that even with widespread participation, the protocol's goals of halving CFC use by 1998 would not be attained. Projections showed that if industrialized countries phased out CFCs as scheduled, but the developing countries did not go along, the use of CFCs by these countries would soar from 15% to 50% by the end of the century, which would leave chlorine levels slightly above the current level even with reductions by developed countries. Thus in June 1990, representatives from 75 countries met in London to sign an accord that strengthened provisions of the treaty. This accord called for eliminating CFC usage worldwide in a decade, setting up an international fund of $200 billion to help less developed countries subsidize purchase of CFC substitutes, and building new plants to produce refrigerators and other products that use CFC substitutes.

In 1989, the U.S. Congress enacted an excise tax on ozone-depleting chemicals that it hoped would discourage their use and encourage an expedited search for safe substitutes. In February 1992, President George H. W. Bush announced a speedup in the phaseout of ozone-destroying chemicals by U.S. manufacturers. Responding to a report from NASA that chlorine monoxide had reached record levels over Canada, the United States, and Europe, the president said that the United States would phase out production of ozone-destroying chemicals by the end of 1995, 5 years earlier than agreed on in the international treaty.

The net effect of these actions was to reduce the levels of ozone-depleting substances in the atmosphere. Based on measurements of inorganic chlorine in the atmosphere, which stopped increasing in 1997 and 1998, stratospheric chlorine levels were thought to have peaked and were no longer increasing. The natural ozone production process was expected to heal the ozone layer, and ozone concentrations in the stratosphere were expected to recover in about 50 years. However, in the winter of 2004 to 2005, ozone declined in the upper atmosphere over the Arctic region more precipitously than ever before, stunning scientists. Some of this decrease was attributed to violent storms on the sun's surface and bitter cold temperatures rarely seen in the Arctic, in addition to man-made chemicals.

—Rogene A. Buchholz

See also Environmentalism; Environmental Protection Legislation and Regulation; Global Business Environments

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P

Pareto, Vilfredo (1848–1923)

Vilfredo Federico Damaso Pareto was a famed economist and sociologist. He is best known for the economic concept of Pareto efficiency (or Pareto optimality). He made other wide-ranging contributions to economics that since the late 1930s have greatly influenced modern conceptions of demand, welfare, and planning. Pareto's law asserts that distribution of income and wealth follows a regular logarithmic formula. (Pareto charts are a standard statistics display tool.) He also made important contributions to sociology and moral philosophy.

Vilfredo was the only son of a nobleman, who was living in Paris in exile from Genoa for his nationalist views, and a Frenchwoman. The family returned to Italy, where the elder Pareto worked as an engineer. He made a comfortable living raising his family in a middle-class environment, providing many advantages to the young Vilfredo.

Pareto was educated in both France and Italy, graduating at the top of his class in civil engineering in 1870 from the Istituto Politecnico of Turin. Mathematical training and ideas of mechanical equilibrium shaped his contributions to economics. An ardent advocate for free enterprise and free trade, against state subsidies or protection for industry, and against militarism, the strong-willed and self-confident Pareto made his views known in writing and in public lectures that offended political leaders and sometimes led to police action.

From the early 1870s, he worked in Italy as a civil engineer, including being a director of two railway companies, and as a deputy manager and then a director with an iron company. He resigned in 1890 to conduct independent research. He had also lost a large sum speculating on iron in the London markets.

He inherited but never used his father's title of *marchese* (marquis). In 1889, Pareto married a Russian. This marriage broke down 12 years later when his wife left him. In 1902, Pareto met a Frenchwoman, and the two lived devotedly together, marrying shortly before Pareto's death in 1923. Pareto changed citizenship to the city-state of Fiume to divorce his first wife.

The important Italian economist Maffeo Pantaleoni (1857–1924) met Pareto in 1890 and, noting Pareto's interest in applying mathematics to economics, suggested that he study the work of Léon Walras (1834–1910). Pareto and Walras met. Pareto then published a series of theoretical articles applying mathematics to the analysis of economic policies, featuring Walras's general equilibrium approach. These articles and Pantaleoni's strong recommendation led to Walras's decision that Pareto succeed him in the chair of political economy at the University of Lausanne (Switzerland) in 1893.

Pareto's major works in economics, *Cours d'économie politique* and *Manuale di economia politica*, helped develop the Walrasian approach. Subsequently, Pareto concentrated on sociology and had his chair broadened to political and social studies. After his retirement, *Trattato di sociologia generale* and other sociological works appeared. Pareto argued that eternal class struggle is a circulation of power elites promoting sham ideologies.

Pareto later changed his view on free trade. He argued that social planners, aided by a Walrasian model of the economy, could be as efficient as unfettered markets. His belief in democratic liberalism had faded. Although the Fascists invoked his name as intellectual camouflage, Pareto was disdainful of Mussolini's movement and declined many proffered Fascist honors.

—David L. Hammes

See also Economic Efficiency; Pareto Efficiency; Unemployment; Welfare Economics

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PARETO EFFICIENCY

One of the hardiest and most widely cited results in all of economics, Pareto efficiency, was developed by Vilfredo Pareto in "The Maximum of Utility Given by Free Competition," an article published in *Giornale degli Economisti* in 1894, and his *Manuale d'economia politica*, first published in 1906 and revised and translated into French in 1909. Pareto proposed that an allocation or distribution of goods was efficient or optimal if, once attained, any move away from it could not make anyone better off without at the same time making at least one other person worse off. Allocations that are not Pareto optimal allow for redistributions that make at least one person better off while making no one else worse off.

Consideration of Pareto efficiency, the Pareto process, and other associated terms and concepts constitutes a large part of modern welfare economics, the branch of economics devoted to the study of the distribution and allocation of goods and services.

Pareto developed his approach in response to the utilitarian Benthamite "calculus," which was premised on the view that utility was cardinally measurable and comparable across individuals. The view that utility is both cardinally and interpersonally measurable implies, among other things, that social policies can be designed for redistribution of goods leading to the utilitarian goal or ethic of the "greatest good for the greatest number." According to this view, policy makers may calculate the net aggregate utility increase or decrease of any policy change, with policy changes leading to greater increases in net utility being preferred even though some individuals may be absolutely worse off after the change.

Considering the possibility that policy changes would cause some to sacrifice for others led to a focus on the equity or fairness of such changes. For example, who decides who gains and who loses and how much each person or group gains or loses? This requires some socially accepted ethical rule beyond Bentham's "greatest good for the greatest number." This new rule itself—whatever it might be—represents a change in policy and thus is subject to the same focus on equity. Solving this requires a socially acceptable metarule on rule changes, and the infinite regress nature of the problem reveals itself.

Also, from the 1880s onward, it was noted that for the "felicific calculus" of Bentham to work, everyone would have to have identical utility functions in income, which is a special and limiting assumption. Identical utility functions in income imply that the social optimum is one of uniform, or equal, income distribution, where each individual assigns the same utility value to his or her last dollar's worth of income. It is not the equal distribution outcome that is being criticized but the restrictive assumption on utility that produces it.

Once cardinal utility was abandoned, the search was on for a new criterion for judging the efficiency of policies. The inability to make interpersonal utility comparisons means that a simple summing up of individual utilities into one number is impossible. Yet without knowing by how much "losers" lose relative to how much "winners" gain from any policy change, measuring the impact of a policy and hence finding a social optimum (or utility *optimum optimorum*) becomes extremely challenging.

Pareto—heavily influenced by the work and goals of Léon Walras—believed that he had solved this conundrum in the context of a perfectly competitive general equilibrium model by proposing the rule that a social optimum is an allocation of goods that cannot be changed to make anyone better off without at the same time making someone else absolutely worse off.

Such a state is said to be *Pareto efficient* (or Pareto optimal).

In the *Pareto process,* the move to a Pareto-efficient allocation driven by autonomous individuals voluntarily making utility-improving trades, there simply are no losers as no potential loser would have to agree to a distribution in which he or she would be made worse off. In this process, the individual is at the locus of decision making, and each individual is assumed to have an equal voice or the power to veto any suggested distribution.

In the Pareto process, one person or a group can be prevented from acting in their self-interest by the veto power of at least one other fearing harm from a redistributive move. The ethic does not have to be to "restrain oneself"; the "market" or one's fellows—with veto power—will restrain one when there is a collision of self-interests. One can induce others (or be induced oneself) with an offer of some value to accept an initial worsening of their position (prior to the compensation payment). Looking at the Pareto process in this way, it appears as if the ethical rules are simply that people should (1) act purposefully in their own self-interest (autonomy and subjectivity), (2) respect that all exchange is voluntary (utility and teleology), and (3) give everyone veto power over suggested redistributions.

Nor does this imply that the "majority rules." One person may fear that the losses from a particular change are greater than the sum of the gains to all the possible gainers from a change. In this case, it would not be possible for gainers to compensate the loser even if they were to offer their gains to the loser. Here, the interests of a single large loser outweigh the interests of many small gainers.

This does not deny opportunism or apparently "perverse" one-time or short-run behaviors that may be part of establishing a reputation, for example, tit for tat, in a longer-run repeated game context leading to long-run gains. A one-time redistribution when the parties are noncooperative may end up in a prisoner's dilemma, where, given limited information, they both do worse than they would if they could collude and enforce agreements. In a situation of one-time play or single exchange, a social rule or convention—for example, habit, custom, tradition—may lead to a better outcome for both individuals than following their own narrow, short-run self-interest. Work on the evolution of cooperative rules has established this result and gives a decision-making foundation for rules of thumb and other "social conventions" that otherwise appear ad hoc. In a repeated game context, following one's own long-run self-interest may generate these rules and customs as dominant strategic outcomes.

Pareto-improving moves are those in which at least one person is made absolutely better off by a policy change without reducing the satisfaction (or utility) of any other member of society. Thus, Pareto-improving moves may be measured without resorting to cardinal utility. A move is *strongly* Pareto improving and the allocation is said to be *Pareto superior* to the previous position if at least one person claims to be better off while no one else claims to be worse off. If at least one person is made worse off, the move is *Pareto inferior*, and if a move leaves no one better or worse off, it is *Pareto neutral.*

Pareto-efficient allocations presume full employment of resources. If there were involuntarily unemployed resources, resources wishing to be employed but currently unemployed, then a policy could conceivably be devised that would be Pareto superior. The unemployed resources could be employed, they would be better off, and no other individuals would be worse off as their allocations would be unaffected or might even increase. Involuntarily unemployed resources have no opportunity cost of employment when they are involuntarily unemployed.

Pareto proved one of the most important propositions in neoclassical economics, that every Pareto optimum may be reached by a competitive process, and the corollary that perfectly competitive processes lead to a Pareto optimum. Known variously as the *invisible hand theorem* or the first and second fundamental theorems of welfare economics, to some this tour de force proves mathematically the program begun by Adam Smith in *The Wealth of Nations.*

Somewhat embarrassingly, there are an infinite number of Pareto-efficient allocations, each as "good" as the other—*good* in the sense that a proposed move away from any of the Pareto-efficient distributions would be vetoed by at least one person. There is no overarching or metasocial utility function that ranks these Pareto-efficient allocations. Every initial endowment of resources may be allocated among society's members differently. Every initial allocation may result in an infinite number of final allocations that meet the Pareto efficiency criterion. The Pareto process takes the initial allocation, no matter how skewed or equal, as a given. It does not presume to answer the question of how that particular allocation became the starting point. In this sense, given its silence on the matter, one might view the starting point of the Pareto process as implicitly justifying the existing distribution of goods.

The differing initial allocations will lead through a competitive process to different-ending, albeit Pareto-efficient, allocations. Each of these distributions is Pareto efficient, yet each implies a potentially drastically different final distribution of resources influenced by the starting distribution of resources. All we know is that through the competitive process, no one voluntarily makes oneself worse off through exchange; however, there is nothing that guarantees that the initial endowment even ensures that all members would make it to the market to start the Pareto-improving trading process.

If attaining a Pareto-efficient outcome is taken as a justification for perfect competition, it must be emphasized that other processes, in addition to perfect competition, may also ensure the attainment of a Pareto optimum. For example, Lerner and Lange, the exponents of "market socialism," used the existence of the Pareto process and the Walrasian general equilibrium framework to argue that central planners could mimic markets, using shadow prices calculated from their competitive general equilibrium models to direct individuals' effort, yielding a Pareto-efficient allocation. This claim led to some of the most heated exchanges in 20th-century economics, resulting in the development of the view that stresses the individuality and informational efficiency of the market process. Social planners could "be" the market; however, they would have to know so much and be able to calculate so quickly that for all practical purposes, such a program—while theoretically possible—would be operationally impossible. Critics of market socialism also stressed the supremacy of processes that made autonomous individuals the decision makers, fearing that allowing central authorities the power to make decisions would lead to a loss of the individual's rights.

While economists may be able to prove that the perfectly competitive process leads to a Pareto-efficient allocation, the practical question of what this means operationally must be addressed. In a world with imperfect competitors, missing markets, increasing returns, asymmetric and imperfect information, negative and positive externalities, public goods, common property resources, and second best considerations—in short, in a world that must admit market failures—where is the "invisible hand" that will lead us to a Pareto-efficient outcome? As is well known, *that* invisible hand is truly invisible.

This leads some economists, following Friedrich Hayek (following Smith), to focus not on end states, or on equilibria, but on market *processes.* The phrase "It's the journey, not the destination" is apt here. Casting aside the pursuit of static equilibrium and making nugatory the idea of a Pareto-efficient *outcome*, these economists focus on *processes* that are dynamically efficient as measured by lower informational costs and lower transaction costs and by weighting individual choice more highly than other methods of allocating resources. Reducing frictions in markets becomes the solution not in ensuring that a social optimum—or Pareto optimum—*is* attained but in ensuring that if one exists, individuals, driven by self-interest and protected by their veto power, may at least approach it. To many, this represents a return to the original insights and program of Adam Smith, who wrote much more about resource flows occasioned by changing self-interest guided as if by the invisible hand *and* the impartial spectator than he did about static equilibria.

Other welfare economists backed away from Pareto efficiency but not from the concept of equilibrium. They have tried to design compensation mechanisms allowing gainers to compensate losers, thus operationalizing Bentham's idea of "the greatest good for the greatest number" without resorting to a cardinal ordering of utility. In their schemes, monetary payments represent a willingness to pay. If after a policy change, gainers are willing to pay at least as much as it takes to compensate losers and losers voluntarily accept the payments, then that change moves society in the "right" direction. The search for individual gain leads to a better social outcome.

This view, stressing a conceivable welfare-improving reallocation after the policy change, raises the issue of whether or not reallocations before the fact might also be welfare improving. If so, some argue that the initial allocations ought to be changed before a particular policy is changed.

Pareto efficiency is based on three assumptions: (1) Individuals are the best judge of their own utility, (2) social utility is defined only in terms of independent (not interdependent) individual utilities, and (3) interpersonal utility comparisons cannot be made. These are value-laden assumptions that leave any claim of a "value-neutral" Pareto process and allocation in doubt.

In the end, Pareto's attempt to provide a simple rule that could be used to assess the outcome of *actual* social policy is incomplete. In a Walrasian competitive general equilibrium framework, such a demonstration may be made. However, it is widely accepted that the world in which we live, hence the world of actual social policy and reallocations, does not closely resemble a Walrasian general equilibrium model.

—David L. Hammes

See also Arrow's Impossibility Theorem; Autonomy; Bentham, Jeremy; Competition; Economic Efficiency; Hayek, Friedrich A.; Invisible Hand; Market Socialism; Methodological Individualism; Pareto, Vilfredo; Perfect Markets and Market Imperfections; Prisoner's Dilemma; Self-Interest; Unemployment; Utilitarianism; Utility; Welfare Economics

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Parmalat

In 1961, a 22-year-old college dropout, Calisto Tanzi, inherited his family-owned prosciutto business, to which he added a pasteurizing facility in Parma, Italy, which was later to become known worldwide as Parmalat. It steadily grew into a diversified multinational dairy, beverage, and bakery company and one of Europe's most influential corporations. In 2002, Parmalat Finanziaria was the holding company of a group of more than 200 subsidiaries operating in 30 countries with assets of €10 billion and annual sales of €7.6 billon. More than 36,000 people were on its payroll. But in December 2003, the company was declared insolvent in one of the world's largest corporate bankruptcy scandals, and Tanzi himself was alleged to have engaged in financial fraud and money laundering in a case that rivals Enron and WorldCom in notoriety.

After the 2003 shock of unexpected bankruptcy at Parmalat, it was later uncovered that the company had kept off–balance sheet debt transactions to the tune of €14.3 billion ($16.9 billion) hidden from the public. Such irregular accounting practices are illegal, since they give investors and potential investors a false and misleading picture of the financial health of a corporation that can unfairly influence market investment decisions. In fact, Parmalat was able to continue to reap large loans from banks such as Bank of America, Citicorp, Crédit Suisse Group, and Italy's Banca Nazionale del Lavoro while it maintained its false record keeping.

Calisto Tanzi and his family had reached Italian celebrity status before the scandal at Parmalat. Some affectionately called Tanzi "Mr. Milk" after Parmalat's chief product of milk distributed in a special tetrahedron package that extended its shelf life. Many admired Tanzi's risk taking, which had taken him from rags to riches. With control of 51% of the outstanding shares of Parmalat Finanziaria, he ran the firm as a family business. His own net worth was placed at €1.3 billion. He had associated the family business with sports teams and had done much philanthropic work in Parma. He provided funds that went to the restoration of the city's theater and basilica, and he gave to the area's AIDS patients and assisted the local poor. Some would have called him the model entrepreneur—before it came to light that he was a fraudulent deceiver and perhaps the mastermind in the Parmalat scandal.

Authorities claim that for 13 years Parmalat had sought and received bank loans based on revenues that it had inflated by claiming sales to fictitious firms. Investigators reported that Tanzi allegedly conceived the fraudulent scheme, which he executed along with his top managers and some external lawyers and auditors, although the last two professional groups have claimed their innocence. The overall plan began to come to light when, in the winter of 2003, a bond payment that was due went unpaid and it was discovered that €3.9 billion from a Parmalat subsidiary in the Cayman Islands that was supposedly deposited in a Bank of America account did not exist at all. Moreover, the investigation revealed that Tanzi had skimmed and transferred anywhere from €500 million to €1.3 billion to other family firms to cover losses there. In all, a total of €8 billion was missing from the company's "cooked books." In short, Parmalat was a case where managers simply invented assets to offset huge liabilities and falsified their accounts over a 15-year period, finally forcing the company into bankruptcy on December 27, 2003. Trading in Parmalat shares was suspended the same day.

The overriding question, of course, is how such a successful firm could go down such a road to infamy. There are a number of theories that attempt to explain the Parmalat scandal. First, it was held by some that the firm had expanded much too quickly and diversified too broadly and in so doing created massive debt that Tanzi felt should be hidden from the public and his creditors. For example, in the 1990s, Tanzi and his family had sour business dealings in sports and tourism. He also tried to enter the media business with the purchase of a TV network, which was eventually sold with a loss of an estimated €45 million. Such a business track record would have damaged Tanzi's borrowing power, so to maintain his company's status as a good credit risk, off–balance sheet fictions were created and perpetuated for over a decade.

Another possible explanation has to do with the corporate governance structure of Parmalat. According to this view, Tanzi's management style and running of such a huge conglomerate as if it were a family-owned business took its toll on the operations. And finally, it has been said that Tanzi should not shoulder the full blame for the collapse of Parmalat and that there also may have been complicity on the part of the external group of professionals whose job it was to serve the public as watchdogs of the firm and ensure that transparency was a feature of its financial dealings. After the Italian authorities became aware of the depth of the scandal, a special government-appointed "extraordinary administration" took over control of Parmalat. The head of this administration, Enrico Bondi, has claimed that there were others external to the firm that had played a major role in the fraud schemes that were uncovered. He sued 45 banks for allegedly having had a hand in the fraud. Bondi sought €8.06 billion from Citibank and Bank of America, but in 2005, most of his claims had been dismissed in a U.S. court where they had been filed.

Bondi also accused auditors from Grant Thornton International and Deloitte & Touche Tohmatsu for having engaged in professional malpractice. The Italian branch of Grant Thornton had been the auditor of Parmalat's Bonlat subsidiary in the Cayman Islands, which was the unit that had booked €3.95 billion in fictitious assets with Bank of America and that first brought the whole scandal to light. Under Deloitte & Touche's audits, Parmalat had booked its actual debt as if it were real equity, allowing the company to make continued inflated earnings statements. Bondi's claim, then, was that Parmalat, along with the investing public, was a victim not only of Tanzi's alleged criminal behavior but also of the failure of banks and external auditors to do their jobs properly. In such ways, it was hypothesized, had Parmalat traveled the road to become Europe's Enron.

—Peter Madsen

See also Accounting, Ethics of; Bankruptcy, Ethical Issues in; Corporate Accountability; Corporate Governance; Deceptive Practices; Enron Corporation; European Union; Finance, Ethics of; Fraud; Manipulation, Financial; Scandals, Corporate; Transparency; WorldCom

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PARTIAL EQUILIBRIUM

Equilibrium is the condition of balance among the forces acting on a system. Partial equilibrium focuses on the conditions within the system without considering its effects on, or effects from, other systems.

Perhaps the most well-known analysis of equilibrium in the business context is the balance between the forces of supply and demand for goods. Partial equilibrium is the condition of balance among forces directly affecting the supply and demand for a particular category or type of good without considering the effects on other types. For example, a partial equilibrium analysis of the supply and demand for gasoline considers the direct influence of the price of gasoline but not the effects of the price of public transportation on the supply and demand for gasoline or the effect of the price of cars of varying fuel efficiency on the supply and demand for gasoline.

Equilibrium processes in social systems play out over long periods of time as many individuals make many transactions, each decision based on the individual's self-interest and subjective understanding of information and knowledge. Over the long term, society progresses as each individual strives to allocate resources to those transactions he or she believes to be the most rewarding.

The process, however, is vulnerable to individual ignorance and error. The precise conditions for partial equilibrium are uncertain, unknown, and unlikely to withstand the shocks of innovation and creative change. As self-interested individuals make decisions over time and without a guiding hand, society bears the risk of short-term shortages or surpluses in the distribution of goods. In this way, partial equilibrium, in common with more general social equilibrium perspectives, puts analytical faith in long-term distributive justice and does not address short-term deficiencies.

The equilibrium of supply and demand is critically dependent on the ethical functioning of the economic system and the marketplace. Information about prices in the market plays a key role in these processes, and this information must accurately and honestly reflect the quantity and features of the goods that will be offered or demanded at any given price. Fraudulent information will disrupt the equilibrating processes of supply and demand, as will denial of fair access to willing and able suppliers and customers. Thus, even in free markets, governments may enforce the rules of commerce to ensure commutative justice and economic integrity.

Governments also may seek to improve society by disrupting the free functioning of equilibrating processes. For example, there is a partial equilibrium perspective for the quantity of illegal and harmful drugs in society, just as there is one for ethical pharmaceutical drugs. Partial equilibrium on its own is a process or analytical perspective without an embedded morality. Governments have a role to install legal and regulatory boundaries, constraints, and compliance requirements as significant forces for social responsibility.

The self-interested agency of individual managers on the behalf of business principals provides the dynamic energy for economic and market systems over time to converge toward or diverge from partial equilibrium. Patterns in equilibrating processes may differ if there is a tendency for management decisions to be biased toward or away from specific ethical principles. For example, partial equilibrium for housing in society may proceed at different rates or follow different patterns over time if a residential construction industry is managed by decision makers who seek to maximize value for shareholders rather than to return reasonable value to shareholders in order to reserve some organizational assets for social responsibility activities.

Partial equilibrium is a condition of balance between self-interested buyers and sellers in a social exchange process. It is a very simplified description of society, however, and the likelihood that a tendency toward partial equilibrium can bring about a just society over the short term, or reliably over the long term, is risky at best.

—Greg Young

See also Equilibrium; Nash Equilibrium; Self-Interest

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Participatory Management

Participatory management refers to involving nonmanagement employees in decisions that directly affect them. It is a form of decentralization that pushes decision making down to the lowest possible level within an organization. Participation can be very limited, with managers obtaining input from a few employees regarding a minor task, or very extensive, where all employees participate on teams that make a wide range of productivity and budgetary decisions and are financially rewarded for doing so.

Participatory management is often juxtaposed with the traditional command-and-control system of management, where nonmanagement employees are excluded from an organization's decision-making process. Factors contributing to the spread of participatory management systems include the trend toward self-management, a more educated workforce, and more than a century of praise by leading management theorists.

Types of Employee Involvement

Participatory management systems come in many shapes and sizes depending on the answers to the following four questions: (1) Who gets to participate? (2) What decisions do they get to participate in? (3) How much authority do they have over the final decision?

(4) Are the participants financially rewarded for improved performance?

The most common form of participation is a suggestion system. Suggestion systems can be designed for a select group of employees or all employees. The employees may provide input on one particular issue or a wide range of issues. Some suggestion systems offer financial incentives for submitting the suggestion, and some offer bonuses based on the financial impact of the suggestion. Usually, the person offering the suggestion has very little authority over the final decision. Survey feedback is another common form of limited participation where nonmanagement employees provide input but have no decision-making authority.

Quality circles, a group of employees who meet regularly to discuss workplace improvements, typically have greater decision-making authority. Quality circles usually involve a limited number of employees chosen based on their particular expertise.

A few organizations allow nonmanagement employees to sit on their boards of directors. Although the number of nonmanagement employees participating is minimal, the range of decisions they can influence is very broad.

Scanlon-type gainsharing plans provide a broad range of participatory features, including a suggestion system, participation on department decision-making teams, voting privileges on a review board, and a group-based performance bonus. All employees are encouraged to submit written suggestions that can reduce costs, improve efficiency, and increase revenue. These suggestions are examined by department teams composed of nonmanagement employees based on common job tasks. The teams may consist of every nonmanagement employee in the department or elected representatives and may meet monthly, weekly, or daily. The department teams are provided a limited budget to implement suggestions that affect only them. Expensive suggestions, or interdepartmental suggestions, are forwarded to a review board composed of management and nonmanagement employees for implementation consideration. Nonmanagement employees receive group-based bonuses by surpassing historical productivity benchmarks or reducing historical cost benchmarks.

Authoritarian Roots and Justifications

Authoritarian managerial power at the workplace has a long history that includes the institution of slavery in Greece, Rome, and the United States. As is evident in the writings of the Social Darwinians, authoritarianism is a deserving reward for successfully climbing the organizational ladder.

At the time of the American Industrial Revolution, there was a need to organize and motivate a large number of formerly self-employed agrarian workers or craftsmen to efficiently perform factory work. According to Frederick Winslow Taylor, the managerial system of 19th-century America operated under the notion of “ignorance and deceit.” Workers deceived employers about production output capacity, and employers deceived workers about the wage value of their output. Each interest group was ignorant of the other’s knowledge. Because of these deceptive practices, Taylor argued, industrial organizations were inefficiently managed.

Taylor recommended that managers divide every job task into its most basic components, scientifically conduct time and motion studies to determine the most efficient method for performing the task, supervise workers very closely, and link pay to performance. All planning functions were to be performed by managers and all labor functions by nonmanagement employees. The adoption of Taylor’s scientific management techniques significantly increased productivity.

Taylor’s management methods were implemented in capitalist and communist societies. Vladimir Lenin was one of the earliest proponents of Taylor’s authoritarian-based scientific management. He demanded that Soviet workers unquestioningly subordinate themselves to the single will of managers. According to Lenin, managers should coordinate workers through a unified command and to achieve a technically rational organization.

In addition to tradition and production efficiency justifications, other arguments favoring centralized command-and-control management systems over participatory ones include the following:

- Employers have a constitutional right to set the terms of employment as they see fit.
- Few employees advocate participation.
- Empirical research suggests only modest performance improvements from employee participation.

The Participatory Alternative

Participatory management was formulated as an alternative to the traditional command-and-control authoritarian model. In the 1920s, Elton Mayo and human relations school of management researchers documented the productivity benefits of fulfilling an employee's social needs and advocated collaborative mechanisms at the workplace.

During the 1960s, Douglas McGregor and other human resource school of management proponents argued that work should be a place where people continue to develop psychologically and socially. According to McGregor, participatory management represented an ideal process within organizations. Although some people disliked working and needed to be dictated to and coerced, many other people wanted to take on new responsibilities and welcomed the opportunity to constructively collaborate in an organization's decision-making process.

Tom Peters and corporate culture scholars maintain that the most successful organizations in this age of fast-paced innovation and customer responsiveness are composed of "empowered" employees at all levels, in all functions, and in nearly everything. Peters recommends that all employees participate in hiring coworkers, designing work tasks, assessing new technologies, formulating budgets, and measuring their own performance. W. Edwards Deming's total quality management approach and Peter Senge's "learning organization" both emphasize local autonomy, where those working in a specific area solve their own problems rather than await decisions made by centralized authorities.

Most recently, organizations have been adopting participatory management techniques due to the impact of downsizing and globalization. Organizations are eliminating layers of management to maintain global cost competitiveness. The remaining employees must take on greater managerial responsibilities, even at the lowest levels of the organization.

Research Findings

Researchers have not reached any definitive conclusions on whether participatory managed firms are more productive than traditional command-and-control managed firms. A major obstacle in achieving consensus on the empirical evidence is that there is no one standard form of participation. For instance, some researchers group together quality circles and gainsharing systems even though these two participatory systems have many differences and a wide range of permutations.

In general, meta-analytical researchers have concluded that the impact of participation on employee performance and satisfaction is statistically significant but rather small. Participation has a more positive effect on a particular personality type—namely, employees who tend to believe that they control their own destiny.

Political behaviors within organizations help explain some of the contradictory research findings. A plethora of case studies document how to properly implement and manage employee participation. Yet management and nonmanagement employees engage in unhealthy power games around the participatory mechanism. Internal political issues arise as a result of managers giving up power, nonmanagement employees taking on power, and both parties sharing power. The power dynamics of participation must be managed appropriately for organizations to achieve the desired outcomes.

From a multistakeholder perspective, case study research has found that gainsharing's collaborative problem-solving mechanisms benefit owners in terms of cost savings, customers in terms of improved product quality and service, suppliers in terms of product feedback, and production employees in terms of improved health and safety conditions and other favorable changes in employee policies.

In conclusion, many benefits can be achieved through participatory management mechanisms at both the individual and the organizational level of analysis. But success requires strong commitment from upper-level managers and significant training of nonmanagement employees. Until participatory management systems can be designed to significantly outperform command-and-control management systems, the right of employers to determine employment relations will remain more important than the human dignity associated with involving employees in decisions that directly affect them.

—Denis Collins

See also Authority; Employee Relations; Empowerment; Meaningful Work; Working Conditions

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PATENTS

A patent is a governmental grant of exclusive control over a new invention—a material, product, or process—for a specific period of time, normally 20 years. A patent is granted as a reward for innovation, usually technical innovation. Recently, in some countries, including the United States, a patent may be granted on a new method for doing business. To qualify for a patent, the discovery must be useful, novel, and nonobvious—that is, not an extension of existing technology that would be obvious to an expert in the field. The patent holder has the legal right to prevent others from producing, using, selling, or importing objects that infringe on the patent. A patent holder may license third parties to manufacture or sell the invention, usually in return for royalties. A patent holder can prohibit a competitor from using or selling an equivalent invention, even if the competitor has made an independent discovery, not relying on the patent holder's research.

Patents are frequently described as monopolies, but there is no guarantee of monopolistic rewards unless the invention attracts willing buyers. In addition, the economic benefits of a patent are secure only if the patent holder has the financial ability to defend the patent against infringement or legal challenges, because patent litigation is very costly. Individual inventors or small businesses may not be able to defend patent rights.

Patents are granted by national patent offices; among the most important are the United States Patent and Trademark Office and the Japan Patent Office. Some economic regions cooperate on patent policy, notably the European Patent Office. In 1994, during the creation of the World Trade Organization, member nations signed the Agreement on Trade-Related Aspects of Intellectual Property Rights (TRIPS). This international agreement sets rigorous basic standards for legal protection of intellectual property rights in member countries.

The TRIPS agreement recognized some permissible national limitations on patent rights. The agreement permits compulsory licensing of patents, allowing competitors or the government to manufacture essential patented products or to use crucial patented processes to respond to a national emergency, such as a public health crisis. When a compulsory license is issued, the patent holder is entitled to reasonable compensation. The TRIPS agreement also allows a nation to refuse to patent plant, animal, or human life and to refuse to patent products or processes that cause serious environmental harm. If a country does not permit the patenting of plants, the government must offer an alternative legal mechanism to protect the property interests of plant breeders who create new varieties.

Influenced by the legal tradition of some European countries, TRIPS allows nations to refuse to patent an innovation if necessary to protect the *ordre public* or morality. The *ordre public* is similar to the public interest. The concept is comparable to legal restrictions on contracts that violate public policy. In the early 20th century, some patent offices refused to approve applications for contraceptive devices, for example. Those who advocate very limited use of the *ordre public* exemption question whether the staff of a national patent office has the training or resources to resolve the ethical issues raised by patent applications and, hence, to decide wisely that certain applications be rejected on the grounds of offense against standards of public morality.

Moral Justifications for Patents

According to some ethicists, a patent is an example of a natural right to property and ought to be defended in business ethics. However, others emphasize that patents are a government exemption from the normal rigors of the competitive marketplace. They claim that the use of government power to privilege certain parties to commercial transactions needs to be ethically justified.

Natural Right to Property

Some business ethicists see patents as a clear example of the human right to benefit from the fruits of one's labor. An inventor deserves a reasonable opportunity to reap the rewards associated with an invention, because the inventor's genius, hard work, and persistence have created something of novel social value. Some explicitly connect their position to John Locke's more general defense of private property. However, some who are critical of patents reply that Locke's position on property included a key proviso: A person has a moral claim to expropriate property from nature by hard work as long as other people have access to resources that provide them an equally good opportunity to create property. These critics point out that a patent gives the patent holder exclusive control over a technical idea. Once a patent is granted, others pursuing independent research lose any opportunity (for the duration of the patent) to benefit financially from their efforts if their inventions turn out to be equivalent to the subject of a patent. So, these critics conclude, patents violate Locke's proviso that other persons must have as good an opportunity to obtain similar property.

Other critics of the patent system point out that inventions are rarely the result of a flash of personal genius, completely dependent on the intellectual resources of a solitary human being. Most technical innovations depend on prior technological development and, indeed, broader stocks of social knowledge. Inventors receive from their communities the technical training that is a prerequisite for the inventor's creative accomplishment. So while inventors deserve a governmentally protected share in the value created by their ingenuity, society may place limits on property rights in an invention, because society has contributed to the innovation as well.

Fair Social Bargain

Some ethicists describe the patent system as a social bargain designed to advance the common good by encouraging, over the long run, greater technological progress. To them, the patent system is an arrangement where inventors are granted a limited period of exclusive control over their innovations in return for disclosure of adequate technical information about the discovery—information that would enable a skilled peer to duplicate and to operate the invention. These commentators warn that without patent protection, inventors would safeguard their discoveries as trade secrets. Inventors' secrecy would inhibit technological progress. According to this view, patents involve a trade-off where higher prices for buyers and possible temporary stifling of associated research are tolerated in return for more risk taking in initial research and prompt public disclosure of research findings to fellow inventors. However, there are questions about the extent to which contemporary patent documents actually promote technical progress. Some patent critics say that researchers are rarely inspired to develop important new technology through studying patents.

Utilitarianism

Many supporters of patent rights make a utilitarian argument that the social benefits of the patent system outweigh its costs. To them, the extra profits attributable to patent exclusivity are a necessary incentive for the creation of socially useful technological innovations. They frequently use as examples worthwhile products, such as innovative drugs, that are extraordinarily expensive to develop but could be copied relatively cheaply and quickly by competitors. If "free riders" were allowed to exploit the hard-won technical creativity of inventors, socially beneficial research would soon be undermined.

Some commentators have noted that there is a built-in irony in the relationship between patents and technological innovation. Fear of infringing on a patent may inhibit other inventors from developing improvements on a patented invention during the life of the patent. Thus, patents may actually retard technological progress for a time. Smaller companies may be particularly reluctant to attempt innovations that might trigger expensive patent infringement battles. Still, without the lure of the higher profits that patents make possible, the original discovery might never have taken place.

The utilitarian argument in support of patents hinges on an assessment that the social benefit of technological progress outweighs the social costs patents entail. However, those who question the moral legitimacy of patents warn that the social costs associated with patents are often not fully appreciated. These costs include governmental costs to examine and adjudicate patents, the stifling of innovation in areas where existing patents create a legal minefield, legal and commercial disadvantages for smaller firms without strong patent portfolios, misallocation of social resources to very expensive legal battles (costs ultimately borne by consumers), and the lack of social utility produced by those firms whose primary business is the aggressive enforcement of their patent portfolios.

There are some who question the utilitarian characterization of patents as essential incentives for innovation. They point out that being the first to market an innovative product—the so-called "first-mover advantage"—sometimes leads to strong financial rewards even in the absence of a patent. In other cases, patents fail to provide an effective incentive for research to meet urgent human needs. The potential rewards from a patent are too limited to be an attractive incentive if the innovation benefits only a small group, for example, those suffering from a rare, but debilitating, disease. Patents may not stimulate research beneficial to even a large group if the group is too poor to constitute a feasible consumer market. Thus, patents may not provide viable incentives to develop novel products desperately needed by some vulnerable social groups.

Other critics of the patent system contend that patents are not well suited to calibrate morally appropriate rewards for socially useful technical innovations. Some inventors get large rewards for novelties that are of trivial human benefit; other inventors cannot find a viable market for innovations of much greater benefit to humankind. These commentators suggest that the appropriate financial rewards for technological innovations would be distributed more effectively if governments or philanthropists offered monetary prizes for socially beneficial technical innovations. Proponents of the patent system respond that a system of prizes for innovations would be beset by practical problems, favoritism, and potential corruption. They conclude that a patent system in which consumers pay a premium for patented products that they genuinely want is a more efficient way to stimulate technological progress.

Controversial Ethical Issues Concerning Patents

Consistent Treatment of Lesser Developed Nations

Some commentators have questioned whether lesser developed countries have a duty to strictly respect patent rights during the early stages of their economic growth. This argument stresses moral consistency. Advocates for the lesser developed countries point out that nations such as the United States achieved rapid economic development during the early industrial era partly by exploiting ("pirating") the intellectual property of international competitors. For example, U.S. textile mill owners copied innovative British machinery without permission or compensation. Critics charge that the advanced industrial nations, led by the United States, are now inhibiting the economic development of lesser developed nations by imposing a global patent regime that prohibits the very sort of free transfer of technology that created wealth for the richer nations in the past.

Impact on Access to Medicines

There are also ethical questions about the impact of patents on access to life-saving, new medicines. Prior to the TRIPS agreement, some countries, particularly poorer countries, refused to grant patents on pharmaceuticals because patents drove up the prices of products crucial for the health and lives of citizens. When TRIPS was adopted, there was increasing pressure to safeguard the patent rights of pharmaceutical companies. About the same time, the AIDS pandemic threatened the survival of millions. As a result of expensive research, innovative drugs were discovered that made HIV infection a manageable, chronic disease. Companies selling patented AIDS drugs charged monopolistic prices. In some lesser developed countries, which were not yet required to comply with TRIPS, generic drug companies manufactured cheap copies of patented AIDS medications. Pressure from health agencies and nongovernmental organizations led to the Doha Declaration, which clarified that WTO countries were entitled to use compulsory licensing of patents in response to a national health emergency.

Supporters of the pharmaceutical companies emphasize that patent rights vigorously enforced globally are crucial as an incentive for research that saves lives. Some commentators even point out that the situation of patients in poorer countries is not made worse if patents prevent them from having access to new medicines. Such patients were struggling with life-threatening diseases before the drugs were invented; they are in the same (dire) condition—no worse off—if they cannot afford new patent-protected medications. Those who charge that patents play a critical role in making AIDS drugs inaccessible to poor people respond that the rights to life and health take moral priority over property rights created through the patent system. These commentators assert that governments—which grant patents as a privilege designed to promote the public interest—have a greater responsibility to protect citizens from life-threatening diseases than to protect the property rights of corporations.

Patenting Human Genetic Material

There are also ethical controversies about issuing patents on human DNA. Critics of such patents assert that a substance such as DNA, which occurs in nature, does not satisfy the legal requirement that a patent claim be novel. Proponents of gene patents point out that patents are granted for genes or gene sequences that have been isolated or purified, so the material is not in its naturally occurring state. Other biotechnology patents cover novel techniques devised by the inventor to manipulate genetic material or the discovery of a practical use for a human gene. Thus, those who defend patents involving human genetic material insist that these patents are appropriate rewards for human ingenuity, not a government grant of control over naturally occurring human genes.

Critics of gene patents further warn that patents on human genes might lead to morally inappropriate property rights over parts of human bodies or even human persons (persons who were the “product” of patented genetic processes). Patent advocates remind people that patents give the patent holder negative legal power to exclude others from duplicating or commercializing a discovery, not a positive entitlement to sell the invention. A patent on a process for cloning mammals and on the mammals that are the product of that technique would not entitle the patent holder to sell a human baby conceived using the technique. (The University of Missouri holds a U.S. patent on mammalian cloning; it denies any intention to pursue human cloning. The university says it would use its patent, if necessary, to prevent others from commercializing human reproductive cloning.) Some lawyers further assert that claiming property rights over a human conceived using patented genetic material or processes would be unconstitutional under the Thirteenth Amendment, which outlaws slavery.

Some scientists are concerned that patents on human genes might seriously impede biological research. The Myriad Genetics patents on using the BRCA1 and BRCA2 genes to detect increased breast or ovarian cancer risks are patents that arguably have inhibited research. There is an exception in patent law that permits a researcher to use patented material for certain scientific, noncommercial research, but in the United States, case law has narrowed the protection against infringement charges that the research exemption affords.

Opponents of broad patents on human genes warn that these patents might also allow patent holders to charge “reach-through” royalties. In other words, the patent holder might be able to demand payments from companies that made products discovered using the patent holder’s innovation—even if the patented material or techniques were not a part of the final product that the company accused of infringement had produced. Reach-through royalties might substantially raise costs for consumers of those end products. In the field of biotechnology, these additional patent royalty costs might raise the prices of essential goods such as medicines or diagnostic tests.

Some groups say that manipulation of human DNA might involve morally objectionable types of genetic engineering. Therefore, they assert that the government ought not to encourage manipulation of human DNA by offering the financial incentive of a patent. According to this position, the government should not dignify manipulation of human genetic material by according this scientific work the social recognition implied by a patent.

Some ethicists describe the patenting of human genes or gene sequences as an example of morally unacceptable commodification of human life. Other ethicists assert that human genetic material is closely connected to human integrity or identity. They point to the close connection between elements of the genetic code and important characteristics of human bodies and even behavior. Then, they argue that reducing human genes to the subject matter of a patent violates the moral imperative to respect human dignity. Some opponents of patenting of human DNA connect such moral arguments to the morality exception in European patent law and in TRIPS. They urge governments to deny patents on human genetic material as they are a violation of the *ordre public* or morality.

Other ethicists say that biochemical substances, including genes and gene sequences, are morally distinguishable from whole human beings. A gene or a gene sequence is not a person and does not have the moral value attributed to human beings. For one thing, the biochemical substratum of human genes occurs in other animals, not just in humans. According to this view, patents on human genes, which are mere biochemical substances, do not have direct implications for respect for human dignity.

Conclusion

Patents are a form of property right created by governmental action. Some business ethicists see patent rights as grounded in a natural right of inventors to control the fruits of their genius and effort. Other ethicists insist that patents, which they see as government privileges exempting patent holders from the rigors of the free market, require careful moral scrutiny. Specific patents raise business ethics issues: For example, do patents on new medicines support or interfere with human rights to life and health, and do patents on human genes have implications for respect for human dignity?

—Barbara Hilkert Andolsen

See also AIDS, Social and Ethical Implications for Business; Copyrights; Doha Development Round of 2001; Genetics and Ethics; Intellectual Property; Locke, John; Property and Property Rights; Utilitarianism; World Trade Organization (WTO)

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Paternalism

Paternalism is commonly understood as an infringement on the personal freedom and autonomy of a person (or class of persons) with a beneficent or protective intent, although this definition is somewhat contested in the ways discussed below. As the ensuing discussion suggests, paternalism generally involves competing claims between individual liberty and authoritative social control. Questions concerning paternalism may include as well both the claims of individual rights and social protections and the legal and socially legitimated means of satisfying those claims. The discursive use of the term *paternalism* is almost exclusively negative, employed to diminish specific policies or practices by presenting them in opposition to individual freedom.

History of Paternalism

The term *paternalism* first appeared in the late 19th century as an implied critique predicated on the inherent value of personal liberty and autonomy, positions elegantly outlined by Kant in 1785 and Mill in 1859. The etymology of paternalism, rooted in the Latin *pater* (father), reflects the implicit social hierarchies of patriarchal cultures, in which fathers or male heads of families were understood to be authority figures responsible for the welfare of subordinates and dependents. In this tradition, adult members of states, corporations, and communities functioned under the presumably benevolent authority of kings, presidents, and executives. Prior to industrialization, patronage systems informed the stratified economic, political, and social arrangements prevalent throughout Europe and the Americas. Paternalism, as it evolved through the industrial age of the 19th and 20th centuries, applied the model of family relations and practices of patronage (fatherly protection, tutelage, and control) to relationships between classes of people understood as unequal: employers and workers, the privileged and the underprivileged, the state and the masses.

Historically, then, paternalism is a critical term applied in the West to the system of beliefs and practices emerging in the transition from a social order of patriarchal class structures, including slavery in the United States, to a free society of autonomous and equal individuals. Although it is not defined by a single institution or set of institutions, paternalism was prevalent among the early industrial companies. For example, the efforts of Ford's Sociological Department to promote clean and sober lifestyles included monitoring employee bank accounts, church attendance, and family life—measures now considered extremely intrusive but not uncommon for a time when laborers were largely employed by people whose wealth, education, and social privilege far exceeded their own. In the United States, the ongoing debate between social reformists and free market advocates shifted from the political and economic integration of former slaves in the late 19th century to a broader concern in the 20th century with the rights of workers, the poor, children, and other marginalized groups such as criminals, the mentally ill, and people with disabilities.

Following several decades of relative silence about paternalism in the mid-20th century, the term was reintroduced, in the context of criminal law, to become a topic of extensive philosophical debate with the 1971 publication of Gerald Dworkin's article on morality and law. As the discourse of paternalism has evolved, its meaning has become more nuanced. Responding to what he considered intrusively interventionist policy and program changes affecting the poor (e.g., welfare, child support, homelessness), Mead defined the "new" paternalism as "social policies aimed at the poor that attempt to reduce poverty and other social problems by directive and supervisory means." From a different perspective, free market advocates apply their longstanding opposition to paternalism in championing social policies that emphasize the freedom of individual citizens rather than dependence on government or employers in planning and paying for their own health care, college education, and retirement. Standing's 2002 argument against supervision of the poor as the means of ensuring their economic security echoes Mead but insists that the human need for (and right to) collective agency and guaranteed "structured reciprocities" of mutual responsibility between citizen stakeholders and their government cannot be dismissed as paternalism.

Paternalism as a Theoretical Concept

Dworkin identified paternalism as "limitation of a person's freedom or autonomy by force or coercion, without his consent, to prevent harm, mitigate risk, or promote the welfare, interests, needs, good, or values of the person whose freedom is being curtailed" (Dworkin, 1972). To be considered paternalistic in Dworkin's analysis, an action should (1) limit a subject's freedom, (2) be performed without the subject's consent, and (3) be performed with a beneficial intent. Kleinig elucidates Dworkin with the observation that incentives may effectively replace coercion as a mechanism of social control. Buchanan adds that deception is also an effective but noncoercive means of interfering with a person's freedom.

In establishing the basic theoretical framework of paternalism based on the conditions and justifications for restricting freedom and autonomy, Dworkin differentiates among various types of paternalism as hard or soft, broad or narrow, weak or strong, pure or impure, and moral or welfare. Primarily concerned with the safety and welfare of the person, an advocate of *hard paternalism* would permit restrictions of liberty to prevent suicide or grave personal harm even when a person in question is fully cognizant of his or her actions and their consequences. In contrast, an advocate of *soft paternalism* would be concerned primarily with the autonomy of the person, justifying restriction of liberty only to ascertain whether the person in question were indeed choosing to harm or endanger himself or herself with full volition and knowledge of the facts; the soft paternalist would not deny the freedom to inflict self-harm or even death if that were an authentically free and knowledgeable choice.

Similar to soft paternalism, *weak paternalism* would consider it legitimate to use coercive means to achieve a person's desired consequence, such as requiring seatbelts, in the assumption that people desire life and health and therefore should be forced to take measures to protect themselves. *Strong paternalism* would prevent a person from achieving a desired consequence on the grounds that he may be confused or mistaken about his ends but not if he understands his choice. In such a case, a severely intoxicated person could be prevented from driving if he or she intended to drive home and was incapable of perceiving his or her inability to drive safely, but that person could not be prevented from getting intentionally intoxicated to facilitate a fatal car crash.

Broad paternalism would include coercion from any source including private institutions, families, and individuals to restrict or control a person's actions, whereas *narrow paternalism* would include only coercion by the state. *Pure paternalism* would restrict the actions of people who may be harmed by their own behavior, while *impure paternalism* would restrict the actions of third parties to protect potential victims. For example, unauthorized consumption of street narcotics is illegal to prevent people from self-endangerment or death—a pure paternalist intervention. An impure paternalist intervention would criminalize the prescription of narcotics by physicians or their production by pharmaceutical companies in order to protect the public.

Finally, *moral paternalism* is differentiated from *welfare paternalism* on the basis of the type of good intended for the person whose freedom is being restricted. Local blue laws were instituted in some communities for the purpose of promoting a moral standard of sobriety, quiet, and church attendance on Sundays, whether or not the individuals in those communities wished to observe Sunday as a religious day or considered engaging in Sunday commerce or drinking to be morally corrupting. Coercive measures imposed to promote the moral good are different from others, such as driving speed limits, inoculations for schoolchildren, or architectural design standards in neighborhoods, designed to promote the general welfare of the citizenry.

A decade after his original article, Dworkin clarified his original defense of soft paternalism, noting his position that paternalism is sometimes justified in cases where the person(s) in question is demonstrably incompetent or unable to act responsibly in his or her own self-interest. Critics have charged that this justification blurs the difference between soft and hard paternalism because of the difficulty in establishing universally accepted criteria for determining incompetence, thus creating a "slippery slope" of potential encroachment on personal liberty.

Moral Considerations of Paternalism

Paternalism raises a cluster of moral questions about the nature of a free society, its obligations to individual members, and the obligations of individuals to themselves, to each other, and to society. A key question concerns the classification of circumstances in which the limitation of individual freedom or autonomy may be properly considered to be paternalistic.

The central moral issue of paternalism is the legitimacy of limiting human freedom and autonomy in a free society of equals where all individuals are accorded respect, autonomy, and freedom by virtue of their humanity. Following Kant and Mill, this moral position derives from the assumption that human beings are best capable of determining and pursuing what is in their own interest; to deny persons this right would be to treat them as instruments of their own good rather than as ends in themselves. Moreover, individuals in a society of political equals are thought to be capable as well of discerning the commonweal and modulating their exercise of personal freedom accordingly. Paternalism denies the full humanity of individuals by failing to respect their capabilities for acting in their own best interest. Moral arguments for paternalism must offer compelling reasons to justify the restriction of freedom and autonomy.

Kant's objections to paternalism are absolute, with explicit moral prohibitions against lying and force as its chief instruments. Mill distinguishes between paternalism in relation to children and to adults: The moral presumption would favor paternalism for a child and prohibit paternalism for an adult. Mill, however, considers paternalism as morally justified among adults to prevent harm to someone who is unaware of an impending danger (e.g., about to cross a bridge without knowledge that it is unsafe). In analyzing normative judgments of paternalism, Dworkin considers two possible normative options: Either (1) it is never permitted to limit the freedom of others in an attempt do good for them against their wishes, or (2) it is possible to do so under some circumstances. The first option is often justified on the Kantian grounds that it is impossible to do good by limiting freedom. The second option may be justified on various grounds. Consequentialists may argue that the good done may outweigh the harm caused by loss of autonomy. Others may argue that individual autonomy may be protected in the long run by restricting it in the short run, such as in Mill's prohibition against willfully contracting oneself into slavery. Moral contractualists may justify paternalism on the ground that given appropriate knowledge and motivation, all reasonable people would agree to interference in certain circumstances, such as to prevent suicide caused by a temporary state of depression.

Paternalism is sometimes justified on the grounds of preventing harm. Mill's harm principle, however, justifies interference only in cases in which there would be harm to others; it prohibits interference to prevent self-harm or consensual harms. The harm principle would require toleration of (1) competent self-harm and self-imposed risk, (2) harm to consenting others, and (3) harmless acts. The harm principle could thus be applied to legally prohibit classes of actions intended to harm others (murder, rape, theft, assault) without their consent. The harm principle would also apply in upholding a zone of privacy for consensual or self-regarding acts involving consenting adults and in decriminalizing victimless crimes.

The harm principle justifies restriction of freedom on behalf of others to prevent risk or harm in cases involving children, the mentally incompetent, or those with impaired judgment or faculties because such individuals are considered incapable of authentic consent. Furthermore, the harm principle may also permit consensual or self-paternalism wherein competent individuals or groups choose to impose self-restraining measures, such as living wills or legislative limits, involving future acts.

Although the harm principle may be cited as a justifiable ground for restricting the freedom of individual agents, it leaves unresolved many of its disputed moral questions. For example, even if agreement were to be reached to disallow paternalism intended to prevent self-harm, consensual harm, or harmless acts, reasonable people could conceivably disagree about what constituted self-harm, harm to others, and valid consent. These reasonable disagreements remain contested issues, as illustrated by contemporary debates. The default framing of retirement savings plan options ("opt-in" versus "opt-out" as the default) is viewed by some as a protection of individual choice in the disposal of earned income and by others as a failure to provide proper incentives for individuals to avoid the risk of an impoverished old age. Despite scientific studies, some communities do not regard the risks of secondhand smoke sufficiently harmful to warrant indoor smoking bans. The debate over assisted suicide illustrates divergence of opinion about suicide as self-harm, its harm to others, and the validity of consent on the part of a person seeking assistance in committing suicide. While in some jurisdictions, young women under the age of 16 are considered capable of consent in contracting a marriage, other jurisdictions consider these same young women incapable of valid consent in seeking birth control or an abortion. In each of these examples, the harm principle is insufficient as a basis for achieving moral consensus.

Feinberg delineates principles for reconciling opposing views regarding permissible grounds for interference with someone's actions for the sake of preventing harm. First, he establishes distinctions: Self-inflicted harm is still harm; intended self-harm is different from unintended self-harm as a consequence of another intended action; some risks are more reasonable than others; voluntary assumption of risk is a matter of degree. He distinguishes between *strong legal paternalism*, which justifies state protection of people against their will from the harmful consequences of their own voluntary choices, and *weak legal paternalism*, which prohibits state interference except to protect individuals from self-harm from actions presumed to be nonvoluntary or coerced. Like Dworkin, he advocates weak paternalism as a means to provide protection for individuals in circumstances where the full exercise of volition may be compromised.

Paternalism Applied to Social Policy

The use of the law to restrict or require actions from people for their own good is known as *legal paternalism.* Societies may vary in the breadth or manner in which they use the law to restrict the freedom of their constitutive individual or group members, but every society applies some degree of legal paternalism to prohibit acts considered dangerous, risky, or reprehensible. Bentham classified laws by their design to (1) protect people from harm caused by others, (2) protect people from harming themselves, and (3) require people to help others. Bentham considered only the first class of laws to be legitimate.

Legal paternalism justifies state coercion to protect individuals from harm, inflicted by either themselves or others, and to give incentives for behavior that results in what is deemed good by lawmakers and others who bear the responsibility of acting in the public interest. As Feinberg notes, most societies try to find a reasonable balance between extreme paternalism, which infantilizes adults, and an absolute rejection of paternalism, which invalidates even the possibility of coercion as an instrumental means of achieving the good.

In a democratic society of political equals, the duly elected officials and appointed policy makers who make up the governing structure act as direct or indirect agents serving a citizenry of their peers. In this framework, limitation of individual freedom and autonomy for the sake of the common good is an act of self-governance; such self-imposed or consensual paternalism poses no moral dilemma. On the other hand, political and policy decision making in a complex society rarely involves the participation of the entire citizenry; actual decisions (laws, regulations, professional standards) are often made by a select group of stakeholders with specialized knowledge and privileged access to pertinent information and analysis. Perhaps more accurately referred to as "fraternalism" rather than "paternalism," actions taken on behalf of others in these circumstances exemplify the moral responsibility of the greater knowledge, power, or resources associated with specialized roles in a complex society of equals. For example, a public official closing impassably flooded roads during a hurricane would not be acting paternalistically. A group of legislators, policy analysts, and medical professionals who collaborate to restrict access, through safety or efficacy standards, to a particular drug may be acting beneficently and protectively on behalf of society on the basis of their specialized knowledge; this might be considered an example of weak or welfare paternalism because they are applying, in the public interest, knowledge or expertise not reasonably expected of ordinary citizens. It would be paternalistic if such a group were to withhold accessible and relevant facts or knowledge from the citizenry to intentionally diminish public participation in or awareness of the decision-making process.

Agents of governments, employers, families, professionals, and institutions often apply the harm principle to justify paternalism on the ground that an individual, or a class of individuals, lacks the capability for effective self-management in some essential aspect of life. These concerns are particularly evident in addressing specific areas of social policy and practice involving people with disabilities, the poor, the aged, and the deviant. Paternalism can be considered morally appropriate when those whose interests are at stake lack the capacity for self-determination, either temporarily or permanently. When people are dependent on society without evidence of contributory responsibility for their dependent condition, paternalism may be viewed as appropriate. When disability or incapacity is determined justly, paternalism allows able members of society to provide the less able with a quality of life, a level of human dignity, and relief from suffering that they cannot provide for themselves.

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See also Autonomy; Freedom and Liberty; Human Rights

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Patients' Bill of Rights

In March 1977, President Clinton appointed the Advisory Commission on Consumer Protection and Quality in the Health Care Industry (referred to here as the Commission) to develop a "Consumer Bill of Rights" to promote and ensure health care quality and value and to protect consumers and workers in the health care system. The Commission was composed of 34 members selected from the private sector. Members included representatives of consumer advocacy groups; institutional health care providers; health care professionals; health care insurers; health care purchasers; state and local government representatives; and experts in health care quality, financing, and administration.

In November 1997, the Commission submitted a report to the president containing the Patients' Bill of Rights.

The Patients' Bill of Rights has three major objectives: (1) to strengthen consumer confidence by ensuring that the health care system is fair and responsive to consumers' needs, provides consumers with credible and effective mechanisms to address their concerns, and encourages consumers to take an active role in improving and ensuring their health, (2) to acknowledge the importance of a strong relationship between patients and their health care professionals, and (3) to reaffirm the critical role consumers play in safeguarding their own health by establishing both rights and responsibilities for all participants in improving health care.

The Patients' Bill of Rights contains eight principal areas of rights and responsibilities:

1. *Information disclosure:* Patients have the right to receive accurate, easily understood information to help them make informed decisions about their health plans, professionals, and facilities.

2. *Choice of providers and plans:* Consumers have the right to a choice of health care providers that is sufficient to ensure access to appropriate high-quality health care.

3. *Access to emergency services:* Consumers have the right to access emergency health care services when and where the need arises.

4. *Participation in treatment decisions:* Consumers have the right and responsibility to fully participate in all decisions related to their health care. Consumers who are unable to fully participate in treatment decisions have the right to be represented by parents, guardians, family members, or other conservators.

5. *Respect and nondiscrimination:* Consumers have the right to considerate, respectful care from all members of the health care system at all times and under all circumstances. An environment of mutual respect is essential to maintain a quality health care system. Consumers who are eligible for coverage under the terms and conditions of a health plan or program or as required by law must not be discriminated against in marketing and enrollment practices based on race, ethnicity, national origin, religion, gender, age, mental or physical disability, sexual orientation, genetic information, or source of payment.

6. *Confidentiality of health information:* Consumers have the right to communicate with health care providers in confidence and to have the confidentiality of their individually identifiable health care information protected. Consumers also have the right to review and copy their own medical records and request amendments to their records.

7. *Complaints and appeals:* All consumers have the right to a fair and efficient process for resolving differences with their health plans, their health care providers, and the institutions that serve them, including a rigorous system of internal review and an independent system of external review.

8. *Consumer responsibilities:* In a health care system that protects consumers' rights, it is reasonable to expect and encourage consumers to assume reasonable responsibilities. Greater individual involvement by consumers in their care increases the likelihood of achieving the best outcomes and helps support a continuous quality improvement, cost-conscious environment.

Many other areas of the health care industry and various health care providers have developed their own Patients' Bill of Rights. For example, there is a Pharmacy Patient's Bill of Rights, a School of Dentistry Patient's Bill of Rights, and a Mental Health Patient's Bill of Rights, and the American Hospital Association has created its own Patient's Bill of Rights. Many state and local health care providers have established rights and responsibilities for individuals, such as the Child's Bill of Rights developed by the Children's Hospital of Central California.

The Pharmacy Patient's Bill of Rights delineates the patient's rights and responsibilities with respect to appropriate drug therapy and the patient's responsibilities and the pharmacist's rights with respect to the quality of services provided. The School of Dentistry Patient's Bill of Rights emphasizes care that is of high quality, timely, and courteous. It also highlights issues of informed consent, the right to have patients' complaints heard, patient record confidentiality, and access to emergency care.

Similarly, the Mental Health Patient's Bill of Rights is a detailed document that focuses on the mental health patient's right to know. It describes the patient's rights and responsibilities in terms of the benefits provided, expectation of professional expertise, contractual limitations, appeals, and grievances. The Mental

Health Patient's Bill of Rights also discusses issues of confidentiality, free choice, determination of treatment, parity of treatment, nondiscrimination, benefits of usage, treatment review, and accountability among treating professionals.

The Child's Bill of Rights provides specific rules and requirements. For example, as patients of the Children's Hospital of Central California, children have the right

- to be called by name and not by a number or by the name of the illness;
- to be greeted with a smile and treated with loving care;
- to know where they are supposed to be before they have to be there and to have their daily routine remain as normal as possible;
- to have their family members with them, whenever the family can stay, as long as the family members do not get in the way of their care; and
- to not have people whispering about them over their beds or out in the halls unless they know what is happening and not have people talking about them as if they were not in the room.

—*James Weber*

See also Consumer Activism; Consumer Protection Legislation; Consumer Rights; Consumer's Bill of Rights; Health Maintenance Organizations (HMOs); Rights, Theories of

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Patriarchy

Patriarchy is a form of social organization in which the father is the head of the family or a society in which men govern or rule. Patriarchy was a system that perpetuated itself because the male children would inherit the father's lands, wealth, and so on. The influence of patriarchy can be seen in all the world's cultures to varying degrees. The number of men in important governmental positions compared with the number of women is frequently quoted when discussing both the causes and effects of patriarchy. Feminists have expanded the definition of patriarchy to include how cultures view maleness and masculinity as the standard others are judged against in an attempt to expose power relationships between groups and individuals.

Due to the focus of this encyclopedia on business ethics and society, this entry will discuss the second definition of patriarchy as it affects business. There are two distinct views regarding the relationship between capitalism and patriarchy. The "unified system" theory contends that men's authority over women causing economic dependency is due to women's ability to have children. Thus, according to this view, capitalism and patriarchy are both part of the same overarching social system because they share the same concept of gender roles: men as powerful authorities and women as caretakers. A less extreme interpretation of this theory is that it is natural and appropriate for men to be in power and women to be in the home due to each gender's supposedly natural inclinations and skills. Another theory states that women's economic dependency on men is just one way the social power system becomes obvious. This power system, patriarchy, may or may not correspond with capitalism. This theory is the "dual systems theory," meaning that patriarchy and capitalism may be similar in some ways and at some moments in time, but they are not the same system. One persuasive example is that although women have gained social rights in some countries and the old rules of patriarchy have become less powerful, the free trade market has not changed and economic development of those countries has continued to grow, thus implying that patriarchy is not a necessary condition for capitalism. Arguments have been made for and against each theory.

Many businesses seem to follow the pattern of patriarchy, with men in key positions of power. While this trend has slowly been changing in developed nations, patriarchy is still accepted as the natural order of society in many developing countries. There is pressure on individuals within these nations to maintain this system. For example, women in many developing countries are not given access to education, believed by many researchers to be a prerequisite for becoming economically independent. Some believe that educating a female family member would put one's family in danger. There have been examples of rapes and murders as a reprisal for such actions. Keeping their female counterparts subservient may play a role in the lack of economic development in these countries because women become an unutilized resource of labor and innovation. Nations that have recently become more accepting of women in the workforce have, in general, seen a more marked increase in national wealth. India and China are examples of this.

In developed countries, legal requirements for equal opportunity have helped increase the number of women in the workforce. However, on average, women make less than men in the same position with comparable skills, and the promotion of women into managerial and executive positions has not advanced at a similar rate. Some researchers have labeled this the ghettoization of occupations. Women are relegated to support roles within the corporate system, such as administrative assistants or assistant managers, and struggle to move within the company both vertically and horizontally. Researchers have also documented the "glass ceiling," where a woman finds that she cannot move beyond a certain point in her career, while her male counterparts continue to rise up the ranks of the business.

Curiously, while some Marxist feminists have argued that capitalism simply reinforces the patriarchal oppression of women, a free market also provides the possibility for social change. By allowing women the opportunity to work and become more independent, capitalism has changed the landscape of the human family unit. If enough women become empowered in this way, the structure of corporations and society will change, as has already been seen in developed nations.

—*Amy Parziale*

See also Authority; Autonomy; Barriers to Entry and Exit; Capitalism; Civil Rights; Darwinism and Ethics; Developing Countries, Business Ethics in; Diversity in the Workplace; Equal Employment Opportunity; Equality; Equal Opportunity; Equal Pay Act of 1963; Ethics, Theories of; Ethics of Care; Family-Friendly Corporation; Feminist Theory; Gender Inequality and Discrimination; Glass Ceiling; Human Rights; Industrial Revolution; International Business Ethics; Maternal Ethics; Multiculturalism; Other-Regardingness; Poverty; Preferential Treatment; Reverse Discrimination; Rights, Theories of; Right to Work; Sexual Harassment; Stress, Job; Values, Personal; Violence in the Workplace; Wages for Housework; Women in the Workplace; Women's Movement; Work and Family; Work-Life Balance

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Pension Benefit Guaranty Corporation (PBGC)

The Pension Benefit Guaranty Corporation (PBGC) is a government body established by Title IV of the Employee Retirement Income Security Act of 1974 (ERISA) to ensure payment of pension plan benefits when the plans are terminated. The PBGC is headed by an executive director who reports to a board of directors. The board of directors consists of the secretaries of labor, commerce, and the treasury and is chaired by the secretary of labor. The PBGC states that its mission is to encourage the continuation and maintenance of voluntary private pension plans, provide timely and uninterrupted payment of pension benefits, and keep pension insurance premiums at a minimum.

The PBGC acts as an insurer and guarantor of private pension plans with two main insurance funds, one covering pension plans sponsored by single employers and the other covering multiemployer pension plans. In 2005, the single-employer insurance program covered 34.6 million workers and retirees in 29,651 pension plans. The multiemployer program covered 9.8 million workers and retirees in 1,587 pension plans.

Employers that sponsor pension plans pay the PBGC insurance premiums at a rate that is set by Congress. The PBGC also receives the assets of the plan when it takes over a pension plan. Pension plans paid the PBGC yearly insurance premiums of $2.60 per worker or retiree in multiemployer plans and $19 per worker or retiree (plus $9 for each $1,000 of unfunded vested benefits) in single-employer plans in 2005.

The PBGC takes over a pension plan when an employer voluntarily closes its plan. This could occur as a standard termination, in which case the plan must have enough money to pay all benefits before the plan can end, or it could be a distress termination, where the plan does not have enough money to pay all benefits and the employer must prove financial distress. Here, the PBGC pays plan participants the guaranteed benefits. The PBGC can also seek to close a single-employer plan without the employer's consent when the employer deems that such an action will protect the interests of workers, the plan, or the PBGC's insurance fund. The PBGC guarantees pension benefits to a maximum level that is set by law and adjusted annually. The maximum pension benefit guaranteed for plans terminated in 2005 was set at $45,613.68 a year.

While the PBGC exists to ensure the promised benefit of terminated plans, it is operating at a substantial deficit and faces a looming crisis. Until 2002, the PBGC had a $7.7 billion surplus. In 2003, it ran an $11.2 billion deficit and has an $85 billion exposure to companies with a junk bond rating (i.e., bonds rated below investment grade, which typically offer a higher return) that are at higher risk of default on their pension obligations. The PBGC also estimated a $400 billion gap between assets and liabilities in the private defined-benefit pension system in the United States in 2003.

Social and Ethical Issues

The charter of the PBGC to both promote private defined-benefit pension plans and ensure the security of those plans presents a problem for the agency. As the claims on the PBGC increase, it is pushed to tighten regulations and increase the insurance premiums on such plans. Those are actions that in turn lead plan sponsors to close weak plans and others to avoid establishing new defined-benefit plans.

With the government insuring private defined-benefit pension plans, this creates a moral hazard. A private employer with limited cash or in financial distress may not be able to provide workers with increases in cash compensation, but it can provide enhanced pension benefits, as ERISA allows the sponsor 30 years to fund the benefit. Employees would be inclined to accept the enhanced pension benefit because it is guaranteed by the PBGC. Thus, increasing pension benefits in financially distressed firms becomes a more viable action because of the insurance underwriting the future promise, which in turn increases the overall level of risk in the pension system.

Even more important are the implications of shifting the long-term economic and financial risk incurred by private companies to the government. When private companies are able to step out from under the long-term financial commitment of a pension plan on a voluntary basis, it can affect the competitive relationships among employers in a given industry. Companies that seek to support pension plans may find themselves at a disadvantage relative to firms that shift their long-term pension liability to the PBGC.

Finally, as the premiums paid by plan sponsors prove inadequate to cover the benefits insured by the PBGC, meeting that obligation could require additional funding from tax revenue. Since the majority of taxpayers are not covered by a defined-benefit pension plan, they will find themselves taxed to pay benefits to individuals who have a benefit that is not available to them. Furthermore, no such protection is afforded to the defined-contribution form of pension plans, which are more widespread.

—Joanne H. Gavin and Ken A. Sloan

See also Employee Retirement Income Security Act of 1974 (ERISA); Moral Hazard; Pensions

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Pensions

Pension Programs

Pension benefits are a critical component of income security for retired workers. In the broadest terms, a pension program is any program that is established by means of which a worker earns a benefit that will provide income during retirement. Favorable tax treatment dating back to 1921 encouraged the development of the U.S. pension system. Most pensions take the form of an annuity and generate periodic payments to the recipient. They can be set up by the individual's employer, trade unions, or the government. There are two main types of pension plans: defined benefit (DB) and defined contribution (DC).

Defined-Benefit Plans

A DB plan provides benefits based on a formula that typically multiplies years of service, final average pay, a pension rate (e.g., 1.5% for every year of service), and frequently a partial offset for the primary social security benefits the participant receives. Under a DB pension plan, the pension benefit received by the participant is defined by the plan's formula and is usually structured to provide an annual pension payment during the life of the worker, with a reduced payment made to the spouse after the worker's demise for the duration of his or her life. The employee is able to approximate the pension he or she would receive by calculating the number of years of service he or she expects to have at retirement and by estimating what the final pay would be. The DB plan formula represents a promise: "We (the company) will pay you a pension of *x* dollars dependent on how long you work for us and what you are being paid just before your retirement." The employee does not have to be concerned with any investment risk, and as long as he or she remains employed by the company, the pension is perceived to be secure and backed by the assets of the pension trust established to meet those future promises. The employee does bear the risk that after retirement, the real value of the pension received will be eroded by inflation since the benefit paid is generally a fixed amount. In addition, there is a growing awareness of the risk associated with an employer's termination of or default on a DB plan. DB plan designs are effective at ensuring that the funds in the plans are only accessible for the intended purpose of income during retirement.

Defined-Contribution Plans

DC plans are most commonly 401(k)-type plans, with more than 80% being profit-sharing and thrift-savings plans. Initially, DC plans were offered as supplements to or in conjunction with DB plans. Increasingly, DC plans are being offered as the sole pension plan by organizations. DC plans address a key issue important to participants, the lack of portability in DB plans. However, DC plans make retirement income heavily dependent on the investment decisions made by the individual plan participant and shift that investment risk from the employer and plan sponsor to the individuals participating in the plan.

In a DC plan, the employer eliminates both the long-term obligation and the funding volatility faced in DB pension plans, promising instead to contribute a specific amount each year pegged to variables such as participant pay or firm profitability. In a typical DC plan, the employer may promise to contribute a certain amount each year into an account established in the plan for the participant. DC plan designs eliminate the portability problem inherent in the DB plan design. Whatever a person earns at one company remains invested and growing, so the pension funds ultimately available to that person on retirement would be, theoretically, the same whether they were all earned through one employer or represented funds accumulated from several DC plans. In a DC plan, the issue from the participant's perspective is not portability but investment risk.

Comparison of the Plans

The primary downside of a DB pension plan, from the perspective of most employees, is the lack of portability. While legislation established vesting and accrual requirements that protect the pension benefit earned by the employee, the structure of the promise is such that if an employee's career consisted of periods at more than one employer (even if each employer had an identical DB plan), the cumulative pension benefit would be less than the benefit earned if the entire career was at one company. This relates to the benefit being tied to final average pay.

In a DB pension plan, the employer, or plan sponsor, is expected to make contributions to a trust in order to fund the pension liabilities being incurred by the plan. In addition to being affected by the demographics of plan participants, the amount of the employer contribution is determined in large part based on the investment results of the trust. During years in which plan assets earned a higher return, employer contributions would be lower, and during years in which plan assets earned a lower return, employer contributions would be higher. In a DB plan, it is the employer that bears the investment risk. This presents DB plan sponsors with a degree of funding volatility for obligations incurred under the plan, which spans a very long period of time.

However, while the organization bears the investment risk, the participant faces a risk associated with the termination of or default on the plan by the employer. When the promises made span decades, there is no assurance that the employer will still be in business, and on termination or default, the plan is taken over by the Pension Benefit Guaranty Corporation (PBGC), and there is a high probability that the payments available under PBGC guidelines will provide for a substantially smaller pension payment than had been earned under the plan.

Reducing funding volatility was a major driver behind employers' shift from DB to DC pension plans. In a DC plan, the employers' obligation is satisfied once they make the promised annual contribution. It is the employee who will benefit if the return on the assets in his or her account is higher than planned, and it is the employee who will be affected if the return on assets in his or her account is less than planned or if the plan experiences an investment loss. This risk is especially acute as the employee nears retirement, since even small-percentage losses translate to relatively large dollar losses and the employee will have less time to make up for losses or underperformance in the years remaining before retirement.

Another criticism of DC plans is that pension funds can be accessed or diverted from the intended purpose. In a DB plan, the assets invested in the pension trust to cover the participants' future pension obligations are not available to them except for the promised purpose of providing income in retirement. However, in most DC plans, the employee has access to the funds and can use those funds for purposes other than retirement income. When I terminate my employment with an employer, my DC plan account balance can be withdrawn and rolled over into my new employer's DC plan or into an individual retirement account (IRA). However, I can also take those funds and use them for any purpose, incurring in that year both an income tax liability and an early withdrawal penalty. Even if I remain with my employer, I can often withdraw money for specific purposes such as medical expenses, educational expenses, or purchase of a home. Many plans also provide loan features that allow participants to borrow against their accounts, thus reducing the balance invested and accumulating earnings.

Social and Ethical Issues

Irrespective of the form of the pension program offered by employers, there is an implied covenant that the program will provide some degree of reliable and adequate income in retirement, and some view the decline of the DB pension plan as meaning that fewer individuals will have that. Those who view the DB plan as the best vehicle to deliver on this promise look to Congress to act in order to reverse the trend. Among the actions they call for are reducing the overregulation of DB plans, repealing the cap on compensation that can be used to calculate a DB plan benefit, privatizing the PBGC and shifting it from a requirement of plan sponsors and employers to a voluntary election made (and paid for) by individual plan participants, and easing the ability of employers to recover surplus assets in DB plans. While there is no doubt that some actions by Congress could increase the relative attractiveness of DB pension plans, the question should not be how we can make DB plans more attractive for employers but whether moving back in the direction of DB plans would provide for a greater degree of adequate and reliable retirement income.

Some Challenges in Defined Benefit Pension Plans

The concept behind a DB pension plan is straightforward. An employer estimates the age at which plan participants will retire, the amount of the annuity they will receive at that time, and how long they will receive those payments based on life expectancy. From that, enough money must be set aside to fund those payments based on estimated earnings from the assets invested.

The employer bears the risk associated with underperformance of the investments. The employer also bears the risk of not having sufficient funds set aside if life expectancy is underestimated. This is becoming an increasingly large risk as we see medical and technological advances increase life expectancy in ways that are at best difficult to forecast. Those are the traditional risks of which plan sponsors are generally quite cognizant. They are risks inherent in any forecast or plan.

An inherent structural issue with a DB plan design, and a potentially more serious risk, is associated with the maturation of the company sponsoring the DB pension plan. A DB pension plan carries with it a promise that is multigenerational in nature. An employee hired out of college may work for four decades before retiring and then draw pension benefits for two or more decades after leaving the company's employment. In a young company, the majority of payments from the plan are 30 to 50 years off. There is sufficient time to invest, and any shortfalls from expected returns on invested assets have time to be recouped.

As the company matures, the plan faces an increasing number of pensioners in relation to active participants. It also means that a higher proportion of the fund's assets will be needed to make the promised payments each year. Just as individuals in a DC plan face greater investment risk as they approach retirement because the impact of shortfalls will be larger and there will be less time to recoup them, sponsors of DB plans face similar risks. While the risk increases for a mature company's DB plan, with prudent management of that risk to ensure that cash inflows from investment returns on the plan's assets and cash outflows to retirees are matched, the plan can continue to operate without difficulty. This translates to a need for a much more conservative investment strategy than is in place today in DB plans. It is also required that there be an ongoing new flow of contributions to offset any shortfall from invested assets.

A critical point is that DB plans by design become increasingly risky as they mature, and unless a plan remains in place and is active, as more of the participants begin drawing out pensions, there is an increasing likelihood that the trust will be unable to deliver the promised benefits even if it is fully funded at the time it is terminated. Even for active plans, the ability of the plan to meet its promises is affected by the mix of new and active participants with retirees. The higher the proportion of retirees to active participants, the greater the risk presented to the plan. Thus, there is a structural mismatch between the dynamic relationships that make a DB plan viable and the underlying demographics of the workforce—that is, an aging population and an increasing ratio of retirees to individuals active in the workforce.

These structural issues are exacerbated when you place them in the context of economic conditions. In its 2004 bankruptcy filing, U.S. Airways said that it would be "irrational" to keep making contributions to its underfunded pension plans, since it "provides no benefit" in helping the company stay alive. While this may be one of the more dramatic examples, it illustrates an important point. Pension assets are invested, and the majority of those assets are in equities. When the economy weakens and stock values fall, the value of the assets held in pension plans falls, often creating an underfunding. In 2002, two thirds of the 360 Standard and Poor 500 companies that offered a DB plan indicated that they were underfunded. Under the DB model, the employer should increase contributions to make up for that shortfall. However, if the reason underlying the weak stock values is related to weaknesses in the economy, then the company sponsoring the plan is also likely to be facing some business pressures. The greater the underfunding and the greater the business pressures, the greater is the likelihood that the company will either elect to terminate the plan or be forced to terminate it through the actions of creditors.

An employer offering a DB pension plan has a responsibility to employees to make sure that the plan will be there when they retire and will be able to meet the payments promised. Yet 75% of DB plans were not there to provide the promised benefits. Economic necessity (or expediency) resulted in their termination. Those terminations meant reduced benefits to participants. When three quarters of plans of a given design, namely DB plans, prove to be not viable, it is unreasonable to strive to perpetuate that approach to providing retirement income.

Issues With Defined Contribution Plans

Structurally, DC plans do not face the issues of underfunding the benefits promised because the promise generally takes the form of a contribution to the employee's account in the year in which the benefit is earned. For employers, this removes the funding volatility and the decades-long liability that plagues DB plans. Nor does a termination of a DC plan carry the same loss for participants since the assets accrued belong to the participants and not the trust. Hence, they remain invested and earning a return for the participant. A DC plan also eliminates the negative impact on pension benefits associated with job changes.

These issues are not structural issues in the concept of a DC plan but issues related to design features. DC plans can provide a pension benefit that is as large as or larger than that accruing from a DB plan. Issues of adequacy stem from two primary sources: (1) the accessibility of the money intended to provide retirement income for other purposes and (2) the quality of the investment decisions made by the participant and the risk associated with those decisions.

DC plans present an appealing source of funds for participants facing financial needs. They have an account that has what they perceive to be a substantial balance, and they may be decades from retirement. Under that scenario, many individuals tap into their plans to fund other financial needs. Consider individuals who are laid off by their employer. They take their DC plan assets and roll them into an IRA. As unemployment drags on beyond the time covered by their severance payment, they withdraw some money from their IRA. They pay income tax on this withdrawal and also pay a 10% penalty for making a withdrawal before age 59½. In addition, many DC plans allow the participant to take out a loan for any reason. In 2003, 18% of all eligible participants in 401(k) plans had an outstanding loan against their account. If DC plans are to provide adequate retirement income, the issue of access to retirement funds for nonretirement purposes needs to be addressed.

The issues of investment decisions and risk pose a more substantial problem when it comes to ensuring the adequacy of retirement income from a DC plan. With 64 million active participants in private sector DC plans in 2004 and the performance of the stock market since 2001, large numbers of employees near retirement are experiencing firsthand the issues of investment risk and fund adequacy. By some estimates, many DC plan participants will need 30 years to make up for the losses incurred in the bear markets of 2000 and 2001.

While investment risk cannot be eliminated, it can be reduced. First, prudent management of investments requires determining objectives and determining the best way to achieve those goals. Most individuals have no conception of how much money they need to accumulate in order to provide a specific level of income for their retirement years. Most individuals don't know how many years of retirement they should expect—that is, projected life expectancies. Making matters worse, even if a participant knows that some investments generally provide higher returns along with higher risks, they generally have no way of assessing the degree of risk that is appropriate based on their age and the accumulated assets in relation to retirement income targets. All this would suggest that more emphasis on education and communication is necessary, which should be provided to employees by employers sponsoring DC plans. While this is appropriate, plan sponsors need to consider design elements that either allow or require professional management of accounts. Regulations currently allow for such plan-directed management; however, legislation would need to address the fiduciary risks associated with that approach, as well as the fiduciary risk that emanates from employees being provided education, which is currently treated by the regulations as providing financial advice.

One way of reducing the risk some employees experience with the collapse of their 401(k) plan is to adopt regulations that prohibit concentrating assets in any single investment, most commonly today the employer's company stock. DC plan designs that direct company contributions to company stock should be severely restricted, if not prohibited outright. Enron employees were covered under a DC plan that required that the company's contribution be held in the employee's DC account as Enron stock. With the collapse of Enron, the value of those holdings dropped precipitously and effectively wiped out the value of all contributions made by Enron toward the retirement of the employees. Furthermore, the percentage of funds in a DC plan that participants can direct to any single source should be limited. It would be advantageous if such regulations also included age-based risk parameters. Such guidelines could provide the framework to shape investments toward lower-risk portfolios as an individual participant nears retirement.

Finally, DC plans need to move to a design that enables participants to easily translate their DC plan assets into an annuity income stream. When an individual is in retirement and the assets need to be managed to provide an income stream for 20 or more years, few individuals can prudently manage the risks and investment fluctuations that will occur over that period.

Conclusion

The controversy over DB versus DC will continue to be a subject of debate as long as some individuals feel that employers are moving from DB to DC to meet their own financial needs and manage their risks by shifting them to the employee, while others feel that the move is logical, even ethical, given the financial volatility of many corporations in the 21st century. This discussion has attempted to highlight some issues that indicate that forcing companies to continue offering DB plans may not be as simple as many workers believe it to be.

—Joanne H. Gavin and Ken A. Sloan

See also Benefits, Employee; Deferred Compensation Plans; Employee Retirement Income Security Act of 1974 (ERISA); Enron Corporation; Individual Retirement Accounts (IRAs); Pension Benefit Guaranty Corporation (PBGC)

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People for the Ethical Treatment of Animals (PETA)

People for the Ethical Treatment of Animals (PETA) is an organization committed to ending abusive treatment of animals in business and society and promoting consideration of animal interests in everyday decision making and general policies and practices. Founded in 1980 by Ingrid Newkirk and Alex Pacheco, PETA's objectives have been supported by scholarly work in ethics—most notably, Peter Singer's *Animal Liberation,* which Newkirk cites as providing the impetus behind PETA's establishment.

PETA's earliest efforts concentrated on exposing the abuse of animals in experimentation, and this area continues to be a focus of its activities. PETA has made efforts to minimize the suffering of animals in laboratory settings by appealing to industries that have traditionally engaged in extensive and invasive animal testing—such as the cosmetics and pharmaceutical industries—to discontinue animal testing in favor of cruelty-free alternatives. Business has responded to these efforts. Many cosmetics industry leaders, for example, have discontinued the practice of testing on animals, and more than 500 cosmetics companies have signed a pledge of assurance that they will not engage in animal experimentation. The auto industry has also responded to PETA's concerns about the treatment of animals in testing by eliminating the use of animals in crash tests; the successful alternative of using crash test dummies has become an industry standard.

In the course of its growth and influence, PETA's activities have targeted other areas of commerce closely associated with animal abuse. PETA's concern for the maltreatment and destruction of animals for fur in the fashion industry, for example, has prompted many industry leaders, including Georgio Armani, Calvin Klein, and Ralph Lauren, to go "fur-free." The once standard use of animals in entertainment, such as in the circus industry, has also been reduced. There is tighter legislation, and new industry standards are being set by competitors, such as Cirque du Soleil, that do not use animal acts. Other significant changes include raising standards for the treatment of animals by suppliers for fast-food chains and increasing public awareness of the abusive practices of suppliers in countries that lack protective legislation, such as China.

PETA's efforts to alter public attitudes toward animal concerns include creative campaigns that, while serious in their message, include humorous and spoof-like elements. For example, in addition to distributing information on the health costs associated with meat products and exposing the abusive treatment of animals used in the meat industry, such as calves and chickens, PETA developed a spoof on the beef industry's "Beef . . . It's What's for Dinner" campaign by recasting the slogan as "Beef . . . It's What's Rotting in Your Colon." While such an approach has been effective, it is also controversial and has been objected to by opponents of PETA's position on animal interests as well as those who favor the position but take a more moderate view concerning the methods of promotion.

PETA's position justifying the consideration of the treatment of animals is that animals have rights in proportion to their "interests," and that these rights should be respected and protected. As PETA explains it, an animal, like a human, has an interest, for example, in not experiencing pain unnecessarily. Thus, that interest should be taken into consideration—the right not to have unnecessary pain inflicted should be protected. An animal does not, however, have all the interests that humans do. For example, animals do not have interests in voting, so they, like children, do not have rights to vote that should be protected.

While there have been objections to its position, many of PETA's advancements in promoting animal protection have resulted from its exposure of cruelty and abusive conditions alone. To objections that have been raised, such as that animals do not have rights because they cannot reason and that changes in attitudes and practices toward animals decrease concerns about people, PETA replies that such claims tend to be irrelevant to the issue or are based on misunderstanding. There are, for example, humans who cannot reason, or reason as well as some animals, but they are assumed to have rights in proportion to their interests.

Hence, there is no principled reason to deny that members of other species have rights in proportion to their interests on the basis of reasoning capacity. Calling on the positions of Albert Schweitzer and Jane Goodall, PETA also claims that there is reason to think that the promotion of concern for the well-being of animals tends also to promote, rather than weaken, concerns about the well-being of humans.

—E. D. Kort

See also Animal Rights; Animal Rights Movement

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Perfect Markets and Market Imperfections

The perfect market entails a structure of production and exchange in which optimal outcomes, both private and social, are attained efficiently and simultaneously without the need for intervention by nonmarket actors. In other words, the price and profit signals in the market lead automatically to production efficiency at minimum unit cost and to allocative efficiency at the most desired mix of output. In a perfect market, the self-interested behavior of individuals responding to price signals is sufficient to direct society as it answers the basic questions of what to produce, how to produce, and for whom to produce.

The model of the perfect market rests on the assumption of perfect rationality in the utility and profit maximization motives of economic agents (consumers and producers). Additional assumptions of a perfect market include the voluntary exchange of homogeneous goods and services within complete and perfectly competitive markets under perfect and symmetric information about the prices, quality, and availability of output. These assumptions ensure that no individual market participant can influence market price and that all necessary inputs and possible outputs have a pecuniary value and are traded unconstrained by time or circumstance. In addition, one must assume the absence of several noteworthy features of actual markets, which include externalities, public goods, direct transaction costs, asset specificity, taxes, and other distortions, as well as economies of scale and scope and other resource, political, or technological barriers to entry and exit. In total, the restrictions result in a level of certainty and stability in the market that generate both the full and efficient employment of resources as well as the maximum and correct mix of output by each firm.

However, the assumptions necessary to sustain the model of perfect markets—with its Pareto-optimal levels of production and allocative efficiency, market order, and social coordination—limit its ability to explain or anticipate actual economic processes and events. As such, the perfect market model remains more an abstract theoretical construct that forms an ideal and useful point of reference against which imperfect market structures such as monopoly, oligopoly, and monopolistic competition can be assessed.

The Behavior of a Perfect Market

Although markets have existed since the Stone Age, the concept of a perfect market developed during the Industrial Revolution as the focus of economic activity changed from the motive of subsistence to one of gain. Adam Smith employed the idea of an "invisible hand" to illustrate how the motive of gain operates through the self-interested behavior of individuals who, by responding to price and profit signals, unintentionally promote wider social interests.

Each producer is a price taker for a homogeneous good or service who has no control over the price he or she can charge in the market. Because each producer would like to maximize profits, his or her output settles at the level where marginal cost equals marginal revenue. If the market price of a product or service is sufficiently high at this level to generate profits in excess of the rate normally expected from the next best alternative use of resources, producers are said to be earning economic profits. In this instance, the producer's return is above the normal rate sufficient to maintain it in production. Under perfect market conditions, this result is short-lived as new suppliers are immediately attracted into the market. The response is immediate because the absence of specific assets and economies of scale or scope, as well as the presence of perfect markets to price and trade assets, leads to little, if any, distinction between fixed and variable costs. As a consequence, suppliers instantaneously enter and exit, and there is no distinction between the short- and long-run market conditions.

Typically, the markets for agricultural commodities and financial instruments are used to illustrate the behavior of a perfect market. In these cases, the main assumptions relating to numerous producers of identical products with low barriers to market entry are present. For example, if the market price of soybeans should exceed the average cost of production, the sale of soybeans generates revenue in excess of all implicit and explicit production expenses. Consequently, farmers will be willing, able, and motivated to switch quickly to the cultivation of soybeans or to sell their stored stocks. Although no individual farmer is large enough to affect the market price, the combined shift by numerous farmers will lead to an increase in the market supply of soybeans, which consequently puts downward pressure on the price. As the price of soybeans declines, economic profits (or what might be considered excess profits) diminish, and farmers switch again to the cultivation of other crops. Should agricultural prices decline in general, those farmers who are no longer able to cover their costs of production will exit the market and thereby free resources for other uses. Because of their structure and the prompt reaction by market participants, perfect markets function to ensure production efficiency where price equals minimum average cost.

Along with efficiency in production, perfect markets also ensure allocative efficiency. Here, society achieves its optimal combination of outputs. Following the above example, when the market price of soybeans results in economic profits, consumers are signaling a desire for a different mix of output—in this case, a mix that includes an increased supply of soybeans. Consumer utility, as revealed in the market price, exceeds the opportunity cost of production, as measured by the average cost of resources used in production. In a perfect market, allocative efficiency is quickly established as resources are redirected to soybean production, thereby increasing supply, reducing prices, and eliminating economic profit. The elimination of economic profit indicates that consumers are getting exactly the amount of soybeans that they desire, again at a price equal to the minimum average cost of production.

Market Imperfections

In reality, conditions and structures are often less than ideal, and markets might not function automatically to achieve the efficient outcomes predicted by the perfect market model. The failure of the market mechanism to generate optimal outcomes is commonly attributed to one of three sources: the presence of market power, externalities, and public goods. In each of the three cases of market failure, the market directs resources away from levels of productive efficiency and fails to produce the optimal mix of output desired by society.

First, the presence of economies of scale; information asymmetries embodied in technology, trademarks, and patents; and brand differentiation through marketing creates barriers that often hinder market entry and exit. These characteristics confer a degree of market power to an established producer, at least in the short run, that impedes the function of the highly competitive structure described in the soybean example. Instead of numerous producers each too small to directly affect market supply and price, a limited number of producers might operate behind high market barriers. Consequently, output is restricted to and maintained at a level that results in both production inefficiency and prices that generate economic profit. Should a farmer have a patent on a strain of insect- or drought-resistant soybean, the resulting power to control the supply of this desirable commodity will prevent the perfect market model from functioning as assumed.

Second, the cost or benefit of an activity or transaction often spills over to a third, unrelated party. Because market prices might reflect only private considerations, they likely do not measure the entire value to society of a specific productive activity. These indirect considerations are known as externalities and, like market power, also prevent markets from operating as assumed in the perfect market model. When production generates external costs, a reliance solely on market prices can result in overproduction. Conversely, output that generates external benefits can lead to underproduction. With our example of soybeans, farmers might not include the effects of pesticide or fertilizer use in their measure of market price.

Therefore, if the negative social effects of runoff on water supplies are not factored into the price of soybeans, the market price of soybeans will not reflect their true social cost. As a result, the market produces too many soybeans, with its resultant pollution—more than would be provided if all private and social costs were considered.

Third, some output—known as public goods—generates economic value that cannot be limited to specific, paying consumers. Once these outputs are available, producers are unable to exclude those who do not pay from their benefits. In addition, consumption of public goods by one individual does not lessen the amount available for consumption by others. The nonexcludable and nondivisible characteristics of public goods result in free rider problems wherein everyone simply waits for someone else to supply the output. As a result, the market alone is unable to produce these goods in sufficient amounts. The soybean farmer does not face this problem since soybeans produce private benefits only for the individual consumer. Other services such as national defense or airport security are not similarly excludable and require nonmarket, usually government, intervention to ensure their production in the amounts required by society.

Generally, market imperfections can be ascribed either to the inability of the basic assumptions of the perfect market model to hold or to the failure of the market mechanism to function in the prescribed manner. With the former, for example, the assumption that information is precise, symmetric, and perfectly available results in a level of certainty that is rare in reality. The presence of imperfect information often results in uncertainty before a transaction in the form of adverse selection bias and high search costs or uncertainty after a transaction in the form of principal-agent problems and high enforcement costs. On the one hand, the imperfections issuing from any or all of the sources of market failure present opportunities for private gain as individuals design and implement strategies to take advantage of these deficiencies. On the other hand, market imperfections also result in socially suboptimal outcomes that compel intervention or regulation on the part of the state in an attempt to offset the failure.

Because government actions and other extramarket regulation interfere with the market process described above, some political and economic observers frequently prescribe a hands-off (or laissez-faire) approach that relies on price and profit signals to efficiently direct the market process. A balanced commentary here would consider the inability of markets to operate perfectly in tandem with the inability of government intervention to unambiguously remedy these shortcomings.

The perfect market concept, along with the origin and scope of market imperfections, provides essential elements in understanding how societies attempt to achieve ideal market outcomes through a mix of private and public actions. As a result of this diverse interplay between the private and public sectors, there exist a variety of state/market linkages—from laissez-faire to corporatist to command approaches—that prevail from one country to another.

—Gerald Groshek

See also Economic Efficiency; Externalities; Free Market; Laissez-Faire; Mixed Economy; Opportunity Cost; Pareto Efficiency; Profits; Regulation and Regulatory Agencies

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Persuasive Advertising, Ethics of

One of the standard questions that is addressed by business ethics is whether or not there is something ethically objectionable about some or all forms of advertising. This question is usually posed in terms of asking whether advertising is merely the provision of information to consumers that enables them to find the right product to satisfy their preexisting desires or needs or whether advertising manipulates, brainwashes, or deceives persons into buying products that they would otherwise have had no interest in purchasing. That is, this question addresses the ethics of using what is termed persuasive advertising rather than the ethics of using what is termed informational advertising. Questioning the ethics of using persuasive advertising is distinct from other ways in which advertising can be subject to ethical criticism—for example, advertising addictive products such as cigarettes or alcohol or advertising to children.

Types of Advertising

In general, there are seven different types of advertising recognized by business ethicists. The first is pure informational advertising. Such advertising merely conveys straightforward information about the product that it is being used to promote. For example, if the product in question is a certain type of car, such advertising will present factual information about the car in question, such as its top speed, its costs, and its safety rating. The second type of advertising is deceptive advertising. Such advertising presents information about the product that it is promoting as though it were true information, when, in fact, the advertiser believes the information to be false. For example, were a certain brand of cigarettes to be advertised as being good for its smokers' health when the advertiser believed that smoking it was in fact harmful, such advertising would be deceptive advertising. (It is important to note here that for an advertisement to be a deceptive advertisement, the advertiser need not know that he is providing his consumer audience with false information. Instead, he need only believe this to be the case.) The third type of advertising that is possible is that termed "puffery." Such advertising consists of hyperbolic promotional claims about the product advertised. For example, a hamburger chain might indicate in its advertisements that its staff are so customer-friendly that even its CEO cooks hamburgers there and interacts with the consumers, or the advertiser of a certain brand of soda might indicate through its promotional material that its soda is so tasty that even polar bears enjoy it. The fourth type of advertising is bombardment, or name recognition advertising. Here, advertisers attempt to expose as many consumers as possible to their advertisements for a particular product for as long as possible. The aim of such advertising is to establish in consumers' minds that if they require a certain product, then they should buy the advertised brand of that product. This aim is achieved through advertising bombardment by establishing in the consumers' minds a link between the purchase of a certain type of product and the purchase of a certain brand of that product. This type of advertising is often termed "name recognition" advertising. The fifth type of advertising is misleading advertising. Here, an advertiser does not actually present any information to the consumer that he believes to be false. However, he does attempt to mislead the consumer without doing so. For example, an advertiser promoting a certain type of car might mislead consumers into thinking that its performance is better than it is by claiming, correctly, that it had the best performance in its rally class, without noting that its performance was such that its rally class consisted solely of that type of car. The sixth type of advertising is associational advertising. When an advertiser uses this type of advertisement, it attempts to associate the product it is selling with certain nonmarket goods, such as happiness or sex appeal. For example, an advertiser promoting a certain brand of beer might attempt to associate the consumption of that beer with an enhanced attractiveness to the opposite sex. The final type of advertising that is widely recognized by business ethicists is so-called coercive advertising. Coercive advertising is advertising that the consumer cannot avoid. For example, the use of advertising inside public transit vehicles is held by some business ethicists to be coercive insofar as the persons inside such vehicles cannot avoid looking at it; they are thus coerced into viewing it.

John Kenneth Galbraith and the Dependence Effect

With these types of advertising outlined, they can be divided into two main categories of advertising: (1) that which is purely informational and (2) that which is persuasive. In the first category fits, clearly, informational advertising, while the six other forms of advertising outlined above fit into the category of persuasive advertising. Insofar as advertising merely conveys factual information to a consumer, it is held to be morally unobjectionable. It is the second category of advertising—persuasive advertising—that is considered by many business ethicists to be morally problematic. Naturally, each type of persuasive advertising is subject to different criticisms that pertain specifically to the techniques used to persuade consumers to purchase. However, persuasive advertising as a whole is subject to two general criticisms that are supposed to show that it is per se immoral. The first of these criticisms was offered by John Kenneth Galbraith in his 1958 book, *The Affluent Society.* Galbraith started his general criticism of persuasive advertising by outlining his demons analogy. Galbraith noted that if a man was assailed by demons every morning that instilled in him passionate desires for various consumer goods, we would think that it would be sensible for him to secure the goods in question so that he could quench these desires and thus be free of their urgings. Moreover, Galbraith stated, since being subject to these desires would be unpleasant, we would have reason to think that it would be sensible for this man to satisfy these desires no matter what the consumer goods were that the demons motivated him to pursue. However, Galbraith continued, even though we might think that this man was sensible to act in this way once the desires were instilled in him, if we came to learn that this man had cultivated the demons in the first place, and if we also learned that his efforts to satisfy the desires that they instilled in him led them to greater efforts to instill yet more desires within him, we might wonder how rational he was. Indeed, Galbraith concluded, we might think that this man's problem of being beset by this array of desires that forced him to act in ways in which he would not have acted had he not been subjected to them would be better solved not by his satisfying these desires but by his not being subjected to the demons in the first place.

With this analogy in place, Galbraith stated that the man subjected to the urgings of the demons is analogous to the consumer subjected to the urgings of advertisers. Galbraith argued that as a society becomes more affluent, persons will have wants created in them by the process by which they are satisfied. This is because, argued Galbraith, if a person wants a certain good and then buys it to satisfy this want, this purchase will provide a reason for the retailer of that good to desire to sell yet more to the consumer in order to ensure that the retailer continues to make money. As such, then, the producers of goods will be motivated to create new desires within consumers who purchase their goods through advertising and salesmanship. If this is so, the wants that persons will have will come to depend on the output of goods that need to be sold by their producers. Given this, Galbraith continued, one can no longer assume that a higher level of production of consumer goods will lead to an increase in the overall level of welfare. This is because the higher level of production might merely be sustained in a situation where a higher number of wants were being created by advertisers, which would in turn require a higher level of want satisfaction. The process by which the wants of consumers are thus dependent on the activities of advertisers acting at the behest of the producers of consumer goods was termed by Galbraith the "Dependence Effect."

As well as arguing that owing to the influence of advertisers, a higher rate of production need not lead to a higher level of consumer satisfaction, Galbraith also argued that advertising would have adverse effects on the distribution of resources. Galbraith argued that a community's well-being could be improved just as well by investing its resources in buying goods for public consumption as it could by buying goods for private consumption. For example, argued Galbraith, a community's well-being could be improved just as well by buying schools or parks as it could by private individuals buying bigger cars. Galbraith then noted that, in general, communities satisfied their desires for private goods rather than their desires for goods for public consumption. The conventional wisdom, Galbraith claimed, was that this distribution of the income of the persons in the community was arrived at through a democratic process, by which the members of the community used democratic processes to arrive at the way in which they would distribute their individual incomes between goods for private and goods for public consumption. But, claimed Galbraith, this conventional view of how a community arrives at its decisions concerning the distribution of the income of its members rests on the implicit assumption that the wants of consumers are determined independently of any external factors. However, argued Galbraith, given the fact of the Dependence Effect, this is not true. Since persons' wants for consumer goods are "synthesized," or created, by advertisers, and no such effect occurs with respect to nonconsumer goods, those produced for public consumption, the existence of advertising skews the wants of the members of each community toward consumer goods and away from goods produced for public consumption. As such, Galbraith concluded, persuasive advertising is immoral as it interferes with the decision procedure by which persons come to assess how to spend their incomes on goods for private consumption versus public consumption. Thus, for Galbraith, persuasive advertising is ethically suspect as its operation will serve to undermine the well-being of those subjected to it, insofar as it adversely affects their decision procedures and, in doing so, leads them to make decisions that might not reflect their true desires. Moreover, for Galbraith, in affecting consumers in this way, advertising also serves to undermine their individual autonomy. This is so as they are now, to an extent, being controlled by the advertisers rather than being in control of their own decisions and actions.

F. A. Hayek and the Non Sequitur of the Dependence Effect

In 1961, F. A. Hayek responded to Galbraith's ethical objection to advertising. Hayek pointed out that Galbraith's argument depended on the claim that a large proportion of the desires that a person in modern society experiences are not desires that he would experience spontaneously if he were not situated in a modern consumer society. Instead, noted Hayek, for Galbraith many of the desires that persons have are created by the process by which they are satisfied; that is, they are created by the production of consumer goods and by the advertising of such goods. From this, Hayek noted, Galbraith assumed that such desires could be neither important nor urgent, and so we would lose nothing were such desires to be eliminated, perhaps by restricting or eliminating the advertising of consumer goods or restricting or eliminating their production. Hayek accepted that Galbraith was correct to note that many desires that persons have are created by the process by which they are satisfied. It is true that we would not desire any of the amenities of modern society if we did not live in an age when they are being produced. However, Hayek argued, to accept this is not to endorse Galbraith's further claim that such desires therefore fail to be urgent ones to satisfy or are somehow rendered less important. To make this further claim from the first one was, Hayek argued, to endorse a non sequitur. Indeed, claimed Hayek, if we were to accept Galbraith's argument that for this reason persuasive advertising is in many instances unethical, we would have to accept the idea that other cultural phenomena that similarly generate desires in persons would also be ethically suspect. But this, argued Hayek, shows how absurd Galbraith's argument against advertising is. For example, Hayek noted, other similarly synthesized desires would include the desires for literature, art, and music. Although a person would not, Hayek argued, experience desires for such artifacts were such artifacts not produced, this does not show that it is not important to satisfy these desires or to have these goods. From this, Hayek concluded that rather than being unethical, persuasive advertising is ethically acceptable. This is because advertisers are hired by the producers of consumer goods to advertise their wares, as they believe that advertising can influence the decisions of consumers. However, although advertising might indeed be one of the elements that shapes consumers' tastes, it cannot determine them. It is the consumer who decides what goods he or she will buy, not the advertiser. As such, concluded Hayek, Galbraith's criticism that advertising undermines consumers' well-being and adversely affects their autonomy is mistaken.

Autonomy, Advertising, and Consumer Well-Being

The debate between Galbraith and Hayek is one of the central debates in business ethics concerning the ethics of advertising. It is clear that at its heart, it is a debate over the effects that advertising has on consumer autonomy and consumer well-being. This is not surprising, for these two concepts underlie other debates that concern the ethics of advertising. Deceptive advertising, for example, is morally condemned on the grounds that deception serves to undermine the autonomy of the person who is so deceived. It achieves this insofar as the person subjected to such advertising directs his or her actions in accordance with the claims that are made in it, claims that are believed to be false by the advertiser. If the consumers direct themselves on the basis of such claims, it will be the advertiser, and not the consumers, who will be really in control of the actions they perform with respect to the product in question—even though the consumers themselves do not realize this. Moreover, such advertising is also condemned on the ground that if consumers' autonomy is undermined through deception, they will be less able to direct themselves successfully in accordance with their own desires and values, and so, as a result, it is likely that their well-being will be lower than in the counterfactual situation where their autonomy is not so undermined. Similar charges are offered against both puffery and bombardment advertising. For both types of advertising, it is claimed by those critical of persuasive advertising on ethical grounds that the autonomy and well-being of consumers are likely to be adversely affected through being exposed to them. If consumers are subjected to puffery, such critics claim, they are more likely to make a decision based on a false view of the product that they are contemplating. This is likely to adversely affect their well-being and autonomy for the same reason that deceptive advertising might do so. Similarly, if bombardment advertising is effective, it might preclude consumers from exploring other brands of the product they are contemplating buying through associating in their mind the particular brand advertised with the type of product in question. This too might adversely affect both their autonomy and their well-being by having the consumers' purchase of the product directed primarily by the advertiser and not by the consumers themselves. Similar conclusions can also be made about misleading, coercive, and associational advertising.

Yet although these ethical objections to persuasive advertising are widespread, recent work in business ethics (e.g., by Ann Cunningham) has cast doubt on their twin claims that persuasive advertising undermines both consumer autonomy and consumer well-being. It is argued by those who defend persuasive advertising on ethical grounds that advertisers cannot directly control the decisions that consumers make. In particular, they cannot prevent consumers from assessing their claims to see if they can believe them or not. Moreover, even when no direct claims are made—when, for example, puffery, associational advertising, and bombardment advertising seek to promote a view of the product advertised through the use of nonpropositional images, consumers who are exposed to such advertisements can still ask themselves if they have a good reason to buy the products in question. Thus, contrary to those who claim that persuasive advertising is unethical as it adversely affects human autonomy and well-being, the defenders of advertising hold that such charges assume that advertisers have more power than they actually have. This defense of the ethics of advertising is not an unqualified one. Those who propose it often differentiate between different types of advertising, with those whose claims are more amenable to consumer evaluation being more ethically defensible. Thus, insofar as the implicit claims of puffery are easy to assess, this advertising technique is more defensible than deceptive advertising, which, when successful, will present claims to consumers that they cannot readily assess. For this reason, deceptive advertising is frequently considered to be ethically illicit.

—James Stacey Taylor

See also Advertising, Subliminal; Advertising Ethics; Consumer Preferences; Consumer Rights; Deceptive Advertising; Marketing, Ethics of

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Piracy of Intellectual Property

Piracy of intellectual property refers to the unauthorized use, reproduction, and/or distribution of protected material such as computer software, video games, music, or movies. Piracy has become an increasing concern in recent years because of the rise of the Internet and the speed with which copyrighted material can be distributed globally to a large number of people.

What is labeled *piracy* is literally the infringement of intellectual property rights—that is, copyright, patent, and/or trademark infringement. *Piracy* literally refers to robbery and other crimes committed at sea, where prey are more vulnerable in the absence of conventional law enforcement mechanisms. The term *piracy* is used in connection with intellectual property infringement, particularly with regard to electronic and audiovisual materials, because of the similar difficulty in detecting and preventing this sort of inappropriate behavior and the mass scale on which it can occur.

The use of the term *piracy* is, however, controversial. Unlike theft on the open seas, accompanied often by violence, loss of life, and permanent loss of property, intellectual property infringement does not have the same sort of victims. Whereas it can be argued that the piracy of intellectual property devalues the protected intellectual property (by making it more readily available) and deprives the owners of potential sales, it does not inherently involve violent crime or complete theft. Holders of patents, copyrights, and trademarks still retain their rights; they just lose the exclusivity of those rights.

The harm imposed by intellectual property piracy actually extends beyond the emotional and financial damages to the holders of patents, copyrights, and trademarks. In fact, piracy threatens the system of protected rights that encourages individuals and organizations to invest in the development and distribution of intellectual property. Furthermore, it jeopardizes the marketplace trust that attaches meaning to recognized expressions of ideas.

Patent Infringement

Intellectual property infringement has been a concern as long as intellectual property rights have been protected. In fact, instances of patent infringement were documented in the 19th century during the Industrial Revolution, when American law did not grant reciprocity to intellectual property developed in other countries. Early manufacturing in the United States was based on technology patented in Britain, without any compensation being paid to the legitimate foreign patent holders. At the time, this was condoned by the government in the United States.

Patents are granted to protect the opportunity of individuals and organizations to recoup their investment in inventions. Patent infringement occurs when the creator or user of an invention refuses to acknowledge the priority of the patent holder. The high cost of enforcing patents deters many holders from pursuing legal action, and many pirates take advantage of this.

Trademark Infringement

Trademark infringement occurs when products are manufactured or sold under the trademark of another company without that company's permission. The widespread distribution of counterfeit products—fake purses, knockoff watches, and so on—has turned this into a serious problem. Trademark infringement began about 20 years ago, with the men on 5th Avenue in New York standing around with suitcases full of knockoff Rolex watches that they sold for $10 apiece and the storefronts in Chinatown openly selling counterfeit handbags by Coach, Louis Vuitton, and so on, for a fraction of the retail value of the originals. In fact, vendors were so bold and the supply was so great that many would hand customers catalogs from which to choose their purchase.

The counterfeiters remain in business today, but several things have changed. First, the vendors are no longer as bold. Many of the transactions take place behind closed doors, in unmarked buildings in unadorned rooms, and potential customers are scrutinized before they are invited to consider purchases. Second, the product line has expanded. Luxury purses and watches are no longer the extent of counterfeit merchandise available. All sorts of luxury items and clothing are still available, along with fake medicine, fake automobile parts, and fake electronics. Third, the marketplace has grown beyond New York, and the merchandise is traveling not just to the United States but from the United States and other Western countries as well. In 2004, 800,000 doses of counterfeit medicine were seized at the borders of countries in the European Union. Most of those fake drugs were on their way to countries among the poorest in the world. Fourth, many of these items are now exchanged in e-commerce to unsuspecting customers, and this is undermining the brand names that have become staples in the global economy.

Influence of China

The recent emergence of China as a player in the global economy has exacerbated rampant intellectual property infringement. In addition to the counterfeit goods exported from China (and other parts of Asia) are the fake items sold in China to tourists and to China's enormous population. China is replete with factories to which all sorts of electronics and other products are outsourced. There is thus a large amount of intellectual property available for pirates to steal. In addition, the hoards of available workers enable factories to churn out both legitimate and counterfeit merchandise at lightning speed.

The result is significant confusion regarding brand legitimacy. LG, for example, experienced this firsthand as it attempted to introduce a local version of its Chocolate phone. Sluggish in launching its Chinese version, LG found that copies were available in China before the originals. By the time legitimate LG phones were ready for sale in China, the fake phones were so prevalent in the market that the LG phones were viewed as the counterfeits.

China remains a sort of "attractive nuisance" to pirates. There is so much intellectual property available to be copied, and the costs are so low and the profits so great, that the practices continue, and trademark infringement remains a significant concern.

Copyright Infringement

During the past decade, copyright infringement has also mushroomed. In earlier years, the main concern of copyright holders was "bootlegged" copies of songs, movies, and so on. The bootlegged versions were not exact replicas but were, instead, generally separately recorded, second-rate copies. As technology has advanced, concerns about copyright protection have also advanced, because of both the increased magnitude of the harm and the enhanced quality of the counterfeit copies.

In 1999, the birth of Napster added the considerable challenge of peer-to-peer file sharing to the list of threats to copyright protection. Peer-to-peer file sharing occurs as individuals make exact copies and share original computer files of protected material, such as music in the MP3 format, video in AVI and MPG formats, and computer software in all sorts of formats. Napster was the first known entity to facilitate the sharing of files via the Internet through a system of linked servers and users. Other decentralized programs have since been introduced, such as Kazaa, Livewire, BearShare, and, more recently, BitTorrent.

At its peak in 2001, Napster claimed 26.4 million users—that is, 26.4 million people who were sharing pirated intellectual property. Since that time, authorities have clamped down on these practices. The Recording Industry Association of America has reacted strongly against Napster, which was eventually shut down in response to the legal action taken against it for its participation in rampant copyright infringement. Today, Napster exists under new ownership as a fee-based music subscription service.

The downfall of Napster created significant barriers to Internet-based file sharing as a vehicle for the distribution of copyrighted material, but it has not put an end to it—it has just made it more difficult.

Warez

"Warez" is the name that has been given to copyrighted material being pirated (i.e., being exchanged in violation of copyright law). It refers primarily, but not exclusively, to software. There are various subgroups of warez, including appz (retail versions of computer applications) and gamez (computer-based games and video games). In spite of the fall of Napster, users continue to share warez via the Internet.

Legislation

Laws in the United States, as well as in many other countries, recognize the value and importance of intellectual property and grant exclusive, defined rights to the holders of patents, copyrights, and trademarks. Furthermore, they provide legal remedies to victims of intellectual property infringement. The problem is that detection can be tricky and enforcement is difficult and often costly.

Furthermore, the presence of international actors, not all of whom are constrained by the same sorts of laws and norms that govern the United States, further complicates the situation. A poignant example pertains to the Russian online company AllofMP3. AllofMP3, an online music store based in Moscow, has the appropriate licensing agreements with the Russian Organization for Multimedia and Digital Systems, which is the organization responsible for regulating licensing in Russia. These documents are similar to the arrangements that the Russian radio stations have with the organization. Under this agreement, AllofMP3, per Russian law, has the right legally to distribute the music from all artists and all labels, without consideration of the copyright infringement laws of other countries, such as the United States.

While in the past, online companies have been able to evade expulsion by organizing in countries that do not safeguard intellectual property rights in the same way as the United States, the tide appears to be changing. The threat by the United States to withhold Russia's membership in the World Trade Organization forced the Russian government to adopt intellectual property laws that overlap or mimic those of the United States. It was anticipated that early in 2007, this would put an end to AllofMP3. Already, credit card companies such as Visa and Mastercard had withdrawn their business from the Web site.

This is becoming less of an impediment, however, as more and more countries are passing local legislation that respects the rights of intellectual property holders and recognizes reciprocity with other countries. In addition, international treaties continue to call for reciprocity with regard to the recognition of intellectual property rights.

Arguments Against Regulation

As legislation and litigation tend to be the favored responses to alleged intellectual property infringement, there are very strong arguments against continued regulation of intellectual property pertaining to music, mathematical formulas, and so on. The ease with which individuals can infringe on the rights of the creators of protected material has been fueled by the rise of the Internet. The question remains, Who is truly being harmed?

This battle between the corporations and the individuals who pirate the protected intellectual material is often portrayed as a battle between the corporation and the individual, with the belief that the artist is also being harmed by the alleged infringement. This belief appears somewhat misguided, however, in that many artists argue that swapping of music and movies, even though prohibited by laws, does not threaten their livelihood. In fact, artists have argued that the Internet and file sharing have enhanced their profitability as a result of their increased exposure. Many musicians, for example, assert that existing regulation protects the labels to the exclusion of the artists; they contend that free, single-track sharing creates much more exposure for the artists (and perhaps even profits for the labels) since more money comes from concert tickets and sales of compact disks.

There are also significant questions and challenges to "ownership" as it pertains to intellectual property. People do not own their ideas to the exclusion of others; on the contrary, they share their ideas with others. What is protected are the rights to claim credit, both reputationally and financially, for the ideas.

The very phrase *intellectual property* is somewhat misleading in that it suggests exclusive ownership, whereas that is not what it actually means. The entitlements associated with copyrights, patents, and trademarks are linked primarily to the right to the financial benefits that accrue from the use of the intellectual property.

Conclusion

Piracy of intellectual property remains a prevalent concern in the United States and abroad. Detection remains difficult (and is often not attributable to the source), and enforcement continues to be costly.

Piracy is tempting for many reasons, not the least of which is the ease with which it can take place. In addition, many people do not consider it theft since it does not involve obvious victims—owners of intellectual property are deprived only of the exclusivity of their rights, not of the rights themselves.

What pirates need to remember is that it is the system itself that creates the value of the intellectual property they steal. In other words, the value of copyrights, trademarks, and patents relies on the system of providing exclusive rights in exchange for investments in intellectual property. While the practices of these pirates do not constitute theft in the traditional sense, their actions do have significant financial consequences and do serve to undermine the system of intellectual property rights in general.

—Tara J. Radin and Ozgur Toraman

See also Copyrights; Intellectual Property; Internet and Computing Legislation; Patents; Trademarks

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Plagiarism

Samuel Johnson (1709–1784), the English lexicographer and the author of the *Dictionary of the English Language* (1755–1756), commented on a certain piece of writing that he believed to have been plagiarized. He stated that he thought the passage was both good and original. However, he added that the part that was original was not good and the part that was good was not original. Plagiarism has long been a subject of interest in academia, the media, and the creative arts. It has been with us since our ancestors first learned to commit their thoughts to paper or parchment.

So what actually is it? Plagiarism is, according to one source, knowingly presenting the work or property of another person as if it were one's own without appropriate acknowledgment or referencing. In plain language, plagiarism is a form of literary theft. It is intellectually dishonest and usually (though not always) occurs within an academic context. A London-based dictionary of 1721 defined plagiarism as stealing other people's works and publishing them as one's own. Samuel Johnson said that plagiarism was a form of theft. It was literary adoption of the thoughts or works of another. It was one of the most reproachable, though perhaps not the most atrocious, of literary crimes.

John Aubrey (1626–1697), a social gossip and a writer of anecdotes, described someone he thought was a plagiarist in the following terms. He was, he said, a person of real worth who stood very gloriously up on his own basis and did not need to be beholden to any man for fame, yet he was so greedy of glory that he stole feathers from others to adorn his own cap. Another comment from the 17th century was that it was a worse sin to steal dead men's writings than their clothes. These comments from the 17th and 18th centuries suggest that people have always felt strongly about literary theft. Dictionaries offer a range of definitions: (1) the wrongful appropriation, or purloining, and publication as one's own of the ideas, or the expression of the ideas (literary, artistic, musical, mechanical, etc.), of another; (2) the unacknowledged use of somebody else's ideas or words, the misappropriation and publication of ideas and words as one's own, or the act or practice of taking the thoughts, writings, or inventions of another as one's own; (3) using the work of another with intent to deceive; and (4) passing off someone else's work as your own, intentionally or unintentionally, for your own benefit.

There are a number of other issues to consider: For instance, where do imitation and legitimate borrowing fit into this argument? Thinking people would regard any form of plagiarism (whether in academia, the media, or the creative arts) as morally objectionable. The argument becomes confused if we take the opposite approach and argue that very little intellectual activity was ever original. People have been tweaking or filching other people's ideas forever, as the examples later in the section will illustrate. Plagiarism is a subset of the intellectual property argument. It is a Western construct and one that did not really apply to the classical masters of old. So what actually is intellectual property?

Intellectual property is the term given to creations of the intellect or the mind that have commercial value or can generate monetary reward. Examples of creations of the intellect include inventions, literary works, artistic works, music, creative writing, and films. With respect to industrial properties, the term includes patents for inventions, trademarks for brand identity, designs for product appearance, and copyright for materials.

Intellectual property rights are the specific legal rights that protect the owners of intellectual property. The two concepts, intellectual property and plagiarism, are closely related. For example, someone steals the idea for an invention or claims to have composed a hit tune that sounds similar to an earlier classical composition, thereby standing to gain at somebody else's expense. These are forms of plagiarism and are both morally and legally reprehensible.

Authoritative sources and originality become central in any discussion about plagiarism. Authority figures and authoritative sources were the usual starting points for any serious intellectual investigation. In the 17th and 18th centuries, three schools of thought existed with differing views about the way to acquire new knowledge: (1) Scholasticism, (2) Humanism, and (3) Cartesianism. The Scholastics studied the writings of Aristotle (384–322 BCE) and Saint Thomas Aquinas (1226–1274). They based much of their approach to learning on the syllogistic method of reasoning. Humanism was a term for a learning style that involved studying the literature of the classical masters and *imitating/copying* their style. René Descartes' (1596–1650) thinking is best expressed in his *Cogito, ergo sum* (I think, therefore I am) proposition. Each of these methods had its followers and supporters, but it was the Humanists who practiced and advocated a style of learning that contained many aspects of plagiarizing or plagiarism. Their approach to learning consisted largely in imitating the style and ideas of the early Greek and Roman masters. They could see nothing wrong with this approach, as copying or imitating was for them the sincerest form of flattery. There are ethical, moral, and legal reasons why plagiarism is unacceptable. Plagiarism is a form of literary theft, and so a person who plagiarizes or takes material that belongs to another is guilty of theft. There are also aesthetic arguments, but the moral argument with respect to professional integrity outweighs the others.

Plagiarism in Classical Times

Etymologically, the word *plagiarism* comes from the Greek *plagion*, meaning "slanting" or "athwart." *Plagion* has military connotations and refers to the flanks of an army. When used in a literary or metaphorical sense, it came to mean "sideways," "askance," or "treacherous."

Martial (Marcus Valerius Martialis, ca. CE 40–103), a Roman poet from a Spanish/Celtic background, is associated with the earliest use of the Latin form *plagiarius*, meaning "kidnapper" or "seducer." He excelled in writing epigrams, many of which are obscene and pornographic. Gradually, *plagiarius* came to mean "steal," in a more general sense, and later, specifically, "literary theft." Martial had accused another poet of stealing some of his ideas. He was possibly guilty of this himself, because according to his critics he had imitated earlier Greek poets.

Seneca (Lucius Annaeus, ca. 4 BCE–CE 65), orator, writer, and poet, was supposed to have said with respect to plagiarism that originality was the art of concealing one's sources. There are numerous stories about people such as Aristophanes, Isocrates, and Democritus using ideas from others who went before them. Virgil (Publius Vergilius Maro, 70–19 BCE) was a Roman poet who used ideas from Theocritus, Hesiod, and Homer. Later writers imitated or copied the writings of Æsop (Aisopos), the traditional creator of the Greek fables. Horace (Quintus Horatius Flaccus, 65–8 BCE), another Roman poet, used Æsop's well-known fable about the crow who disguised himself with peacock feathers. Versions of this story have appeared in English literature in a variety of guises.

Plagiarism in the 17th and 18th Centuries

A line that appears on the cover page of *Poetaster: A Comical Satyr*, written in 1601 by Ben Jonson (1572–1637), the English dramatist and poet, had appeared earlier in Martial's Book VII, Verse 12, an epigram consisting of 99 verses. We know that Jonson used ideas taken from Ovid (Publius Ovidius Naso, 43 BCE–CE 17), Horace, and Seneca and that his name appears in investigations of plagiarism in English literature. According to one source, Jonson invented the pejorative term *playwright* in 1687 to describe someone who had put together the work of others. Jonson alluded to the works of Horace and Virgil and to Rome. Jonson wrote that the name Canidia was but a borrowed name and that the ditty was borrowed. The words were Horace's, he stated, "Hang him plagiary." This use of the term *plagiary* appeared in 1601. It referred to someone who forcefully possessed another. It had appeared earlier, in 1555, as *plagiaire* (French), and, in 1577, as *plagium* (Latin), translated as a net to entangle game, but was used in English Civil Law when referring to kidnapping or man stealing. It appeared also in July 1607, when Thomas Legge, Master of Gonville and Caius College, Cambridge, referred to the fact that someone had kidnapped his ideas for a play, *The Destruction of Jerusalem*. The use of Latin or French was common among the educated and upper classes of that time, many of whom would have been familiar with one or both languages. Alexander Pope (1688–1744), another English poet and satirist, was a great imitator. According to one source, he borrowed anything and everything from Homer, Horace, Virgil, Chaucer, Spenser, Shakespeare, and Dryden.

In the world of musical composition, George Frideric Handel (1685–1759) was a musical magpie. He took ideas for many of his melodies from a range of other European composers, a practice that was not altogether condemned but seen as a form of flattery for the original composer.

In the field of dramatic art in the 18th century, the character "Sir Fretful Plagiary" had appeared in Richard Brinsley Sheridan's (1751–1816) *The Critic; or a Tragedy Rehearsed*. Sheridan, the Irish-born dramatist and then politician, is better known for *The Rivals* and *The School for Scandal*. His plays and his stage characters, such as Sir Fretful Plagiary, Sir Lucius O'Trigger, Lydia Languish, and Mrs. Malaprop, reflect something of the scandal-ridden Anglo-Irish society of the 18th century. From that time, the word has come to mean "literary theft."

Plagiarism and Students

With respect to student behavior, plagiarizing is a serious misdemeanor, and with the advances in data storage and retrieval, plagiarism seems to have made a student's life superficially easier. Universities allocate resources to combat it, but it is probably well entrenched. Academic dishonesty and issues of educational integrity appear to be on the increase. Whether this is due to an increase in student numbers or an increase in actual cases is yet to be determined.

We know that the total number of students attending universities has dramatically increased over the last decades. Whether this behavior involves plagiarism (accidental, inadvertent, due to cultural differences) or cheating is also yet to be determined. Universities have evolved into business organizations (students have become customers, and staff meetings are concerned with budgets and cash flow) in addition to being centers of learning and intellectual excellence. It is possible, therefore, that the underlying ethos of many universities may have been diminished.

There have always been moral and pedagogical imperatives with respect to plagiarism. The cultural dimension has become more of an issue in disputes involving student plagiarism. Some students come from countries where different teaching styles and standards prevail, where the unacknowledged copying of content matter and rote learning are normal. Libraries and student information services prepare information bulletins about plagiarism and ways of ridding their campuses of it. They have produced information on topics such as student rights and responsibilities; guiding ethical principles; penalties for plagiarizing, such as suspension, exclusion, a fine, or expulsion; and copyright and moral rights. Yet despite these measures, plagiarism is probably rife on most campuses. Suggestions to counter instances of academic dishonesty range from developing academic honor codes at one end of the scale to having an authoritarian approach whereby university proctors (officers responsible for student discipline) would coordinate investigations of suspicious written submissions.

Another approach would be to rely on the professionalism and the interest of individual members of the staff. A staff member who has established good rapport with students could present a case why plagiarism in any form is unacceptable. He or she would be more likely to persuade students that plagiarism is unacceptable than would readings taken from a Web site. The fact that plagiarism is now prevalent on campuses probably relates to pressures on students to complete their courses in minimum time and the perceived drop in standards in writing skills and general ability. Anecdotal evidence suggests that earlier generations of students may have been superior with regard to general ability and writing skills.

Conclusion

This entry first identified some early literary figures who were said to have been plagiarists. Second, it identified the need for policies and procedures to be in place for the busy academic who may have to sit in judgment of unethical student practices. Third, as Samuel Johnson said, plagiarism was not the most atrocious of literary crimes. It might be reproachable, and for many students it was but a minor indiscretion, easily rectified by the addition of references and sources. Sometimes, the students involved were incredulous when told of the importance attributed to plagiarism. However, there could well be serious consequences and repercussions for the person found guilty of plagiarism. The student or academic who has been involved in a case of plagiarism might not receive the recognition, fame, reputation, or financial reward that he or she would otherwise deserve at some future time.

At the research and thesis level, plagiarism is a serious matter and is the responsibility of the supervising committee. At the undergraduate level, subject controllers need to design assignments that will discourage plagiarism. They must monitor, review, and supervise the type of assignments that are in place if plagiarism is to be controlled. If the same questions keep appearing, undergraduate students (where enrollments are sometimes in excess of 1,000–2,000 students) are more likely to take shortcuts.

A footnote with respect to the earlier reference to Samuel Johnson now follows. The footnote relates to Johnson's comment about reproachable literary crimes. It concerns another practice, known as literary hoaxing. To illustrate, two cases involved the publication of novels and the subsequent fallout from their publication. The first case involved a supposed author, J. T. LeRoy, who wrote about life on the streets. However, this was a hoax. J. T. LeRoy was the pen name of two musicians. When a public appearance of the author was required, the sister of one of the hoaxers acted the part. The second case involved James Frey, the author of *A Million Little Pieces*, marketed as an autobiography but later found to be full of inconsistencies.

A second footnote relates to plagiarism becoming evident in most forms of creative human activity. Examples of plagiarism can be found in the creative arts, the print media, and now it seems in political speech writing. Examples are well known and do not need repeating here. It has provided unwelcome publicity for some and has been the cause for some people to lose their jobs. In one incident, the writer was aware of a situation where the parties concerned received a lot of media publicity over what started as a minor disagreement. The disagreement initially related to accusations of plagiarism, followed by counteraccusations of "soft marking," that is, less rigorous marking for fee-paying students in the hope that the episode would just go away. It did not. The incident blew up and became well-known. It received major coverage on national television and in the national dailies. Some chose to regard the initial plagiarism in this case as a serious misdemeanor; others described it in less dramatic terms.

Finally, we may ask, What is the difference between a literature review and a plagiarized piece of prose?

The literature review in a thesis contains sources, references, and citations. In a plagiarized piece of prose, there is no attempt to show from whence the material came. The reader will probably see that much of the material in this contribution has its origins in authoritative sources. However, there is one major difference between this piece and a plagiarized piece. There is no attempt at deception. Plagiarism will always be present in some form. Academics need to be vigilant and, like the *paidagogos* of old (the trusted slave and tutor in ancient Athens), to take students in hand and lead them through the complexities of the learning process.

—Michael W. Small

See also Accountability; Authenticity; Collusion; Deceptive Practices; Fairness; Fraud; Integrity; Intellectual Property; Property and Property Rights

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Pluralism

Pluralism generally is defined as the quality or state of being plural. Often, pluralism is used in the context of political science, particularly related to modern democracy. David Truman and Robert Dahl are two important exponents of political pluralism, which typically has competed with elitism and majoritarianism as a view of modern democratic societies. In its essence, political pluralism is the idea that individuals form interest groups that then compete with each other for favorable government policies. No group has more inherent power than another, and public officials (after lobbying by the interest groups) decide on policy based on their views of the public interest. An important feature of political pluralism is the understanding that competing groups' values are equally valid—that is, the claims made by interest groups cannot be ranked generically, allowing public officials to exercise their judgment in making policy decisions.

Applied to moral philosophy, the above definition typically translates to the idea that more than one moral principle, or more than one intrinsic good, are equally and universally valid. This definition places moral pluralism in contrast both with monism (the idea that one and only one principle is always and everywhere valid) and with subjectivism (the idea that no principle is universally valid).

Isaiah Berlin, perhaps the most well-known pluralist thinker of the 20th century, worked in both political and moral philosophy. Berlin emphasized objective pluralism (*objective* meaning that human values are part of the essence of humanity), which he wished to contrast with subjectivism. For Berlin, there were many different and irreducible values (also called ends or intrinsic goods) that men could seek. Although humans can understand others' values, and perhaps even admire them, because of their irreducible plurality, those values will at times be incompatible, and there is no common yardstick by which to judge which value is more important. In a political context, Berlin infers from this that people should be allowed as much freedom as possible, compatible with freedom for all; in a moral context, he infers that people with different values should respect each other. He does, of course, allow for the possibility of people, groups, and societies being wrong and of the necessity to fight those who are.

An example of a pluralistic theory that includes principles is that of Sir David Ross, a British academic like Berlin. Ross's theory is deontological in nature as well as pluralistic. He gives seven types of duties, none of which are seen to be more basic than any of the others, and three or four intrinsic goods. The duties include fidelity (keeping an explicit or implicit promise), reparation (making up for a previous wrong), gratitude (paying someone back for a good deed), justice (ensuring that people get what they deserve), beneficence (helping people in certain ways when we can), self-improvement (trying to improve our own condition in terms of virtue or knowledge), and nonmaleficence (not harming others). The intrinsic goods Ross lists are virtue, knowledge, justice (pleasure in proportion to virtue), and (at times) pleasure. When duties or intrinsic goods conflict, Ross calls on us to use our moral judgment to decide, all things considered, what is the proper action in the specific situation.

Mark Timmons argues that the most plausible versions of most moral theories are pluralistic in nature—what he calls "limited moral pluralism" in that there is a plurality of principles or goods, and the theory cannot give a final answer regarding the right action in specific situations without resort to moral judgment. For example, utilitarianism or natural law theory could each allow for a plurality of intrinsic goods and give limited guidance on how to resolve conflicts among those goods.

Other major theories can be seen in the same light. For example, Kant's theory could be seen as containing a collection of rules that specify duties but not containing any overarching principle from which the rules themselves would be derived (admittedly, it is not often interpreted in this manner). Virtue theory under this prism actually would contain many virtues, several of which would be central to the individual as a virtuous agent but none of which would be more important in that characterization than any of the others, and such a theory would contain no principle from which to derive rules on which virtue is more important in any given situation. American pragmatism also can be seen as a pluralist theory. However, it is different from the above examples in that the pluralism results from a plurality of individual ideas, not of principles or intrinsic goods.

Pluralism often is argued for because it seems to represent the reality of moral decision making better than the alternatives. A related argument in favor of pluralism concerns its treatment of moral judgment. Such judgment can be seen to be used by nearly all people in many situations. Judgment cannot be captured in a single principle, so a pluralistic account of morality fits better with our observations of people making decisions.

Two arguments against pluralism are that it is inconsistent and that it is indeterminate. That is, people who use moral pluralism privilege different principles or goods in different situations. Also, pluralistic theories give no easily identifiable rule for people to use in making decisions. Pluralists argue in return that inconsistency is important because situations and people are different and that indeterminacy is unimportant because the real world is complex and moral judgment is needed to navigate it.

Most of the moral decision frameworks put forward in the business and society fields are pluralistic in one form or another. For example, most theories arguing for consideration of multiple stakeholder interests are pluralistic to the extent that they do not rank stakeholders, thus putting the onus on managers to balance competing and valid stakeholder interests.

—Brian K. Burton

See also Absolutism, Ethical; Ethics, Theories of; Relativism, Moral

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Political Action Committees (PACs)

Political action committees (PACs) are lawful mechanisms established to raise and pool political contributions from individuals and then channel that money to political candidates. Their operations are based on the First Amendment values of both freedom of speech and freedom of association. Though some critics of political money have suggested that PACs be outlawed, no serious proposal has been made, and such a proposal would in any case be of dubious constitutionality.

Brief History of PACs

Labor unions were the first primary sponsors and promoters of PACs, and the largest early PAC was the AFL-CIO's Committee on Political Education. Corporations learned about the utility of PACs from unions and began aggressively organizing PACs in the 1970s. Corporate contributions to candidates for federal office had actually been banned since 1907 by the Tillman Act, though the act had often been violated. In fact, the Watergate scandal surrounding the Nixon reelection campaign in 1972 involved illegal corporate contributions to the Committee to Re-elect the President. That scandal led to the passage of the 1974 Federal Election Campaign Act, which more tightly regulated contributions and political expenditures. By imposing a contribution limit on PACs, this act also implicitly validated the PAC mechanism and reinforced its legitimacy.

Due to the growing concern over illegal corporate contributions and the shutting off of that pipeline to candidates, along with the congressional approval of PACs, more corporations from the late 1970s onward began organizing PACs. The Public Affairs Council, the association of corporate public affairs professionals, was especially instrumental in promoting the formation of corporate PACs and in training PAC administrators.

Types of PACs

The law allows for two types of PACs, an affiliated PAC and an independent PAC. Affiliated PACs may be organized by corporations, labor unions, and nonprofit organizations. Among corporations, large firms and those in regulated industries tend more often to form PACs. Political advocacy groups such as environmental organizations, professional associations, and business associations also form affiliated PACs. Three of the largest association PACs are those of the National Realtors Association, the American Medical Association, and the American Trial Lawyers Association.

Independent PACs are not affiliated with any preexisting organization and are self-standing organizations. They are usually organized by like-minded individuals with the aim of promoting a particular ideology or cause. The earliest independent PAC, which contributed money to only liberal candidates, was the National Committee for an Effective Congress. Two PACs organized to contribute to only conservative candidates were the National Conservative PAC and the Committee for the Survival of a Free Congress. Emily's List was organized to raise money on behalf of women congressional candidates, and the League of Conservation Voters raised money to contribute to congressional candidates who were strongly committed to protecting the environment.

To facilitate the selection of the appropriate recipients among incumbent candidates, independent PACs would also create rating systems based on congressional voting patterns to determine which legislators were the most pro-environment, pro–free markets, proconservative, proliberal, prolabor, prodefense, or probusiness. Beyond independent PACs, other organizations and publications also produce vote-rating systems, and the Business-Industry PAC exists primarily to advise corporations and business associations on which probusiness candidates to support. To determine which challengers might be worthy of support, PACs will either interview or send questionnaires to such candidates in an attempt to ascertain their positions on issues crucial to the PAC, since they have no prior voting records.

PAC Operations and Structure

The PAC actually is a committee composed of managers and officers who supervise the solicitation of funds to the PAC and decide how to disburse the moneys to candidates. They select as recipients those candidates who would best serve the strategic interests of the corporation and who might occupy key positions of power in Congress or sit on committees with jurisdiction over issues of great importance to the firm.

The PAC solicits voluntary contributions from managers and executives and can solicit from shareholders as well, though companies rarely engage in that type of solicitation campaign. To guard against coercion, Federal Election Commission regulations prohibit supervisors from soliciting from subordinates. To protect individual rights and freedom of choice, PACs may allow contributors to earmark or designate their contributions for specific candidates, although that system would undermine the value of centralized strategic decision making.

Contributions and Independent Expenditures by PACs

The aforementioned 1974 law contained two provisions regarding the disbursement of PAC moneys. The first provision limited contributions to candidates to $5,000 per election, which would allow a PAC to give $5,000 to a candidate running in a primary election and another $5,000 prior to the general election. That provision still stands as good law and was upheld by the U.S. Supreme Court in the landmark *Buckley v. Valeo* decision of 1976. The Court reasoned that although there was a certain speech value in any contribution, the First Amendment is not violated by a contribution limit, since the limit serves a compelling government interest of preventing the corruption of candidates.

The second provision of the 1974 law affecting PACs placed a limit on independent expenditures—that is, on money spent endorsing the candidate or on behalf of the candidate rather than contributed directly to the candidate. In the *Buckley* case, the Supreme Court struck down the limits on independent expenditures as a violation of the First Amendment, since expenditures had a higher free-speech value and since expenditures cannot corrupt a candidate. They are not given to a candidate, and there is thus no exchange relationship with the candidate.

The result is that PACs must abide by the $5,000 limit in contributing to a candidate but face no limits in mounting an independent expenditure campaign. However, corporations generally do not engage in independent expenditure campaigns, since they lack the expertise and resources to mount effective advertising campaigns. National association PACs do take advantage of that legal right, though. They generally have large staffs and can hire experts to design independent expenditure campaigns. The National Realtors Association and the American Medical Association, for example, have engaged in such endorsement campaigns.

Another law that gave further impetus to PAC activities is the Bipartisan Campaign Reform Act (BCRA) of 2002, otherwise known as the McCain-Feingold Law. One of its major purposes was to ban unregulated corporate soft money donations to political parties. Such donations had become popular as a way to evade the strict limitations on corporate PAC contributions to candidates established by the 1974 law. In banning corporate soft money donations, the BCRA provided an incentive to corporations to either establish or revitalize their PAC operations, and many companies did just that.

Negative Impacts of PACs

Critics of PACs allege that they have created several negative impacts for the political process, and some of those impacts also have negative ethical aspects:

- *Escalation of campaign costs:* Due to the proliferation of PACs, candidates have more private sources of campaign contributions, and that cash has fed the steady escalation of campaign costs from one election to the next.
- *Entry barriers to challengers:* Corporate PACs and other affiliated PACs tend to favor incumbent candidates over challengers, since the incumbents are known quantities with whom they have built relationships. As the rich get richer, this creates equity problems in political contests, and incumbents also become entrenched in safe seats for long periods of time.
- *Special interest influence:* With campaign contributions comes access to legislators, which other interests may not enjoy, and that raises the specter of influencing candidates as well, again creating equity problems. Studies tend to show that money does not buy legislative votes, but it does reinforce sympathizers and mobilizes legislative leaders to lobby internally on behalf of their contributors. Those low-income interests in the population that cannot afford to play the campaign finance game may be shut out of the process, raising even more serious equity questions.
- *Exploitation of contributors:* The relationship between contributors and candidates is a two-way street, and while contributors might exploit candidates, candidates can also exploit contributors. Rather than contributors always buying access, candidates can also sell access. By stressing the upcoming important issues of corporate concern before a candidate's committee, the candidate's aide can imply that access to their legislative offices comes at a price. This mutual exploitation relationship raises questions of Kantian violations, as each party is treating the other as a means rather than an end and according little respect to the other party.
- *Erosion of party discipline:* This impact is less laden with ethical aspects, but to the extent that candidates can build their own effective fund-raising operations dependent on individual donors and PACs, they need to rely on political parties far less. The parties then have less influence on a legislator's positions on key issues. Advocates of strong political parties see this as a negative impact, but those who believe in independent thinking and freedom for legislators would see this as a positive impact.
- *Undermining civil discourse:* The independent ideological PACs have created many of the negative attack advertisements that one sees on the airwaves during campaign seasons. They do so through independent expenditures, since they can use these ads either to endorse candidates or to attack candidates whom they oppose. The attack ads often convey messages that candidates would be unwilling to say on their own. This is particularly true of contentious ads on moral issues such as gay rights or abortion. During the 2004 election, ideological PACs were also joined in the negative ad campaigns by the so-called 527 committees (named after a section of the Internal Revenue Service [IRS] code), established to evade the ban on soft money contributions to political parties instituted

by the BCRA. The so-called Swift Boat ads against Senator John Kerry are one example. Instead of making soft money donations to political parties as before, wealthy donors contributed instead to "independent 527 committees," which in turn produced ads supporting or opposing candidates.

Positive Impacts of PACs

Supporters of PACs argue that they have created a positive net gain for the political process, in the following ways:

- *Democratization of politics:* Instead of corporations and other institutions relying on their own assets or budgets to support candidates, PACs rely on voluntary contributions from individual managers or members. This promotes individual participation in the political process, a key ethical concept as well, based on deontological reasoning.
- *Political education:* PACs and their institutional sponsors usually combine solicitation efforts with political education campaigns. In that way, employees learn more about the candidates running for office and the central issues in the campaign, thereby becoming better citizens, which is vital to a self-governing democracy.
- *Expanded political participation:* As a result of the above two factors, an individual donor base combined with more political education, voter turnout is likely to grow and PAC supporters are more likely to get involved in politics in other ways, perhaps even by running as candidates.

—John M. Holcomb

See also Campaign Finance Laws; Interest Groups; Iron Triangles; Nongovernmental Organizations (NGOs); Trade Associations

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POLITICAL ECONOMY

Political economy was a term widely used from the late 18th century to the end of the 19th to designate the comprehensive study of economic activity in its relationship to public policy, custom, and law. With the great 19th-century advances in economics (including partial and general equilibrium theory and marginal utility theory) came considerable specialization and formalization, and by the early 20th century, the more general field of political economy had split into economics on the one hand and political science on the other.

The term *classical political economy* refers to a (predominantly British) subset of the works of political economy. Classical political economy was social theory at its grandest. The classical political economists combined comprehensive views of economic progress—and all its attendant complications and discontents—with arguments about the legitimacy and role of government and about the basis of individual and social morality. They were the last great generalists in the Western tradition.

Exactly whose work is properly placed within the classical school is a subject for much academic debate, but its core figures certainly include its widely acknowledged founder, Adam Smith (1723–1790); its greatest and most influential theorist, David Ricardo (1772–1823); and its consolidator and clarifier, John Stuart Mill (1806–1873), who came to believe late in his life in the consistency of classical economics with socialist policies. Karl Marx (1818–1883), who coined the term *classical political economy*, regarded himself as both an inheritor and a critical reformer of this great tradition. That the classical political economists are sometimes referred to as "Ricardians" or "classical Ricardians" speaks to the centrality of Ricardo's thought to the school.

Precursors to the classical system include the French physiocrats Richard Cantillon (1680–1734), François Quesnay (1694–1774), and A. R. J. Turgot (1727–1781), from all of whom Smith borrowed extensively, and Smith's friend, the Scottish philosopher and historian David Hume (1711–1776), whose essays "On Money" and "On the Balance of Trade" informed classical monetary policy. Ricardo's closest disciples, who continued to advance his doctrine after his death, were James Mill (1773–1836), J. R. McCulloch (1789–1864), and Thomas de Quincey (1785–1859). Jean-Baptiste Say (1776–1832), J. C. L. Simonde de Sismondi (1773–1842), and T. Robert Malthus (1766–1834) were, in different ways, both in competition with and in the orbit of the classicals. Henry Fawcett (1833–1884), John E. Cairnes (1823–1875), and the great moral philosopher Henry Sidgwick (1838–1900) continued to promote the classical doctrine to the end of the 19th century—even as the "marginal revolution" and other economic advances were beginning to consign it to the pages of history.

Mercantilists and Physiocrats

The dominant school of economic thought from the 16th to the early 18th centuries—as both the European nation-state and modern international trade were developing—was "mercantilism." The mercantilists held that the wealth of a nation was to be measured by its stock of precious metals. The economic goal of any nation was to win what the mercantilists regarded as the zero-sum game of world trade. This could be achieved only by one nation selling more goods to other nations than it purchased from them, thus amassing a stockpile of bullion. This favorable balance of trade was to be maintained by various protectionist policies including, especially, tariffs.

In France in the 1760s, there arose a new economic school opposed to mercantilism: the "physiocrats," associated most powerfully with the work of François Quesnay. In contrast to the mercantilists, whose policies promoted manufacture and commerce, the physiocrats were convinced that the source of any nation's wealth was the productivity of its agricultural sector. In the manufacturing and commercial sectors, they reasoned, total output was logically equal to the sum of the inputs, yielding no net gain in productivity. Agriculture, however, was different, in that land could actually produce more value than was put into it. For a nation to achieve its highest possible net product, therefore, it needed to concentrate on agricultural improvements. This meant, among other things, eliminating various medieval strictures on land use and alienation.

The physiocrats' innovations in economics were many. Quesnay's work theorizing the flow of income between different sectors of the economy was highly influential, as was his advocacy of laissez-faire economic policy. Cantillon is credited with developing an early supply-and-demand model for short-run market price and with defining long-term market equilibrium in terms of a balance among flows of income. He also conceived of labor supply and output in terms of the land necessary to support laborers and thus developed a "land theory of value." Turgot studied the role of capital accumulation in economic growth, advanced theories of supply-and-demand price determination, and wrote—before Adam Smith—about the economic productivity of the division of labor.

Adam Smith

There is hardly anything wholly original in Adam Smith's economic writings, yet there is still ample reason for counting him as the founder of classical economics. First, there is the sheer scope of his classic work *An Inquiry Into the Nature and Causes of the Wealth of Nations.* Where his predecessors had contented themselves with pamphlet-length arguments about particular economic issues, Smith wrote a truly comprehensive tome. *The Wealth of Nations* was at once a definitive refutation of mercantilism and the founding document of classical political economy. The book develops economic theory across the whole range of micro- and macroeconomic topics, examines much of economic history in light of that theory, and makes numerous policy recommendations. It contains more arguments about more areas of economic policy than any earlier, and most later, works; Smith's work announced the research agenda of modern economics.

Smith's most famous contribution to economics is the idea of "the invisible hand," the market mechanism whereby the uncoordinated actions of self-interested competitors result, thanks to the interplay of pricing and competition, in the efficient allocation of resources both within and between industries and in the lowest-cost provision of social needs. But it would be a mistake—and the mistake has often been made—to brand Smith as a naive laissez-faire theorist who thought that the unfettered market could resolve all social ills. He had a lively sense of the rapacity of merchants and manufacturers and of the necessity to use regulation and good institutional structure to keep self-interest from running amok.

Smith is also famous for his analysis of the productive power of division of labor, both within the manufacturing sector (as illustrated in his famous discussion of the many distinct tasks involved in factory pin manufacture) and within society as a whole.

Smith made a number of errors and followed innumerable theoretical blind alleys. He notoriously failed to recognize the advent of the Industrial Revolution all around him (though he did recognize the dehumanizing effect of repetitive, specialized factory labor on the laborer). He toyed with a number of different and incompatible theories of value; he proffered an untenable distinction between "productive" and "unproductive" labor. But however many his errors, the fact remains that he was an acute observer of economic behavior and analyst of economic policy and made his observations across an unprecedented range of social and governmental activity. Smith was, in addition, an important jurist, a theorist of ethics, and an entertaining essayist and critic.

David Ricardo

Ricardo was a follower of Smith but differed from Smith both in his overall social outlook and in his technique. In outlook, Ricardo was decidedly more pessimistic. His vision was of a society locked in unending economic conflict, with landlords reaping the greatest benefits for the smallest contribution. Capitalists pay their workers only survival wages, but those wages are driven up by the greed of protectionist landlords, who use tariff legislation to prevent cheap food imports from undercutting their prices. Capitalists' profits are further undercut by their competition with one another. When they do manage to earn profits, capitalists invest them in new productive capacity. This causes the demand for labor to increase and increases the profits accruing to labor—but only temporarily, because wealthier workers will soon have more children, increasing the labor supply and driving wages down to subsistence level again. This population growth drives marginal land into food production at a higher cost. The market price of grain therefore rises, giving a windfall to landlords with highly productive land and cutting into capitalists' profits by again raising the subsistence wage they must pay their workers. Hardworking capitalists thus see their profits undercut both by competition and by food prices; hardworking laborers are kept at subsistence level by population pressure; and landlords reap profits undiminished by competition and increased, not decreased, by population pressure.

This description of the Ricardian economic vision also reveals Ricardo's distinctive technique—his major contribution, for better or for worse, to all subsequent economics. Ricardo's economics is not based on the subtle Smithian observation of the complex behaviors of real people. It is instead based on abstract models, theoretical interactions of prototypical (and often unidimensional) economic actors: the laborer, the capitalist, and the landlord. Ricardo demonstrated an ability to predict the economic consequences of policies by reference to abstract theories involving very few, and very "thin" and abstract, variables. This model building remains one of the most powerful and controversial tools of economics; not for nothing did Joseph Schumpeter label the economist's unhealthy habit of overabstraction "the Ricardian vice."

Throughout his career, Ricardo engaged in a series of debates on economics with his archrival and close friend Rev. Thomas Robert Malthus. Malthus was well known for having advanced the theory that population pressure would always outstrip progress in economic productivity. Workers who earned more than subsistence wages would have more children, and while population would increase "geometrically" (as those children had children of their own), economic progress and agricultural productivity could only be "arithmetic," or linear. Thus, even the greatest innovations in productivity cannot keep the mass of mankind from a life of poverty and near starvation. Ricardo incorporated a version of this population pressure theory into his own. But Ricardo disagreed strongly with Malthus on another of his dismal theses—namely, that manufacturing productivity could give rise to a "general glut," the economic stagnation that would result when too many goods were produced to satisfy too little demand. Following Jean-Baptiste Say, Ricardo argued that no general glut was possible, because every good, in being produced, gave income to someone. That income would inevitably be used to purchase more goods, for people have an unquenchable desire for commodities. This idea—that a general glut of goods in the market is impossible because the income generated by the production of goods will always be used to buy other goods—has come to be known as Say's law. It is sometimes described by the misleading formula "Supply creates its own demand."

John Stuart Mill

John Stuart Mill is today better known as a political and moral theorist than as an economist, but his *Principles of Political Economy* was the undisputed leading text in economics for the entire latter half of the 19th century. Mill's work is the summation of classical political economy; his was the work from which the postclassical economists first learned their economics.

Mill saw his work as little more than a refinement and restatement of Ricardo's: "I doubt if there be a single opinion in the book, which may not be exhibited as a corollary from his doctrines." But Mill (particularly in later editions of his work) was more inclined than Ricardo to be sympathetic to socialist and other reformist argument. Mill was willing and able to engage in Ricardian theoretical abstraction, and he believed generally in laissez-faire policies, but he balanced both these tendencies with a real-world concern for effective social reform.

He made room for such social reform by drawing a sharp distinction between economic production and economic distribution. The laws of economics governing production, Mill thought, are rooted in nature: The productivity of labor power or of land is determined by objective forces. But distribution is determined not by nature but by society and is thus subject to our control. Where Ricardo saw landlords' enrichment and workers' impoverishment as following inevitably from economic laws, Mill saw these things as correctable through progressive social policy: taxation, redistribution, and education.

Like Adam Smith, Mill was noted not only as an economist but also as a progressive social and political theorist, as a philosopher, and as an essayist and critic.

Karl Marx

Karl Marx's economics is often taken to mark a decisive break from classical political economy. But Marx saw his own work as inheriting the insights of the classicals and, in some sense, completing them. Marx thought highly of the classicals not only for having made great strides in mapping out the laws governing production in the capitalist economy but also for having dealt explicitly with the broader social forces and contradictions to which those laws gave rise.

What Marx thought was missing from the insights of the classicals, though, was the full realization that the laws they were charting were not eternal but were the laws only of a particular historical moment. Marx saw those laws as unique to a historically determined system of production (the capitalist system) that had itself arisen inevitably from the forces and contradictions inherent in the previous (feudal) economic system. In his own work, Marx sought, in part, to correct and qualify the insights of the earlier classicals into the workings of the capitalist economic system. But he also sought to situate that system within a dialectical history of the progress of economics. Much of his work consisted in reviewing and illustrating the wrenching dialectical progress of previous economic regimes toward capitalism. And, of course, much of it consisted in his efforts to isolate particular contradictions within the capitalist system that would, in his view, push capitalism toward its own historical completion, destruction, and transformation into what Marx regarded as the next, and final, economic regime: communism.

Conclusion

Mill published his *Principles* and Marx his *Communist Manifesto* in 1848, but as early as the 1830s, economists had begun to experiment with "marginal analysis" and with utility-based theories of economic value. The "marginal revolution" that displaced classical political economy was well under way when Mill died in 1873, and it was complete only a few years after Marx's death a decade later. But although later economists acquired formal tools superior to the classical political economists' and were able to correct many of their technical errors, none has matched the power of their sweeping social vision.

—Stephen R. Latham

See also Marx, Karl; Mill, John Stuart; Smith, Adam

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Political Legitimacy

Political legitimacy concerns the foundation of authority and the obligations of government and organizational leaders. Consent of the governed or managed exists in accordance with the degree of legitimacy that operates between the leadership and the led, which shifts in relation to events, perceptions, and preferences.

In a political context, legitimate government requires its citizens to limit direct democracy and transfer authority to the representative model. In a theocracy, political leaders look to a deity as the source of legitimacy. In hereditary monarchy, a legitimate king or queen is a person with a certain parentage.

International business complicates political legitimacy when cross-border activities raise questions in relation to who should govern such activities when sovereignty is contested. The onset of globalization through the flow of trade, money, and people means that business activities often transcend traditional political borders.

The feature that shapes and determines the possibilities and outcomes associated with political legitimacy is power, a series of implicit and explicit interventions made with the ability to enhance or detract from the legitimate political process. Power operates in a political system through coercion, compulsion, and participation, each of which undermines or strengthens legitimacy.

Business activities in the form of lobbying may damage political legitimacy because they may be perceived to employ unfairly money or gifts as bargaining tools. Lobbying is a technique used to influence the outcomes of political decisions, particularly in the area of regulation and compliance, that may have an impact on costs and profits in a range of industries, sectors, and markets.

Wider institutions such as religious bodies have an impact on political legitimacy. For example, the Catholic Church urges believers to question the legitimacy of institutions that undermine canonic moral principles or the natural law. Various faiths have views on consumerism, interest, profit, and speculation that may shape the policies relating to behavior, introducing codes and practices that may hinder business investment. The influence of culture and society on political legitimacy should not be ignored.

In the world of international relations, the operation of political legitimacy is further complicated by the absence of a formal world government. The structure of the international order is legitimated under certain conditions. The fault lines of legitimacy primarily relate to concerns expressed by interested parties regarding the legitimate status of a state, its related agencies, and the documentation of that legitimacy. International business works alongside the international community at various levels through organizations such as the United Nations, the International Monetary Fund, the World Bank, and the World Trade Organization. The degree to which these organizations are perceived by some stakeholders to prioritize the interests of developed market institutions negatively affects their perceived political legitimacy, particularly in developed countries.

Therefore, political legitimacy depends on the relationship between the authority of leaders and the consent of those led, and the uneven power relations between them, which is further complicated by the presence of money where there is economic inequality.

—Paul D. Sheeran

See also Civil Rights; Ethics of Dialogue; Exploitation; Free Will; Locke, John; Political Theory

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Political Risk

Political risk refers to the probability of loss for commercial market direct investment activity that can be attributed causally to noncommercial, or specifically governmental, politically motivated events or decisions. Originally, and still often, termed *country risk* or *sovereign risk* by analysts and business leaders, the events or decisions at issue are traditionally related to concerns surrounding the likelihood of expropriation or nationalization of a single business or an entire industry, currency inconvertibility or restrictions on convertibility, restrictions on transfer or repatriation of profits, and war or civil disturbances, related to a government's activities or decrees. Additional, more recent concerns include a wide range of nonmarket and government-sanctioned or officially sponsored episodes, such as restrictions on export of goods or services produced, corruption (including but not limited to bribery and extortion), mistreatment of citizens (human rights), and terrorism (state or antistate in origin). Political risk analyses can then refer strategically to probabilistic losses associated with all three stages of an investment business plan: entry into a new market (initial direct investment activity), continuation in a current market (including expansion, merging, or contraction of ongoing business), and exit from a market (winding up the business and selling off assets in an orderly fashion).

While the probabilities for losses related to all such events or decisions could be calculated for investments in one's home country, the notion of political risk is typically applied only to direct investment activity in a host country—that is, where one is not a citizen. Likewise, while these calculations can be made by companies whose homes are is in either developed or developing countries, for investments targeting developed or developing host countries, the vast majority of political risk analyses are generated by or on behalf of businesses based in developed countries seeking to invest in developing host countries.

Although discussion and assessment of nonmarket risks when doing business abroad have been traceable since the beginnings of cross-border trade in the ancient world, formal political or country risk analysis as we know it today historically grew out of the mid-20th-century needs of businesses in the extractive industries, such as mining, and oil and gas companies to calculate the risks associated with operating in relatively unknown and potentially politically unstable regions of the world. Since such companies had to go where the resources were located, they needed some means to help determine whether the investment required would likely yield acceptable returns. Experience suggested that whether returns would indeed be acceptable would only be calculated properly if nonmarket risks could be folded into their business plans. It was not enough, for example, to discover an oil field with sufficient proven reserves to be profitable after explorations were conducted if its operations subsequently would be expropriated once the plant was built and functioning as planned, or if the recovered oil was restricted to host-country use at government-mandated subproduction cost prices, or if profits could not be converted into one's home currency and repatriated.

Attempts to calculate and address these concerns have led (and continue to lead) to some normatively perverse incentives and outcomes: Generally, political risks are easier to identify and key political actors more amendable to influence under dictatorships than democracies, where transparency is limited and reforms are difficult to enforce, and managing risks and opportunities in such environments suggests that government stability is more desirable than overall economic growth for the country. Corruption is consequently a closely related concern, especially since empirical studies hint at but fail clearly to establish direct negative impacts between decisions by corrupt regimes of whatever political stripe concerning business investments and a country's economic development. See, for example, the work of Transparency International through its annual *Corruption Perceptions Index* for data related to business perceptions.

Contemporary global expansion of business operations across a wide range of industry sectors, from manufacturing industrial and consumer goods and foods for international markets to cross-border provision of professional services such as accounting and marketing, today demands market and nonmarket probabilistic loss calculations for all sorts of international investment activities. Concomitantly, freer production and movement of goods and services require less emphasis on accommodating problematic regimes.

In the face of these uncertainties and potential losses, businesses look to analysts to help factor nonmarket contingencies into their investment planning. Some companies establish in-house bureaus or departments to offer analyses and advice; others look to professional service firms that provide, for example, banking, accounting, or legal advice and also supply political risk calculations as part of their advisory packages; still others seek out independent practitioners and firms that specialize in providing political risk analyses.

Whatever the locus of the analysts, political risk advice is typically conducted and proffered in a quantitative or qualitative form, with emphasis on macro or micro perspectives, in aggregated regional or country-specific geographies, according to the theoretical commitments of the analysts and the needs of the business. Hence, one report might provide a quantitative analysis of macroeconomic conditions across Southeast Asia to a computer components manufacturer, where the principal political risks might concern foreign exchange volatility and convertibility. A second report might provide a qualitative analysis of the specific conditions for mining in Irian Jaya, where the principal political risk could center on managing the triangle of relations between the indigenous inhabitants, the Indonesian government, and the company.

One standard qualitative methodology uses a panel of country experts, often political scientists or other academic and business specialists who have considerable experience in the region or country under study, to provide responses to questions in a formal survey that permit narratives as well as scaled scores. A variation on this method affords a feedback loop whereby all initial responses are returned to panel members so that they can reevaluate their initial judgments in light of others' anonymous responses. The reworked final set of replies then becomes the basis of a combined averaged, scaled, and narrative report. One standard quantitative methodology uses a panel, often of professional economists or econometricians, to assess macro- and microeconomic and politicosocial conditions in a region or country on the basis of data reported by international agencies such as the International Monetary Fund and the World Bank, as well as publicly available data from the government(s) under study, along a narrow, weighted range with a set scale for each criterion. These numbers are then averaged to produce a single number along a set scale for an overall evaluation of risk in that market. See, for example, the range of country and regional reports available from the Economist Intelligence Unit.

A standard mixed methodology uses a panel of academics, businesspeople, and professional economists, who provide narrative rationales along with weighted, scaled scores for a report that gives a single number along, say, a 100-point scale (0 = *no risk*, 100 = *certainty of loss*), with a historical assessment of how the region or country has moved along the risk scale over the past 5 to 10 years and its likely place along the scale over the next 5 to 10 years. See, for example, the work of firms such as Oxford Analytica and the semiannual risk surveys published by *Euromoney* magazine. A relatively recent innovation in the mixed methodology category is to apply Bayesian decision theory to aid in the computation of probabilities of risks and outcomes for particular projects in specific locales.

Finally, managing risks, whether political or commercial in nature, requires more than knowledge about the possibilities of incurring losses. So to give incentive to companies to engage in foreign direct investment, government-sponsored and private reinsurance agencies now provide political risk coverage. For example, the Overseas Private Investment Corporation (OPIC), an agency of the U.S. government, has long provided political risk advice and insurance to American companies seeking to establish operations overseas. The Multilateral Investment Guarantee Agency (MIGA), an international governmental financial agency within the World Bank Group, has provided political risk insurance since 1988 to companies from member states (irrespective of whether the member is a developed or a developing state) seeking to invest and operate in another, developing country member state. OPIC provides political risk insurance for investments in more than 140 countries, while MIGA can underwrite political risk insurance across its more than 180 members.

—Daniel Walter Skubik

See also Alien Tort Claims Act; Bayesian Approach; Foreign Corrupt Practices Act of 1977 (FCPA); Foreign Direct Investment (FDI)

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Political Theory

Political theory treats a wide range of concerns having to do with normative aspects of the state, power, individuals, and groups. Some political theorists concern themselves with more or less traditional attempts to justify and explain specific regime types, such as liberal democracies, or their underlying philosophies, such as liberalism. Others work on more recondite areas, such as the attempt to ground political and social action in the absence of metaphysical foundations or specific aspects of the history of political thought.

This entry, however, shall focus on several overarching conceptions important in considering political questions within contemporary liberal democracies. With this in mind, we will begin with three major concepts, liberalism, liberty, and consent, and then focus on three areas of specific concern for the student of business, distributive justice, property, and natural or human rights.

Liberalism

Liberalism is the term for the political philosophy that underwrites most contemporary Western societies. Originating in the early modern political thought of Thomas Hobbes (1588–1679) and John Locke (1632–1704), it still provides a philosophical foundation for contemporary political philosophers as different as John Rawls (1921–2002) and Robert Nozick (1938–2002).

Liberalism relies on several key assumptions about human nature, including the following: that human beings are fundamentally rational, that human beings are endowed with inherent "natural" rights antecedent to any social contract or political association, and finally that people are naturally competitive and basically self-interested. These assumptions suggest that people are capable of living freely and determining their own interests, as opposed to being controlled by passions, emotions, or irrationalities. As a result of these basic assumptions, several conclusions follow. The most important of these is that political organization should be oriented to maximizing the individual's ability to pursue whatever idea of the "good life" is desired, provided that it does not interfere with the abilities of others to also pursue their conception of the good life. In this sense, government is considered to be "instrumental" in that it is limited in size and scope to doing what the individual cannot do for himself or herself.

In the "classical" liberalism of John Locke, the government is restricted to the very basic functions of defense, policing, and judicial work and, to a lesser extent, regulation of commerce and public works. All other matters should be left to individuals' own inclinations. Government plays an important role in regulating disputes between individuals, but it should remain to the greatest degree possible neutral on the question of the good life, preferring to prevent infringements on individual rights rather than designating ways of living.

In a more abstract sense, political communities under liberalism are considered to be artificial constructs, designed to guarantee particular rights to individuals while avoiding any unifying conception of the good. Freedom of the individual is paramount under liberalism, and the particular kind of freedom emphasized in liberalism is termed "negative" freedom, or liberty (see below).

The classical liberalism of John Locke described above has its closest present-day American equivalent in the various libertarian philosophies, a prominent example being Robert Nozick's *Anarchy, State, and Utopia* (1974). Mainstream liberalism today, however, relies on a more expansive notion of the role of the state and its role in assisting individuals toward their conception of the good life. John Rawls perhaps best represents this position, arguing in *A Theory of Justice* that the state has a responsibility to ensure that all members of the political community have at least some minimal ability to pursue the good life. Rawls's position provides a philosophical basis for the contemporary welfare state.

Liberty

That much debate surrounds the concept of liberty should not be surprising, given its foundational role in political theory since the time of Plato; much disagreement remains about the basic meaning of the term. In the latter part of the 20th century, theorizing about liberty was decisively shaped by Isaiah Berlin (1909–1997), whose seminal essay "Two Concepts of Liberty" influentially divides the term into "negative" and "positive" types.

Negative liberty finds its roots in the thought of Thomas Hobbes, who in *The Leviathan* famously defines liberty as "the absence of external coercion."

Although Hobbes's definition is extreme, his point is clear: Liberty consists in freedom from interference on the part of either the government or the wider society, with the latter given a prominent role first in the writings of John Stuart Mill (1806–1873). Negative liberty depends heavily on liberal neutrality on the question of the good life and on an idea of a self that has the ability to develop and fulfill its own idea of the good life. The individual, in this sense, seeks noninterference to the greatest degree possible from the government and the wider society in pursuit of the good life. And as Mill points out in *On Liberty*, negative liberty restricts interference in the lives of individuals to cases where the behavior of the individual would harm others; the individual's own good is not sufficient warrant for interference.

Positive liberty, in contrast, usually begins with a more unified conception of the good life and a conception of the self more dependent on the wider social and political community. Individuals need certain key characteristics to fully thrive as human beings. These characteristics can be as simple as a good education, self-control, or a level of material comfort, but most depend on conceiving the individual as being split between a higher and a lower nature, and the latter ought to be suppressed or at least controlled in pursuit of a higher self. Berlin highlights the darker side of positive liberty, noting that totalitarian regimes often have very well-defined ideas of self-fulfillment, which they force on an unwilling population. Writing during the height of the Cold War, Berlin draws parallels between positive liberty and the excesses of Communism under Stalin, where self-fulfillment involved the sublimation of the individual to the collective.

Berlin's account of liberty has not gone unchallenged. Gerald MacCallum, for example, argues that freedom always has a triadic structure consisting of an agent, an obstacle, and a goal, where the goal can be to *do* or *not do,* to *become* or *not become* something. Despite criticism, Berlin's conceptual apparatus of negative and positive freedom remains an important basis for understanding human freedom.

Consent

Consent is a key term in the contemporary justification of the state. States are frequently said to be legitimate to the extent that they rest on the consent of the governed; liberal states in particular, with their heavy reliance on the autonomy of the individual, need to demonstrate consent on the part of the governed. Consent to the state also generates political obligations. Individuals who consent to the state agree to abide by promulgated laws.

In general, an individual is said to be able to consent when he or she has knowledge of the gravity or consequences of agreeing and freely agrees (or is not coerced). Both of these qualifications—as we shall see—create serious and perhaps insuperable problems for the theory of consent.

Political theorists distinguish between two types of consent: express and tacit. Express consent consists of active declarations—usually verbal or written—of agreement. Examples of these are loyalty oaths, oaths of citizenship, and oaths of office. In general, express consent is considered to be binding, and individuals who have expressly consented generate obligations to the state that they have a moral responsibility to honor. In most contemporary states, express consent is a relatively rare phenomenon and cannot be relied on to provide legitimacy to the government.

Tacit consent, however, proves more difficult to establish. John Locke makes one of the earliest arguments for tacit consent in his *Second Treatise of Government* (1689), where he argues that simple presence in a given territory indicates tacit consent to the government. Locke's argument clearly fails, however, in that it is not clear that the individual is knowledgeable about the agreement or necessarily has the option to leave. More recent attempts to establish tacit consent are equally problematic, most failing to meet the criteria for consent outlined above, and political theorists have turned to other means of generating legitimacy for the state and moral grounds for obeying the law, such as arguments based on duty, fair play, and gratitude. Unfortunately, as A. John Simmons argues, these arguments are equally difficult, and this fact presents a major problem for liberal theories of government.

Distributive Justice

Distributive justice concerns the manner or pattern by which social benefits and goods are distributed within a society. The attempt to arbitrate between the competing claims of individuals, groups, classes, firms, or geographical areas should be kept distinct from procedural justice, which is concerned with proper adherence to administrative processes. Although discussions of distributive justice go back to Aristotle, we will focus here on the most influential contemporary accounts.

John Rawls

Rawls's 1971 work, *A Theory of Justice*, places the regulation of the individual's conception of the good life as the primary responsibility of government. In this sense, distributive justice concerns itself with how to distribute the prospect of obtaining what Rawls calls "primary goods": basic rights, powers, liberties, authority, and opportunity. These are things that Rawls claims every rational person would be assumed to want, as they allow for maximal flexibility in the pursuit of one's goals.

Conflicts over the distribution of primary goods can be resolved by appealing to two principles. The first of these is the "principle of greatest equal liberty," or that each of us has an equal right to the same total system of basic liberties. This system—where "basic liberties" are roughly equivalent to the U.S. Bill of Rights—is to be as extensive as possible.

Rawls divides his second principle into two parts, the "difference principle" and the "principle of fair equal opportunity." According to the former, social and economic inequalities are to be arranged to the greatest benefit of the least advantaged, while the latter requires that we go beyond formal equality of opportunity to ensure that persons with similar skills, abilities, and motivations enjoy comparable potential for success. Rawls is clear that the first principle is necessarily prior to the second principle. In other words, we must satisfy the principle of greatest equal liberty *before* we satisfy either the difference principle or the principle of fair equal opportunity. In practical terms, these two principles justify a substantial degree of redistribution of resources in a society to ensure that those worst off have ample opportunity to pursue the good life.

Rawls justifies his two principles of justice by appealing to the decision preferences of hypothetical individuals in what he calls the "original position"—a version of the older state-of-nature argument used by the earlier liberal theorists to justify the social contract. Rawls places these individuals behind a "veil of ignorance," allowing them to know that they will be members of the society the rules for which they will create but not allowing them to know any specifics about the position they will occupy in that society. Rawls argues that these individuals will favor maximizing the fortunes of the least well-off, in effect hedging their bets lest they wind up occupying that position.

A Theory of Justice has attracted much attention, and a good deal of it is critical. Michael Sandel, for example, has claimed that Rawls's conception of individuals in the original position rules out the possibility of a person's being constitutively attached to his or her ends and that this conception is invalid and incoherent. Other critics have pointed out that it is not at all clear that the individual in the original position will select to maximize benefits for the least well-off given any reasonable account of risk taking.

Similarly, it is not entirely clear why basic liberties need to be equally distributed at all. Certainly, individuals do not maximize the use of all their liberties. It might make more sense to give more of some liberties to some individuals and fewer to others, and these may not be inconsistent with their own understanding of the good life.

In response to his critics, Rawls substantially revised his argument in later editions of *A Theory of Justice*, attempting to distinguish his theory as relevant to a property-owning democracy rather than a welfare state conception. In a later work, *The Law of Peoples*, Rawls also objected to the application of his principles of justice to the international sphere.

Property

Much of contemporary political thought surrounding property is fairly recent in origin, although one can find early discussions of property in texts such as Locke's *Two Treatises of Government* and Hegel's *Philosophy of Right* (1821). More recently, C. B. Macpherson, in *The Political Theory of Possessive Individualism* (1962), called attention to the subject by arguing that the major figures of 17th-century political thought were deeply indebted to possessive assumptions about market society, and he did so through an analysis of their (flawed) theories of property.

Macpherson's argument was quite controversial, provoking attempts to develop new rights-based accounts and rules to explain what property is, what rights are associated with it, and how to justify its acquisition. These issues are particularly pressing in that property is clearly implicated in the distribution of power and justice; if an adequate explanation of the distribution and transferal of property is unlikely, existing social and economic structures can be called into question.

One important voice in this debate can be heard in Nozick's entitlement theory in *Anarchy, State, and Utopia*, where he discusses a system of property justification similar to Locke's, arguing that labor creates entitlement and that property acquisition can only be limited when it is shown to worsen the situation of others, which he seems to narrowly define as depriving others of property altogether. Once property has been established, the owner is free to alienate the property through market exchange, gift giving, and so on.

Nozick's arguments, however, are highly problematic and do little to answer some of the basic questions about the acquisition and distribution of private property. In this sense, they are symptomatic of the problems facing a rights-based account of property. In fact, Jeremy Waldron (1953–) concludes—partially based on Nozick's argument—that no rights-based argument for private property is possible.

More typical of recent discussions of property is Stephen Munzer's *A Theory of Property* (1990). Munzer, recognizing the important role property has in the living of a fully human life and drawing heavily on Kant and Rawls, argues for a system of heavily constrained private property, with justice and equality taking precedence over efficiency and desert.

Rights

The liberal sense of self involves the claim that individuals have rights: inherent moral claims that protect certain values such as liberty, equality, or autonomy. In this sense, rights are distinct from privileges, which accrue to individuals on the basis of their membership in a particular political community. For liberalism, rights provide an important barrier between the individual and the government or the wider society.

When we say that "*A* has a right to do *X*," we mean that one ought not interfere with *A*'s ability to do *X* and that there is nothing wrong with *A* claiming a right to do *X*. We also assume that the right is universal, so that if *A* has the right to do *X*, so do all other individuals.

Critics of rights-based justice, including Mary Ann Glendon and Michael Sandel, have concerns about the emphasis on rights in liberal democracies. The most general of these is that the use of rights is too egoistic to allow for an adequate sense of community to develop. In addition, rights-based disputes are not subject to easy resolution, thus leading to increased litigation. These critics would prefer to see more of an emphasis on duties or responsibilities, drawing the individual into the community as opposed to constantly marking off the boundaries between the self and community. Feminist critics such as Carol Gilligan, while agreeing with Glendon and Sandel, also point out that an emphasis on rights mirrors a privileging of aggressive, masculine values.

The criticisms listed above sometimes mask a deeper concern with the underlying justification for rights. Early modern thinkers such as Locke grounded rights in divine command, while later thinkers preferred to talk about "natural" rights. Either approach, however, leaves one open to the charge that the assertion of a right looks like just that, an assertion, without evidence or proof. As Jeremy Bentham pointed out, the assertion of a right lays down as truth what one cannot prove.

This is a vexing and difficult problem for liberals and provides much traction for critics. Communitarians such as Charles Taylor, in particular, assert that rights-based liberalism, grounded in a sense of self that is antecedent to society, does not square with our perception of reality. Instead, they argue, society should be viewed as antecedent to the self, providing the individual not only with important formative characteristics but also privileges. These privileges extended by society are not to be viewed as the sole possession of the individual. Liberals complain, correctly, that this view of the self substantially weakens the barrier that rights provide against the government or society but fail to provide a persuasive alternative understanding of the self.

—Jeff Miller

See also Anarchism; Arendt, Hannah; Aristotle; Autonomy; Bentham, Jeremy; Capitalism; Communism; Communitarianism; Engels, Friedrich; Equality; Freedom and Liberty; Hayek, Friedrich A.; Hobbes, Thomas; Human Nature; Hume, David; Kant, Immanuel; Kantian Ethics; Libertarianism; Locke, John; Machiavellianism; MacIntyre, Alasdair; Mill, John Stuart; Nozick, Robert; Nozick's Theory of Justice; Property and Property Rights; Rawls, John; Rawls's Theory of Justice; Rights, Theories of; Rousseau, Jean-Jacques; Utilitarianism

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POLLUTION

Pollution is defined as undesirable physical, chemical, or biological changes in the characteristics of water, air, or land that negatively affect the survival, health, or activities of humans and other living organisms. For much of human history, the natural world was considered as an adversary to be defeated and as a reservoir of resources to be exploited—pollution was at most a local problem for some communities and was not of widespread practical or ethical concern. However, as the world rapidly industrialized and as problems of pollution grew in regional and global scope, ethical theories of the environment were advanced to address the ethical and moral obligations of humans to stem the adverse impact of human-generated pollution.

The amount of pollution attributable to human activity has grown geometrically over the past two centuries, coincident with global industrialization. In 2001, humans generated about 927 million metric tons of solid municipal waste (garbage) and about 270 million metric tons of solid hazardous waste. Improper disposal of solid wastes can cause groundwater pollution, mercury and polychlorinated biphenyl (PCB) poisoning, birth defects, increased cancer rates, and many other human health consequences. The United Nations estimates that during 1995 humans emitted about 22,000 million metric tons (2,204 pounds) of carbon dioxide (CO_2) into the air, 141 million metric tons of sulfur dioxide (SO_2), and 99 million metric tons of nitrogen oxides (NO_x), among many other gases. Worldwide per capita emissions of CO_2 average about 4 metric tons annually. In the United States, Australia, and Canada, annual CO_2 emissions approach 20 metric tons per capita. Western Europe, Japan, and other industrialized nations emit about half this amount. Carbon dioxide is implicated in global warming, sulfur dioxide in acid rain, and nitrogen oxides in smog and increases in ground-level ozone. Aggregate statistics for the quantity of polluted wastewater (sewage) that is discharged each year are unavailable due to measurement problems, but the quantity is huge and is growing.

As human-generated pollution has come to affect much of the natural environment, consideration of pollution as a topic of ethical and moral discourse has grown. Three broad strands of ethical theory have been brought to bear on the problem of pollution. There are those who assert that the natural world is valuable unto itself and that moral behavior demands that humans protect the natural world from pollution regardless of the cost or its impact on humans. A second perspective is that pollution is wrong in principle only when it causes avoidable harm to humans, and possibly to other "higher-order" sentient animals. The third perspective is that pollution is never wrong in principle but only when the harm of pollution outweighs its human benefit. Much of the current debate and controversy about pollution can be traced to these three ethical perspectives and to their inherent differences.

Environmental and Social Impact of Pollution

The impact of pollution on global societies, economies, and ecosystems is profound. Human-generated emissions of greenhouse gases (GHGs) are widely implicated in global warming. GHG emissions, including carbon dioxide, methane, nitrous oxide, and fluorinated gases, among others, totaled 33 billion metric tons (CO_2 equivalent weight) in 2000. Based on longitudinal temperature studies, scientific theory, and computer climate models, worldwide temperatures may increase by 1.4 to 5.8 °C between 1990 and 2100, with unknown consequences. Predictions vary widely, but some forecasts suggest that sea levels may rise as the polar ice caps melt, precipitation patterns may shift, agricultural productivity patterns may change, ocean currents may destabilize, and ecosystems may evolve (e.g., from wet to arid), with unpredictable impacts on plant and animal life. Beyond global warming, emissions of sulfur dioxide, largely from coal- and oil-burning power plants, are a cause of acid rain, which damages forests and fish populations in lakes and streams. Chlorofluorocarbons (CFCs) used in refrigeration and air conditioners are thought to be a cause of ozone depletion in the upper atmosphere.

On a regional and local scale, agricultural runoff and dumping of raw sewage have damaged the ecosystems of many rivers, lakes, and estuaries. For example, in India, every year the Ganges River accepts raw sewage from 70 million living people and the cremated remains of some 30 million dead. The use of DDT as an agricultural pesticide in the 1950s and 1960s is implicated in the sharp decline of some bird species during that period. Air quality is chronically poor in many of the world's largest cities. Mexico City arguably suffers from the worst air pollution in the world: Sulfur dioxide levels range from one to four times the upper limit set by the World Health Organization (WHO), and the WHO guidelines for dust and soot are exceeded by three to six times. The disposal of hazardous wastes also creates serious environmental problems. Globally, about 275 million metric tons of hazardous waste is produced annually. There are 34,000 hazardous waste sites in the United States alone and 1,600 Superfund (abandoned or uncontrolled) hazardous waste sites.

Finally, pollution catastrophes occur periodically, with great social and environmental consequences. In 1984, the accidental release of toxic methyl isocyanate (MIC) gas used in the manufacture of pesticides killed more than 15,000 persons and injured hundreds of thousands of others in Bhopal, India. In 1986, a nuclear power plant in Chernobyl, Ukraine, suffered a catastrophic steam explosion, producing a radioactive plume that badly contaminated parts of Ukraine, Belarus, and Russia; an estimated 4,000 people there are expected to die prematurely because of exposure to radiation. In 1989, the oil tanker *Exxon Valdez* hit a reef in Alaska's Prince William Sound, spilling between 11 and 35 million gallons of crude oil in the enclosed sound and killing about 250,000 sea birds, 2,800 sea otters, 300 harbor seals, 250 bald eagles, as many as 22 orca whales, and billions of salmon and herring eggs. It may be 30 years before Prince William shoreline habitats fully recover.

Causes of Pollution

Why does pollution occur? Since the societal and environmental effects of pollution are usually negative, why not simply stop polluting? The simple answer is that all human activities, processes, and systems generate by-products that are unintended and unwanted. When these by-products have harmful effects on human activity or on the environment, they are termed *pollution*. As an example, humans have burned wood for heat and light for thousands of years. Burning wood involves a chemical reaction that combines oxygen in the air with carbon in the wood, releasing heat and producing carbon dioxide, smoke, and ash (unburned solids), among many other compounds. The carbon dioxide, smoke, and ash are undesired by-products of burning wood that can pollute the environment if disposed of incorrectly. In fact, it is impossible to burn wood (or coal or oil) without creating carbon dioxide, smoke, and ash since these are the inevitable by-products of hydrocarbon combustion. And so it is with all human-related activities, as well as those of all living organisms. Raw materials (air, water, food, minerals) are acquired and then converted into something useful (energy, nourishment, materials, products). But there are always "leftovers" that can become harmful or deadly "pollution" if disposed of incorrectly. The challenge for humankind is to minimize, manage, and control its waste streams so as to minimize their negative environmental impact and to thereby minimize pollution.

Environmental Impact

The impact of pollution has grown in step with the human population. A common conceptual model defines the impact of pollution as the product of population, resource consumption per capita, and consequent pollution per unit of resource consumed:

$$\text{Impact of pollution} = \text{Population} \times (\text{Resource use/person}) \times (\text{Pollution/unit resource})$$

The increase in global pollution in recent decades can be explained, at least in part, by this equation. First, world population has exploded over the past two centuries. World population reached 1 billion in about 1800, 2 billion by 1925, 3 billion by 1960, 5 billion by 1990, and 6 billion by 2000. Second, during this same time period, industrialization has created human prosperity on a scale never seen before (albeit unevenly distributed). This prosperity greatly increased the per capita consumption of global resources. Third, as industrial production grew and complex manufacturing processes multiplied, the amount of pollution generated per unit of resource consumed increased. In terms of the equation above, all three terms have increased remarkably over the past two centuries, which helps explain the geometric growth of pollution over the same period.

Tragedy of the Commons

A second explanation for the increase in pollution can be attributed to the *tragedy of the commons.* This expression refers to medieval Europe, where common grazing areas were set aside for pasturing livestock. Since these "commons" were owned by no one but used by many, there was a tendency for local herders to place too many animals on the commons, with the outcome that the commons became overgrazed and were less productive than they would have been with fewer animals. While all might agree that too many animals used the commons and that community welfare would have been improved with fewer animals, it was detrimental to any individual herder to withdraw livestock from the commons. If the community decided to collectively limit use of the commons, then all would benefit. But even if this agreement could be accomplished, individuals had incentives to "defect" from the agreement and to graze more animals than their quota. Without a better enforcement or incentive mechanism, the result was a "tragedy" in that the commons were overgrazed even though less grazing would have benefited all.

This situation provides an analogy that can be used to partially explain the difficulty in reducing human-generated pollution. The atmosphere, oceans, seas, rivers, lakes, and unproductive land have traditionally been owned by no one but are available to all for use as dumping grounds for the waste streams of human activity. These "environmental commons" are modern-day equivalents of the medieval grazing commons. For much of history, pollution from human activities was small compared with the environmental commons, and the aggregate impact of human pollution on nature was relatively small. But as human populations exploded in the 19th and 20th centuries and polluting activities increased geometrically, the negative impact of human pollution on the environmental commons also exploded. Even if individuals, industries, or communities unilaterally decided to reduce their pollution, each would pay a cost relative to others using the same environmental commons but not reducing their contributions to pollution.

Contractual Ethics and Pollution

One possible answer to the *tragedy of the commons* is *contractual ethics* or *contractualism.* Contractual ethics intends to create rules or contracts by which all individuals in the sphere of the contract must abide. For example, in the case of the overgrazing of a common pasture, medieval communities developed strong rules and cultural norms regarding who could use the commons and how many animals they could graze there. Violators of the rules and norms were subjected to social sanctions such as being prohibited from using the commons in the future.

In more recent times, government agencies have passed laws and established regulations that limit and prohibit certain types of polluting activities and regulate how various forms of pollution are handled. These regulations are binding on all citizens and businesses operating in the jurisdiction, and violators are typically dealt with by the civil and criminal justice systems. By establishing these laws, the tragedy of the commons is avoided because there is no legal opportunity to easily defect and there are significant penalties for those who try. While the costs associated with these regulations are substantial, the costs are distributed across society so that one group, business, or individual is not particularly disadvantaged by the regulations. In general, the intention of government regulation and law is that all parties bear the costs and all gain from the benefits of clean air legislation. In this way, it can be in our rational self-interest to submit to coercive rules and regulations. In many instances, we can all benefit when we mutually agree to restrict our actions and when we can be assured that our agreement will be enforced.

More specifically, contractual ethics posits that groups of individuals form *social contracts* that are mutually coercive and mutually beneficial to members of the group and that mitigate harm to society and promote behavior that is valued by society. These contracts may take the form of government law and regulation, religious creeds and doctrines, industry standards, or third-party accreditations. Note that in some cases participation in the contracts is obligatory (e.g., government law), but in other cases participation is voluntary (e.g., third-party accreditation). As an example of the latter, many firms voluntarily work to be certified by the International Organization for Standards (ISO) as compliant with its ISO 14000 environmental management standards. (ISO is an international nongovernmental organization that sets international standards used by governments and industries around the world.) ISO 14000 is a set of management standards intended to ensure that products and services have the lowest possible environmental impact, and it includes pollution management standards. ISO 14000 is entirely voluntary, but many businesses and governments require that their vendors be ISO 14000 certified, thus bringing economic pressure and industry sanctions to bear on many businesses that might otherwise defect from this "social contract."

The scope of social contracts necessarily expands as human communities grow and increasingly interact with and affect one another over time. In medieval Europe, social contracts governing the use of a commons involved only a single village or manor. In current times, the activities in one nation-state may have a severe impact on the well-being of other nation-states around the world. For example, air pollution generated in the United States causes acid rain in Scandinavia, industrial pollution in China influences weather on the west coast of North America, and carbon dioxide emissions from human sources around the world may contribute to global warming. One of the great challenges of contemporary environmentalism is to develop enforceable social contracts between nation-states that will mitigate and control the harmful effects of pollution on the entire world.

Utilitarian Ethics and Pollution

Utilitarian ethics focuses on the outcomes or consequences of an act (or acts) with the goal of maximizing human pleasure, happiness, and prosperity, or, more generally, human "utility." Utility is defined as the sum of all the benefits and all the harms that flow from an act. The benefits and harms included in utility calculations can include physical pleasure and pain, happiness and distress, wealth and poverty, education and ignorance, beauty and ugliness, and health and sickness, among many others. A utilitarian perspective does not identify pollution as either good or bad. Pollution has no moral content. The rightness or wrongness of pollution depends on the *consequences* of pollution—that is, on the goodness and badness that flows from it.

A general utilitarian view of pollution is that the harm caused by pollution must be balanced against the needs of humankind and the human benefits that flow from pollution-generating activities. For example, coal-burning power plants create energy in the form of electricity but produce air and water pollution as side effects. Humans need energy to flourish but are harmed by pollution. A utilitarian would argue that if the benefits of the energy created by the power plant exceed the harm done by its pollutants, then the "greater good" is served by allowing the power plant to operate.

A utilitarian perspective on pollution has two main attractions. First, it provides a single absolute principle with which to evaluate and judge polluting activities: Does a polluting activity on balance increase or decrease the general welfare of humankind? If yes, then the activity should be undertaken. If no, then it should not. Second, utilitarianism provides a concrete means or calculus to assess morality (e.g., utility maximization) rather than just offering general rules or platitudes (e.g., "don't pollute unless you have to"). Utilitarianism suggests that morality derives from the benefit it provides to humankind and that humankind is not a slave to some external morality—moral actions must benefit humans or they are not moral.

Because utilitarianism fundamentally relies on cost-benefit analysis to judge the ethical content of an act, it is critically reliant on science and scientific reasoning to inform us of the likely consequences of our actions (positive and negative). Science provides utilitarianism with intellectual and rational support, but it also suggests several problems when a utilitarian evaluates polluting activities. First, how can we truly know the consequences of our actions? Second, how do we actually calculate the "greater good" or "maximize utility"? And third, over what time frame should we maximize utility?

Knowing the Consequences

The first problem of utilitarianism is that it is difficult to know all the antecedents and consequences of our actions, and consequently, it is difficult to evaluate the utility of those actions. For example, coal-burning power plants historically create significant pollution, including sulfur dioxide gases that cause acid rain. For many years, power plants have built very tall stacks to better disperse and dilute the effects of airborne and gaseous pollutants. These stacks do, in fact, reduce airborne pollution in the region surrounding a power plant but have the unanticipated consequence of causing acid rain in regions far away from the plant. When sulfur dioxide is launched high into the atmosphere, natural chemical processes convert it to sulfuric acid, and high-altitude winds blow the acid across continents and across oceans. The sulfuric acid eventually washes out of the atmosphere in rain, causing damage and destruction to forests and lakes far distant from the originating power plant. A similar example is the longtime use of CFCs in refrigeration and cooling systems and their eventual effect in reducing upper-atmosphere ozone, thus creating an "ozone hole" over Antarctica during the greater part of each year.

When utilities built power plants with high stacks, and refrigeration companies designed compressors using CFCs, no thought was given to acid rain or ozone depletion because their detrimental effects were unknown and unanticipated at the time the design decisions were made. In fact, high stacks were originally designed into power plants at additional expense to *reduce* regional pollution, but it had the unexpected side effect of increasing pollution farther away. This case provides a good example of the problem of *unanticipated consequences* when evaluating the pollution impact of human activity.

The utilitarian response to the problem of forecasting outcomes is to assert that humans cannot know everything but must still make consequential decisions every day. Even choosing to do nothing is a decision with its own anticipated and unanticipated consequences. Imperfect and insufficient knowledge is a dilemma of human existence that cannot be avoided, so the best we can do is to assess the *expected* utility of an action and adjust to consequences as they occur. In the case of coal-burning power plants and acid rain, retrofitting power plants with stack scrubbers, installing more efficient coal-burning technology, and burning low-sulfur coal has reduced (but not eliminated) the occurrence of acid rain in many parts of the world. To the utilitarian, this is an acceptable outcome. Decisions were initially made to produce needed energy and reduce known sources of pollution, and when new sources of pollution were created and identified, corrective action was taken.

Calculating Utility

A related problem with utilitarianism is that of calculating utility. In the case of power plants and acid rain, what is the true benefit of the energy created by a power plant, and what is the true harm of acid rain? Who decides the relative worth of the benefits and harms? For example, environmentalists and ecologists might assign a very high weight to the harm caused by acid rain and a relatively low weight to the benefit of cheaper electricity. To them, the ecological damage caused by acid rain far exceeds the benefit of more abundant energy and lower electric prices. Conversely, industrialists and urban consumers may ascribe a much higher value to low electric prices than to the health and well-being of fish in a remote lake hundreds or thousands of miles away. How do we decide which perspective is correct, and how do we calculate utility?

The utilitarian answer to this problem is that conceptions of utility evolve over time as a part of ongoing political and cultural discourse and debate. It was once acceptable to dump raw sewage into streams, rivers, lakes, and seas because the amount of sewage was small relative to the size of the waterways and because technology had not evolved to the point where there existed practical alternatives. As populations grow and sewage volumes increase, the harm caused by untreated sewage accelerates, and as technological solutions become available, the relative ratio of harm to benefit of dumping raw sewage changes. While utility was once maximized by dumping raw sewage into waterways, sewage treatment is now the norm in industrialized countries even though the direct costs of sewage treatment are significant. Contemporary debates about environmentalism and pollution change a society's calculation of utility, as does evolving technology and growing human knowledge. The utilitarian perspective is that human culture and the natural world evolve dynamically, and so must our calculations of utility.

Time Frame

A third problem with a utilitarian perspective of pollution is the time frame over which utility is calculated. In many cases, pollution may have long-term effects that are difficult to know and to quantify. For example, a current debate involves the disposal of radioactive wastes from nuclear power plants. All nuclear power plants generate radioactive by-products, some of which will remain dangerously radioactive for thousands and tens of thousands of years. How should we determine the potential long-term harm that these wastes cause? Proponents of nuclear power argue that these wastes can be safely buried in geologically stable formations in areas remote from human habitation. Critics of nuclear power counter that areas that have been geologically stable may become unstable through natural processes and that some future civilization may unwittingly dig into a buried waste dump, unleashing significant radioactive harm on an innocent populace.

The utilitarian answer to the problem of time is similar to the answers to the first two problems: We must make the best calculations of benefit, harm, and net utility that we can, given current human understanding and preference, and then we must be prepared to modify and correct our decisions as history unfolds. In the case of nuclear waste in the United States, the current societal calculation of utility is currently tipped in favor of not interring nuclear waste in central repositories, and nuclear waste remains stored in temporary facilities adjacent to nuclear power plants. As technology evolves and if the environmental costs of burning fossil fuels continue to grow, the calculation of benefit and harm may begin to favor the central burial of nuclear waste even if there is some small chance of a problem in the distant future. Conversely, if there are new nuclear accidents such as Chernobyl or if nuclear wastes are used in terrorist attacks, then calculations of utility may dictate that nuclear power be abandoned altogether as an energy source. Since morality resides in maximizing human utility and not in an act itself, a utilitarian is morally indifferent to the outcome of this debate so long as it ultimately maximizes human welfare.

Contemporary Ethics and Pollution

Attitudes and beliefs about the ethics of pollution are evolving rapidly as global pollution rises and its attendant problems become increasingly a matter of concern. Pollution and its associated effects are being addressed using a variety of controls and methods that reflect the ethical theories of morality, including contractualism, utilitarianism, and rule-based deontology.

Contractual Control of Pollution

The earliest and most prevalent response to pollution has been contractual control in the form of laws, rules, and regulations. For example, in 1306, King Edward I of England banned the use of sea coal in London because of the smoke it caused. In the 1880s, Chicago and Cincinnati passed clean air legislation to cope with the rapidly declining air quality. In the United States, the federal government passed a series of Clean Air Acts in 1955, 1963, 1970, and 1990 that addressed air quality standards, motor vehicle emissions, toxic air pollutants, acid rain, and stratospheric ozone depletion. In 1972, the Federal Water Control Act was enacted, which requires (with subsequent amendments) a permit to discharge pollutants into navigable waters, funds the construction of sewage treatment plants, and establishes water quality criteria for the Great Lakes. Similar laws and regulations have been established in the European Union and Japan and are under consideration in rapidly industrializing countries such as India and China. In 1991, Germany passed its so-called Green Dot legislation, which requires manufacturers to take back and recycle packaging associated with their products, and is considering legislation that would require manufacturers to accept the return of their products at end-of-life for recycling. In 2005, the European Commission issued a directive for all members of the European Union to develop recycling plans similar to Germany's.

Globally, signatories of the United Nations Kyoto Protocol agreed to reduce emissions of carbon dioxide, methane, nitrogen oxide, and CFCs by 5.2% compared with their 1990 levels. The Kyoto Protocol is an international treaty negotiated in Kyoto, Japan, in December 1997, with the intent of reducing the long-term concentration of atmospheric GHGs, which are implicated in global warming. By September 2005, 156 countries had ratified the agreement, with the notable exception of the United States, which argued that the treaty would cause undue hardship to the U.S. economy. The unwillingness of the United States to sign the Kyoto Protocol illustrates the difficulty in establishing voluntary contractual obligations between independent parties.

Utilitarian Approaches to Pollution

Over the past decades, considerable work has been undertaken to better understand and measure the impacts of pollution on general welfare and to modify the decision making of individuals and organizations. These include better accounting for the externalities of polluting activities, creating economic incentives to reduce the propensity to pollute, and technological innovations to directly reduce and eliminate pollution.

Accounting for Externalities

To better incorporate environmental externalities, some have advocated the use of a *triple bottom line*, which includes both social and environmental measures of performance as well as the traditional financial measures. Corporations, governments, and nonprofit organizations would include data on each of these three criteria as part of their normal reporting requirements and would be accountable for social and environmental performance just as they currently are for financial performance. One problem with the triple-bottom-line concept is determining standard metrics so that organizations can uniformly and comparably report social and environmental performance. Critics also argue that the triple bottom line diverts organizations away from their core competencies on which society relies. We do not expect social service agencies to build automobiles, and equivalently, we should not expect automobile manufacturers to provide social services. But despite problems and criticisms, many organizations now report their environmental and social performance in addition to financial performance.

Economic Incentives

A number of economic incentive structures have been proposed and implemented to help reduce pollution. Perhaps the most innovative is the creation of pollution markets where companies buy and sell rights to pollute using tradable pollution permits. Government agencies set upper limits or quotas on the aggregate amounts of a particular type of pollution (e.g., carbon dioxide) that can be discharged annually, and companies bid for pollution credits that assign them a fraction of the total quota. Companies that invest in pollution abatement equipment or newer, less polluting processes need to purchase fewer credits, while those with older plants need to purchase more credits. Markets for pollution credits provide economic incentives for firms to invest in pollution control activities and penalize those that do not. Over time, controlling agencies can reduce pollution caps or quotas, thus increasing the price of pollution credits and reducing the total amount of pollution allowed. A number of emissions trading markets currently exist, including the European Union Greenhouse Gas Emission Trading Scheme, which trades carbon dioxide emissions; the voluntary Chicago Climate Exchange, which trades carbon dioxide and sulfur dioxide emissions; and the regional exchanges in Illinois and New York.

Another approach to economic incentives is to directly tax polluting activities and products with the so-called "green taxes." Examples of green taxes include carbon taxes on fossil fuels, garbage disposal taxes, taxes on effluents and hazardous waste, and taxes on end-use products such as gasoline and gas-burning vehicles. For example, Germany has green taxes on petroleum and fossil-fuel-generated electricity. By directly taxing polluting activities and products, economic incentives are created for producers and consumers to switch to less polluting equivalents; for instance, power companies are encouraged to increase investments in renewable energy sources such as wind, and consumers are encouraged to switch from gasoline-powered autos to hybrid autos.

Innovation

A third utilitarian approach to the problem of pollution is technological and procedural innovation, which reduces pollution by inventing new processes and products that inherently generate less pollution than the incumbent alternatives. These innovations can include management and procedural innovation in addition to hard (physical) technological innovation.

For many years, the mantra for mitigating pollution has been "reuse, recycle, and reduce." Perhaps the easiest means to delay pollution is to reuse materials and products rather than throwing them away after one use. When materials and products have reached the end of their useful life, they can be either discarded (often in a landfill) or recycled. Recycling is the process of reprocessing materials and components into other useful products and materials. The third "R" is reduction of the amount of materials consumed; this is sometimes called *dematerializing.*

On a larger scale, businesses and governments are investing heavily in developing alternative energy technologies to supplement or replace fossil fuel power. Since the power industry is a large contributor to global pollution, finding cleaner methods to generate electricity could have a significantly positive impact on pollution levels around the world. Candidates include wind, solar, geothermal, and tidal power technologies, as well as others that are more speculative. In addition to investigating new power-generating technologies, electric power industries are also developing cleaner methods to burn traditional fossil fuels, such as fluidized bed coal technology, which improves efficiency while reducing pollution.

Industrial Ecology

A related approach to pollution is that of *industrial ecology*, which proposes that humans shift from open-loop to closed-loop industrial systems. In open-loop systems, resources are extracted from the environment, consumed, and then discarded as waste and pollution. In contrast, closed-loop systems use the waste stream of one process as the raw material or feedstock of another. The perspective of industrial ecology is that industrial processes are not separate from the biosphere but rather are a part of it in a larger ecosystem. Just as in nature, the wastes of one species are usually a resource for other species, so too the waste streams of one industrial process can be a resource for other processes. For example, the warm water generated from the cooling towers of a power station might be used for fish farming rather than dumping it into a nearby river and changing the area's ecology. By treating industrial and economic activities as closed-loop systems, we may significantly reduce pollution and ultimately reduce costs by reusing material resources rather than discarding them. The promise of industrial ecology and other utilitarian approaches to pollution is to help provide humanity with the methods, means, and incentives to live in sustainable equilibrium with the natural world.

—Stephen R. Lawrence

See also Acid Rain; Anthropocentrism; Bhopal; Christian Ethics; Corporate Ecology; Deep Ecology; Environmental Assessment; Environmental Ethics; Environmentalism; Environmental Protection Legislation and Regulation; *Exxon Valdez*; Gaia Hypothesis; Greenhouse Effect; Hazardous Waste; Kyoto Protocol; Land Ethic; Love Canal; National Ambient Air Quality Standards (NAAQS); Ozone Depletion; Pollution Externalities, Socially Efficient Regulation of; Pollution Right; Recycling; Tragedy of the Commons; Triple Bottom Line; Utilitarianism

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Pollution Externalities, Socially Efficient Regulation of

In economics, an externality is a benefit or cost that accrues to some entity that is a third party to the market transaction. Because under an externality the market price of the good will reflect the benefits and costs of the buyers and sellers of the good but will not incorporate the costs or benefits affecting the bystanders affected by the production or consumption of the good, the market will generally fail to provide these goods in socially optimal quantities. Viewed in this manner, an externality is the difference between the public and private costs (or benefits, depending on the nature of the externality) of a market activity. In the case of positive externalities, output will be below the socially optimal level, while negative externalities will be associated with output in excess of the socially optimal level.

One classic example of a negative externality is the production of pollution. When the externality occurs on the production side, it may be that a firm generates pollutive wastes in the course of producing a good. Generally, the producer will not incorporate the costs those wastes may cause on society in the price of the good. As a result, the good will be underpriced in the market, relative to the socially optimal level, and thus overconsumed. An example of a pollution externality on the consumption side might be the air pollution generated as consumers drive motor vehicles. The price of the car and the price of the gasoline, in a completely free market, are unlikely to include any costs related to this pollution.

Equilibrium output in the market occurs, and economic welfare is maximized, when output is produced at the level where marginal revenue equals marginal cost. In competitive markets, price equals marginal revenue. In both competitive and concentrated markets, the structure of supply and demand will determine the marginal revenue and price. However, the supply and demand in these cases will only reflect the private costs and values to the market participants: the buyer and the seller. A benevolent social planner would view a different set of costs or values. In the case of pollution generated during the production of a good, the planner would realize a supply schedule that reflected higher costs: costs that included both the private costs and the third-party (public) costs. As a result, a market operating under the planner's considerations would charge a higher price for the good and produce a lower quantity of output.

Mechanisms to change the level of output and the price of a good associated with a pollution externality are varied. Private solutions are occasionally possible for some externalities; and the Coase theorem implies that if private parties can bargain costlessly over the allocation of resources, they can internalize the costs and benefits and solve the problem of externalities on their own. It can be difficult to reach such agreements or enforce them without cost, especially when they involve a large number of economic agents; and the assignment of rights that often must exist for the theorem to work may also be difficult to accomplish or enforce. As a result, public solutions to externalities have often been pursued.

Public policies regarding pollution externalities can take one of two approaches, a command-and-control approach or a market-based approach. The command-and-control approach involves output restrictions, requirements to use specific technologies, or even outlawing of certain types of releases. Market-based approaches attempt to use incentives to align private interests with social goals. Arthur Pigou (1877–1959) was an early advocate of addressing the difference between private and social costs through the use of taxes and subsidies, and taxes and subsidies to correct externalities are thus often referred to as Pigovian taxes or subsidies; for instance, a tax such as a specific levy for each amount of pollution produced is a Pigovian tax. Firms are free to choose how, or if, they wish to reduce their pollution, and policy makers, by setting the tax at different levels, can control how rewarding it is for firms to pursue pollution reduction. Presumably, the tax would also generate revenue that can be used for environmental cleanup or to otherwise alleviate the social costs that remain and are still externalized. Unlike most other types of taxes and because they correct externalities, Pigovian taxes increase economic efficiency. Unlike command-and-control approaches, the tax structure also provides a set of incentives to continue pollution reductions, whereas the maximums permitted under command-and-control policies tend to also become the minimums.

Tradable pollution permits are another major market-based approach to reach socially optimal pollution levels. Under this approach, the government can decide on the amount of pollution that is permissible and then sell permits to emit the pollution. Firms in industries where alternatives to pollution are not available or are very costly will be more willing to pay for the permits than those firms in industries where pollution control is less costly. However, such market-based solutions may fail when there is no acceptable level of pollution or when the administrative costs are prohibitive, such as would be the case in levying a charge on consumers for individual vehicle emissions.

Information demands play a large role in the success or failure of most pollution control policies. Command-and-control approaches require policy makers to know what technologies are available for industries and to have detailed knowledge of the firm and its costs and activities. Often this information is difficult to obtain. Pigovian taxes have fewer knowledge requirements, but the taxing authorities must know the market demand for the firms to correctly set the taxes at a rate that will result in the optimal output level being reached. Tradable pollution permits have the lowest information requirements in that an output level is chosen and the market then allocates the ability to pollute where it is of greatest value.

All approaches to the socially efficient regulation of pollution externalities are limited by the difficulty of determining what the socially optimal or economically efficient level of pollution output should be. Policy makers, much like individual firms in the market, will seek to equate the marginal benefits of pollution control with the marginal costs of that control. However, determining the marginal benefits of additional pollution control can be difficult, if not impossible. Measurement of the marginal costs of pollution control can be extremely difficult, even under market-based approaches, where the impact of any costs will not be uniform across producers, industries, or geographic regions. Under any approach, the affected profit-maximizing firms will seek to pass on the additional costs of pollution control to consumers, and their ability to do so will depend on how responsive consumers and other economic agents are to price changes. Similarly, different groups or types of consumers are likely to be affected differently by any increased pollution control costs a firm is able to pass on. As a result of these sorts of challenges, it can be very difficult for policy makers to determine the optimal level of pollution that yields economically and socially efficient outcomes.

—James E. Roper and David M. Zin

See also Coase Theorem; Competition; Economic Efficiency; Emissions Trading; Equilibrium; Externalities; Information Costs; Market Failure; Monopolies, Duopolies, and Oligopolies; Pollution; Pollution Right; Social Costs; Social Efficiency; Transaction Costs

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POLLUTION RIGHT

Polluting, or contaminating, the environment is widely recognized as an undesirable by-product of both good and bad activities. For instance, animal waste in a stream could be an undesirable effect of the desirable activity of raising cattle. Similarly, the production of power in power plants is a beneficial and necessary activity, yet such plants emit significant amounts of the pollutants sulfur dioxide, nitrogen oxides, carbon dioxide, and mercury. Many industries emit harmful products and gases into the environment, all of which are either man-made or facilitated products of manufacturing. Barring a technological miracle, a certain amount of pollutants in the environment is a necessary evil in many activities.

The fact that pollutants are viewed as an acceptable by-product of certain activities that are desirable to the economy gives rise to the precept that, at least to a certain degree, people have a right to pollute. Understandably, many individuals and groups concerned with the environment seek to limit that right. Some of the many issues related to the right to pollute are the following: To what degree is pollution acceptable? What kinds of pollution are tolerable? and What are the means for limiting such pollution?

Federal and state governments have attempted to provide answers to these questions, in part, by setting limits on the amount of pollutant emissions that companies may acceptably produce and levying fines against those companies that are out of compliance with such levels or even types of pollutants. For example, federal legislation provides that a power plant be allowed to emit a certain level of sulfur dioxide. Legislation also provides that credits for the right to pollute be distributed at no cost to power companies. All pollution emitted by the power companies reduces their allocation of pollution credits. If a company successfully reduces its emissions to amounts below the prescribed allowable levels, the remaining credits can be banked for later use by the company in its existing or potentially expanded operations. Alternatively, such pollution credits may be traded, or sold, to other companies that are still exceeding the required maximum emission levels under the federal statute, thus enabling such businesses to continue in existence rather than allowing regulation to result in their closure. These marketable pollution rights allow businesses to sell the right to pollute to one another.

Although the right to pollute is thus legally traded, the question of the ethics of such trading confronts society on many levels. Research claims that more African Americans than whites live near power plants, thus exposing them to greater pollution risks. The fact that power plants are allowed to purchase the right to pollute means that such a right may affect African Americans at a greater rate than whites, leading to allegations of discrimination against such a right. Pollution rights given to businesses enable industry to cut the costs of polluting, but it is arguable whether the sale of pollution rights results in any significant decrease in pollution overall. The caps on emissions themselves are the vehicle designed to decrease pollution. However, if a plant is emitting pollutants at a greater level than the cap allows, significant fines can be avoided by purchasing the right to pollute in excess of such a level at a lower cost to the business than the potential fine. This situation encourages the economic growth of industry but may not have the desired effect on the overall reduction of pollution levels, at least in certain areas.

—Mary Ellen Wells

See also Emissions Trading; Environmental Ethics; Environmental Protection Legislation and Regulation; Pollution; Public Utilities and Their Regulation

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Ponzi Scheme

A Ponzi scheme is a variant of the centuries-old fraud popularly known as "robbing Peter to pay Paul," which requires luring an initial group of gullible investors by offering them an improbably high return on their money, presumably made possible by investing their funds in a superbly profitable business venture. In reality, this great enterprise is either nonexistent or is merely a front, and the initial investors are actually paid with the funds provided by a second group of investors. These, in turn, are paid with the funds provided by a third group, and so on. The term *Ponzi scheme* is now used generically to describe all such swindles.

This type of fraudulent scheme takes its name from the Italian immigrant Charles Ponzi (1882–1949), who in 1920 promised a 50% profit in 45 days to investors in his newly created firm, the Securities Exchange Company. This generous offer implies an annual rate of return exceeding 2,500%, whereas banking interest rates at the time hovered around 5% per annum. The company's ostensible goal was to use those funds to profit from the even more fabulous arbitrage opportunities available by trading in international reply coupons. Each coupon was redeemable for a postage stamp in more than 60 countries belonging to the Universal Postal Union and, thus, effectively functioned as postal currency.

The geographical arbitrage Ponzi claimed to exploit sprang from the fact that the purchase price of a postal coupon differed across countries, after adjusting for currency exchange rates. Ponzi's company allegedly profited from these price disparities by purchasing international reply coupons in a country where they were cheap, exchanging them for stamps in a country where the coupons were expensive, and selling the stamps for cash.

The final step of this arbitrage cycle was the hardest to execute, and Ponzi never revealed how he managed to cash the stamps, saying only that the cashing mechanism was "his secret." Furthermore, analysts noted that the necessarily small value of each coupon meant that Ponzi's company could only profit by purchasing an inordinately large number of them, far in excess of the relatively meager worldwide supply required for purely postal transactions. These and other contemporaneous objections did not deter the swarm of mostly small investors eager to exchange their hard-earned money for "Ponzi notes" issued by the Securities Exchange Company. Indeed, in less than 1 year, more than 30,000 individuals invested a total of nearly $10 million in the fledgling enterprise.

Alas, the arbitrage cycle described by Ponzi was just a ruse. In August 1920, Ponzi's scheme unraveled after the press revealed that Ponzi had served jail time in both Canada and the United States. As a result, the flow of fresh funds came to an abrupt halt, the Securities Exchange Company could no longer meet its financial obligations, and Ponzi was tried and convicted for fraud. After spending several years in jail, Ponzi was deported to Italy in 1934. He later went to Brazil, where he died penniless.

—Ricardo J. Rodriguez

See also Arbitrage; Fraud

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Population Growth

According to the *United Nations,* the demography of world population will change dramatically in the near future. The changes will have a major impact on the economies and lifestyles of societies, particularly in industrialized nations, which may lead to the redistribution of global power and wealth. A brief history of population growth is first discussed and analyzed, followed by an analysis of consequences of the new demographic challenges of aging populations and varied birthrates throughout the world.

Population Growth

At the onset of the 21st century, a population explosion seems to be the biggest challenge of the years ahead. The long hours of morning and evening commutes, traffic jams, environmental pollution, the growing competition for parking spaces in malls during holiday seasons, and many other nuisances of our everyday life are making us realize that our planet is getting crowded. Furthermore, starvation in many parts of the world due to inadequate food supplies, residents living in areas prone to flooding, wars waged over scarce resources, illnesses, and so on, are other constant reminders of a burgeoning population, particularly in the developing world. But how fast is the population really growing? Should we be concerned? Will our children's lives be affected by it?

A review of history will reveal the true nature of population growth throughout the globe. During the first millennium, humans survived with minimal population growth. According to the demographer Massimo Livi-Bacci, from the University of Florence, the estimated growth rate of the world's population from CE 1 to 1750 was just 0.064% per year. The total world population in 1750 was less than 800 million. The life expectancy remained the same, at about 25 years, between the years 500 and 1750. Later in that century, infant mortality rates fell significantly, primarily because of improved pediatric care and better hygienic living conditions. This led to rapid population growth, especially in the European countries. The growing population of the poor and middle classes demanded a greater share of wealth, thus leading to the revolutions in Britain and France and ending monarchic rule in both countries during the 19th century.

The fast growth in population during the 18th and 19th centuries made the leaders of the European societies concerned about maintaining the balance between the human population and the availability of natural resources. A famous demographer and political economist during that period, Thomas Malthus, discussed the fate of humankind in his *Essay on the Principle of Population* in 1798. He famously predicted that because of the limited land on earth, food production in the world would not be able to keep up with the geometric growth rate of the human population. He did not, however, foresee the coming of the Industrial Revolution, which dramatically changed everything from food production to the standard of living in the next two centuries.

The Industrial Revolution started slowly in Europe but quickly gained momentum. By the late 19th century, people in Western Europe and North America were enjoying the prosperity brought to them by new technologies. The population growth enhanced technological progress, especially in medical science and practice. At the same time, the abundance of food, energy, and other useful goods and the efficiency of distribution of all commodities in these societies resulted in population growth in these parts of the world. Human consumption per capita also increased at a faster pace than ever imagined. Arts and science flourished in this century, resulting in a better lifestyle for humankind.

Though most of the innovations and industrialization processes started in the European countries and the United States, they were gradually diffused throughout the European colonies, located in different parts of the world. The life spans of people started to increase due to better food supply and improved social hygiene and public sanitation by the end of the 19th century. Even though we have had natural disasters and wars, the world population has increased sharply since 1900, according to UN estimates. The graph in Figure 1 indicates the nature of population growth since the beginning of civilization. It shows how world population more than doubled during the last half of the 20th century.

According to the latest UN estimate, if growth continues at the current pace, the world population will reach 11 billion by the end of 2050. Yet many

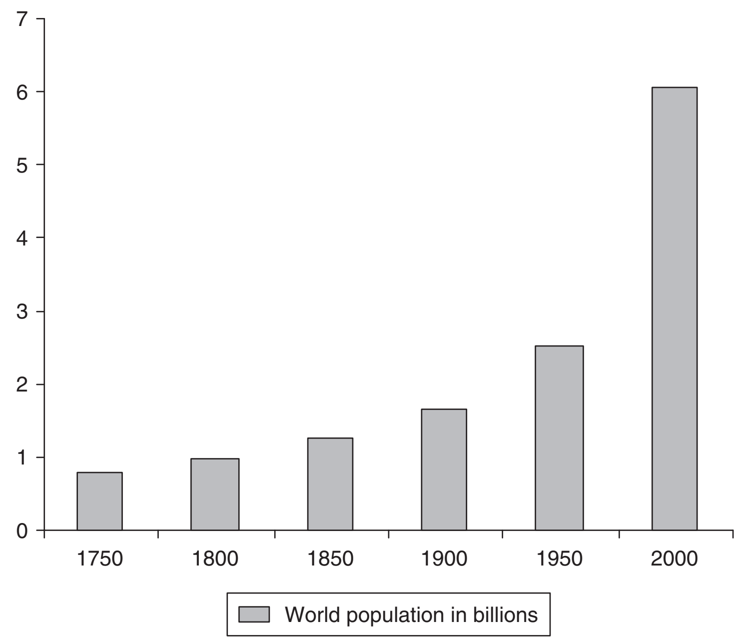

Figure 1 World Population Growth Between 1750 and 2000

Source: United Nations Population Division.

demographers have noticed that growth rates are not staying the same but are declining, particularly in most industrialized nations. Thus, the future population growth in many parts of the world remains uncertain.

Analysis of Population Growth Rates

As noted before, while the world population has been growing over the years, the population growth rate has been declining in most regions, particularly in the developed world. It reached its peak at 2% in the 1960s and had declined to 1.2% by 2005. According to the 2005 UN report, without any significant change in current trends, particularly in most regions of the developed world, population growth will slow down and eventually stop, and then the population will start declining. It has been projected that the world population will level off at just above 10 billion by the year 2200 before it starts declining. Many developed countries—for instance, Japan and Italy—already have zero growth rates, and Germany and Russia have negative growth rates. The United States is still able to maintain a growth rate of 0.91, compared with Canada and Great Britain at 0.88 and 0.28, respectively.

The main reason behind such low growth rates is the drop in fertility rates throughout the world. Most nations are unable to meet the minimum required fertility rate of 2.1 children per woman. Many developed countries, such as the United Kingdom (1.66), Germany (1.39), Italy, Spain, and Russia (1.28), Japan (1.4), Turkey (1.92), Canada (1.61), and Australia (1.76), are all below the fertility replacement level. The United States is one of the few industrialized nations that is still able to maintain the minimum required fertility rate of 2.1. The two most populous countries in the world, China and India, have current fertility rates at 1.73 and 2.73, respectively. In contrast, many countries in Africa and parts of Asia and the Middle East have maintained high fertility rates—for instance, Afghanistan (6.69), Bangladesh (3.11), Ethiopia (5.22), Nigeria (5.49), Pakistan (4.0), Saudi Arabia (4.0), and Yemen (6.58). This may result in a new demography in the coming years, with higher and younger population densities in these parts of the world. Nevertheless, the average fertility rate for the world today is 2.59, a little above the replacement level.

Some of the probable causes for this worldwide reduction of fertility rates are the rise of urbanization, feminism, female education and participation in the workplace, social and government policies for population control in developing countries, the availability of contraception and the legalization of abortion, and the rising cost of raising children. Also, reduced infant mortality indirectly is causing fertility rates to fall. A range of lifestyle and environmental factors such as smoking, alcohol consumption, and exposure to chemicals can also affect a couple's fertility, especially for women. Epidemics such as AIDS have also had a devastating effect on population growth in many areas. Women with the HIV virus have lower fertility rates than do women without it. In some Asian countries, governmental birth control policies and the use of modern medical technology for sex identification and abortion are resulting in a sudden increase of the male-to-female ratio. This is especially worrisome for countries with large populations, such as China and India. History has shown that higher male-to-female ratios have resulted in increased violence in such societies.

Coping With Depopulation

Nations with fertility rates below replacement levels are trying different ways to improve their situations. Russia is planning to adopt a 10-year program that will encourage women to have children by providing them with financial incentives and subsidies. Australia is offering a $4,000 tax-free bonus for every baby and is also committed to pay all child care costs for women who want to work. Many of the developed countries (e.g., France, Italy, Poland, and Japan) have offered some combination of bonuses and monthly payments to families. Singapore spends $3,000 for the first child, $9,000 for the second child, and up to $18,000 each for the third and fourth children.

Immigration is another option for these countries, which they are considering with caution. Japan, Russia, Germany, France, Singapore, and other countries recently have liberalized their strict anti-immigration laws in response to their acute population implosion problem. At the same time, these nations are afraid of losing their identity by bringing in an influx of immigrants. Also, changes in their societies are needed to encourage and welcome immigrants. According to the UN population report, there is a growing interest among governments, civil society, the private sector, and others in capitalizing on the benefits and minimizing the negative consequences of migration.

The United States is the largest industrialized economy of the world that is still able to maintain its fertility rate at the minimum replacement rate of 2.1. The United States ranks third after China and India on current population count, and it is projected to stay in third place after India and China in 2050. Part of its success in maintaining a modest growth in population is due to its liberal immigration policy, which accounts for 40% of its population growth annually, up from 24% in the 1980s. Where many countries are fearful of losing their identity, diversity in population has been promoted as the unique identity for this nation.

Aging Nations

Life expectancies of the world's peoples have grown more over the last half century than in the previous 5,000 years, mostly due to the reduction in infant mortality rates, improvements in lifestyles, and the excellence of modern medical systems. Even the developing and underdeveloped countries are able to save their infants and children from many life-threatening diseases by providing vaccinations on their own or with the help of the United Nations. Currently, only 12% of the population throughout the globe is over age 65, but this is projected to reach close to 21% by 2050. Most of the European nations and Japan are already facing a faster increase in the number of retirees than in the number of new workers in industry. China will experience one of the fastest aging populations during this generation, making it older on average than the United States by 2015.

As per the prediction of the United Nations, the median age of the world population will rise from 26.4 today to 36.8 in 2050. More precisely, the median age will be 45.2 years in developed nations and 35.7 years in less developed nations. Currently, Japan has the oldest population, with a median age of 41.3 years. People age 80 and older are the fastest-growing segment of the population in this century.

The graying of its population poses a serious threat to any nation's economy. In all industrialized societies, working adults are providing for underage and retired nonworking populations. The public pension systems, similar to the social security systems in the United States, support the elderly when they reach their retirement age. This would probably work in the long run if the population of new workers and retirees remained the same. However, the enormous increase of retirees and the severe reduction in the working population will strain the tax burden of working adults over the next decade, since the latter are contributing to the social security system through payroll taxes.

Also, providing health care for the aged population will cost nations dearly. In the United States, people over 65 years of age, roughly 12% of the current population, are consuming 38% of all health care costs. With rising health care costs and the increase in the older population, governments of these aging nations will have to decide whether to reduce the promised pension and medical care benefits or increase payroll taxes on the shrinking numbers of workers. Providing the necessary benefits to the elderly without compromising the working adults' financial status poses a challenge to our political leaders and to our society.

Most developing and underdeveloped countries are without established government programs for financial and health benefits for the elderly, who will face a more difficult challenge. For example, populous countries such as China and India will have a huge population of elderly people in the near future with neither any government benefits nor any personal savings. Moreover, the working adults in these countries are continuously migrating toward the mega cities, leaving their old relatives behind without any financial or medical help. Another drawback of aging nations is the short supply of creativity and innovation. Studies have shown that these qualities flourish in people of younger ages. The nations with higher median age will lose their competence in these sectors.

However, there are some positive outcomes in countries with an aging population. These countries will see a substantial reduction in their crime rates. New business options such as asset management, health care, cosmetics, plastic surgery, exercise training and equipment, and so on, will be created to cater to the needs of the vast elderly population. Marketers and media will continue to create a whole new set of products targeting these senior citizens.

New Demography Equals New Challenges

The combination of reduced fertility rates and the fast growth of the aging population has a tremendous effect on a nation's economic, military, and geopolitical situations. The declining labor force will result in reduced gross domestic product (GDP) growth, which has been projected to be 0.5% to 1% per year between 2010 and 2030. According to a study by the McKinsey Global Institute, the household financial wealth of the top two European nations, Germany and the United Kingdom, will decrease 25% and 34% in the next 20 years. The slowdown in savings and accumulation of financial assets in Europe's wealthiest countries could deter economic growth severely.

Military forces of today's powerful and wealthy nations will experience major changes in their internal and external security systems. Military expenses might be curtailed to pay for the needs of the ever-growing aging population. Also, reduced numbers of youths may result in smaller armies. Reductions in police forces could encourage *more* criminal and terrorist activities in the world. Nations will have to choose among a limited number of young adults and decide whether to send them to the military and police forces or keep them working in industry.

Governments will have to find new strategies to control their budget deficits, keeping taxes low for the working population and at the same time providing for the needs of retired people, and keeping their countries secured internally and as well as in the global arena. Since population density will increase in developing and underdeveloped countries, global powers among the nations will be redistributed depending on the economic and military strength of the nations. At the same time, these countries with higher populations will also have to struggle with ethical issues such as alleviating hunger for the poorer classes, putting the brakes on the overcrowding of cities, and eradicating contagious diseases, among other things. Bridging the gap between the haves and the have-nots will be one of the most pressing problems for governments in these regions.

The forecasted recent population growth followed by future population decline presents a multifaceted challenge for our generation. The uncertainty and challenges of the future demographic mosaic portend an unclear and doubtful future. The result might be a redistribution of global power and an increased interest on the part of national governments in implementing effective economic, humanitarian, and environmental policies as well as evaluating their ethical and practical implications.

—Mousumi Roy

See also Age Discrimination; Agribusiness; Birth Control; Bottom of the Pyramid; Civil Rights; Colonialism; Communitarianism; Economic Growth; Environmentalism; Equal Opportunity; Gender Inequality and Discrimination; Globalization; Gross Domestic Product (GDP); Human Capital; Human Nature; Immigration Policy; Income Distribution; Industrial Revolution; International Labour Organization (ILO); Natural Resources; Outsourcing; Pensions; Pollution; Poverty; Redistribution of Wealth; Sustainability; Trade Balance; Unemployment; United Nations; U.S. Bureau of the Census; Wealth Creation; Well-Being; Work and Family; World Health Organization (WHO); World Resources Institute (WRI); World Trade Organization (WTO)

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Pornography

Pornography can be defined as material whose primary purpose is to sexually arouse its consumer. It should be distinguished from material that is sexually explicit but does not have as its intention the arousal of the consumer (e.g., a medical textbook on human reproduction) and material that is not sexually explicit but may unintentionally arouse a consumer (e.g., an ad for shoes that appeals to a foot fetishist).

Because the term *pornography* is almost always used in the pejorative, the term *erotica* is often employed as an alternative for sexually suggestive material that is not degrading or dehumanizing. For instance, in an attempt to cast pornography in terms of harm rather than content for the purposes of legislation, Catharine MacKinnon and Andrea Dworkin define pornography specifically as graphic sexually explicit work that subordinates women through pictures and words. However, attempts to distinguish between "good" pornography and "bad" pornography often crash on the rocks of subjective taste; one person may find Rodin's *The Kiss* pornographic, and another may feel that Reage's *The Story of O* is a nice piece of erotica. The distinction between "hard-core" and "soft-core" pornography is likewise slippery, though the latter often indicates simulated sex and no images of genitalia.

Pornography is not a legal term. Instead, the courts use the term *obscenity* to refer to material that falls outside the protection of the First Amendment. What qualifies as obscenity is determined by a three-part test: An average citizen applying community standards would find that the work appeals to prurient interest; the work depicts, in a patently offensive way, sexual conduct as specifically defined by the applicable state law; and the work taken as a whole lacks serious literary, artistic, political, or scientific value. Despite this test, it is easy to sympathize with Justice Potter Stewart's famous comment that despite his own doubt that he could succeed in intelligibly defining pornography, he knows it when he sees it. Definitions that depend on community standards encounter a problem when public proclamations and private behavior do not coincide. When, for instance, the percentage of homes that order pay-per-view pornography greatly outweighs the percentage of those who claim to favor a total ban on pornography, a decision must be made whether a community standard is defined by what people profess to believe or by their actual behavior.

Another issue in the definition of pornography is its medium of presentation. Photographic and filmic images are generally considered of a different order than written pornography, because of the mass extent of their distribution and exhibition, because of the profilmic reality of actual bodies and activities, and finally because the sense of reality that photography-based images convey makes them more likely to be accepted as reality and thus to influence social behavior. The advent of computer technology has greatly eased and expanded the transmission of pornography. The use of company computers by employees to find and view pornographic material has become one of the primary arguments for monitoring computer activity in the workplace in recent privacy disputes. Computers have also introduced a new class of images—namely, digital illustrations that have the appearance of photographs. Such "virtual pornography" has been at the center of recent court cases that hinge on photorealistic, sexually explicit images of children that were not created using actual children.

Despite its air of disrepute, the pornography industry is a multi-billion-dollar business. Although the actual distinction might seem slight, there is an enormous difference in public presentation between companies that produce pornography and those that merely distribute it. Hotel chains, for instance, make millions of dollars from selling pay-per-view access to pornographic films yet do not brand themselves as part of the adult-entertainment industry. Certainly, it raises eyebrows when a company refuses to publicly discuss a service that makes up a significant portion of its revenue stream. Some socially responsible investment funds, primarily Christian but also feminist, make a point of not holding stock in such companies.

Market forces seem to have the effect of simultaneously encouraging both less tasteful and more tasteful content. Some argue that the consumption of pornography follows an escalating curve, as a user becomes desensitized to certain content and seeks out more extreme forms. Such a pattern encourages producers to continually top themselves by pushing the boundary of the acceptable. At the same time, the identification of women and couples as an untapped and growing market for pornography has resulted in attempts to create more tasteful forms of pornography, such as films with more narrative content and less fascination with anatomy.

Pornography and Harm

Discussions about the harmful effects of pornography usually focus on its consumption, but a case can be made for the deleterious effects on those involved in its production, such as the abuse of children that results from the creation of child pornography. The coercion of female performers can be explicit or may take subtler forms, such as the lack of economic options for women. Recently, emphasis has been placed on the health risks to performers, in particular exposure to the HIV virus. But these arguments can play into the hands of the defenders of pornography; greater public acceptance of pornography as a conventional business might result in greater self-regulation, including greater worker protection. With regard to public safety, pornography can be lumped with alcohol, prostitution, the drug trade, and gambling. Given the impossibility of completely uprooting such vices, some argue that it would be better to raise them out of their *demimonde* status so that they could be properly regulated by state, union, and market forces. A full legalization of various forms of sex work removes the surrounding criminal infrastructures and might better ensure the well-being of both producers and consumers.

Such arguments must take into account, however, the effects of pornography on consumers and society. The most serious and the most contested link between pornography and behavior is rape. Among those who argue for such a link, there is some disagreement about the definition of pornography. Some argue that pornography that includes violent content belongs to a special class, whereas other commentators argue that it is merely a difference in degree rather than kind. The depiction of women as objects of violence is merely a logical extension of the depiction of women as endlessly available sexual objects in "nonviolent" pornography, and both lead to the same result. The exact definition of "violent" and "degrading" pornography has also been thrown into question by the case of lesbian-produced sadomasochistic pornography, material the defenders of which say is an expression of a consensual, positive subculture despite its outward similarity to humiliating images in heterosexual pornography.

In any case, a definitive link between rape and pornography is difficult to either prove or disprove. Both detractors and defenders of pornography too often fall back on anecdotes and speculation rather than scientific certitude. While there is no reason to doubt the sincerity of antiporn feminists, there are those in the procensorship camp who have seemingly used the threat to women as a red herring. According to some activists, the 1992 Canadian Supreme Court decision that redefined obscenity explicitly to protect women from pornography's harmful effects was subsequently used by customs agents to specifically target gay and lesbian pornography, work that either didn't feature women at all or was produced by and for women.

But even if the link between pornography and nonconsensual sex is impossible to prove, other consequences must be considered. Acts of violence toward women, such as rape, are just the far end of a continuum of negative behavior toward women that may be caused in part by pornography. A full accounting of pornography would have to take up a much broader conception of public good, one that would include more intangible elements, such as women's self-image, gender equality, and the quality of relations between men and women. Such an account would have to include the relatively new concept of "pornography addiction," which places this product in the same class as cigarettes, alcohol, and gambling. The possibility that their products are potentially addictive, even if in just a small minority of users, raises special ethical concerns for companies involved in the production and distribution of pornography. A perhaps more immediately tangible harm can be seen in the effects of pornography distribution in particular neighborhoods. Zoning laws cite public good in regulating where sex shops and strip clubs can be located. Such legislation, however, must take into consideration the fact that such laws have the effect of protecting one area at the expense of another.

Another major concern is the potential direct and indirect effects of pornography, a product designed exclusively for adults, on children. The issue of children's exposure has come to the fore with the ease of access to pornography on the Internet, where the general anonymity of computer users makes it difficult to offer content to some and restrict it from others. An extreme case is the anecdotal evidence that sex offenders use pornography to entice minors into performing sexual acts. Some studies claim that the age of exposure to pornography correlates with the age of first sexual activity. But given the inconclusiveness of the debate surrounding the effects of violence in the media on children's behavior, it is unlikely that there will soon be any definitive evidence of the harmful effects on children of exposure to adult material.

Moreover, it is not surprising to note the changing standards of what constitutes a negative effect. For instance, earlier studies of pornography repeatedly decry the fact that it causes deviant behavior such as homosexuality, an argument that today lacks force when a substantial portion of the public no longer believes that homosexuality is either "caused" or "deviant." Indeed, there are those who argue that pornography not only is harmless but also has generally beneficial effects. One rather crude argument is that pornography can function as a form of "safety valve," allowing for a safe release of sexual pressures that might otherwise lead to antisocial behavior. Some propornography feminists argue that both the production and the consumption of pornography by women is a step in reclaiming their sexuality. Sexual minorities can point to pornography as a realm that validates their sexual identity and behaviors in the face of a disapproving culture. Defenders of pornography also argue that excessive censorship will have a general chilling effect on free speech. Such a position may concede that pornography results in concrete harms but asserts that they are outweighed by the potential harms of restricting free expression.

—Clark Farmer

See also Feminist Ethics; Feminist Theory; Gender Inequality and Discrimination; Internet and Computing Legislation; Socially Responsible Investing (SRI)

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Positive Economics

Economists have long subdivided their discipline into two branches: positive economics and welfare economics. Positive economics aims to be scientifically descriptive (what is) and predictive (what will be) of objective facts. While positive economics emphasizes a purely scientific methodology, whether any social scientist can be truly unbiased with respect to facts or values is open to serious question. This approach to economics invokes the positivism associated with the French sociologist Auguste Comte (1798–1857). Comte advocated the application to social studies of the methodology of observation and experimentation then developing in the natural sciences (e.g., physics and chemistry). For Comte, positivism was the third and final stage of human reasoning, succeeding the previous metaphysical and theological stages for explaining causality (i.e., why reality is the way it is). The positive economist functions as a scientist studying phenomena; but human behavior is not necessarily subject to something analogous to the fixed physical laws of nature. This purely scientific approach to human behavior applies often unrealistic assumptions to predict long-term outcomes such as unemployment trends or equilibrium between supply and demand and neglects to include descriptive measures of the short-term consequences borne by real people, who may suffer unemployment or shortages of housing and health care. The purely scientific approach deliberately eschews subjective value judgments, regarded as strictly the province of welfare economics. Positive economics is thus unable to address ethical dilemmas. These two limitations of positive economics are addressed below.

The Is-Ought Distinction in Economics

The two branches of economics closely parallel the is-ought (or descriptive-normative) distinction in ethics. This fact-value distinction is of long standing in economic literature. Positive economics came from a conscious decision to simplify the problem of economic analysis. The social and moral sciences deal with very complex considerations. To enable more rapid progress of knowledge, social scientists in the 19th century decided to divide the scope of political economy (as economics was then called) into two branches with different methodologies. A normative branch would focus on policy making for a moral society and public welfare. A separate, positive science would describe the workings of the economic system as it is.

Positive economics adopts a strongly consequentialist perspective in the spirit of utilitarianism. This orientation can be illustrated by examples at the microeconomic and macroeconomic levels of analysis. Microeconomics studies choices by individuals, households, firms, and governments. At the microeconomic level of analysis, positive economics describes and predicts, for example, how changes in specific prices or taxes will affect human choices. A regressive tax affects less wealthy households more than it affects wealthier households. A positive analysis might conclude that a regressive tax is relatively efficient or inefficient in acquiring private resources for public activities. Positive economics studies the causes and effects of horizontal mergers among producers in markets for goods and services. A positive analysis might conclude that a specific horizontal merger will reduce consumer welfare. A positive analysis might conclude that the global expansion of Wal-Mart increases the welfare of consumers and investors while decreasing the welfare of its employees, suppliers, and competitors.

Macroeconomics studies the aggregate results of microlevel choices by multiple decision-making units. At the macroeconomic level of analysis, positive economics describes and predicts, for example, the relationship among wages, unemployment, and price inflation. Edmund Phelps received the 2006 Nobel Memorial Prize in Economic Science (this title reflects the positivist tradition) for an explanation of this relationship. According to Phelps's explanation, wages and prices rise together, pushing one another, until the unemployment rate reaches an equilibrium (or natural rate), at which point inflation halts. This process of interaction involves what economists term rational expectations. Both workers and managers have to form changing expectations about the current and future state-conditions of the world, and they do so with incomplete information. Rational expectations are at best guesses about future equilibrium conditions; in principle, rational expectations should be the same as economic theory predictions.

Developmental History of Positive Economics

In a general sense, all the currently important approaches to economic inquiry adopt a basically scientific orientation. Karl Marx (1818–1883) claimed to have discovered the scientific laws of capitalist development, ending in socialism as the final stage of economic history. The Austrian School of Economics evolved in the later 19th century as a methodological criticism of the historicist school in Germany and England. The historicist school used historical data to test its theories. Responding in part to Marx, the historicists argued that the so-called economic laws being developed by the English classical economists (Adam Smith and his 19th-century successors) are highly dependent on specific historical and sociological contexts. This historicist school informed American Institutionalism, which similarly stressed that the interactions among historical and sociological factors helped shape institutions such as governments and markets. The econometrics favored by positivists is simply statistical analysis of historical data. The Austrian School—including the Austrian-born economists Ludwig von Mises (1881–1973) and Friedrich Hayek (1889–1992), winner of the 1974 Nobel Memorial Prize—later emphasized criticism of both socialist central planning and neoclassical mainstream economics. The Austrian-born economist Joseph Schumpeter (1883–1950), who emigrated to the United States, served as a bridge between the Austrian and neoclassical approaches. The significance of the Austrian School for positive economics is in the thinking that economics is best understood at the level of individuals making subjective decisions within the conditions of their local context. Therefore, positivists must clearly explain the logic that links descriptive models and measures to individual decision making and why purely backward-looking analyses of historical data, as studied through econometrics, are useful descriptions of the current contexts in which individuals make their decisions.

Mainstream economics since the last quarter of the 19th century has been neoclassical economics. This mainstream approach was initially synthesized from a combination of the classical and the Austrian approaches by Alfred Marshall (1842–1924) in his 1890 book, *Principles of Economics.* Positivism, as a specific view of scientific methodology, dominates this mainstream neoclassical approach. Milton Friedman, recipient of the 1976 Nobel Memorial Prize for his work on the quantity theory of money, is a well-known modern representative of this mainstream economic tradition of positivism.

Adam Smith emphasized the invisible hand efficiency of the relatively free market mechanism; and this efficiency approach to resource allocation theory dominates modern neoclassical economics and its positivist methodology. The so-called Socialist Calculation Debate occurred from the turn of the 20th century through at least the 1930s. The essence of the debate was whether government central planning in a socialist economy could perform as well as, or perhaps even better than, a laissez-faire market economy. Markets involve various defects such as externalities, monopoly power, and public goods. Central planning might adequately mimic the general equilibrium outcomes of the ideal decentralized market system. A necessary condition would be that government planners calculate and use the prices of a competitive market economy. This theory of central planning led to the development of mathematical programming techniques for computing such prices. Ludwig von Mises and Friedrich Hayek argued that central planning would not be sufficient to duplicate the complex information and incentive advantages of the market economy. The implications of this debate, especially in light of the collapse of the Soviet-style planned economies in the 1990s, is that the development of positive economics has progressed to the certainty that scientifically useful observations and descriptions are those that can be clearly related to the price information people use to make economic decisions.

The Methodology of Positive Economics

Marshall described economics, beyond the classical conception of markets, as the study of human choice or decision making in everyday life. He emphasized that economics is a logically rigorous approach to reasoning about human choice. The scope of positive economic inquiry has thus steadily broadened. Gary S. Becker, the 1992 Nobel Memorial Prize winner, extended microeconomics to the study of traditionally sociological subjects such as the family, crime and punishment, and discrimination in the markets. In his 1992 Nobel lecture, Becker emphasized that economics is essentially a way of looking at life. This emphasis on logical reasoning defines positive economics as a scientific methodology. As noted earlier, however, positive economics tends to invoke highly unrealistic assumptions in order to derive long-term predictions, such as unemployment trends or equilibrium between supply and demand, and to neglect the short-term effects on real people, who may suffer unemployment or shortages of housing and health care. For example, neoclassical economists may talk about the advantages of competitive markets, whereas real markets have important monopoly elements. This tendency arises with the conscious use of simplified, abstract analysis to focus on the essential logic of choice.

Logic and behavior may be different. In 1953, Milton Friedman published an influential and widely critiqued paper arguing that the empirical realism of economic model assumptions is largely irrelevant in theory development. Any primitive assumption (or intuition) is acceptable if the deductive implications prove to be empirically valid for the purpose of predicting behavior and outcomes. Indeed, the more unrealistic the assumptions, the easier the construction of a theoretical model for testing. Economic theories have purely instrumental value in terms of generating testable predictions. It has been suggested that Friedman's views unevenly combine positivism, pragmatism, and realism and that, if anything, pragmatism is the dominant element.

Key elements of positive economics are methodological individualism (i.e., agent optimization), price theory, equilibrium, the use of mathematics, and the use of econometric hypothesis testing. Methodological individualism means that microeconomic analysis begins with assumptions about the optimizing choices and behavior of a representative actor (or agent). For example, a representative actor presumably prefers more wealth to less wealth, all other conditions being held constant (the *ceteris paribus* assumption, as expressed in Latin) for the purpose of this specific choice opportunity. Generally, all human actors behave the same as this representative actor. Price theory, pioneered by Marshall, explains how supply (i.e., marginal cost) and demand (i.e., marginal utility) jointly determine market prices. A market price is one type of economic equilibrium.

Positive economics is today strongly and increasingly mathematical in reasoning orientation, because mathematics can be readily applied to the analysis of logical choices. Marshall studied physics; and neoclassical economics arose as a conscious effort to be a physics of human choice. In the 20th century, this mathematical approach has increasingly emphasized the axiomatic method for studying general equilibrium, culminating in the Arrow-Debreu model. Economics has evolved from physics toward pure mathematics.

Over roughly the same period, econometrics has become increasingly important for statistical testing of empirical hypotheses derived from economic theorizing. For example, econometric methods might be used to test statistically whether raising teacher salaries improves student academic performance.

Rationality and Behavioral Economics

Positivism emphasizes a strong rationality assumption in modeling the choices of *Homo economicus* (economic man) that tends to equate the economic logic of choice with predicted and desirable human behavior. Rational choice equated with logic is, even under conditions of uncertainty, relatively easy to model. Gary Becker coauthored a pioneering 1988 article on whether addiction might be rational. Rationality means simply that an actor aims, in a general sense, at optimization in economic choices (i.e., agent optimization). A rational actor seeks less rather than more of an undesirable condition and more rather than less of a desirable condition. A firm generally attempts to minimize its costs and maximize its revenues. Cost is undesirable; revenue is desirable. This view, as developed further in the next section, tends to denigrate altruism and corporate social responsibility. Rationality simply asserts that actors are logical in their choices given some goal (or set of goals) and some resource (or set of resources). To the degree that human choices deviate from this rationality assumption, positivism can be misleading with respect to predictions and policy-making prescriptions.

Human choice and behavior may prove to be much more complicated and difficult to predict. For example, Adam Smith expected that as wealth increased, people would tend to be more sympathetic toward others. A behavioral revolution has occurred in economics over the past two decades. Behavioral economics investigates the empirical validity of the assumption of rationality and thus of the rational expectations theory mentioned earlier. Behavioral economics focuses on the possible interrelations between economics and psychology. Psychologists are concerned with understanding how emotion and cognition interact in forming preferences and making choices. A real person may have very inconsistent preferences and may make apparently conflicting choices. There are strong limits on information availability and human cognitive processing, which Herbert A. Simon (winner of the 1978 Nobel Memorial Prize) characterized as bounded rationality. Simon also argued that economic actors engage in satisficing rather than optimization: An actor stops searching for an optimum as soon as a satisfactory threshold is reached. For example, an actor may decide that 40 hours of work a week is sufficient, even though more wealth might be obtained by working more hours. Considerations of values and ethics may be in reality very important to people in shaping their choices.

Andrei Shleifer developed behavioral finance as an alternative to efficient market theory. In 1999, Shleifer won the John Bates Clark medal of the American Economic Association, regarded as second only to the Nobel Memorial Prize. In his 2001 Nobel Memorial Prize lecture, George A. Akerlof argued that macroeconomics must be grounded in behavioral economics. Akerlof shared the prize with A. Michael Spence and Joseph E. Stiglitz for studies of the asymmetric information properties of markets. Asymmetric information means that one party has more valuable information than other parties, or thinks so. This reality or perception greatly shapes human choice and behavior. When managers withhold information from the other stakeholders of a corporation, or distort it, they are manipulating markets.

Positive economics is today making greater efforts to understand the realities of human choice and behavior. In 2002, the Nobel Memorial Prize was shared by the economist Vernon L. Smith and the psychologist Daniel Kahneman. Smith popularized the use of laboratory experiments for studying economic behavior. Kahneman, together with Amos Tversky (1937–1996), applied insights from psychology to economics. Much of their work concerns how heuristics and biases affect human judgment under conditions of uncertainty. They developed prospect theory to explain how individuals mentally account for gains and losses; loss aversion occurs because losses have a greater psychological impact than gains. Neoclassical economics assumes additive utility functions, whereas prospect theory suggests that an actor may compare gain or loss to some reference point. This difference in viewpoint has great implications for policy-making prescriptions.

Value-Free Economics in Relationship to Ethics

Positive economics treats value judgments as subjective and thus cannot address ethical dilemmas. In keeping with utilitarianism, one individual's preferences are as good as another person's preferences. In Pareto-efficient gains, such as voluntary market exchanges, at least one person's welfare improves without harming the welfare of any other person. In such gains, the value content of individual welfare functions is not relevant.

An important assumption in neoclassical economics is self-interest. Comte coined the term *altruism* to describe the regard for others as more important than self-interest. Comte believed that everyone had a responsibility for the general welfare. Adam Smith, in *The Theory of Moral Sentiments* (1759), defined citizenship in terms of obedience to laws and government authority and good citizenship in terms of such a concern for the general welfare.

Milton Friedman argued that the corporate social responsibility of businesses reduced to self-interested wealth seeking, although it is important to note that Friedman very clearly limited wealth seeking to behavior within the limits defined by laws and customary ethics. A key element in Friedman's argument was that any broader notion of corporate social responsibility is corporate altruism at the expense of the firm's key stakeholders. If the firm's managers practice such altruism, it is theft from the other key stakeholders and in the self-interest of the managers. If the owners of a publicly traded firm practice such altruism, it is in effect socialism undermining the proper role of government. This approach reduces corporate altruism to strategic philanthropy practiced for the self-interest of the firm. The owners of a privately held firm can do as they please, much like individuals.

Conclusion

Positivism is the approach to scientific methodology that lies at the intellectual core of mainstream neoclassical economics. The Austrian School of Economics and modern behavioral economics have sought in different ways to modify the impact of positivism on mainstream neoclassical economics. Positivism has both strengths and weaknesses. A methodological advantage is that positivism focuses economic analysis on the rational logic of human choice and the resulting predictions for the long-term functioning of markets. A marked disadvantage is that positivism tends to ignore the psychology of human behavior and the short-term effects and defects of markets. Most important, positivism eschews subjective value judgments and tends to denigrate altruism and corporate social responsibility. Business ethics addresses the importance of altruism and corporate social responsibility and the ethical dilemmas that positive economics cannot handle.

—Duane Windsor

See also Altruism; Arrow, Kenneth; Austrian School of Economics; Bounded Rationality; Capitalism; Chicago School of Economics; Consequentialist Ethical Systems; Consumer Sovereignty; Cost-Benefit Analysis; Development Economics; Economic Efficiency; Economics and Ethics; Economics of Well-Being (Post-Welfarist Economics); Efficient Markets, Theory of; Equilibrium; Externalities; Free Market; Friedman, Milton; Invisible Hand; Is-Ought Problem; Market Failure; Market Power; Methodological Individualism; Mixed Economy; Monopolies, Duopolies, and Oligopolies; Monopsony; Normative/Descriptive

Distinction; Opportunity Cost; Pareto Efficiency; Partial Equilibrium; Perfect Markets and Market Imperfections; Positivism; Property and Property Rights; Public Goods; Rational Choice Theory; Rationality; Rationality and Ethics; Regressive Tax; Self-Interest; Strategic Philanthropy; Supply-Side Economics; Utilitarianism; Wealth Creation; Welfare Economics

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Positivism

The term *positivism* can be traced back to Enlightenment thinkers such as Pierre Simon De Laplace and David Hume and was adopted by Auguste Comte in the 19th century to designate a philosophical movement which held that science is the only kind of valid knowledge and that empirical facts are the only possible objects or building blocks of knowledge. It held that humanistic areas such as ethics, politics, and religion would be meaningless unless they could become scientific disciplines. Logical positivism or logical empiricism, the dominant form of positivism usually viewed as coextensive with positivism in general, developed out of discussions held by the Vienna Circle, a group growing out of the analytical tradition and composed of Austrian and German philosophers, which began in the early 1920s. Equating knowledge in general with scientific knowledge, they denied the validity of traditional philosophical concerns with metaphysics, ethics, and epistemology. During the following decades many of the positivists moved to England and the United States, where they exerted an enormous influence. Positivism soon became the major framework for the philosophy of science and a powerful school of philosophy in general. While it no longer exists as a unified movement or school of philosophy, its ongoing influence is evidenced in the present widespread focus on issues relating to scientific thinking and developments in formal logic and in a concern with a particular type of rigor in various philosophies.

Positivism holds that there are only two sources of knowledge, logical reasoning and sense experience. Logical knowledge includes math, with math reducible to formal logic. Logical/mathematical truths are based on the rules of language, which are conventions, and thus are true independently of sense experience. They are not truths of some "higher order" or "higher realm of being" but are independent of sense experience only because they are empty of content. Empirical knowledge, whose truth is dependent on sense experience, is composed of scientific knowledge such as physics, biology, physiological psychology, and so forth.

The logical positivists' major points of focus were on what became known as the verifiability theory of meaning and its consequences, the structure of scientific theories, investigations into logic and mathematics, and the philosophy of language as a concern with the possibilities of an ideal logical language as a representation of reality.

Perhaps their most famous tenet was the verifiability theory of meaning, which held that the cognitive meaning of a statement is its method of verification. A statement is meaningful if and only if it can be shown to be true or false, at least in principle, through sense experience. Its meaning is reducible to, or is nothing more than, the sum of all conceivable observation experiences that would go to verify its truth.

Traditional metaphysics, which incorporates abstract speculation about the nature of reality, has no significance as it is not reducible to observation statements. Statements about the existence and nature of God or the absolute are meaningless, for example, as there is no set of observations that could conclusively verify or falsify their truth. Such knowledge claims are always more than, or beyond, any possible set of observation circumstances or statements.

Even traditional epistemology loses its significance unless it is reduced to the scientific descriptions offered by disciplines such as behavioral psychology or physiology. Claims about the external world are as meaningless as claims about metaphysical entities, as there is no possible way of verifying that an external world does or does not exist as a cause of our sensations. Thus, the differing understandings of the relation of the mind or thought to an external world are all equally meaningless.

Positivism resulted in noncognitivist theories of ethics. According to noncognitivism, moral claims do not assert moral facts, and the assertion of some "realm of values" beyond or above sense experience is senseless. Moral claims are neither confirmable nor disconfirmable; they cannot be shown to be true or false by observational means and so are devoid of cognitive content. While noncognitive theories can take numerous forms, the emotive theory became the more dominant one. According to this view, normative statements are not assertions of anything but are merely expressive of or appeals to human emotions. For example, to say "Stealing is wrong" either evinces our own emotions of disapproval concerning stealing or is a way of trying to influence others to feel that same way. Ethics should concern itself with the clarification of moral language, with the metaethical question of what moral terms mean. In ethics itself, the only viable philosophic endeavor is to catalog the various ways societies and their members express their feelings in moral language and analyze the role moral language plays in influencing human behavior.

While past philosophers had at times argued in one way or another that various assertions in the above areas of philosophy were useless or unprovable, the positivists went beyond that. Statements concerning these various issues are not just useless or unprovable but devoid of meaning, empty of cognitive content. It is literally senseless to either assert or deny them. The sole role of philosophy is to clarify and define the meaning of statements. Philosophical claims are about the way language is used, not about a world or realm beyond language.

The positivists were intensely concerned with clarifying the structure of scientific theories. Scientific theories are axiomatic systems in which "rules of correspondence" supply a correlation between the abstract concepts of theory and observations. A scientific theory is thus expressed in two types of language, observational and theoretical. According to this view, scientific investigation does not penetrate nature in a way the senses cannot, but rather, scientific investigation is the rigorous, economical organization of what is given to us in experience. And since what we have in experience are not objects "out there" but sensations, the goal of scientific investigation becomes that of discovering the relations between sensations. The construction of theoretical entities is useful in science, but these are not an attempt to get at some transphenomenal realities. Rather, they are learning devices or models. According to the positivist analysis of science, a theory is a hypothetico-deductive system, similar to a logical or a mathematical ordering. The issue of the predictive power of theories or the process by which theories are formed was seen as irrelevant. What is the object of concern is only the relationships between the theory and the empirical or observational evidence. Positivists were also interested in the development of what is called the unity of science, the view that all special sciences, such as biology, psychology, chemistry, and so forth, can be understood, ultimately, through the fundamental laws of physics. Their ultimate goal was the establishment of a unified language of science, with philosophy equivalent to the logic of science.

Positivism has had a big impact on legal theory. While the term *legal positivism* houses a variety of related tenets, they are all intertwined with the general view, which is commonly called the separability thesis, that there is no connection between legal validity and morality. Law and morality are conceptually distinct, and the concept of law must be entirely free of moral considerations.

Legal positivism usually takes the noncognitivist view that moral judgments—in this case, moral judgments made about human laws (their justice or injustice, goodness or badness)—are not claims about moral facts but are merely expressions of feelings or choices or commands. Legal positivism has led to debates concerning the issue of mandatory pro bono service as a duty of any officer of the court. Is this equivalent to the taking of property without just compensation?

The separability thesis in legal positivism is mirrored in the separation thesis in business ethics—namely, that the norms and practices of business and morality are conceptually distinct. The arguments concerning mandatory pro bono service are analogous to the arguments in business ethics concerning corporate social responsibility (CSR). Is there is any real moral issue attached to CSR, whether as a duty entailed by the nature of the corporation and corporate membership in relation to the larger society or as a demand that infringes on the property rights of shareholders?

Positivism accepts the fact-value distinction, denying the reality of value as normative because it is not reducible to the factual. Some contemporary positions, such as relational holism or emergentism, undercut the fact-value distinction in favor of empirical situations that are concretely rich, value-laden relational complexes in which both facts and values emerge as wedded dimensions of complex contexts that cannot be dissected into atomic bits. Such an approach does not reduce values to facts but rather understands empirical and normative business ethics as inquiries that focus on different dimensions of a concrete unified situation based on the two fields' differing contextual interests. Such a view provides a basis for interdependent shared problem domains, the intersubjective construction of meanings, and a general openness onto "the other." It provides a basis as well for a relational view of corporate citizenship within the complexes of community life and responsibilities and for stakeholder theory as providing an understanding of one type of commitment within these relational webs.

—Sandra B. Rosenthal

See also Fact-Value Distinction; Normative Theory Versus Positive Theory; Pragmatism; Reductionism; Social Contract Theory; Stakeholder Engagement

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POSTMODERNISM

Postmodernism refers to a wide range of eclectic thinking applied to art, architecture, fiction, literature, philosophy, and cultural and literary criticism, among other things. It is considered a reaction to the assumed certainty of scientific or objective attempts to explain reality. As such, postmodernism conflicts with explanations that claim to be universally valid—that is, for all cultures, groups, traditions, and ethnicities—and instead focuses on the relative truths for each person.

Modernity has its roots in Latin from the phrase *just now*. The Postmodern, then, literally means "after just now," or "after modernity." It refers to the appearance or actual dissolution of those social forms associated with modernity. Postmodern is "post" because it denies the existence of any ultimate principles, and it lacks the optimism of there being a scientific, philosophical, or religious universal truth, a characteristic of the modern mind. It is important to note, however, that postmodernism is a response to modernism—that is, the negation of or disbelief in the modern outlook—rather than simply an approach that arose after modernism. In many ways, the society we live in is still considered modern, not postmodern.

According to the postmodern theorist Jean-François Lyotard, the term represents a culmination of the process of modernity and enlightenment thought, toward speedy cultural change, to a state where constant change is the status quo, leaving the notion of progress contradictory. Postmodernism, thus, relies on concrete experience over abstract principles, always cognizant that the end result of one's experience will necessarily be fallible and relative rather than certain and universal. While modernism deals with purpose, design, hierarchy, distance, synthesis, centering, and presence, postmodernism is synonymous with play, chance, anarchy, participation, antithesis, dispersal, and absence. As a cultural movement, factors such as globalization, consumerism, the fragmentation of authority, and the commodification of knowledge have greatly contributed to the development of postmodernism.

History and Development

Ihab Hassan points out several instances when the term was used before postmodernism became a theoretical discipline in the 1970s. John Watkins Chapman, an English academic painter, used it in the late 1870s to mean postimpressionism, whereas Federico de Onis used it in 1934 to mean a reaction against the difficulty and experimentalism of modernist poetry. The eminent historian Arnold Toynbee used it in 1939 to mean the end of the "modern," Western bourgeois order dating back to the 17th century, while Bernard Smith, in 1945, referred to it to mean the movement of socialist realism in painting.

By the late 19th century, Soren Kierkegaard and Karl Barth's important fideist approach, or the view that religious knowledge depends on faith and lifestyle, brought irreverence to reason and the notion that "truth is subjectivity." Nietzsche introduced the concept of existentialism and injected a new nihilism and atheism that influenced culture. The early 20th century saw aspects of postmodernism arise with the emergence of the Dada movement, which focused on the framing of objects and discourse as being as important as, or more important than, the work itself.

Many philosophers during the mass postcolonialism period after World War II speculated that one could not have an objectively superior lifestyle or belief. This idea was further expounded by the antifoundationalist philosopher Heidegger, followed by Jacques Derrida, who reexamined the fundamentals of knowledge and deconstructionism. These philosophers broadly argued that rationality and logic were neither as certain nor as clear as the modernists or rationalists assert.

The main postmodernistic movement started in the late 20th century and is reflected in the social and philosophical realities of that period. Many, such as John Ralston Saul, have argued that postmodernism represents an accumulated disillusionment with the promises of the progress of science so central to modern thinking. Important books on postmodernism during this period include those by Jean-François Lyotard and Richard Rorty. Jean Baudrillard, Michel Foucault, and Roland Barthes are others who contributed strongly to the development of postmodern theory during this period.

Postmodernism and Business Ethics

Postmodern business ethics assumes that values and actions are determined without objective valuation grounds on a relative basis. Values both are born and die socially. There is no objective measure of value, and there is no need for it. Although many authors consider postmodernism synonymous with relativism, one should not make the mistake of viewing morality as a relative phenomenon with no universal basis. It is, however, a local and temporary custom, affected by the nuances of local or tribal histories and cultural inventions.

Advertising and other forms of promotional activities as well as entertainment communications such as movies have proliferated tremendously, and the lines between these promotional and media techniques have become increasingly blurred. For example, product placements are increasingly replacing advertising, while "video news releases" from private companies and the government are often assumed to be hard news. Media products in this era are characterized by relativism, cynicism, irony, and hedonism. These tumultuous changes have prompted professional marketing organizations to be concerned about the conduct of professionals with regard to law and the benchmarks for moral decency in human exchange relationships.

According to Stephen Brown, postmodern consumers, concurrently, have become more cynical, world-weary, self-obsessed, and hedonistic in their craving for instant gratification and their ever-increasing need for stimulation. Brown further notes that rather than relying on rational decision making, they are increasingly becoming victims of the fast pace of social and cultural change and the decline of absolute values of morality and entities without moral sensibilities or critical faculties.

Ronald Green argues that business ethics is postmodern because it rejects unitary or totalizing explanations of reality. He further states that this is so because the premise of postmodernism rejects the position that any single economic or social theory can address or eliminate the ongoing ethical problems of organizational and ethical life. Finally, business ethics shares postmodernism's decentering of perspective and the discovery of otherness, difference, and marginality as valid modes of approach to experience.

Andrew Gustafson summarizes four major characteristics of postmodern business ethics:

1. *Holism:* There should not be such a radical separation of personal and professional ethical behavior. One is always a human being, irrespective of whether one acts as a corporate agent or sometimes as a self-interested private agent. Thus, the same ethical litmus tests should apply for decision making on behalf of the family household as well as the business organization in which the individual is employed.
2. *No abstracted ethics in a vacuum:* Postmodern business ethicists rely on a narrative approach instead of an abstract theory. In other words, a postmodern ethic considers the entire worldview of a person and thinks of business as an integral part of the way one looks at all of life. Ethics proceeds by analogies rather than by strict principles alone, and narratives, rather than superficial rules, constitute the postmodern method. The focus of virtue ethical theories is more on being and character than on rules for action. The heroes and saints are viewed more holistically than by abstract detached principles.
3. *Suspicion of universal theories:* Postmodern business ethicists are more interested in coming up with local rules that can work and be agreed to than in attempting to create a universal system of ethics. Their primary focus is on building particular segments of consensus rather than on propounding "one-size-fits-any-situation" rules. For example, while Karl Marx and Sigmund Freud believed that "self-interest" plays a role in what we consider good or just, Derrida believed that we are primarily influenced by our linguistic conception of the world, while Socrates held the view that sheer ignorance was the primary reason behind having a deficient view of the truth. Thus, the postmodern approach accepts the various explanations regarding what is objective rather than expecting universal acceptance of one theory.
4. *Tempered quest:* Postmodern business ethicists strive for conceptions that have a better fit and an ethics that makes better sense and can work better than other approaches, at least for now. As such, it is not a quest but a tempered quest for certainty, using satisfying (instead of maximizing) approaches.

The desire of postmodern business ethics is to come to grips with the political and social pluralism in any culture and to acquire a flexible method of making ethical decisions.

Postmodernism and Its Critics

The interesting paradox of the postmodern position is that in placing all principles under the microscope of its skepticism, it must realize that even its own principles are not beyond questioning. As noted by the philosopher Richard Tarnas, postmodernism "cannot on its own principles ultimately justify itself any more than can the various metaphysical overviews against which the post modern mind has defined itself."

Marxist critics are among the harshest critics of postmodernist trends and posit that postmodernism is symptomatic of "late capitalism" and the decline of institutions, particularly the nation-state. They further contend that the nature of exploitation remains fundamentally unchanged in the postmodern era. Some postmodernists, such as Lyotard, have noted that in advanced societies, socialist struggles and their goals have been transformed into the regulators of the system. Others have asserted that it is the expected reaction to mass broadcasting as well as to a society conditioned to mass production and mass politics.

Many argue that postmodern scholars do not completely dismiss the scientific method and that they are too caught up in the idea of the primacy of moral judgments. Roy D'Andrade, for example, critiques postmodernists' definitions of objectivity and subjectivity by examining the moral nature of their models. He claims that these moral models are purely subjective and argues that despite the fact that utterly value-free objectivity is impossible, it is the goal of the scientist to get as close to that objective as possible.

Pauline Rosenau specifically identifies seven contradictions in postmodernism:

1. Postmodernism's antitheoretical premises can essentially be considered a theoretical stand.
2. While postmodernism accentuates the irrational, instruments of reason are freely employed to advance its agenda.
3. The postmodern prescription to focus on the marginal is itself a judgmental emphasis of exactly the kind that it otherwise attacks.
4. Postmodernism emphasizes the interrelatedness of texts yet often treats texts in isolation.
5. Postmodernists cannot argue that there are no valid criteria for judgment by stubbornly rejecting modern criteria for judgment.
6. The field of postmodernism practices a double standard by being critical of the inconsistency of modernism but refusing to be held to the norms of consistency itself.
7. Postmodernists contradict themselves by relinquishing the claims of truth in their own writings.

Jurgen Habermas further argued that postmodernism contradicts itself on the basis of performative contradiction and the paradox of self-reference and notes that postmodernists assume concepts they otherwise seek to undermine—for instance, freedom, subjectivity, and creativity. Postmodernists have either rejected these criticisms or provided a counterresponse. Lyotard, for example, refutes the notion that intersubjective communication implies a set of rules already agreed on and that universal consensus is the ultimate goal of discourse. He recommends having an "irreducible plurality" of all phenomena with their own local rules and practices.

Conclusion

Postmodernism has been interpreted as being a "perspective" or a new paradigm or thought. Living a social life loaded with multiplicity of meanings, without a right meaning attributable to an event or a process, and a fragmented reality with no interactions among the parts may have in many ways created the "death of reason." While critics argue that this leads to an "anything-suits" brand of ethical practice, not tempered by rigorous morality, postmodernists encourage us to look past the macro perspective and instead consider how rules and ethical norms are being defined at a micro level by different cultures and subcultures.

—Abhijit Roy

See also Absolutism, Ethical; Communism; Consumerism; Cultural Imperialism; Deontological Ethical Systems; Globalization; Kantian Ethics; Marxism; Moral Realism; Multiculturalism; Neo-Kantian Ethics; Nihilism; Pluralism; Positivism; Postmodernism and Business Ethics; Rational Choice Theory; Rationality; Situation Ethics

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Postmodernism and Business Ethics

The postmodern perspective on ethics emerged as a critique of what Alasdair MacIntyre, in *After Virtue,* has called the "Enlightenment Project" for justifying a human-centered system of moral sense making. In pre-18th-century Europe, ethical norms served as external guideposts to help humans journey toward a preordained transcendental purpose, or *telos*, as revealed in the Greek concept of the good or the Christian vision of the godly life. The Enlightenment faith in science as an extension of human rationality undercut the dependence on the teleological assumption that an external "great chain of being" linking all life forms to a higher purpose could provide an external justification for the moral precepts that guide human actions. Thus, a self-consciously modern justification for creating and maintaining a moral order requires a way to derive "universal" ethical norms from a shared *capacity to reason.* Postmodern ethicists, such as Zygmunt Bauman and Richard Rorty, would eventually come to question the modernist assumption that moral claims can be justified by applying various reasoning procedures to tap into universal truths embedded within an essential, unchanging human nature. Thus, Immanuel Kant's categorical imperative defines a procedure whereby a moral norm can be generalized to become an ethical principle that reasonable persons potentially affected by its application would consider fair to all concerned parties. Jeremy Bentham and the later utilitarians hold out the "greatest happiness for the greatest number" as the consequential measure of an ethical action. John Rawls extends a "veil of ignorance" as a refinement of Kant's procedure to ensure that the potential partiality of "reasonable persons," based on their self-knowledge of previous circumstances, would not impair their judgment of what constitutes a principle of justice. Postmodern critics argue that such ethical rule systems pose the threat of external social control because their reasoning procedures ignore or suppress consideration of the particular contexts, contingencies, and paradoxical juxtapositions that can inform individual moral choices within local communities of discourse. A troubling consequence of this critique is the inherent difficulty of defining and justifying a postmodern ethic dedicated to ironic word play and a celebration of *difference.*

Does Postmodernism Lead to Ethical Relativism?

Proponents of a postmodern ethics, as well as of postmodern thought generally, are vulnerable to the charge that their epistemological (ways of knowing) and ontological (ways of being) assumptions and methods of analysis pose a serious problem of "incommensurability," which may open the floodgates to a sea of ethical relativism or normative nihilism. This problem suggests an inability to know anything for sure, since all knowledge claims are regarded as contestable "language games" that must be subjected to a rigorous methodology of textual "deconstruction." This methodology questions all knowledge claims but especially "totalizing metanarratives" that make pretensions to a universal truth that is vulnerable to critical scrutiny. To European postmodern critics, the totalizing, hegemonic claims of fascism, communism, and even free market capitalism illustrate the destructive potential of overreaching by the ruling elites, who try to bend the rhetoric of the Enlightenment Project to their own advantage. This postmodern critique holds that universal claims of objectively valid truths are suspect for the following reasons: (1) Interactions between the researcher and the object of research necessarily influence the meaning that is constructed; (2) facts are inseparable from the values that shape the way meanings are constructed; and (3) knowledge claims are acts of colonization rather than voyages of discovery, since learning outcomes arise from a power struggle among the contestants of language games.

If applied to the agency theory of the firm, a widely accepted rationale for modern corporate governance practices, the methodology of textual deconstruction would scrutinize the claim of top business executives that they allocate organizational resources according to the "best interests" of the firm. The rationale that business managers owe a primary fiduciary duty to maximize profits for shareholders could be deconstructed as being not so much an objective scientific account as a narrative that reinforces the claims of shareholders and management to ownership and control rights while undercutting other stakeholder claims. An executive decision to "lower transaction costs" or "reduce resource dependency" by seeking to minimize environmental regulations or to limit employee wage or benefit claims could be reinterpreted as an assertion of power politics to realize a particular interest's favored value position rather than as a finding of objective management science. Postmodern philosophers hold that meanings are constructed within contested narrative space, not surgically extracted from an underlying stratum of objective reality.

The controversial and still unfolding relationship between postmodernism and business ethics is framed by a sharp exchange in a 1993 issue of the *Business Ethics Quarterly* between Ronald Green and Clarence Walton. Green argued that business ethics is assuming a postmodern cast by rejecting a unitary or "totalizing" explanation of reality and by legitimizing the right of "others" to be heard and to have their interests or "stakes" taken into account in corporate decision making. He suggested that recognition of the need to "decenter" business ethics to include the (frequently marginalized and noisy) voices and stories of those who can affect or are affected by business operations is implicit in both stakeholder and corporate social responsibility theory and practice. Walton focused primarily on the methodology of textual deconstruction, developed by European postmodern philosophers such as Jacques Derrida, Michel Foucault, and Jean-François Lyotard, to criticize Green for opening the way in business ethics to a nihilistic threat of ethical relativism. If all moral claims are deconstructed to reveal their partisan, self-interested nature as narrative ploys in competing language games, then the possibility of rationally constructing a set of universal ethical principles binding on all persons, reasonable or otherwise, would appear to be at risk.

Andrew Gustafson, in a thoughtful reply to Walton's denunciation of Green's tentative foray into postmodern territory, argues that postmodernism is not inherently nihilistic and relativistic. He finds that the methodology of textual deconstruction of meta-narratives can be applied usefully to ask tough questions about "what we can know" about any knowledge claim. He concludes that while postmodernism may be better at asking questions than in providing answers, such questions are relevant to developing a better theory of business ethics.

The diversity within postmodern thought also must be acknowledged. Pauline Rosenau notes that both negative and affirmative themes are evident within postmodern thought throughout the social sciences. A postmodern approach to business ethics is more likely to arise from within the affirmative camp, which poses interesting questions about the creative role of cognitive (thinking) and affective (feeling) processes for awakening an ethical sense of responsibility within *relationships* between the self and the other. Such questions are especially relevant to further theory development, since an improved management capacity for building and sustaining relationships through communicative practices is critical for the advancement of emerging management trends toward stakeholder engagement, corporate social responsibility, and corporate citizenship.

Zygmunt Bauman's Postmodern Ethics

In his groundbreaking book *Postmodern Ethics*, Bauman, as an affirmative postmodern European, takes on what he sees as the coercive threat of external normative control posed by the Enlightenment Project as well as the counterclaim that the postmodern critique opens the door to moral relativism and social anarchy. He recognizes that the decline of teleological assumptions about humanity's place within a great chain of being threatened to sever the link between private personhood and social order. However, he objects that the Enlightenment thinkers' self-consciously "rational" methodology for deriving universal principles and rules of ethical conduct do not gain much traction at the personal level. Such guidelines tend to take the form of *negative duties*, defining what individuals should *not* do rather than inspiring them to exercise a *positive ethical responsibility* toward others. Given the unlikelihood that most individuals will conform voluntarily to negative proscriptions, powerful interests extend the political and legal arms of the modern instrumental state to preserve social order by imposing legislative enactments grounded in supposedly "universal" ethical rules. The emergence of this external apparatus of ethical control has the ironic consequence of negating the assumption of internal ethical responsibilities within a process of personal growth and transformation. This insight suggests that the regulatory focus on requiring ethical "compliance systems" in the aftermath of the corporate scandals at Enron and elsewhere will have little positive effect in the absence of personal transformation and ethical commitment within a supportive ethical culture in business organizations.

For Bauman, morality does not arise primarily from a *rational* process of cognitive sense making. It emerges more from the workings of the heart than the head. Bauman draws on the French affirmative postmodern philosopher Emmanuel Levinas to situate the source of ethical behavior within a *moral impulse*, which Levinas characterizes as "being *for* the Other." For Levinas and Bauman, the essence of morality is not adherence to a principle drawn from an external essentialist meaning but rather openness to the possibility of internal self-transcendence by assuming a responsibility to care for others. Moreover, this personal responsibility arises in relationships with particular others in local communities of discourse rather than from a generalized love of humanity in the abstract. It is in this sense that Bauman holds that morality is not "universalizable." However, he rejects the charge of ethical relativism because each person's moral impulse exerts a counterforce to the downward pull of self-interest. Thus, an internal moral impulse is available to animate each person's potential for finding and expressing responsibility to care for particular others. For Bauman, humanity is defined not so much by its objectively determined essential nature as by its affirmative capacity for self-development.

Richard Rorty and the Ethics of Storytelling

As an American neopragmatist philosopher, Richard Rorty offers a complementary perspective on the possibility of a postmodern ethic. In his address to the 2005 annual meeting of the Society for Business Ethics, Rorty challenged the essentialist claim, going back to Plato, that moral norms must correspond to an underlying, universal Truth, whether embedded externally in a great chain of being or internally within a common human capacity to reason. For Rorty, the central question of the modern age—What does it mean to be a human being?—has become less relevant than new, more pragmatic, existential, and ultimately postmodern questions: How can we create a better world for our descendants? What sort of person shall I try to become? He noted that an applied ethic dedicated to answering these questions must look to history, politics, and literature for stories of human experience that highlight personal or social *aspirations* toward a better life. Such stories are useful to the extent that they call forth in a person facing an ethical challenge an imaginative, empathetic sympathy for the plight of others. Thus, a postmodern ethic does not ask "What is real?" or "What is rational?" but rather "What is it useful to talk about?" in the ongoing developmental quest to construct a better life for ourselves and for others. For Rorty, moral progress will come not from an abstract, rational effort to get in touch with human essences but rather from unleashing the potential of human imagination—making intuitive leaps that offer guidance on how personal and social aspirations can become new, emergent realities. Thus, Rorty concludes that the proper role of the business ethicist should be that of a poet, inspiring others to dream better stories and to embark on a pragmatic, incremental journey toward realization of a just life for all.

Related Developments in Business Ethics

In 1994, R. Edward Freeman, the leading exponent of stakeholder management theory, challenged the "separation thesis," which holds that business rationality and moral rationality are logically distinguishable because of the conventional (i.e., modern) distinction between facts and values as building blocks of knowledge. This influential doctrine maintains that business rationality should ground organizational actions in an empirical investigation of objective "facts," whereas moral rationality should ground ethical rules in a logical process for deducing universal moral principles. Standard practice is that business rationality should prevail until an ethical dilemma prompts an exceptional appeal to an alternative mode of moral rationality.

Freeman's challenge of the separation thesis served as an open invitation to new expressions of moral imagination to find ways to better integrate business and ethical thinking, both from his research associates, such as Daniel Gilbert and Andrew Wicks, and from a range of other business ethics and business and society scholars, including the author of this entry. In 1999, Diane Swanson noted that extant theories of corporate social responsibility and performance suffer from an "integration problem." Social responsibility and performance cannot be specified or measured purely in terms of "facts," since responsibility and performance, necessarily, will be defined differently, depending on the value orientation of stakeholders. This insight supports Freeman's call for a new approach to corporate decision making that integrates stakeholder value orientations with consideration of the "facts." Swanson advocates abandonment of the conventional "value neglect" approach to business decision making in favor of a new "value attunement" orientation within corporate governance processes that seek common ground among contending stakeholder claims. She concludes that this orientation will most likely arise from a communicative ethic or a dialogue based on mutual respect among corporate managers and groups in the community.

While not specifically labeled as postmodern, recent developments in business ethics, stakeholder theory, and corporate social responsibility and performance are being influenced by postmodern insights. New terms such as *stakeholder engagement, multistakeholder learning dialogue*, and *whole-systems management* suggest that business ethics is becoming more than a useful adjunct to control for lapses in individual ethical judgment within organizational settings. An emerging theory and practice of business ethics are being slowly integrated into a more complex and emergent organizational context where a managerial capacity to respect, listen to, and learn from stakeholders is being recognized as critical to both business success and system sustainability. The challenge remains that better stories, such as Sandra Waddock's *Leading Corporate Citizens*, must be converted from an inspiring account of the dreams of the few into an emergent reality for the many.

—Jerry M. Calton

See also Absolutism, Ethical; Agency, Theory of; Corporate Social Responsibility (CSR) and Corporate Social Performance (CSP); Ethical Nihilism; Ethics of Dialogue; Integrative Social Contract Theory (ISCT); Kantian Ethics; Postmodernism; Pragmatism; Rawls's Theory of Justice; Relativism, Moral; Stakeholder Engagement; Trust; Utilitarianism

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Poverty

Poverty is broadly defined as a condition in which a person or group of people lacks the essentials and necessities to achieve a minimum standard of living and well-being. Poverty is most frequently defined by economic circumstances, where individuals have insufficient access to resources. However, it may also be defined by the social ramifications that are predicated by a deprived state of social or political power.

The prevalence of poverty varies throughout the world. Industrialized nations have a lower incidence of poverty than less developed nations. In developing nations, poverty is a bleak reality. The causes of poverty are diverse, but in countries with densely impoverished regions they are geological, agricultural, ecological, and geopolitical. Official reporting agencies debate the method with which poverty is measured and reported, but general international indices include infant mortality, hunger, and child malnutrition. Infant mortality rates and child malnutrition are the most prevalent in the African continent, for example, where some regions report that as many as 20% of all preschool children are underweight. Furthermore, childhood hunger is the most ubiquitous in South Asia, with dense pockets of poverty juxtaposed with areas experiencing the benefits of economic growth.

In the United States, the official rates are determined by the U.S. Bureau of the Census (Census Bureau). The Census Bureau has been measuring poverty rates since 1964 when it developed its official poverty indices known collectively as poverty thresholds. Poverty thresholds define the minimum levels below which poverty exists and are viewed as a comprehensive poverty measure. They are used for statistical purposes. U.S. poverty thresholds are indexed to inflation and other economic indices and updated annually. Some debate the methods with which the Census Bureau determines poverty thresholds because it estimates rates using total income. Noncash sources, such as food stamps, are not factored into the calculations. Still, they are the most widely used indices. The Department of Health and Human Services also produces an index called poverty guidelines. It is another federal poverty measure, but it is different from poverty thresholds because it is used for administrative purposes only, such as determining eligibility for federal programs.

The Census Bureau examines income level, household composition, ethnicity, age, occupation, education, geographic factors (such as region, urban or rural areas, economic differences between states and regions), and health insurance costs and coverage to report annual figures and year-over-year comparisons. Data reported in 2006 for 2005 indicated that 37.0 million people (12.6% of the population) in the United States were at or below the poverty level. The majority of this figure represented women and children who did not participate in the workforce that year. This figure remained relatively stable as compared with 2004. The most marked increase was for seniors, aged 65 and older, whose poverty total increased by approximately 3%. Otherwise, blacks, Hispanics, whites, and other household compositions remained stable year over year.

At the time the Census Bureau began to define and monitor poverty in 1964, U.S. rates exceeded 20% of the population. In the most recent decade, however, they have ranged between 10% and 15%. History has proven that the rate varies the most when the overall economy is in a recessionary period.

The Influence of Business and Society on Poverty

In the United States, the poverty threshold is tied to economic health and income levels. Thus, the roles of business and society are significant in influencing the well-being of many individuals and groups who live at or below the poverty thresholds. Influencing factors include the composition or type of business, the demographic of those who are seeking work, wage levels, education, and health insurance benefits.

The United States experienced an unemployment rate of 5.08% in 2005 (4.63% in 2006), at a time when 12.6% of the population was determined to be impoverished. Despite a high overall level of employment, many working individuals did not meet the minimum cost-of-living standards to rise above the poverty level. These "working poor" are defined as members of households in which there is at least one working adult who spends a minimum of 27 weeks in the labor force or is searching for work. In 2004, the U.S. Bureau of Labor Statistics reported that there were 7.8 million working poor (5.6% of the overall population). The majority of these individuals work full-time. Blacks, Hispanics, and Latino workers were twice as likely to be counted in this group as whites. In addition, the majority of the working poor did not possess a high school level diploma.

Closing the gap between gainfully employed workers and impoverished workers is a challenging task. There are many who study this disparity and impress on businesses the need to increase wages in order to improve the lives of U.S. workers. They argue that it is an employer's ethical duty to provide a living wage. Opponents of this debate contend that economic conditions would be impaired by a living wage because the labor market would outprice businesses' ability to pay workers. Unemployment rates would increase as a result.

Over the years, the U.S. Congress has attempted to regulate minimum wages to address income levels. In the past, the minimum wage level has not kept pace with cost-of-living standards. Between 1979 and 2003, real wage rates (adjusted for inflation) fell behind other cost-of-living indices. In addition, the last increase in the minimum wage was in 1996. Proponents of the minimum wage promote increases to benefit U.S. workers. This group argues that increases will improve the overall standard of living and promote economic growth. Opponents state that increases will cause unemployment and slow economic growth and will reduce the demand for workers because they will price businesses (small businesses in particular) out of the labor market. This group also argues that government influence disrupts free market forces that would automatically adjust rates to an economically viable wage.

Three additional factors further compound the economic challenges of business and society when addressing the needs of the impoverished: The greater part of the U.S. economy is composed of the service sector, the costs of health care and health care insurance have escalated exponentially, and there is limited access to education.

Like most industrialized economies, the majority of the gross domestic product (GDP) of the United States is based on the service sector. As the economy has shifted from the agricultural and manufacturing sectors, available jobs are in service industries. According to the Census Bureau, in 2005 the majority of the working poor worked in service occupations; sales and office occupations; and production, transportation, and material moving occupations. This poses a challenge to business and society as a disproportionate number of jobs are in a sector with narrow margins and historically low wages.

In addition, the United States maintains a private health care system, which has promoted high levels of quality health care, but with escalating costs. The United States spends more on health care than any other industrialized nation, even those that provide government-sponsored coverage to their residents. In 2006, health care costs represented 16% of the GDP. Furthermore, the majority of U.S. citizens attain health care insurance coverage through their employers as a benefit of employment.

Employer-sponsored health insurance coverage was created following World War II to provide incentives to workers. The government also instituted tax incentives for employers to offer health care coverage as a benefit. Today, it is extremely challenging for businesses to offer these worker benefits because of the associated costs. Since 2000, employment-based health insurance premiums have increased 87%. On average, health insurance for a family costs $10,880 per year. Comparing this cost with the 2005 average income of $19,971 for a family of four, it is apparent that health care costs are demoralizing. In the meantime, the number of people without health insurance coverage increased from 15.6% to 15.9% in 2005, while 59.5% of individuals were covered by employment-based health insurance that same year. To manage rising costs, employers will often share them with employees.

It follows that health care inflation is increasingly affecting the numbers of individuals who have access to health care and health care insurance. The majority of individuals are dependent on employers to pay part, if not all, of their insurance premiums. Whether nonworking or working, those who are impoverished are unable to meet the escalating costs of health care and health care insurance unless they are employed by an employer that pays for the premiums.

Attaining a high level of education has proven to be necessary to securing higher-paying jobs. On average, individuals with advanced degrees earn four times more than those without a high school diploma. Impoverished individuals are less likely to attain a high school diploma and fewer still have access to a college-level education.

Conclusion

When faced with these economic challenges, businesses must weigh the opportunity of increased profits, competitive advantage, and business sustainability against the needs of the nation's poor and its working poor. Many businesses, particularly those in the predominant service sector, have difficulty meeting the expenses of competitive wages and health care premiums while considering the critical business goals of annual profit and growth. Society faces significant challenges as it addresses the educational needs of those who do not have access. Yet the ethical dilemma goes far beyond a business decision when a human life or an individual's minimal needs are at stake. It is a delicate balance.

—Pamela C. Jones

See also Benefits, Employee; Business Ethics; Business Ethics and Health Care; Developing Countries, Business Ethics in; Economics of Well-Being (Post-Welfarist Economics); Gross Domestic Product (GDP); Just Wage; Living Wage; Minimum Wage; Unemployment; U.S. Bureau of the Census; Well-Being

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Power, Business

Many observers believe that the modern corporation is the most powerful institution in society today, eclipsing the power and resources of many governments. Some statistics uphold this point of view. One report published in 2000 indicates that when measured by company sales and country gross domestic product, 51 of the world's 100 largest economies are not nations or governments but in fact corporations. Among the top 200 global corporations measured by size, 82 were U.S. companies, and 41 were Japanese. Combined, these companies' annual income was 18 times that of the 1.2 billion people in the world who lived on less than $1 a day in 2000 (estimated to be about 1.1 billion in 2005). Furthermore, the report indicates that these companies' economic activities make up some 27.5% of the total of all economic activity but that they employ less than 1% of the total workforce.

Businesses have power in multiple arenas: economic, technological, political, and sociocultural. These arenas encompass economic power because of companies' control over financial, human, and material resources and technological power because businesses influence how quickly new developments in technology appear. Companies also have considerable political power through their efforts to influence public policy, laws, and associated regulations in their favor, through the use of political action committees, testimony before legislative bodies, and other tactics. They exert sociocultural power because business activities such as marketing and advertising as well as products and services influence both individual and societal norms and expectations and environmental power because of the pressures that business activities place on the natural environment. In addition, businesses not only have power over their own employees; because of this power, they also exert influence over families and community life in general.

Businesses today, particularly multinational businesses, command a good deal of resources and attention because of their power and influence. Companies incorporate for a variety of reasons, but among them are limitations to the risks undertaken by owners. Incorporation allows owners to avoid taking on the debts incurred by the company, without which the debts of the company are also the debts of the owner; hence, incorporation grants owners limited liability. Incorporation also permits the company to develop an organizational form that allows for greater complexity, necessitating more coordination of activities, growth, and control of resources, and consequently the capacity to develop products and services that influence the purchasing behavior of customers. These benefits of growth and power have enabled large companies to produce goods and services desired by societies and individuals around the world.

The power of business is such that *BusinessWeek* magazine asked whether there was "Too Much Corporate Power?" in a cover story published in 2000. The magazine's survey of U.S. citizens found that although two thirds thought that businesses should get the credit for prosperity and that large corporations make good products that are globally competitive, nearly three fourths believed that businesses had too much power over their lives. In the survey, the American public perceived that large companies did not share productivity gains with their employees, the chief executive compensation was excessive, and there was a growing gap between the wealthy and the poor. In addition, the government, which traditionally put controls on corporate activities through legislation and regulation, and labor unions, which focus on obtaining good wages and working conditions for workers, lost power relative to corporations in the last part of the 20th century.

There are also issues around corporate control—that is, who really owns or controls the corporation—with many scholars suggesting that although owners or shareholders ostensibly own the company, in fact most companies are actually controlled by their top management team, led by the chief executive officer. Concerns about control, termed agency problems, arise when these top executives act in their own self-interest rather than in the interests of shareholders. Many observers believe that the very high compensation for executives in U.S. companies in the early 2000s is an example of an agency problem and a problem of misguided use of corporate power.

Much of the power corporations have today arises from the fact that they are treated as persons. In 1886, the U.S. Supreme Court ruled that corporations could be treated as a "natural person" by the law and had the same rights as individuals. This ruling means that companies have all the rights that citizens do in the United

States, including the right to free speech, to lobby legislators, and to make political contributions. Power comes from the fact that corporations control significantly more resources than do most individuals and therefore have more economic clout to bring to bear on public discourse, legislation, and other public policy matters, which leads some observers to suggest that corporate power and democracy are incompatible. Corporate abuses of power can occur in all the domains mentioned earlier. For example, some companies use their power to manipulate communities and governments by getting tax breaks for locating in a given place and later shutting down the facility. Companies with long supply chains have been noted in recent years for abuses of employees' human and labor rights, as well as for serious problems associated with environmental health and safety in the workplace and for environmental pollution in unregulated or less regulated areas.

The major imperative of firms as defined in U.S. law and the dominant economic theory called neoclassical economics is to maximize shareholder wealth. Wealth maximization, in turn, tends to lead corporations to want to continue to grow, and with more growth comes greater power because of the attendant control over economic and other resources. Combined with the agency problem mentioned above, this consolidation of resources means that a great deal of power resides in the hands of corporate executives, who make decisions on the basis of the company's and potentially their own self-interests rather than the public interest or common good.

Other issues related to corporate power in the early 21st century involve the consolidation of many industries into oligopolies, or industries in which there are only a few dominant firms, particularly as firms globalized. This consolidation took place through mergers of already giant corporations as well as the growth and success of some companies. Of particular concern to some observers is the control by a few companies of industries associated with the public good, such as telecommunications, agriculture, transportation, energy, and similar large industries. Testimony to the economic clout of some firms is the success of the giant U.S. retailer Wal-Mart, which by itself in 2002 represented some 2.5% of the U.S. gross domestic product.

Concern about corporate power also arises because companies spend so much money on advertising and marketing their products to consumers that consumerism is on the rise around the world. Given its limited ecological resources, many environmentalists believe that the earth cannot sustain the levels of consumption prevalent in the industrialized nations. Studies of the ecological footprints of developed nations show that significantly more resources are consumed per capita in developed countries than in developing countries, which also have lower standards of living. Differential rates of consumption fostered by corporate marketing are considered problematic because of the inherent inequities across peoples and nations that they imply: The developed world consumes 45% of all the meat and fish, with the poorest fifth only 5%, and 58% of the energy, with the poorest fifth less than 4%, among other indicators, according to the United Nations Human Development Program.

—Sandra Waddock

See also Chicago School of Economics; Economic Efficiency; Economic Growth; Free Trade, Free Trade Agreements, Free Trade Zones; Mergers, Acquisitions, and Takeovers; Profits; Prudence; Wealth

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Pragmatism

Unlike other philosophic approaches, pragmatism posits no ideal, ultimate, absolute principles of right and wrong. Good and bad are determined by the application of human intelligence to the problems at hand and by the effect that negotiated compromises have on the lives of individuals and the communities in which they live. Pragmatic philosophy is an outgrowth of the earlier work of Charles H. Peirce, William James, John Dewey, and George Herbert Mead and later extensions by C. I. Lewis, W. V. O. Quine, and Richard Rorty. The approach generally adheres to a correspondence theory of truth: Truth consists of a relation to reality. The competing coherence theory associates truth with some specified set of propositions.

Pragmatic concepts have been applied to ethical issues in business by Sandra B. Rosenthal, Rogene A. Buchholz, Joshua Margolis, and William C. Frederick. Rosenthal and Buchholz developed a pragmatic theory of the corporation that emphasizes the inseparability of the corporation and society. They further argue that these reciprocal relationships define the corporation's moral responsibilities to employees and the communities whose lives are affected by corporate operations.

Pragmatism is an analytic approach that emphasizes the continuity of experience and nature, the relationship of organism and environment, and the derivation of truth and value from the lived experiences of humans in social and organizational contexts. Values emerge from applying human intelligence to problems encountered in the course of everyday living, where both past and present experience provide guides for resolving practical dilemmas. Human goal seeking is an ongoing process of finding, adjusting, and improving the means appropriate to achieving the sought ends-in-view. This means-ends process implies no ultimate, predetermined, absolute goal, end, or purpose to be attained beyond the immediate need to confront and resolve a problematic situation. Knowledge gained in the course of resolving such matters becomes instrumental in addressing future issues and dilemmas.

Pragmatists cultivate an open-ended view of human possibilities, relying on human intelligence based on prior experience to support reliable ways of confronting problems. The sources of human experience are the many diverse and pluralistic social and cultural traditions resulting from historical and evolutionary developments extending far back in human times. Culture and nature are intertwined and coevolved aspects of human development, providing a broad base of experience and values selectively useful for supporting life in the present.

A pragmatic approach to business ethics begins within the workplace, identifies the values in contention, ascertains the respective goals and interests of the contending parties, proposes negotiations to establish an instrumental way to compromise opposing viewpoints, and seeks a pluralistic solution satisfying an optimum number of ends-in-view. Pragmatism recognizes that any resolution achieved today is subject to continued revision and improvement tomorrow. Hence, human pragmatic experience yields an ongoing, continuous means-ends activity that enables business operations to continue while achieving some of the goals sought by both business and nonbusiness participants.

—William C. Frederick

See also Negotiation and Bargaining; Pluralism; Positivism; Rationality; Reciprocal Altruism

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Predatory Pricing and Trading

Predatory pricing is an anticompetitive measure employed by a dominant company to protect market share from new or existing competitors. It generally involves temporarily pricing a product low enough to end a competitive threat. Thus, the two major parameters under consideration are costs and the intent of the firm. Costs are usually easy to define yet there is a debate on the appropriate ones to use. Intent, on the other hand, is easier to comprehend yet most difficult to prove.

The exact legal (statutory) conditions for predatory pricing vary across the globe. In the United States, pricing below a dominant average variable cost (the *Areeda Turner* test) was last used by the Supreme Court in 1993 as a criterion for this practice in deciding *Brooke Group Ltd. v. Brown & Williamson Tobacco Corp.* According to the Court, this practice arises when a business rival prices its products in an unfair manner in an attempt to eliminate competition and exercise control over prices in the market. While the law should protect price competition, it should distinguish unfair pricing practices that would eliminate competition. The basic antitrust dilemma is to distinguish price predation from hard competition.

Generally, the following conditions must exist to constitute predatory pricing:

- The predator must have the market power to unilaterally increase its prices.
- The predator must charge prices that fall below a predatory price standard (which varies from country to country).
- The predator should be able to recoup its losses after the competitors have been driven out of the market.

The predatory pricing argument is as follows. The predatory firm initially lowers its price until it is below the average cost of its competitors. The competitors are then forced to lower their prices below average cost, thereby incurring losses on every unit sold. They are then faced with a difficult situation: If they opt not to drop their prices, they are bound to lose their entire market share and their profitability in the long run; on the other hand, if they do cut their prices, they will also lose a lot of money. After forcing competitors out of the market, the predatory firm raises prices and recoups its losses in the short run and increases its profits in the long run.

Researchers over the past four decades have yet to provide a clear-cut example of a monopoly created by predatory pricing. Some contend that competitors who are unable or unwilling to cut prices make these claims. In most cases, the courts have wrestled with how to characterize price predation. So far, three tests have been used: (1) predatory intent, (2) below-cost pricing, and (3) likelihood of recoupment of costs. In most cases, they have considered a combination of these three cases.

History and Cases of Predatory Pricing

The notion of predatory pricing can be traced back to the dawn of the industrial era. Notable examples include John D. Rockefeller's Standard Oil Company, which was accused of using low prices to drive away competitors in the late 19th century. AT&T spent $100 million per year in the 1970s defending against claims of predatory pricing.

American Airlines in the Mid-1990s

Between 1995 and 1997, three small carriers—Vanguard, Sun Jet International, and Western Pacific—entered the Dallas market by offering low-priced service to midwestern cities. American responded by matching their fares and increasing service on these routes. For example, American's one-way fare from Dallas to Kansas City was $108 before the low-cost start-ups entered the market in 1995. American promptly cut fares to $80 and almost doubled the number of flights to 14. All three start-ups subsequently abandoned Dallas Airport. Soon after, American raised its prices to $147 and scaled back the number of flights. None of the start-ups remain in business today.

The airline industry typically operates with very high fixed costs (e.g., equipment) and low marginal costs. On the other hand, as noted earlier, to win predatory pricing cases, one has to prove that the firm sold products or services for less than its average variable cost. The U.S. Congress enacted the Airline Competition Preservation Act in 2001, putting the airline industry on notice that it planned to monitor anticompetitive and "predatory" practices. The act issue guidelines to prevent large carriers from eradicating the start-ups. One such suggestion was to force the dominant carrier to continue offering the low fares for 2 years if they respond to a low-fare service by a new entrant. The proposal also gives the Transportation Department the authority to investigate whether or not an airline is charging an average fare on a route that is unreasonably high.

Microsoft in the Late 1990s

In 1996, Microsoft began giving away its Web browser, Internet Explorer, as well as free software and marketing assistance to use its products. This enabled the company to successfully overcome the marketing dominance of its archrival Netscape Communications in the mid-1990s. In addition, to gain supremacy in the software industry, the company repeatedly gave away software that other companies were selling, thus hurting other firms such as Stac, Symantec, Novell, and Oracle.

Microsoft has aggressively defended these giveaways, arguing that lower prices are good for consumers. Moreover, bundling several types of software packages into an affordable unit is driven by customer needs. The courts have sided with Microsoft to date, and the company has stayed out of further controversy by refraining from raising the prices of its products, coupled with a strong public relations campaign involving several corporate social responsibility programs.

Wal-Mart in 2000

In 2000, government officials in Wisconsin, Oklahoma, and Germany accused Wal-Mart of pricing goods below cost with the intent of driving competitors out of the market. The Wisconsin Department of Agriculture, Trade and Consumer Protection filed a complaint against the giant retailer for violating the state's antitrust law by selling butter, milk, laundry detergent, and other staple goods below cost in stores in many cities and towns, thereby forcing other local stores out of business, gaining a monopoly, and ultimately increasing its prices.

In Oklahoma, Crest Foods, a three-store supermarket chain, filed a predatory pricing suit against Wal-Mart, contending that the latter regularly sent employees to visit their store to monitor prices and subsequently targeted price cuts, often dipping well below their own costs, so as to undermine them. Similarly, in Germany, the Federal Cartel office accused the retailer of predatory tactics using "corner product" items such as milk and vegetable oil. German law prohibits below-cost pricing because the practice decimates small businesses and independent shops.

Support for the Rationale for Predatory Pricing

Many economic models based on game theory and the theory of imperfect competition have shown that predatory pricing can be rational and profitable under specific circumstances. For example, by using "low-cost signaling"—that is, by increasing production and simultaneously lowering costs below the price—a firm may hoodwink its competitors into believing that it has a lower cost of production than the rest, thereby persuading them to leave the market as it would not be profitable for them to compete. Aggressive pricing also enables predators to acquire the reputation of being "tough," which may deter many potential entrants in the future. A final reason for predatory pricing is that aggressive pricing strategies will ensure more loyal customers from whom the company can make a profit in the future.

Skepticism Regarding the Theory of Predatory Pricing

Many question the justification for the theory of predatory pricing since it is an irrational practice and the laws designed to prevent the practice only discourage competition. The Federal Trade Commission has not successfully prosecuted any firm for this practice in over two decades, and there are no empirical examples illustrating demonstrated predatory pricing by a firm. Such practices can be very costly for a larger firm (usually the predator), and a price war is an extremely risky venture given the uncertainty of how long it is likely to last. In addition, the competition may temporarily shut down its operations and resume when the price wars are over. Critics further argue that there has been no case when predatory pricing has led to monopoly. Conversely, there is strong evidence of the practice having failed repeatedly.

It is interesting to note that when Ford introduced the Model T in the early 1900s, it actually lost money and market share to Buick, Oldsmobile, and other competitors. By 1910, the auto industry was booming, yet Ford decided to cut its price by 20%, to $780, which was below the average total cost. On the contrary, General Motors, Ford's major competitor, had decided to increase its prices. Ford may have "preyed" on its competitors, yet few would argue against the fact that the customers were the ultimate beneficiaries. However, it does make one wonder whether such actions would have been allowed in today's environment.

Issues for Further Research

There are many issues that are yet unresolved regarding the effects of predatory pricing on marketing decisions and strategies. For example, it is not clear what the long-term effects of predatory pricing on customer behavior are. As noted before, consumers benefit by paying less in the short run, yet the impact of higher prices set by the predatory firm after the demise of competition is not clear. Are consumers aware of predatory practices, and if so, how, and does it cause any backlash? Research is also needed to identify product-, company-, and industry-based factors that contribute to the occurrence of predatory pricing practices.

Another issue relevant in international trade pertains to the circumstances under which dumping may be considered predatory marketing. Dumping occurs when a foreign firm sells a product in a host country at a price below the cost or at a price below that at which the firm sells the same product in its domestic market. This is not the same as predatory pricing as firms often sell in free markets for nonpredatory reasons as well, such as during recessions or when the company's sale price remains high enough to cover the variable cost as well as part of the fixed costs they would continue to incur even if they stopped selling. Although the U.S. antidumping law and policy do not specifically prohibit predatory pricing, it is worth investigating the relationship between dumping and predatory pricing in other markets throughout the world and the necessary conditions under which one is considered to be the other.

—*Abhijit Roy*

See also Bankruptcy, Ethical Issues in; Barriers to Entry and Exit; Collusion; Dumping; Economics and Ethics; Price Discrimination; Price-Fixing; Pricing, Ethical Issues in; Transfer Pricing

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Preferential Treatment

The term *preferential treatment* refers to forms of recruitment, appointment, hiring, and promotion that give preference to (members of) groups previously or presently affected by discrimination.

Preferential treatment is often called "affirmative action." But whether the two terms are synonymous will depend on the narrowness or broadness of the definitions used.

The forms of discrimination that lead to policies of preferential treatment need not be intentional or rooted in racist or sexist attitudes. Discrimination is sometimes unintentional and connected to practices that have discriminatory effects. Hiring by personal friendships and word of mouth are common instances, as are some seniority systems. Advertising and interviewing only in certain geographical regions or at certain colleges may have the effect of excluding minorities from consideration for jobs. Even bias-free individuals may engage in selection procedures that have disproportionate and adverse effects on certain groups. Preferential treatment policies have been established to redress policies or practices that have had such discriminatory effects.

Preferential policies make the properties of race and sex morally relevant considerations, even though these properties should, under circumstances free of discrimination, be morally irrelevant. However, the reasons for using these properties in preferential policies are different from the role these properties play in invidious discrimination. Racial discrimination and sexual discrimination typically spring from feelings of superiority and a sense that other groups deserve lower social status. Preferential treatment entails no such attitude or intent. Its purpose is to restore to persons the status that they have been unjustifiably denied, help them escape stigmatization, and foster relationships of interconnectedness in society.

Preferential treatment can appear in the form of specific target goals or, in more subtle ways, of giving special opportunities to minorities or women. Merely terminating discriminatory attitudes or practices does not constitute preferential treatment. To stop a policy of hiring by family connections or to terminate a seniority system might have the desired effect of ending discrimination, but it would not involve preferential treatment.

Preferential policies are often said to have their moral foundations in the principle of compensatory justice, which requires that if an injustice has been committed, just compensation or reparation is owed to the injured person(s). However, it has been disputed that any form of justice is adequate to justify policies of preferential treatment. It is generally agreed by all parties to the discussion that individuals injured by past discrimination are owed compensation as a matter of justice. However, controversy has arisen over whether past discrimination against *groups* such as women and minorities justifies preferential treatment for current group *members*. Critics of group preferential policies hold that only identifiable discrimination against *individuals* requires, and warrants, a policy of compensation; they argue that group preferential polices are unjust. Some supporters of preferential policies try to show that principles of justice do apply to groups, but other supporters appeal to social ideals and good social outcomes rather than principles of justice. Each of these three positions is considered below.

Those who claim that preferential compensatory measures are *just*, in the sense of required by justice, argue that past discrimination warrants present remedies, including preferential treatment of groups. Proponents note that the effects of discrimination linger. For example, African Americans whose families were victims of past discrimination may be handicapped by poverty and undereducated parents, whereas the families of past slave owners are still being unduly enriched by inheritance laws. On this account, those who have inherited wealth accumulated by iniquitous practices have no more right to their wealth than the sons of slaves, who have some claim to it as a matter of compensation. In the case of women, the argument is that cultural attitudes foster in women a lack of self-confidence and prejudicially exclude them from much of the domestic and international workforce or treat them as a low-paid auxiliary labor unit. Consequently, only highly independent women can be expected to compete with men on initially fair terms; and even these women may not be able to compete equally in the setting of multinational corporations having operations in many countries.

Those who claim that group compensatory measures are *unjust* argue that no criteria exist for measuring just compensation to groups, that employment discrimination in society is presently minor and controllable by enforcement of existing law, and that those harmed by past discrimination are no longer alive to be compensated. Some minority groups that were once underprivileged and discriminated against but are now successful argue that their long struggle for equality is being jeopardized by programs of "favoritism" to specific minorities and women. Instead of providing compensation, these opponents of preferential treatment argue, strict equality as well as merit hiring and promotion should be enforced while attacking the roots of discrimination.

The third view is that some compensatory measures are not justified by principles of justice but are justifiable on some other moral basis. Proponents argue that even if preferential policies are unfair in their treatment of some individuals (producing so-called reverse discrimination), these preferential plans can be justified on consequentialist grounds because they can be reasonably expected to serve public utility as society's principal instrument to the end of eradicating intolerable social situations of discrimination.

Arguments for and against preferential treatment have had a profound effect on corporate life and on many other social institutions. The once widespread acceptance of racial segregation and sexual dominance in America has surrendered to a more polite culture that accepts racial integration and sexual equality. As women and ethnic groups have made advances, public opposition to preferential treatment has hardened. However, many writers have pointed out that despite the vast changes in attitude and increases in opportunities in recent years, social data indicate that many underlying practices and patterns of discrimination—or at least failures of proportional representation—remain fundamentally unaltered. Controversies over preferential policies are not morally a thing of the past.

—Tom L. Beauchamp

See also Affirmative Action; Civil Rights; Employment Discrimination; Equal Employment Opportunity; Equal Opportunity; Gender Inequality and Discrimination; Minorities; National Origin Discrimination; Racial Discrimination; Religious Discrimination; Reverse Discrimination; Sexual Harassment

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PRETEXTING

Pretexting is the practice by which personal information is obtained under false pretenses. It often takes place by telephone or via the Internet. For example, pretexting occurs when someone calls a credit card company, pretends to be a particular credit card holder, and obtains information about the true credit card holder's account. It has been deemed both inappropriate and illegal according to the laws of the United States. The term is derived from the false "pretext" that is used to obtain personally identifying information.

Individuals who participate in pretexting are known as "pretexters," many of whom sell the illegally obtained information to others. This information may be used to obtain credit in someone else's name or to investigate or sue a particular person. Pretexting is similar in many ways to identity theft in that it involves theft of personally identifying information.

A variety of tactics are used by pretexters to obtain someone's personal information. For example, it is common for a pretexter to call a person and claim to be asking questions on behalf of a survey firm. After obtaining the desired information, a pretexter then typically uses that information to obtain that person's financial information, such as account numbers, credit card numbers, and so on. In this way, the pretexter can also acquire identification information such as work history and social security numbers.

Hewlett-Packard

Although it is generally assumed that such an illicit practice would only be undertaken by unscrupulous characters, recent newspaper headlines have indicated otherwise. Hewlett-Packard (HP) has recently been the subject of investigations by the California attorney general's office and the U.S. House of Representatives. It is believed that pretexting was condoned by the most senior executive, the chairperson of the board of directors.

During 2005, HP instituted an investigation of numerous leaks to the press by its board of directors. HP hired a private investigation firm to carry out the inquiry. The private investigation firm subsequently hired another firm that used pretexting techniques to obtain phone records, allegedly with the knowledge of HP personnel. The resulting investigations have led to the dismissal of key management executives in the company, including both the chairperson and another member of the board of directors.

Although consumers in the United States are critical of corporations, HP has been considered a role model by many people, particularly in terms of ethics and responsibility. When such an event occurs, it undermines the reputation of the corporation and, in particular, the perceptions of consumers regarding the integrity of the corporation.

Trust is a valued and valuable commodity. It is, however, undermined by behavior such as pretexting, particularly when it is sanctioned by business leaders. Unfortunately, the deterioration of trust resulting from such an incident affects business in general, not just the individuals or companies directly involved.

—Tara J. Radin and Ozgur Toraman

See also European Union Directive on Privacy and Electronic Communications; Hewlett-Packard; Identity Theft; Internet and Computing Legislation; Privacy; Reputation Management; Trust

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Price Discrimination

Price discrimination occurs when a seller charges different prices to different customers for the same product. Such unequal treatment raises questions of fairness. Under certain circumstances, price discrimination may violate the Robinson-Patman Act's prohibition against predatory pricing.

Price discrimination may violate our ethical intuitions. Behavioral economics teaches that people are highly sensitive to perceived attempts to exploit or price-gouge them. In a famous experiment by Daniel Kahneman and coworkers, 82% of subjects considered it to be "unfair" or "very unfair" for a hardware store to raise the price of snow shovels after a large snowstorm. Similarly, Coca-Cola was the subject of snide editorials and columns when it was rumored that the company had begun testing a vending machine that could automatically raise prices for its drinks in hot weather. Customers complained when the Mets baseball team introduced variable pricing—from $8 to watch the Mets play the Brewers on a weekday up to $16 to see Barry Bonds on Saturday. New Jersey's top civil rights official has determined that ladies' nights (where a bar offers women a lower price of admission or free drinks) illegally discriminate against men, and many states prohibit the practice. Wal-Mart has been accused of driving mom-and-pop stores out of business by selectively lowering prices in stores that compete with them.

Sellers don't want to provoke a customer backlash. Accordingly, they are hesitant to engage in practices such as off-peak pricing. Ski operators are reluctant to boost holiday prices, and hotels are reluctant to charge a market-clearing price for hotel rooms. The Cornell economist Robert Frank quotes a ski industry consultant as saying, "If you gouge them at Christmas time, they won't come back in March." Afraid of growing public anger, Coca-Cola quickly slapped down rumors about its weather-sensitive vending machines.

Nevertheless, in the economist's lexicon, price discrimination is a term of art and does not necessarily have any pejorative connotations. This entry assesses claims that price discrimination is unfair or illegal.

Does Price Discrimination Allow Sellers to Exploit Customers?

A seller will earn higher revenues if it can charge different prices than if it can charge only one price. This is because customers differ in how much they are willing to pay for a product or service. Take the case of airfares: One customer might want to fly to Hong Kong badly enough to pay $1,000 for the fare, while another customer might be unwilling to buy a ticket unless the price is $600 or less. If the seller (here the airline) can charge only one price for both tickets, it will earn $1,200 (i.e., two fares of $600). However, if the airline can price discriminate—that is, charge the first customer $1,000 and the second customer $600—it can make an additional $400 in profits. Each customer pays no more than he or she is willing to pay, but the airline has expropriated virtually all the "consumer surplus" (i.e., the difference between what customers are willing to pay and what they actually have to pay for the good or service in question).

Some people fear that the Internet has enhanced the ability of powerful online retailers to engage in price discrimination (so-called "dynamic pricing"). This scenario goes as follows. Online retailers collect vast quantities of information about customers' preferences and buying habits. Then, they construct consumer profiles from this information. Finally, they use the profiles to estimate each customer's reservation price (the maximum he or she is willing to pay) for a good (or service) and price the good accordingly. In this way, the retailers can price their goods so as to squeeze the maximum dollars out of each customer.

The catch with each of these scenarios is that they assume that the seller has monopoly power (or there is some other market failure). If the airline, for example, is *not* a monopolist, then the high prices it charges its customers can be expected to attract new entrants into the market. Other airlines will offer the customers lower prices. As in the standard economic model, the airlines will successively undercut one another's prices until they have competed away the profit and the price is back at long-run equilibrium.

In summary, price discrimination cannot be used to systematically "gouge" customers unless the seller has a monopoly (or there exists some other market failure). But if there is a monopoly, then that, not price discrimination, is the problem.

Is Price Discrimination Unfair *Between* Customers?

A second objection to price discrimination is that it unfairly discriminates *between* customers. It appears to violate Aristotle's conception of justice, which requires that like cases be treated alike and different cases be treated differently. Is it fair that one passenger should pay $1,000 to fly to Hong Kong when the person sitting next to him or her has paid only $600?

Note that there must be some underlying economic explanation for the difference in fares. Otherwise, in a competitive market, the price discriminator would lose its $1,000 customer to another airline. This is the tip-off to the fact that, most likely, there is some morally relevant difference between the two passengers that justifies the price difference. The customer with the $1,000 seat may be getting more for the higher fare. Obvious examples are the convenience of being able to buy a ticket the day before the flight or the ability to cancel the ticket if a business meeting is called off.

Passengers don't simply buy (or rent) a seat on an airliner. The fares they pay reflect other features as well. Other price differences between customers are not arbitrary. A meal on a Saturday is not the same as a meal on another day of the week. A Coke on a hot day is worth more (in terms of utility) than a Coke on a cold day. Seen in this light, there is strictly no unfairness because the good or service is *not* identical. Aristotle's definition of justice requires not only that like cases be treated alike but that *unlike cases* be treated differently in proportion to their difference. Here, despite superficial similarities, the goods and services are different.

On close inspection, moreover, the $1,000 customer may actually be a *beneficiary* of the difference in fares. If the airline can fill only half its seats at $1,000 on a particular route but the flight breaks even only at 60% capacity, then selling an additional 20% (or more) at $600 will make the flight profitable. In this way, everyone is a winner. If airlines were required to charge the same price for every seat, many seats would remain empty and many flights would remain grounded.

Price-Gouging Following Disasters

Perhaps price discrimination is never more vilified than following a disaster. And the gap between our commonsense intuitions and standard economic analysis is never wider than in such circumstances. After Hurricane Hugo struck Charleston, South Carolina, in 1989, the price of a $20 sheet of plywood jumped to $200, and a $125 chain saw cost $750. The city council passed emergency legislation making it a crime to charge prices higher than those that prevailed pre-Hugo, and the mayor declared martial law.

However, many economists argued that attempts to suppress price-gouging made matters worse. First, if sellers aren't permitted to charge higher prices during a shortage, they have less incentive to carry spare inventories. Second, higher prices also ration demand and ensure that scarce resources are applied to their most valuable uses. Third, in a shortage, the choice generally is between higher prices and empty shelves.

Benign Price Discrimination

Finally, there is a class of cases where treating people alike seems obviously unfair. In other words, price discrimination is morally called for. For example, we demand that drug companies make their anti-AIDS drugs available at a lower cost to people with HIV in Africa and other poor countries. We also don't object if museums give students discounts.

Note that drug companies can supply anti-AIDS drugs to Africans only if market forces are somehow prevented from working. If Merck or GlaxoSmithKline supplies anti-AIDS (or antimalarial or antituberculosis) drugs to Africans, there is the risk that arbitrageurs will buy the drugs in Africa and smuggle them back into Europe or America, where they will earn a large profit. Benign price discrimination is no more stable than the malignant version.

Illegal Price Discrimination? The Robinson-Patman Act

Price discrimination may constitute "predatory pricing" in violation of Section 2(a) of the Robinson-Patman Act. But predatory pricing allegations rarely succeed in courts today. The reason is that for the act's prohibition of price discrimination to apply, the price must (a) injure competition and (b) be below cost. Thus, if Wal-Mart charges lower prices in one store than in another, competitors won't prevail in court by simply showing that they have been injured (i.e., have lost revenues and/or been forced out of business). After all, legitimate price competition also reduces revenues. To prove predatory pricing, the competitors must further show that Wal-Mart has priced its product below its cost. The desuetude of Robinson-Patman is explained by the courts' reluctance to interfere with healthy competition. Moreover, public policy is much less preoccupied with monopoly than in the past. The reason is that most economists believe that monopoly profits will attract rivals into the market and so are likely to be ephemeral.

—Ian Maitland

See also AIDS, Social and Ethical Implications for Business; Antitrust Laws; Arbitrage; Consumer Protection Legislation; Federal Trade Commission (FTC); Just Price; Monopolies, Duopolies, and Oligopolies; Predatory Pricing and Trading; Pricing, Ethical Issues in; Welfare Economics

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PRICE-FIXING

Price-fixing is any agreement between competitors ("horizontal") or between manufacturers, wholesalers, and retailers ("vertical") to raise, fix, or otherwise maintain prices. Many, though not all, price-fixing agreements are illegal under antitrust or competition law. Illegal actions may be prosecuted by government criminal or civil enforcement officials or by private parties who have suffered economic damages as a result of the conduct.

Horizontal Price-Fixing

Examples of horizontal price-fixing agreements include agreements to adhere to a price schedule or range; to set minimum or maximum prices; to advertise prices cooperatively or to restrict price advertising; to standardize terms of sale such as credits, markups, trade-ins, rebates, or discounts; or to standardize the package of goods and services included in a given price. All such agreements are per se illegal under United States antitrust law; that is, the court will assume that any such agreement is anticompetitive and will not hear arguments to the effect that the agreement actually enhances quality, competition, or consumer welfare in a particular case. Horizontal price-fixing agreements are also illegal under European Union (EU) competition law, where they are similarly subject to so-called hard-core restrictions.

There is nothing illegal about competitors actually setting the same prices as one another or even about them doing so consciously. (Indeed, in a perfectly competitive market, we would expect retailers to sell their goods at the same prices.) The offense lies in their *entering into an agreement with one another* to set or raise or maintain prices. (Section 1 of the U.S. Sherman Act, for example, prohibits any "contract, combination or conspiracy" that restrains trade.) The agreement, to be a violation, need not set a particular price; the law frowns on any agreement that interferes with competitors' ability to set their own prices with complete freedom. Thus, agreements that set price ranges, establish formulae for rates of change in prices, or supply guidelines for competitors' responses to changes in their cost structures are all violations, even though they neither establish a precise common price nor eliminate all possible price competition. Not every competitor in the market need participate in the agreement. Even an agreement between two tiny competitors in an enormous, busy, and otherwise competitive market will be a violation.

Analysis of Horizontal Price-Fixing

Economists generally agree that horizontal price-fixing agreements are bad for consumers. Competition normally drives prices down, as competitors seek to lure away one another's customers. In a competitive market, therefore, the consumer realizes the greatest possible amount of *consumer surplus*—the value to the consumer of the good in excess of what the consumer actually has to pay for it. Price-fixing agreements, since they reduce competitors' ability to respond freely and swiftly to one another's prices, diminish consumer surplus by interfering with the competitive marketplace's ability to keep prices low. More important, horizontal agreements among competitors may facilitate their joint acquisition of *market power*—the ability to sustain higher prices than free competition would allow, without losing customers. A wide enough agreement could permit competitors to act as de facto monopolists, raising prices and cutting back on production to the detriment of consumer welfare. Moreover, they could do this without gaining any of the efficiency benefits of an actual merger or consolidation.

There are some critics of horizontal price-fixing policy, however. Some conservative economists argue that it is scarcely worth policing horizontal price-fixing arrangements, since they are economically unstable. Each member of a horizontal price-fixing agreement has a strong incentive to defect, secretly offering lower prices to attract a greater share of customers. In addition, any market with inflated prices induced by a horizontal agreement will rapidly attract new entrants, and they can easily restore prices to the competitive level. Finally, many economists are skeptical of courts' and prosecutors' abilities to distinguish real price-fixing arrangements from other complex arrangements with legitimate, procompetitive purposes.

In addition, there have been some concerns about the per se prohibition of horizontal price-fixing agreements in contexts where it is difficult for consumers to judge the quality of goods or services on their own. Take medical care, for example: Patients are often unable to judge for themselves whether the care they receive is of high or low quality. (High-quality care does not guarantee good outcomes, and patients who have received care of poor quality may nonetheless get better.) If high-quality care is both expensive to provide and hard for consumers to detect, the argument goes, then vigorous price competition will drive high-quality care off the market. Patients will not pay more for a difference in care they can't detect or verify. On the other hand, if price competition is minimized through horizontal agreements, then the pressure to cut costs by cutting quality will be reduced.

A third argument against the prohibition of horizontal price-fixing agreements involves the social desirability of cross-subsidization of services for the poor. Physicians, lawyers, and institutional health care providers have frequently argued that a reduction in price competition among them can give them the cushion necessary to supply necessary services at a reduced price or at no cost to poorer consumers. (Another, perhaps more intuitive, way to put this is that vigorous price competition reduces margins, and reduced margins result in cutbacks in charity care and pro bono work.) While competition law has not accepted these arguments, a number of state and local legislatures and regulators have created schemes under which competing health care providers, for example, can apply for permission to fix their prices under close state supervision in order to subsidize low-cost care for the poor. These schemes shield the providers from prosecution by extending the state's immunity from antitrust enforcement to cover their private actions.

Vertical Price-Fixing

Vertical price-fixing arrangements include agreements by manufacturers to set minimum or maximum resale prices for their products. Minimum resale price-fixing is often termed *resale price maintenance.* Direct agreements to maintain resale prices are per se illegal in the United States and subject to "hard-core restriction" in Europe. In both places, however, it is possible for manufacturers to achieve de facto resale price maintenance through indirect means—for example, by refusing to deal with retailers who discount their goods or by offering rebate programs that gear rebate amounts to pricing levels. These indirect means are especially difficult for courts to sort out when the vertical pricing arrangements are combined with other vertical restraints, such as geographic exclusivity deals, service and parts agreements, promotional agreements, and so on.

Maximum vertical price-fixing is at least prima facie procompetitive, since it appears designed to keep prices to consumers low. It is therefore generally judged on a case-by-case basis, with the court balancing the pro- and anticompetitive effects of the agreement in question against each other. (This case-by-case standard of evaluation is known in U.S. law as the *Rule of Reason*; it contrasts with the per se standard, which permits no such balancing.)

State-mandated and -supervised vertical pricing schemes—such as state price controls on auto insurance or on hospital charges—are immune from federal antitrust prosecution under U.S. law. In contrast, EU member states enjoy no such broad "state action immunity" from European competition law. Government-sponsored price-fixing schemes at the U.S. federal or EU-wide level (e.g., agricultural price supports) do not violate domestic antitrust laws but may be challenged as protectionist by other countries through the World Trade Organization.

Analysis of Vertical Price-Fixing

The economic effects of vertical price-fixing are complex, but economists are generally agreed that at least some prohibited vertical price-fixing could be efficient and procompetitive. Consider, for example, a resale price maintenance program put in place by the manufacturer of a certain brand-name appliance. The program guarantees adequate profit margins for the brand's retailers and lets them attempt to capture market share from one another via nonprice competition. Such nonprice competition might include the provision of excellent and attentive service by sales staff in well-stocked retail showrooms, armed with informative promotional brochures. The price maintenance program's limits on *intra*brand price competition have the long-term effect of enhancing the brand's reputation for quality and service; this, in turn, would enhance *inter*brand competition. Without price maintenance in place, however, low-service discount retailers can free ride on the costly services provided by others. Consumers could get their information from the salesman in the comfortable showroom but then actually purchase their appliances from the free-riding low-service discount warehouses. In the long run, without price support, excellent service will be driven out of the market, and the brand's ability to compete with other brands on quality and service will be diminished. Resale price maintenance might also serve to secure margins for small-volume retailers who, without some such guarantee, would be disinclined to devote shelf space to the product. Here, again, intrabrand competition is curtailed to secure distribution channels that facilitate more vigorous interbrand competition. Where the prospect of enhanced interbrand competition is minimal, however—as in the case of a manufacturer with market power in the product being sold—the anticompetitive effects of resale price maintenance may dominate.

Maximum price-fixing keeps costs to consumers down. While it may impose burdens on retailers, those burdens may not be injurious to competition, since retailers who find the maximum resale price burdensome can in many cases simply switch to a different supplier. Moreover, in situations where manufacturers grant geographically exclusive distribution rights to retailers (perhaps to retain control over the secondary markets for parts, service, and repairs), maximum price-fixing can prevent the "local monopolists" from gouging consumers. Finally, maximum price-fixing can limit the total damage to consumers from the repeated markups that occur when all levels of the distribution chain—manufacturer, wholesaler, and retailer—are in the hands of firms with significant market power.

International Price-Fixing

Internationally, price-fixing has been common through the ages. OPEC, for example, is a well-known decades-old cartel of oil-producing nations that sets its production levels cooperatively, with an eye toward keeping oil prices high. OPEC is protected from prosecution under other nations' antitrust laws, both by the international legal doctrine of sovereign immunity and by Austrian law governing service-of-process (OPEC is headquartered in Vienna). Recently, however, the argument has been made that OPEC's price-fixing practices could be attacked through the World Trade Organization, to which the OPEC member nations belong.

In the last decade of the 20th century, an unusual number of global price-fixing cartels surfaced. Among those prosecuted criminally were cartels fixing prices on lysine, vitamins, graphite electrodes, sorbates, sodium gluconate, construction, computer memory chips, marine construction, and citric acid. These cartels inflicted billions of dollars of losses on consumers, raising prices from 30% to 100% during the course of the conspiracies. The cartels were prosecuted vigorously in several countries. Criminal fines paid by companies in half a dozen of the cases exceeded U.S.$100 million; to these were added billions of dollars in payments of private claims to customers alleging economic damages. Executives from Germany, Belgium, the Netherlands, England, France, Switzerland, Italy, Canada, Mexico, Japan, and Korea have been convicted, fined, and in some cases jailed for price-fixing violations.

—Stephen R. Latham

See also Antitrust Laws; Cartels; Competition; European Union; Free Trade, Free Trade Agreements, Free Trade

Zones; Organization of Petroleum Exporting Countries (OPEC); Surplus, Consumer and Producer; World Trade Organization (WTO)

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PRICING, ETHICAL ISSUES IN

Pricing, one of the four functions of marketing (along with product, place, and promotion), is a dynamic process by which buyers and sellers determine what, and how many, units of wealth should be exchanged for a needed product or service. Buyers and sellers have differing goals in this exchange process. Usually, buyers are interested in obtaining needed products and services at the lowest possible price, while sellers tend to concern themselves with maximizing their profits.

Price affects both the supply of, and the demand for, a particular item. Generally, higher prices encourage sellers to produce more of an item but discourage buyers from purchasing large quantities of the item. Contrariwise, low prices tend to whet buyer demand for an item while discouraging sellers from producing. There is a price point, called *price equilibrium*, at which the supply of and demand for an item are equal. At price equilibrium, buyers purchase as many units of production as sellers make available.

The ethical issues in pricing are similar to those governing other aspects of business and deal primarily with fairness—fair competition and fair treatment of buyers and sellers. Generally, any pricing practice that maintains the competitive nature of the market and is fair to market players is ethical; practices that hamper free competition or unfairly treat specific constituencies of buyers or sellers are likely to be unethical.

Anticompetitive Pricing

Anticompetitive pricing practices impede the natural dynamism of a free market. Some anticompetitive pricing practices are illegal, in addition to being unethical. In *price discrimination*, the seller offers identical products or services at different prices. There are three types of price discrimination. Price may vary by customer, when the value of the product or service is subjective or demand is highly elastic. Price may vary by quantity sold, which allows the buyer to enjoy scale economies on large purchases. Price may vary by location or customer segment, which allows both the seller and the buyer to enjoy economies of location. From the seller's perspective, perfect price discrimination would allow the seller to charge each buyer the maximum price the buyer is willing to pay; this form of price discrimination would create an infinite number of points along the demand curve at which the maximum price could be attained from various buyers, each involving a different quantity sold. In theory, perfect price discrimination could be attained at any level of seller output at which there is at least one buyer willing to pay the asking price for the good.

Many forms of price discrimination are ethical. For example, many restaurants offer a children's or senior citizen's menu. Supermarkets offer discounts to customers who use coupons or become price club members. Cinemas may have lower-priced tickets for matinees or for children. Price discrimination may occur even when the seller does not have a monopoly. In this instance, sellers operate in competitive markets but enjoy some degree of discretion in pricing due to brand loyalty, special product characteristics, or market segmentation.

Price discrimination may be predatory in nature, such as when prices are set below cost for certain preferred customers or with the intention of driving smaller competitors out of the market. *Predatory price discrimination* may violate specific laws, such as the Robinson-Patman Act, antitrust legislation, and Federal Trade Commission regulations. Determination of the legality or ethicality of pricing discrimination must be done on a case-by-case basis.

Price-fixing is the process by which a number of sellers agree to sell their commodity for a specified price in a specific market. While all sellers in a market may indeed sell their wares for the same price, this situation is price-fixing only when the sellers agree to do so in advance. In most states, seller collusion to set prices at a certain level is illegal. There is often tacit collusion to fix prices when some sellers' pricing strategy is to match, but not exceed, the price of an industry leader. The Federal Trade Commission has decided in many instances of tacit collusion that the circumstances did not meet the definition of price-fixing because the sellers did not agree among themselves in advance to charge the same price. Tacit collusion can only be considered price-fixing as defined by the Federal Trade Commission when the sellers have advance knowledge of each other's pricing actions and agree to behave similarly. Many states also have "below-sales-costs" laws, which make it illegal to sell goods or services below costs if the purpose of such a strategy is to force competitors out of the market to create a monopoly. Price-fixing is sometimes a form of *predatory pricing* and may be determined as such on a case-by-case basis.

Another anticompetitive pricing practice, *resale price maintenance*, occurs when producers make rules that govern the pricing behaviors of wholesalers or retailers of their products. This is done to limit free competition among sellers and keep all sellers reasonably profitable. Resale price maintenance also helps maintain a premium image for some products and might be used to support after-sales customer service. While resale price maintenance is not strictly illegal, it does inhibit free trade.

Unfair Pricing

Unfair pricing practices are also unethical. Unfair pricing techniques are those that involve fraud or manipulation or violate the requirement that fair market exchanges be informed and voluntary. Unfair pricing also exploits buyers in cases of significant time pressure beyond the buyer's control, emotional distress, and lack of information or experience or where the buyer's normal bargaining power is diluted in a situation of emergent need. *Price-gouging* is a form of unfair pricing that is often considered unethical and is sometimes illegal. It occurs when sellers raise the price of scarce goods to the highest price the market will bear regardless of the cost associated with the production of the goods being sold. Price-gouging is often targeted in areas where substitute goods are not readily available. Frequently, price-gouging is also practiced for items in temporary shortage, such as ice during a power outage or temporary lodging after a natural disaster. Generally, sellers who are able to price-gouge enjoy at least temporary monopoly status in the market in which the price-gouging takes place. Many communities have outlawed price increases during emergency situations unless the seller can show demonstrable cause for the price increase.

Deceptive pricing is another form of unethical pricing and occurs when a seller intentionally misrepresents the total cost of an item, makes incorrect comparisons between the seller's price and the prices offered by competitors, or significantly and artificially inflates the asking price of a product or service with the intention of offering a deep discount for the item. In such a case, the bargain received by the purchaser is a false one, unless the original price is one at which the product was offered for a reasonably substantial period of time or a significant number of items were sold for the original price. In another form of deceptive pricing, products or services are sold as a set; buyers are not given an opportunity to purchase each item independently or decline those items for which they have no desire. The buyer ends up paying for items not needed or wanted.

Hidden costs are another type of deceptive pricing, in which the costs of the item are not readily apparent on examination of the item or the accompanying documentation. Undisclosed shipping or handling costs, finance charges, or maintenance fees are some examples of hidden costs. Failure to disclose such costs is illegal in many states and may violate some Federal Trade Commission regulations. In short, deceptive pricing occurs anytime the price of a product or service is misrepresented, is incorrectly compared with the price of a competitor's product, or includes items the buyer does want but is not given the right to refuse or when all costs are not revealed and made explicit to the buyer at the time of purchase.

Manipulative pricing is another form of unethical pricing, in which price points are set to make buyers think the actual price of an item is lower than it really is. Odd-even pricing is one kind of manipulative pricing, wherein an item is priced in such a way that buyers think the item costs less than it really does. For example, a seller might price an item at $9.99 to lead buyers to believe that the price of the item is significantly less than $10.00. In another form of manipulative pricing, sellers allow buyers to purchase goods and make payments over time, in an attempt to make buyers believe the item costs less than it would if paid for in one lump sum. For example, an item might be sold for $50.00, or for five payments of $9.99. The five-payment scheme might confuse buyers into believing that paying for the item in increments is a significant savings over making just one payment. Another form of manipulative pricing involves setting the price of an item and then offering a seeming discount for volume purchases. The seller might price a particular item for $5.00 or two for $9.99. Again, this form of pricing may confuse buyers into thinking purchasing two of the item results in savings, when it really does not.

The Concept of a "Just Price"

Many discussions of the ethics of pricing decisions stem from the idea of the *just price*, an economic concept originated in the 16th century by Dominican theologians at the School of Salamanca. The theory of just price uses concepts of natural law philosophy as the foundation of economic thinking. The just price of an item is the sum of material costs necessary to produce the item plus a reasonable wage that would allow the seller to maintain a lifestyle appropriate to his or her station in life. The just price, therefore, represents the inherent value of the good or service. Just price theory predates capitalist economic thought. Its origins in Spain in the 1500s mean that just price theory is based on certain assumptions about culture and commerce that do not hold true in a free market economy.

First, just price theory assumes that the household, rather than the firm, is the owner of the tools of production and that human labor is the chief source of wealth. Therefore, a just price must compensate the seller for the cost of materials and labor expended in the production of goods. Fair exchange is based on the value of the labor of the seller, which may increase only if the seller's station in life improves. Since this was unlikely in medieval times, the established price for an item rarely changed.

Second, just price theory assumes that people in similar occupations do not trade goods or services with each other and that the value of labor and raw materials does not change due to factors external to the naturally established price.

Third, profit is not a factor in the computation of a just price; in circumstances where production or labor costs decrease, sellers are expected to pass those savings along to buyers.

Finally, the theory of just price has as an underlying principle the assumption that virtuous human conduct is characterized by restraint from extreme action. Thus, a merchant's most virtuous conduct would be to take a moderate stance by holding to the naturally established price for an item.

The four assumptions underlying the just price theory create the following practical implications for its implementation:

1. Sellers may not sell their wares for more than the naturally established exchange price.
2. Sellers may not raise prices to recoup losses due to business downturn or inventory shrinkage.
3. Sellers may not raise prices in times of natural disaster.
4. Sellers may not raise their price for a commodity once it has been established.

While just price theory may have worked in medieval Europe, the degree to which it would be successful in a secular, capitalist economy is unclear. The limitations on seller behavior imposed by just price theory are incongruent with the demands of a free market and would probably impede the efficient allocation of goods. In addition, the inability to earn a reasonable profit would most likely retard long-term economic growth as it would hinder expansion and discourage new competitors from entering the market.

The question of ethics in pricing is best answered by considering the seller's motivation for choosing a particular strategy and the impact the strategy has on stakeholder constituencies. If it is a seller's intention to use pricing as a means of profit maximization regardless of its impact on those who need the product or service, if the intention is to use price to limit the availability of products needed to sustain life, or if pricing is used as a means of forcing competitors out of the market, such motives are likely to be unethical. If, however, the seller's intention is to make needed products and services available to all who need them, and to make a fair living in the process, this would likely be an ethical approach in pricing. Thus, it is not the strategy itself that is ethical or unethical; it is the reasons for choosing a particular strategy and its impact on the market that determine the ethics of the particular pricing approach.

—Cheryl Crozier Garcia

See also Barriers to Entry and Exit; Barter; Collusion; Consumer Fraud; Deceptive Practices; Efficient Markets,

Theory of; Equilibrium; Federal Trade Commission (FTC); Just Price; Natural Law Ethical Theory; Price Discrimination; Price-Fixing; Profits

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Primary Goods

For many, the term *primary goods* refers to John Rawls's use of the term in his book *A Theory of Justice.* In this context, the term was used in reference to distributive justice as the first sort of good one might desire to create well-being (which assists one to live out one's rational life plan). A second meaning also occurs in the literature in those theories that focus on goods needed for action. Finally, there is a third understanding of primary goods as capability. Thus, the three senses are well-being, specific goods attainment, and capability.

Rawls and Primary Goods

Rawls defines primary goods as things that everyone presumably wants, such as rights, liberties, powers, opportunities, income, and wealth. These primary goods are meant to promote well-being. Rawls admits that there are certainly other primary goods (such as health), but they are not at the disposition of society to provide. A theory of distributive justice can only concern itself with that which society can provide.

From this standpoint, Rawls would have us imagine that these primary goods are equally distributed to all in society. Since this egalitarian allocation will not be a stable one, trade-offs will result. Rawls's difference principle is meant to govern such transfers. The difference principle states that social and economic inequalities should be arranged so that they are reasonably expected to be to everyone's advantage and so that they are attached to positions and offices open to all. Thus, with primary goods, all trade-offs that result in inequalities (generally for the sake of economic efficiency) must be structured so that the least advantaged gain from the action. For example, in a business contemplating executive stock options (which will increase the inequality of wages in the company), there must be a direct tie to how the typical line worker in the company (the least advantaged) will also benefit. It is not enough to say that the incentives will make the executives do a better job for stockholder wealth. (This would be the position of Milton Friedman.) The difference principle would require companies to offer line workers the first share in greater profits, either through salary or through contributions to their retirement plans. This is because the difference principle only allows increases in income to the advantaged group so long as the least advantaged are proportionally rewarded as well. This is because the least advantaged must always share in equal fashion whenever a more advantaged group is given more.

The principle behind economic growth implied by the difference principle is that of chain connection. Under chain connection, helping the least advantaged directly by giving them additional primary goods will give a positive upward stimulus to the economy. By giving goods directly to the least advantaged, they will be helped. Also, since the least advantaged will spend this subsidy, there will be a subsequent positive economic stimulus. This positive economic stimulus will be felt throughout the economy. It can be summed up by the maxim "All rise together with the tide." Chain connection is the opposite of trickle-down macroeconomics, which asserts that the way to help the least advantaged is to give tax breaks or other incentives to the rich so that they will invest the money in securities, with the result that businesses will have more money to hire more workers (which will include the poor). The poor under the trickle-down approach are not the proximate but the remote target in economic stimulus.

Another important point to be made about primary goods is that those fundamental liberties are to be shared equally and not bartered or exchanged for other goods. Such liberties include political liberty (the right to vote and to be eligible for public office), freedom of speech and assembly, liberty of conscience and freedom of thought, freedom of the person, the right to own property, and freedom from arbitrary arrest and seizure. Primary goods such as the use of one's time, talents, and income are the only goods eligible for barter. The others (basic liberties) are sacrosanct. Thus, the primary goods eligible for exchange must be carefully monitored by application of the distribution principle so that the macroeconomic strategy of chain connection comes about.

The Second Approach: Primary Goods and Action

The second approach to primary goods can be seen from the vantage point of the foundations of action. This understanding of primary goods can be found in the writings of Alan Gewirth and Michael Boylan. Under this approach, the question becomes, Which goods permit fundamental action? Gewirth takes a rather general view of what these goods might be by classifying them as goods of freedom and well-being at the basic level (most fundamental but unspecified), the nonsubtractive level (less fundamental but specified as those goods one already possesses), and the additive level (the least fundamental but specified as those goods one wishes to possess.) Boylan's approach is similar in that the goods sought are those that permit action (which is assumed to be the primary human need). However, the significant difference is that Boylan offers a table of actual goods (such as food, clothing, shelter, and protection from unwarranted bodily harm) that are set in categories from the most fundamental to action to the least. The point is that when there is a conflict between claims for competing goods of agency, society has a duty to provide goods to the claimant that are more fundamental. Thus, if wealthy citizens want a tax cut directed to them so that they might buy more luxury goods or increase their passive investment income (excess discretionary spending) but the consequent would be lower spending on food programs for the very poor, then the claims of the poor trump those of the rich because the good they desire is more proximate to the fundamental conditions of action (compare this also with Henry Shue). In the action theory approach, primary goods still find a way to affect public policy, but the justification is somewhat different from Rawls's (though the policies advocated may be very similar).

The Third Approach: Primary Goods and Capability

The third kind of primary good allocation strategy is to enhance the capability for action. This is the strategy proposed by Amartya Sen. Instead of focusing on the goods themselves, Sen is thinking about capability for action. An example of this is when one person is not eating because he is fasting and another person is not eating because he has no food at all. Both individuals lack food (a primary good). But the first lacks it by choice: He is choosing to fast. He could also choose to end the fast at any time. In the latter case, an individual lacks a primary good and has to find a way to obtain it or die.

It is Sen's conjecture that public policies on the inequality of goods distribution are all wrong. What we really should be thinking about is how to enhance the capability sets of individuals so that they might realize the sort of life that appeals to them (also known as a rational life plan). How do we go about finding ways to increase the capability sets within a society? Look at cultural/political amalgamations that work. Some of these are not directly tied to money or material goods. If one judges contentment by mortality rates, then a country such as Costa Rica, which has a fraction of the per capita income of the United States yet virtually the same mortality rate, is a success. Institutions such as free and available health care and gender and minority rights may be two examples of policies that encourage the creation of robust capability sets. In this way, primary goods are to be seen as powers or capacities rather than actual specific goods themselves.

—Michael Boylan

See also Affirmative Action; Agency, Theory of; Business, Purpose of; Capabilities Approach; Consumer Goods; Cost-Benefit Analysis; Equality; Kant, Immanuel; Rawls, John; Social Contract Theory; Social Ethics

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PRISONER'S DILEMMA

Prisoner's dilemma is a term used to describe certain types of non-zero-sum situations in game theory where rational self-interested individuals make choices that lead to suboptimal results. Many games are zero sum in that a positive result for one side (+1) will result in a loss (−1) for the other (+1, −1 = 0). In a prisoner's dilemma, however, the outcome is often negative for both parties. Economists, mathematicians, and psychologists, among others, use game theory to observe and predict the choices that people will make when faced with various outcomes. The games involve each player having preferences and choices about the outcomes. They have information about the options open to the other party but do not know exactly how they will behave. The outcomes are not fixed but depend on the choices the players make. Two-player games of this type are useful because they provide objective quantitative data about rational choices under variable conditions.

The name *prisoner's dilemma* came about from a story developed in 1950 by the mathematician Albert Tucker, who was trying to explain a problem that arises in games developed by his colleagues Merrill Flood and Melvin Dresher as part of their work for the RAND Corporation. The narrative varies in its particulars but sets up a paradoxical dynamic where individual benefits are balanced against mutual gain. Classically, two suspects are separated, and then the interrogator who has sufficient evidence for a minor charge makes a proposition to each suspect separately: Whoever confesses first and implicates the other will get a plea bargain and a small fine, while the accomplice will face the harshest charge possible and a consequent long sentence. Each suspect gets to think about the deal and slip a note under the jail door by morning. This dilemma leaves the individual with two distinct choices, to confess or to keep quiet, but the outcome depends on what the other person does. If one keeps quiet, that person will only do well if the other suspect remains quiet as well; if the other person confesses, the nonconfessor will end up in prison for a long time. Each prisoner reasons that he or she is better off confessing irrespective of what the partner does. Yet paradoxically the best mutual outcome would result from not confessing. Central to the dilemma is the fact that the actors have to operate in the absence of full information and trust. Left to ponder what is in one's personal best interest, each prisoner's best rational choice (called an "equilibrium") is to minimize the risks posed by the various options and confess as quickly as possible.

The dilemma is often represented graphically, with rows representing the choices of one party and columns the choices of the other (see Table 1). Thus, if one confesses while the other keeps quiet, the result would be that the one who kept quiet has a significant negative outcome, whereas the confessor benefits. Similarly if both confess, then there is a negative result for both.

The setup means that both parties will have a common set of individual preferences. Often the choices are given the more value-laden terms "cooperation" (c) and "defection" (d). The best individual ranking of payoffs would be confession when the other is silent (d/c), followed by mutual silence (c/c), then mutual confession (d/d), and finally, keeping quiet while being implicated by the partner (c/d). Still, both prisoners are reasoning the same way at the same time, with the result that as a group they are worse off than if they could have cooperated more. The game thus leads to an outcome that is Pareto suboptimal. In other words, there are other choices that the players could have made that would have left both better off without either being made worse off.

In game theory terms, the rational dynamic that leads the players to choose as they do is known as a *dominant strategy.* Anyone faced with the dilemma is forced to choose what to do regardless of the other person's choice, and in this case it makes the most sense to confess in the absence of full information. The game is also *symmetrical* in that both parties are given identical choices and are aware of each other's preference ordering.

Business and Daily Life

Once we recognize the dilemma, we can see it in business and in everyday life, from nuclear disarmament treaties to gas pricing at stations across the street from each other. For example, most airlines would like to get rid of their frequent flyer programs, which reward travelers with free seats at given reward levels and thus deprive the airlines of potential revenue. However, it is illegal for the airlines to collude, and therefore, they have to make moves in the market that make assumptions about the way their competitors will behave. If all airlines simultaneously abandoned their frequent flyer programs, they would all be better off. However, if one announces that it is going to, the others are faced with the choice of doing so as well (cooperating) or capitalizing on the market opportunity to make short-term gains (defecting). So although they would all be better off dropping the programs, in the absence of full trust and knowledge about the future behavior of others, none is willing to make the first move.

Another everyday example is where traffic flows in a single direction on a two-lane highway. If one of the lanes is blocked due to roadwork, signals advise motorists to merge to form a single lane. Drivers then have the choice to either slow down and allow cars in the blocked lane to merge gradually or race ahead and cut in at the front. It would be mutually beneficial for all motorists to have a slower but constant flow of traffic; but if there is any suspicion that someone will not cooperate, then the drivers are faced with the choice of enduring the consequent stop-and-go traffic caused by the defector or becoming defectors themselves. Similarly, there will be a temptation for political rivals to implement a negative campaign that attacks the other side even though both realize that they would both benefit from not doing so.

The prisoner's dilemma is especially prescient in analyzing cases where there is a limited resource held in common but there are incentives for individual gain at the cost of the general welfare, such as exploiting the environment. Thus, we can see that if fishing grounds are depleted, it makes sense for everyone concerned to agree to wait until they have a chance to replenish. At the same time, there are potentially huge rewards for someone who defects from the agreement. If everyone thinks the same way, then it will be rational, if not moral, to defect from a ban on fishing.

Table 1 A Prisoner's Dilemma

	Confess	*Keep Quiet*
Confess	−3, −3	0, −6
Keep quiet	−6, 0	−1, −1

Preference Ordering

The prisoner's dilemma is a form of *mixed motive* game in that the preference orderings can be adjusted so that it is not always in someone's best interest to cooperate or defect. In the classic case above, the order is d/c > c/c > d/d > c/d, where ">" represents the preferred outcome. Other orderings have been given individual labels too. The sequence d/c > c/c > c/d > d/d represents the game of "chicken" made famous by teen movies in the 1950s. Opposing parties engage in a destructive course of action, such as driving cars toward each other, and the winner is the one who steers away (cooperates) last. The best outcome is to stay on track while the other car swerves away. However, there are no rewards and a huge downside if no one veers and a crash occurs. This game of chicken is the sequence set up by brinksmanship or hardball bargaining in business. There are great benefits if one side can cause the other to cave in, but if both act in the same adversarial way, then they are likely to lose out on a potentially profitable deal and spoil their future relationship at the same time. Lengthy labor strikes reflect this outcome.

The order c/c > d/c > d/d > c/d is sometimes called a stag hunt, after a story from Rousseau. Here, people are engaged in a cooperative enterprise that none could succeed at individually. However, if a smaller reward presents itself to one of the participants—such as an easily caught rabbit—the temptation is to abandon the team project and go for the surer reward. Again, if everyone behaves similarly, then they are all better off seeking their own pickings, but the worst outcome is to be operating for the benefit of the team when everyone else is out for themselves. This case illustrates what happens when a group project lacks strong unanimity of purpose or lack of trust in the ultimate outcome.

So far, the games described have been symmetrical and one-time choices. Considerable research has gone into studying the effects of changing these variables. The payoffs may be adjusted, and sometimes each party will have a different preference order. For example, if one party were very rich so that the marginal utility for the profit and loss would be relatively less than it would be for a poorer player, the situation allows the rich side to play chicken since it could accommodate a mutually unfavorable result, whereas the poorer player has a traditional prisoner's dilemma ordering.

Other factors may affect the way the prisoner's dilemma is played. Conditions may be relaxed so that the parties may confer, for example. Although communication sometimes increases cooperation, it also gives players the opportunity to set up sham agreements and lie to each other.

Iterated Games

If we imagine our prisoners pondering what to do, it will make a difference if they have dealt with each other previously. In repeated (or iterated) games, where the payoff matrix is known, certain strategies will emerge as being more successful over time. Robert Axelrod has run a number of computer versus computer games, and it turns out that when players can punish each other through defection or, alternatively, reward each other through cooperation, the most successful strategy is the one labeled "tit for tat" (TFT), whereby one initially cooperates with and then reciprocates the move made by the other party. Axelrod describes the program as nice in that one is never the first to defect, retaliatory in that it penalizes defection, forgiving in that it does not aim to punish beyond the move at hand, and clear insofar as its strategy is very explicit. In computer tournaments (more than 120,000 moves), TFT survived better than any other program.

The prisoner's dilemma itself is a rational exercise, and therefore, the lessons we draw from it will be prudential but not necessarily moral. The research implies that over repeated encounters, each side will be better off cooperating rather than seeking short-term gain. Trust and reputation have considerable benefits because they will allow parties to reach optimal solutions instead of defaulting to behavior that focuses solely on defensive postures. These insights can certainly be used to develop a practical ethics and have been used to explain the development of altruism when a population is self-interested.

Unlike computers, humans bring a range of emotions and psychological drives that often make their actions subrational in a technical sense. Individuals often bring a desire to do better than the other side no matter what the cost (the so-called auction dynamic), a desire for vengeance, a need to maintain a notion of personal integrity (e.g., never to squeal or defect even in the face of considerable incentives), or numerous other factors that influence play. This reality leads some commentators to suggest that corporations with clear mandates may be more rational than humans. However, this logic suggests that corporations may just be strategic players, with an expedient egoistic morality.

The prisoner's dilemma and similar games are necessarily artificial and do not represent the full richness of human interaction. Nevertheless, by paring down complex issues into straightforward choices, they provide useful quantitative data for many areas of social science research.

—Kevin Gibson

See also Altruism; Auction Market; Decision-Making Models; Equilibrium; Free Riders; Game Theory; Marginal Utility; Nash Equilibrium; Negotiation and Bargaining; Prudence; Reciprocal Altruism; Rousseau, Jean-Jacques; Tragedy of the Commons

Further Readings

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PRIVACY

Privacy is a surprisingly obscure and disputed value in contemporary society. With the tremendous advances in technology alone, calls for greater protection of privacy have increased in recent decades. Yet there is widespread confusion concerning the nature, extent, and value of privacy. Some Western countries, for example, do not acknowledge a legal right to privacy as recognized within the United States, while others, such as New Zealand and Australia, are sophisticated in their centralized and consistent approaches to personal privacy issues. Even within the United States, there is significant disagreement about privacy. The U.S. Constitution, for example, makes no mention at all of a right to privacy (though it also neglects to mention other rights, such as the right to marriage), and the major Supreme Court decisions that have relied on a fundamental right to privacy, *Griswold v. Connecticut, O'Connor v. Ortega*, and *Roe v. Wade,* remain highly contentious and controversial. The strongest arguments in favor of the right to privacy stem instead from the Fourth Amendment protection from unreasonable searches and seizures and from the omission of privacy from the rest of the Constitution and the inclusion of the Ninth Amendment, which explains that the enumeration of certain rights does not deny the remaining rights, and the Tenth Amendment, which provides that powers not given to the government are reserved to the people.

Two general understandings of privacy can be found in the legal and philosophical literature on this topic: privacy as the right to be left alone within a personal zone of solitude and privacy as the right to control information about oneself. Each interpretation can be problematic, but each has important implications for business. It may be considered unreasonable by employers for a worker to expect to be left alone in the workplace, so the first interpretation may pose conflicts in business ethics. Likewise, though the Supreme Court's decisions define privacy according to the latter interpretation, employers may be entitled to a good deal of information about employees. Establishing the proper limits of privacy, including drawing the line between the personal and the public at work, is a significant challenge in connection with business ethics.

Before turning to some of these more specific issues, however, it would be first worthwhile to consider the connection between these two senses of privacy. Certain decisions that one makes about how one lives one's life, as well as the control of personal information, play a crucial role in defining personal identity. Privacy is important because it serves to establish a boundary between individuals and thereby serves to define one's individuality. The right to control certain very personal decisions and information helps determine the kind of person one is and the person one becomes. To the degree that one values individuality and the distinct and individual treatment of others, one ought to recognize that certain personal decisions and information are rightfully the exclusive domain of the individual.

Specifically in connection with privacy, ethical issues arise in the process of gathering information, assessing its accuracy, correcting it, and disclosing it, as well as in connection with the substance of the information itself. The simple awareness that others have personal information about them may feel to some invasive or violating. For that amorphous reason, privacy is a slightly difficult concept to define and includes the ability to control what others can find out about you. Why do we care that someone has our personal information? We can imagine items of personal data that we simply do not want others to know, notwithstanding whether they would actually do something with that information. We do not like people knowing things about us; it comes down to one's ability to be autonomous in controlling one's personal information.

Do you care about the information that others have about you? Should you care if your boss knew of all of your off-work activities? Consider Milton Hershey. Milton Hershey would tour Hershey, Pennsylvania, making note of workers' lawns that were not kept up or homes that were not maintained. He would even hire private detectives to find out who was throwing trash in Hershey Park. Another business owner, Henry Ford, used to condition wages on workers' good behavior outside the factory. He had 150 inspectors in his Sociological Department to keep tabs on workers' hygiene habits and housekeeping.

Privacy Issues Unique to Information Technology

Information technology provides us with a host of ethical challenges. New technology imposes new implications for the balance of power in the workplace. For some time, we have had in-home offices, allowing for greater invasions. Moreover, the line between personal and professional lives has become blurred as workers conduct personal business in the office and professional business at home. The office usually provides faster, cheaper, and easier access to the Internet, while some work must be done at home to be completed according to our modern, technologically enhanced pace.

The privacy implications of both these blurred lines and the advancing technologies at work are monumental. Should the technological ability to find something out make it relevant? With new employee-testing technology, employers can obtain all sorts of personal information. Through genetic testing, hair follicle testing, or drug testing, employers can find out anything they want to know about their employees. But with the ability to do something comes a responsibility to do it ethically. Should an employer obtain the information simply because it has the ability to do so?

Legislation of Privacy

Georgia was the first jurisdiction whose courts recognized a common-law right to privacy. The court in *Pavesich v. New England Life Ins. Co.* justified its conclusion by finding a right of privacy in natural law, recognized by municipal law, inferred from expressions used by commentators and writers on the law as well as judges in decided cases, and embraced within the absolute rights of personal security and personal liberty. Though some states rely on statutory protections rather than common law, only two states—North Dakota and Wyoming—fail to recognize *any* of the four privacy torts generally accepted by the courts. Other states that provide constitutional recognition and protection of privacy rights include Alabama, Arizona, Florida, Hawaii, Illinois, Louisiana, Montana, South Carolina, and Washington. However, in all states except California, the application of this provision to private sector organizations is limited, uncertain, or not included at all.

Federal Legislation

More than 100 bills on privacy protection have been introduced in Congress, but only one on the collection of personal information from kids on the Internet has been approved. For an extended period of time, the White House only supported privacy protections related to medical information, because they believed that this type of uncertainty will dissolve as firms and employees become more comfortable with the medium.

The Privacy for Consumers and Workers Act (PCWA), proposed first by another name in 1989, then again in the 101st, 102nd, and 103rd Congresses, was finally debated by the Subcommittee on Labor-Management Relations in 1993. The bill was revised and eventually approved by the House Education and Labor Subcommittee, though the 103rd Congress failed to pass it. The bill provided some additional mandates for adequate notice of when the employee is being monitored on the job. This would have been a critical requirement since adequate and effective notice may remove an employee's reasonable *expectation* of privacy, and some intrusions may be acceptable once notice has been given. On the other hand, in other situations, even the best form of notice does not transform a wrongful intrusion.

The PCWA sought to find a balance between the employer's desire to maintain quality and the employees' (and consumers') expectations of privacy in their communications. Specifically, the act also provided that workers who had been employed for less than 60 days could be monitored periodically or randomly without notice or limitation, while employers would be required to provide notice of periodic or random monitoring to workers from that time until they had been employed for 5 years. Once a worker had been employed for 5 years or more, periodic or random monitoring would be completely prohibited. In addition, employers could not disclose information obtained through monitoring. Notwithstanding the amount of time an individual had worked for a firm, monitoring would be capped by the PCWA at 2 hours per week.

Some researchers contend that adequate universal information privacy safeguards can only be achieved by the enactment of public policy legislation by the Congress and the president. David Linowes, former chairman of the U.S. Privacy Protection Commission, contends that appropriate and effective legislation would require that (1) there be minimum intrusiveness into the personal affairs of an individual, (2) fairness be emphasized (therein including disclosure), and (3) there be a means for confidentiality when information privacy is expected.

The Electronic Communications Privacy Act of 1986 (ECPA) is also relevant to this analysis as it prohibits the "interception" or unauthorized access to stored communications. However, its impact is to punish electronic monitoring by third parties rather than employers, since courts have ruled that "interception" applies only to messages in transit and not to messages that have actually reached company computers. In addition, the ECPA allows interception where consent has been granted. Therefore, a firm that secures employee consent to monitoring at the time of hire is immune from ECPA liability.

Other U.S. statutes related to the protection of privacy are as follows:

- Cable Communications Policy Act
- Children's Online Privacy Protection Act
- Customer Proprietary Network Information Electronic Communications Privacy Act
- Fair Credit Reporting Act
- Family Education Rights and Privacy Act
- Federal Trade Commission Act
- Gramm-Leach-Bliley Act
- Health Insurance Portability and Accountability Act
- Identity Theft Assumption and Deterrence Act
- Privacy Act
- Right to Financial Privacy Act

Given the nature of the legal uncertainty or instability with regard to these challenging areas of information gathering, one finds that perhaps the only source to which one should look for an answer is ethics. Yet Professor John Haas from the University of Notre Dame reminds us that we remain vulnerable to a plethora of dangers when the development of our moral systems is not able to keep pace with technological and medical developments. Even the courts recognize this dilemma when they deal with new challenges, such as in *State of Washington v. Young*, where the court reviewed the legitimacy of police use of infrared thermal detection devices aimed at an individual's home without a warrant or notification. The court held that subjective expectations of privacy may be unconsciously altered when affected by the fast-paced changes in technology. The court in that case cautioned that our decisions should reflect thoughtful and purposeful choices rather than simply mirror the current state of the commercial technology industry.

Constitutional Protections

The Fourth Amendment to the U.S. Constitution protects the right of people to be secure in their persons, houses, papers, and effects, against unreasonable searches and seizures. This protection implies a reasonable expectation of privacy against intrusions *by the state, only.* As this provision of the Constitution does not apply to actions by private sector employers, their employees must rely instead on state-by-state laws and the common law made and accepted in the courts. A similar limitation exists in connection with the First Amendment's protection of personal autonomy and the Fifth Amendment's protection against self-incrimination—each of these only protects the individual from invasions by the state. Currently, employment-related privacy legislation that would apply to private sector employers has been proposed in several states, but those states fall in the distinct minority.

What the courts will generally consider in cases involving both the Fourth Amendment and common-law privacy protections is (a) whether the employer has a legitimate business interest in obtaining the information and (b) whether the employee has a reasonable expectation of privacy. Several examples of common-law actions by the courts are illustrative of the courts' attempts at creating this balance, but perhaps more significant are the settlements reached by firms concerned about the *prospect* of a judge's decision.

Common-Law Protection of Privacy

Supreme Court Decisions

One of the first cases to designate a right to privacy was *Union Pacific R. Co. v. Botsford*, decided in 1891. In that case, the court established the inviolability of the person, though it did not base the decision on its constitutionality but instead on privacy as a sacred right, carefully guarded by the common law, defined as the right of every individual to the possession and control of his or her own person, free from all restraint or interference of others unless by clear and unquestionable authority of law. Again, in 1928, in a dissenting opinion in *Olmstead v. U.S.*, Supreme Court Justice Brandeis identified the right to privacy as the core value in American life.

Constitutional protection of the right to privacy was most clearly and articulately established by the Supreme Court in the 1965 case of *Griswold v. Connecticut*, where the Court was asked to determine whether the Constitution protects marital privacy in connection with a couple's ability to be counseled in the use of contraceptives, where a state restriction against such counseling exists. The Court in this landmark case held that though the Constitution does not include a specific right to privacy, the Bill of Rights created zones of privacy. The Court found that the First, Third, Fourth, and Ninth Amendments created the right to privacy in marital relations. Since the Connecticut statute conflicted with the exercise of this right, the statute was declared null.

In 1973, the Court heard the now well-known case of *Roe v. Wade*, in which a pregnant single woman challenged a state statute prohibiting abortions except in cases where the mother's life was threatened. Roe argued that the statute violated the Due Process Clause of the Fourteenth Amendment, which protects against state action the right to privacy, including a woman's qualified right to terminate her pregnancy. In that case, the Court recognized that the state may have legitimate interests in protecting both the pregnant woman's health and the potentiality of human life and thereby needed to define that "potentiality." The Court then balanced these competing interests and designed a response based on the chronological progression of the fetus.

In 1987, the Court determined the case of *O'Connor v. Ortega*, which involved supervisory searches of public employees. It was this case that established the "reasonable expectation of privacy" standard for application throughout public sector workplaces and, by inference, also established the boundaries of protection for private sector employees. In addition, the expectation of privacy in the public sector workplace, according to the Court, was to be balanced with the particular circumstances of each case, the government's need for supervision and control, and the expectations of the employees involved.

Additional Judicial Decisions

Case law recognizes the tort of intrusion into seclusion, which finds liability when one intentionally intrudes on the private affairs of another if the intrusion would be highly offensive to a reasonable person. As we begin to live more closely with technology, and the intrusions it allows, the concept of reasonableness under this formulation becomes tenuous. Additional state-by-state protection through regulation often focuses on online privacy to the exclusion of workplace privacy, though related legislation has been proposed in several states.

In one case, two McDonald's restaurant employees used voice mail to transmit love messages during an affair. They believed that these messages were private since the firm had told them that only *they* had the access codes. The franchise owner monitored the voice mail messages and later played messages for the wife of one of the workers. The lovers sued for invasion of privacy. They settled for several million dollars, so we do not yet have any judge's decision in a situation like this. In another case that never made it to the courts, the Minnesota attorney general sued several banks for revealing personal information about clients to marketers in exchange for more than $4 million in fees. One bank eventually agreed to pay attorney's fees plus $2.5 million to Habitat for Humanity.

While the law has not yet settled in connection with monitoring or the privacy of obtained information, hence the settlements, monitoring does seem justified by several cases where e-mail was later used as evidence to encourage a settlement. Within the past several years, several large firms, including R. R. Donnelly, Morgan Stanley, and Citicorp, have found that cases often hinged on e-mail transmissions that people originally thought had been deleted. In one case, this included an e-mail containing 165 racial, ethnic, and sexual jokes sent to the entire firm. In another, the e-mail included sexual jokes about why beer is better than women. Had the firms enforced stringent policies about the use of e-mail and monitored to enforce these policies, perhaps these e-mails would never have been sent.

The *New York Times* also found itself with some problems. They fired 24 employees at a Virginia payroll processing center for sending inappropriate and offensive e-mail in violation of corporate policy. The public sector is not immune to similar challenges: The U.S. Navy reported that it had disciplined more than 500 employees at a supply depot for sending sexually explicit e-mail. It happens all the time, and it is continuing to happen.

In cases where the courts have been able to address the issue, it seemed at first that notice of monitoring might emerge as the critical factor. Perhaps persuaded by early case law, of the 67% of mid- to large-size firms that monitor, 84% notify their employees of this activity. Notice might range from a one-line comment in the middle of an employee manual that someone receives on the first day of work to a dialogue box reminding you that e-mail may be monitored that pops up each time you hit the "send" button to transmit an e-mail.

Many court decisions seem to depend on whether the worker had notice that the monitoring might occur. Since the basis for finding an invasion of privacy is often the employee's legitimate and reasonable expectation of privacy, notice of monitoring would remove that expectation. This conclusion was supported in *K-Mart v. Trotti*, where the court held that search of an employee's company-owned locker was unlawful invasion since the employee used his own lock.

The basis for the decision was that the employees were left with the legitimate, reasonable expectation of privacy because they used their own locks. On the other hand, an employer's search of employee lunch buckets was held reasonable by another court only 2 years earlier.

In a later 1990 case, *Shoars v. Epson*, Epson won a suit filed by an employee who complained about e-mail monitoring. In that case, the court distinguished the practice of *intercepting* an e-mail transmission from *storing and reading* e-mail transmissions once they had been sent, holding that the latter was acceptable. In a 1992 action, Northern Telecom settled a claim brought by employees who were allegedly secretly monitored over a 13-year period. In this case, Telecom agreed to pay $50,000 to individual plaintiffs and $125,000 for attorneys' fees.

Similarly, an employee-plaintiff in a 1995 federal action won a case against his employer where the employer had monitored the worker's telephone for a period of 24 hours to determine whether the worker was planning a robbery. The court held that the company had gone too far and had insufficient evidence to support its claims. One might therefore conclude that if an employer adequately notifies workers that it will conduct monitoring, it has effectively destroyed any reasonable expectation of privacy on the part of the workers. It would now be *unreasonable* to expect privacy since one is told not to expect it. However, in a case where the alternative extreme was true, where a firm notified workers that it would *not* monitor, the court did not follow congruent logic. It did not find a reasonable expectation of privacy based on a firm's pledge not to read e-mail.

In this case, *Smyth v. Pillsbury*, Smyth sued the firm after a manager read his e-mail. At the time, Pillsbury had a policy saying that it would not read e-mail. One might presume that this policy should have created a reasonable expectation of privacy. But instead, this was the first federal decision to hold that a private sector, at-will employee has no right of privacy with respect to the contents of his or her e-mail when it is sent over the employer's e-mail system. The court found that there is no reasonable expectation of privacy in the contents of e-mail communications voluntarily made by an employee to his or her supervisor over the company's e-mail system, notwithstanding any assurances that such communications would not be intercepted by management. The end result of *Smyth,* then, is to allow for monitoring even when a firm promises not to monitor. Evidence of the impact of this decision is the fact that only one state, Connecticut, requires employers to notify workers when they are being monitored.

In an Arizona case, a husband and wife who worked as nurses were fired from a hospital after hospital officials learned that they ran a pornographic Web site when not at work. The couple explained that they engaged in this endeavor to save more money for their children's college education and that it would be irrelevant to their employer. Though their dismissal attracted the attention of the American Civil Liberties Union for what it considered was at-will gone awry, the nurses had no recourse. In another case, a police officer was docked 3 days' pay when his wife posted nude pictures of herself on the Internet as a surprise to her husband. However, the pay suspension was justified by the department in that case since police officers could arguably be held to a higher standard of conduct than average citizens.

Courts have often supported reasonable monitoring of employees in open areas as a method of preventing and addressing employee theft. For example, in *Sacramento County Deputy Sheriff's Ass'n v. County of Sacramento*, a public employer placed a silent video camera in the ceiling overlooking the release office countertop in response to the theft of inmate money. The California Court of Appeals determined that the county had engaged in reasonable monitoring because employee privacy expectations were diminished in the jail setting.

The facts of any particular case might determine and thereby explain its outcome. For instance, in a 2005 case, *U.S. v. Hill*, the Eighth Circuit found against an individual who claimed that he had a reasonable expectation of privacy in a convenience store bathroom where he had locked the door. On the surface, this ruling might seem of concern to the average person using a store bathroom. However, that perception might change when one learns that the individual went in there with a member of the opposite sex; that there was no response when police knocked on the door; and that they then picked the lock on the door and found the individual half dressed and with illegal narcotics all around him. The court found that since he was in the restroom with another person, was using the restroom for a purpose other than its intended use, and did not exit the restroom after having been asked several times, without any excuse (such as illness), any expectation of privacy that he might have enjoyed when he first entered the restroom had expired by the time the police arrived.

Privacy: Additional Issues Specific to the Workplace

As in other areas of lightning quick advances, the law has not yet caught up with the variety of ways in which an employer can now gather information about employees. While the law might be clear with regard to tapping a worker's telephone, it has taken longer to find that clarity with regard to monitoring a worker's e-mail or text pages on a handheld device. Employee monitoring in the private sector workplace is generally governed by state legislation and case law precedent. (As mentioned above, the Fourth Amendment protection against an unreasonable search and seizure governs only the public sector workplace through the Constitution's application only to state action.)

As discussed above, case law is not yet conclusive with regard to many workplace privacy issues. It becomes all the more critical to maintain this patchwork regime of privacy protection in the workplace when one considers the implications of the European Union's (EU's) Personal Data Protection Directive. In addition to striving to harmonize the various means of protecting data throughout the EU, the directive also prohibits firms in the EU from transferring personal information to a non-EU country unless that country maintains adequate protections of its own. In fact, the United States would not qualify as having adequate protection, so the Department of Commerce negotiated a Safe Harbor exception for firms who maintain certain protections of information within their possession. If a firm satisfies these requirements, the directive allows the information transfer. If not, both firms can be held liable. The Safe Harbor requires that the receiving firm provide

- Clear and conspicuous notice
- A choice to opt out
- Onward transfer only to firms with adequate protections
- Reasonable measures to ensure reliability and protection from disclosure or loss
- Processing of only information relevant to the purpose for which it was gathered
- Access by data subject and the ability to correct misinformation
- Mechanisms for ensuring compliance and consequences for noncompliance

Of course, these issues are not limited to the United States. The Global Business Privacy Project has identified seven major developments of importance to businesses in connection with cyberethics:

1. The European Union Privacy Directive
2. The commencement of an international privacy standards process
3. New national and global information flows
4. Information superhighway initiatives
5. Model business principles for global businesses
6. New information technology applications
7. New global interest in fashioning consumer data protection laws

Privacy Rights Since September 11, 2001

The United States has implemented widespread modifications to its patchwork structure of privacy protections since the terror attacks of September 11, 2001. In particular, proposals for the expansion of surveillance and information-gathering authority were submitted, and many, to the chagrin of some civil rights attorneys and advocates, were enacted.

The most public and publicized of these modifications was the adoption and implementation of the Uniting and Strengthening America by Providing Appropriate Tools Required to Intercept and Obstruct Terrorism (USA PATRIOT) Act of 2001, Pub. L. No. 107-56. The USA PATRIOT Act expanded states' rights with regard to Internet surveillance technology, including workplace surveillance and amending of the Electronic Communications Privacy Act in this regard. The act also grants access to sensitive data with only a court order rather than a judicial warrant, among other changes, and imposes or enhances civil and criminal penalties for knowingly or intentionally aiding terrorists. In addition, the new disclosure regime increased the sharing of personal information between government agencies to ensure the greatest level of protection.

Title II of the act provides for the following enhanced surveillance procedures, among others, which have a significant impact on individual privacy and may affect an employer's effort to maintain employee privacy:

- Expanded authority to intercept wire, oral, and electronic communications relating to terrorism and to computer fraud and abuse offenses
- Roving surveillance authority under the Foreign Intelligence Surveillance Act of 1978 (FISA) to track individuals (FISA investigations are not subject to Fourth Amendment standards but are instead governed by the requirement that the search serve "a significant purpose")
- Nationwide seizure of voice mail messages pursuant to warrants (i.e., without the previously required wiretap order)
- Broadening of the types of records that law enforcement may obtain, pursuant to a subpoena, from electronic communications service providers
- Permission of emergency disclosure of customer electronic communications by providers to protect life and limb
- Nationwide service of search warrants for electronic evidence

Pursuant to these provisions, the government is now allowed to monitor anyone on the Internet simply by contending that the information is "relevant" to an ongoing criminal investigation. In addition, the act provides anti-money-laundering provisions designed to combat money-laundering activity or the funding of terrorist or criminal activity through corporate activity or otherwise. All financial institutions must now report suspicious activities in financial transactions and keep records of foreign national employees while also complying with the antidiscrimination laws discussed throughout this text. It is a challenging balance, claim employers.

Though some of its surveillance and information-sharing provisions were set to expire (or "sunset") in 2005, the USA PATRIOT Act was not the only legislative response. By September 2002, the Office of Management and Budget had recorded 58 new regulations responding to terrorism, and both federal and state agencies have passed a number of new pieces of legislation. Not everyone is comfortable with these new protections. Out of concern for the USA PATRIOT Act's new permitted investigatory provisions, some librarians now warn computer users in their libraries that their computer use could be monitored by law enforcement agencies. The *Washington Post* reports that some are even ensuring privacy by destroying records of sites visited, books checked out, and logs of computer use. The American Civil Liberties Union reports that a number of communities have passed anti–USA PATRIOT Act resolutions.

Employers have three choices in terms of their response to a governmental request for information. They may

1. voluntarily cooperate with law enforcement by providing, on request (as part of an ongoing investigation), confidential employee information;
2. choose not to cooperate and ask instead for permission to seek employee authorization to release the requested information; or
3. request for a subpoena, search warrant, or FISA order from the federal agency before disclosing an employee's confidential information.

—Laura P. Hartman

See also Business Law; Chief Privacy Officer (CPO); Consumer Protection Legislation; Deontological Ethical Systems; Duty; Electronic Surveillance; European Union; Human Rights; Justice, Theories of; Kantian Ethics; Litigation, Civil; Normative Ethics; Rawls, John; Rights, Theories of; USA PATRIOT Act; Working Conditions; Work-Life Balance; Workplace Privacy

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PRIVATE GOOD

A private good is a product or service produced by a privately owned business and purchased to increase the utility, or satisfaction, of the buyer. Most of the goods and services consumed in a market economy are private goods. The prices of these products, such as hamburgers, haircuts, and dental services, are determined to some degree by the market forces of supply and demand. Private goods are both excludable and rivalrous. *Excludability* means that producers can prevent people from consuming the good or service, based on the consumer's ability or willingness to pay. *Rivalrous* means that one person's consumption of a product reduces the amount available for consumption by another.

The absence of excludability and rivalry introduces market failures that ensure that some goods and services cannot be efficiently provided by markets. For example, pure public goods are, by nature, nonexcludable and nonrivalrous. The most often cited example of this type of good is national defense. Pure public goods are nonrivalrous because they can be consumed collectively. For example, a nation's army can protect all its citizens at the same time, and one person's consumption does not reduce the amount available to other consumers. At the same time, it is impossible to exclude any consumers from military protection. This nonexcludability leads to a free rider problem, by which consumers get the benefits of the good or service without paying for it. If left to the devices of private markets, pure public goods will be underproduced or not produced at all because it is not profitable to do so.

Inefficiency in the production and consumption of private goods also arises when there are spillover effects, or externalities. A positive externality exists if the production and consumption of a good or service benefits a third party not directly involved in the market transaction. For example, an individual's education provides a direct benefit to him or her and also provides benefits to society as a whole through the provision of more informed and productive citizens. Private markets will underproduce in the presence of positive externalities because the costs of production for the firm are overstated and profits are understated. A negative externality exists when the production or consumption of a product results in a cost to a third party. Air and noise pollution are oft-cited examples of a negative externality. Private markets will overproduce when negative externalities are present because the costs of production for the firm are understated and profits are overstated.

Social and ethical questions regarding private goods arise in connection with these inefficiencies. In the case of pure public goods, the government becomes the producer, and the level of production is determined through a political process. When externalities are present, policy makers must decide how to correct the markets through mechanisms such as public provision of the good (e.g., public education) or rules, fines, taxes, and the assignment of property rights. Common pool resources, such as pastures or oceans, are similar to public goods to the extent that they are nonexcludable. However, since they are rivalrous, individuals may overuse these resources, resulting in the "tragedy of the commons." A possible solution to overuse is to introduce private ownership or to assign property rights to grazing lands and fisheries.

Issues of fairness and justice also arise with respect to private goods. Excludability implies that consumers will get different amounts of goods and services. If people have a right to basic necessities, such as food and safe drinking water, then complete reliance on private markets is unacceptable, especially when there is wide disparity in the distribution of income. Similar questions arise with respect to other goods and services, such as health care. Those who believe that people have a right to health care maintain that it should be provided by government as a public good. As a private good, health care may be provided more efficiently, but the poor and those without insurance may be unable to afford it. This illustrates the tradeoff between efficiency and equity. In these instances, public policy determines which private goods should become public goods.

—Rebecca Summary and Eleanor G. Henry

See also Economic Efficiency; Economics and Ethics; Efficient Markets, Theory of; Externalities; Free Riders; Managed Competition; Market Failure; Privatization; Property and Property Rights; Public Goods; Tragedy of the Commons

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PRIVATIZATION

Privatization is a public policy decision to reduce the role of the state in the economy. It is a process that transfers control of economic and financial resources from a government to a private sector entity. In the 1990s alone, global privatization receipts totaled $936.7 billion. Among the key industries affected were telecommunications, postal services, electric and gas utilities, airlines, railroads, coal mining, iron and steel manufacturing, and banking. Italy had the largest privatization program, followed by France, Australia, the United Kingdom, Spain, Mexico, and Portugal.

The impetus for privatization stems from evidence that direct state ownership or control of major national industries and companies cannot create adequate economic growth and prosperity for the future. In the former Soviet Union and Eastern Europe, privatization represented the dismantling of the Communist command-and-control economies. For Western Europe, sub-Saharan Africa, and Latin America, privatization was the reversal of earlier nationalization policies following World War II.

Different Meanings of Privatization

Most commonly, privatization transfers control of resources by way of a sale of state-owned assets, such as highways, bridges, ports, airlines, factories, and banks. A sale can be effected by means of an initial public offering or a direct sale to a preselected buyer. Also, a voucher method has been widely used in Eastern European countries, in which governments issued paper claims to citizens to be exchanged for shares or units in a portfolio of companies.

The term *privatization* can have a broader meaning, especially in the United States. Other than in the electric utility industry, the United States has not had a tradition of significant government ownership, so the sale of state-owned enterprises has not been common. The most prevalent means of transferring control from the government to the private sector is outsourcing, or contracting out. For example, when a municipality or a county contracts with the private sector for services such as solid waste disposal, street construction, facilities operations, building repair, or ambulance services, there is a transfer of control, though not a sale, of an economic activity to the private sector.

Privatization also can refer to the deregulation of an industry to improve the competitive environment. Nothing is sold or contracted out, but the government loosens its control on an economic activity and allows the private sector greater freedom to operate. Equally, market liberalization is a means of increasing competitiveness and can be called privatization. It is a way of bringing increased levels of private sector participation into the economy by removing certain barriers to entry. Dropping statutory constraints on private sector health care delivery is an example, and allowing foreign banks to enter a domestic marketplace by removing regulatory impediments is another.

Privatization in Theory

Fundamentally, privatization is justified by the claim that the private sector can achieve economic efficiency levels that are unattainable in the public sector. Efficiencies lead to wealth creation, higher employment, lower consumer prices, improved service, and a better standard of living. Consider two theories that try to explain why the private sector is necessarily more efficient than its public sector counterparts.

First, property rights theory maintains that ownership is an important determinant in the efficiency of a company. Share ownership provides financial incentives to act efficiently because owners are entitled to retain profits, sell shares, and transform the assets of a company. Owners are motivated by self-interest to improve performance in order to derive the highest level of benefit possible. Correspondingly, companies suffer financially if they are not efficient: Falling share prices, inability to raise capital, and, ultimately, bankruptcy can result. Governments are neither motivated by profit nor concerned about bankruptcy; hence, they do not have an incentive to be efficient and wealth creating. Consequently, the private sector rather than the public sector should be the preferred environment for businesses.

Some theorists point to a principal and agent problem. That is, self-interested managers (agents) may focus more on getting high salaries, bonuses, and perquisites than on the interests of shareholders (principals). To ensure that agents discharge their responsibilities, principals monitor their performance through financial reports, independent audits, and oversight by a board of directors. Monitoring can be very costly, so it reduces some of the efficiency gains. The property rights response is to propose the use of mechanisms that align the interests of owners and managers—for instance, using stock options as part of executive compensation.

The second justification for privatization is public choice theory. It implies that governments have their own agency problems. That is, self-interested bureaucrats respond to power, prestige, and perquisites. And self-interested politicians are motivated to act in ways that maintain or enhance their power, such as providing higher than economically warranted levels of service and capital goods to obtain public favor. Finally, coalitions of self-interested voters come together to lobby for legislation that promotes their objectives. None of this is compatible with cost efficiency, and none of these groups have to face market tests such as falling share price, reduced revenues, or bankruptcy.

The persuasive force of the property rights theory rests importantly on the presumption that the marketplace provides the primary standard for assigning value. However, critics argue that governments are not intended to be motivated by profit; indeed, the social contract perspective suggests governments should provide services even where profit and efficiency are not feasible. Examples include national defense, activities to protect minority rights, and utility service in sparsely populated rural areas. In addition, it is maintained that some social services, such as education, health care, waste disposal, and natural resource management, should be assessed by qualitative measures that reflect the common well-being of citizens, not profit or efficiency. Furthermore, the principle that ownership itself holds the primary explanation for economic performance can be questioned. What about other important factors that affect corporate performance, such as regulatory controls, level of taxation, product mix, production capacity, access to capital, leadership, organizational structure, competitive positioning, and economic cycles?

Finally, is ownership per se really so motivating? In a widely held public company, small shareholders have almost no control over, say, setting dividend policy or reorganizing the company. And to the extent that ownership is motivating, it can be mediated by specific situational details. For instance, a retired person living on a modest fixed income could find very demotivating a company's decision to stop paying dividends and reinvest its free cash. Yet all of his or her theoretical property rights still remain.

With respect to public choice theory, the presumption is that what explains behavior is self-interest. Yet we know from our daily lives that family love, loyalty to friends, dedication to social causes, commitment to democratic principles, and much else besides also motivate people. Why, then, it is argued, should we accept such a dim view of elected officials, public servants, and interest groups? Why would the virtues of public service not find some place in their behavior? One author notes the ironic discrepancy between the enlightened self-interest that produces benign results in the marketplace and the seemingly pathological behavior it yields in government.

Privatization in Practice: Benefits and Costs to Society

Many governments have argued that robust privatization programs can yield significant benefits to society. For instance, governments use privatization as a means of generating funds to pay down debt or maintain social programs without raising taxes. In addition, governments can relieve themselves of future financial burdens by transferring enterprises to the private sector that are expected to require ongoing subsidies to cover losses or capital expenditures. Collateral benefits can include improved credit ratings if the proceeds are used to reduce state debt. And for developing countries, eligibility for World Bank loans can be achieved where having a privatization program is a prerequisite.

A second benefit is enhancement of the financial markets. Privatizing state-owned companies through the use of capital markets increases the number of companies listed on stock exchanges, giving investors a greater choice and more inclination to become active in public markets. In turn, market liquidity improves, and this benefits other listed companies by giving them generally greater access to capital. In the case of countries with less developed capital markets, having more listed companies encourages market and regulatory improvements.

Third is the argument that a government can improve its own efficiency by reducing what it manages. By selling state-owned enterprises, it removes them from the political agenda, thereby freeing up time for more pressing public policy matters. Equally, bureaucratic management time and attention are saved.

Fourth, social benefits can be promoted by privatizing entities in a way that achieves widespread ownership. The voucher privatizations in Eastern Europe were intended to promote egalitarianism because even the poor could have ownership. Similarly, wealth redistribution was a British objective in the 1980s. Furthermore, sales to owner-operators could both foster a culture of entrepreneurship and create less dependency on the state.

These potential benefits are not without costs. For instance, some researchers contend that privatization in fact works against the equitable distribution of economic benefits. In certain European privatization programs, the main beneficiaries were allegedly large banks, legal and financial advisers, and management consultants. In addition, a number of former politicians were rewarded with board-level appointments or senior management jobs in privatized companies. Observers of the privatization programs of both Mexico and Chile comment as well on the concentration of ownership that resulted, despite the fact that mechanisms were developed to encourage worker participation in ownership.

The disadvantage of privatization for workers is often cited as a cost, especially for less skilled workers, who are vulnerable to wage cuts or job loss. For example, after Brazil sold the Federal Railroad System, service levels improved. However, the 40,000-person labor force was ultimately reduced to 11,500. Significant labor cutbacks also occurred with the privatization of major ports and the steel industry. In rebuttal, it could be argued that such labor reductions demonstrate prior overstaffing and that the cuts will lead to economically healthier organizations.

Privatization can also give rise to important political concerns such as resentment against foreign ownership. This might arise, for example, in a developing country if strategically important assets, such as national television and radio stations, the postal system, and railroads, were sold to foreign corporations.

The debate for and against privatization positions the private sector's ability to deliver economic efficiency and prosperity against societal concerns about inequitable distribution of public goods and harms to the economically and politically least advantaged. Deciding which side to support is complicated by a number of factors that can affect our choice. First, privatization has different meanings. An outright sale of a major state-owned enterprise may have consequences and invite criticism that contracting out for road repair does not. Second, the magnitude of the sale might be important. Selling a national postal system could have implications for national sovereignty and hence raise serious concerns. But selling a small family-run business to its operators would have no national significance and may seem quite benign. Third, assessing the economic and societal merits of privatization requires agreement on what values are to be promoted and on what criteria success will be judged. Sometimes they face off against each other without resolution. Fourth, the circumstances under which a privatization takes place are sometimes crucial to its success and our approval. An initial public offering in a country with a well-developed capital market that achieves a wide distribution of ownership can be highly beneficial. However, sale of a major state asset in a transitional economy to a political friend of the government is not.

Clearly, as with most important public policies, decisions require balancing different social and economic principles, careful consideration of contextual factors, and sound execution.

—*A. Scott Carson*

See also Deregulation; Economic Efficiency; Economic Incentives; Free Market; Globalization; Interest Groups; Justice, Distributive; Nationalization; Outsourcing; Property and Property Rights; Public Choice Theory; Regulation and Regulatory Agencies; Self-Interest; Shareholder Wealth Maximization

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Procedural Justice: Philosophical Perspectives

Procedural justice is a conception of justice that proposes that following certain specified procedures will result in an outcome that is just. Procedural justice typically is employed as the preferred method of settling cases in which parties disagree on the just outcome of conflicting private interests or of conflicting conceptions of the public good.

Among the philosophical issues associated with procedural justice are the clarification of types of procedures; the relation between procedures, outcomes, and related values; and, perhaps most central, the issue of whether or not justice should be conceived of *as* procedural in the first place. In other words, if we know what the outcome should be, as we must to assess it for its justice, why should we be bothered with procedures at all?

Types of Procedures

Among the first questions to be answered in the attempt to find a just outcome to some conflict is which of the available procedures ought to be employed. Even a cursory glance at the history of human conflict reveals a remarkable range of possible procedures by which matters of justice may be settled. This range runs from combat (in which the disputing parties fight for the winnings—justice belongs to the winner of the fight) to chance (in which parties agree to allow luck to determine the outcome—justice follows the flip of a coin). Between these lie a variety of possible procedures that are more morally justifiable because they draw on supporting values, such as equality, merit, or fairness, rather than relying on luck or violence.

A common procedure by which justice may be obtained is bargaining. Bargaining covers those situations in which one of the parties in the conflict offers the other some benefit in exchange for completing some action. The particular benefit offered may be an advantage that the other party seeks or the removal of some threat that the other party dreads. Bargaining is the procedure of choice for most of us when we seek commodities and services or when we contract for employment. In such cases, the offer of advantage comes in the form of an offer to pay a selling price or an offer of salary. Bargaining is also used to settle economic and social conflicts, such as when workers strike for better compensation or when social groups protest for the reformation of discriminatory laws. The threat of strike or of protest represents the disadvantage to be removed at the successful completion of the bargaining process.

An alternative to bargaining is what is often referred to as a "discussion on merit." This procedure is devoid of threats or inducements from or against any party and involves the parties' willingness to deliberate the merits of each other's position. This procedure is noted for its tendency to allow parties to modify their positions in response to the merits of the other's argument. Ideally, even when no party gets all that it wanted or was entitled to, the outcome is such that all parties are satisfied. This last feature is important, since the conflicting parties could use force, coercion, or threats to ensure that the outcome would be closer to their position in the dispute, but they opt not to employ such methods. Discussion on the merits emphasizes rational, reflective discussion by all parties on the respective merit of each position. In this procedure, each party asks itself, "What is the best outcome, even if that outcome is not maximally to my benefit?"

Another frequently employed procedure is contest, understood as a demonstration of relevant abilities. This procedure is most useful in situations in which the dispute is about who is best suited to occupy some position, office, or title. Contest is frequently employed in hiring processes that include a demonstration of ability—giving a lecture to a class for a faculty position, administering medications for a nursing position, operating the bus for a bus driver's position, typing a letter or transcription for a secretarial position. Rather than a discussion of the merit of a party's claim, contest is a demonstration of each party's relevant achievement. As long as each party is aware of the terms of the contest and each undertakes it in the same manner as the others, the outcome is most likely to be seen by disputants as fair.

Another important type of procedure is voting. Voting is among the most justifiable of the procedures and is one that has a fairly long track record of success. It is among the more justifiable procedures, because of the related values: (1) *equality,* especially when each party has one vote; (2) *fairness,* especially when each party is not coerced and has access to all relevant information; (3) *liberty,* especially when parties are free to vote as they wish or even withhold their vote; and (4) alternately, *openness* or *privacy*, depending on whether the vote is by show of hands or by secret ballot, respectively. Voting may take a variety of specific forms to suit the circumstances in which the conflict arises and to suit the particular issue to be settled. A vote by show of hands after considerable deliberation and reflection among the members of the board of directors of a corporation may be the best way to decide whether or not to proceed with a stock split. However, a snap vote or straw poll may be the best way for a hiring committee to narrow the candidate pool for the position of office manager. In both cases, the use of voting will lead to a just outcome only if the parties agree that they are equally capable of sharing the decision and that the option that receives the most votes is the just outcome, whatever it is.

As an alternative to voting, conflicts may be settled by the ruling of a single authoritative figure, such as a legislator, a chairperson, or an executive officer. Vesting decision-making authority in a single individual or in a single body, committee, or panel may be the best means for settling conflicts that require a respected authority's sanction to ensure compliance. It is often considered the procedure of choice to settle disputes that require access to specialized, technical knowledge beyond the comprehension or expertise of the parties to the dispute or for disputes in which the preference of all parties is for a settlement to be determined by a neutral or impartial authoritative arbiter. An example can be found in civil disputes in which a judge has the requisite technical knowledge of the applicable laws, has the respect of the parties, and is impartial as to the particular outcome.

Finally, the best procedure for settling a dispute may involve some combination of these types. For instance, a procedure for settling employment contracts may involve a combination of bargaining and voting. A procedure for a board of directors to decide how to proceed with modifications to stock availability may involve a combination of discussion on merit and voting. The preferred procedure for hiring an office assistant may involve a combination of discussion on merit, contest, and authoritative determination, where the hiring committee deliberates the merit of each candidate to narrow the pool, followed by each candidate's demonstration of his or her ability, which then informs the manager's final determination of who will be hired.

Procedural Justice and Related Values

Typical in most conceptions of procedural justice is the association of justice with one or more values, such as equality, fairness, liberty, desert, or merit. Values often help confirm whether we are on the right track with regard to what we are trying to accomplish. In economics, for example, some of the related values are efficiency, productivity, and marketability. Any one or combination of these values functions to determine whether a modification is economically worth pursuing. For example, efficiency sets the parameters for whether or not some modification to the manufacturing process is economically justified. If the modification results in greater efficiency, then it is worth implementing. If it results, instead, in the same or lower efficiency, then the modification is not economically justified and is not worth implementing. Moral values work in a similar way when what we are concerned with is justice rather than economics. The function of these related moral values is twofold: (1) to justify the procedures used (i.e., to determine that *this* is the appropriate procedure to use) and (2) to validate the outcome (i.e., *this* outcome is a just outcome). These two functions are closely related.

Consider the example of selecting a new chairperson for the board of directors of a major corporation. If the company executives decide that the position of chairperson should go to the best-qualified candidate (on merit), it would be reasonable to employ a procedure that reveals the merit of the candidates. Drawing straws among candidates would be ruled out, since this procedure allows luck to determine justice. A contest of arm wrestling would similarly be ruled out, unless the case could reasonably be made that meritorious arm wrestling is a reliable indicator of meritorious corporate oversight. A suitable procedure would be one that reliably reveals the candidates' ability to perform in the role of chairperson. In such cases, merit serves as the measure of a procedure's likelihood to deliver a just outcome. Any procedure that fails to meet the standard set by the related value would fail to be a just procedure. The justice of any outcome would therefore be in doubt.

The preceding example illustrates the justificatory relation between values and procedures. But what of the second function, in which values serve as a standard against which the outcome is validated as an outcome consistent with justice?

Take the example of a jury trial (typically a mixture of discussion on merit and voting). The desired outcome is the conviction of the guilty party or, at the very least, the acquittal of an innocent person. The desired procedure is one in which the likelihood of an injustice, such as the conviction of an innocent person, is minimized. The relevant value is desert, such that those who deserve punishment receive it and those who do not are not punished. In case the jury convicts an innocent person, the outcome of the trial is an injustice, but it is only understood as such when the outcome is compared with the operative value, desert. In such a case, someone is punished who did not deserve it. The outcome contravenes the value against which the justice of jury trials is measured.

What does it mean when related values are violated? The first response may be that the procedure employed was itself unjust. However, the violation of related values may indicate instead that the procedure was not properly followed (e.g., witness perjury, jury tampering, failure to disclose available evidence). It may also mean that this case is one of those cases in which a generally reliable procedure did not result in the expected outcome. If such failures are repeated, however, it may indicate an inadequacy in the procedure itself.

Perfect, Imperfect, and Pure Procedural Justice

The reliance of procedural justice on values such as equality, fairness, and merit raises a philosophically interesting distinction: (1) the justification of procedures when the outcome is independently known and (2) the justification of procedures when the outcome is not independently known. In the first case, procedural justice may be understood in terms of either perfect or imperfect procedural justice. In the second case, procedural justice is best understood in John Rawls's sense of pure procedural justice. More often than not, the just outcome is neither known in advance nor known independently from the application of some procedure. This makes all the difference when the issue involves someone's life or liberty, where it is not obvious or certain beforehand what outcome would result in justice. This fact of human social life and of the limitations of human knowledge underscores the importance of procedures to justice.

A case of perfect procedural justice arises when there is independent knowledge of the outcome and it is possible to devise procedures that will reliably, or perfectly, lead to that outcome whenever it is applied. In short, perfect procedural justice arises when the procedure ensures no unjust outcomes. An example of perfect procedural justice is the solution of a conflict about the fair distribution of pie among dinner guests, in which the person slicing the pie is the last to select his or her piece. This will ensure that not only the pie is as equally divided as possible but also the distribution among the guests is fair. It would be irrational for the pie slicer to assume that a larger piece would be left for him or her after the other guests had taken theirs, assuming that more pie is better than less pie. This example notwithstanding, perfectly just procedures are difficult to construct for all cases in which they would be useful.

Imperfect procedural justice is similar to perfect procedural justice in that the just outcome is known independently but it is not possible to devise procedures that will reliably lead to it. In imperfect procedural justice, it is recognized that even the best possible procedure may result in the occasional unjust outcome. An example of imperfect procedural justice is contest applied to a case of employment, which only reveals the most meritorious candidate on the day of the contest and is not a general predictor of similar or constantly high-quality performance over the term of the employment contract. A candidate for an office position may be interviewed on a day when he or she has a cold, though it is not obvious to observers, and is slower to respond than usual. This may create the impression that the candidate is dull or disinterested in the job. Alternately, a candidate may do exceptionally well when the assigned task is one he or she has done repeatedly and for which he or she has developed an impressive expertise. However, the candidate may be the least qualified to do the other related tasks of the job, which would only become apparent after he or she is hired. The procedure in question only imperfectly results in just outcomes. In such a case, it is wise to combine this procedure with another, which may also only imperfectly result in justice but when combined with the first procedure improves the likelihood that justice will be achieved, or at least that injustice will be avoided. It may be that the best that can be achieved in any case is an imperfect procedure that reliably, but not always and not perfectly, results in a just outcome.

Disagreement as to the possibility of identifying perfectly just procedures is deep and is reflected in the choice of commonly used examples: Jury trials, democratic elections, collective contract bargaining, and mediated arbitration are all taken as examples of either perfect or imperfect procedural justice. This is a strange phenomenon, since if a procedure is perfect, it should never result in injustice. But if the same procedure is used by some scholars as an example of perfect procedural justice and by others as an example of imperfect procedural justice, then which is really the case? Are jury trials perfect, in which case at least they do not result in injustice? Or are they imperfect and result most of the time in just outcomes but some of the time not? The answer is important since it shapes collective expectations of what the results of the procedure should be, when the procedure should be applied, what counts as evidence of success or failure, and how to respond to incidences of failure in the process.

Pure procedural justice is a third variation of the concept of procedural justice. Pure procedural justice obtains in circumstances in which we do not have independently verifiable knowledge of what the just outcome is. In such cases, the procedure itself determines what justice is. In this way, the procedure guarantees the justice of the resulting outcome. The challenge in cases of pure procedural justice is determining the justice of the procedures in advance of their application. At this juncture, the justificatory role of associated values—such as fairness, equality, or desert—is crucial. John Rawls devised a theory of justice on the basis of pure procedural justice. His account of justice includes a decision-making procedure for arriving at the requirements of justice for the basic structure of society. Unlike instances of perfect or imperfect procedural justice, we do not have any independent means of identifying the requirements of justice for the basic structure of society, yet it is imperative that we do so if what we want is a just social order. In Rawls's formulation, justice requires that any result from this procedure be fair among the parties, that each party be treated as an equal, and that the procedure be rational, or at least reasonable. If these conditions are met, then the resulting procedure would itself result in justice for all parties. In this way, the procedure itself verifies the justice of the outcome.

These ways of conceiving of procedural justice help resolve the final philosophical issue: Why would justice require following procedures at all?

By way of an answer, in normative ethics, it is clear that a moral outcome may be attained by any variety of means. Among the principal problems in ethics is establishing which of the available means *ought* to be used. A dialysis patient in terminal renal failure may be saved by a variety of means, including the abduction of and forced removal of a healthy kidney from a child. This means of securing a morally desirable end would rightly be ruled out as immoral on almost every account of ethics. The concern with procedural justice is similar. Though we may know what the just outcome is, following the specified procedure is important to ensure that the expected outcome really is just and that no related values are violated in the process.

Consider the jury trial scenario. The police, the prosecutors, the judge, and even the defense lawyer may all know by independent means that the accused is the guilty party. The defense lawyer may know this from the accused's sincere confession at their first meeting. The arresting officer may know this because he witnessed the accused do what is charged, and so forth. Barring for a moment the very important philosophical problems of knowledge by observation, testimony, and confession, each of these individuals knows what the just outcome is: The accused deserves punishment, and a guilty verdict should be issued by the jury.

The importance of following established criminal law procedures, however, ensures not only that the outcome is just (i.e., that the one who deserves punishment is punished) but that the accused has every opportunity available to dissuade the jury from believing that he or she is guilty. This includes the opportunity to challenge what is asserted as true or known by those claiming to know. Sending the accused to prison, circumventing a trial, may be more efficient but may not be just in the fullest sense of the term—that is, when justice is understood in conjunction with the related moral values of fairness, equality, and desert.

Alternatively, in the case where it is not possible to establish independently what the just outcome is, pure procedural justice prompts us to consider the possibility of advancing procedures that satisfy the related values and that, thereby, can ensure a just (or not unjust) outcome, whatever it may be.

Procedures are also important for the very simple requirement that like cases be treated alike. The most effective means of achieving this basic tenet of common-law legal systems is to establish a set of procedures that apply to all cases of dispute or conflict of a certain sort. For example, all cases in which the conflict revolves around a dispute over criminal violations where life or liberty is at risk will be decided by jury trial combining discussion of merit and voting. Other conflicts with less severe penalties may be decided by a presiding judge according to established minimum sentencing guidelines and limited discretion. Consistency in decision making, and thereby satisfaction of the values of equality and fairness, is facilitated by consistently applied procedures.

—Christina M. Bellon

See also Equality; Fairness; Justice, Compensatory; Justice, Distributive; Justice, Retributive; Justice, Theories of; Meritocracy; Nozick's Theory of Justice; Primary Goods; Procedural Justice: Social Science Perspectives; Public Goods; Rawls, John; Rawls's Theory of Justice

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Procedural Justice: Social Science Perspectives

Procedural justice refers to the fairness of the procedures used in decision making. In contrast to distributive justice, which concerns the fair allocation of benefits and burdens (e.g., pay, workload), procedural justice addresses individuals' evaluations of and reactions to the fairness of the procedures used to distribute those outcomes. For example, in a business situation, the concept of procedural justice might be used to analyze the fairness of the process used to make hiring decisions, to evaluate performance, or to decide who will be laid off in a corporate downsizing. This entry examines procedural justice as an element in dispute resolution, allocation of outcomes, and organizational contexts. It also examines the concepts of interactional justice, relational justice, fairness theory, fairness heuristic theory, and uncertainty management theory.

Procedural justice theory in organizational behavior goes back to work in the 1970s that studied how those involved with dispute resolution in legal settings evaluated the fairness of the procedures used for resolving disputes and making decisions. Key to procedural justice at that time was voice, or the amount of input that participants had in the decision-making process.

Research indicates that procedural justice is associated with positive attitudinal and behavioral effects. However, violations of procedural justice can lead to negative consequences such as sabotage and lawsuits against the organization. Leadership training in justice principles not only emphasizes the importance of ethics but also contributes to the development of fair human resource procedures.

Dispute Resolution

John W. Thibaut and Laurens Walker were the first to develop the concept of procedural justice. Their research showed that disputants' attitudes were more positive to the extent that disputants were given "voice," or the opportunity to express their views, and they used the term *process control* to refer to voice in this sense. Although they focused on the application of the theory in legal settings, it is relevant in nonlegal settings as well. Thibaut and Walker contrasted the legal procedures used in an adversarial system, in which the court functions as an impartial referee between opposing parties, with those used in an inquisitorial system, in which the court participates in the process of gathering information. They found that their research participants preferred the adversarial system, which allows the decision maker only minimal control over the process of evidence gathering and presentation and gives more control to the disputants with respect to the process of evidence gathering and presentation. Thibaut and Walker found that disputants who have an opportunity to provide input into the decision-making process are more likely to perceive it as fair. Numerous studies supported their finding that there is a positive relationship between process control and perceived fairness.

Allocation

Gerald S. Leventhal developed a broader model of procedural justice, in which he identified six characteristics that individuals consider when deciding whether a process is fair: consistency, bias suppression, accuracy, correctability, representativeness, and ethicality. Turning from the dispute resolution context to the allocation of benefits and resources, Leventhal and his colleagues argued that procedural justice is an important consideration in allocation decisions. They developed the allocation preference theory, which holds that allocators will favor procedures by which their goals can be achieved, including the achievement of distributive justice. The authors of the allocation preference theory indicate that justice in allocation can be attained through seven components of allocative procedure:

1. The selection of decision makers
2. The establishment of ground rules to evaluate the prospective recipients of rewards
3. Information gathering with respect to prospective reward recipients
4. The definition of the decision process structure
5. The establishment of safeguards to monitor the behavior of both the allocator and the prospective reward/resource recipients
6. The establishment of procedures to seek redress on the part of the complainants
7. The establishment of mechanisms to change possibly unfair allocative procedures

Research has upheld the significance of these criteria, which have also been applied in other contexts.

Procedural Justice in Organizational Contexts

Jerald Greenberg and Robert Folger applied the concept of procedural justice to organizations. They found that employees in organizations who are given the opportunity to provide input in decision making react with greater satisfaction. They described this result as the "fair process effect," which refers to the positive effects of perceived procedural justice on people's reactions. Since this initial demonstration of the fair process effect, it has also been found in many later studies in a variety of contexts. Studies indicate that employees who perceive their treatment as fair react positively, as evidenced by better job performance, higher organizational commitment, and greater acceptance of organizational policies. On the other hand, employees' perceptions of unfair treatment lead to negative effects such as higher turnover rate, greater work stress, and lawsuits.

Folger and Greenberg advocated giving employees a chance to contribute to evaluation of their own job performance and an opportunity to choose from different benefits options. They also suggested that employees be given information on the criteria attached to each pay level. According to Folger and Greenberg, employees' participation in these human resource functions related to evaluation and compensation promotes procedural justice.

Interactional Justice

First introduced as an independent variable, interactional justice is viewed by various scholars as a component of procedural justice, although some have treated it as a separate construct. Research indicates that interactional justice consists of interpersonal and informational components. The interpersonal justice component involves treating people with respect, dignity, and propriety. The informational justice component refers to authorities' truthfulness in implementing procedures and explaining decision outcomes. Interactional justice may arise from the actions of a system or an agent. To clarify the constructs of procedural and interactional justice, a line of research crosses justice source (e.g., system, agent) and justice content (e.g., consistency of procedures, treatment with respect) to examine the effects of procedural and interactional justice.

Relational Models of Procedural Justice

In their "group value" or relational model, E. Allan Lind and Tom R. Tyler argued that individuals in organizations are concerned about fair procedures because procedures tell them something about how the organization treats people—essentially, how it values members of the group. They developed the self-interest and group value models of procedural justice. With the self-interest model, or "instrumental perspective," individuals seek decision control to maximize their own outcomes. However, according to the informed self-interest model, individuals can gain more favorable outcomes from group cooperation than from individual efforts in the long run. Therefore, the fairness of procedures in making decisions overrides the individuals' preferences for certain self-interested outcomes.

Evidence indicates that procedural justice, independent of outcomes, is enhanced by voice—the opportunity for affected parties to provide input into the decision-making process (or process control, as defined by Thibaut and Walker). The informed self-interest model does not explain process control's noninstrumental value-expressive effects, which are explained in Lind and Tyler's group-value model. Lind and Tyler asserted that the functioning of groups is governed by group identity and group procedures. Fair procedures allow group members to express their views. Value-expressive effects occur when individuals value their membership in a group, regardless of whether their decision-making input will result in a favorable outcome for them, because the consideration of their views confirms their status in the group and their rights as members to participate in group processes. Therefore, voice enhances perceived procedural justice even if it does not produce a favorable outcome.

The group-value model was later revised and labeled a relational model of authority in groups. The latter model indicates that procedural justice judgments are affected by three relational concerns with authority: trust, neutrality, and standing. The authority who considers fairly the views of an individual can be trusted. Decision making that is unbiased indicates the authority's neutrality. The authority who treats an individual with dignity and respect provides status recognition for the latter. The authority's relational concerns of trust, neutrality, and standing as evidenced in the procedures used affect individuals' procedural justice judgments.

According to the relational model of justice, employees who experience fair procedures in an organization feel that they are valued members of the organization. The group engagement model extends this idea by asserting that procedural justice strengthens employees' sense of identity as members of the work group. The group engagement model incorporates three identity judgments: pride, respect, and identification. Pride refers to perceived group status, respect refers to one's perceived status in the group, and identification refers to the extent to which one affiliates oneself as a member of the group. When employees are treated with procedural justice, they perceive their organization to be of high status, their standing in the organization to be high, and their identification with the organization to be strong. These identity judgments resulting from procedural justice lead to high levels of employee cooperation. Conversely, a lack of procedural justice erodes pride in the group, respect for it, and identification with it; these weak identity judgments lead to lower employee cooperation.

Fairness Theory

Robert Folger's referent cognitions theory (RCT) and Folger and Russell Cropanzano's fairness theory, a successor to RCT, involve counterfactual thinking. RCT involves conscious mental simulations of counterfactual alternatives. With fairness theory, counterfactual alternatives can be brought to mind spontaneously. Fairness theory attempts to hold an authority accountable for injustice, with three types of accountability judgments: *would* judgments, *should* judgments, and *could* judgments. With the *would* counterfactual, one's actual state of being is contrasted with whether one would have been better off with another procedure or outcome. With the *should* counterfactual, what was carried out is contrasted with what should have been done according to moral standards. With the *could* counterfactual, a contrast is made between what one has done and what one could have done in terms of feasible options. An experience will be evaluated as unjust if an authority who has inflicted injury on an individual (i.e., the individual *would* have been better off with a different process or outcome) *could* have chosen another feasible option and *should* have acted differently so as not to violate some moral standard. With RCT, the *would* counterfactual is linked to the *should* counterfactual. What would have occurred is conceptualized to be linked to what should have been done. With fairness theory, the *could* counterfactual is connected to the *would* and *should* counterfactuals separately. In other words, fairness theory contends that in addition to the *should* aspect, there are contextual factors that promulgate various feasible options, as denoted by the *could* aspect, which RCT does not take into consideration.

Fairness Heuristic Theory

Fairness heuristic theory is based on the argument that people use a "fairness heuristic" to determine whether to accept an authority's directives. The earliest relevant information, as opposed to information made available later in time, exerts the greatest influence in the formation of fairness judgments. Therefore, for an authority to receive support from subordinates, the latter should be treated with procedural justice the moment they join the organization. Also, where there is no available information pertaining to the trustworthiness of an authority, perceptions of fair treatment serve as the key in determining whether or not to accept the authority's decision. In other words, trust in the authority can be instilled by fair procedures. When information is available with respect to an authority's trustworthiness, then procedural justice information will have a lesser impact on people's reactions. Social interdependence in groups, teams, and organizations is associated with problems such as exploitation and exclusion. Therefore, fairness judgments are needed to assess the trustworthiness of the authority, especially when information pertaining to it is not available, and to determine whether to respond positively to the demands of that authority.

Uncertainty Management Theory and Distributive Justice

Uncertainty management theory also relies on the fairness heuristics. However, while perceived fairness is used in fairness heuristics theory as a surrogate for trust, a source of uncertainty, it is used in uncertainty management theory to deal with not only trust but also other uncertainty sources. Research indicates that people react to perceived fairness more strongly when they have to cope with various sources of uncertainty, such as procedural and distributive issues.

Despite their significant intercorrelation, empirical tests of the theoretical relationship between distributive and procedural justice show them to be distinct constructs and to differentially influence employee attitudes and behaviors. Furthermore, a number of researchers have demonstrated that perceptions of distributive and procedural justice interact to influence outcomes. For example, reactions to negative outcomes are found to be less negative when the procedure is thought to be fair. Nevertheless, discussion is continuing in the organizational behavior literature about the usefulness of the distinction between distributive and procedural justice. Some are concerned that justice researchers have sliced justice into such narrow slivers that it may be less useful or descriptive of how individuals really think about justice in organizations, and they are now discussing the importance of employees' more holistic perceptions of justice and injustice and their use of a more general justice heuristic in their evaluations and reactions.

—*Marjorie Chan*

See also Due Process; Fairness; Justice, Distributive; Justice, Theories of; Participatory Management; Procedural Justice: Philosophical Perspectives; Self-Interest

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Productive Efficiency

Productive efficiency, measured by the ratio between output and input, improves when the same input yields more, or better, output and is maximal when the output cannot be increased without increasing input. When the input is monetized and the output is not, the measurement can be called cost-effectiveness, cost utility, or cost efficacy. Productive efficiency is contrasted with allocative efficiency, which describes societywide allocation of resources and the resulting increase in general welfare.

Information about productive efficiency is often highly useful. Furthermore, its basic concepts add a useful clarity to many discussions; for instance, "cost cutting" is not synonymous with improved efficiency, since the result of cost cutting can be less or poorer output. On the other hand, productive efficiency is an inherently comparative and evaluative term and can be easily misunderstood as simple and objective.

To say that a process or system is "efficient" or "productively efficient" is to compare it favorably with some other process or system, or some other period of time, where the same kind of input is used for the same kind of output. When input and output are simple to define and easy to measure, productive efficiency is similarly easy to measure. Other things being equal, efficiency is ethically desirable; inefficiency leads to the unnecessary and therefore wasteful use of scarce resources. Nevertheless, efficiency cannot reasonably be seen as an ultimate goal; instead, it is a desirable quality in pursuing further goals. Allen Buchanan, in *Ethics, Efficiency, and the Market*, discusses the extent to which efficiency is ethically desirable. Janice Stein, in *The Cult of Efficiency*, dissects the contemporary tendency to value efficiency as an end in itself.

Ordinarily, both input and output refer to complex sets of diverse factors. In the transformation of steel into paper clips, for instance, the input includes not only the quantity of steel used but also the labor, the time taken, the machinery used, and other factors. The output could be defined as the quantity of paper clips, their quality, the price they bring, the improvement they bring to the handling of paperwork, and other things. Therefore, in measuring productivity, one must specify what ratio is being examined: the number of paper clips per pound of steel, per hour, or per factory; the market value of paper clips produced per any or all of these units; and so on. What counts as waste under one description (e.g., "unnecessary time" used in manufacture) can alternatively be described as an increase in leisure or as a contribution to better labor-management relations. Furthermore, what counts as "input" under one description (e.g., labor) can also be seen as an output (the satisfaction and self-esteem built into many kinds of work).

For ease of comparison, it can be useful to translate inputs and outputs into a single unit of measurement, often either money or utility (here meaning preference satisfaction). But doing so can also obscure ethically significant differences in kind—for example, the extinction of a species, the harshness of a tired parent, 3 months' greater life expectancy. Such translations, in other words, can be useful but always risk offering precision at the cost of losing sight of important differences.

Some argue that resources used throughout the life cycle of a product (not just during its manufacture) should count as a cost. As an example, vinyl siding, discarded after its useful life, produces toxic waste. The damage to air and water (an externality, i.e., an effect on parties who were not part of the initial exchange) can also be considered an "input" from a societal point of view. In addition, since factors of production are always in limited supply, their use in one project carries an opportunity cost.

—Judith Andre

See also Cost-Benefit Analysis; Economic Efficiency; Economics and Ethics; Pareto Efficiency

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Product Liability

Product liability refers to the responsibility of manufacturers to compensate for injuries brought about through the use of their products. Legal and moral accounts of product liability seek to determine the conditions under which businesses can be held responsible for such harms. Since the risk of injury in the use of consumer products can never be completely eliminated, the notion of product liability raises important legal and philosophical questions about who should bear the burden of costs for such injuries. Determining the answer to these questions raises deontological issues of fairness and justice as well as utilitarian considerations as to how society can best prevent and recompense such harms. The wide publicity of famous cases of product liability, such as those involving McDonald's coffee, the Ford Pinto, Dow Corning breast implants, Firestone tires, and asbestos products, has particularly amplified such legal and moral questions.

Historical Background

The Anglo-American law of liability until the end of the 19th century was largely governed by the doctrine of privity. Under the law of privity, injured persons could not legally collect compensation from parties with whom they did not have an explicit contractual relationship. Thus, since manufacturers who sold their products through retailers did not have a direct contractual relation with the final purchaser of those products, they were effectively immune from lawsuits for injuries to consumers brought about by those products. As such, the privity barrier essentially made it impossible for most victims of product-related injuries to recover damages from a manufacturer of a defective product unless they had purchased the product directly from the manufacturer. While the law of privity may have made sense when most products were bought directly from the persons who made them, its legitimacy began to come into question as retail distribution was becoming a hallmark of the modern economy.

In the United States, the landmark 1916 case of *MacPherson v. Buick Motor Car* more or less abolished the barrier of privity. In that case, a New York court rejected Buick's argument that it could not be held responsible for an accident due to a defective wheel that it had used in the production of its automobile simply because it had no direct contractual relationship with the person injured. The court ruled that Buick should have detected the wheel defect while the automobile was being assembled and that Buick had a reasonable duty to provide consumers with safe and reliable products.

The *MacPherson* ruling was soon adopted in most U.S. jurisdictions, and it ushered in a new theory of "due care" in product liability law. Under the due care theory, companies are held responsible for taking reasonable precautions to produce products that are free from potentially harmful defects. Generally speaking, under the theory of due care, a person could recover damages for an injury if it could be proved both that the product that caused those injuries was defective and that the defect in question was the result of negligence on the part of the manufacturer of the product. Demonstrating negligence involved showing that the manufacturer was at fault for the defect in failing to adopt reasonable standards in the design or production of the defective product.

While the doctrine of due care in liability provided injured consumers with a greater ability to recover for damages caused by defective products, the burden was still on the injured party to prove negligence on the part of the manufacturer. A series of court decisions in the mid-20th century, including *Escola v. Coca Cola Bottling*, *Henningson v. Bloomfield Motors*, and *Greenman v. Yurba Power Products*, eventually eroded even this requirement. In each of these cases, the courts awarded damages to consumers without requiring proof of negligence on the part of the manufacturers, ushering in the era of strict liability in torts. Under the rule of strict liability, manufacturers can be held legally liable for injuries caused by the defective nature of a product even if they were not negligent in producing that product. In certain contexts, distributors, assemblers, retailers, and any other party involved in placing a defective product on the market can also be held strictly liable for injuries caused by that product. Although injured parties can still bring legal action under negligence, the doctrine of strict liability is presently recognized, to some degree, in nearly all U.S. jurisdictions.

Forms of Defect and Compensation

While the theory of strict liability does not require proving negligence, it still requires that the injury in question be caused by the defective nature of the product. Thus, under both negligence and strict liability, proving liability involves demonstrating the defective nature of the product. Since there is some risk associated with the use of any product, this issue is of moral and legal significance as well. In general, products may be defective in manufacturing, design, or warning. Manufacturing defects occur when a product does not conform to the manufacturer's own specifications, as when a food product becomes contaminated during processing or a tool leaves the production line missing a screw. Defects in design occur when a product line is designed in a manner that is deemed to be unreasonably dangerous, as when the design of a ladder makes it likely to fail under anticipated weights. Finally, defects in warning occur when consumers fail to receive proper instructions as to the safe use of a product, as when a pharmaceutical company fails to inform consumers of a drug of possible dangerous interactions with other common medications.

Since no manufacturer can anticipate or prevent every possible risk involved in the use of a product, the determination that a product is defective in any form concerns judgments as to the reasonableness of the risk presented. To constitute a defect, most theories accept that the condition must constitute an unreasonable danger to the consumer. In this regard, the reasonable person standard is often appealed to in determining the existence of a defect. The reasonable person standard holds that a product is sold in a defective condition when it presents dangers to ordinary consumers in its expected use that would not be reasonably foreseen by them. However, some courts have lowered the standard for determining defectiveness by holding that manufacturers should also anticipate the unreasonable ways in which people might put their products to use in producing them. It should be noted that some products—for instance, many pharmaceuticals—have inherent dangers associated with them. In cases of such unavoidably unsafe products, a standard of social risk/utility is often used to adjudicate questions of manufacturers' responsibility. A social risk/utility standard holds that if the dangers inherent in the use of the product are outweighed by the potential benefits of its use, and there is no other means of obtaining those benefits or making the product safer given current technology, then the product should not be considered unreasonably dangerous as long as information concerning the risks is provided to consumers.

In seeking restitution for injuries caused by defective products, plaintiffs can request both compensatory and punitive awards. Since product liability cases generally fall under civil law, and not criminal law, such awards are usually measured in monetary terms. Compensatory awards are meant to compensate injured parties for the losses they incur as a result of their injuries. These losses can include medical expenses incurred as a result of the injury as well as lost earnings, both past and future, due to the injury. They can also include awards for the pain and suffering and other intangible harms associated with the injury. Finally, juries can award punitive damages to victims for the purpose of punishing the defendant, though this is more usually restricted to cases of negligence. The last two forms of compensation have been made particularly contentious because of the well-reported examples of extremely large jury awards to victims, as in the case of the nearly $3 million award originally issued by the jury to the woman burned in the McDonald's hot coffee case. As a result, tort reform in some jurisdictions has involved placing monetary limits on awards for noneconomic and punitive damages.

Social and Ethical Issues

There is a good deal of debate surrounding product liability law, particularly with regard to the rule of strict liability. These moral concerns are generally divided into questions of fairness and justice and those of social and economic utility. Both proponents and opponents of the theory of strict liability appeal to such concerns in making their cases. For instance, many critics of the rule of strict liability hold that it is inherently unfair to manufacturers, since it holds them responsible for defects even when they have fully exercised reasonable precautions in producing the defective products. As such, they claim that it is unjust to hold manufacturers responsible for harms if they were not at fault in bringing about such harms. Such critics are often particularly opposed to what they see as the unfairness of much mass tort litigation, such as asbestos and tobacco suits, since this litigation often involves holding a current business responsible for harms that originated long ago and under the control of different persons. For all these reasons, many opponents of the rule of strict liability argue for a return to standards of negligence or comparative negligence in liability cases.

Proponents of strict liability also appeal to considerations of justice and fairness, though. They argue that if companies are not held responsible for harms caused by defective products, then injured persons will go uncompensated. Since the injured person is not at fault for an injury caused by a defective product, it is just as unfair, they maintain, to deny that person the ability to seek recourse for the damages caused by such defective products. Indeed, they argue that since someone has to bear the costs involved in injuries caused by defective products, it is most fair that the party that profits from their production should do so. In this vein, some proponents of strict liability have even argued that since businesses can only profitably operate within a specific underlying social and economic system, they should also help bear the cost of the harms produced with that system, even when they are not directly at fault.

Both proponents and opponents of strict liability also appeal to utilitarian considerations in their arguments. Proponents of strict liability maintain that the doctrine of strict liability provides businesses with the incentive to be as careful as possible in producing safe and reliable products. They also argue that businesses can build the costs of such liability back into their products and thus efficiently spread the cost to all consumers of those products. Opponents of strict liability, on the other hand, argue that the litigation and insurance costs associated with strict liability place an increasingly unbearable cost on businesses that is stifling to the economy and hurts the competitiveness of businesses in the United States with their international competition. Critics of strict liability have also argued that the doctrine discourages companies from introducing new or innovative products, particularly those, such as pharmaceuticals, that are unavoidably unsafe. As the utilitarian arguments, both for and against strict liability, appeal to long-term social and economic benefits and costs that are difficult to measure precisely, determining the overall utility of the strict liability approach is likely to remain a contentious matter in the foreseeable future.

—Daniel E. Palmer

See also Common Law; Compensatory Damages; Consumer Product Safety Commission; Due Care Theory; Implied Warranties; Liability Theory; Litigation, Civil; Negligence; Tort Reform

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Professional Ethics

Professional ethics is a branch of applied philosophy and can be understood as the application of ethical concepts and principles to professional practice. Questions relating to the justification of these theories and concepts are also part of professional ethics.

A key element in ethics is the identification and justification of rules or standards that can be used to distinguish right and wrong behavior and identify what ought to be done. These rules and standards can be used by people to identify what they ought to do in various circumstances and to evaluate particular behavior. Likewise, professional ethics is concerned with rules and standards that distinguish right from wrong. These rules and standards constitute the principles of professional conduct and are the foundation for professional ethics. They are used by practitioners to identify what they ought to do in particular situations, and they can be used to evaluate professional behavior.

Professional ethics is grounded in the belief that professional roles require particular norms and principles to guide behavior. The focus is on the special relationships between practitioner and client or patient and what that relationship entails. Professional ethics does not encompass all the norms and principles that apply to everyone but only those that pertain to individuals in their professional roles. Professional ethics, then, is concerned with the moral principles and values relevant to the roles and conduct of professionals in society and can therefore be thought of as a system of norms that can be used to justify and inform beliefs and behaviors.

Professional ethics is a recognized field of study with an established academic literature. Since the 1970s, there has been increasing attention paid to applied ethics, and subdisciplines have developed in a wide range of areas, such as accounting ethics, banking ethics, engineering ethics, teaching ethics, real estate ethics, and so on, in addition to the more established areas of bioethics or medical ethics and legal ethics. The study of professional ethics can take various forms. The most common approaches are concerned with one or more of the following dimensions: the ideal norms that a particular professional should aspire to, the common norms that are actually accepted by most professionals, the elements contained in the codes of professional associations, or the contractual relationship between the profession and society.

The Professions in Society

Until the mid-19th century, the professions were limited to the church, law, and medicine, with the army and navy sometimes included. Today, an increasing number of occupations are regarded as professions, and many more aspire to be recognized as professions. There is constant pressure both on and from within particular nonprofessional and quasi-professional occupations to become more professional and to claim public recognition as a profession, giving rise to the phenomenon of the emerging profession.

The professions occupy an important position in society because their roles have an impact on the lives of many people. Because societies have evolved and become more complex, individuals increasingly seek professional advice concerning various aspects of their lives. As the role of professions expands, existing professions mature and new professions are created. At the same time, the behavior of professionals, especially those based on private practice, have increasingly come under close scrutiny. For example, advances in health care technologies have drawn attention to bioethics, and the fiascoes surrounding Enron and WorldCom, for example, have focused attention on accounting ethics. Recent research has demonstrated that public perceptions of accountants' professional ethics and honesty have declined in recent years, while the professional ethics and honesty of doctors, teachers, and the police are perceived to have increased.

What Is a Profession?

A profession has been described as a community of people circumscribed by the activities they perform. These activities are grounded in a common theoretical background that is acquired through formal education. There is no single definition of a profession, and various commentators have provided checklists of attributes that are claimed to distinguish the professional from the nonprofessional. It is implicit in this approach that the professions possess unique characteristics that set them apart from other occupations. The core features included in such lists are as follows: (1) There is a systematic body of theory that must be mastered through tertiary education, professional development activities, and experience; (2) there is a dependent relationship between the client and the professional; (3) the professional exercises autonomy in performing his or her work; (4) there is a tradition of service and values that promote the public interest rather than self-interest; (5) there is a certification or licensing process for practitioners; and (6) there is a representative body that develops and enforces a code of professional conduct.

Others claim that professionalization is a matter of degree and what is important is developing skills and strategies for improving performance rather than acquiring the characteristics of a profession. Nonetheless, there seems to be a core of three features common to all professions, with other characteristics varying depending on the profession: First, extensive training is required; second, this training has a significant intellectual component; and third, the skills and expertise of the practitioner provide an important service in society.

It has been argued that the primary quality that sets professionals apart from nonprofessionals is the reliance that clients or patients place in professionals due to their superior knowledge and expertise. There is a resulting power differential between the professional and the client. In many instances, the client has no option but to rely on the judgment and expertise of the professional. The clients must trust that the professional is competent and committed to helping them because the ordinary person, in many cases, is unable to make a judgment about the capability of the professional. Only ethical conduct on the part of professionals can ensure that their power is not abused and the trust of the client is warranted.

While professionals have enjoyed prestige and privileges within society, this has been because they are thought to bear more responsibility and have a heavier moral obligation than others. The status of any profession rests on social consent, and in return the profession accepts a responsibility to subordinate self-interest to the public interest. When a profession is recognized, it is granted an exclusive franchise as only those who are licensed can practice. The justification for licensing is that the public good would be threatened if unqualified people were permitted to practice. The benefits that attach to a profession include social status, respect, and wealth.

Almost all well-established professions are located to some extent in universities. The professional schools within universities have as one of their basic functions the transmission of both the generalized and the systematic knowledge that forms the basis of professional practice. Another role of the university-based professional schools is research aimed at creating new and better knowledge. In relation to normative standards or ethics, universities provide ethical training of students. Some ethics training is explicit, and some is combined with the learning of substantive knowledge. The behavior of the teaching staff also provides a model for ethical behavior.

Codes of Professional Conduct

The most visible aspect of professional ethics is the code of professional conduct adopted by each profession, and much of the professional ethics literature takes as its focus codes of professional ethics. Although some writers distinguish between terms such as codes of ethics, codes of conduct, and codes of practice on the basis of their content, in practice, professional codes tend to include elements of all three. A code of professional conduct provides a set of rules that promote a professional attitude and behavior consistent with the ethical expectations of the public.

A profession's code of conduct serves both its own interests and the public interest. The code serves as a public relations tool by fostering a positive image of the profession that contributes to building and retaining public confidence. Codes also reassure the public that the profession is monitoring itself by establishing high standards of conduct and implementing disciplinary procedures to deal with violations. Codes protect potentially vulnerable clients from incompetent and unscrupulous practitioners and also protect the qualified practitioner from unfair competition. They establish minimum standards of behavior that provide a reference point for decision making and a benchmark for assessing the ethics of members' conduct. Any behavior that is inconsistent with the code of professional conduct is judged unethical.

Professional ethics, however, involves much more than a code of conduct. Practitioners are required to do more than simply act in accordance with the identified norms and regulations of the profession. This is because the norms and regulations must be interpreted and applied in different contexts. Moreover, no set of rules or regulations can cover every possible situation, and indeed, they are not meant to. One characteristic of a profession is that practitioners are required to act autonomously; they must exercise judgment, which involves identifying and choosing between alternatives.

Some of the "big issues" in professional ethics include the question of whether deception is ever permissible on the part of the professional in either a paternalistic sense (e.g., if a doctor believes that it is in the best interests of the patient not to be told the truth about his or her medical condition) or a nonpaternalistic sense (such as a researcher not fully informing the research subjects of the aims of the research). The issue of informed consent is central to medical ethics, and the question of what information a client needs to be given in order to make an informed decision (e.g., before entering into a contract) is common to most professions. Client privacy and confidentiality raise important ethical issues for all professionals. The issue of distributive justice also arises with respect to the allocation of scarce resources by professionals. When professionals are employed in businesses or by the state, other issues arise concerning the potential for a conflict of interests between the employer and the patient or client.

Critical Inquiry

Although professionals have undoubtedly enjoyed prestige and privileges, there are several challenges to professional legitimacy and authority. Three relevant features of the role of the professions in Western society during the past 50 years or so have been claimed to lie at the heart of the problem of their position in a liberal society: First, the professions provide an important service that people depend on; second, they serve basic values and have a monopoly over the provision of services; and third, despite occupying monopolistic positions, the professions have not been subject to much public control.

Some commentators have claimed that the professions are simply offering commercial services. Despite the claim that the professions operate for the public good, they are really just another form of business, albeit a well-entrenched and well-organized form of business. These critics question the privileged position occupied by the professions. Others have pointed out that the ideal notion of a professional—an autonomous, self-employed person whose actions are determined by the client's needs and interests and who is a member of a professional organization that regulates its members through a code of ethics—is no longer widely applicable. More and more professionals are employed in large firms or by the state, which complicates the ethical issues faced by professionals because they have ethical commitments to both their clients and their employer. In this situation, the question of who should determine the needs of the client—the client, the professional, the employer, or the state—becomes a key ethical issue, and a professional code of conduct is of little assistance.

Other commentators question the normative claims made by professionals. The problem is that professionals see themselves as being ruled by ethical norms or standards that permit, and in some cases oblige, them to do things not permitted by general ethical norms. This situation has been questioned, and many philosophers conclude that to be legitimate, professional ethics must be derived from or be identical with or focus on specific aspects of ordinary morality. These critics question the content and application of professional ethics.

—*Josie Fisher*

See also Accounting, Ethics of; Bioethics; Codes of Conduct, Ethical and Professional; Ethics, Theories of; Finance, Ethics of; Legal Ethics

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Profit Maximization, Corporate Social Responsibility as

The claim that the social responsibility of business is to increase its profits is associated with the late Milton Friedman and is the title of a famous article he published in 1970. The article is a devastating critique of the popular idea that corporations have social responsibilities that trump profit maximization. It has proved to be prophetic. The article was written, as it states, against a background of "widespread aversion to 'capitalism,' 'profits,' [and] the 'soulless corporation.'" At the time, Friedman further noted, managers would often disguise actions that were really intended to increase profits in the cloak of corporate social responsibility (CSR). But today, in a remarkable reversal, Friedman's doctrine of shareholder value is triumphant, and managers often use the rhetoric of profit maximization as a cloak for actions that are, in part at least, really driven by considerations of CSR.

The doctrine of CSR teaches that corporations have responsibilities to promote certain social goals, even at the expense of their own profitability. CSR requires more than simply playing by the rules—that is, engaging in free and open competition without deception or fraud. It imposes on corporations affirmative obligations to play their part in solving social problems and righting social wrongs. At the time the article was written, corporations were exhorted to help fight inflation and high unemployment among inner-city youth. Today, corporations are urged to combat global warming, help solve the AIDS crisis, alleviate poverty at home and abroad, and much more.

The argument of Friedman's article is actually less a case for profit maximization than it is a demolition of the case for CSR. And Friedman's position is more complex and nuanced than is suggested by the polemical title of his article. The critical passage in his article is as follows:

> In a free-enterprise, private-property system, a corporate executive is an employee of the owners of the business. He has direct responsibility to his employers. That responsibility is to conduct the business in accordance with their desires, which generally will be to make as much money as possible while conforming to the basic rules of the society, both those embodied in law and those embodied in ethical custom.

It is apparent that Friedman's objection to CSR is not that it leads to spending money on social goals but that it does so *without the consent of a corporation's owners.* Managers have accepted a fiduciary obligation to manage the corporation in accordance with the desires of its owners, and CSR would permit or require them to violate that obligation. As Friedman notes, things would be quite different if the managers had promised something else. If a group of people established a corporation for a charitable purpose, such as building a hospital or a school, then the manager of that corporation would have a fiduciary duty to carry out that objective.

It is also an entirely different matter, Friedman says, if the manager chooses to devote some of his *own* money or time or energy to help achieve a social objective, because in that case "he is acting as a principal, not an agent; he is spending his own money or time or energy, not the money of his employers or the time or energy he has contracted to devote to their purposes." If managers disagree with a corporation's priorities, then of course they are free to "refuse to work for particular corporations."

There are other objections to CSR. First, it empowers managers to spend other people's money for a general social interest. That is objectionable because it usurps a function of government: It means that managers are in effect "imposing taxes, on the one hand, and deciding how the tax proceeds shall be spent, on the other." It places public decision making in private hands and bypasses the traditional checks and balances of our political system. Second, nothing in the training or experience of managers qualifies them to make public policy—they are "experts at making money, not social policy." Third, CSR harms the foundations of our free society by reinforcing the idea that profits are wicked and so must be controlled. From that idea, it is a short step to the detailed regulation of the economy by "the iron fist of Government bureaucrats."

Friedman makes a final point that has passed relatively unnoticed: Not only is CSR undesirable, but it is probably *unworkable* too. That is because the manager who strays too far from minding the bottom line will likely be fired by the shareholders—"either the present ones or those who take over when his actions in the name of social responsibility have reduced the corporation's profits and the price of its stock." The market for corporate control strictly limits the scope for managers to engage in CSR (unless of course it is profitable).

Friedman's *positive* case for seeing profit maximization as business's social responsibility is really the subject of two other classic works—*Capitalism and Freedom* (1961) and *Free to Choose* (1980). There, Friedman lays out the case that individual freedom can thrive only where markets are substantially free. This is because the freedom to determine one's own economic choices (including whether or not to seek to make a profit) is both an important element of individual freedom in itself *and* a necessary condition for political freedom. Economic freedom and political freedom are linked because political freedom is illusory if one's livelihood is under the control of the government. History attests that there have been no free societies without free markets. (Unfortunately, the reverse does not hold: Relatively free economies have coexisted with tyrannies.)

Friedman's thesis has scandalized many critics, particularly because it appears to celebrate the profit motive at the expense of the common weal. Many of these criticisms are wide off the mark or simply based on misreadings of Friedman's article. Space limitations permit only a superficial review. First, it is wrong to say that Friedman celebrates self-interest. As we have seen, he doesn't object to managers contributing to worthy public purposes; he just wants them to contribute their own money, time, or effort. Second, Friedman's case for profit maximization does not rest on the supposed greater efficiency of market economies. The goal of efficiency is a distant second to Friedman's concern to secure our freedom. Third, it is false to claim that Friedman's position privileges shareholders at the expense of "stakeholders." The corporation's stakeholders all voluntarily acquiesce in this arrangement or the corporation could not exist. Employees freely choose to work for corporations because they offer favorable wages and conditions. Consumers purchase from them because they offer better products, and so on. Fourth, the frequent charge that corporations don't "give back" to society is mystifying. Corporations pay market prices for their inputs, and they pay taxes. In fact, as is well known, the owners of corporations—the shareholders—are subject to double taxation on their shares of corporate profits. The corporation's shareholders make numberless other contributions to society. Advocates of CSR have failed to offer a convincing explanation for why shareholders should be expected to give back yet again, this time under the rubric of CSR.

There are, however, some more damaging criticisms of Friedman's thesis. One can best be suggested by an example. What should a manager do if he or she discovers that one of the corporation's plants is emitting a dangerous chemical into the atmosphere but that a loophole in the law would permit it to go on doing so? For the British economics writer Samuel Brittan, the answer is obvious: "The absence of effective legislation should not excuse a chemical company for polluting the air." However, it is not clear what Friedman's position would be. He might take a hard line and argue, as he does elsewhere in the article, that the manager should not make "expenditures on reducing pollution beyond the amount that is in the best interests of the corporation or that is required by law in order to contribute to the social objective of improving the environment." (Assuming that the government is unaware of the loophole, would the manager have a duty to bring it to the government's attention?) Or he might invoke the passage quoted earlier, which requires the manager to conform to the basic rules of society, both legal and *ethical.* That is to say, Friedman might argue that the manager has an ethical responsibility to stop the pollution. Neither answer is satisfactory. The first is blind to the fact that there are always gaps in the laws that may have to be filled by business's sense of responsibility. The second won't do because the clause about ethical custom should probably be disregarded as an embarrassing loose end in an otherwise tightly constructed argument. On many issues, there simply is no canonical "ethical custom," and Friedman points us to no source for one. Critics have predictably seized on the clause to argue that CSR is part of society's ethical custom, thus negating Friedman's thesis. The first answer—that the manager has no duty to do more than the law requires—is probably more consistent with the position Friedman has staked out in the article and elsewhere.

A final criticism is that much of the debate over CSR versus profit maximization is moot. One reason is that, as Friedman himself has explained, the market for corporate control severely limits the scope for managers to exercise social responsibility. However, that assumes that there is (and will continue to be) a functioning market for corporate control. To the extent that, say, state antitakeover statutes weaken the market, the legitimacy of CSR may become a live issue once again. Another reason why the debate over CSR may be moot is that virtually all shareholders today had notice of corporations' CSR policies when they purchased stock in them. Arguably, by purchasing the stock, they consented to at least the existing level of CSR. That removes Friedman's main objection to much of contemporary CSR.

—Ian Maitland

See also Agency, Theory of; Berle-Dodd Debate; Business, Purpose of; Business Judgment Rule; Corporate Social Responsibility (CSR) and Corporate Social Performance (CSP); Fiduciary Duty; Free Market; Friedman, Milton; Market Failure; Market for Corporate Control; Profits; Shareholder Model of Corporate Governance; Shareholder Wealth Maximization; Trustees

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Profits

One of the most important functions of business is to sell goods and services for profit. In the economic view of the firm, business decision makers are assumed to desire as large a profit as possible for their organization, and a good society develops conditions for businesses to produce and sell valuable products and services as efficiently as possible in order to improve the quality of human life. In this economic view, opportunities to make profits are signals that society's resources can be used more efficiently.

For a business, profit refers to the amount of revenue it receives from customers in excess of the costs it incurs over a defined period of time. This profit is a form of wealth that belongs to the owners of the business. Business owners can reinvest their profit to produce more goods and services that people value, or they may exercise their liberty to use their profits to further their own personal satisfaction. Government may tax profit to use for other social purposes and public goods.

A business by definition is an organization that intends to make a profit by selling goods and services that its customers value. When it conducts its activities with trustworthy integrity, then its profit after its cost of capital is a monetary measure of the increase in social wealth that the business created by transforming a portion of society's supplies into more valuable goods and services. Thus, many view profit as a moral good when it is generated within the bounds of economic efficiency and good moral character. Adam Smith, for example, argued in the 19th century that self-interested exchange brings about welfare by maximizing the output of scarce goods and services subject to the constraints of costs when it is bounded by a competitive marketplace operating with principles of honesty, trust, social contract, and protection of private property. Milton Friedman, Nobel Prize–winning economist of the 20th century, followed this perspective when he famously wrote that the ethical responsibility of business is to generate as much profit as is legally and honestly possible.

Most people agree, however, that profit can be unacceptably excessive. The great religions of the world, for example, have guidelines for principled profit in commerce—that it reflect fair value for buyer and seller, that it not be an outcome of hoarding that unfairly limits the availability of products, and that it not be an obstacle to broad distribution of essential goods throughout society. Similarly, most governments have commercial laws to prevent businesses from taking advantage of short-term circumstances, such as natural disasters or wars, that may create opportunities for excessive, or windfall, profits. Many businesses voluntarily adopt codes of conduct that call for fair negotiations with customers and suppliers so that all parties are satisfied with the value and reasonable profit created.

Despite these guidelines to constrain excessive profits, many argue that business naturally tends toward excessive profits whenever it does not directly pay for all the costs of its effects on environment and community. For example, a business's profit might be considered excessive if the business does not directly bear all the costs of rectifying pollution it generates in its operations or of unemployment it causes when it lays off workers. These perspectives focus attention on the deficiencies of fairness in profit making whenever business is granted liberty to shift cost away from itself and onto society.

Profit and Law

In the legal framework of the United States, *Dodge v. Ford* of 1919 is a commonly cited precedent that establishes that the primary responsibility of business management is to make profits for owners according to the charter of the corporation. Beyond the requirements of this precedent, the government also requires businesses to comply with Generally Accepted Accounting Principles (GAAP) regarding the recording and reporting of costs, revenues, and profit. Furthermore, publicly owned firms must report their profits annually to shareholders. All businesses must report revenues, costs, and profits to the government for purposes of taxation.

These legal obligations, however, often leave room for judgment and aggressive accounting practices that may violate law and the norms of financial integrity. One of the most successful corporations in the United States, Enron, declared bankruptcy in 2001 because of illegal and aggressive accounting practices. Although Enron's financial practices had been audited by public accountants, conflicts of interest prevented the auditors from stating a truly independent opinion regarding the financial integrity of Enron. Other serious business scandals made the lack of financial integrity appear to be a widespread and fundamental threat to the profit-based system of market capitalism. In response, the U.S. Congress passed the Sarbanes-Oxley Act of 2002 to compel publicly owned businesses to implement ethics management programs and for top management to certify by signature the financial integrity underlying the reporting of business profits. This has placed a significant burden of accountability on chief financial officers and chief executive officers.

Profit and Care for Stakeholders

The market context in which a business makes and allocates its profit depends on the decisions and actions of many interdependent parties or stakeholders—customers, suppliers, managers, employees, owners, and government. The quality of a business's relationships with these stakeholders can help or hinder its efforts to sustain itself as a profitable entity. Accordingly, it is critically important that a business operate in a manner that fosters trust and cooperation in these relationships. This is a challenging task because satisfying their preferences may conflict with the profit-making goal of business. For example, customers may demand low prices and costly features that together reduce profit. Employees may demand benefits that require financial resources to be allocated to their needs instead of going to profit. Owners may prefer that profit be distributed to them as dividends rather than reinvested in the business to pursue opportunities for future profit. Government regulatory regimes may increase business costs and limit the scope of permissible profit-making activities.

Business owners are primary stakeholders entitled to business profits to use as they see fit, subject to taxation. Thus, profit contributes to the liberty of business owners by giving them the economic means to realize their own preferences. For this reason, some consider taxation of profits distributed to owners as a reduction in shareholders' liberty for some other social purpose. Participatory government, such as democracy, provides a public policy mechanism for shareholders to participate in holding government accountable for the justice of such transfers of property. Citizenship, personal virtue, and self-interest are weighty principles to balance individual rights, utilitarian benefits, and universal rules of distributive justice.

Often, business owners employ professional managers as their agents to generate profit from the assets of the business. When owners cannot observe the actions of their managerial agents, however, the owners bear a moral hazard that managers might act in their own self-interest rather than in the best interest of the owners. Owners can reduce this risk by monitoring managers, but monitoring has costs. Thus, the good virtue of reliable professional managers increases profits both by putting owners' assets to their best use and also by reducing the costs of monitoring.

An economic view of profit-seeking businesses suggests that they are likely to charge as high a price as possible given their understanding of the conditions of competition and demand. Economic demand, however, is a quantitative expression of the needs and desires of real people, some of whom may not have the means to pay market prices. As Dr. Martin Luther King noted, it is an injustice to pursue profit without concern for the poor people of the earth, and excessive profit taking in a world where the necessities for human dignity are not fairly distributed may cause revolutionary and repressive cycles of violence. This concern for distributive justice is also found in Article 25 of the Universal Declaration of Human Rights adopted by the General Assembly of the United Nations in 1948. Thus, profit-seeking businesses show care for stakeholders by balancing their need for profit with the needs of customers and potential customers in economically disadvantaged communities. Broadening the scope of affordable products may be one way to achieve this balance. Recent efforts of major pharmaceutical companies to price drugs differently in developed and less developed countries is one example of such broadening. Government control of allowable rent that landlords can charge tenants for housing is another example.

Corporate social responsibility considers business performance for a broader set of stakeholders than just owners. For example, a triple bottom line (including financial, environmental, and social performance) values "reasonable profit" instead of maximum profit in order to address the ethics of a scope of duty beyond the creation of profit for owners. In the United States, legal support for a triple-bottom-line perspective is embedded in many laws governing business care for the environment and the conduct of due diligence in mergers and acquisitions.

Triple-bottom-line governance of profit has been criticized by some because it is dependent on the judgment of managerial agents constrained by the owners of capital who may be self-interested and remote from the needs of workers and communities. To respond to these criticisms, alternative mechanisms to generate and allocate profit include worker collectives, employee stock ownership plans, democratic capitalism, and market socialism.

Ethics and Types of Profit

The amount of revenue a business receives is determined by the price its customers pay for a quantity of its products and services and the costs it incurs to acquire factors of production (land, labor, and capital), knowledge and capabilities, and inputs of supplies and to operate processes that create its finished products and services. There are several different types of business profit that are identified by subtracting different categories of costs from revenue. These types include gross profit, operating profit, retained profit, and economic value added. Each type of profit highlights interesting ethical issues and dilemmas for further discussion.

Gross profit is calculated by subtracting the cost of sales from revenue. This cost includes the cost of supplies and materials that go into making the products, and so it reflects the business relationship with its suppliers. This relationship may be a function of several factors, including their relative market power and the degree of mutual trust and cooperation. For example, costs of goods may be reduced and profit increased for a business that uses its power legally to pursue efficient production and economies of scale. Furthermore, suppliers may be more accommodating and flexible in their contractual terms for trustworthy businesses that pose less of a moral hazard. Flexibility in contracting reduces transaction costs and thus increases profit.

Cost of sales also includes direct labor costs. Business may increase its profit by reducing its direct labor costs. There are several alternative approaches to reduce labor costs, including increasing the productivity of workers, locating labor-intensive operations in low-wage countries, and outsourcing operations to shift labor costs to other independent businesses. Recent trends toward globalism and free trade have encouraged business to source labor from low-wage areas of the world. As a result, many labor organizations and public policy makers in high-wage countries have argued for fairness and justice in helping workers make the transition to new employment opportunities. They point out the potential for social disruption if workers' prospects for a good quality of life are disadvantaged in a world order geared to enabling global opportunities for business profit.

Production costs also are subtracted from revenue to calculate gross profit. As discussed earlier, businesses reduce their production costs when they do not directly pay for all the costs of their effects on environment and community. Many advocacy groups prefer business to directly take on more of these costs and to accept responsibility for them. Unscrupulous businesses may also attempt to improve their profits by pricing their products to reflect high-quality production and materials while secretly substituting inferior processes and supplies. Government regulation and inspection often attempts to prevent such fraudulent profit-seeking practices.

Operating profits are calculated by subtracting selling, general, and administrative expenses from gross profit. The bulk of these expenses come from marketing expenses such as advertising and promotions, travel and entertainment, executive salaries, and sales agents' salaries and commissions. Recent discussion has focused attention on the fairness of these expenses in relation to business integrity and value-creating activities for society. For example, marketing practices in the U.S. pharmaceutical industry create demand by directly advertising pharmaceuticals to consumers or by rewarding doctors rather than by the merits of objective scientific research. In other industries, some unethical businesses may falsely advertise a scarce and valuable item at a low price as bait to lure customers but then switch them to a higher-priced and more profitable item from among the only ones available. Such bait-and-switch tactics are illegal in the United States.

The administrative expense category also raises issues of properly accounting for CEO pay and its relationship to business profitability. When CEO pay is tightly linked to business profitability, however, the executive has an incentive to be aggressive, perhaps inappropriately so, in the reporting of profits. This is one important reason why independent outside auditors without conflict of interest are necessary to ensure financial integrity in the reporting of business profit.

Taxes paid to the government are subtracted from operating profits, leaving profit after tax. Some view taxes on business profit as a confiscation of private property and an infringement of individual liberty by government for social purposes. This argument may have some weight in societies that tax business profit twice—once levied on the business and again when the profits are distributed to owners in the form of dividends. Others, however, note that business has similar responsibilities as does any citizen to support society by paying taxes. Because this civic duty can be a significant burden on profit, businesses often participate through lobbying activities in the public policy process that sets taxes. There are many discussions of the fairness, integrity, and legality of these lobbying activities and relationships businesses may use to reduce the impact of taxation on their profits. Interestingly, a libertarian business ethic argues that honest and full tax payments satisfy business responsibility to society. Unfortunately, some unprincipled businesses may resort to dishonest accounting or to black market operations to avoid paying taxes. This is another important reason for independent outside auditors without conflicts of interest to ensure financial integrity in the reporting of business profit.

Profit and the Ethics of Innovation

Profit seekers often strive for the first mover advantage that comes from introducing innovations to the marketplace. While there are potential rewards of profitability for successful innovation, there also are risks of failure that typically are borne by the owners of capital, their managerial agents, and their immediate stakeholders. For some innovative businesses, however, the risk of failure may have some small possibility of catastrophic failure. Current discussion focuses on such significant consequences in genomic commerce and nanotechnology. For example, profit seekers may create human-animal hybrids that enable animal diseases to leap the species divide and proliferate in human populations that have no immunity. Similarly, an existential threat may be posed should nanoparticles unexpectedly become embedded in human organs with no way to remove them. A precautionary principle to defer profit-seeking action until consequences and contingencies are better known has been more accepted outside the United States, as evidenced by the 1992 Rio Declaration on Environment and Development and the European Commission's Communication on the Precautionary Principle.

Conclusion

Smoothly functioning markets that maximize profits signal that welfare, defined as subjective self-interests of individuals, is maximized. To ensure smooth functioning, government must enforce contracts, protect private property, and tax to fund public goods. Discussion regarding business profit will continue to address the balance of incentives for wealth creation with rules and enforcement to protect stakeholders and the broader society against self-interest and opportunism.

—Greg Young

See also Accounting, Ethics of; Asymmetric Information; Bait-and-Switch Practices; Bankruptcy, Ethical Issues in; Black Market; Bluffing and Deception in Negotiations; Business, Purpose of; Business Law; Capitalism; Competition; Corporate Social Responsibility (CSR) and Corporate Social Performance (CSP); Cost-Benefit Analysis; Fiduciary Duty; Freedom of Contract; Free Market; Friedman, Milton; Internal Audit; Internal Revenue Service (IRS); Market Power; Outsourcing; Profit Maximization, Corporate Social Responsibility as; Rent Control; Sarbanes-Oxley Act of 2002; Shareholders; Social Costs; Transaction Costs; Triple Bottom Line; Wealth

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Promises

Promises are utterances or statements expressing an intention, resolution, or commitment to the promisee (one to whom the promise is made), thereby creating a new obligation to carry out the content of the utterance or statement. When a promise is made, the promisor (the one who is making the promise) understands that if the promise is not kept, then a moral obligation will have been breached. Keeping promises is critical to ethical business practice and is frequently viewed in relation to the obligation to be honest. Promises are the key to trust; thus, breaking a promise is generally a breach of trust. Furthermore, since many contracts are based on promises, a full understanding of promises is central to both moral and legal issues in the practice of business. This entry will examine the following issues: How is a promise different from other kinds of utterances or statements such as intention, resolution, or vow, which do not carry the same obligation? How does saying "I promise" create an obligation? Why is that obligation binding? Under what circumstances is it moral to break a promise? How is promise keeping important to the ethical practice of business?

Making Promises

One usually engages in economic transactions with a view to reciprocal advantage, but there are circumstances in which one cannot be certain that the other party will hold up its end of the bargain. In fact, from a standpoint of pure self-interest, it would seem advantageous *not* to perform on the promise if one has already received a benefit. Without promises, self-interested agents would not be willing to assume the risk involved in transactions requiring trust or future performance; this would limit economic efficiency, and one would miss out on many beneficial transactions. To overcome these problems, to cope with the uncertainty in such exchanges, one makes a promise—a form of words that affirm the performance of future acts to those outside one's normal sphere of interest and trust. To say or write "I promise" is not just to *say* or *write* something. It is also to *do* something—namely, to put oneself under an obligation and to make oneself responsible to potential sanction if the promise is not kept.

A basic issue with promises is how they differ from other types of language, such as statements of intention, vows, and commitments. Some argue that the difference is only a matter of degree, not of type. A promise, in this view, is a stronger level of commitment than an intention (where one could still change one's mind) and needs to be communicated in a social context (where intentions and vows do not necessarily need to be). In another view, promising is a species of consent. It is an expression of one's consent to restrict future behavior or liberty (to not change one's mind, to carry out a particular action) in exchange for present or future benefit.

Critics of these views argue that a promise is a fundamentally unique type of utterance or statement. They insist that it produces particular expectations and creates a right on the part of the promisee, who can choose whether or not to exercise this right, as well as a new obligation on the part of the promisor. Consequently, a promise is different because it creates confidence, reliance, and trust between the two parties in a way that statements of intentions, commitments, or vows do not.

Another important debate is whether making promises gives rise to the rules and practices that govern promise making or whether it is these social conventions that make a promise possible and meaningful. One line of thought is that the concept of a promise only makes sense against a background of these rules and practices—promise-making procedures, which delineate what it means to make a promise. In contrast, some believe that promises come first as an informal practice, and the more formal social conventions arise later to solve problems and regularize the practice.

One final issue in making promises is the false promise. If one is in difficult circumstances, can one make a promise that one knows one cannot keep? Self-interest and prudence might argue that it would be advantageous (especially in the short term) to make a promise, even if one has to renege on it later. On more careful examination, the long-term consequences of a false promise may be hard to accurately foresee, and the lie may cause more resultant inconveniences than keeping the promise. This line of thought is based on the fear of adverse consequences, but that may not be sufficient grounding for a moral obligation. When examining a false promise from the standpoint of duty, one must ask whether the maxim of the action (making a false promise to extricate oneself from difficulty) can be willed as a universal law. However, this would ultimately prove self-defeating. If that maxim were universal law, then any future promises would not be believed and accepted, or they would be retaliated against by making false promises in return. Therefore, one ought not, that is, one has a *moral* obligation not to, make false promises.

From the perspective of U.S. law (rooted in English common law), promises are binding and legally obligatory if (1) the promisor receives benefit from the promise, (2) the promisee acted to his or her detriment, and (3) there was a mutual exchange of promises. This suggests that the difference with promises is that one party gives something up and the other party gains a benefit, with the understanding that at some future point the roles would be reversed. A failure in this regard is viewed as a violation of justice in the sense of fairness.

Obligation to Keep Promises

Central to understanding the obligation to keep promises is the question of what it is about promises that creates a new obligation. How does one get from the utterance or statement to a moral obligation?

The first suggestion is that there is a basic, self-evident (via reason or moral intuition) moral principle that moral persons ought to keep their promises. Promise keeping is a basic duty that must be observed, although this duty must be considered in the larger context of other moral duties. In this view, there are competing moral duties, and one must make decisions about their relative weight and import.

The second suggestion is that the performance of promises, along with rules and conventions about private property, forms the foundation of justice. Promising is not natural; it is a product of social conventions. The concept of a promise would have no meaning or force without these conventions. One version of this argument has it that promises are founded on the interests and necessities of society. At first, the obligation to perform on a promise is due to self-interest, since not doing so will result in sanctions and adverse consequences. As the conventions governing promise making and promise keeping become a matter of public interest and convenience (as legal systems and economic transactions based on promises develop), a new obligation to keep promises is produced.

A different version of this argument says that since promises are based on social convention, there is no moral obligation to keep one's promises apart from the sanctions and penalties imposed by the law or the government. One keeps promises, in this view, *only* out of fear of sanction and punishment and self-interest; there never develops any mechanism for extended trust other than external sanctions from the law or state. Without sanctions and punishment, promises would be meaningless words.

Reputation

Reputation plays a crucial role in the discussion of promises, regarding both why one makes promises and what happens if one fails to keep them. One tends to receive promises from those people who do not habitually renege on their promises. When one makes a promise, one hands over one's reputation as a security deposit or collateral, which will be forfeited (or at least damaged) if the promise is not kept. It subjects the promisor to the sanction of being viewed as untrustworthy, and this will usually impair the promisor's ability to participate in such transactions in the future.

Reputation is a kind of commodity that one has an interest in preserving, like property. One perspective suggests that credit bureaus function as a kind of reporting agency on persons' reputations for keeping promises. One's credit score, reflecting the extent to which one keeps financial promises, can be traded on for financial gain and is increasingly used in job application processes or background checks to gauge how responsible and reliable an applicant is. In an analogous way, reputation is arguably a company's strongest asset; it helps the company acquire and keep customers, build business relationships, and attract employees and leads to higher stock valuation, which, in turn, makes it cheaper to raise capital. This concern for reputation may also broaden one's concerns from simple self-regarding interest to a concern for what others think. Many argue that this initiates the bonds of trust needed for both society and the efficient practice of business.

Trust

Some view promise keeping not as a universalizable rule but as a mechanism that builds relationships of trust. Keeping promises helps to build the bonds of trust in society, and failing to keep promises is a violation of trust. The concept of trust is closely connected to promising but includes more than just promising; there are aspects of trust related to other forms of commitment that are much less explicit than promising.

Trust, in this view, is an open-ended set of activities and practices. It is a flexible relationship that is not self-interested, not merely rule following, and not just a feeling. "Authentic" trust is self-aware, cognizant of its own conditions and limitations, open to new ideas, and based on choice and responsibility. It is not simply mechanical reliance or a prediction of what someone will do. One trusts a person and regards that person as trustworthy when he or she does what one justifiably expects. Trust is gained, therefore, by keeping promises, doing one's duty, discharging obligations, respecting others, and being honest. Consequently, trust is seen as a bond of society and a core value for the practice of business. To have authentic promise making and the social practices and benefits that come from it, one needs this phenomenon of reliance, of taking one at one's word, of committing to promises in a consistent way.

Breaking Promises

If there is such a strong obligation to keep promises, one might wonder if it is an absolute obligation. Are there ever circumstances under which it is either permitted or even ethical to break a promise? In general, breaking (or failing to keep) a promise is seen as either dishonesty—especially in the case where one made a promise that one had no intention of carrying out, simply to gain an advantage—or analogous to lying.

However, promises are not always binding. Where a promise is made by a child, by fraud or under coercion, or by misunderstanding or by mistake or in the case of an impossible or illegal or immoral promise, most commentators insist that one cannot be morally or legally bound to keep it. In these cases, there is either no obligation at all or there is an obligation, but the promisee has an obligation to release the promisor from that obligation.

There may also be appropriate reasons to break a promise. The circumstances may have been significantly altered via unforeseen events, bad luck, or intervention of fate, or the other party may have failed to keep its promises. Although a regular habit of promise breaking can breach trust or prevent it from getting off the ground in the first place, not every instance of breaking a promise is necessarily a breach of trust. The promise may not be performable because circumstances have changed, or the promise might even be renegotiated if the promisor comes clean that he or she has bitten off more than he or she can chew. In the latter case, one commentator argues that this is a confirmation of trust, not a violation of it.

Furthermore, it is possible to make an argument that breaking a promise in certain circumstances might promote the greater good or social utility and, therefore, can actually be the moral course of action. If keeping the promise would produce undue hardship on either of the parties, or if it would cause damage to the relationship, impair trust, or make future cooperation less likely by producing resentment or conflict, one might argue that it would be ethical to *not* require performance of the promise *in this case*. Those who take this line of thought are quick to point out that keeping promises on a regular basis is still important for social utility and that reputation is necessary as a measure of reliability and essential in forging bonds of trust.

In the case of hostile takeovers, there are two important issues related to promises. First, there is the charge that the practice of takeovers transfers wealth to the shareholders by violating implicit contracts or promises with the other stakeholders. Second, one might ask, Does the new management have to keep the promises made by the prior regime? Both these issues focus on the fact that making promises produces expectations; not meeting these expectations can produce adverse consequences for the company's reputation and its ability to maintain trust. If the expectations were contractual or actually promised, it would be unethical to break a promise, even if the new regime was not the one that made it. This is especially true if there were legitimate expectations, which most commentators insist need to be honored to preserve reputation and maintain trust.

Business Relationships

Business is a group activity, and at the core of successful business relationships is trustworthiness and promise keeping. Without these, the economic and social costs of doing business increase considerably. Many argue that promises and promise keeping enable markets and facilitate economic transactions with few or no legal strictures. As a social norm, promise keeping facilitates economic production by encouraging cooperation and accountability and discouraging predation. It helps promote fairness and economic prosperity (without which unfairness and inefficiency would reign), and it produces a kind of social capital in the form of reputation and trust that can be traded on as an intangible currency.

For some commentators, the idea of a social contract provides a significant source of norms in business, and promises form the foundation of the social contract. Businesses ought to keep promises in ad claims (avoid deceptive brand promises in marketing), return calls on time, keep personal promises (whether related to the business or other matters), meet financial commitments, and keep commitments to employees (time off, financial compensation, due recognition). Business also should not encourage inappropriate expectations. Trust is so important that legitimate expectations should be kept regardless of what form they take.

One area where this may seem to go against conventional business strategies is in marketing. Traditionally, marketing attributes desirable qualities—sexiness, wealth, beauty, power, coolness, or physical prowess—to the consumption of a product, the implied promise being that if one consumes the product, then these qualities will or may also be acquired. Many ads promise intangible benefits (status, well-being, the good life) from their products, on which it is very difficult or impossible to deliver. Other ads promise that their product is the "best," "freshest," "fastest," or some other superlative on which the company cannot possibly deliver, since multiple competing products claim the same qualities. One line of thought holds that these practices must change because (1) buyers want vendors who keep promises; (2) products are too complicated; and (3) repeat negotiations to find a new supplier are too costly, in terms of both time and money. Rather, businesses should see marketing in terms of developing a relationship of trust with the consumer, a relationship that must be maintained by the making and keeping of "authentic" promises.

Another concern is how one might measure the extent to which companies *are* keeping their promises. Clearly, various kinds of financial ratings can be a useful way to see how a business keeps certain kinds of promises, and reputation is seen as a key indicator, particularly in the long term. Social audits are also seen as a useful way to see if companies are keeping their promises about social, ethical, and environmental performance claims, since they allow for a process of self-reflection and intentional improvement in areas that are found to be weak.

Conclusion

The concept of making and keeping promises forms a basic and essential building block in the practice of ethical business because making a promise carries with it a special kind of ethical obligation to carry out that promise. If the promise is not kept, the promisor understands that he or she is failing in a central moral duty, as well as risking his or her reputation, violating trust, and impairing future relationships. In business, promise keeping is seen as a core value and basic obligation since it directly affects a company's reputation, while failing to keep or breaking promises can undermine trust and will ultimately raise the social and economic costs of doing business.

—Pauline Kaurin

See also Contracts; Deceptive Advertising; Social Contract Theory; Trust

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Property and Property Rights

To have a right of property or to own property is to have, with regard to some resource or thing, a relation to other people that establishes a rightful claim as to how one may use, enjoy, or deploy that resource. Although we often think of property in terms of some material good or resource (e.g., "This land is my property"), the assertion of property, property ownership, or a property right is, in fact, a statement that one's relation to that thing is defined in terms of rules that establish what one may do with that thing and what others may or may not do. If one owns one's bicycle, then one has the right to drive it on a municipal street, to paint it blue rather than red, or to loan it for a fee. If one owns one's house and the land on which it sits, then one may plant a flower garden on the south side, paint the shutters, attach a porch, or sell the house and land to someone else. However, ownership may not include a right to build a bonfire on one's front lawn or to raise swine or chickens in the backyard.

The concept of property has played a pivotal role in political and social philosophies throughout the ages, and since ancient Greece, property has been regarded as a fundamental institution of society. In what follows, the major focus is on the nature of property rights, specifically, the rights of private ownership or private property. What is the importance of private property? What goods in society should be privately rather than publicly held? As a first approximation, one may note that private property is an institution essential to business. Market exchange involves a transfer of property from one person (or organization) to another. Private property has other important functions in market societies. Private property ensures that current owners take into account future income, thus ensuring that the owners consider the long-run effects of their decisions. Since private property is necessary for exchange and since it encourages prudential decision making, it is an institution essential to business competition. Thus, private property provides the foundation for the complex or spontaneous order that characterizes markets.

Conceptual Issues

The concept of property refers less to the material resource than to ways of relating to that resource. Property is often understood in terms of a set or bundle of rights. The rights in question may be considered—at least typically or for the most part—as *claims*: A person's right to X entails a claim that others either act or forbear to act in certain ways. If these other persons fail to act or forbear to act in the appropriate way, then they may be compelled to do so. A right (or rights) to property may be further specified in terms of who holds the right, who must honor the right through an action or forbearance, and what sort of acts or forbearances are required. A complete discussion would also include an account of when the right is violated and how such a violation may be remedied and by what means.

Early in the 20th century, Wesley Hohfeld analyzed the concept of a right into a set of four categories: a claim, a liberty, an immunity, or a power (or privilege). Liberties and claims share entailments to one another, as do immunities and powers. The first pair of categories is most relevant to an analysis of a property right. For example, if a person P possesses a liberty to do some act, then another person Q has no claim against P that P either perform or not perform that action. For example, if I am at liberty, with respect to all others, to buy a car, then no one has a claim that I buy the car or that I not buy it. However, let us suppose that there is but one car and that I am at liberty to buy it. That I am at liberty to buy the car does not entail, however, that no one else is at liberty to do so. For other individuals may have the same liberty and another person may succeed in purchasing the car before I can do so! Other rights do involve claims. Person P has a claim right that another person Q not perform some action if and only if Q has a duty *not* to do that act. And if Q has a duty not to perform that action, then Q is not at liberty to carry it out. If we apply this analysis to property, then, as we will see below, within John Locke's state of nature, each person is at liberty to mix his labor with an unowned resource. Thus, once I mix my labor with an unowned resource, I have a claim right to that property such that you may not justifiably interfere with my possession. Thus, my claim right limits your liberty. Such a right may also be understood to be a *negative* rather than a *positive* right in the sense that it requires that you refrain from doing an action (interfering with my property), not that you perform some specific action. If I own property, then I possess a liberty to act toward that property in certain ways, but others do not. (The other pair of Hohfeldian categories may be understood as follows: A *power* entails that one can alter or change another's liberties, claims, or duties; the party subject to such change has a *liability.* Regulatory agencies or Congress, for example, have certain powers with respect to business firms. If a person has an *immunity,* on the other hand, then another has a disability to alter that individual's rights.)

Turning to property rights or ownership, A. M. Honoré describes 11 features of the concept of "full" ownership. These attributes constitute a complete and unrestricted notion of ownership. Although all these attributes need not be present to assert that one owns something, some of them are necessary in any instance of ownership. The attributes include the right to *possession* (the right to exclude others, which holds *in rem*, against persons in general, rather than *in personam*, against particular individuals); the right to *use* the resource for one's personal enjoyment or benefit; the right to *manage* the thing, to decide how it is to be used; the right to the *income* derived from the object or thing; the right to the *capital* (specifically, the right to alienate, consume, modify, or destroy); the right to *security* from expropriation; the right to *transmit*; and four additional attributes, including indeterminate length of ownership; a duty not to use the thing in ways harmful to others; the fact of liability (so that the resource may be taken as payment for debt); and the residual nature of the object, such that if a right lapses it returns to the original owner. These 11 attributes, constituting a variety of claims, powers, and liberties, are necessary for *full* ownership, even though we often speak of "ownership" when some of these attributes are absent. Each attribute may be subject to varying applications and interpretations. The first five seem to be the most significant, with possession (the right to exclude), use, and capital as particularly crucial. In the case of owning a home, one may have the full complement of the 11 attributes, but in the case of owning, say, a mutual fund, one has a right to the income, but one does not have a right to manage the fund.

Kinds of Property

The conceptual accounts just delineated are compatible with distinct kinds of property: private, collective, and communal. Private property is that form of property for which an individual (or a small set of named persons) has rights of management and exclusion, among others. Communal property, however, may be understood in terms of a resource that may be used freely by all members of a group (excluding nonmembers) but whose general use is determined by custom, tradition, government, or even individual users. Examples of communal property might include common grazing lands (as in the medieval commons) or public parks. Although the family home is a quintessential case of private property, the structures of ownership *within* the house are typically communal rather than private: The sofas and chairs in the living room or den are open to the use of family members and are not owned by particular members of the family. Thus, communal ownership need not entail government ownership. Collective property refers to some thing or resource whose use has a specific purpose (as defined by the government or the group as a whole) that purports to satisfy some general interest of a group or whole. For example, a government building is collective property, as is a government-owned industrial concern or housing project.

Honoré's bundle of rights may apply as much to collective or communal ownership as to private. For example, a collectively owned property may be a resource in which nonmembers are excluded and that is managed by some group appointed by the collective, and so on. In the United States, approximately 30% of the land is owned by the government, and much of this land is more communal (such as parks or range land) than collective. Robert Ellickson has pointed out that different types of property have distinct incentives and diverging costs and advantages. Private property, for example, may be preferable for small and medium enterprises. The recognition that property may be of distinct kinds is an important consideration, but the remainder of this discussion focuses on private property.

What sort of things may one have property over? Property is often considered in terms of tangible or real property in land, resources, or specific goods. Other forms of property are intangible or abstract and include all sorts of financial instruments, such as stocks and bonds, as well as forms of intellectual property. For example, copyright law expresses the common assumption that ideas originate with a person or persons and that those who have discovered or elaborated an idea should have the opportunity to reap the benefits of their efforts.

Among tangible goods, one of the first if not the most fundamental of property rights is that over one's person or body. (John Locke takes this to be the principal form of property, a natural right.) Many of Honoré's rights of ownership seem to establish exactly the ownership of self. A right to use, to manage, or to exclude the interference or actions of others would seem to hold of the self (or body), implying thereby that each person has an ownership right in the self. However, it is not obvious that the right to one's physical body (part of, if not identical to, the self) would be the same type of ownership as a right to own furniture. If one owns a chair, then one may destroy the chair, remove its legs, or sell it to another person. It is not obvious that the ownership of one's body would allow one to destroy oneself, to amputate one's healthy legs, or to sell oneself into slavery. Some might contend that differences such as these suggest that we do not really own the body or self. In such a view, it is argued, one must distinguish between having ownership of self and enjoying rules that protect one's interests or exclude others from certain sorts of actions.

A corollary question is the extent to which human beings may claim ownership of other living species. There are commonsense cases in which we easily accept ownership, as in the case of owning a goldfish, a hamster, or a dog. Yet in these instances the ownership is distinct from other types of ownership, in particular in the kinds of rights that one may claim. Some have argued that ownership should be extended to endangered species. Those who defend this argument point out that a significant reason that some species are endangered is because the animals are treated as a commons in which no single individual has any incentive to care for the animals or to take into consideration the long-run survival of that species. Rather, in these circumstances, each individual has an incentive to kill or hunt as many of the animals as he or she can before someone else does the same.

Apart from the particular kinds of things that we might have property over, there is another way of understanding property rights. Are these rights conventional or legal, human rights, or natural rights? A legal right is a right recognized within some actual legal system; a human right is a right that pertains only to human beings; a natural right is a right that is grounded in some feature of nature and is considered to hold regardless of what convention or legal systems allow. A human right may be understood to be either a natural right or a legal right. Taking this into account, a *moral* justification of property is a justification in which it is argued that property is a human or a natural right. There are a variety of such justifications.

Justifications of Private Property

A justification of property may take one of several forms. One basic justification purports to show why there should be some rules of property (private, communal, or collective) rather than no such rules. A second sort of justification seeks to show that one kind of property is justifiable (or preferable to another set)—for example, that the institution of private property is justified (or that private ownership of land is preferable to communal). A third sort of justification seeks to show why some particular person (or group) ought to have a right to this particular thing. The accounts that follow focus largely on the second sort of justification.

The philosophers of ancient Greece discussed the institution of private property in relation to its effect on virtue and the good life. However, Plato, in the *Republic,* argued that those who are to serve as rulers (or as warriors) should live in communal conditions to preserve unity and to guard against the emergence of private interests that would draw these rulers away from the public good. In contrast, Aristotle suggested that property was essential to moral goodness. In his *Politics* (Book II), Aristotle notes that those resources or goods that are held in common will receive less attention and care than those held by individuals. For Aristotle, in contrast to Plato, common property may generate discord, for it will encourage the lazy to reap rewards commensurate with those who work hard. Private property, on the other hand, not only encourages responsibility but is also essential for other virtues, including friendship, generosity, and self-control.

Instrumentalist Justifications

The concerns of the ancient Greeks point to a more general kind of argument for private property—that it is a means or instrument to some other good(s). Such instrumentalist justifications are consequentialist but not utilitarian. For example, property may be taken as an essential means to secure liberty. Private property secures a sphere in which one may act freely, and it also ensures that, against the power of the state, there will exist several and dispersed sources of material wealth. Property-owning individuals, and those contracting with them, will have the independence to oppose social pressures of conformity, whether coming from the majority culture or the government. This was certainly the argument of Thomas Jefferson, as well as defenders of the agrarian ideal, who found in the landowning farmer the independence and responsible virtue necessary for a free society. More recently, Milton Friedman has argued (*Capitalism and Freedom*) that political freedoms, such as those of speech and the press, depend on private property and that such property ensures political liberty more generally. A different kind of instrumentalist argument for private property rights has been forwarded by Friedrich Hayek, who contends (*The Constitution of Liberty*) that several (or private) property allows for the generation of a spontaneous order. Not discounting the argument for liberty, Hayek contends that dispersed property provides the conditions for voluntary cooperation and productive innovation, thereby bringing about a vibrant and wealthy society, a spontaneous order that is more complex than could have been designed by collective decision making. There are, in fact, correlations between standards of living and the protection of property rights: Nations that have secure protection of such rights (as well as other rights) generally have more wealth (and freedom) than nations that have tenuous protection of property rights. Hayek's account of spontaneous order, not to mention Adam Smith's system of "natural liberty," provides evidence of how the institutionalization of secure property rights may generate an unintended social order of great complexity.

Property as Freedom

Somewhat distinct from the instrumentalist argument that property is a means to freedom or social benefits is the argument that *identifies* property and freedom. As articulated by some contemporary libertarians, this argument maintains that since freedom involves acting without interference from others, property alone effectively defines that sphere within which one may act freely. Within the confines of one's own property, one is free to do what one wants and to choose with whom one wants to contract. Even if one argues that the private property rights of one person also *limit* (as do all rights) the liberties of others, who are no longer free to use that property, the guarantees of property also ensure transmissions of rights. Thus, if I own some land, then I may also transfer that land to you, by a rental agreement, thereby ensuring for you a right of use that is secure from interference from me and from the state.

The identification of property and liberty is not, however, so obvious. Among contemporary philosophical theories, John Rawls's theory of justice is notable for how it does not discuss the issue of property. In his *Theory of Justice* and his *Political Liberalism*, he leaves open the question of whether the principles of justice, especially the first principle of liberty, require that productive property be privately owned. Rawls declares that one of the basic liberties is personal property, but this sort of property does not entail that the basic economic arrangements of society must include private ownership of productive property or that freedom of contract may include all market exchanges. Rawls's account suggests, therefore, that private ownership is not essential to liberty and, as he affirms more explicitly, that forms of market socialism are compatible with principles of justice.

Occupancy, Labor, and Natural Rights

Apart from these general arguments for private property, there are significant arguments based on occupancy and labor, of which the most notable is Locke's labor theory of natural property rights. Before turning to Locke's theory, it is best to note how one might seek to justify the property of a particular person by appealing to some notion of first occupancy: Given some unowned resource, whoever manages to occupy it first has a justifiable claim to it. In the *Metaphysics of Morals*, Immanuel Kant contends that the actual possession of the first occupant must be legitimated within a civil society in which everyone's will and interests are respected. A contemporary argument is that of Carol Rose, who suggests that so long as some institution of property is legitimate, then a prima facie rule of first occupancy is the most efficient. The contemporary Austrian economist Israel Kirzner has also suggested that we might consider, in relation to profits and property, an application of the general intuition of "finders keepers": Insofar as one creates, discovers, or notices that which others have not, then it is one's own to keep.

John Locke's labor theory of property is a notable argument that extends the idea of first occupation and, in so doing, attempts to establish both the legitimacy of private property and an account of why a particular person may justifiably hold an ownership right over a previously unowned resource. In his *Second Treatise of Government,* Locke begins by describing a state of nature in which the land is held as a commons and individuals, each bearing natural rights to life and liberty, live together freely. What actions would generate a right of private ownership? Locke begins with the assertion of self-ownership. Since the individual owns himself or herself (to include one's body, acts, thoughts, and beliefs), the individual owns his or her labor. When one "mixes" one's labor with some unowned resource, then one's property in the self is extended to that material resource and one acquires, thereby, a property in that resource that excludes any other person.

Locke places a significant proviso on this account: One may acquire property only so long as one leaves "enough and as good" for others. If one interprets this clause as making an assertion about the appropriation of finite resources, then it is never possible to take some plot of land and to leave enough and as good for others: If at any point the property of one person is disallowed by this proviso, then so is everyone's property acquisition. However, if the proviso is understood to refer to the *value* of things, then appropriation is not only justified but is perhaps preferable to all other options. For it is precisely Locke's point that private appropriation also creates value (benefits) where none had previously existed. In this sense, the very act of private appropriation may increase resources rather than diminish them, thereby generating benefits and enlarging the options available to all. If the alternative to private appropriation is that of leaving the goods in the commons, then there will be little incentive for any individual to cultivate land if the cultivated land may then be appropriated by anyone regardless of effort or contribution. To leave resources in a commons is, as David Schmidtz has argued, to leave everyone worse off than if the land were privately appropriated.

Utilitarian Justifications

Locke's argument is a natural rights argument that is accompanied by an account of the benefits of the institution of property ownership. The idea that property has such benefits was developed in the 18th century by, among others, David Hume. In his *Treatise of Human Nature,* Hume contends that property is not so much a natural right, as Locke suggested, as a rule or convention that arises gradually, if not unintentionally, over time. Given a scarcity of resources, limited benevolence, and conflicting ends, social cooperation will not be possible unless we agree to ensure the security or stability of our possessions (and their secure transfer via contract). As rules of property emerge, perhaps taking on diverse forms across societies and social groups, social cooperation is made possible, as well as ongoing commerce and industry. Emerging against universal circumstances and a uniform human nature, these conventions are, in Hume's account, laws of nature whose presence also assumes moral legitimacy as we recognize the general benefits that they generate.

One may, however, generate a more explicit utilitarian doctrine according to which private property is the preferred institution for maximizing utility, whether utility is understood in terms of wealth, preferences, or happiness. Clearly, it is argued, some institution for assigning goods is necessary, and the institution selected should provide security and liberty for creation and experimentation, as well as an incentive to use one's resources and labor as efficiently as possible. In general, the best institution for doing so is that of private property. That said, for the utilitarian, the actual constellation or mix of private, collective, or communal property is determined by a consideration of the type of resource in question. Thus, utilitarian arguments need not conclude that *all* property must be private: The mix of private and public property may differ depending on particular circumstances and traditions as well as the types of resources to be owned.

Property and Personality

Alongside the instrumentalist, the Lockean, and the utilitarian justifications of property, there is that of the 19th-century German philosopher G.W. F. Hegel. In his *Philosophy of Right*, Hegel contends that property should be understood as the expression or embodiment of one's will. An individual's free personality must find an external embodiment, and property constitutes the actualization of one's freedom. Out of one's subjective actions and decisions, one develops a material and external embodiment of oneself. This objective embodiment, unlike mere possession, also requires the recognition of others. For Hegel, then, property has an inescapably social component. This sort of argument that links property to personality would, unlike the Lockean or the utilitarian account, seem to entail that each person should have property.

Criticisms of Property Rights

Apart from criticisms of particular aspects of specific justifications of property, there are general criticisms of private property. Some have argued that property ownership entails that owners have power over others. Morris R. Cohen notably asserted that "the essence of private property is always the right to exclude others." It may be admitted, for example, that a property right may limit the liberty of another person to use one's property, but it is not obvious that a system of property rights or an individual's particular ownership of property entails power over others, including those who do not own property. Institutions of private property may, in fact, increase options rather than decrease them. Private property provides incentives to innovate and to produce new goods and services, the net effect of which is to generate more rather than fewer choices. Nonetheless, a property owner, such as a factory owner, may direct the activities of those who are employed by him or her. This sort of direction need not be objectionable insofar as the employee is free to go elsewhere for work. Further protection of workers may be sought through government regulation of working hours, working conditions, wages, and benefits.

It was Karl Marx who argued, more generally, that private property allows one class to exploit the productivity of another class. Property owners have the purchasing power to secure the labor of others who do not own property but must labor to survive. As the propertied class or bourgeoisie accumulates wealth, the means to exploit the laboring classes increase, alienating the workers from their very actions and from one another. Under common ownership, Marx contends, the worker is no longer alienated from his or her labor because the work is no longer a means to an end but an end in itself. However, the Marxist analysis has been subject to withering criticism. Both Ludwig von Mises and Hayek argued that a fully functioning socialist economy could not achieve any sort of efficient operation without the incentives that operate in a private property economy. How will the governing directors of the economy know what to produce, how to produce it, and by what means unless freely determined prices emerge out of the competitive interaction of privately run firms? Such prices provide signals as to what people desire and how these desires might be efficiently met.

Nonetheless, critics also charge that a market economy of private firms and corporations will create or perpetuate great inequalities of wealth and income. Even if there is movement among or between social classes, that does not help the person or groups who have little or no property: Those who do not possess property will be at the mercy of those who do. If one holds, however, that property ownership need not be absolute, a market economy is compatible with taxation policies that seek redistribution of wealth or that attempt to ensure some economic threshold below which no one will fall.

Applications and Considerations

Property is a relevant consideration for a variety of topics and controversies in business ethics. It is worth recalling that the practice of business is, in fact, the exchange of property for profit. Property includes a right of management or use, and the question of what constitutes legitimate management or use arises in a variety of areas.

Some of the questions at the intersection of business ethics and property rights are also questions of constitutional import. As the fundamental law of the land, a constitution has significant effects on the legal status of property. John Locke, for example, had a great influence on the outlook of those who devised the U.S. Constitution. Many of the signatories to the Constitution maintained that its very purpose was to protect property and that doing so would preserve life and liberty. James Madison, following the ideas of Locke, maintained that the primary function of the government was to protect property, to include one's life and estate. Even so, the Constitution makes scant reference to "property," a fact that does not gainsay its importance, for the founders regarded the right to acquire and hold property as part of the common-law inheritance, scarcely in need of written constitution. Article IV of the Constitution includes the "Property Clause," which specifies that Congress shall have power to make rules and regulations on property belonging to the United States. More notably, the Fifth Amendment includes the "Takings Clause," which specifies that property shall not be "taken for public use, without just compensation." This clause attempts to ensure that no single property owner must bear the burden of a public use that should be borne by all. The phrasing also suggests a distinction, not always clear, between the *use* of property and the *devaluation* of that property for the owner. For example, regulations that serve to inhibit or prohibit an economic activity on one's property may devalue that property. The Supreme Court has invoked the Takings Clause to invalidate some laws or regulations that effectively deprive an owner of an economic use for the property. Most recently, however, in *Kelo v. City of New London* in 2005, the Court ruled that eminent domain is permissible if the taking of the property will generate "public benefits." This suggests a broader notion of "public use" than the traditional and would seem to allow for private property to be taken and allocated to another party if only that party will generate greater tax revenue for the state.

Constitutional and moral questions have surfaced with regard to questions of employment and working conditions. For example, whether the right to use and to manage one's property includes a right to discriminate is relevant to discussions of affirmative action. Similar questions of use and management affect the status of contracts and working conditions. If an owner should be free to dispose of his property as he sees fit, then this might permit exchanges otherwise prohibited by minimum-wage laws or allow the disposal of hazardous materials on one's own property. Similar considerations of management and use arise in discussions concerning regulations that place constraints on the sort or degree of risk an employer or owner may require of an employee.

The value of property rights also arises with regard to corporate governance. Should the corporation be managed for the benefit of its owners, the stockholders, or for those stakeholders who have a significant interest in the success of the corporation? One may argue that a stockholder or shareholder *owns* stock and that managers therefore have a fiduciary duty to these owners, a duty that trumps any obligations to stakeholders. The stockholder, for example, has succeeded in buying the ownership shares precisely because he or she has consumed less than he or she earns. It is to society's benefit that resources be put to the most productive uses; the management of corporations in the interest of the owners (stockholders) should ensure this better than the stakeholding alternative. Others argue, however, that the sort of property relation that exists between stockholders and shares in a corporation is distinct from the ownership relation of, say, a homeowner to his or her home. The homeowner is responsible and liable in a way that a stockholder is not, and the property of the stockholder is held solely for profit. The call for the corporation to be managed with an eye to stakeholders, as well as stockholders, also rests on an appeal to a moral principle of respect for those affected by the decisions of the corporation.

Although we often think of ownership as referring to land or material resources, there is also intellectual property in ideas, discoveries, or inventions. Originally invoked for written documents, a copyright grants to the originating party an exclusive right to copy or sell a product; a patent provides, for a specified interval, protection for inventions, discoveries, or innovations. The arguments for copyright are both nonconsequentialist and consequentialist. The consequentialist arguments center on how copying will generate a decline in the prices of the good and reduce the incentives for its production. The nonconsequentialist argument stipulates that copying the work of another, including computer software, is theft. In this view, for example, the author or programmer has a property right in the work, and copying violates that right. Setting aside the consequentialist argument, the nonconsequentialist claims are not so obvious as they first appear—especially if one takes property rights to be important. A copyright law has the effect of prohibiting others from using their own property, including their own minds as well as their own material resources. For example, if an author writes a novel and then sells that novel to another person, why should that person be prohibited from copying that novel and selling it himself (preserving the name of the original author rather than passing himself or herself off as the author, which would be fraudulent)? Of course, if the author of the novel (rather like the manufacturers of computer software) sells the book on condition that no one else replicate it, then any replication on the part of the buyer is a violation of the contractual agreement. In the case of patents, if one person discovers a new use for some chemical agent and patents that invention, then anyone else who, independently, discovers the same thing is prohibited from using that discovery, even though the discovery was wrought through that individual's own effort and resources. These brief considerations would suggest that the nonconsequentialist arguments for intellectual property rights are, by their very appeal to property, quite controversial.

It is often assumed that private property and market transactions generate negative externalities such as pollution and environmental damage (not to mention the depletion of natural resources). Yet it is not obvious that this should be taken for granted. In the ideal case, property law should ensure that all negative externalities, and presumably all benefits, would accrue only to those engaged in production or in the exchange. As an illustration, if property rights are enforced, then the factory down the street cannot spew smoke that will affect others living nearby on their property. If this occurs, the third party is bearing some of the costs of an exchange between the factory owners and the consumers of the factory's products. In a real sense, then, many environmental problems result not from private property but from its absence or its nonenforcement. Property enthusiasts have maintained that the enforcement of clear property rules may do a better job of altering incentives and internalizing costs than do regulations, pollution taxes, or tradable permits.

Considerations of property and the institutions of property also have significant relevance to issues of privatization and globalization. If the legal enforcement of property rights is essential to the growth of wealth, then one of the most important elements for economic development will be the institutionalization of a rule of law. The rule of law not only allows for the recognition and enforcement of property but also serves to discourage the use of bribery. The importance of the rule of law in maintaining legitimate property rights has come to the fore as formerly Communist nations have attempted to privatize industries that had been collectively owned and managed by state officials. One clear lesson is that genuine privatization must include the recognition and enforcement of property rights and contracts, along with the institutionalization of the rule of law and the staffing of regulatory agencies by persons who are committed to an impartial administration of rules of property and contract. Even these reforms do not, however, answer the question of who is the proper owner of the companies to be privatized. It is not at all obvious that the owners are those who had formerly managed or worked in these organizations, as has been assumed in many countries, for many of those who managed state firms may have done so only because of their affiliation with the Communist Party.

Finally, business ethicists often appeal to the principle and value of autonomy. Property offers one means of ensuring autonomy, for it grants to the owner the rights of decision, use, and control. Whether the link between autonomy and property entails a classical liberal approach to business and society or one that favors a more egalitarian distribution of property is a question of some importance. It also serves as a reminder of how the consideration of a fundamental institution such as property is relevant to the very issue of choice and moral decision.

—F. Eugene Heath

See also Agrarianism; Anarchism; Aristotle; Capitalism; Communism; Copyrights; Economic Incentives; Externalities; Friedman, Milton; Hayek, Friedrich A.; Human Rights; Individualism; Intellectual Property; Invisible Hand; Kant, Immanuel; Locke, John; Management, Ethics of; Marx, Karl; Nationalization; Nozick, Robert; Patents; Rawls, John; Regulation and Regulatory Agencies; Self-Ownership; Shareholder Model of Corporate Governance; Socialism; Spontaneous Order; Wealth Creation

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PROTESTANT WORK ETHIC

We are a culture whose history is steeped in the hard work and accomplishments of our pioneering forebears. Our most ingrained cultural constant and our enduring national myth is what Max Weber dubbed the Protestant Work Ethic. At its core, the Protestant Work Ethic is the conviction that all work, any work, is good, noble, and a demonstration of diligence and duty. It is also an active demonstration of religious devotion and piety, as well as commitment to the perfectibility of the "human condition" at both the material and the spiritual level.

Most historians attribute the origin of the work ethic to Martin Luther. According to Luther, one was summoned by God to a secular "calling," which today we would call a job, profession, or career. Before Luther, most work was looked on as a curse more than a calling. To the ancient Greeks, whose physical labor was in large part done by slaves, work brutalized the mind and made workers unfit for the practice of humanizing virtues. The Greeks regarded work as drudgery, an activity to be conducted with a heavy heart. Work enslaved the workers to the task, corrupted the soul, and impeded the worker's pursuit of "the good life."

Luther stressed that all work, all callings were necessary to life. No calling was to be recognized as more necessary or blessed than another, and therefore, all callings were of equal worth in the sight of God. For Luther, work was a form of serving God. Thus, the only way to live acceptably before God was through devotion to one's calling.

With John Calvin in the 16th century, we find Luther's ideas extended, systematized, and institutionalized. Work was the will of God, and even ceaseless dumb toil sufficed to please him. Calvin preached the predestination of the elect. He believed that the elect could be recognized by certain outward signs, which included self-denial and devotion to duty, and that God caused the elect to prosper. "To prosper" or "to succeed" meant to enjoy not only wealth and happiness on earth but also eternal salvation. Success was the symbol of selective salvation. Calvin managed, no matter how indirectly, to provide a rationale that linked work and the divine with material success and comfort.

In *The Protestant Ethic and the Spirit of Capitalism,* Max Weber observed that the rise of Protestantism and the rise of capitalism generally coincided in England and throughout most European countries. Weber's explanation was that many basic Protestant ideas encouraged capitalistic activities. For example, Protestantism taught that each person would be individually judged by God and that judgment would be based on one's whole life's work or "calling." Protestantism also taught that the fruit of one's calling—money—should not be spent frivolously or unnecessarily. According to Weber, these ideas led to a life of hard work, self-discipline, asceticism, and concern with achievement. This ethic helped advance the rise of the private entrepreneur in that it led to the accumulation of money that would not be spent on luxuries but that could and should be put into one's own business.

The direct theological descendants of the Protestant Reformation, and of John Calvin in particular, were the Puritans who migrated to New England. Citing the biblical parable of the talents in Chapter 25 of the book of Matthew, Calvin urged the Puritans to prosper. The gospel of work in America was also preached from many other pulpits. William Penn constantly reminded the Quakers that diligence and frugality were virtues.

Perhaps the final solidification of the work ethic in America occurred with its practical translation and secularization by Benjamin Franklin. In his various publications, Franklin taught that wealth was the result of virtue and the proper display of character. In his *Autobiography,* he defines the ethic of work in his list of ideal traits. With Franklin, the work ethic shifted from a direct form of worshipping God to an indirect way of rendering service to God by developing one's character and doing good to others. Unlike the Puritans, Franklin's craftsman no longer worked for God's glory but for himself. Franklin maintained that God helped those who helped themselves. Nevertheless, hard work remained the primary standard for private success and social usefulness.

By the 19th century, the Protestant ethic in America had changed its name at least three times, but its essential focus had not changed at all. Whether it was called the Protestant ethic, the Puritan ethic, the work ethic, or the immigrant ethic, hard work was seen as good in and of itself—the only ticket to survival and the possibility of success.

According to the noted labor historian Daniel Rodgers, the central premise of the work ethic is that work forms the core of the moral life. Work, said Rodgers, made men useful in a world of economic scarcity. It staved off the doubts and temptations that preyed on idleness; it opened the way to deserved wealth and status; it allowed one to put the impress of mind and skill on the material world. In many ways, the work ethic posited one's very right to existence. One achieved worth through work. Work is the means by which we achieve status, stuff, and success.

—Al Gini

See also Right to Work; Violence in the Workplace; Well-Being; Worker Rights Consortium (WRC); Working Conditions; Work-Life Balance

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PRUDENCE

Prudence is good judgment in the pursuit of one's interests. A prudent person characteristically acts in a rationally self-interested way, with long-term considerations in mind. An imprudent person might pursue short-term pleasures and later deal with bad consequences that outweigh the pleasures. Prudence is therefore not just a matter of desire satisfaction; in fact, prudence often involves deferring gratification in aid of maximizing it. Prudence is a virtue in a manager or a professional person, particularly one who is another person's agent. Imprudence in one's own case is foolish; imprudence on another's behalf is morally irresponsible.

A prudent investor takes rational risks. One's risk curve depends on how one evaluates certain possible states, particularly gains or losses. Your risk curve may differ from mine without either of us being imprudent. You are imprudent if you invest in ways that ignore your evaluations or if your evaluations turn out to be mistaken—if, for example, it turns out that you mind losing $1,000 much more than you thought you would.

In popular usage, the notion of prudence carries the connotation of undue caution. This is not how moral philosophers have historically understood prudence. Aristotle argues that prudence is the virtue that entails all others. So courage, for example, is of a piece with prudence. A courageous person knows when to stand and fight and when to run; he or she habitually makes that sort of distinction rationally, even when in danger.

Prudence is of particular interest to virtue ethicists, who follow Aristotle in believing that ethics is primarily about being a certain sort of person rather than acting according to certain principles. So a courageous person, a species of prudent person, fears what is in fact worth fearing and acts accordingly. This does not involve weighing the personal rewards and costs in (say) a utilitarian way but instead has to do with acting on well-habituated moral intuition supported by emotion. In particular, it would not be characteristic of a courageous person to run because others are probably going to run; the courageous person might stand and fight futilely. An agent who looks for utilitarian grounds for not exercising a certain virtue is in danger of losing that virtue. That would be bad for the agent in the long run.

In some ways, prudent people and well-managed companies are similar. They have an agenda that is based on certain values that stand them in good stead in the long term. But creating that sort of organization and the strategic capacity that it requires is difficult, and most firms are not that good. Similarly, if you are a prudent person with coherent and sustainable values that regularly inform your desires and drive your actions, you are a rare bird. For contrary to what many economists presuppose, people do not always act in a self-interested way. They may be ignorant of probable consequences or they may have incoherent values. Sometimes they consciously act against their values.

Aristotle calls prudence (*phronesis*) a virtue, a component of character that is part of a good life—in fact, a sufficient condition of all the virtues. A prudent person is a self-interested one, but that raises a problem. One might wonder whether prudence is an ethical virtue, for ethics is surely about the interests of others, and selfishness is a vice. Kant is one of many philosophers who distinguish the prudential from the ethical: The dear self is the beneficiary of the former and interferes with the latter.

Aristotle differs from most modern moral philosophers in that he does not presuppose that morality is necessarily about the interests of people other than oneself. Ethics is about the good life, primarily a life of personal fulfillment. Philosophers have often asked why one should be ethical—that is, what self-interested reason one has for being ethical. Arguing that one should be prudent in Aristotle's sense would not answer the question, for one would still have to show that his form of prudence qualifies as a genuinely ethical trait.

Aristotle does not claim that doing the right thing will make one happy. His claim is rather that being the sort of person who characteristically does the right (courageous, benevolent, honest) thing will make one a happy person. The argument begins by denying that the difference between a good person and a bad one is that the bad person does what is enjoyable while the good person is willing to set aside enjoyment and instead do the right thing. This suggests that prudence is antithetical to morality. On the contrary, Aristotle claims, the person of good character, the prudent person, is one who enjoys doing the right thing. Enjoying doing the wrong thing is a sign of bad character. The claim is compelling. Surely it is not preferable to be the sort of person who does the right thing reluctantly.

We must not assume that what is in one's interests is independent of one's character and values. It is true that things such as food and shelter are in anyone's interests. Beyond such essentials, however, interests, and therefore what is prudent, may differ from one person to another, depending in part on what people consider the features of a good life to be. It is difficult to determine the limits of what could be regarded as a good life, but there is some leeway, and a plurality of conceptions of the good life may all be equally good.

The crucial question is whether a good life has to be a moral life. Here is a reason to think so. Suppose that an individual could exercise a kind of higher-order prudence and decide what he or she would consider a good life—that is, decide what he or she would most value and accordingly desire. What would the criteria be for choosing well? Self-interest will not be one of them, for the person is deciding what will count as self-interest. One criterion surely would be sustainability: Other things being equal, it makes little sense to take the good life to be one of uninterrupted success and pleasure, for one will surely experience frequent disappointment. Coherence is another: One should not aspire to enjoy fitness without exercise or be offensive and have many friends. Few could rationally aspire to a life of vanquishing all others, or even of being altogether independent of others.

The good life from the agent's viewpoint can be a moral life if what the agent most enjoys is the life of a good character in a good community, in which trust, mutual respect, honesty, and similar virtues are the norm. If Aristotle is right in claiming that human beings are rational and communal creatures—capable of intending, acting on values, and creating their lives subject to the constraints of their interdependence with others—then one must live in harmony with one's fellow citizens but cannot do so if one treats them dishonestly, disrespectfully, and so on. If that is the case—that is, if Aristotle's analysis is correct—then the standard virtues will normally be necessary for happiness, at least in a good community.

A good community will encourage the virtues that help build and sustain it. For example, it will require its citizens to be honest without calculating whether their fellow citizens are likely to be honest. Children will be taught that it is good to be honest. Those who grow up to be liars will be despised and likely punished by their fellow citizens. In such a community, desiring to be and being an honest person stand one in good stead. Widespread honesty will create social capital that will enhance life in the community. There may be some communities, however, in which there is so little support and reward for honesty that it is futile to be honest, for the dishonest people will take advantage of the honest ones. So in the wrong kind of community, it will be difficult for prudence to include self-interestedness and attentiveness to the interests of others.

An organization may encourage the virtues that sustain it—trust and trustworthiness, for example. But suppose it rewards an extreme form of independence and aggressiveness among its employees. Those traits may lead to internal competition and uncooperativeness, hence organizational ineffectiveness. A dysfunctional organization characteristically has a culture that wars with its mission in just that way. In such an organization, cooperativeness and other virtues may not serve the agent's interests.

Arguably, what makes business ethics a difficult matter is that success in business requires competitive ruthlessness rather than benevolence. It does require competitiveness, but whether it requires ruthlessness depends on whether the environment of business is such that an honest person with decent sensibilities can be successful in it. There are some markets and some organizations in which an honest person cannot succeed. In such environments, good ethics is not good business, and prudence splits into two antithetical traits.

Even in a good community or organization, not everyone will enjoy being prudent in the appropriate sense. Some prefer competition and the exquisite pleasure of crushing others, by fair means or sneaky. The risk in this sort of life is part of the fun. People with the requisite skills and inclinations can often maintain such a life for a good long time and find it to be satisfying on the whole, even taking into account a short stay at a minimum security facility.

Even for such people, however, a higher-order prudence may link self-interest to ethics. If we ask the typical MBA candidate, "What sort of life do you want?" we might get a Darth Vader answer. But the more interesting question is this: "What sort of life do you want to want?" Most people like ice cream better than broccoli, and given a choice would take the ice cream. But at least some of these people wish they liked broccoli more than ice cream because broccoli is healthier. Similarly, given the choice between adopting Nietzschean values and adopting Aristotelian ones, a prudent person might well choose the latter, along with the desires it entails.

Not everyone can choose to have certain values and desires, but some people can do something much like it. Social psychologists argue that character is overrated as an independent variable explaining behavior: The features of one's environment are more influential. Few people are prudent. We are more vulnerable than we think, and we should be conscious of environmental influences and careful in avoiding situations that can influence us in wrong directions. That is, we should prefer to be in a good community. Prudence is therefore extremely important when one is choosing a career or an employer.

An MBA student may believe, correctly, that he or she is the sort of person who will enjoy working for (say) McKinsey. But it is also true that an MBA who goes to McKinsey will likely soon begin to adopt the values that the culture encourages. People who say that the travel takes them away from their families and that the internal competition is dysfunctional will be considered losers. Meanwhile, a student who goes to work at Johnson & Johnson will probably not spend years wishing he or she were with McKinsey. In a strong culture, you become a certain sort of person.

The most prudent possible agent is one who can decide what values and desires to have and then arrange to satisfy them to the greatest extent possible. So a highly prudent MBA candidate will understand that the choice of McKinsey or Johnson & Johnson will in due course create certain desires and values. He or she can then consider which set of values will be sufficiently coherent and sustainable to create a satisfying life in the long run. Such a person will likely be ethical.

—Edwin M. Hartman

See also Aristotle; Rationality; Self-Interest; Smith, Adam; Values, Personal; Virtue; Virtue Ethics

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Prudent Investor Rule

The Prudent Investor Rule generally provides that a fiduciary shall invest and manage property held in a trust as a prudent investor would, by considering the purposes, terms, and other circumstances of the trust and by pursuing an overall investment strategy reasonably suited to the trust. A person who holds property for the benefit of another is said to hold that property in trust and is known as a fiduciary. The terms *prudent* and *discretion and intelligence* were first applied to trustee decisions in an 1830 Massachusetts court case, in which the court first established a "Prudent Man Rule" by determining that trustees must take their investment cues from "men of prudence, discretion and intelligence."

State statutes setting forth prudent investor rules have varied in their application of the general rules of trust management. The concepts originally established by the Prudent Man Rule became limited over the years as states began enacting "legal list" statutes specifying the types of investments in which trustees were permitted to invest. The Restatement of Trusts (Second) codified the principles of the Prudent Man Rule and broadened the permissible investment strategies but still prohibited any "speculative" or innovative investments. In addition, the application of the Prudent Man Rule was extended beyond the rule's origins in income trusts to a greater variety of situations involving charitable trusts, public funds, and pensions. Each situation bears its own particular complexities with respect to trustee obligations. For example, pension fund management's additional conflict lies in the reconciliation of the trustee's duties to the employer and employees when the effect of the decisions made may differ dramatically depending on whether the employees are current or retired. Likewise, remainder trusts pay income to the initial beneficiary for a period of time and ultimately pay out the remainder or residue of the trust property to a second party. Given the tension inherent in such competing ownership interests of successive beneficiaries, the investor must maintain a balance between all relevant interests in arriving at the best course of action, requiring greater flexibility in trust investment principles.

The criticisms of the Prudent Man Rule were addressed in the revision of trust legal principles set forth in the Restatement of Trusts (Third) in 1992, which attempted to reconcile trust investment law with ongoing investment practices. The revised principles of the Restatement of Trusts (Third) then gave rise to the promulgation of the Uniform Prudent Investor Act (UPIA) in 1994. UPIA has been adopted by a significant majority of states.

In contrast to traditional trust management principles, the Prudent Investor Rule as stated in the Restatement of Trusts (Third) and UPIA adopts the revised principles of trust law, requiring the trustee to justify the reasonableness of each investment rather than demonstrating avoidance of all speculation, and serves to provide consistent application of a more process-oriented trust investment law. The Prudent Investor Rule and UPIA incorporate Markowitz's modern portfolio theory, which provides that trust management must reduce risk by mathematically diversifying assets across a spectrum of classes of assets as well as within each individual asset class to reduce risk and maximize reward.

The Prudent Investor Rule had historically advocated that investors build investment portfolios from securities that each individually had low-risk and high-reward characteristics. Modern portfolio theory finds fault with the traditional approach for yielding a portfolio with assets selected using the same criteria, potentially resulting in an overall decrease in value of the assets chosen using the same criteria and assumptions as the one that initially decreases in value. The Prudent Investor Rule of the Restatement of Trusts (Third) uses the broader asset selection methods of modern portfolio theory to allow trustees greater flexibility in managing each trust's respective assets to minimize risk and reap maximum rewards.

—Mary Ellen Wells

See also Employee Retirement Income Security Act of 1974 (ERISA); Fiduciary Duty; Trustees; Trusts

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Public Choice Theory

Public choice theory is the application of economic principles to politics. It is most often considered to be an area of study lying between market exchange "economics" and "political science" ideologies, although some scholars consider it to be more a branch of economics. Public choice theory's main tenet is that voters, politicians, and government officials are motivated by the same basic economic factors as market actors and as a result do not always operate in the public's best general interest. Legislators are considered to make decisions with tax payers' money to advance predominantly (if not exclusively) their own self-interests and are primarily interested in their own power, prestige, advancement, reputation, status, income, and perquisites. Public choice theory offers a critical examination of the decisions made and roles played by voters, legislators, regulators, lobbyists, and various special interest groups, and the subsequent positive and negative impact of these decisions on the general public interest. It is predominantly a skeptical, cynical, and less naive view of democratic government and also offers suggestions for the improvement of modern political governance systems. The view applies purely positive economics (how people behave) and eschews normative economics (what should be).

History of Public Choice Theory

The application of economic principles to political processes began in the 1940s and 1950s. The approach grew out of an awareness of the deficiencies (or inefficiencies and injustices) of current governments in "curing" existing social ills and in addressing effectively the concerns of the "general public." Government had been perceived as the panacea for addressing market failures, market inefficiencies, and social inequities and was considered to be an infallible controller of the public interest, with noble ideologies and perfect information. In addition to a reaction against this widely held perception, public choice theory also grew out of both the public's and scholars' increased awareness of the growing size of the federal government (through expanding taxation and expenditures), which began to equal or surpass the size of the private market sector.

Public choice theorists indicate that they simply attempted to provide a coherent understanding and interpretation of what everyone could allegedly readily observe about governments at the time—most notably that

- collectivist schemes (governments) were failing,
- little correction of social ills was occurring, and
- governments were growing and making things worse.

Public choice theory applied the economic concepts of self-interest, market exchange, and methodological individualism to the main players involved in and responsible for the public interest, including voters, legislators, regulators and other bureaucrats, special interest groups, lobbyists, public action committees, trade associations, and more recently the media. Public choice theory states that it takes common economic principles of behavior in the marketplace and assumes that these self-interest motives are the same motives operating in the political arena for the above organized constituents.

Rational Ignorance of Voters

A fundamental premise of public choice theory is that efficient, effective, and "just" government policies and activities in democracies are an underprovided public good. An important reason for this "failure of government" is the "rational ignorance" of voters. Voters understand that an individual vote has negligible impact on the result of an election, while the personal cost of becoming knowledgeable and well-informed on political issues and candidates consumes enormous time and energy. As a result, it is rational for voters to abstain from voting, or at least to remain ignorant and uninformed. This behavior is evident historically in the low turnout of voters in U.S. elections.

Interest Groups

While individual voters have little incentive to influence elections and the legislative process, a plethora of special interest groups exist that have a very strong incentive to lobby and influence the government to enact and implement specific policies that would benefit their special interests at the expense of the general public. The classic example given by James M. Buchanan and Gordon Tullock is the success of local farmers (in need of getting their roads repaired) in lobbying for special legislation to pay for the improvement of their individual roads. The road repairs are funded by the general public, who receive no such benefit. Similar examples are sugar manufacturers, who receive special subsidies, either directly or through protectionist measures. The benefits of these activities are received by a small special interest, with the costs being dispersed over all citizens in an almost imperceptible and unnoticeable manner.

Public choice advocates criticize the pervasiveness of benefits received by special interest groups and the resulting inefficiencies and injustices of government as these interest groups, legislators, and government bureaucrats take care of their own self-interests at the public's expense. Special interest groups contribute to politicians through legitimate financial contributions, lobbying, and perquisites and potentially through illegal bribes and kickbacks. These exchanges and the resulting inefficiencies and injustices are what public choice theorists refer to as "government failure."

Majority Rule and the Public Interest

An important concept in public choice theory and democratic forms of rule is "majority rule": The elected ruling political party makes decisions favoring established party platform issues and supportive constituents. Kenneth Arrow, a major forerunner of public choice theory, stated that majority rule could not work to promote the general interest in democracies. Arrow's "impossibility theorem" states that a majoritarian democracy would be inherently unstable as it fosters discrimination against outvoted minorities. Pure majority rule would then contribute to inefficiencies and injustices in democracies as special interests receive benefits at the expense of the general public.

For a society or a political form of government to be just, all groups must benefit from its activities and resource allocation decisions. A solution to the problem of majority rule was addressed by public choice theorists through the concept of "unanimity": All members of a voting group must first agree on policy decisions, for subsequent collective action to be taken. All persons would secure a net gain as a result. Public choice theorists recognized that unanimity was impractical and unrealistic and, as a result, developed the concept of supermajority rule. Based on early work by Knut Wicksell, supermajority rule would require, for example, that five sixths of a voting block agree for any collective action to be taken by an existing government or collective body.

Constitutional Economics and Rent Seeking

The most prominent scholars associated with public choice theory are James Buchanan and Gordon Tullock. Buchanan won the 1986 Nobel Prize in Economics. Buchanan and Tullock's 1962 book, *The Calculus of Consent,* addressed the potential unjust and inefficient issues allegedly associated with majority rule. The central contribution of their book was to identify two structures of "collective decision making" by governments. "Ordinary politics" involves the decisions made in legislative gatherings or sessions. "Constitutional politics" concerns the "rules" of how ordinary politics are conducted. The rules of congressional decision making are based on the Constitution, allowing for unfettered majority rule to the exclusion of unanimity and supermajorities and to the benefit of special interests. Constitutional economics explains the underlying rules specifying how self-interest is promoted by legislatures, special interest groups, voters, government officials, and bureaucrats.

An associated term coined by Anne Krueger in 1974 and discussed conceptually by Tullock in 1967 is "rent seeking." This idea emphasizes that there is value to be gained (rents) through politics and that special interests will try to gain favor (seek rents) by lobbying and donating funds to candidates who will promote their constituents' interests in "exchange" (e.g., roads for local farmers, subsidies, tariffs, quotas, tax breaks). To the extent that other groups likewise expend resources to gain such rents but are unsuccessful, interest competition results in waste and inefficiencies for the general public.

Legislators, Vote Trading, Logrolling, and Capture Theory

Public choice economists closely examine the action of legislators. In a "just" society, legislators are expected to pursue the "public interest." Legislators, however, use other people's money raised through taxes, and legislators have little incentive to spend money wisely or fairly as a result. Efficient or fair expenditure of taxpayer resources by legislators does not save any of their own money nor reward them for any saving in expenditures. As a result, there is no economic incentive for government officials to be efficient or fair to the general public.

Legislators have the power to tax, extract, and spend resources in inefficient and unjust ways because voters poorly monitor their behavior. One technique used by politicians is "logrolling," or "vote trading," in which politicians trade their votes to support each other's bills or initiatives to benefit each legislator's individual constituent group (to the detriment of the general public). Local uninformed voters only know that their local representative got something for them and are unaware of the larger inefficiencies for both themselves and the general public.

Public choice theorists have also addressed the role of regulators in government under the label of "capture theory," introduced by George Stigler, a Nobel laureate in economics (1982). Regulatory agencies rely on Congress and legislators for their budgets. Lobbyists can influence legislators to provide funds for regulatory bodies, and in this sense, the regulatory agencies (and legislators) are "captured" by the lobbying interest groups.

Suggestions to Correct "Government Failures"

Public choice theorists have offered solutions for "government failures." One suggestion is to introduce "rules" that would limit government legislation that caters to special interests and to curtail the expanding expenditures of the federal government. One attempt was made in the 1980s by James C. Miller, a public choice theorist who headed the Office of Management and Budget. Miller was instrumental in passing the Gramm-Rudman-Hollings (Balanced Budget and Emergency Deficit Control) Act of 1985, which set a limit on annual government spending and required automatic cuts if the overall limits were not met. Additional rules have been offered to limit logrolling and the power of special interest groups.

Another suggestion by public choice theorists is to initiate responses on the local government level through referenda and initiatives for voting by the public before any legislative action is taken. To streamline federal bureaucracies, some public choice theorists suggest that private enterprises take on the responsibilities currently allocated to federal bureaucratic organizations. The idea is to use market exchange activities to implement and control procedures more efficiently and effectively.

Critics and Opponents of Public Choice Theory

Critics and opponents of public choice theory emphasize that human actors respond for many reasons and that self-interest and economic benefits are not the be-all and end-all of every human action. Public choice theory has been criticized as being "immoral" or lacking any moral component in its analysis of human behavior in the political arena. It has been criticized as the simple transference of economics to politics, when in reality, voters and legislators do not behave in the same manner as individuals and markets do in purely financial exchange relations. This criticism argues that individuals behave differently for the public than they do for themselves.

Public choice theorists agree that individual actors respond in many ways for many reasons and that economics is one of many factors but an important one. They assert that self-interest does not simply go away in politics. It may be mitigated by social and political roles in the consideration of public interests, but ordinary incentives and their impact and motivating value do not simply vanish.

Impact of Public Choice Theory

Public choice theorists do not claim any new insight or discovery but rather a rediscovery of wisdom and common sense in bringing the perspective and implications of economics into democratic politics. The approach purports to offer insights into political activities such as tax exemptions, loopholes, tariffs, quotas, growth in governmental bureaucracies, and various other "rent-seeking" behaviors of legislators and regulatory agencies. Public choice theorists claim to have had an impact on critical thinking and on new public attitudes about government and collective decision making. They claim to have made the public more critical of politicians and regulators, more cynical about the motives of government officials, and less naive about the success of ideological democracies and socialistic approaches to solving the social ills of society.

—Daniel W. Greening

See also Agency, Theory of; Arrow's Impossibility Theorem; Collective Choice; Corruption; Economic Rationality; Normative Theory Versus Positive Theory; Political Action Committees (PACs); Positive Economics; Public Goods; Public Interest; Rational Choice Theory; Regulation and Regulatory Agencies; Rents, Economic

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Public Company Accounting Oversight Board

The Public Company Accounting Oversight Board (PCAOB) is a private, tax-exempt regulatory entity that Congress created through the Sarbanes-Oxley Act of 2002 (SOX), principally to promulgate and enforce rules regarding the auditing and governance of publicly held corporations and the practice of public accounting.

Structure of the Public Company Accounting Oversight Board

Title I of the SOX sets out the responsibilities of the PCAOB "to oversee the audit of public companies . . . subject to the securities laws . . . to protect the interests of investors and further the public interest in . . . informative, accurate, and independent audit reports." Despite the PCAOB's federal charter, Congress created it as a private entity, a tax-exempt organization, under the proximate authority of the Securities and Exchange Commission (SEC), and provided that board members would not be federal officers.

The SOX assigns the SEC, in consultation with the chair of the Federal Reserve Bank and the secretary of the treasury, authority to appoint five board members to the PCAOB, consisting of "prominent individuals of integrity and reputation who have a demonstrated commitment to the interests of investors and the public, and an understanding of the responsibilities for and nature of . . . financial disclosures . . . and the obligations of accountants with respect to . . . audit reports."

These are full-time, exclusive positions with 5-year terms, except for the first group, whose terms will end on a staggered basis on each anniversary of the first appointment; the chair serves for 5 years. Two members must be, or must have been, certified public accountants (CPAs), while the others should not have been CPAs. Members can serve only two terms, consecutively or nonconsecutively, and are subject to removal for a good cause. The board maintains an ample staff of attorneys, subject-matter experts, and administrators.

The PCAOB's duties include registering public accounting firms (hereafter, firms) that audit issuers of securities in public capital markets (hereafter, issuers); setting professional standards for auditing, quality control, ethics, independence, and other matters; inspecting, investigating, and sanctioning firms and their members; and enforcing SOX provisions, PCAOB rules, professional standards, and securities laws regarding audits. Firms must submit activity reports to the PCAOB at least annually. These reports, and the original registrations, are available for public inspection, except for proprietary information. To finance its operations, the PCAOB assesses registration and annual fees on firms that practice before it.

With regard to standards for auditing, quality control, and independence, the SOX provides for a *discretionary* zone of cooperation between the PCAOB and private sector advisory bodies, including the authority to adopt professional standards from such groups. However, subsequent provisions signal the significant reemergence of direct oversight of the accounting profession by laying out stiff *minimal* requirements for firms regarding auditing standards and quality control standards for audit reports. The PCAOB may recognize, but also can overrule, private authorities, including the Financial Accounting Standards Board (FASB), regarding such requirements. Although the PCAOB may solicit recommendations from private sector "expert advisory groups" within the profession and from others, it retains "full authority to modify, supplement, revise, or subsequently amend, modify, or repeal" the resulting standards. In other words, what for decades had been the SEC's largely rule-based deferential delegation to the private sector standard-setting process had become in the SOX a potentially more case-based, even issue-based, exercise of regulatory oversight.

As indicated below, this statutory oversight authority had remained with the SEC since its creation in 1934 (and under the SOX, it continues to do so). With the SOX, though, the proximate *exercise* of this authority shifted perceptibly, and the federal government reclaimed much of what it had delegated, though ostensibly through an *alternative* private entity. Yet in the future, the PCAOB's private status may turn out to be not significant, since the SEC's "oversight and enforcement authority" over the body remains quite wide-ranging.

Title II of the SOX changes the legal guidelines to promote formal, arm's-length relationships between firms and issuers. Among other things, these provisions affirm the fiduciary duty of the issuer's audit committee to preapprove audit engagements and the obligation of auditors to make timely reports of the issuer's critical accounting policies and practices, alternative presentations of financial information, and other material in written communications between the parties. In addition, to sustain the arm's-length nature of the relationship, the SOX requires the audit partner for each engagement to rotate at least once every 5 years, and it prohibits a firm from performing an audit for an issuer whose chief executive officer or senior financial officer had worked for the firm and "participated in any capacity" in the audit of the company during the year preceding the beginning of the audit.

Title II also enumerates a long list of services that firms may not offer to issuer audit clients, including bookkeeping, financial information systems, appraisal, internal audit, human resources, investment, and legal services. The previous proliferation of these parallel services, while plausibly complementary to effective and efficient audits, became excessive, distracted CPAs financially and operationally from their original central concern as auditors, and in some cases compromised their independent professional judgment—for example, when audits came to involve review of their own work. However, the SOX empowers the PCAOB to grant exemptions from these restrictions on a case-by-case basis—for example, for firms to calculate compensation packages for the chief executive officers of issuers.

The SOX applies as well to foreign firms that prepare or provide audit reports for issuers in the United States, and it subjects them to the rules of the PCAOB and the SEC as though they were American firms, with the exception that registration by itself will not subject them to the jurisdiction of federal or state courts, other than for controversies between the firms and the PCAOB. Even for foreign firms that do not issue audit reports, the SOX empowers the PCAOB to use its rule-making authority to assert jurisdiction when it determines that "it is necessary or appropriate" to do so, in light of the purposes of the SOX and in the public interest or for the protection of investors.

Historical Context for the Public Company Accounting Oversight Board

Numerous scandals and other ethically problematic behaviors involving financial markets marked the final decades of the 20th century, including the savings and loan crisis, conflicts of interest and social disruptions from leveraged buyouts, insider trading, and the blatant disregard of proscriptions against auditor investments in clients. However, with the beginning of the 21st century, fraudulent corporate financial reporting and the complicity of the accounting profession elicited outrage on a new scale from the public and regulators. In part, this was due to the ineffectiveness of public and private sector regulatory responses to previous scandals. The unsympathetic demeanors and extravagant behaviors of some of the miscreants undoubtedly aggravated public reaction, particularly since reports of these frauds and the bankruptcies associated with their personal enrichment came in the context of a declining economy with diminishing jobs and retirement savings. With greater direct and indirect popular participation in capital markets in the 1980s and 1990s, and the robust returns of the second half of the latter decade, there had been growing public confidence in the prospects for economic opportunity. However, the combination of an economic downturn and major scandals disillusioned many and led them to believe that capitalism and some of its key figures—including corporate leaders and CPAs—had betrayed this confidence.

The United States has long had a robust and formidable apparatus for regulating its capital markets, the accounting profession, and corporate governance practices, with many of the elements of this framework originating in the rigorous intellectual discourse and principled leadership of the accounting profession in the 19th century—that is, prior to and apart from federal, state, and other private regulatory initiatives. When Congress passed the Securities Act of 1933, it assigned the responsibility for regulating the issuance of securities across state borders to the Federal Trade Commission. It was only in the Securities Exchange Act of 1934 that Congress created the SEC and invested it with the authority to regulate public securities markets and to set and enforce standards for the practice and the profession of accounting. However, in recognition of the aforementioned long-standing expertise and leadership of the profession in developing a theoretical and practical apparatus for these standards, the SEC voted in 1938 to delegate this statutory authority to the profession itself. Although the entities through which the profession did this varied, from the Committee on Accounting Procedure (1936–1959) to the Accounting Principles Board (1959–1973) and, eventually, to the FASB (1973 to the present), this public-private partnership prevailed essentially without interruption until the early 2000s.

This experimental arrangement toward a regulatory framework was uneven in its effectiveness, as the recurring scandals in the 20th century demonstrated. Sometimes the regulatory hand of government made incremental adjustments in this framework, particularly in securities regulation. Depending on the ethos of the time, this stiffened disclosure and other requirements, as with the Williams Act of 1968, or loosened them, as with the Private Securities Litigation Reform Act of 1995. Often the mere threat of legislative tinkering with the regulatory framework was sufficient to motivate the accounting profession to take preemptive regulatory action to stave off the blunt instrument and loss of control that legislation portended. However, the profession itself was not of one mind on many issues, as even the threat of government regulation failed to quash internecine arguments between the FASB and practitioners over accounting for stock options and other issues.

The combination of market failure of the self-regulatory initiatives of the profession and the influence of the profession and its allies on legislators and regulators led to a weakening of this framework, just as opportunists in the corporate world sought to manipulate their investors, their accountants, and the public. The scandals at the beginning of the new millennium revealed that this public-private regime was insufficiently resilient or responsive to prevent and detect widespread and massive fraud in corporate reporting and audit practices. It became clear that some modifications to this regime would be necessary. From the perspective of the accounting profession, the form these would take ideally would remain mindful of the beneficial contributions of the profession as well as its latter-day missteps.

There had been prescient and diligent efforts at reform years before the major scandals broke out, but they were largely ineffective. In the 1990s, SEC Chair Arthur Levitt Jr. repeatedly tried to limit the ability of accounting firms to provide consulting and other nonaudit services for their audit clients, but he faced chronic resistance from Congress and President Bill Clinton. After reports of accounting irregularities at Enron and other companies in late 2001 and early 2002, many members of Congress, including some who had accepted campaign contributions from interest groups associated with these companies and the accounting profession and who had blocked Levitt, expressed outrage in at least 11 investigations. During one such hearing, a previous critic, Senator Robert Torricelli (from New Jersey), addressed Levitt directly and offered a rare admission in Washington: "We were wrong. You were right."

At the same time, the accounting profession tried to influence public perceptions of the scandals and accountants' complicity, but the scale and scope of the irregularities and the damages they caused, the public familiarity with the firms' names, and the stories of executive hubris and greed created an impetus that limited the profession's ability to deflect criticism by the public, commentators, and Congress. As the U.S. Department of Justice prosecuted the American unit of Arthur Andersen, the once venerable global firm whose audit practice had been the focus of much of the controversy at Enron and other companies, the other major firms eventually abandoned their lobbying alliance with and support for the firm as they worked to influence the path of reform. After its conviction, Andersen followed through on the humiliating necessity to terminate its audit practice and resign from the SEC Practice Section of the American Institute of Certified Public Accountants (AICPA). The U.S. Supreme Court later overturned the conviction, but the reputational and economic damage was complete—and catastrophic—for the firm.

Scandals at WorldCom and other companies in 2002 inflamed public outrage and led President George W. Bush to condemn corporate misconduct, though in muted language. Despite his initial reticence in providing a dramatic regulatory response, he eventually signed the SOX into law on July 30, 2002. In addition to heralding profound changes for corporate governance, this legislation significantly altered the regulatory framework for the accounting profession, and in reasserting federal regulation of the profession's audit function through the agency of the PCAOB, it marked a dramatic change from the policies that had prevailed for the preceding 64 years.

Establishment of the Public Company Accounting Oversight Board

As formidable as this statutory response to rehabilitating corporate America and the accounting profession seemed abstractly, the moral frailties of those who implemented it in 2002 quickly aggravated the problems that had occasioned it, and this tested the credibility of the PCAOB before it even began to operate. Doubts among observers about the competence and the independence of the then SEC chair Harvey L. Pitt only deepened with the perception that his lukewarm response to the scandals and financial crisis was due to his lingering sympathies for his former CPA firm clients. He compounded this image with his stealthy and awkward attempt to install the retired federal judge William H. Webster, former director of Central Intelligence and the Federal Bureau of Investigation, as the first PCAOB chair, instead of John H. Biggs, the former chair of TIAA-CREF, who likely would have been firmer with the profession.

The controversy deepened after disclosures that Webster had chaired the audit committee of U.S. Technologies, which some had suspected of financial fraud. Pitt had kept this information from the other SEC commissioners prior to the vote. The resulting uncertainty generated global concern about the integrity of American capital markets, and this even affected the stability of currency markets. After their positions became untenable in the eyes of the public, Pitt and Webster resigned a few weeks later, and the former New York Stock Exchange chair William H. Donaldson and William J. McDonough, president of the Federal Reserve Bank of New York, assumed their respective positions. In 2005, they stepped down, and California congressman Christopher Cox assumed leadership of the SEC, while Willis Gradison, a board member of the PCAOB, became acting chair.

Analysis of the Work of the PCAOB

Once Congress, the SEC, and the PCAOB largely resolved the difficulties in implementing the provisions of the SOX, including the establishment of the PCAOB, corporate leaders, investors, financial analysts, attorneys, accountants, regulators, scholars, and other observers and participants in capital markets began to assess the meaningfulness and effectiveness of the putative reforms and the likely direction they would take, including influences on sectors about which the SOX is silent. While many hailed the promulgation of the SOX and the appearance of the PCAOB as necessary correctives, there were concerns among these constituencies as well about risk management and the need to balance the enormous costs of compliance with the costs of errors or irregularities in financial reporting and auditing.

The accounting profession largely accepted the new regime, although controversy erupted again when, during January 2003, Pitt, who was in his last weeks in office, oversaw the most prodigious promulgation of SEC rules since the founding of the commission. Many observers, including some in Congress, perceived the episode as a last attempt by an advocate for the profession to weaken the regulatory implementation of the SOX. Some critics, especially among scholars, expressed concern about the legalistic focus of the SOX provisions, an emphasis that some compared unfavorably with the nearly contemporaneous revised federal organizational sentencing guidelines for white-collar crime, which reflected a broader managerial approach that encompassed factors of organizational culture and ethics rather than mere compliance.

Moreover, while the costs of complying with the provisions of the SOX raised the risk profile for senior corporate executives, corporate directors, and the attorneys, accountants, and financial professionals who worked with them, there was little doubt or disagreement about the significant and lucrative business opportunities this occasioned for those who were willing to continue such a service. Accountants in particular complained about the SOX and the PCAOB, including the flight from the profession that the concomitant burdens occasioned, but the reality was that their services were in unprecedented demand because of these requirements.

In ongoing assessments of the scope of the SOX and the work of the PCAOB, one must keep in mind what the board does not do, at least according to the letter of the law: namely, promulgate standards for the vast majority of firms that provide auditing and nonauditing services for clients that do not meet the statutory definition of "issuer." The regulation of most of these firms falls outside the scope of federal securities statutes and regulations and PCAOB rules, yet the size of this practice area abundantly confirms the necessity for multilevel, integrated, and institutionally pluralistic oversight as well. In practical terms, this means a continuing prominent role for the state boards of accountancy that license firms and, of course, for private entities such as the AICPA and parallel state CPA societies, for example, through promulgating and enforcing substantive codes of conduct and performing regular peer review. Regardless of whether a sector or firm falls under the jurisdiction of the SOX, an effective regulatory framework also requires correlative vigilance on the part of other observers and participants in capital markets, including the media, stock exchange managers, and the investors themselves.

At the same time, in light of federal experience, the provisions of the SOX and the rules and example of the PCAOB have set de facto standards of best practices for organizational governance and professional due diligence, and this, along with similar legislative initiatives at the state level, has begun to extend the influence of the new regulatory framework far beyond the ranks of "issuers" and "firms" that the SOX cites.

A salient example is the exempt organization sector in the United States, which, as of 2003, managed approximately $1.76 trillion in assets, making it one of the largest discretely identifiable economies in the world. While exempt organizations presently must follow a strict regulatory regime under the Internal Revenue Code, treasury regulations, state laws, and other public and private guidelines, they need not comply with the provisions of the SOX. However, due to scandals and the negative public perceptions of some prominent exempt organizations, including the United Way, the Nature Conservancy, the American Red Cross, and American University, there have been calls from Congress and elsewhere to extend these or similar requirements to this sector. Many of these organizations voluntarily have followed guidelines analogous to the practice requirements of the SOX as best practices—for example, assigning audit and tax services to two or more accounting firms. In many instances, the impetus for these practices comes from board members of exempt organizations, many of whom are familiar with SOX requirements because they must comply with them in their own companies.

The SOX represents a 21st-century attunement to a 20th-century regulatory framework that presumed *19th-century* standards of proficiency, professionalism, and restraint on the part of accountants. Its comprehensive provisions, particularly the establishment of the PCAOB, proportionately responded to the most notorious practices, including financial statement irregularities; compromises of auditor independence; bias in securities analysis in investment banking firms; and breaches in fiduciary duty, corporate accountability, and principled governance. The early reaction from most practitioners and scholars has been that the SOX represented a necessary modification to the regulatory framework for corporate governance and the accounting profession. However, more experience with this regime will inform this ongoing process of attunement and help guide the virtually certain broadening of the scope for its application to other sectors and contexts.

—Lester A. Myers

See also Enron Corporation; Financial Accounting Standards Board (FASB); Sarbanes-Oxley Act of 2002; WorldCom

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Public Domain

The public domain comprises the body of community resources, including knowledge and innovation, in which no person or other legal entity can establish or maintain proprietary interests. This includes creative works such as writing, art, music, software, and other inventions. The public domain also includes the physical domain, including land, oceans, and the atmosphere.

The Environmental Commons

One important element of the public domain is the idea of the "commons." In particular, there is an ideological tension between advocates of the public domain, who support the promulgation of collective rights, public goods, and other shared resources, and those who advocate the establishment and ownership of private property. This tension often arises out of concerns about the "tragedy of the commons," as posited by Garret Hardin and others, when the interests of private property owners impinge on the commons. The absence of specified, enforceable property rights encourages overuse of the commons by private interests. Examples include overfishing of unregulated public fishing grounds or building of private condominiums that restrict access and views of a public beach.

Environmental nongovernmental organizations (NGOs) operating in civil society tend to regard themselves as advocates for "public rights" to protect the commons, in the belief that these groups "speak" for species who lack voice and legal standing. In contrast, libertarians argue that the commons should be privatized so that property rights can be enforced to save community resources. They point to the work of Ducks Unlimited in buying up threatened wetlands to set aside habitat for waterfowl (and hunters). Disputes over government policies that provide extractive industries, such as timber and mining, with partial access to public lands suggest that privatizing the commons will remain a controversial public policy issue.

Creative Works

In the United States, certain works do not qualify for copyright protection, and therefore exist in the public domain. These include creative works that consist entirely of common knowledge, facts, or symbols, such as tables, lists, and measurement standards. Works that have been performed or presented but that have not been recorded or otherwise "fixed in a tangible form of expression" also exist in the public domain.

Creative works that are owned or produced by the federal government automatically exist in the public domain and may not be copyrighted. Artistic interpretations of these works may be copyrighted. For example, a painting based on an astronaut's photograph of a manned space mission may be copyrighted, but the original photograph exists in the public domain.

The various laws and rulings of the U.S. government also exist in the public domain. Various publishers of legal databases and manuals have successfully asserted copyright control over their indexed and annotated versions of federal legislation and jurisprudence.

When a publisher or rights holder fails to renew the copyright on a work, the work lapses into the public domain. These are commonly referred to as "orphaned" works.

Slogans, trade dress, and other marks may be protected through trademarks and service marks but may not be copyrighted.

The proposed WIPO (World Intellectual Property Organization) Treaty on the Protection of Broadcasting Organizations would allow broadcasters to copyright their transmissions for 50 years. This includes the transmission of public domain works. One criticism of this treaty is that it effectively creates an endless copyright, allowing broadcasters to remove works from the public domain through systematic retransmission. The proposed treaty also applies to Webcasting or narrowcasting, which is the transmission of materials to a self-selected audience over the Internet.

The Knowledge Commons

Creative works may be considered as part of a vast "knowledge commons," in which users store, analyze, and share intellectual property. In some countries, cultural biases tend to favor the rights of users over publishers. For example, South Korean manufacturers often appropriated the brand names and trade dress of popular Western products, until the United States and European countries prevailed on the South Korean government to enforce international agreements on intellectual property ownership. Howard Rheingold and others have examined the self-organizing capabilities of stakeholders, who use mobile phones and computers to find each other and establish communities in the real and virtual worlds. Paul David refers to the "overfencing" of intellectual property by rights holders, which may serve as a countering force to suppress or stifle innovation and creative thought. The delicate balancing act between users and owners has become more challenging as the Internet and telecommunication technologies have tipped the balance of power and allowed the rapid creation, acquisition, and distribution of creative works on a global scale.

The Internet and the Public Domain

It is a common misconception that material that is freely available on the Internet is also in the public domain. Authors and creators can claim copyright over any works they create and post to the Internet, just as they might when they publish in another medium. However, it is illegal to post or distribute a copyrighted work on a computer network without the express permission of the publisher or rights holder.

Open-Source Software

Various types of public domain licensing schemes allow software developers to distribute their works to the public while maintaining control over how the software is maintained, developed, or extended. These licenses collectively form the open-source software (OSS) movement, which derives its name from the right of users to examine the underlying source code of these software works.

One example of OSS is the GNU General Public License (GPL), which was first developed in 1989 by Richard Stallman as the legal foundation for his GNU (GNU's Not UNIX) software project.

The GPL provides four freedoms to software users:

1. The freedom to run the program for any purpose
2. The freedom to study how the program works and modify it
3. The freedom to redistribute copies
4. The freedom to improve the program and release the improvements to the public

Access to the actual source code is a precondition of Items 2 and 4.

The GPL differs from other schemes by employing the principle of copyleft. Anyone who distributes a modified version of a GPL-licensed work must do so under the GPL license. Thus, GPL works and their derivatives exist in the public domain and cannot be sold or licensed as proprietary works. In 2005, approximately 70% of the free and OSS projects hosted by the two largest OSS sites were licensed through the GPL.

The GPL has been challenged in various courts as an overly restrictive licensing scheme. At least one legal challenge has portrayed the GPL as a price-fixing scheme, with a target price of 0.

Many other OSS licensing schemes exist, including the Berkeley Software Distribution license. In general, these licenses provide limited forms of protection to software creators and rights holders when compared with the absolute protection of the GPL.

The Creative Commons license is an alternative licensing scheme that allows users to create works that may or may not remain in the public domain, based on a list of permissions selected by the creator or rights holder. Creative Commons works carry the legend "Some rights reserved." While this legend may also describe other licensing schemes, it stands in deliberate contrast to the copyright legend, "All rights reserved."

The Creative Commons scheme is an attempt to reconcile traditional copyright law with digital and network distribution and use. Creative Commons licenses are based on national and international copyright laws and are also expressed as machine-readable license agreements that may be attached or linked to a creative work. Creators may sanction the creation, distribution, and licensing of proprietary derivative works. Eleven different licenses are available, in logical combinations of four core principles: attribution, noncommercial use, derivation, and "share alike."

—William A. Sodeman

See also Copyrights; Environmental Protection Legislation and Regulation; Intellectual Property; Patents; Trademarks; Tragedy of the Commons

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Public Goods

Economics distinguishes between private goods and public goods. By definition, any pure public good lacks two key technical attributes that any pure private good possesses. While largely theoretical, the distinction is very important for understanding actual markets and governments. In practical terms, private goods are basically those that markets can produce and sell. Public goods are basically those for which markets will fail or at best perform below social requirements. Given such conditions of "market failure," either governments or private clubs must act if there is to be production and distribution of the good. Real markets often require government activities of some type. Enforcement of private contracts in courts is an example. Many private goods are therefore not strictly speaking "pure."

Pure private goods exhibit the two attributes that economists term rivalness of consumption and price exclusion. There is a buyer and a seller (i.e., an owner of the good for sale). If one consumer purchases a loaf of bread, another person cannot consume that particular loaf; a person who cannot afford to purchase does not consume bread. When higher demand for ethanol in gasoline caused the world price of corn to increase, low-income consumers in Mexico relying on corn for tortillas as a staple food had serious problems. The result in Mexico was political protests calling on the government to enact price ceilings.

Pure public goods lack both of the attributes possessed by pure private goods. National defense involves nonrival (i.e., joint) consumption and impossibility of price exclusion. A pure public good is not reduced by individual consumption, does not involve transferable property rights, and does not assign full costs to individual consumers through the price mechanism. Once a pure public good is available, multiple consumers can freely make use of the good. The behavioral prediction is that a rational consumer will "free ride" in the sense of not paying for this free use and indeed will conceal preference (i.e., demand) for the good. If so, compulsory taxation by government will be necessary (and justified).

Pure public goods such as national defense are in fact relatively rare. The broad concept of public goods is therefore further subdivided into three categories. In addition to pure public goods, such as national defense, there are club goods and common pool resources (or common goods). The concept of public goods thus includes what economists term mixed (or ambiguous) goods, which combine private and public attributes, as happens with club goods and common pool resources. (As already noted, many private goods are not strictly "pure" either.) Club goods, such as a movie theater or a toll facility, involve joint consumption but price exclusion. When one goes to a movie theater, one buys a ticket for access but sees the movie with an audience. Common pool resources, such as air, occur freely in nature. Common goods such as fish swimming freely in the ocean involve rival consumption (i.e., individual harvesting) but no price exclusion.

Pure public goods are very difficult if not impossible to produce for private profit. A business typically cannot recoup the full costs of trying to provide national defense. Businesses are unlikely to supply unprofitable public goods except in strictly limited quantities out of motives of corporate social responsibility. Some club goods (e.g., movie theaters) are suitable for business, while other club goods may require nonprofit organizations (e.g., symphonies or operas) or governments (e.g., toll bridges and roads) to produce them. There is consumer demand for the various types of public goods, but such demand is collective or social in the sense that anyone obtaining access to the good with or without payment can consume it equally and jointly. The result is often market failure or, at best, suboptimal market supply. Some form of collective (i.e., nonmarket) action through the government or nonprofit organizations typically will be needed to satisfy consumer demand for a public good that does not occur freely in nature. In the case of a common pool resource occurring in nature, collective action regulating free consumption may be needed. Unless there is effective regulation by private clubs or government, there may be increasing air pollution or progressive depletion of the common pool resource (as is happening with global fish stocks).

Public Interest and Collective Choice

Public goods typically require collective (i.e., nonmarket) choice concerning the public interest in government or nonprofit provision or government regulation. In economics, a "good" is technically a physical item such as a loaf of bread (a type of consumption good) or a machine tool (a type of capital good). A "service" is an activity such as a dental examination or a pipeline inspection. The word *good* is often used broadly to include both goods and services, as a form of shorthand. A "public good" is not "the public good" or "the common good"—terms referring to "the public interest." Provision means funding rather than production. Much of the production for the public sector occurs, outsourced, in the private sector.

Public goods are widespread phenomena. The term *public goods*, also known as social goods or collective-consumption goods, covers three related conditions in which goods (or services) are consumed jointly rather than individually. Common pool resources (or common goods) such as air occur naturally for free use by any consumer. In some circumstances, free consumption results in overgrazing. A classic or pure public good, which is a relatively rare occurrence, reflects market failure or suboptimal market supply due to an extreme instance of beneficial (i.e., positive) externalities. National defense, public order, and justice are the standard examples. There are private security services and volunteer fire departments. Generally, government must act to provide such goods in sufficient quantity to satisfy consumers. Club goods are consumed collectively or jointly but by only a subset of society. Examples are golf courses or toll bridges and roads. Either the government or private entities might provide club goods, depending on the conditions.

Related to public goods is the notion of merit goods. A merit good is underconsumed because individual consumers ignore positive externalities. A merit bad (or a demerit good) is overconsumed because individual consumers ignore negative externalities. A merit good, while provided in some quantity for profit by the market economy, ought in someone's judgment to be provided in a greater quantity, requiring collective action. Examples are education and health. There are for-profit schools and hospitals, but there are arguably broad social benefits (i.e., positive externalities) from wider consumption. Analogously, a merit bad, while provided in a satisfactory quantity for profit by the market economy, ought in someone's judgment to be provided in a lesser quantity, requiring collective action. Examples are tobacco and illegal drug consumption, which arguably ought to be reduced.

Public goods, with related notions of merit and demerit goods, are a key concept in the theory of welfare (or normative) economics. The concept generates a prescriptive theory of public and nonprofit expenditures. Prescriptively, the government should provide goods and services strictly in the public interest, defined as maximizing net national wealth. Provision by governments and nonprofit organizations should be complementary to business production rather than substitutes. What the government actually should provide, and how, is a matter of considerable controversy. For example, lighthouses involve an interesting range of options: Some lighthouses may be provided through general taxation and some through port fees on users.

The correspondence between government activity and this prescriptive theory of public goods is very rough for several reasons. First, a government may in practice provide private as well as public goods (including regulation services), subsidies of private activities, and transfers of wealth among citizens. The theory of public goods is a normative framework for prescribing what the government ought to do rather than describing what a particular government actually does for whatever reasons. Second, there are very few "pure" public goods other than perhaps national defense and human rights enforcement. Third, there are very few "pure" private goods. For example, a private good is often transported to market on a public roadway. Most goods are impure or ambiguous in the sense of having mixed public and private characteristics in various degrees. Fourth, the private sector includes both businesses selling private goods in markets and nonprofit organizations. Some nonprofits operate like businesses, some operate as clubs or voluntary associations providing collective benefits to their members, and others are dependent on government subsidies and private donations.

Private Good

The best way of defining a public good is by contrast to a private good. Pure public goods and pure private goods have polar-opposite characteristics. A private good is one traded in markets by buyers and sellers, whose interactions determine prices and volumes. Buyer and/or seller may be a business, household, government, or nonprofit organization. It is the attributes of the good itself that matter for definition purposes. What a private good possesses by way of two key attributes, a public good lacks by definition. The two polar-opposite conceptions define a continuum along which in reality lie various mixed goods and services.

The two key attributes of a pure private good are price excludability and rivalness of consumption. If the buyer and seller cannot agree on a price, then a transfer does not occur. On eBay, Internet trading is basically an auction often conducted with a time limit and minimum bid requirement. The buyer offering the highest price wins, and all other buyers are excluded. This attribute generates a demand function. At the same time, and inherently, private goods have clearly identified owners, and consumption of the good is rival or individual. Ownership generates a supply function. If a buyer purchases a loaf of bread from a seller, that loaf once consumed cannot be shared by others; and in a reasonably functioning market system, there is no reason why others should demand a share of the loaf. Excludability is the inherent purpose of the price mechanism. The qualities of excludability by price and rivalness of consumption are preconditions for market exchange and business activity.

Public Choice Theory

A pure public good lacks both the essential qualities of price excludability and rivalness of consumption. Collective (i.e., nonmarket) action through government or nonprofit organizations will be necessary for provision or regulation. By definition, a pure public good is one that for technical reasons involves nonrival consumption and that once produced cannot be denied to any particular consumer through the price mechanism. Economists say that the marginal cost of production (i.e., the cost of producing one more unit) is 0 and, thus, price should be 0 (i.e., free). Such goods can occur naturally, as in the case of air. The classic example of market failure is national defense. If the government defends the country by the provision of a daily air force patrol authorized in the extreme case to shoot down hijacked commercial aircraft being directed by terrorists against targets, then that provision covers everyone in the spatial coverage of the air patrol. No one can be readily excluded by pricing. Consumption of this air protection service is nonrival or joint. Everyone consumes the service simultaneously. There is demand and willingness to pay for public goods: Consumers do want such goods. No business will undertake the provision of such a public good, because it cannot collect any revenues. Rational consumers can free ride by concealing their true willingness to pay for the good. Compulsory taxation or charging by government and regulation of free consumption of the natural environment will be necessary.

Pareto Efficiency

Even a reasonably competitive market economy cannot achieve Pareto efficiency if there are significant unmet needs for public goods. Pareto efficiency means that resources are allocated such that no voluntary trade can improve the welfare of one individual without reducing the welfare of another individual. The failure of market transactions to achieve Pareto efficiency unaided is the justification for provision of public goods by governments and nonprofit organizations. This failure also justifies corporate social responsibility by businesses, including broadly the defense of human rights proclaimed in the Universal Declaration of Human Rights adopted in 1948 by the UN General Assembly.

The Tragedy of the Commons

A common good, also called a common property or common pool resource, is a good for which price exclusion is not feasible but rivalness of consumption occurs in the sense that individual consumption does diminish availability of supply. Such goods or resources occur typically in the natural environment. There are many instances of common pool resources—leading to “the tragedy of the commons.” The technical situation of diminishing supply and nonexcludability will lead inevitably to overgrazing of the common resource. Some ownership device or regulatory scheme will be needed to avoid such destruction.

Nonprofit Organizations

Nonprofit organizations typically provide what are called club goods. A club good is one characterized by nonrival (joint) consumption but with price excludability feasible. A club good reflects the provision of collective (group) benefits. A club good benefits only a subset of society. Where the government provides such a club good, a subsidy or transfer to the subset of society is involved. Nongovernmental organizations functioning as activist pressure groups provide club goods to their members. A voluntary association or a country club, for example, provides collective consumption benefits to the members, but membership depends on payment. A near instance is a privately owned movie theater (or a commercial air flight). Businesses can generate profit in such conditions. Price excludability is feasible. No consumer can get into the theater lawfully without purchasing a ticket—sold on a seat-by-seat basis. Once in the theater, however, consumption is nonrival, in the sense that a number of consumers can see the same movie at the same time in the same place. It costs the theater the same to show a movie to one person or the theater capacity, because the cost of running the movie is fixed rather than variable. Availability of supply does diminish with individual consumption in the limited sense that one's precise location within the theater can matter. Consumers who care about seating location will arrive earlier. Once all tickets for a showing are sold, then consumers must queue by availability of showings. An alternative is to wait until the movie is available on video (through purchase or rental) or on television (through cable purchase or general broadcast).

In principle, a commercial firm might build and operate a toll bridge or road, but if so, it must hold an effective monopoly to profit sufficiently. Where a business owns the toll facility, the bridge operates like the movie theater—and for the same reasons. There is typically no economic reason for the government to operate movie theaters (although it may on military facilities, for instance). A government may provide and operate a toll facility because the fixed cost of investment to construct the facility is too large or too risky for a private entity. Government operation creates, however, a pricing issue for consideration. Until facility capacity is reached (i.e., cars are bumper-to-bumper), the marginal cost of allowing any additional consumer is effectively 0. The toll collection itself imposes operating expenses and slowdowns. Construction and maintenance costs might be recovered by a general levy on gasoline sales. The user charge approach focuses cost distribution on the beneficiaries.

Free Riders

Free riders are individuals who benefit without paying. Free riding involves important ethical and social issues. Public goods of all types can be viewed as extreme examples of positive externalities, whose economic value (i.e., consumers' willingness to pay) cannot be captured by the provider. Given the conditions of nonexcludability and nonrivalry, a rational consumer can use a public good without paying for it. This phenomenon is called the free rider problem: The consumer rides freely without paying. (A softer version is the easy rider problem: The consumer contributes something.) Free riding reflects the relatively low benefit and relatively high cost to the individual of paying. In the case of a private good, a consumer purchases where benefit of consumption equals or exceeds cost of purchase. The free rider problem undermines collective action in a wide variety of circumstances. One person or group may be willing voluntarily to provide a public good, because benefits exceed costs, and thus be willing to tolerate free riders. Adam Smith, in *The Theory of Moral Sentiments* (1759), defined citizenship as legal compliance and good citizenship as concern for the welfare of others. Good citizenship is the offset to free-riding behavior.

Merit Goods and Merit Bads

A merit good can be distinguished from a merit bad. A good—collective or merit—is something most consumers want but rationally will not pay for voluntarily unless compelled to do so by price excludability or compulsory taxation. Typically, a social good reflects positive externalities (i.e., benefits). Some form of collective action, whether provision or regulation, becomes necessary. This collective action may occur through the decision of an individual donor who tolerates free riding, the formation of a voluntary association or club that can restrict benefit access, or government provision or regulation.

A merit bad (or demerit good) is something most consumers do not want but wind up paying for anyway. Typically, a merit bad reflects negative externalities (i.e., costs). Prime examples are air and water pollution, secondhand smoke, noise pollution, street crime, drug abuse, and so forth. Government regulation (a governmentally provided service) may be warranted to protect common pool resources from destruction (i.e., overgrazing).

Regulation

Related to public goods is the problem of regulating a natural monopoly. Nature has a natural monopoly of air production. Some forms of natural monopoly must be operated or regulated by government. Natural monopoly may be distinguished from coercive monopoly. In the latter, artificial barriers to entry erected by some method prevent competition and leave market control with a single company or cartel of companies—such as the Organization of Petroleum Exporting Countries. Patents, copyrights, and trademarks are a form of public interest coercive monopoly, intended to stimulate innovation through economic rent protection. A patent permits a pharmaceutical company, for example, to obtain an economic rent, defined as charging price in excess of average cost of production. In the United States, cable television service is typically provided through a private local monopoly licensed by the local government.

Pricing of private goods depends on market (or industry) structure. Under perfect (or workable) competition, price equals marginal cost equals average cost—at the lowest feasible minimum average cost. The notion of cost here includes a competitive return (i.e., just enough profit to stay in business). Under monopoly, price exceeds marginal cost (thus generating a return or profit margin greater than the competitive), and typically, average cost is above the competitive minimum. Government regulation shifting a monopoly to workable competition might improve Pareto efficiency, depending on the cost of regulation.

A natural monopoly is a cost situation that results irresistibly in control of supply of a product or service by a single company. The cost situation is one in which a large fixed investment (i.e., capital cost) is required to begin operation, and the result is what economists call economies of scale (or increasing returns to scale). As volume of production increases, the long-run average cost falls steadily without reaching a turning point. (Typically, returns to scale first increase and then decrease, so that the average cost curve of the firm has a U-shaped function.) The large fixed investment creates a significant barrier to entry by competition. The offsetting factor tending to limit expansion involves the increasing costs of organizational control. If the optimal size of the firm—where scale economies intersect with organizational control costs—is as large as the whole market, then the situation is one of natural monopoly. The government can either operate or regulate such a natural monopoly. This situation is common in electricity generation and water supply. Some municipalities operate local public enterprises in these industries; other municipalities (or their states) regulate private enterprises typically granted a local or regional monopoly.

Spatially Limited Benefits and Fiscal Federalism

Local and regional public goods are defined by spatial limitation of benefits. For example, police and fire services are often provided by municipalities. Their authority and service provision typically terminate—by law—at the boundary of the municipality. If one dials (in the United States) the 911 emergency number, the call should go to the appropriate local authority. State police and highway patrol operate on a larger regional basis. The U.S. National Guard is operated on a state-by-state basis and reports to the state governor for civil emergencies. Once called up by the president, National Guard units move into federal service. It is possible for some services to spill over local or state boundaries into another jurisdiction. These spillovers are a type of externality from the point of view of the jurisdictions involved. Spatial limitation of benefits and jurisdictional spillover of benefits and costs are the economic basis for fiscal federalism. The U.S. government should supply national goods and municipalities local goods, with states handling regional goods. Spatial variations involve intergovernmental cooperation problems.

International, Regional, and Global Public Goods

Spatial variations of international public goods define regional and global ethical and social issues. An international public good is shared by two or more countries. Restriction of benefits to a set of collocated countries—such the European Union or the North American Free Trade Area—constitutes regional public goods. A global public good is one with global effect. This global effect notion has a broad reach: Certain benefits may reach across population groups and generations as well as across boundaries. For example, the eradication of dangerous diseases such as smallpox or polio has benefits globally and temporally. Once these diseases are eradicated, no one needs to be vaccinated. There are important international policy regimes for civil aviation, passports, postal services, telecommunications, and so forth. International cooperation and bargaining are often involved. The notion of global public goods becomes bundled with the problem of distribution of public goods across income levels and, thus, issues of distributive justice. Vaccinations and other medications are desperately needed by low-income developing countries and populations. The issue is who will finance such medical care and similar public goods.

—*Duane Windsor*

See also Agency, Theory of; Barriers to Entry and Exit; Collective Choice; Commons, The; Competition; Corporate Social Responsibility (CSR) and Corporate Social Performance (CSP); Corporate Social Responsiveness; Cost-Benefit Analysis; Externalities; Free Riders; Market Failure; Maximum Sustainable Yield; Monopolies, Duopolies, and Oligopolies; Nongovernmental Organizations (NGOs); Nonprofit Organizations; Pareto Efficiency; Private Good; Public Choice Theory; Public Interest; Regulation and Regulatory Agencies; Social Costs; Tragedy of the Commons; Welfare Economics

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Public Interest

Although the concept of the public interest has a long history, it remains one of the most often used yet ill-defined concepts in public discourse. The difficulty in specifying the public interest parallels the similar problems the literature has had in clearly distinguishing public from private organizations. The following review of the concept will include applications of the concept both to economic activity and to general contexts of the evaluation of public action.

The Public Interest and Economic Activity

In the context of economic activity, the precursors of the modern notion of the public interest included, in Roman and medieval times, the concept of a "just price" controlled to protect consumers against exploitation. Such a price contrasted with the "natural price" produced by the unfettered market. Later, special expectations began to be assigned to certain areas of commerce. The guilds of medieval towns received a monopoly in their trade in return for their willingness to hold themselves out in service to anyone who came to them for assistance. This norm of universal service is echoed, of course, in the requirements for such service placed on modern-day public utilities. Royal charters or franchises during the age of mercantilism presumed a governmental purpose in the enterprises. And the common-law designation of some occupations as "common callings" that were said to be "affected with a public interest" gave rise to expectations that service would not be denied and that it would be provided at a reasonable price.

Over time, the rights and duties of such businesses were expanded and became a recognized set of expectations that applied to an emerging business class, the "public utility." Such enterprises had obligations to serve all who requested service, to be certain such service was both safe and adequate, to not engage in unjust discrimination among customers, and to charge only "just and reasonable" prices. In return, the state had to protect private property, defend the right to receive a reasonable level of payment for the service, allow reasonable restrictions on the provision of services, provide the right of eminent domain as long as the property was taken for "public use," with just compensation, and so on.

A long line of court cases have attempted to determine the boundaries of what was "affected with a public interest" and hence potentially subject to special expectations or controls under common law or black letter regulation. Perhaps the most memorable was the U.S. Supreme Court case of *Munn v. Illinois*, 94 U.S. 113 (1877), in which Chief Justice Waite wrote, "Property does become clothed with a public interest when used in a manner to make it of public consequence, and affect the community at large. When, therefore, one devotes his property to a use in which the public has an interest, he, in effect, grants to the public an interest in that use, and must submit to be controlled by the public for the common good, to the extent of the interest he has thus created." The difficulty of decoding such language, making it more operational than hortatory, is evident.

Eventually, the Court decreed, in *Nebbia v. New York*, 291 U.S. 502 (1934), that "the phrase 'affected with a public interest' can, in the nature of things, mean no more than that an industry, for adequate reason, is subject to control for the public good. . . . There can be no doubt that upon proper occasion and by appropriate measures the state may regulate a business in any of its aspects, including the prices to be charged for the products or commodities it sells." In essence, the state, giving reasons, can regulate just about any aspect of business in the name of the public interest.

Debates of this sort are not by any means settled issues, even today. Recent cases over the ability of municipalities to condemn property under eminent domain for public purposes that involve the support of private business have been highly controversial. Indeed, they have led to proposals to change some state and local laws to enhance protection of private property against such public takings. Thus, what is covered by the "public interest" remains a prominent issue for practical analysis.

The Public Interest in Political Philosophy

There is no settled view of the concept in political philosophy, much less in the sphere of its practical application to economic activity. The literature contains a host of typologies—systematic sortings by dimensions claimed to extract important aspects of the concept—that purport to distinguish key alternative meanings of the concept. The types distinguished are sometimes little more than lists, and the labels given to the types can seem arcane and somewhat distant from practical application. Here are some prominent examples:

In 1955, Edward Banfield found "unitary" meanings (distinguishing "organismic" from "communalist") and "individualistic" approaches (distinguishing "utilitarian," "quasi-utilitarian," and "qualified individualistic"). In 1957, Frank Sorauf distinguished alternative meanings: as commonly held value, as wise or superior interest, as moral imperative, as balance of interests, or as vague, essentially undefined value. In 1959, W. A. R. Leys and C. M. Perry found both formal meanings (simple or pluralistic) and substantive meanings (utilitarian, procedural, or normative). In 1960, Glendon Schubert identified "rationalist," "idealist," and "realist" types. In her 1970 book, Virginia Held divided the theories of the public interest into "preponderance" theories, "common interest" theories, and "unitary" theories. In 1974, Clarke Cochran listed "normative," "abolitionist," "process," and "consensualist" types.

These typologies seem bewildering in number, and though in their authors' discussion they provide numerous, valuable insights concerning subtleties in the meanings of the public interest, they are often not very systematic in construction. The Sorauf, Schubert, and Cochran typologies are lists with no structure; the others sort the concept with varying, often incomplete logics.

Barry Mitnick provides a sorting that offers a systematic logic to array the various meanings of the public interest. The distinctions made by the scholars above, in addition to analysis in other works in the literature, are disaggregated and sorted. The dimensions that seem to generate the definitions of the public interest that appear in the literature are the following: whether or not a holder of the public interest is required; the level of the holder (no holder—ideational or holder—individual/group-organizational vs. systemic); whether participation by the polity is required—that is, some set of acts or procedures is necessary to determine the public interest; whether or not the public interest is rule determined—that is, whether or not those who determine the public interest must follow formal or informal rules; and, finally, the number of sets of preferences that are used to determine the public interest—whether only one (unitary) or whether a number must be combined in some way (combinatorial, whether from multiple same or multiple different preferences).

This generates a large typology that subsumes those definitions that are specified clearly enough in the literature. For example, the public interest is a type of "pluralistic aggregation" when a holder is required, the determination occurs at the individual or group level, a rule applies, and multiple, different sets of preferences are combined—we get the public interest via, to take one case among many possible ones, an election. On the other hand, the public interest is described as "consensual" when a holder is required and multiple-same preferences are combined. Examples include unanimity, a Paretian process, or "consensual majoritarianism."

The typology allows us to classify conceptions of the public interest but may draw criticism from those who require a kind of contentful instruction: Don't tell me *how* to construct it; tell me *what* it is in the case I am worrying about. But the concept of the public interest is inherently vague; we can only set up the conditions for its determination or appearance. In this respect, the concept of the public interest is similar to the concept of Pareto optimality in economics. The latter occurs when no further trade in the market is possible that makes at least one actor better off without making any other actor worse off. Its desirability stems from the presumed consumer satisfaction that occurs from having traded until no further trades are possible. But nothing is said about exactly what circumstances would be supposedly better than others; Pareto optimality, like the public interest, merely establishes the conditions under which the desirable state can occur, not what that state actually is. Thus, the public interest remains elusive in content although understood in construction.

—*Barry M. Mitnick*

See also Common Law; Due Process; Free Market; Pareto, Vilfredo; Pareto Efficiency; Public Utilities and Their Regulation

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Public Relations

Public relations is a business function that can have any number of names—namely, corporate communications, corporate affairs, public affairs, or external affairs. The senior public relations officer usually reports to the chief executive officer, although sometimes the function reports to a second-level senior officer (e.g., chief administrative officer or, occasionally, the general counsel).

No matter what the name, the function will have a core mission of ensuring good relations with important constituencies, particularly the media. In many instances, the function will include a government relations component, manage corporate charitable contributions, handle relationships with the local community (and sometimes plant communities), and maintain relationships with important activist and interest groups involved with issues affecting the company's business. The same function is also likely to manage internal communications with employees and may have an important role in communications to the financial community—for example, it may produce annual reports and organize annual meetings.

Evolution of the Function: The First Decades

Public relations has grown and evolved as a business function from its earliest days at the beginning of the 20th century. Ivy Lee is often credited with being the "founder" of the field when he began to advise John D. Rockefeller about ways to improve his public image, through philanthropy, policies toward workers, selection of plant sites, and so on.

While the press agency aspect of public relations was—and remains—a core activity, Ivy Lee's determination to go beyond simply issuing press releases laid the groundwork for a much broader business function that would provide input to basic business decisions. Rockefeller at first resisted the advice but eventually gave in to the notion that public reaction had to be a factor in his business decisions.

Later, when Edward Bernays, another "founder" of the public relations profession, wrote the first book on the profession, titled *Crystallizing Public Opinion*, he too went beyond press relations. A student of Freud, he discussed the critical roles that events, third-party opinions, and social trends played in forming public opinion. He argued that public relations professionals had to be able to manipulate these elements if they were to be truly successful.

The early founders of the public relations function focused on image making. Given the historical period in which they were operating, which included the influence of F. W. Taylor's scientific management and the development of sophisticated mass marketing, Bernays and others worked to develop a scientific patina for public relations that ultimately came close to being a glorification of propaganda. Indeed, Bernays's second book was titled *Propaganda.* In it, he argued that in a complex democratic society, propaganda provided the means through which consensus could be reached, and he posited that those who knew how to manipulate public opinion were, in essence, the true ruling power in society.

While public relations professionals learned to shy away from promoting themselves in such terms during the 1930s, 1940s, and 1950s, the focus remained on image making. The corporate public relations function was grounded in press relations activity—sending out press releases, maintaining good contacts with reporters, holding press conferences—but also included speech writing and the development of corporate brochures and films and, occasionally, systematic "speaker's bureaus" that would send out representatives to make speeches and presentations to schools and community groups. Ronald Reagan, for example, spent many years doing the speech circuit for General Electric.

Companies such as AT&T (then a national telephone monopoly), DuPont ("Better Things for Better Living Through Chemistry"), and General Motors were practitioners of very sophisticated image efforts, as were many smaller companies and some industries. Several also worked with the emerging field of public opinion research to develop public opinion tracking surveys to monitor their image and report back to management on how they were doing.

Evolution of the Function: Into the Maelstrom

Rachel Carson's *Silent Spring* and Ralph Nader's *Unsafe at Any Speed* ushered in a new era for public relations. Suddenly, the companies and industries that had felt confident about their image-making abilities found their reputations collapsing under a barrage of new questions about corporate behavior—environmental impacts, workplace discrimination, safety, operations in South Africa, and so on. The age of issue management had begun.

The term *issue management* is credited to Howard Chase, who coined it in 1976, describing a process of how issues emerge through a mixture of events, media, and activist groups: how issues grow and how they eventually lead to regulation—as they did in the early 1970s, in a panoply of new federal regulatory agencies, including the Occupational Safety and Health Administration, the Environmental Protection Agency, the Consumer Product Safety Commission, the Equal Employment Opportunity Commission, and so on. Like Bernays and Ivy, Chase argued that smart business management disciplines could be applied to the world of public opinion if a company or industry acted quickly during the early stages of issue development to reduce the underlying problem, to show that the perceived problem was not really a problem, or to offer other solutions besides regulation.

The public relations function—both within companies and in the agency world—expanded exponentially to deal with the new issue-laden environment, becoming more focused on public affairs activities. New lobbying offices were opened, not just in Washington but also in state capitals and in many European nations (and ultimately in Brussels). Public affairs experts emerged to offer new services, such as ally development (i.e., finding or creating third parties to communicate points of view), constituency mobilizations (e.g., letter-writing campaigns), and issue advertising (a technique pioneered by Mobil Oil during the energy crisis of the 1970s because of what it viewed as biased media coverage of energy issues).

Drawing on the evolving techniques used in political campaigns, public relations practitioners began to target their audiences through psychographic profiling, becoming more sophisticated at identifying and then mobilizing political forces. No longer was public relations concerned about a generalized public opinion;

now the question was who were the opinion leaders on particular issues and who were the mobilizable publics who needed to be reached through direct mail, telemarketing, or targeted media campaigns.

The field of marketing offered other new possibilities, such as focus group message testing to determine the right mobilizing messages. One of the most visible and successful issue-driven campaigns was probably that launched by insurance companies, pharmaceutical companies, and others to stymie President Bill Clinton's health care reform in the early 1990s. The message was crafted around protecting the right of health care consumers to choose their own providers. Through television and print advertising, targeted mobilization of letter writing, ally development, and other techniques, the Clinton plan was stopped in its tracks.

Parallel to these developments was the emergence of television as the dominant medium both in the United States and elsewhere. Until the 1960s, the public relations function had been mostly focused on print media—the leading local newspapers, the wire services that fed them, and major national magazines. Following the Kennedy assassination, television stations and the three nationally dominant networks (NBC, CBS, and ABC) vastly expanded news coverage and created new programs that covered issues of the day (e.g., *60 Minutes*, the morning news and talk shows). Then came CNN, followed in later decades by CNBC, MSNBC, Fox News, and so on.

Television became—as it continues to be—the most powerful force in defining and prioritizing public concerns. And it changed the timetable of the news cycle, which used to define the day in terms of the deadlines for going to press or the nightly news shows. Now there was no cycle—only endless news coverage.

Public relations professionals developed new skills and techniques to respond, taking advantage of the technological changes. An early innovation was media training for executives appearing on television, a medium where physicality is often as important as the words spoken and where message delivery strategies can differ depending on whether an interview is live or on tape.

In the 1980s, public relations agencies invented the video news release (VNR) and Radio Actualities, which were electronic versions of the traditional press release. They also developed "B-roll," which is a collection of video snippets with or without audio components that TV producers can use in developing a news segment. They learned how to create press conference environments that played first and foremost to television and only secondarily to the print media.

As satellite technology developed, both VNRs and B-roll could be distributed electronically and instantaneously. Equally important, companies and agencies discovered that they could have their own broadcast studios on the premises, offering a business executive live for an interview with a TV news host thousands of miles away. By the 1990s, "satellite media tours" allowed a spokesperson to sit in a small studio for a few hours and make sequential appearances on multiple local TV shows, answering local reporters. Then, with the advent of the Internet, "sound bite" sequences could be stored centrally for any reporter to pull down on demand.

These technological innovations became particularly useful for crisis communications, yet another emerging specialty in public relations. Starting with the nuclear accident at Three Mile Island in 1979, the Tylenol cyanide poisonings in 1982, and the chemical plant disaster in Bhopal, India, in 1984, companies began to realize that rapid and appropriate communications were critical in a fast-moving crisis environment. Various crisis communications experts began to outline procedures for managing communications in a crisis, and companies developed crisis communications manuals. Crisis preparedness planning became part of normal business practice. Companies in industries susceptible to large accidents (oil, chemicals, airlines) established technology-laden crisis communications centers on their premises, and many companies began to engage in crisis simulation exercises, in which press inquiries and press management were critical factors.

Another new field that developed was litigation communications. More and more companies under legal fire began to realize that battles were fought in the court of public opinion long before they were engaged in the court of law. With the investment community concerned about the potential costs of litigation and customers and employees worried about corporate or product reputation, no company could afford to be silent while plaintiff lawyers leaked documents and information to television and print reporters. So more experts emerged in the public relations profession—many of them trained as lawyers—to develop communications strategies that would precede courtroom activity and then carry the company through a trial and/or to a settlement.

Public Relations Today

The globalization of the media and the development of the Web have offered even more challenges and opportunities. Public relations functions are now the owners and operators of the company's Web site and, often, the company's Web communications strategy. Public relations professionals design and proactively manage large corporate Web sites containing massive amounts of information that once had to be printed in brochures and sent out in press kits. Reporters—once only reachable by phone, mail, or fax—now became available by e-mail, and conversely, reporters can now have quick access to in-depth and constantly updated information, statements, visuals, and video snippets any time of the day or night.

Today, the field of public relations involves activities, techniques, and subspecialties that parallel the social and technological complexities of the age. But the focus remains constant. Now it is called "reputation management," a reformulated statement of "image making." And while companies are more successful at managing political issues, the reputation of business in general and of most companies remains at an all-time low—as it was even before a series of corporate scandals (Enron, Tyco, WorldCom) raised new questions about corporate ethics and integrity.

Ironically, approaching its 100th year of existence, the public relations field also retains its own image problem. Phrases such as "flack" hang over the field, left over from movies and novels (e.g., *The Sweet Smell of Success* of 1957) in which the press agent is portrayed as amoral and scheming. There are more ominous phrases, such as "spin doctor," not unrelated to the profession's once lauded relationship to propaganda. Even the acronym *PR* continues to carry negative connotations, the reason why so many corporate departments now bear names such as Corporate Communications, Corporate Affairs, or External Relations. Countless professional confabulations have discussed the dilemma of the bad image of the public relations profession, but the experts in image making cannot seem to solve their own image problem.

Beyond Message Delivery to Dialogue

During the 1990s, the newly emerging ideology and methodology of corporate responsibility (sometimes corporate social responsibility) offered a new approach to the field of public relations. The underlying assumption of corporate responsibility—once articulated by Ivy Lee to John D. Rockefeller—is that a business cannot survive and be sustainable in the long term without the support of key constituencies. Those constituencies are not limited to those with economic ties (investors, employees, customers, suppliers) but include other critical social groups (the media, the government, communities, and what is now termed "civil society" and was once called interest groups).

The theory of corporate responsibility does not focus on the image of the company with these groups, however. It focuses on the concept of stakeholder engagement and the need to carefully listen to constituency groups as part of the decision-making process, attempting to address concerns as part of business development. It is a model where the company becomes a more transparent and open-minded entity, discussing issues and even business ideas with others so that social groups become involved actors in what is decided, while not, in any way, controlling the decision. The goal is not image or reputation but rather decision making that is compatible with the social and ethical concerns of communities that could be affected by it.

While the "managing reputation/image" model of public relations has always included the notion of "listening," this activity has been largely left to opinion research and to the intuition and accumulated experience of the public relations professional. More important, listening has been merely a step in the process of developing the message that then gets delivered by the most effective voices and techniques to get the particular perceptual outcome—for example, an issue belief, favorability for the company, and so on.

Now, according to the theory of corporate responsibility, listening has to be redefined as a serious kind of dialogue—a two-way conversation—where views are shared, common ground defined, and disagreements respected. The quality of the relationship is paramount, not the perception of the company.

This approach creates new challenges for the public relations field, which as of 2005, only some companies and industries have embraced—and only in some narrow issue areas. It changes the job of the public relations function to not just carry messages to the outside but also bring the outside in. In this way, business management is more likely to make decisions that are compatible with societal expectations and values.

This redefinition of the function requires that public relations professionals become more adept at give-and-take exchanges and at finding common ground, not in a context of a negotiation but in a context of dialogue and respectful sharing. This is a different skill set from that which has generally guided the profession—namely, the ability to develop influential messages (in print and in visual and aural forms) and deliver them creatively to intended audiences.

Becoming More Businesslike

While public relations functions learn to operate within the new corporate responsibility paradigms, it is unlikely that they will stop doing what they have long existed to do. Companies will continue to need core public relations activities—media relations, internal communications, Web site management, corporate identity and positioning, financial communications, issue monitoring and management, government affairs, contributions, and community relations—all being performed at the leading edge of technology and of communications theory and practice.

These public relations activities are increasingly managed in ways that parallel other core business functions. Long-term and short-term plans are developed as part of the business-planning process. Desired outcomes are agreed on and often expressed in perceptual terms—that is, a particular audience will hold a particular belief—or in terms of an action that an audience will take as a result of a belief: for example, purchase shares in the company. As in any business plan, the situation analysis is laid out, and strategies are outlined along with tactics (messages, messengers, and media).

Measurement can occur at several levels. *Output* is a measurement of the activity of the function: issuing press releases, making contacts with government officials, writing speeches, or improving the Web site.

Impact is a measurement of target audience exposure to the messages. This measurement parallels the field of advertising where reach, frequency, and gross rating points can be used as readings of how often an intended audience target is exposed to the message. Impact in public relations can be measured in terms of both message accuracy (described through word counts and subjective analyses of whether media coverage accurately delivered the desired message) and the number of people exposed to the media that carried the information.

The most elusive measurement is *outcome*—that is, whether all the public relations activity (the output) reached the audience the right way (the impact) to actually create or sustain the desired belief. Opinion research can be used to measure outcome (e.g., Did the percentage of believers increase?), but often public relations professionals are not eager to have their work judged on their ability to move public opinion. This reluctance then raises the question of whether the public relations profession will allow itself to be measured on its core mission, which is to influence opinion.

The movement of public relations into more of the business mainstream, including the use of business tools such as planning, objective setting, strategy articulation, and measurement, has not yet closed the gap that most public relations professionals—all the way back to Ivy Lee—would like to have closed. That is the gap that keeps them somewhat to the side in critical decision making. Public relations professionals yearn to have a "seat at the table" earlier in the decision-making process. They know that the adage "Actions speak louder than words" is valid, and that no "spin doctor" or "message delivery strategy" can turn a bad corporate behavior into an acceptable one. In the end, good public relations can help a company, but it can never replace—or cover up—bad decisions.

—Jim Lindheim

See also Advertising Ethics; Corporate Social Responsibility (CSR) and Corporate Social Performance (CSP); Crisis Management; Deceptive Advertising; Persuasive Advertising, Ethics of; Public Relations Ethics; Reputation Management; Stakeholder Engagement

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Public Relations Ethics

The ethical issues of public relations arise because public relations is not just a set of techniques to disseminate information. There is always a perceptual objective to be achieved, and ethical dilemmas abound in how that objective is achieved.

Codes of ethics exist within the public relations profession at various levels—in trade associations (The Public Relations Society of America, The Council of Public Relations Firms, the International Association of Business Communicators, etc.), in public relations agencies, and within the public relations departments of companies. Except in the specialized area of government relations, there are few laws that govern how public relations professionals go about their objective of persuasion. Enforcement of codes is sporadic, and sanctions are few. The codes that exist cover a variety of issues (protecting confidentiality, avoiding cultural offense, financial management), but three areas remain ethically ambiguous: (a) truthfulness of information, (b) relations with the media, and (c) motivation of third-party support.

Truthfulness of Information

The public relations industry makes a variety of statements about a commitment to supply information that is accurate and honest and known not to be false. Some of these statements go further to require that public relations professionals make an effort to confirm the accuracy of the information they are communicating and to correct any misinformation that is transmitted.

The ethical gray areas include what might be termed "lying by omission" or "being factually correct while leading to a misimpression." In both cases, there may be a commitment to "telling the truth" but perhaps not the whole truth. Indeed, only a slice of the truth might be presented, and this might be done in a fashion that knowingly leads the audience to a conclusion that they might not have reached if they had the "full story."

Such activities are very common in public relations (as they are in marketing), since public relations can involve "spin"—that is, finding the best thing to say and avoiding discussing the negatives. In some cases of regulated communications, such as FDA regulation of pharmaceutical information, there are both guidelines and a watchdog over this parsing of the truth. But even with regulation, the line between acceptable and unacceptable can be muddy.

Relations With the Media

The public relations profession has a symbiotic relationship with the media. Public relations people want their messages and stories in the press, and journalists need information and access.

In some parts of the world, direct payments to journalists for press coverage are a matter of course. In most countries, however, such "pay-for-play" practices are forbidden by the ethical codes of the media. However, there are some subtle distinctions in what *pay* may mean. Many—but not all—media outlets forbid reporters from accepting any travel reimbursement or entertainment from a company or an agency. But reporters can be invited to speak at conferences, sometimes for honoraria; and moonlighting reporters have been known to accept writing or video-editing jobs through companies that they own.

Most media also create an institutional barrier between their desire to sell advertising to a company and the company's desire for good media coverage. Nonetheless, many public relations professionals know when purchasing of ads will help with favorable coverage, and many media are now offering advertising in "special issue sections" (e.g., a report on environmental issues) where advertisers also will get coverage.

In early 2005, a major industry scandal erupted when a syndicated "columnist/commentator" received a government contract for his advertising firm to help explain a government program. The work also included speaking well of the program as a commentator. While the controversy led to apologies and the discussion of new rules for government public relations contracts, the practice is not rare. Various experts who widely comment through their own columns or TV appearances as specialized reporters (e.g., "our travel reporter") have contracts with companies to provide favorable comment. No disclosure of these relationships is required by public relations codes of practice.

The 2005 scandal also led to a focus on video news releases (VNRs) issued by government agencies. A VNR is designed to be a fully produced news segment that a TV news show can simply slip into its news program. It includes a "reporter," who may or may or may not appear on camera, and some government VNRs may include an "interview" with a senior government official that is actually a scripted appearance. In the 2005 controversy, reform proposals ranged from forbidding government-produced VNRs altogether (even for important public information programs) to requiring a visual disclosure on the entire tape. Government has no ability to require such disclosure on VNRs produced by the private sector.

Third-Party Spokespeople

Many public relations efforts involve motivating third parties (e.g., respected experts, happy consumers, celebrities, or interest groups) to carry a message to the media or directly to the intended audience. This may involve simply finding such people and encouraging them to make their views known. At the other end of the ethical spectrum is the paying of spokespeople, preparing and training them, writing their words, and "pitching" them to the media, all without disclosure of who is providing this support.

Strategies can also include the support of "coalitions," which are essentially front groups that will buy advertising, serve as spokespeople, and sometimes lobby a particular issue. Such support can include the re-creation of such groups or providing special grants to existing nonprofit groups to support specified activities on behalf of the company. Sometimes these relationships are publicly disclosed, sometimes not.

Disclosure is usually the ethical remedy suggested for these third-party practices, since it seems to be acceptable to pay a spokesperson or provide a VNR or even have a financial relationship with a business owned by a journalist if these relationships are fully disclosed. To date, however, the public relations industry—and some in the media industry—have resisted such a "sunshine" approach since the effectiveness of numerous public relations tactics would be greatly reduced if the mechanisms behind them were revealed.

—Jim Lindheim

See also Advertising Ethics; Codes of Conduct, Ethical and Professional; Disclosure; Marketing, Ethics of; Public Relations; Self-Regulation

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Public Utilities and Their Regulation

Public utilities are economic entities "vested with the public interest," also known as "common calling enterprises." "Vested with the public interest" is a centuries-old concept based on the common-law notion of "status," a complex set of rights and responsibilities associated with the provision of services of public necessity. Those who engage in common calling enterprises are bound by status to provide goods and services in accord with the needs of the broader community.

Public utilities are defined by the necessity of the goods and services they provide and the inherent market power they possess. Public utility services are essential because of both what is provided, such as water or electricity, and the network system of delivery. Many public utilities are infrastructure organizations, entities that maintain the fabric of social and economic institutions by providing network connectivity for individuals and continuous interconnections among buyers and sellers. The demand for public utility services is time critical; even relatively brief service interruptions can result in significant economic loss and social disruption. Due to the necessity of utility services, consumer demand is highly price inelastic, and governments assert oversight responsibility.

Historically, grist mills, granaries, docks, wharfs, toll roads, intra-urban transport systems, and railways were considered to be public utility entities vested with the public interest. Currently, electric power, natural gas, telecommunications, and water and sewerage are considered to be the core public utilities, although not all aspects of their supply are public utility in nature. For example, natural gas transmission and distribution are public utility services, though natural gas production is not.

Most utility markets will not sustain numerous independent suppliers. Instead, utility markets are served by a very limited number of entities, most often by a single firm. Public utilities firms are often referred to as "natural" monopolies because their control of utility markets is rooted in technologies of production rather than artificial constraints such as anticompetitive practices or governmental grants of exclusivity.

Public utility technologies are capital intensive and manifest extensive economies. Public utilities typically require 5 to 10 times as much investment per dollar of revenue as do economic enterprises in general. Many factors lead to the capital-intensive nature of utilities. Utility services often require permanent physical connections between suppliers and consumers. Utility supply systems, such as electricity, natural gas, or telecommunications, are tightly coupled, highly interdependent, and subject to significant reliability externalities; changes in the level of use by one customer can affect the reliability of service for others. Unlike airplanes or parking garages, when public utility demand exceeds the available supply, system failure can ensue, resulting in a loss of service for all customers. Because there tends to be little or no storage, high levels of service reliability can only be maintained by building system capacity significantly in excess of expected peak demand.

There are various types of public utility economies. Transmission systems, for example, exhibit economies of scale; when fully utilized, the larger the capacity of a natural gas pipeline or electric transmission line, the lower the average cost of delivery. Local distribution systems exhibit economies of density; the cost per customer served decreases as service area density increases. Utilities have economies of diversity; the cost of having a single firm serve a number of different types of customers is less than the costs of having different firms serve different types of customers. The combination of the various types of economies leads to market "cost-subadditivity"; it is less expensive for one firm, or at most a very small number of firms, to provide service to an entire market than it would be to divide market service among many firms.

High levels of capital intensity result in substantial barriers to entry. Extensive economies preclude the market sustainability of many independent providers. The result is that necessary public utility services are provided by organizations with substantial market power.

Industries vested with the public interest bear a responsibility to provide service at just prices, without discrimination, and on a reliable basis. Just prices are based on the costs of service rather than the relative bargaining power of buyers and sellers. Nondiscrimination means that all must have access to the service and that similar customers must be treated similarly. Reliability pertains to the continuous provision of utility service of acceptable quality. These common-law responsibilities emanate from a system of social ethics attuned to concerns with protection, fairness, and attainment of the social good.

Open markets cannot be relied on to ensure the attainment of common calling responsibilities. Unlike firms in competitive markets, monopoly utilities have the capacity to set prices in excess of costs, engage in price discrimination, limit access to the service, and maintain reliability levels below that which would best serve the public interest. Some form of governmental intervention is necessary if public interest objectives are to be attained. The two primary approaches for governmental intervention are (1) extensive regulation of privately owned utilities and (2) government provision of public utility services. While there are several governmentally owned utilities in the United States, the predominant means of oversight has been through extensively regulating privately owned utility companies.

The common-law basis of public utility regulation in America was affirmed by the U.S. Supreme Court in *Munn v. Illinois*, 94 U.S. 113 (1876). In its seminal decision, the Supreme Court held that the state of Illinois could regulate grain elevator storage prices because grain elevator storage was an undertaking vested with the public interest—storage was necessary for effective supplier participation in grain markets—and storage was provided by a shared monopoly. Although subsequent Supreme Court decisions broadened the bases for establishing a state's constitutional authority to regulate business, American public utility regulation developed in accord with the *Munn v. Illinois* standards.

Utilities in the United States are regulated at both the state and federal levels. In 1907, New York and Wisconsin became the first states to establish public utility regulatory commissions. By the late 1920s, over two thirds of the states had regulatory agencies. Today, all states have public utility commissions.

Federal public utility regulation, particularly with respect to price control, arose primarily in the 1930s. The Communications Act of 1934 placed telecommunication regulatory authority in the Federal Communications Commission (FCC). The Federal Power Act of 1935 and the Natural Gas Act of 1938 placed energy utility regulatory authority in the Federal Power Commission (now named the Federal Energy Regulatory Commission, FERC). Other important federal public utility regulatory statutes include the Telecommunications Act of 1996, the Public Utility Regulatory Policy Act of 1978, the Natural Gas Policy Act of 1978, and the Energy Policy Acts (1992, 2005).

The primary responsibility of public utility commissions has been to regulate utility prices. Commissions have a wide range of other regulatory powers, including control over market entry, service requirements, construction, issuance of securities, ownership, affiliate relationships, product standards, accounting, information and reporting systems, operating standards, and so forth. While significant in their own right, these additional regulatory powers primarily serve to enable effective regulation of utility prices.

State commissions regulate retail prices and utility construction. The FERC regulates electricity and natural gas wholesale prices and transmission rates. The FERC also has regulatory authority over natural gas pipeline construction. The FCC regulates interstate telecommunication prices and controls the provision of wireless telecommunication licenses.

Federal and state public utility commissions are almost always required by statute to set "just and reasonable" utility prices. Historically, prices were considered to be just and reasonable if they were based on the costs of service. Traditionally, commissions determined just and reasonable prices through company-specific litigated rate cases. Commissions evaluated revenue requirements through assessment of service costs—a utility's jurisdictional specific operating expenses, taxes, depreciation, and necessary returns on investment—and established prices accordingly. Utility prices were established on a forward-looking rather than a retroactive basis. While previous deficient or excess earnings provide a reason for changing utility prices, the utility is neither allowed to recover lost earnings nor required to return excess profits.

In various jurisdictions, commissions augmented traditional rate-making methods by automatic adjustment clauses and performance-based rate mechanisms. Automatic adjustment clauses give a utility the ability to periodically adjust its prices based on changes in only some of its costs, such as the cost of fuel or purchased gas supplies. Performance-based rates incorporate profit incentives and rewards into the pricing mechanisms. The incentives or rewards may be based on a number of factors, such as utility productivity, service quality, plant availability, and consumer energy use efficiency.

In recent years, several commissions have moved away from company-specific cost-based pricing. These commissions have adopted formulaic price-capping mechanisms or have established other standards for determining just and reasonable prices. Price caps "decouple" a utility's prices from its cost of service. Price caps establish an upper boundary on the annual rate of change of a utility's average prices based on economywide inflation indices adjusted for assumed rates of productivity improvement. Alternatively, some utility commissions now accept negotiated or market-based rates as just and reasonable if there is buyer access to alternative providers.

Public utility regulatory commissions, particularly those at the state level, require a utility to obtain a "certificate of public convenience and necessity" prior to the construction of a new plant and equipment. The reason for licensing construction is to avoid the adverse consequences of overbuilding, such as threats to utility solvency or the need to impose substantial increases in customer prices. Traditionally, construction projects were evaluated on a project-specific, case-by-case basis. From the 1970s into the 1990s, many state commissions moved from a case-by-case evaluation of electric utility projects to a comprehensive planning framework. Commissions assessed future demand requirements; evaluated the private, environmental, and other social costs of a range of alternative construction and energy use efficiency options; and established a least-cost plan to ensure ongoing system reliability. Commissions then decided whether to grant construction approvals based on a specific project's conformity with the least-cost plan. This planning approach constituted a major shift in regulatory function; commissions moved from focusing primarily on price control to engaging in systemwide planning. While various consumer and environmental groups embraced regulatory planning efforts, most utilities saw commission planning as an inappropriate infringement on managerial prerogatives. In the latter part of the 1990s, commissions moved away from system planning as the FERC opened wholesale electric power markets and "non-utility" electricity suppliers entered the market.

For the greater part of the century, regulators viewed their primary responsibilities as being the direct control of utility prices and the assurance of service reliability. In recent years, however, regulatory policy has turned to opening utility markets. By the early 1980s, the FERC no longer regulated natural gas wellhead prices. In the mid-1980s, the FERC opened wellhead supply markets to local distribution companies and end-use consumers. In its Order 636, the FERC required natural gas pipelines to provide transmission service for the delivery of natural gas supplies purchased by local distribution companies and consumers directly from producers or through market brokers. As the direct purchase of natural gas supplies increased, interstate pipeline companies were transformed from natural gas merchants into the equivalent of common carriers. The FERC began to open wholesale electricity markets in the late 1990s. In its Order 888, the FERC required open access to transmission services. The FERC has also promoted the formation of regional transmission organizations to handle the operation of transmission systems and oversee emerging open wholesale markets.

As the FERC was opening up wholesale markets, some states opened retail markets to alternative providers. Natural gas retail consumers, particularly industrial customers, were allowed to purchase supplies directly from producers and brokers. Electric retail consumers were allowed to designate who would provide the kilowatts they consumed. Although the natural gas and electricity commodity markets were opened up, the transmission and distribution systems have remained under more traditional forms of regulatory control.

In the telecommunications industry, public utility regulatory control has been substantially eliminated. Prior to the 1980s, AT&T controlled 85% of local telecommunications markets and virtually all the long-distance market; long-distance rates were regulated by the FCC and local rates by state commissions. Several factors have altered the industry since then, including AT&T's divestiture of its local operations pursuant to a 1984 antitrust consent decree, the growth of the Internet, the development of broadband services and alternative means of broadband access, the rapid expansion of wireless telecommunications, and the passage of the 1996 Telecommunications Act. In the 1990s, the FCC ended its regulation of long-distance rates. Most state commissions have now relaxed rate regulation by adopting price cap mechanisms or by accepting negotiated prices as just and reasonable rates. Wireless and broadband services have developed outside public utility regulatory controls.

Various reasons have been given for the substantial shift in public utility regulation policies. Some believe that technological changes have obviated the need for substantial regulatory oversight. Transmission advances enabled the opening up of regionwide wholesale markets. Technological advances fostered cost-effective, small-scale, independently owned power systems. Technological advances have reduced the cost of telecommunications operations and fostered the development of alternative types of services and different means of delivery—such as broadband services that can be provided through existing telephone facilities, by cable, by wireless, by satellite, and over power lines. Some believe that the movement toward deregulation was prompted by claims that regulatory deficiencies hampered technological development and induced significant inefficiencies in the provision of utility service. Some suggest that a partial opening of some portions of utility markets led to the cascading inability of commissions to maintain effective or reasonable regulatory controls in general. Some argue that those seeking increased profits and reduced regulatory interference successfully influenced politicians through campaign contributions and effective lobbying. Some argued that regulatory systems were dismantled for ideological reasons when conservatives and free market advocates gained control of the various branches of state and federal governments.

Some of the results of opening utility markets have been beneficial. Long-distance phone rates have declined. The development and adoption of new technologies have brought forth a range of new telecommunication services for consumers. Utility companies have become more attuned to customer needs. Various investors have gained substantial profits as utility systems were deregulated and sold.

However, many results of deregulation have been less than favorable. Wireless and broadband services lag behind those in other industrial countries. Wireless and broadband access is not being made available to all; there is a persistent digital access divide between urban and rural areas and between low-income consumers and others. Telecommunication companies have indicated their intention to alter Internet service accessibility by ending network neutrality on their broadband systems. Utility markets have become more concentrated as major mergers have swept through the telecommunications and energy utility industries. Local phone rates have increased substantially. Natural gas and electric power wholesale prices have become much more volatile. Retail electric and natural gas prices are now much higher than had been previously predicted. Discouraged by the results of deregulation, many states reversed it or put further deregulatory efforts on hold. Previous proponents of deregulation, including associations of large industrial energy users, now argue that various efforts at deregulation have failed and that a return to traditional systems of regulatory control should be seriously considered.

Public utilities are not static. As technologies and needs change, so do the goods and services that bear public utility attributes. People living two centuries ago could not have imagined today's public utilities—they had yet to be invented. Likewise, public utility regulation is not static. As social and economic institutions change, so do the forms of governmental oversight. Administrative regulation, today's predominant institutional mechanism for public utility oversight, did not evolve until after the late 1800s. What remains constant, however, is the premise that there are goods and services that are public utility necessities and the conclusion that the public interest requires their regulation.

—*Rodney Stevenson*

See also Common Law; Deregulation; Economies of Scale; Enron Corporation; Federal Communications Commission (FCC); Internet and Computing Legislation; Just Price; Market Failure; Monopolies, Duopolies, and Oligopolies; Public Interest; Regulation and Regulatory Agencies; Telecommunications Act of 1996; WorldCom

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Punitive Damages

What Are Punitive Damages?

They Are Additional to Other Damages

Punitive damages are additional to the compensatory damages a judge or a jury may grant a plaintiff. Special damages are designed to replace "out-of-pocket" costs to the plaintiff. General damages are designed to compensate for the more ephemeral losses—such as pain and suffering; loss of consortium; or loss of care, love, and affection—to the plaintiff. Punitive damages are awarded to punish and make an example of the defendant.

Punitive Damages Cannot Be Insured

Generally, compensatory damages are paid for by an insurance company. Common law and many state laws or regulations prohibited insurance companies from insuring or paying punitive damages. Punitive damages must be paid for by the party against whom they are assessed.

Punitive Damages Are Quasi-Criminal Assessments

Punitive damages serve a similar purpose as criminal penalties—they punish the defendant and serve to make an example of the defendant. However, because civil defendants are not afforded the same due process and procedural protections as their criminal counterparts, the imposition of punitive damages inherently includes the danger of arbitrary and excessive deprivation of property. This problem is exacerbated when the decision maker, usually a jury, has also been presented with the inflammatory evidence necessary to merit the imposition of punitive damages. For an example of bad behavior that can lead to the imposition of punitive damages, read the facts in *State Farm v. Campbell et al.*, 538 U.S. 416 (2003).

Because of their quasi-criminal nature and the potential for abuse or mistake, the threat of punitive damages touches a red hot button for many people, especially the business community. This entry will look at the type of claims that cause courts and juries to award punitive damages, the Supreme Court's theory of ratio of punitive damages to compensatory damages, and some open issues.

One Legislature's Definition

California's Civil Codes § 3294 is an example of how a state's legislature codifies punitive damages. It states, in salient part, the following:

> In an action for the breach of an obligation not arising from contract, where it is proven by clear and convincing evidence that the defendant has been guilty of oppression, fraud, or malice, the plaintiff, in addition to the actual damages, may recover damages for the sake of example and by way of punishing the defendant.

Punitive Damages Generally Require a Tortious Act

The statute requires the alleged offensive act to arise from a tort, not a contract. These are two very different theories of law. A tort is an offense against an individual. A breach of contract is where a party is alleged to have broken its contractual obligation. This definitional difference can be dangerously simplistic and tricky.

One area of law where these two legal theories blend involves the duty of parties to exercise "good faith and fair dealing" in a contract. If one of the parties had larceny in his or her heart when entering into a contract and used some device to take advantage of the other party (or parties) to the contract, the aggrieved party could claim that the offensive party lacked the requisite "good faith." In a lawsuit, the aggrieved party would allege a "breach of the covenant to deal fairly and in good faith." Although this breach arises in a *contract* setting, the breach of this duty has been routinely defined as a *tort*. Therefore, in the case of California's statute on punitive damages, while there can be no punitive damages for the breach of the *contract*, there can be punitive damages for the *tort*. So the aggrieved party can claim punitive damages for the breach of the duty to deal fairly and in good faith but not for the breach of the contract.

The Standard of Proof for Punitive Damages Is Higher

Constitutional Standard: Probable Cause

The lowest level of proof is "probable cause." This is the level referred to by the Constitution in the Fifth Amendment, which allows the state to get a warrant. It is the level by which a law enforcement officer can stop a citizen and then instigate an investigation or interrogation. Probable cause has a very low evidentiary threshold.

Civil Standard: Preponderance

The next highest level of proof is a "preponderance," which is the standard of proof in a civil action. The simile often used to demonstrate this level of proof is to imagine the Lady of Justice's scales. If they should tilt ever so slightly one way or the other, the heavier side has been said to have the preponderance of the evidence.

Criminal Standard: Beyond a Reasonable Doubt

The highest level of proof is "beyond a reasonable doubt." This is the level reserved for criminal cases. The burden is on the state to prove that the accused is guilty "beyond a reasonable doubt." The higher burden is an attempt to offset the extraordinary range of resources the state has to prosecute the accused.

Punitive Damages Standard: Clear and Convincing

Between preponderance and beyond a reasonable doubt lies a level of burden of proof called "clear and convincing." It is beyond the 51/49% of preponderance and below the "beyond a reasonable doubt" standard. Clear and convincing is a compromise that considers the quasi-criminal nature of punitive damages. Courts have historically upheld this standard as reflecting society's and the court's disfavor of punitive damages.

Clear and convincing is the *legal* barrier a plaintiff must cross to prove his or her case. However, in the courtroom, even when a plaintiff meets his or her burden of proving the claim for punitive damages by clear and convincing evidence, juries find it hard to award punitive damages in all but the most egregious cases. Furthermore, appellate courts uphold punitive damages in only the most serious circumstances.

The Purpose of Punitive Damages

As California's statute states, punitive damages are used to make an example and punish the alleged offender. As mentioned above, the imposition of punitive damages assumes the mantle of quasi-criminal punishment. One of the questions plaguing the imposition of punitive damages is, "What does punishment, *sufficient* punishment, look like?"

Suppose a person of modest means chooses a certain behavior, such as using marijuana. What kind of punishment would cause such a person to change his or her behavior? Would a "warning" cause him or her to stop using marijuana? Probably not. How about a $25 fine? Again, probably not. A $250 fine? It might get his or her attention, especially if it were imposed regularly, every time he or she used the drug. Now, how about seizure of all his or her property, a 10-year sentence in a federal jail, and a $250,000 fine? Chances are high this draconian step would cause the miscreant to change his or her behavior.

This is the principle behind punitive damages. Punitive damages should be sufficient to punish and make an example of the defendant, in consideration of the defendant's wealth and ability to pay the damages. The elusive issue is what is just enough but not too much.

Suppose a manufacturer creates a product, develops the product, tests the prototypes, markets the product, and sells the product. Before the product has been placed into the stream of commerce but after the manufacturer has spent hundreds of millions of dollars on the initial development and testing, the manufacturer discovers that the product is defective. Management determines to near certainty that in a common-use scenario, the product uniformly fails catastrophically, with predictable results of serious injury or death to the user. Rather than pulling the product, as Johnson & Johnson did during the Tylenol problem of the 1980s, this manufacturer makes a simple cost-benefit analysis to determine how to proceed.

To a statistical certainty, the catastrophic failure will result in 180 deaths by burning, 180 serious injuries attributed to burning, and 2,100 burned vehicles. The unit cost is $200,000 per death, which was a published U.S. government figure for the value of human life at the time, $67,000 per injury, and $700 property damage per vehicle. The total benefit of doing nothing can be computed by the formula $180 \times (\$200{,}000) + 180 \times (\$67{,}000) + 2{,}100 \times (\$700)$ for a result of $49,500,000. This figure assumes that all persons sue and recover.

Then, the risk management section crunches the numbers and further analyses the cost. They find that 12,500,000 vehicles were sold. The unit repair cost is $11.00. The total cost formula is $12{,}500{,}000 \times \$11.00$ for a result of $137,000,000. The manufacturer decides that it is cheaper to deal with the deaths, injuries, and property damage than to make the repairs. It is decided not to recall the product and to deal with the cases as they appear. The figures used in this hypothetical problem were actual numbers taken from the Ford Motor Company interoffice memo titled "Fatalities Associated With Crash Induced Fuel Leakage and Fires" by E. S. Grush and C. S. Saunby, which was used in conjunction with the Ford Pinto litigation in the 1960s and 1970s.

After a series of configurations resulting in the predicted deaths and injuries, how should society get the company's attention? The company has made a clear decision to sell a product it knew to be defective. It chose to put people at risk after doing its own risk-benefit study. This is a scenario that might merit the imposition of punitive damages. Assuming that a plaintiff can show, by clear and convincing evidence, that the manufacturer knew of the problem, it might be very appropriate to award punitive damages to punish and make an example of the errant manufacturer.

In *Time* magazine, March 10, 2006, there was an article that discussed the *Exxon Valdez* oil disaster. Sixteen years after the accident, Exxon is still disputing the punitive damages award. The attorney of one of the victims was quoted as saying, "Only punitive damages will give Exxon the incentive to prevent future oil spills. The industry's perception is that all they have to worry about is the immediate out-of-pocket costs and they can just pollute and pay."

Some Unresolved Issues

Multiple Plaintiffs and Class Action Cases

One of the unresolved issues involves multiple plaintiffs, such as in a class action case. If one plaintiff were to recover a large punitive damage award, what about the other plaintiffs? If the behavior was considered reprehensible in the first case to trial, what mitigates the behavior in the subsequent cases? On the other hand, if the punitive damage award was sufficient enough to punish and make an example of the manufacturer in the first case, then other punitive damages would be definitionally unfair because the original imposition was supposed to be sufficient to "punish and make an example of" the defendant. On the other hand, is it not unfair to give a large award, seemingly a windfall, to only one of a number of injured plaintiffs?

The "Ratio"

The issue of the ratio of punitive damages to compensatory damages has been before the U.S. Supreme

Court twice in the last decade. The first case was *BMW of North America, Inc. v. Gore*, 517 U.S. 559 (1996), and the second was *State Farm Mutual Automobile Insurance Co. v. Campbell et al.*, 538 U.S. 416 (2003). In *Gore*, the Supreme Court overturned a $2,000,000 punitive damages award that accompanied a $4,000 compensatory award. In *Campbell*, the Court reversed a $145,000,000 punitive damages award where the compensatory damages were $1,000,000.

The Supreme Court, in *Gore* and *Campbell,* refused to give a specific formula or ratio. However, in both cases, the Court said, "In practice, few awards exceeding a single digit ratio between punitive and compensatory damages will satisfy due process." The Court found that single-digit multipliers satisfied both the due process issues presented by the Fourteenth Amendment to the Constitution and the state's need for punishment and deterrence. In *Gore*, the ratio was 500 to 1, and in *Campbell*, the ratio was 145 to 1.

However, to a company such as BMW or State Farm, if the aberrant behavior was very profitable, would the imposition of insignificant punitive damages really be a deterrence? For example, in *BMW*, the company was punished for failing to disclose that they were selling vehicles damaged in the manufacturing process as new vehicles. If the Court's guidance for a ratio was 9 to 1 and the damage was $4,000, the maximum punitive damage would be $36,000. Considering that the vehicle sale price was more than double the maximum amount that could be awarded for punitive damages, would the 9-to-1 ratio be enough to cause the defendant to refrain from the practice of selling vehicles damaged at the factory as new cars?

Popular Prejudices

Over a decade ago, an article in the June 17, 1996, *Wall Street Journal* discussed punitive damages from a business perspective. The authors addressed some of the commonly held misunderstandings regarding punitive damages. They said,

> Here is the latest stunning development about runaway punitive-damage awards: They may not be as common as you think. . . . Punitive awards are generally modest, and meted out in only the most extreme circumstances. . . . According to the study, most punitive awards aren't random, as critics have argued, but instead are closely tailored to the amount of compensatory damages, such as medical expenses and lost wages. Punitive damages are designed to punish and deter bad conduct. . . . The study found a much closer relationship between punitive and compensatory damages in most cases. Where compensatory damages were $10,000, punitives averaged around $10,860. Where compensatory damages were $100,000, punitives averaged around $65,720. And where compensatory damages were $1 million, punitives averaged $397,810.

This is just one example of the public's common misunderstanding of the nature and purpose of punitive damages. More important, it also gives an indication of the depth of passions around the subject. Is this prejudice a function of excellent manipulation of the media by savvy manufacturers or artificial hype brought to the public by the media?

What seems to be accurate is that in most cases, when the public hears the real facts of a case where punitive damages are awarded, they usually have no problem. Once the public hears why a jury gave punitive damages, the reasons predicated on the evidence proven in the trial, the average citizen is supportive. However, when only partial facts are given, many people look at these awards askance.

An example is *Liebeck v. McDonald's Corp*, the (in)famous "hot coffee" case. Many people have a very strong feeling that this case was just ridiculous. However, when they are quizzed to give the facts, invariably they give the wrong facts. When they are told the facts the jury heard, even the most obstinate persons usually feel that they have been duped by the media. Perhaps the more important question is who gave the "story" to the media and why they omitted the essential facts.

Conclusion

The issue of punitive damages touches social and legal hot buttons. However, such damages serve a valid social purpose. Punitive damages are designed to be punitive, to punish and make an example of a wrongdoer. Without punitive damages, society has no other viable means of holding large corporate entities accountable for intentional wrongdoing. One of the current important questions is what constitutes enough punishment. What is enough money to "punish and make an example" yet not so much as to violate an entity's right to due process under the law? The intertwining of civil and criminal law is what makes punitive damages so volatile and yet so effective. As long as punitive damages remain an alternative, they may serve a greater purpose, that of deterring despicable behavior.

—*Michael B. Rainey*

See also Commutative Theory of Justice; Compensatory Damages; Dalkon Shield; Enron Corporation; *Exxon Valdez*; Firestone Tires; Ford Pinto; Global Crossing; Johns-Manville; Price-Fixing; Tyco International

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R

Racial Discrimination

Racial discrimination in the United States is discrimination on the basis of an individual's race, generally manifested in blacks not receiving jobs, housing, education, and so on, of the same caliber as whites. Due to the unique racial history of the United States, racial discrimination often refers to the relationship between blacks and whites. Other groups that have been subjected to discrimination historically include Native Americans, Jews, Hispanics, the Japanese, and Muslims. However, these categories are generally considered to be discriminated on the basis of national origin or religion rather than race and are discussed in other entries.

To understand racial discrimination in the United States, it must be put in its proper historical perspective. Racial discrimination has deep roots in American history. Being founded by immigrants and well known for embracing immigrants from all over the world, the United States has a unique relationship with blacks. Africans make up the only group in what was to become America that did not voluntarily immigrate here. Rather, they were captured in Africa by Europeans and brought to the colonies to be used as a means of cheap labor to supply the ever-growing need of the colonists forging a new country from uncharted (for Europeans) territory. The choice to enslave Africans and the results of that system form the basis for much of the racial discrimination against African Americans still present in the United States today.

The first Africans in an American colony, who arrived aboard a Dutch ship in 1619, were actually not intended as slaves for the colony. The Dutch ran low on provisions and offered several of their African cargo, bound elsewhere, in exchange for provisions. Afterward, Africans brought to America were not enslaved but, as was the case with many Europeans, were indentured servants for a fixed period of generally 7 years. For the Africans, this arrangement lasted for only about 40 years. As the need for cheap labor grew, more restrictions were put on the indentured servitude of Africans, until finally they were enslaved for life and totally owned by their purchaser. Throughout slavery, there were a small number of free blacks and blacks who did manage to achieve a measure of success in business, the arts, and commerce, regardless of their circumstances, often with the help of sympathetic whites, but the system was overwhelmingly one of black enslavement and subjugation.

As the need for cheap labor increased, growing numbers of Africans were imported. Slaves were also bred by owners as a cheap way to increase an owner's slaveholdings, particularly after importation of slaves was outlawed in the early 19th century. Eventually, in some places the slave population rivaled or outstripped the white population. As such, slave uprisings were a primary concern. Each slave could not be watched at all times, so means were needed to prevent the possibility of such an occurrence. Ultimately, the consensus was that the most efficient means of control was a combination of self-monitoring mechanisms to keep slaves in line coupled with strict enforcement of rules by owners.

To create the self-monitoring mechanism, owners ensured that each minute of every day, in every way possible, a slave be reminded of his or her position in society so that the thought of changing the status quo would not even arise. This was accomplished in varied ways, from formal laws to violent punishment; from not being allowed to use their own languages to owners' unrestricted sexual access to female slaves; from using rough "Negro cloth" for slave clothing to making it a crime to teach slaves to read and write. Slave codes and ironclad social customs outlined the role of slaves and owners in minute and careful detail.

Though they varied from state to state, generally, the codes gave owners absolute power over the life, and even death, of slaves. Slaves were permitted little, if any, control over any aspect of their lives. Their children were not their own, they were not allowed to marry without the owner's permission, to read, write, travel outside their owner's property without written permission, gather in groups of three or more, enter into contracts, or raise their voices to whites, and they generally had no rights or status as human beings. Slaves were taught that they belonged to the owner and must obey whites without question. Whites were taught that slaves were inferior to them in every way and were to be treated as little more than errant children. Each learned his or her place from birth and generally maintained it. Transgressions resulted in swift and fierce retribution. To maintain the status quo and prevent uprisings, it was important that slaves understood that violations of law or custom, no matter how small, were not to be tolerated. *Dred Scott v. Sanford*, 19 Howard 393, of 1857 held that a slave who had lived in a free state for 7 years was, in fact, still a slave. Despite many slave revolts, for the most part, to survive, slaves learned to be subservient and respectful to whites and to think they were incapable of being responsible for themselves.

This system was in place from the 1600s until after the Civil War (1861–1865) ended nearly 250 years later. Blacks had virtually never been free in this country, so there was little experience as to how the race of 4 million free blacks would fit into American society. For about 5 years after the Civil War ended, the Freedmen's Bureau (The Bureau of Refugees, Freedmen, and Abandoned Lands) attempted to try to help newly freed slaves, but it suffered from chronic underfunding and stiff white resistance. Blacks were thus released from slavery and, for the most part, simply left to fend for themselves with no education, little support, and much resentment by whites. Promises made to give them land were revoked by Andrew Johnson, the U.S. president who took office after President Lincoln's assassination.

After Southern Reconstruction (1865–1877), when federal troops were stationed in the South to keep it from reverting to pre–Civil War slavery, there was little to keep resentful southerners from doing what they could to return to their previous way of life. Slave codes were replaced with black codes, and for the next 99 years, until the Civil Rights Act of 1964, the era known as Jim Crow existed. Emanating from an 1830s minstrel show act by a white performer in blackface makeup singing and dancing to a song called *Jim Crow* to the delight of white audiences, *Jim Crow* is the term used for the set of laws and social mores that arose after Reconstruction to keep blacks and whites strictly segregated and blacks subservient. *Plessy v. Ferguson*, 163 U.S. 537, of 1896 had held that racial segregation was constitutional and gave judicial affirmation to states' "separate but equal" Jim Crow approach to race.

Jim Crow meant that blacks and whites could not attend the same public or private schools, universities, theaters, parks, municipal swimming pools, libraries, churches, stores, hospitals, doctor's offices, beauty or barbershops or restaurants, or even drink from the same water fountains or use the same toilet facilities, and they could not marry or sit together while riding public transportation. Discrimination in housing, education, and employment was widely permitted. Newspaper classified sections were divided into jobs for whites and those for "coloreds."

For the next 99 years after the Civil War ended in 1865, blacks in the South, where the vast majority of them lived, were in much the same position they had been in under slavery. Jim Crow segregation excluded blacks from most of mainstream life. Unfair sharecropping and convict lease laws kept blacks working for whites at low or no wages. The Ku Klux Klan was a white supremacist organization that used violence and intimidation to keep blacks subjugated. The lynching of blacks, particularly of black men, as a means of social control was widespread, with 3,446 lynched between 1882, when reliable statistics were first collected, and 1968, when most lynching had subsided. Lynchings were often social affairs, complete with families, children, picnics, and photos taken with the hanging corpse. Appeals to the federal government to intervene received no quarter—something for which Congress apologized in 2005, though there were dissenters.

Picking cotton engaged the vast majority of black workers in the South. This task was mechanized soon after the end of World War II. No longer needed for this labor-intensive role and trying to escape the racial oppression of the South, for the first time blacks began leaving the South in significant numbers. They found jobs in cities, filling in for those who left for military service during World War II, and left for military service themselves. Thus began the Great Migration, the largest peacetime domestic exodus that the world had ever seen. From the early 20th century until the 1960s, millions of blacks left farms in the South and migrated to cities. In 1910, 89% of blacks still lived in the South, and 80% of that number lived in rural areas. By 1960, 40% of blacks lived outside the South, and 75% of these lived in cities.

Rural blacks moving to urban areas created many challenges, not the least of which were demands for decent employment, housing, and education as well as other social issues. Jim Crow continued to be a way of life, for both social and economic reasons, even more so since the cities to which blacks migrated had never had so many blacks living in them, and, for the most part, blacks coming from the farms had little or no education that would permit them to move into anything other than menial jobs. Vibrant communities of blacks thrived in some ways under segregation, having their own doctors, lawyers, and so on, but for the most part, blacks were primarily consigned to poorer neighborhoods and jobs as domestics, caretakers, cooks, and laborers.

Under Jim Crow, blacks were also denied the right to vote in elections, with the imposition of poll taxes, literacy tests, and other measures aimed at keeping them from the ballot box. Real estate contracts routinely contained restrictive covenants that prohibited a buyer from conveying the property to blacks. The armed services were segregated, with blacks generally being allowed to perform only manual labor. Though slavery had ended nearly 100 years earlier, blacks were in no way considered equal citizens in the United States.

In 1954, in *Brown v. Board of Education*, 348 U.S. 886, the U.S. Supreme Court struck down segregation in public education and paved the way for dismantling the system of racial segregation in the United States. In response, whites rioted and some public school systems, for instance in Virginia and Arkansas, closed the entire school system rather than allow white and black children to attend school together. Ten thousand federalized National Guard troops were called in by President Dwight Eisenhower, and 1,000 paratroopers were dispatched to handle the crowd of 1,000 angry whites when nine high school students ("the Little Rock Nine") integrated Little Rock's Central High School in Arkansas. Two people were killed and more than 150 federal marshals injured when the University of Mississippi admitted its first black students in 1962. Schools would not be integrated until well into the 1970s, during which time whites began moving from cities to suburbs to avoid the issue. In the years following the integration of Central High School in Little Rock, the civil rights movement, always simmering at a low level, heated up and became more pressing.

In 1963, the largest march ever to take place was held in Washington, D.C., at which the Rev. Dr. Martin Luther King Jr. gave his famous "I Have a Dream" speech. Blacks, whites, Jews, and others came from all around the world to protest the unequal treatment of blacks. The next year, President Lyndon B. Johnson signed into law the Civil Rights Act of 1964, which had been introduced by President John F. Kennedy. The law, which became effective in 1965, prohibited discrimination on the basis of race, color, gender, religion, and national origin in employment, education, public accommodations, and the receipt of federal funds. Though there had been a few pieces of legislation passed after the Civil War (called the post–Civil War statutes) to give blacks the right to enter into contracts like whites, to prevent citizens from being deprived of their rights under the pretense of following state law, and to prohibit Ku Klux Klan–type actions, none were as comprehensive and far-reaching as the Civil Rights Act of 1964. Even though the Civil Rights Act of 1964 relates to a broad set of groups against which discrimination is prohibited, race discrimination has consistently been the most frequent type of claim filed with the Equal Employment Opportunity Commission (EEOC), the agency created by the act to enforce claims arising under it. In 1965, the Voting Rights Act was passed, nullifying the onerous restrictions states had put on blacks registering to vote.

The Civil Rights Act has been in existence for 40 years and significant changes have resulted, but three centuries of exclusion of blacks from virtually all aspects of mainstream society ensured that passage of the law would not immediately result in their equality. Extensive and varied research demonstrates time and again that race discrimination is still very much a part of the American landscape and still greatly affects the everyday life of blacks. Blacks still lag behind whites in the ability to access virtually every significant facet of life, from education to medical assistance; from the criminal justice system to home ownership; and from employment to receipt of bank loans.

For instance, a recent congressionally commissioned study by the Institute of Medicine found that "bias, prejudice, and stereotyping on the part of health care providers" contributes to blacks being less likely than whites to receive appropriate heart medication, coronary artery bypass surgery, and kidney transplants, as well as being more likely to receive a lower quality of basic clinical services such as intensive care. In November 2004, Alabama voters voted to keep this language in their constitution: "Separate schools shall be provided for white and colored children, and no child of either race shall be permitted to attend a school of the other race."

According to U.S. Census data, a black man with a college degree makes 30% less than a similarly situated white man, but more blacks attend college, and hold jobs, than ever before. The average black male with a master's degree earns 20% less than a white man with a master's degree, and blacks with master's degrees have a higher unemployment rate than whites with bachelor's degrees. The median income for whites is $47,800, but for blacks, $29,600. The average net worth of blacks is $6,000, compared, for whites, with an average net worth upward of $88,000. A black male with a high school diploma earns 25% less than a white male with a high school diploma. Research shows employers would rather hire a white man who had served time in prison than a black man who had not, and when given identical résumés with the only difference being the names of the applicants, employers gave 50% fewer callbacks to those with "ethnic" names such as Jamal or Lakiesha than those with traditionally white names such as Megan or Brad. In addition to visual racial profiling by law enforcement and others, researchers have found that there is also linguistic profiling, with blacks who leave messages in response to real estate ads often never receiving return calls, while whites almost always do.

A 5-year, seven-volume study from Harvard by the Russell Sage Foundation in 1999 found that "racial stereotypes and attitudes heavily influenced the labor market, with blacks landing at the very bottom." A comprehensive, 24-year Ford Foundation–funded study, results of which were published in 2002 by Alfred W. Blumrosen and Ruth G. Blumrosen, explored the public sense of reality about job discrimination and found that most people assume that intentional job discrimination either no longer exists or is the act of a few willful individuals, but this is not the case. Rather, they found that "thousands of employers have continued systematic restriction of qualified minority and female workers" (p. 1), resulting in the workers losing opportunities to develop and exercise skills and abilities that would result in better pay, with blacks still being the victims of most of the discrimination. Nearly half of white Bostonians surveyed said that blacks are less intelligent than whites and that they are harder to get along with than other ethnic groups. A 2004 Gallup poll found that 76% of whites, including 9 out of 10 less than 30 years of age, thought blacks were now being treated fairly or somewhat fairly, compared with only 38% of blacks who thought so.

The types of discrimination claims have changed over the years, with the more obvious types of racial discrimination declining, for the most part, but they still exist and tend to be more subtle. Just recently, race discrimination claims have cost several employers millions of dollars. For example, Abercrombie & Fitch settled an EEOC claim by paying $50 million for its discriminatory practice of avoiding hiring blacks and other minorities as sales staff in its stores. Supercuts settled a claim for $3.5 million for failing to hire and promote blacks and for unlawfully terminating them. Home Depot settled for $5.5 million for allowing a hostile work environment based on race, gender, and national origin. Consolidated Freightways entered into a settlement for $2.75 million for permitting a racially hostile environment, including the placement of nooses in the workplace, assaults, threats of physical violence, and racial graffiti at its workplace. Carl Buddig agreed to pay $2.5 million for excluding blacks from working at some of its plants in Illinois, and Milgard Windows agreed to pay $3.37 million for engaging in racially discriminatory hiring practices and then retaliating against the human resources employee who complained about them doing so.

Despite the intensity of the country's racial divide, race has often been a rather ambivalent issue for Americans. One of Jim Crow's staunchest supporters was the erstwhile segregationist, South Carolina Senator Strom Thurmond, who died in June 2003 at the age of 100. Six months after his death, a mixed-race woman came forward and announced that she was his daughter, the union of then 22-year-old Thurmond and her then 16-year-old mother, who worked as a maid in the Thurmond household. Thurmond had acknowledged, supported, and kept in contact with her during her life, while still fighting to protect the institution of racial segregation up to, and including, 1948, when he ran for president of the United States on a "Dixiecrat" ticket composed of Southern Democrats who opposed the softening of racial segregation laws. On the other hand, in the early

1970s, Thurmond was one of the first legislators to hire a black in his congressional office.

—Dawn D. Bennett-Alexander

See also Affirmative Action; Diversity in the Workplace; Employee Protection and Workplace Safety Legislation; Equal Opportunity; Gender Inequality and Discrimination; National Origin Discrimination

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Rand, Ayn (1905–1982)

Ayn Rand was born Alissa Zinovievna Rosenbaum in St. Petersburg, Russia. Attracted by the United States' ideals of freedom and individualism, Rand fled from the Communist U.S.S.R. in 1926. Shocked to find much of the American public unappreciative of their freedom and their country's founding values, Rand set about writing philosophical novels intended to inform and inspire a broad readership about the wonders of individualism and capitalism and the dangers of collectivism and central planning.

Her early Broadway play *Night of January 16th* and her two earlier novels *We the Living* and *Anthem* paved the way for Rand's two enormously influential works of fiction. *The Fountainhead* recounts innovative architect Howard Roark's struggle and ultimate success maintaining his individualism and integrity in a world predominantly peopled by imitators and manipulators. Rand considered her penultimate novel *Atlas Shrugged* to be the complete statement of her Objectivist philosophy. In it, the hero John Galt and other brilliant American capitalists withdraw from a crumbling, increasingly regulated economy. Without their creative force, the economy teeters on disaster. Of the more than 25 million copies of Rand's fiction and nonfiction works purchased to date, *Atlas Shrugged* accounts for more than 5 million.

Rand holds that ethics must be conceived as a logical component of a philosophical worldview. Thus, before explaining her ethical theory, she argues for metaphysical realism and for reason as humans' only epistemology. Only then does she enter the realm of ethics or how humans should conduct themselves. Following Aristotle, she believes that ethics relate to the appropriateness or goodness of humans' behavior *as humans.* Because our epistemology shows us that living things pursue life and that humans' fundamental means of survival is reason, people *should* behave rationally and develop themselves to their fullest potential. The only political system that allows humans the freedom to live and to engage one another rationally is free market capitalism. Rand, thus, offers the field of business ethics one of the strongest available arguments for free markets.

While Rand has strong opinions on the subject of rights, she is not a "rights theorist." Unlike theorists like Robert Nozick, she does not see rights as the foundation of ethics, but ethics as the foundation of rights. Ethical people will strive to build their own characters whether alone or dealing with other people; thus, they will have no rational incentive to engage in force or fraud. Only when dealing with the irrational do people need the protection of rights.

This distinction formed the basis of Rand's disagreement with Libertarianism. She saw this political position as founded on floating rights, ungrounded in broader philosophy. This divergence ultimately precipitated a rift among Rand's adherents that both broadened and deepened ongoing Objectivist research. Dr. David Kelley, by engaging in dialogue with the Libertarians, sanctioned their untenable position, according to Rand's intellectual heir, Dr. Leonard Peikoff. Therefore, Kelley was expelled from what was then the solitary Randian association, the Ayn Rand Institute, which strove to protect, promulgate, and promote Rand's original ideas. Kelley's response was to open in 1989 what is now the Objectivist Center, in Washington, D.C., a think tank working to develop, refine, and apply Objectivism. Many Libertarians now ground their political positions in Rand's Objectivist philosophy.

—Lori Verstegen Ryan

See also Egoism; Freedom and Liberty; Free Market; Individualism; Libertarianism; Meritocracy; Nozick, Robert; Self-Interest

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Rational Choice Theory

Rational choice theory (RCT) is a method of formally describing decision-making situations to explain, predict, or prescribe a course of action. (Rational choice theorists disagree among themselves over whether the theory is properly seen as descriptive and predictive or instead prescriptive.) The theory seeks to explain choice in terms of agents' beliefs and desires, assuming that agents do their best to choose courses of action that they believe will satisfy their desires. RCT is an attempt to understand people's actions as calculated reactions to the situations they face. It holds that through observing actions, we can infer people's preferences; alternatively, if we understand people's options and their preferences, we can predict or prescribe their actions.

Some Examples

A simple example will help. Imagine that the management team at ABC Corp., a publicly traded manufacturer of cell phones, faces a decision whether to license a new, patented technology (say, a novel memory chip) from XYZ Inc. or instead to develop its own memory chip using similar methods, despite the fact that doing so could arguably infringe on XYZ's patent. This is a complex decision.

In its explanatory capacity, RCT might explain ABC Corp.'s decision *not* to risk infringing XYZ's patent as a rational response to the anticipated costs and benefits of doing so. Clearly, if ABC Corp. chooses not to risk infringing the patent, it must be because managers there believe that the benefits and costs of not doing so jointly outweigh the benefits and costs of infringement. Perhaps, they see patent infringement as a very risky behavior (very likely to result in legal action by XYZ) or the likely legal penalty for patent infringement as being very important to avoid—and so they rationally choose to license the technology from XYZ Inc. instead.

In its predictive capacity, RCT might lead us to predict, prior to ABC Corp.'s choice, what managers there will in fact choose to do. The prediction made will depend on some assumptions about what the managers predict to be the costs and benefits of patent infringement. (In practice, a rational choice theorist might not make a prediction about what a specific company such as ABC Corp. will do but rather about what managers at companies facing a choice like the one faced by ABC Corp. are likely to do, on average. That would be typical of the use of RCT in modern economics.)

In its prescriptive (or normative) capacity, RCT might tell managers at ABC Corp. (or managers facing a choice like the one faced by ABC Corp.) what they *ought* to do in such a situation. So (depending on what is known about, or what assumptions are made about, the relevant costs and benefits of copyright infringement and about the company's own mission, vision, and values), the rational choice theorist might tell managers at ABC Corp. that given how much they value avoiding serious legal penalties and given how little it would cost simply to license the technology from XYZ Inc., it would be irrational to risk infringing XYZ's patent.

Rationality

Central to RCT, of course, is the idea of rationality itself. The term *rationality* is a contested one—it is used in different ways by different theories in different fields. As used by rational choice theorists, rationality simply means the capacity to evaluate options and to choose among them according to some set of criteria (normally, the agent's own values or preferences). To say that an agent is rational is simply to say that the agent has the capacity to evaluate options and to choose among them to achieve goals. The standard of rationality assumed by RCT has little, if anything, to say about the quality of agents' goals. Rationality is a property that applies to agents (an agent is called *rational* to the extent to which she or he is effective at choosing actions conducive to the achievement of her or his goals) or to agents' choices (an agent's choice is called rational if it is conducive to securing the agent's ends); but for RCT, *rationality* is not a concept that applies to an agent's preferences or goals themselves. Thus, RCT leaves it to agents to determine what their goals are; there are no irrational preferences. RCT merely assumes that agents choose according to their own goals. This leaves open whether the agent's goals and preferences are narrowly selfish, nepotistic, sympathetic, or altruistic, or aim at promoting the well-being of all humankind, and so on. So contrary to the claims of some critics of RCT, calling an agent rational does not necessarily imply either a "cold," emotionless demeanor or a narrow focus on the agent's own interests.

While RCT does not criticize agents' preferences, it does stipulate that a rational agent's *set* of preferences must have certain characteristics. These axioms are quite technical. But key ones may be stated briefly as follows. A rational agent's preferences must be

- complete (a rational agent is able to rank order any options she or he is offered: preferring one to the other, or vice versa, or being indifferent between them);
- transitive (if a rational agent likes oranges better than apples, and apples better than bananas, then she must like oranges better than bananas); and
- independent (if a rational agent is indifferent between two options, she will still be indifferent between those two options if we add some same third ingredient to each of them).

The reasons for stipulating each of these requirements are too complicated to explore here. It is enough to note that any agent whose preferences do not satisfy these axioms is simply not a *rational* agent *in the sense in which RCT is interested.*

What types of agents does RCT apply to? Traditionally, individual human agents have been the primary subject matter of RCT. Indeed, RCT is in part motivated by the idea that more complex social phenomena can be explained in terms of the net effect of the rational choices of various individual people. RCT is *reductionist* in this sense. (So, for example, upward and downward trends in financial markets can be explained by the rational responses of individuals to things such as changes in income and the price and supply of various goods.) But the application of RCT is not limited to individual human agents. In principle, the RCT framework applies to any entity that is capable of choosing from among a set of options in light of its own desires or preferences. Thus, RCT may apply to the decision-making situations faced by corporations and other organizations as well as by nation-states.

Two Main Branches of RCT

There are two main branches of RCT. One (known as "expected utility theory") deals with decisions in which a single agent chooses in response to a fixed (though not necessarily predictable) environment. Expected utility theory deals with how agents do (or should) evaluate various options, in light of available information. A simple example of such parametric decision making might involve an executive (call her Lori) deciding whether to use the final half hour prior to an important meeting to (a) go for a walk to try to clear her head or (b) prepare for the meeting (by rereading the agenda for the meeting, going over her own notes, etc.). Both activities are valuable, but she cannot do both. Let us assume that going for a walk is only 70% likely actually to clear her head. An RCT perspective on such a situation would have us calculate (at least roughly) the net value of each alternative (in terms of Lori's own objectives). An estimate of the net value of each alternative would be achieved by multiplying the chance of an outcome's occurrence by its value to Lori. So in the case at issue, it is calculated as follows:

Value of going for a walk = (value of getting to the meeting ill prepared with an unclear head × .3) + (value of getting to the meeting ill prepared but with a clear head × .7)

compared with

Value of not going for a walk = (value of being well-prepared but with an unclear head × .3) + (value of being well-prepared but with unclear head × .7).

Whichever calculation produces the highest total is the "preferred" option. Of course, we cannot complete the calculation without knowing how much Lori would value or disvalue each of the four possible outcomes (e.g., we need to know how much Lori values having a clear head at such a meeting and how important it is that she arrive prepared). But if this information were available, this procedure does in principle allow comparison of the value of each alternative.

The second branch of RCT, known as "game theory," deals with *strategic* decision making. That is, game theory is the study of rational decision making in contexts in which the eventual outcome depends on the interaction of several agents' choices. For example, imagine driving a car in a foreign country. Which side of the road should you drive on? Clearly, that depends very much on what you expect other people to do. Without some idea of what others will do, you cannot calculate the expected utility of your options. If you expect other drivers to drive on the right, you should too. If you expect others to drive on the left, then *that* is what you should do. There is no "best" answer, here, independent of our prediction of other people's behavior. (In a business context, such decisions are common: All marketing decisions, for example, are made in light of expectations of what one's competitors are likely to do.) Modern game theory has focused largely on characterizing and analyzing a number of common "games" (situations calling for strategic choice) and devising best (i.e., utility maximizing) strategies for agents to adopt in these games. The best known of these games is the famous prisoner's dilemma, a game in which individually rational choice leads to bad outcomes for all involved and which has been seen as providing a model for many modern ethical issues.

History of RCT

RCT originated as a 17th-century reaction to the skepticism of the 16th century. Notwithstanding the fact that certain belief was thought largely impossible, it was argued rational to hold beliefs, and act on those beliefs, if a relatively intelligent person would have been persuaded to do the same based on the same evidence. This claim was aimed primarily, but not exclusively, at games of chance. This school of thought was pushed toward formalism by the Enlightenment's fancy that a calculus of right reasoning could be constructed.

Earlier examinations of what constitutes "a just gamble" facilitated this focus on games of chance. Church prohibitions on gambling and usury seemed at odds with the civil law, which allowed usury, insurance, and annuities. This sparked debate about what a "just" compensation for risk taking amounted to. There was agreement that a just gamble was one where the price of playing was (roughly) equal to the expectation of reward, but the way to determine this was contested. This debate, framed in terms of expectation, made it natural for the early probability theorists examining mostly games of chance, many taken from a legal context, to talk in terms of people's expectations (a subjective measure) instead of taking a frequency interpretation of probability (an objective measure).

In the early to mid-20th century, RCT received its modern cast. Theorists focused on producing a mathematical system that would mimic the decisions of an ideal practically rational agent by relying on a precise measure of preference, namely utility. Game theory received formal treatments during this same period, being used primarily to analyze strategic (military) situations during World War II. While RCT, in general, typically treated probability as dependent on the agent's beliefs, game theory treated probability as dependent on objective facts about the world. Neither treatment is universally followed today.

Criticisms of RCT

Critics of RCT have pointed out serious problems with each of its descriptive, predictive, and prescriptive ambitions. To begin, people do not always make decisions rationally. Sometimes we choose whether to walk or take the bus based on habit, for example. The consequences of following habit look, to the outside observer, just like the consequences of deliberate choice. It would, therefore, be questionable to describe someone's walking to school as a *choice* they made based on the expected benefits of the various outcomes. One might respond that this only means that RCT should be cautious regarding what it tries to explain—it should only attempt to explain *purposeful* behavior. But even our purposeful behavior is known to not always be based on rational calculation. We often appeal to general *rules of thumb* when making decisions or only analyze *some* of the relevant costs and benefits when making decisions (e.g., ABC Corp. might not take into account the effects of patent infringement on public perceptions of the firm). Since this is sometimes the case, the ability of RCT to explain behavior is at least questionable. The degree to which people are supposed to act rationally when making important life choices is in some dispute—some theorists suppose people (and organizations) more rational than do others.

RCT has also been accused of producing few nontrivial predictions. This will not surprise those who accept that RCT is not adequate as a descriptive methodology. If RCT cannot accurately describe how we *do* make decisions, then it is reasonable to infer that it cannot predict how we will make *future* decisions.

Finally, as a prescriptive device, RCT falls prey to two distinct types of objections. If RCT is seen as making *moral* prescriptions (telling us which course of action is the ethically correct course of action), it is commonly argued that maximizing your satisfaction is hardly an appropriate basis for morality—indeed, "doing the right thing" seems to consist largely of constraining the maximal satisfaction of your preferences. If RCT is seen instead as making economic prescriptions (deciding which course of action will maximize the satisfaction of my interests), it might be thought that RCT is on solid ground. It has been argued, however, that it would be inefficient to appeal to RCT for such advice. If you think about all the possible choices and costs and benefits associated with something as simple as figuring out where to take an important client to eat tonight, you can imagine that doing that calculation itself would take you well past the dinner hour! It seems that, rationally speaking, it can be argued that a rule of thumb (such as "We always take important clients to *da Maurizio*") would be more efficient than appealing to a full rational choice theoretic analysis.

—Chris MacDonald and Chris Tucker

See also Bounded Rationality; Collective Choice; Decision-Making Models; Economic Rationality; Ethical Decision Making; Expected Utility; Game Theory; Public Choice Theory; Rationality; Rationality and Ethics; Revealed Preference; Utility; Von Neumann-Morgenstern Utility Function

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Rationality

Many things have been called rational, or irrational as the case may be, including beliefs, actions, desires, and persons. Of these, perhaps the two that have received the most attention are belief and action. Discussions about the rationality of belief fall under the domain of theoretical rationality; those concerning the rationality of action fall under practical rationality.

Theoretical Rationality

Theoretical rationality is often called "epistemic" rationality, since it is concerned with the question of obtaining knowledge. An agent can be said to know that *p* only if, apart from believing that *p* and *p* being true, he or she is able to give reasons for his or her belief that *p.* Theoretical rationality, hence, can be understood as that capacity of cognitive agents that allows them to adopt beliefs about the world on the basis of reasons. This raises at least two problems. First, what are the grounds on which a rational agent may adopt such beliefs? Second, what are the rational procedures or rules that allow her to invoke those grounds to support her belief?

The first question concerns the notion of evidence. If Jane has evidence for a belief that *p,* then this serves as a reason for her both to adopt and to defend that belief. Maybe the most obvious candidate for evidence is perceptual information—information that the agent receives about the world by means of her sensory faculties. Furthermore, in some cases Jane will be able to justify her belief that *p* long after she has obtained immediate perceptual information about *p.* In this case, she is no longer relying directly on perceptual information but on her memory thereof. The capacity to store information and access it later is of prime importance for an agent's ability to adopt and justify beliefs. Last, Jane may come to adopt a belief because she has been told that *p:* In this case, she is relying on testimonial evidence.

Perception, memory, and testimony all constitute *defeasible* grounds of evidence: The correctness of information received from any of these sources depends on the adequacy of the agent's sensory faculties, her cognitive capacities, and the external circumstances under which the information is acquired. Awareness of the contestability of evidence based on such information and the capacity to assess its quality are important aspects of an agent's rationality.

Not all evidence is concerned with the outside world, however, and evidence that is not external in this sense may not always be falsifiable. For example, rational agents can have information about their own inner states, such as being in pain, that is not subject to reasonable doubt. And some writers believe that intuitive, noninferential knowledge may be available about abstract objects, such as numbers and concepts forming the basis of mathematics and logic, which is not defeasible.

The second question—the question of the rules or rational procedures that allow a rational agent to adopt a belief on the grounds of information obtained via the above-mentioned channels—falls into the domain of logic and concerns the nature of arguments. Any logical argument consists of two or more statements, at least one of which serves as a premise that supports (or, we may also say, offers evidence for) a conclusion. There are two ways in which a conclusion can follow from a premise. If the conclusion follows with a degree of probability from the premise, then the argument is *inductive.* If the conclusion follows necessarily from the premise, it is a *deductive* argument. Most arguments, including scientific ones, rely on inductive inference. On the other hand, according to the traditional view, logic and mathematics proceed deductively. The foundationalist would argue about mathematics that mathematical reasoning is based on intuitively obvious axioms from which theorems can be deduced that are true once and for all. This conception has come under threat in the 20th century from an argument by Kurt Gödel. In his famous incompleteness theorems, he shows that for a large class of important axiomatic theories, such as number theory, mathematical reasoning cannot deduce all mathematical statements that are true relative to that system and cannot even show that the system is internally consistent. Furthermore, according to the "quasi empiricism" of Hilary Putnam and Imre Lakatos, mathematical knowledge is similar to empirical knowledge in possessing a hypothetical status. Mathematical theories are then fallible, and they are arrived at not by means of formal proofs but in accordance with inductive methods of inquiry similar to those employed in the empirical sciences.

In his *Enquiry Concerning Human Understanding*, David Hume pointed out a problem with inductive knowledge. He argued that any inductive inference from true premises to a general conclusion relies on a further hidden premise—namely, that the world in the future will be relevantly similar to the world as it is when the inference is made (that nature is uniform). But the uniformity of nature cannot be presupposed and hence must be justified. The problem is that any such justification can only proceed inductively itself. Hence, Hume concluded that inductive inferences are circular. It follows that one cannot inductively obtain knowledge of those parts of the external world about which one does not have perceptual information.

The problem does not end here. Hume argued that since the idea of necessity cannot be derived from the observation of individual sequences of events, it turns out not to be possible to justify causal necessity on empirical grounds. Yet it is not possible to justify causal judgments a priori (i.e., prior to any experience) either, for it is impossible to tell how objects have behaved prior to having observed them. Hence, causal necessity can only be explained reductively in terms of constant conjunction—a relation between two events in which one invariably accompanies the other.

Immanuel Kant thought that Hume's argument, if sound, undermined not only natural science (and thus a core domain of theoretical reason) but also metaphysics, the philosophical discipline that investigates the general structure of reality. He responded by trying to show that there is a class of judgments that can be made a priori but that are nevertheless "synthetic" (i.e., revealing genuinely new information). Examples of such judgments can be found, for example, in geometry: "The angles of a triangle always add up to 180 degrees" is a judgment that is known a priori yet cannot be deduced from an analysis of the concept of triangle (judgments that can be deduced from the analysis of a concept are called "analytic"). Kant's project in the *Critique of Pure Reason* is to explain the possibility of this kind of judgment. He approaches it by arguing that there are features of experience that the mind bestows on objects and these are hence not supplied by the external world. Since metaphysics is concerned with the question of what these features are, it cannot proceed on the basis of empirical evidence, that is, inductively. The question whether Kant's response to Hume's empiricism is viable has been raised forcefully in the 20th century by W. V. O. Quine's argument that no distinction between analytic and synthetic judgments can be drawn.

Practical Rationality

Practical rationality is concerned with an agent's capacity to choose from among different courses of action. It does not attempt to give an account of our knowledge of the world, but focuses on the reasons and ways of thinking that lead us to choose to do some actions and not others. Thus, a main task for theorists of practical rationality is to give an account of the exact role reason plays in action. There have been many such accounts, but for purposes of this entry we will divide them into two rough categories: those that maintain that reason's role is entirely or almost entirely confined to devising the means necessary to achieve the goals or ends of action and those that argue that the role of reason in action is much larger than simply devising the means to ends.

Writers who argue that reason is confined to working out means to ends typically endorse or have been heavily influenced by David Hume's understanding of practical rationality. According to Hume, the job of reason in action is to choose means to ends that are themselves neither discovered nor sanctioned by reason, but given by desires or passions, as he put it. Reason can devise means to satisfy desires, but since desires are neither true nor false, they are not subject to rational assessment. Furthermore, reason can assess neither which of our desires we should pursue nor the order in which we should pursue them. Consequently, Hume claimed, it is not contrary to reason to pursue goals that we realize are not in our best interests, and may even be detrimental to our interests. For Hume, reason is a mere instrument used to serve ends that are set by desire and only by desire.

Many contemporary theorists of practical rationality accept Hume's idea that our desires and goals are not subject to rational assessment but argue that reason has a role to play in selecting the order in which we ought to pursue them. This approach contends that the basic task of practical reason is to discover means that optimally advance an agent's ends, whatever they might be, and that an agent acts rationally to the extent that he or she undertakes such optimizing actions. The procedure for this, as developed with considerable mathematical precision in decision theory and the theory of rational choice, is first to propose a measure for agents to rank their goals from most to least desirable. This measure gives the "utility" of each goal. The utility of each goal is then multiplied by the agent's estimate of the probability that the goal will be achieved given the means contemplated to attain the goal, and the products are added together to get the expected utility of each action. The rational thing to do, then, is to select the action that has the highest expected utility. Thus, agents can use reason to determine which available actions maximize the satisfaction of desire and, hence, how desires can be pursued efficiently. Note that if the proposed measure of the utility of desires applies to all agents, it may be possible to discover which social policies have the highest expected utility and so guide social as well as individual choice.

Opposed to the Humean view are writers who argue that reason is not a mere instrument in the service of desire but has a much more complicated role in choosing action. There are two main strands of the non-Humean understanding of reason's role in action. The first is that reason is not purely instrumental since it has the dual role of identifying the objective ends of human life and guiding action to achieve those ends. For example, Aristotle argued that there is a good for man that is both knowable by reason and the proper goal of human action. Thus, for Aristotle, and for many writers since Aristotle, reason is not the servant of desire but is an instrument for achieving ends that are to a large extent revealed and endorsed by reason itself.

The second non-Humean strand of practical rationality claims that what makes an action rational is at least in part that it conforms to rules for action that are independent of the agent's ends and do not necessarily advance those ends. According to this position, a rational agent is one who, in circumstances in which the rules are applicable, chooses to act by the rules. There are different accounts of this rule-based conception of rational action depending on what one takes to be the source of the rules. One is that the rules are widely accepted social norms about what is or is not a socially acceptable action. For example, most of us stop at a red light even when the road is clear and no police are in sight because of the social norm that prohibits running the light, regardless of the immediate benefits of doing so. This sort of norm-based reasoning is a familiar part of ordinary life. However, there is a major controversy about how far it can be extended and, in particular, whether it can be extended to cover ethical reasoning.

Those who argue that it does apply to ethical reasoning often accept some type of ethical relativism.

In its simplest form, ethical relativism is the view that what is good to do, or what is ethically proper or right to do, is regulated by socially accepted ethical norms. For example, in societies where there is a social norm against having multiple spouses, it is ethically wrong to have more than one spouse. In societies where there is no such norm, it is not ethically wrong. That is all there is to it, and, at its core, reasoning using social norms to guide action is all there is to ethics.

On the other hand, many writers who reject ethical relativism maintain that ethical reasoning is based on norms that are in principle available to all agents. The most influential version of this position was developed by Immanuel Kant. Kant argued that practical reason should not be based on social norms that arise in different societies from arbitrary historical processes but on rational principles known by rational means, and thus in principle accessible to all rational agents regardless of their cultural affiliations. Kant claimed to have found such a principle, which he called the "categorical imperative." The basic idea here is that unless you can suppose that everyone in similar circumstances could wish to do what you now propose to do, you should not do it. This, Kant believed, is a requirement of reason itself, and reason dictates that it be followed by all rational beings regardless of the consequences.

It is a matter of continuing debate whether Kant's defense of the categorical imperative as a principle of pure practical reason is successful. However, Kant's views about practical reason have inspired contemporary philosophers and social theorists, such as John Rawls and Jürgen Habermas, to propose theories that make essential use of the notion that rational agreement can be based on principles that everyone can accept.

Practical Reason and Social Responsibility

It is not self-evident how the various conceptions of rationality introduced here bear on real-life ethical questions, in business environments or elsewhere. One reason is that it is not clear whether there exists a necessary connection between rationality and ethics. On Kant's account of practical rationality, it is rationally required to act morally and, thus, always irrational to act immorally. This is a consequence of his view that moral requirements flow from the universalizable principles of reason itself. However, on Hume's account, it is entirely possible to be completely rational in accomplishing goals that are immoral. For Hume, reason is confined to devising means to satisfy our desires, and there is no assurance that our desires match up with what is morally acceptable.

But even if we take it that the employment of one's rational faculties leads to morally worthy actions, it does not follow that a rational agent will always be in a position to resolve real-life ethical problems. The complexity of such problems, in business and other contexts, typically defies standardized solutions. The most that can be hoped for is that an agent's familiarity with theories of practical rationality might enable him to better understand the nature and scope of the problems at stake. Unfortunately, perhaps the most obvious difficulty here is that sometimes business interests and ethical concerns follow different such theories and may hence not always be compatible.

Empirical Issues Concerning Theoretical and Practical Reasoning

In recent times, the human capacity for both theoretical and practical reasoning has come under intense scrutiny from the natural and the social sciences. Psychologists have pointed out that intelligent agents frequently commit significant errors when making intuitive judgments about physics, arithmetic, and probabilities. Cognitive scientists have produced evidence that poses problems for the classical philosophical view of rationality as radically disjoint from an agent's emotive faculties. The ideally rational agent, according to this view, bases his or her actions on conclusions that are obtained through rational inferences alone. Any emotive interference makes the agent less than fully rational. It has been observed, however, that an impairment of an agent's emotive skills (through a brain injury, say) can result in a diminished capacity for theoretical and practical reasoning. How exactly philosophers might respond to these challenges is not currently obvious.

—Axel Seemann and Robert Frederick

See also Deontological Ethical Systems; Economic Rationality; Economics and Ethics; Ethical Decision Making; Expected Utility; Hume, David; Kant, Immanuel; Kantian Ethics; Moral Reasoning; Rational Choice Theory; Rationality and Ethics; Utilitarianism

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RATIONALITY AND ETHICS

The word *logos* was used in Greek philosophy to refer to rationality. *Logos* was adopted by the Romans as *ratio*, which became *rationality* in English. Rationality, like ethics, is considered a uniquely human characteristic, a characteristic that distinguishes humans from other life-forms. Aristotle used *logos* to describe humans as rational animals, animals that are capable of knowing in the cognitive and moral sense. This Aristotelean notion of the interdependency between rationality and ethics is a characteristic broadly accepted in classical Greek philosophy.

In Roman and medieval times, rationality was associated with religious thought and belief. This association was severed during the Renaissance and the Enlightenment, when the relationship between ethics and religion was questioned. As a consequence, rationality became the characteristic of autonomous persons who possessed the capacity to develop their own morality because of their capacity to be rational and were in no need of external authority or imposed values.

In addition to the focus on the individual during the Enlightenment, rationality became associated with scientific method and gave birth to the rationalist school of thought. This school of thought claims that knowledge and truth are based on reason, not on external sources or value judgments. Rationality then became associated with utility in value-free science. This development led to scientific rationality, which is based on positivism, the perspective that perceives value judgments as incapable of being rational, and rational judgments as those that relate to utility.

Rationality underwent radical transformations in its journey through history. From the coexistence of rationality and ethics during the classical Greek period, rationality became the source of morality during the Enlightenment. More recently, rationality is generally associated with utility and efficiency rather than ethics.

Types of Rationality

Rationality is generally distinguished as being theoretical or practical. Theoretical rationality is associated with beliefs and knowledge, while practical rationality is associated with intentions and behavior about what is the good thing to do. Practical rationality provides the explanation and justification for behavior.

Alastair MacIntyre explains three main positions on practical rationality. The first is based on acting for one's self-interest. Action in this perspective is based on the calculation of costs and benefits of different alternatives. The second position of rationality is based on the capacity to act impartially toward your own interests but in accordance with the constraints accepted by any rational person. This view makes rationality a standard that can provide a benchmark for human behavior. The third view sees rationality as the capacity to act in ways that bring out the inherent goodness of human beings.

Ethical Theories and Rationality

The three main schools of thought of ethics are deontological or duty based, teleological or consequence based, and virtue ethics. Deontological and teleological ethics contend that ethics is a function of rationality. Virtue ethics, without eradicating the importance of rationality, contends that ethics is primarily concerned with the cultivation of character, and it emphasizes individual virtue and integrity. The character disposes the person to act ethically, so what is important is to develop a strong character. The cultivation of character is important, according to virtue ethics, and happens before the rationalization of actions and the formulation of principles.

Teleological ethics is based on the notion that moral behavior is not intrinsically valuable. The value of moral behavior is determined by its consequences, which can be ascertained through rationality. Rationality provides the ability to know what is good by assessing possible consequences and selecting the one that provides the greatest net benefit. The ability to know what one should do, therefore, depends on rationality.

Immanuel Kant, the most influential representative of deontology, is considered the founding father of the ethics of rationality and the modern conception of rationality. Kant wanted to separate ethics from religion and developed ethics as a consequence of human rational ability. For Kant, rationality and autonomy are related since persons are rational when they follow the laws they are able to make for themselves. Rationality makes persons autonomous because it places the authority for moral decisions on the person and not on any external authority such as the law, religion, or society's traditions. Autonomous rational agents are, according to Kant, ends in themselves and not means because they can author the laws they are bound by, deserving respect and having dignity.

Rationality, for Kant, provides the categorical imperative of morality, the fundamental principle of ethics that prescribes the duties required for moral behavior. The fundamental principle of ethics, which is provided by rationality, requires that what counts as a reason for one person also counts as a reason for everyone else in the same situation. When applied to practice, reason provides the ground of morality in the first formulation of the categorical imperative: So act on that maxim that it can be willed to be a universal law. Thus morality is founded on rational laws rather than emotions, desires, or even religion. The categorical imperative, like the principles of mathematics, is discovered a priori through thinking and not through experience or emotion.

Since the rules of morality are rational, they are the same for all rational beings. In addition, since rational human beings discover the rules of morality autonomously, they are bound by these rules of morality because they are self-legislated, are discovered through thinking, and are not imposed from an external authority.

Kant developed a morality based on rationality. Only an autonomous being can determine its actions in accordance with its reasons for acting, and only such a being can be a moral agent. Autonomous moral agents develop ethical values and standards and are responsible for their behavior.

Other Perspectives of Rationality and Ethics

The Enlightenment relied on rationality to resolve ethical issues. Hume and Rousseau, unlike Kant, sought to oppose the notion that rationality is able to guide human life. For Hume, a rational man is a man who is suffering from a psychological disorder. Hume sees moral judgments as an outcome of moral sentiments rather than rationality. Reason, according to Hume, is a slave to passion, not the other way around, because reason cannot move one to act, while passion can.

Rational self-interest is used by David Gauthier to justify morality. Gauthier adopts a contractarian approach to morality and justifies morality in terms of instrumental rationality. He argues that the justification for morality must be independent from it, that is, morality needs to offer reasons for action, not merely an explanation of action. Rationality provides constraints on individuals' self-interest, and these constraints are the moral principles.

There is another view that positions ethics as prior to rationality, not a consequence of rationality. Emmanuel Levinas, a postmodern philosopher, sees ethics as an outcome of responsibility. This responsibility is born not of the capacity of people to be rational but rather from the existence of other people. The encounter with other people creates the demand for responsibility, thus making responsibility and ethics the outcomes of the existence of persons. Similarly, Bauman, after Levinas, argues that morality does not have a purpose and it is nonrational. Morality, according to Bauman, is an impulse, unpredictable and unregulated.

Business, Ethics, and Rationality

Rational today is a term that has diverse meanings. Generally, rationality requires consciousness, competence, consistency, and awareness. Rational is also the effective and efficient or widely accepted and shared. In economics, rational is associated with optimal. It is related to goal achievement in a value-free context without examining the ethics of the means and the ends of the goal achievement process.

Rationality occupies a central position in management theory and practice. Management and organizational theory relies on rationality to achieve not only effectiveness and efficiency but also morality. Instrumental rationality, for example, the rationality most often employed in business, is the process of finding the means to achieve predetermined ends, without concern for the ethics of such goals.

Business adopted the notion of instrumental rationality as an adequate measure of human nature from other social sciences, especially economics. This understanding of rationality has been used in business to develop theories and models of human behavior. More specifically, the "rational economic man" has been imported from economics to develop human nature in management. The rational economic man has been criticized because the assumptions of its construction are immoral and do not reflect the reality of human existence. Work on heuristics and biases bounded rationality, and satisficing emphasized the inadequacy of the assumption of rationality in business.

Ethics and rationality are examined in business ethics at the individual and organizational levels of analysis. At the individual level, rationality and ethics are examined in terms of personal ethical values, ethical decision making, and ethical behavior at work. Rationality and ethics at the organizational level are also receiving increased attention through the corporate social responsibility and stakeholder theories. The view that ethical behavior is reduced to economic rationality is the classical perspective of corporate social responsibility. More contemporary perspectives of ethics in business see business activity as including responsibilities not only economic and legal but also ethical.

The issue of organizational rationality is also connected with the issue of the ontology of the organization. An ongoing debate sees the organization as a person, a property, and as a partial moral person. This debate has implications for the ethical behavior of both persons and organizations.

People's rationality in the business realm is affected by specialization and the division of labor, the establishment of standard practices, objectives, communication channels, and training, and the indoctrination of members with knowledge, skill, and loyalties. The organization also affects the locus of choice on decision making and shapes what a person perceives as rational at any given moment.

—Eva E. Tsahuridu

See also Bounded Rationality; Deontological Ethical Systems; Kantian Ethics; Rational Choice Theory; Rationality; Utilitarianism; Virtue Ethics

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Rawls, John (1921–2002)

John Rawls, an American philosopher who held the position of Professor of Philosophy at Harvard University, is widely considered to be the most important political philosopher of the latter part of the 20th century. His highly influential writings have contributed greatly to the shaping of contemporary political thought. He began his philosophic career in the context of a cultural climate permeated by the assumptions of utilitarianism with its understanding of individuals as merely means to a goal of general social well-being. A strong advocate of the liberal political tradition, he argued for a political philosophy that, unlike utilitarianism, stresses issues of justice and individual rights.

In his most important work, *A Theory of Justice,* published in 1971, Rawls sought procedures that embodied the moral ideal of justice and put forth his fundamental insight that every individual has an inviolability rooted in justice that cannot be overridden even for the welfare of society as a whole. Basing his political theory on the idea of justice as fairness, he postulated a hypothetical or original position, in which free, equal, and rational individuals devoid of any social attributes, particular ends, or attachments might agree on principles of social cooperation. These individuals deliberate from a basis of self-interested rationality and do so within a veil of ignorance that shields them from morally irrelevant knowledge such as social status or wealth. By insuring impartiality, Rawls concludes that all parties involved would place a high priority on basic liberties, for they would not want to risk a loss of freedom in whatever segment of society they may find themselves. Second, they would choose distribution of fundamental goods that allowed for inequalities only when such inequalities would raise the level of the least well-off. The principles for this social contract result from rational insights, and what results is a temporal, rationally constructed frame or social contract imposed on the contingencies of real-life existence. Social structure is in some sense postulated in abstract principles, and social reasoning is by and large the application of the rule to the particular case.

In *Political Liberalism,* Rawls keeps the key tenets of *A Theory of Justice* but emphasizes that all modern societies have diverse views on basic issues of value, the significance of life, and the relation of these to belief in God. Thus, he concludes that liberal political principles must be acceptable to a wide range of viewpoints. In *Justice as Fairness: A Restatement,* Rawls again holds fast to his core ideas, but formation of the fundamental principles through intuitions is modified to the position that there is a certain ideal implied—that of Western liberal democracies—and the basic values of the agent, now called citizen, are not derived from fundamental intuitions but from an overlapping consensus, thus allowing for more pluralism. Whether one agrees or disagrees with Rawls's position, his work has been, and will continue to be, a powerful impetus for political, social, and philosophical debates, and its scope is unmatched in recent times.

—Sandra B. Rosenthal

See also Kant, Immanuel; Liberalism; Nozick, Robert; Rawls's Theory of Justice; Utilitarianism

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Rawls's Theory of Justice

A Theory of Justice

In *A Theory of Justice* Rawls argues that the primary task of social and political institutions is the preservation and enhancement of social justice, which he understands to include both principles of individual liberty and principles of well-being or welfare. Rawls tries to develop a procedure called the original position that would yield principles of justice. These principles of justice would then serve as guides in the construction and evaluation of social and political institutions.

Rawls does not view people as naive moralists searching for a utopian ideal. Rather, they are sufficiently self-interested to wish to pursue their own individual interests or those of their families and loved ones. Given inevitably competing interests and conflicts, Rawls attempts to provide a procedure that will enable the members of the society to adopt principles for resolving conflicts and for adopting just practices and institutions.

Rawls appeals to a procedural process in the social contract tradition. Rawls's contract is not an actual contract made in history but rather a thought experiment or hypothetical state called the original position.

Persons in the original position are governed by certain constraints both moral and psychological.

One of the key constraints is the adoption of the veil of ignorance, or the ignorance principle. The ignorance principle states that the contract makers are to act as if they did not know their place in society. Such ignorance guarantees impartiality and prevents us from arguing on selfish rather than general grounds. The veil of ignorance would exclude knowledge of one's class position or social status (including the probability of occupying any position or having any specific degree of status), one's fortune in the distribution of natural assets and abilities, one's intelligence, one's physical strength, the nature of one's society, and one's individual conception of good and other values. Operating in this way, none of the contract makers would have any special interests to defend, nor would they have any reasons to form alliances to adopt principles that work to the disadvantage of a minority of other contract makers.

For example, suppose the issue were the distribution of income. Since the veil of ignorance prevents you from knowing how wealthy you are or will be, and it prevents you from knowing your occupation and talents, what strategy would be rational for you to adopt? Surely, Rawls argues, you would want to protect the position of the least well-off. Since the contract makers are rational egoists operating from behind a veil of ignorance, they would adopt the general principle of seeking to minimize their losses. Since they are ignorant of the probability of any specific outcome, they would guard against the worst possible outcomes by making the people in the worst-off position as well-off as possible.

We can now see how unanimous agreement on the principles of justice is possible. Since everyone agrees that it is rational to reduce one's losses and since no one knows what position he or she holds in society, the following two principles would be adopted unanimously: (1) Each person is to have an equal right to the most extensive total system of equal basic liberties compatible with a similar system of liberty for all; and (2) social and economic inequalities are to be arranged so that they are both (a) to the greatest benefit of the least advantaged and (b) attached to offices and positions that are open to all under conditions of fair equality of opportunity.

Some elaboration on these two principles is required. What are the constituent liberties that make up the total system of liberty? Rawls answers this question by providing a list of basic liberties. The list includes political liberty (the right to vote and to be eligible for public office) together with freedom of speech and assembly; liberty of conscience and freedom of thought; freedom of the person along with the right to hold (personal) property; and freedom from arbitrary arrest and seizure as defined by the concept of the rule of law. These are the traditional liberties found in liberal democracies.

The second principle is concerned with the primary goods of opportunities and power, income and wealth. What Rawls does is consider his principle in contrast to several competing ones and then ask which principle would be chosen by self-interested persons constrained by the veil of ignorance. Rawls first considers the principle of natural liberty. In the system of natural liberty, positions are open to those able and willing to strive for them. This is the liberty found in competitive markets.

Rawls argues that this principle of natural liberty would be rejected. If after the initial distribution, someone had vastly more wealth than others, nothing could be done to correct the situation. Moreover, the distribution of wealth at any given time has been strongly influenced by the cumulative effect of the natural and social contingencies of past distributions. Accident, past injustice, and good fortune play an important role in determining who is wealthy at any given time. Since the veil of ignorance prevents us from knowing our own fortune, rational contractors would seek to avoid the risk of turning out to be at the bottom in a society governed by natural liberty.

Rawls has more positive reactions to the principle of equal opportunity. This principle asserts that people with the same abilities, talents, and expenditures of effort should have roughly the same prospects for success in given fields of endeavor. One's family background, race, religion, sex, or social background should not act as an impediment to success. To assure equality of opportunity, society should impose heavy inheritance taxes, offer a broad public education, and pass antidiscrimination legislation. To the extent that such social measures are successful, the distribution of goods and services depends on ability, talent, and effort.

However, in Rawls's view, the principle of equal opportunity is still not sufficient as an adequate principle of justice. He argues that the distribution of talent, ability, and capacity for effort is just as arbitrary from the moral point of view as the distribution of sex, family wealth, and social class. A person has no greater right to more wealth because he is smart than because he is of a certain religion.

In part, Rawls seems to be claiming that behind the veil of ignorance, it would be no more rational to gamble on being smart, talented, or dedicated than on being a member of a dominant group, so we would reason conservatively and try to protect ourselves against bad outcomes. However, he also seems to appeal to our considered ideas about fairness. Distribution is fair, in Rawls's view, only if assets are treated as collective social goods. After all, none of us deserves to have been born into favorable circumstances or with personal traits such as a disposition to work hard. These are gifts distributed at birth as if by a natural lottery and are not earned by us as individuals. Moreover, the distribution of goods and services is a cooperative effort on the part of all. Given the cooperative effort and the morally arbitrary distribution of natural assets and favorable family circumstances, the fairest principle is the one that accepts inequalities only if the inequalities work to the advantage of the least well-off.

When fully spelled out, the Rawlsian argument is that the two principles of justice are justified because they alone would emerge from a fair procedure of rational choice. The procedure itself is warranted because of its coherence with our most firmly held considered judgments about justice and fairness. Finally, Rawls maintains that a society in which the political, social, and economic institutions were constructed in conformity with the principles of justice would be a highly stable one. The citizens of such a society would recognize that the society is basically just and, thus, would desire to act as the principles of justice require. These citizens would also be inclined to support society's basic institutions. In this way, such a society would be well-ordered and stable.

Criticism

Critical reaction to *A Theory of Justice* came from those on the political right and the political left. Libertarians and others who supported capitalist economic institutions thought that Rawls's theory sacrificed liberty for greater equality. Those on the left thought that Rawls conceded too much to the self-interested side of human nature. Those on the left thought that Rawls overemphasized the inequalities that were necessary to provide incentives to the more talented. Moreover, even if such incentives were required, that did not make them just.

The criticism of Rawls that has had the most impact is that it is biased in favor of liberal individualistic Western values and so cannot succeed as a universal theory for all. In part, this criticism is directed to Rawls's theory of the good. In the original position, Rawls rules out any knowledge of what each of us considers to be the good life. Rather, our knowledge of our desires is limited to what Rawls calls primary goods. Primary goods are goods such as rights and liberties, powers and opportunities, wealth and income that every rational person should want since these goods are necessary for achieving any other goods. By limiting our knowledge of the good in this way, Rawls can argue that no one would choose a society where the pursuit of one nonprimary good prevailed at the expense of all the others. For example, no one would choose a society where religious persecution was practiced since behind the veil one does not know if one is in the majority religion or not.

But critics point out that this stipulation is biased against individuals who hold alternative theories of justice in which one value, such as the predominance of a religion, or a limited set of values is given preeminence. Rawls's refusal to rank particular perceptions of the good implies a very marked tolerance for individual inclination.

Another way of putting this point is to say that Rawls has not shown that being neutral with respect to various theories of the good is itself a neutral decision. Thus, Rawls's theory reflects a built-in liberal individualistic assumption that is undefended in the theory.

Political Liberalism

Over a 20-year period, Rawls reflected on criticisms like these and published a response, *Political Liberalism.* In this book, Rawls agrees with his critics that his theory applies only to liberal democratic societies. Toleration and stability are central themes of *Political Liberalism.* In it, Rawls holds fast to his belief that modern liberal democracies are characterized by intense competition among different, often conflicting, theories of the good. How can people who hold these competing conceptions get along? This is a profound question in the first decade of the 21st century.

To answer this question, Rawls distinguishes between a *modus vivendi* and an *overlapping consensus.* A modus vivendi occurs when people agree to grudgingly accept one another rather than fight. A tense stalemate is better than the Hobbesian war of all against all. However, a modus vivendi is inherently unstable since it will tend to break down.

An overlapping consensus exists where there is agreement on certain principles for carrying on a debate and for making decisions in the political realm. True to his procedural inclinations, Rawls believes that people with competing conceptions of the good can nonetheless accept certain common political ground rules. In that way, we have an overlapping consensus on these ground rules rather than an unstable agreement of convenience.

To achieve this consensus on ground rules, there must be some kind of limit on conceptions of the good that can be tolerated, such as allowing for the exclusion of those who have no wish to get along with others and actively seek to eliminate those with different religious beliefs. Imposition of a conception of the good through coercion is not just. Rawls believes that such people do not have reasonable conceptions of the good.

To develop this concept of a reasonable account of the good, Rawls provides a normative characterization of citizenship in a democratic society. Citizens in a democratic society are committed to the use of evidence and to procedural rules for settling debates rather than, say, divine revelation, not available to other citizens or confirmable by public tests. In addition, a citizen should respect the reasonable conceptions of the good that other citizens might have, even when these conceptions are inconsistent with his or her own comprehensive view of the good. Citizens in a just democracy are appropriately tolerant of the reasonable positions of others.

Rawls's account of the reasonable imposes additional requirements on the citizens in a just democracy. Citizens must be willing to let political values have priority over other values in public life. Political values are those that govern the basic structure of social life and are constituted largely by the principles that Rawls developed in *A Theory of Justice:* equal political liberty, fair equality of opportunity, economic reciprocity presumably implemented through the difference principle, and the social bases of mutual respect among citizens. To these principles, Rawls adds the value of public reason as explained above. Rawls believes that any person with a reasonable conception of the good will accept these political values and their priority.

But why should these political values and principles be given priority? Because only in this way is an overlapping consensus possible. And it is the overlapping consensus that makes a liberal democracy and social justice possible. Rawls's theory is a theory of reasonable pluralism.

To a large extent, citizens in the United States have accepted something like Rawls's reasonable pluralism. Thus, when authorities in Afghanistan threatened to execute a citizen who had converted to Christianity from the Muslim faith, there were cries of outrage. To prevent a citizen from changing his or her religion on pain of death is a violation of liberal justice.

The Law of Peoples

In his last book, *The Law of Peoples,* Rawls extends the theory of justice developed in *Political Liberalism* to "the principles and norms of international law and practice." This was an important move since a number of Rawlsians had done this on their own and, in fact, had not captured what would turn out to be Rawls's view. Rawls deliberately avoids providing principles for the just state because he wants his law of the peoples to act as a constraint on some of the traditional prerogatives of nation-states. Moreover, just peoples treat other just peoples who have different comprehensive doctrines of the good as equals and worthy of respect. Nation-states do not adopt this attitude.

Rawls distinguishes among five kinds of people, two of whom, the peoples of liberal democracies and decent governments, can be subject to the law of the peoples. Decent people differ from the people in a liberal democracy because there is a hierarchy in the society and, thus, not all citizens are equal. However, to qualify as decent, these people must meet a number of moral conditions, including the acceptance of human rights.

The law of the people will result from a second original position that has many, but not all, characteristics of the original position in *A Theory of Justice.* Part of the law of the people is constituted by eight traditional principles of justice. These principles include, but are not limited to, principles to honor human rights, to observe treaties, to accept restrictions in the conduct of war, and to assist people who live in situations that prevent them from having a just or decent political regime. These principles constitute the basic charter of the law of the peoples. Rawls believes that his law of the peoples represents a realistic utopia and that liberal and decent societies would accept the law of the peoples. Thus, there would be a reasonable pluralism rather than a modus vivendi among liberal and decent peoples.

These peoples have the right to defend themselves against outlaw states—against states that support terrorism, for example. To what extent outlaw states should be tolerated is a central issue of the foreign policy of liberal states. As the international community grapples with terrorism, outlaw states, and indeed any state that denies basic human rights and thus would not qualify as decent peoples, Rawls's theory of justice faces a practical challenge. What should liberal and decent peoples do in such circumstances?

The Influence of Rawls on Political Economy and Business Ethics

On the publication of *A Theory of Justice,* Rawls was invited to address the American Economic Association. Several economists have tried to show how Rawls's theory was consistent with certain utilitarian theories of maximization in economics. In his discussion of the "Institutions of Distributive Justice," Rawls was heavily indebted to public finance theory, especially that of Musgrave. *A Theory of Justice* is considered a classic of political economy as well as a classic of political philosophy.

There is no major work in business ethics that can be called exclusively Rawlsian. Nonetheless, many business ethicists working from the contract, Kantian, or stakeholder perspective include Rawlsian elements in their theorizing and practical applications of ethical theory to business ethics dilemmas.

—Norman E. Bowie

See also Fairness; Justice, Distributive; Justice, Theories of; Liberalism; Political Theory; Procedural Justice: Philosophical Perspectives; Rawls, John

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Reasonable Person Standard

The reasonable person standard is a test used to define the legal duty to protect one's own interest and that of others. The standard requires one to act with the same degree of care, knowledge, experience, fair-mindedness, and awareness of the law that the community would expect of a hypothetical reasonable person. The standard is objective in that it compares one's behavior with that expected of a "reasonable person," without regard to one's intention or state of mind. The reasonable person standard plays a key role in negligence law, where behavior falling below the standard triggers liability. The reasonable person standard also appears in contract law, criminal law, civil rights law, and elsewhere.

The reasonable person standard has roots in the development of the concept of negligence in common law. The purpose behind the reasonable person standard is the public good. The legal use of the standard clarifies behavioral expectations that allow people to work, plan, and get along together. Similar terms include *reasonable man*, *reasonably prudent person*, and *ordinarily prudent man*. Related terms include *standard of care*, *reasonable care*, *due care*, and *ordinary care*, as well as *reasonable bystander* and *reasonable third party*. In the United States, the "prudent person rule" or the "Prudent Investor Act" operates in fiduciary relationships.

Although the reasonable person standard is well-established, the meaning of "reasonable" is a topic of legal and philosophical debate. In recent years, the standard has been criticized as tainted by the biases of dominant groups.

How the Reasonable Person Standard Works

The degree of caution and prudence used by a reasonable person when doing an activity that could foreseeably harm others is called the "standard of care." The standard of care varies with different actors and circumstances, allowing courts to apply the reasonable person standard flexibly to a wide assortment of cases.

Special Groups

Professionals and tradespersons are judged by the standard of care for their profession or trade. For example, if someone goes bankrupt as a result of following the advice of an accountant, a court of law would ask whether an accountant facing the same circumstances, with the knowledge available at the time the advice was given, would have considered the advice reasonable. Professional licensing requirements, industry safety standards, and similar benchmarks help define the standards of care for trades and professions. However, some circumstances require going beyond the usual requirements to meet the reasonable person standard. Expert testimony is often used to define reasonable behavior for tradespersons and professionals.

People with disabilities are judged according to the behavior expected of a reasonable person with similar disabilities, and the disability is considered as one of the circumstances in the case. For example, if a person with impaired vision drove a car and caused an accident, a court would ask whether a reasonable person with a similar impairment would drive a car. Mental deficiencies are excluded from the circumstances for the purposes of applying the reasonable person standard. Mental deficiencies are considered too easily faked, and their impact on one's duty is considered too difficult to determine.

Minors are judged according to what a reasonable minor of the same age, intelligence, and experience would do in similar circumstances. Rules involving negligence on the part of minors vary from one jurisdiction to another. Case law has determined that a minor engaging in an adult activity, such as driving a car, should be held to an adult standard of care.

People who lack experience in an everyday activity are held to the same standard of care as those with more experience. For example, a teenager who has just earned a driver's license is held to the same standard of care as an experienced driver.

The Role of Circumstances

The reasonable person standard uses different standards of care for different circumstances. For example, a trucker hauling bottled water would be held to a lower standard of care than would a trucker hauling toxic chemicals, since a spill of toxic chemicals would create more danger of harm. People facing emergencies might reasonably behave differently than people in ordinary circumstances. Accordingly, the reasonable person standard asks how a reasonable person would handle an emergency similar to the case in question.

Relationship to Customs and Laws

Following the customs of one's community or occupational group can serve as evidence in favor of one's having met the reasonable person standard. Typically, courts hesitate to label customs as negligence and, thereby, require a large group of people to change their behavior. However, special circumstances can require going beyond custom. For example, it might be customary in a quiet neighborhood to let children ride their bikes in the street. But if a strange dog were loose in that neighborhood, reasonably careful babysitters would be expected to call the children in and perhaps phone the local animal control agency. Conversely, acting contrary to community or occupational group customs could serve as evidence of failing to use an appropriate standard of care.

Compliance with or a failure to comply with federal, state, or local laws may count as evidence in determining whether one has met the reasonable person standard. Meeting the minimum requirements of a law could still constitute negligence if the reasonable person in similar circumstances would have exercised greater care than the law required.

The Reasonable Person Standard in Civil Rights Law

The reasonable person standard operates in civil rights law to help define workplace harassment. In 1986, sexual harassment came to be considered a violation of Title VII of the U.S. Civil Rights Act of 1964. Under Equal Employment Opportunity Commission guidelines, a civil rights violation called "hostile workplace environment" harassment occurs when an employee is regularly subjected to sexually offensive speech, behavior, or materials. An ongoing pattern of offensive conduct is generally necessary to show that a hostile workplace environment exists.

In the 1993 case of *Harris v. Forklift Systems,* U.S. Supreme Court Justice Sandra Day O'Connor developed a twofold test for hostile workplace environment harassment: (1) Is the conduct so severe that a reasonable person would find the environment objectively threatening or abusive? and (2) Does the employee perceive the environment as threatening or abusive?

In the context of hostile workplace environment law, some legal theorists and several courts came to view the reasonable person standard as enshrining the biases of white males. These critics replaced the reasonable person standard with a "reasonable woman" or "reasonable victim" standard. These alternative standards encouraged juries to consider experiences that could lead to a perception of harassment that might not be obvious from a white or male perspective. The alternatives themselves were then criticized as impractical or unfair. Most courts that tried the alternative standards have returned to consistently using the reasonable person standard.

Related Terms

The Reasonable Bystander

In common-law contract theory, a standard called the "reasonable bystander" or "reasonable third party" is used when one party denies having entered a legally binding agreement. If a reasonable bystander observing the parties' outward conduct would have inferred a serious intention to form an agreement, the contract is considered binding. Also, when the terms of a contract are misstated, the erring party can void the contract if the mistake is clear to a reasonable bystander.

The Prudent Person Rule

In a few states, a standard called the Prudent Person Rule requires fiduciaries to invest trusted assets as a prudent person would invest their own assets. The prudent person is expected to take into account factors such as the needs of beneficiaries, the need to preserve the estate, and the desired income. The Prudent Person Rule rests on common law stemming from the 1830 Massachusetts case of *Harvard College v. Armory.* Most states have replaced the Prudent Person Rule with all or part of the Uniform Prudent Investor Act (UPIA). The American Law Institute adopted the UPIA in 1990 in the Third Restatement of the Law of Trusts. The UPIA reflects modern portfolio theory. For example, diversification is required, and individual investments are evaluated in light of the portfolio as a whole. Both the Prudent Person Rule and the UPIA seek to protect clients from shady investments and undue risk taking.

Defining "Reasonable"

What kind of behavior qualifies a person as "reasonable"? Legal experts give a variety of answers, including

- doing cost-benefit analysis and taking care that benefits justify their costs;
- treating others with respect (this interpretation roughly resembles the moral theory of Immanuel Kant: The reasonable person treats others as ends in themselves and not only as means; the principles underlying the reasonable person's actions could be willed as universal laws); and
- acting in accordance with moral and intellectual virtues, such as temperance and wisdom (this interpretation draws on Aristotle's moral theory).

Questions about the meaning of "reasonable person" lack easy answers. Which definition best fits the way the reasonable person standard is actually used? Which meaning best fits commonly accepted ideas from sociology, psychology, and moral philosophy? Does—and should—"reasonable person" have the same meaning across different areas of law? And if the standard requires economic cost-benefit analysis, how can anyone rightly calculate the cost of negligent loss of life?

—David P. Schmidt

See also Cost-Benefit Analysis; Fiduciary Duty; Negligence; Prudence; Prudent Investor Rule; Sexual Harassment

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Recalls, Voluntary

Consumer product recalls occur frequently. In 2000, there were at least 2,523 voluntary recalls. Recalls publicize product dangers and request that consumers return the defective product for repair or replacement. In fact, the recall is a specific type of communication campaign full of ethical considerations. Federal regulatory agencies involved with recalls include the Food and Drug Administration, with 1,915 recalls in 2000, and the National Highway Traffic Safety Administration and Consumer Product Safety Commission, with similar totals of 227 and 207 recalls in 2000, respectively. There were 76 U.S. Department of Agriculture recalls in 2000, 32 at the Environmental Protection Agency and 23 at the U.S. Coast Guard.

Ethical Issues in Recalls

Recalls raise a number of ethical questions. There are about a dozen specific recall ethics issues. Ethics must be considered a primary factor in recall campaigns and the ad hoc American recall system.

The Decision to Recall

An initial ethics issue involves the corporate decision to recall a product. Are such decisions made out of a sense of corporate social responsibility or out of fear of facing a recall order from a regulatory agency? Most recalls are probably motivated not by ethical values and beliefs but by fear of the consequences of not recalling.

Recalls were originally intended as remedies only when public safety was at stake. However, there have been recent cases of recalls of tabloid magazines because they contained illegally taken photographs of Jennifer Aniston and Brad Pitt at a nude beach and a recall of T-shirts because they were considered obscene.

Silent Recalls

Silent recalls, as the title implies, are not generally publicized. In some cases, there is no communication at all. This seemingly incongruous situation results from corporate fear of strongly worded recall warning communication. Manufacturers sometimes convince regulators to avoid publicity in lieu of relying on "internal" communication between manufacturers, distributors, and retailers.

Silent recalls are not uncommon. Between 1995 and 1997, 15 of 51 U.S. Department of Agriculture recalls were not publicized. Instead, the Department accepted a recall plan relying exclusively on intercorporate communication. The ethical adequacy of recalls without any public communication is questionable.

The Duty to Recall

Court decisions have consistently recognized a corporate duty to recall, but that duty has always been quite limited. Recalls are a corporate duty only when there is a widespread severe public safety threat. Does limited legal duty imply a limited ethical responsibility? In the late 1980s and throughout the 1990s, there was a trend away from court-ordered recalls. However, failure to voluntarily recall or comply with regulatory recall requests might result in product liability litigation exposure.

Are Voluntary Recalls Really Voluntary?

The American recall system appears to be one thing but is actually another, in a sense. According to recall legislation, virtually all recalls are called voluntary, unless a court order is required. However, these voluntary recalls only occur after significant regulatory pressure. Is it unethical to refer to recalls as being voluntary when in fact they are not?

Political Interference With Recalls

The recalling regulatory agencies are subject to political influence. They are part of the executive branch of the government and respond to political pressure. There has been typically less recall activity during Republican administrations.

Politics plays another role in the recall system. For instance, child product manufacturer Graco donated substantial sums to 15 political candidates after the recall of its Converta-Cradle in 1972. The result was legislation limiting corporate recall liability.

Product Registration

There is an ethical irony about corporate resistance to product registration legislation. Such laws would make recalls much easier, but manufacturers and retailers argue that this data collection would be time-consuming and costly. They also express concerns over consumer privacy rights.

These reservations, nevertheless, do not stop much corporate information gathering now. These data are used by corporations to cross-market other products to consumers. In addition, these customer lists are frequently sold to other marketers.

Indirect Recall Costs

In addition to the direct costs of a recall, recalling firms suffer other consequences, as well. These indirect costs include reduced sales for the recaller and its competition, stock devaluation, gross national product reduction, and reduced public confidence in the recaller's industry.

Recalls can drive firms out of business. In light of these terrible effects, recalls appear to be ethically justified only in extreme cases.

Antirecall Lobbying

A substantial amount of antirecall lobbying is conducted by trade associations representing manufacturers or retailers. Proposals for corporate product registration at the 1999 Consumer Product Safety Commission Forum on Improving Recalls drew criticism from manufacturers, retailers, and trade associations. Is it ethical for firms to try to minimize their social responsibility by lobbying?

The U.S. Department of Agriculture sought recall powers through the Food Safety Enforcement Enhancement Act of 1990. In opposition were the National Meat Association, the National Food Processors Association, the Beef Industry Food Safety Council, the American Meat Institute, and the National Broiler Council, among others.

Corporations Mislead Government Regulators

Lying is generally considered unethical. Yet that is what happens sometimes in recall situations. It is believed that the Food and Drug Administration has been repeatedly intentionally misled by medical product manufacturers.

Corporations Resist Recalls

Despite legal and ethical obligations, firms frequently resist regulatory recall recommendations. In the 1970s, Firestone refused to recall its "Firestone 500" tires and tried to block the National Highway Traffic Safety Administration investigation. Similarly, General Motors declined to recall 1.1 million cars with brake problems in the 1970s and 1980s. The American distributor of Royal Line Salmon wouldn't participate in a recall of *listeria*-infected product in the 1990s.

We can quantify the result of Firestone's resistance to recall. Thirty-four people died, and there were 14,000 consumer reports of defective tires, which caused hundreds of accidents.

Cost-Benefit Analysis

Recalls can be a matter of life and death to consumers. The use of cost-benefit analysis to make recall decisions is ethically questionable, especially when the tacit corporate calculation of the value of human life is so low.

At least 500 consumers, and as many as 900, were killed in the Ford Pinto in the 1960s and 1970s. The part needed to avert the danger cost $11 per vehicle. General Motors sold 9 million pickup trucks and made $10 billion in profit during the 1990s. A gas tank defect resulted in 1,600 deaths, yet an expenditure of merely $8.59 per vehicle would have made the trucks safe.

Corporations Fail to Report Product Dangers

Despite laws requiring immediate notification, some firms fail to inform regulatory agencies of recall situations. The Food and Drug Administration is often kept in the dark.

The National Highway Traffic Safety Administration receives much recall information, but the largest recalls are typically not reported to the agency by auto manufacturers. Similarly, many manufacturers failed to mention product defects to the Consumer Product Safety Commission, necessitating 1990 amendments to the original Consumer Product Safety Commission Act.

—Dirk C. Gibson

See also Consumer Product Safety Commission; Cost-Benefit Analysis; Duty; Environmental Protection Agency (EPA); Firestone Tires; Ford Pinto; National Highway Traffic Safety Administration (NHTSA); Regulation and Regulatory Agencies; Trade Associations; Tylenol Tampering; U.S. Food and Drug Administration (FDA)

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Reciprocal Altruism

Rooted in evolutionary biology and multi-iteration game theory, reciprocal altruism is a cooperative strategy in which someone chooses to perform an act that incurs an immediate net personal cost to benefit another individual in the hope of reaping a future gain. In biological terms, it represents a willingness to forego one's own reproductive chances in favor of another's chances for the overall benefit of the group. This goes beyond a form of altruism dictated by kin selection in that the short-term selfless behavior is extended to organisms that do not necessarily share a common ancestry. In an evolutionary sense, it seems as though a behavior that imposes a greater net cost on one individual for the sake of an unrelated person would be selected out. On the contrary, natural selection—the mechanism of evolution—will favor this kind of self-denying behavior under certain conditions. Reciprocal altruism is hardwired in our psyches and is responsible for encouraging a range of cooperative social interactions, including business exchanges.

In an economic sense, the evolution of the willingness to cooperate with others was critical to the formation of market transactions in modern society. Thus, the fact that reciprocally altruistic behavior has evolved to include members outside one's own clan has enabled social contracts to form among strangers in business contexts. Humans have developed the ability to share tasks with members of other groups in response to adaptive challenges to perform tasks that could be accomplished neither alone nor by members of a single familial group. The concept of reciprocal altruism is important for business because it is a necessary antecedent to our social institutions and division of labor within organizations. Economic relationships in our global marketplace today are facilitated by the biological and psychological propensity to engage in mutually trusting relationships with unfamiliar others.

These intergroup relationships are highly dependent on the existence of trust. Without trust as a bond for exchanges between strangers, a market system could never develop. While trust between partners can be cultivated over repeated just and fair transactions, various social institutions serve to solidify this bond. For groups to form spontaneously, a degree of reciprocal moral obligation must be present. In some cultures, this impulse still occurs primarily among kin. But in other cultures, this sense of moral duty to reciprocate does spread to nonkin. High-trust societies, such as the United States and Japan, are characteristically open to mutually beneficial relationships among strangers. There is a general moral obligation in Japan for workers employed by a particular firm not to seek higher wages and better employment elsewhere. In return, the employer provides lifetime job security.

Reciprocal altruism assumes that humans are social beings, not governed entirely by rational self-interest. For kin, one-time altruistic behaviors that jeopardize the survival of the provider without the hope of reciprocity make sense because the genes are passed down the lineage. For nonkin, these isolated acts of altruism make little sense in the short term. For reciprocal altruism to evolve as a trait in humans, certain conditions must be present. Only if there is a probability of repeated encounters between the altruist and the beneficiary, resulting in a chance that the altruistic behavior will be reciprocated in some way, would natural selection favor the trait. Social beings establish cooperative relationships with other nonkin individuals out of expectation of future gain.

The biologist Robert Trivers is widely considered the authority on the theory of reciprocal altruism. His work described conditions under which reciprocally altruistic behavior evolved and indicated the design features of the human mind that are necessary for this type of altruism to become advantageous in an evolutionary context. Trivers cites an example involving a drowning man who has a 50% chance of drowning. A stranger has the opportunity to rescue the man with a 50% likelihood that both will die in the attempt. If this were a one-time encounter between the two men, it certainly would not pay for the rescuer to attempt to save the drowning man. Trivers posits that if there is a chance the rescued man will reciprocate that behavior at a later time, then both parties have a chance to benefit from the altruistic act.

To regulate altruistic behavior, Trivers identifies certain characteristics that must have evolved in the brain. In social exchange, individuals must be able to detect and punish cheaters who accept a benefit without reciprocating. Psychological mechanisms have evolved that help people determine which contracting partners do not pay a cost in return for the altruistic behavior. For altruism to evolve, Trivers postulated that the cost must be comparatively small to the bearer and that contact between recipient and provider should be frequent. Otherwise, the fitness costs to the altruist would have been too great for the trait to proliferate in the population. Individuals are less likely to contract with a person who does not reciprocate at least an equal later survival benefit.

Norms of justice and fairness may have formed out of the need to regulate altruism. When benefits are taken by an individual in a social contract relationship but no benefit is bestowed in return, an injustice has occurred for the altruistic party. Human brains have developed the ability to regulate unfair behavior by eliminating future contact with the cheating individual. Throughout evolutionary history, our ancestors found it desirable to foster friendships based on trust with nonkin individuals and to avoid opportunistic relationships. Sentiments that draw people toward altruistic individuals tend to influence the monitoring of social exchange relationships.

Evolutionary game theorists devised a mathematical model to illustrate how cooperative behavior may have evolved in our species. A widely cited game in economics and evolutionary biology is the prisoner's dilemma (PD), in which individuals are assumed to behave in a rationally self-interested manner. The PD tests what strategies people use to distribute particular costs and benefits. It demonstrates that people generally do not choose a strategy of selfishness.

In a single-iteration game, people would rarely have the motivation to cooperate with one another. Cheating on others in exchanges would always benefit a selfish person when players do not have an opportunity to interact in future exchanges. Only in multiple-iterative games does a cooperative social contract evolve over time. In repeated exchanges, cheaters are punished by not having the opportunity to form alliances with others in the future, since no one will contract with them again.

Kinship is not responsible for cooperation in this type of situation. Rather, a contracting party's *history of cooperative behavior* is paramount. Robert Axelrod, who proposed the prisoner's dilemma, coined the phrase *the shadow of the future* to describe this phenomenon—the probability of future interactions with a contracting partner. If a contracting individual has a history of cooperating in past exchanges, then the likelihood of future engagements with that individual increases. Thus, the reputation for trustworthy behavior of individuals in multi-iteration games is critical for determining cooperative encounters down the road. As is often seen in business, reputation spreads through various communication channels. Feedback about adherence to social contracts between parties will affect the reputation of individuals and organizations alike. For business organizations, reputation affects share value. Once the scandals at Enron were exposed to the public, a sharp and perilous drop in the share price of the company followed.

Computer modelers have attempted to devise strategies for participants in multiround games. The most famous strategy, tit for tat, describes the process of reciprocity in nature and provides insight into how cooperative behavior among selfish beings could have evolved through time. Tit for tat mimics the behavior of the other player in the two-person, multiround game. If one person cooperated, the partner would cooperate, but the partner would cheat if he or she observed the other person cheating. The evolutionarily stable strategy is the one that spreads through the population and dominates behavior. In the computer models, tit for tat—the strategy that resembles Trivers's reciprocal altruism—was the only approach that grew in the population. This suggests that proper management of stakeholder relationships in organizations through honoring cooperative, fair agreements will reinforce the norm of reciprocal altruism, thereby enhancing prospects for gain in both economic and social welfare.

—David M. Wasieleski

See also Altruism; Evolutionary Psychology; Game Theory; Justice, Distributive; Justice, Theories of; Social Contract Theory

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RECIPROCITY

Reciprocity is a pattern of mutually contingent exchange of gratifications, or tit for tat. Reciprocity can be shown to be one of the universal aspects of moral codes all around the world and has been argued to be the key for social stability. Reciprocal social mores range from mutual gift exchange to rules of hospitality. As a normative concept, reciprocity typically focuses on an individual's or an organization's return of fitting and proportional benefits for benefits bestowed by others. The return of harm for harm (which we usually call "retribution") tends to be a more controversial aspect of reciprocity. In addition, it is important to note that, because its core element is an exchange, reciprocity is not synonymous with the Golden Rule: Do unto others as you would have them do unto you.

Sociologists, game theorists, and evolutionary psychologists have provided evidence of the evolutionary advantages of tit-for-tat strategies in difficult-to-resolve situations, such as the prisoner's dilemma. Norms of reciprocity, grounded in enlightened self-interest, do not require the invocation of benevolence, or an active concern for the welfare of others, to justify virtues such as truth telling or cooperation. What is more controversial than the cultural universality of the norm of reciprocity and its importance for the evolution of cooperation is the moral question of whether one owes favors in return for involuntary prior favors. For this reason and a few other problems (e.g., the concrete meaning of "fitting," "proportional," or "equivalent" returns of favors), reciprocity has been endorsed a bit more warily by ethicists than by social scientists.

As for organizational behavior and theory, Bowie's and a few other ethicists' formulations of corporate social responsibility have shown it to be grounded in norms of reciprocity as well. According to this conceptualization, a company is a moral community in which stakeholders both create and are bound by the rules that govern their social relations. In turn, these relationships are reciprocal; that is, when one party in business dealings infuses the relationship with moral capital, it creates reciprocal duties on the other stakeholders. The definition of corporate responsibility would be too narrow if it focused only on the obligations of the firm. Other stakeholders also have rights and duties. For example, a company may owe its employees loyalty and fair employment practices, but a similar obligation (of loyalty) falls on employees in return. Similarly, we cannot stop environmental pollution by focusing on the emissions reduction of companies exclusively; customers must also do their part to create a demand for environmentally safe or conscious products. According to Bowie, what is needed is a comprehensive theory for determining the appropriate reciprocal duties that exist among corporate stakeholders. Because of the fact of moral pluralism, such a theory will most likely have to be quite complex and sophisticated.

—Marc Orlitzky

See also Altruism; Benevolence and Beneficence; Corporate Social Responsibility (CSR) and Corporate Social Performance (CSP); Evolutionary Psychology; Fairness; Game Theory; Golden Rule, The; Justice, Compensatory; Justice, Retributive; Justice, Theories of; Motives and Self-Interest; Prisoner's Dilemma; Rational Choice Theory; Rationality; Rationality and Ethics; Reciprocal Altruism; Self-Interest

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RECYCLING

Recycling is a three-part series of activities, to recover, reprocess, and reuse materials that are considered "waste," thus reducing their burden on the environment. These materials come from household use, industrial processes, commerce, and agriculture; they typically include glass, paper, wood, aluminum cans, metal scrap, some plastics, and various organic materials. Through a variety of processes, waste materials are recovered and reprocessed to become substitutes for raw materials obtained from natural resources (such as petroleum, minerals, trees, and soil).

Besides economizing on the use of natural resources, recycling can help reduce quantities of solid waste sent to landfills and can reduce pollution caused by waste disposal: Incineration consumes energy and creates air pollution; landfills contaminate water and also create air contamination. These financial and environmental benefits also translate into social benefits: improved quality of life and a means for achieving sustainability (ensuring that future generations have access to comparable air, water, and natural resources that we enjoy presently).

Recovering value from so-called waste requires *motivation, innovation,* and *marketing. Motivation* often begins with the necessity to save money by not discarding used materials or by substituting reprocessed materials for expensive natural resources. Education and refinement of consumer values also contribute to motivation, as do government-sponsored financial rebates or requirements.

For example, in 1998, an executive order from the president of the United States required that all federal agencies use paper composed of 30% postconsumer fiber. This practice later resulted in a 13% reduction of solid waste material requiring disposal. The California Redemption Value (CRV) for aluminum cans increased from 2 to 4 cents in January 2004, resulting in the collection of an additional 680 million cans. Part of motivation is to provide information, so that consumers and businesses understand what products can be recycled, how to prepare them, and how to transport them to processing stations.

Innovation requires rethinking of procedures (such as instituting curbside pickup of used consumer materials) and manufacturing processes (such as reprocessing newspaper and paper waste to create new paper products or reclaiming wastewater from raising flowers and using it to irrigate another flower crop). Two major areas of recycling operations are internal and external. Internal recycling is the reuse in a manufacturing process of materials that become a waste product of that process. Throughout the life cycle of a product—the extraction of its raw materials, transportation, processing, and manufacturing—waste is generated. But this waste can be salvaged. External recycling is the reclaiming of materials from a product that has been used, such as the widespread use today of refurbished ink cartridges for printers or the transformation of used tires into safer playground equipment, groundcover, and park benches and tables.

Once materials have been reprocessed, *marketing* enables businesses and consumers to know that the recycled content materials are available for use. Marketing can help build commitment to purchase these recycled products. Only then, with purchase and use of these reprocessed materials, can the process of recycling be considered complete. "Green marketing" had a rough start in the early 1970s, primarily because some products advertised as good for the environment performed poorly or because some advertising was deceptive. But as time passed, "green" products improved, and with the U.S. Environmental Protection Agency (EPA) giving consumers new confidence through its Energy Star label, consumers began to respond to marketing of products that are good for the environment, including recycled goods. As Roper's "Green Gauge" Report of 2002 notes, 56% of Americans would do more for the environment if they only knew how. Marketing can help consumers understand which products are recycled or recyclable and why buying them helps the environment.

The United States, as of 2004, attained 28% recycling of consumer goods—a rate that had almost doubled since 1990. Much of this progress has resulted from increasingly stringent environmental rules from federal and local government that have restricted solid waste incineration and landfill options. Success rates for recycling are further improved when coupled with behavioral adjustments that result in reducing needs and reusing products before they enter the recycling process (hence the slogan "Reduce. Reuse. Recycle.").

While Americans are recycling more, they are also generating more waste than any other nation. According to the U.S. EPA, during the past 35 years (from 1970 to 2005), each American has nearly doubled the waste generated every day: from 2.7 to 4.4 pounds per day. The most effective way to halt this trend is through preventing waste. Waste prevention is also known as "source reduction": any change in the design, manufacture, purchase, or use of materials to reduce their amount or toxicity before becoming part of municipal solid waste.

Here is where business can make a vital contribution, because it is in the design, manufacture, and distribution of products that so much waste is created. More large corporations seek increased efficiency in the use of petroleum products and natural resources; cost savings from reduced use have motivated further innovation. Businesses of all sizes have recognized the marketing value in reducing waste and use of materials; consumers increasingly make buying decisions based on perceived corporate social responsibility, so businesses find value in publicizing their proenvironmental practices such as recycling.

The European Union (EU) has demonstrated an even stronger commitment to recycling than the United States. In the 1990s, the EU required that all member states meet a target of 25% to 45% for recycling waste in 1998. The target for 2008 is to recover 60% to 75% of waste. In 2002, the EU created a directive for treating waste electrical and electronic equipment (WEEE) that encourages and sets criteria for the collection, treatment, recycling, and recovery of electrical and electronic waste; it affects any business that manufactures, brands, imports, sells, stores, treats, or dismantles electrical or electronic products within the EU. Since August 2005, a new and important component of this directive is "producer responsibility" to take back used electronic products after consumer use.

The value of recycling has been challenged by antigovernmental, procapitalist critics—most notably Bjorn Lomborg, author of *The Skeptical Environmentalist.* He notes that some resources, such as metals, cannot be completely recovered due to losses through corrosion. Also, some products are unable to be reconstructed, so all the constituents cannot be recycled. Initial efforts in the United States, sometimes, were quite costly and inefficient—collection costs of materials to recycle were often two to four times the costs of simply dumping those materials into a landfill.

However, verifiable economic and environmental improvements resulting from more efficient recycling indicate that these practices will be continued. According to the Bureau of International Recycling, use of secondary materials results in major savings of energy and reduced pollution. For example, use of recycled paper provides a 64% energy savings when compared with use of primary ("raw") materials, 35% less water pollution, and 74% less air pollution. In October 1995, the Chicago Board of Trade began its Recyclables Exchange for the trading of used materials such as glass, polyethylene, and used paper products. This effort marked recognition of recycled materials as legitimate commodities and helped combat large price fluctuations in the recycling industry. In addition, as an industry, recycling produces jobs and promotes technical innovation.

—LeeAnne G. Kryder

See also Consumerism; Developing World; Environmental Colonialism; Environmentalism; Environmental Protection Legislation and Regulation; Sustainability

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Redistribution of Wealth

The phrase *redistribution of wealth* commonly refers to government policies that are intended to increase the income or benefits of poor people using money raised by general taxation of the rich, the prosperous, and the middle classes. Sometimes the debate is limited only to the redistribution of income, but generally any policy intended to benefit the poor, whether in the form of income or services, can be considered an attempt to redistribute the wealth. The ethical debate about redistribution is usually framed as a conflict between egalitarian proponents of redistribution, who claim that society has a collective moral responsibility to look after the poor, and libertarian critics, who see such transfers as an unethical violation of the property rights of those who pay the taxes.

Social classes vary greatly in different countries. This affects the redistribution debate as the current distribution determines the extent and type of poverty and wealth. The debate is sometimes framed in terms of the origin of people's incomes such that the rich are those with substantial investment income, the middle class are those with sufficient salary or wage income to be above the poverty line, and the poor have insufficient income of any sort or depend on government or charity. However, much of the debate, especially with respect to developed countries, uses deciles and quintiles (dividing the population by income into 10 or 5 groups, respectively) for convenience. Generally, the rich are the top 10%, the prosperous the rest of the top 20%, the middle class is the middle 60%, and the poor are the bottom 20% (or sometimes the bottom 10%).

Although the redistribution debate is primarily about government programs that intend to benefit the poor, there are many other government programs that redistribute wealth to the middle class and even to the rich. For example, those prosperous enough to have investments benefit most directly from government subsidies, bailouts (especially of hedge funds), and corporate tax exemptions. Old-age security, government support for postsecondary education, and even road budgets greatly benefit middle-class people.

Government programs that are targeted specifically toward the poor, often referred to as "social welfare programs," are specifically meant to have a redistributive effect. It is the ethics of these programs that are usually addressed in discussions of redistributing wealth. The key ethical positions in this debate are libertarianism, egalitarianism, objections against the extremes of poverty or wealth, and efficiency.

The libertarian argument is that social welfare programs are unethical because they involve taxing some people solely for the purpose of giving the money to others. This violates taxpayers' rights to their property and income. The libertarian position can also be defended on the grounds that it promotes freedom, minimizes government power, supports the morality of free markets, and rewards virtues such as hard work, ambition, skills, and risk taking (at least in those societies in which wealth does not come from crime and corruption).

Libertarianism can be criticized for its assumption that current property ownership and income are morally just. Libertarians morally privilege the current distribution of wealth, often without giving adequate justification. Furthermore, libertarianism assumes that all income should be private and that there should be no social income from community ownership of natural resources, taxes on social capital, or other sources. In defense of libertarians, they are often consistent in that they oppose not only social welfare programs but also all other government programs except security and defense.

The word *egalitarian* is used both for those who believe there should be equal or near equal distribution of wealth or income and for those who believe that the extremes of great wealth and poverty should be avoided. Egalitarians who advocate complete equality of wealth or income usually base their argument on the fundamental moral assumption that economic equality is inherently just and that it is unethical for some people to have a lot more private property than others. The defenders of this position place more ethical value on equality than they do on property rights, and they believe that redistributing the wealth is the only way to achieve a just society. Arguments against egalitarianism are that economic equality kills incentives and destroys productivity; that it is unfair to those who produce more through hard work, skills, and risk taking; and that it requires a totalitarian state to constantly redistribute the wealth.

Some egalitarian arguments in favor of redistribution concern only the extremes—the very poor and the very rich. Humanitarians argue that allowing preventable poverty and destitution is inherently unethical and a violation of basic human rights. The government ought to provide a safety net below which no one is allowed to fall. At the other extreme, some argue that there should be limits on great concentrations of wealth. If people are too wealthy, they can disrupt free markets, such as the Hunt brothers disrupting the world silver market. Large concentrations of wealth can also corrupt democratic political processes.

Extremes of great wealth, especially if it is inherited, raise the ethical problem of a leisure class which makes no contribution to society but which lives in luxury. This is especially an ethical problem if the wealthy class originally obtained its wealth by means now thought immoral, such as British landowners whose family wealth originates from enclosures, clearances, or the slave trade.

Ethically, the efficiency models of wealth redistribution are forms of utilitarianism; they rest on the belief that if redistribution helps society overall, then redistribution is morally justified. One efficiency argument rests on the claim that economic growth (as well as other desirable social characteristics, such as democracy, rule of law, and stability) is mostly driven by the middle class and that the government should therefore redistribute the wealth to achieve a large and thriving middle class. The middle class, it is argued, drives domestic investment, innovation, and anti-corruption campaigns, while the poor are a drag on the economy, and the rich support corruption, special interests, and capital flight. The economic growth argument for redistribution seems to be mainly applicable to developing countries; in developed countries that already have a large middle class, the argument mainly concerns the preservation of that class.

Another efficiency argument concerns security and social stability. Poverty causes crime (especially violent crime), so social welfare programs may be cheaper than police, courts, prisons, private security, and the losses from crime. However, this assumes that social welfare programs are an efficient way to cure poverty, a claim which some people question. Similarly, poverty causes ill health, and ill health is expensive and increases taxes even if public health care extends only to the very ill and seniors.

Objections to efficiency arguments include claims that promoting the general social good can never justify injustices to individuals, including violations of their property rights; that governments do not have the knowledge, wisdom, or impartiality to promote economic efficiency through redistribution; and that the negative effect of redistribution on incentives to work, save, and invest outweigh any efficiency gains from greater equality. Many people also argue that government programs intended to help the poor do not always have the intended result.

Although a government's policy on redistribution is likely to affect business, it is difficult to determine in the abstract what that impact is likely to be. If a government avoids redistribution policies, the impact would depend on the current distribution. If the current distribution has extremes of poverty and great wealth, business may have to deal with violence, crime, and social instability on one side, and capital flight on the other. If current distribution is more even, a favorable climate for business may exist. The impact of redistribution from the well-off to the poor may have various effects on business. Consumer markets may expand as poor people are able to increase their consumption. Savings may decline. Investment may decline with savings or increase with consumption—it is hard to say. It is equally hard to say how labor availability and incentives would be affected. Any disincentive for the poor to work may be offset by the poor being able to afford day care, transportation, work clothes, training, and (in developing countries) enough calories to have the energy to work more. The poor may become more capable of work.

Businesses may also be affected if they have to pay higher taxes for the government to finance redistribution. The impact would depend on whether their competitive situation allows businesses to pass on the tax cost in higher prices or lower costs or whether they are faced with declining retained earnings or profits. Governments need to consider the impact on business carefully, since business is a vital part of the economic system that generates the wealth that is redistributed.

A person's opinion on the ethics of redistributing wealth mostly depends on his or her basic values. Those who highly value property rights and freedom from government interference will take a libertarian stand against redistribution. Egalitarians who think social justice requires economic equality favor redistribution. Humanitarians will object to preventable poverty and destitution but may not favor redistribution beyond a social safety net. People who live in countries with an extremely wealthy inherited upper class may question its moral acceptability. Utilitarians will give weight to efficiency arguments, but the conclusions they draw will depend on their views on the effect of redistribution on economic growth, and on economic data on the relative costs of health care, security, and welfare.

—John Douglas Bishop

See also Egalitarianism; Income Distribution; Justice, Distributive; Libertarianism; Nozick's Theory of Justice; Property and Property Rights; Rawls's Theory of Justice; Regressive Tax; Utilitarianism

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Reductionism

Reductionism is the endeavor of understanding any object of inquiry, such as physical objects, situations, phenomena, explanations, theories, concepts, language, and so forth, by specifying the elements that constitute it. Whenever one level or domain or whole is analyzed as nothing more than another, it is said to be reduced to that other. The whole does not impart meaning to its parts, but rather, the parts are the meaning of the whole. The study of anything must be the study of its parts.

Reductionism can be said to trace back to the Middle Ages with the development of nominalism, which was committed to the reduction of collectives to their constituent elements. However, the full strength and significance of the method of reductionism developed along with the development of Newtonian physics, which incorporated the process of understanding the object of inquiry by analyzing its constituent elements. Newtonian physics depicts the universe as composed of discrete particles operating mechanistically and deterministically according to the universal laws of motion, gravity, and so forth.

But while science takes no position concerning the status of the object that it analyzes, the term *reductionism* implies a philosophical outlook that finds the ultimate meaning of any object to lie not in its inherent qualities as a whole but in the parts that compose it. This position identifies knowledge in general with the findings of science and mathematics and the method of gaining knowledge in general with the procedures of rational analysis used in Newtonian physics. The implicit assumption of this worldview is that physics is the metaphysics of nature. What mathematical physics and physiology find is what, and only what, is truly real and truly knowable, and what we experience is reducible to the procedures and contents of math and science.

This reductionist point of view has implications for the understanding of the scientific method itself, leading to a strong antitheoretical bent. According to this view, scientific investigation does not penetrate nature in a way the senses cannot, but rather, scientific investigation is the rigorous, economical organization of what is given to us in experience. And since, at its extreme, it is held that what we have in experience are not objects "out there" but sensations, the goal of scientific investigation becomes that of discovering relations between sensations. The construction of theoretical entities is useful in science, but these are not getting at some transphenomenal realities. Rather, they are learning devices or models, psychological aids for organizing our sensations.

As theoretical concepts lost their significance, the focus on theoretical entities was replaced by a focus on the structure of empirical concepts and their logical ordering. Science becomes understood as a hypothetico-deductive system, and scientific theory is understood as an axiomatic structure, similar to a logical or geometrical ordering. On this view, a theory is nothing but a logical ordering of the relations between observed phenomena. The question as to why or how theories could have predictive power concerning future experiences is ignored or considered irrelevant. The reductionist framework is not concerned with the dynamics of science, with theory formation and theory growth, or with predictive power, but with the logical formalization of accepted theory, which is, ultimately, the formalization of experienced phenomena and their relations. Within science, the term *reductionism* is sometimes used to refer to the view that all special sciences, such as biology, psychology, chemistry, and so forth, are reducible ultimately to the fundamental laws of physics, a claim which is also termed the unity of science.

Reductionism virtually destroys the meaningful wholes associated with our traditional understanding of humans and the world in which they live. For example, religion is reducible to some nonreligious origin, such as the human psyche, human drives, or brain constitution. Human action as purposive or goal-oriented activity by which we relate to the meaningful world in which we live is reduced to neurophysiological behavior, with humans becoming nothing more than the object as studied by various disciplines such as physiology, neurology, anatomy, behavioral psychology, and so forth. Human values that direct action and the course of cultural development become identified with physiological or psychological drives and needs. Mental activity is reduced to biological or computational functions; mental phenomena are nothing more than neurophysiological functions. Human freedom is but a myth, with human actions governed by the laws of physiology, and with enough information, human actions could be predicted. At its extreme, physical objects themselves become nothing more than experienced sensations in our brain. In sum, the concrete fullness of humans and the qualitatively rich, value-laden, goal-oriented contexts in which they have their being are all ultimately identical with, or reducible to, the systems of mathematical physics and physiology, a position which, in its various forms, falls under the generic label of scientific reductionism. Such reductionism embodies a fact/value distinction in which values are ultimately reducible to facts.

The application of the model of Newtonian physics to the social sciences, in particular, has led to some of the worst abuses of reductionist thinking. Reductionism has been used by modern social science in elaborating the frameworks of new fields of study and academic disciplines and has been highly influential in the manner in which the social sciences and business ethics have developed. In business ethics, reductionism has led away from a normative value-laden approach to an empirical explanatory, descriptive, and/or predictive approach concerned with empirical facts. The empirical approach focuses on identifying definable and measurable factors within the individual psyches and social contexts that influence individual and organizational ethical behavior.

The opposite of reductionism is relational holism, an approach to the phenomenon being described that views the whole as having a significance that is on a different level than, is irreducible to, and is not explainable in terms of parts. Instead it views the whole as an emergent relational complex. This position is sometimes called emergentism, the view that the properties of the more complex level are unique emergents that are lost when reduced back to parts whose interactions give rise to them. For example, for the reductionist, water is nothing but hydrogen and oxygen, while the emergentist holds that the unique qualities of wetness, thirst-quenching ability, bouyancy, and so forth, are emergent relational properties of the whole that are as real as, but on a different level from, the hydrogen and oxygen whose interaction gives rise to them, and these real emergent properties are lost when water is reduced to nothing more than the sum of its parts.

The concept of emergent relational complexes gains support from the "new science" of quantum physics and systems thinking, which illustrates the role of emergent properties within the context of relational systems. This view has important implications for business ethics, for it undercuts the fact-value distinction in favor of empirical situations that are concretely rich, value-laden relational complexes. Such an approach does not reduce values to facts but rather understands empirical and normative business ethics as inquiries that focus on different dimensions of a concrete unified situation based on the two fields' differing contextual interests. In this way, each area of business ethics can recognize that its particular perspective and approach not only cannot substitute for those of the other, but that, in fact, each approach gains its full significance only within the context of the other. In addition to accounting for interdependent, shared problem domains, the concept of relational webs also provides the context for the shared construction of meaning and for a general openness to others. It also provides the basis for a relational view of corporate citizenship within the complexes of community life and responsibilities and for stakeholder theory as providing an understanding of one type of commitment within these relational webs.

—Sandra B. Rosenthal

See also Ethics of Dialogue; Fact-Value Distinction; Is-Ought Problem; Positivism; Stakeholder Engagement

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Regressive Tax

A tax is regressive if it requires those with lower income or wealth to pay a higher fraction of their income in tax. A sales tax, which can be levied either at the point of purchase or at various points in the product or sales process, is generally regressive. Sales taxes are also sometimes called commodity or excise taxes.

Taxes can be classified as regressive, proportionate, and progressive. A proportionate tax takes the same portion of each individual's income. Sales taxes are a fixed percentage tax on the cost of goods purchased. Yet such taxes are in practice regressive, because those with lower incomes use a larger portion of their income for necessities, such as food and clothing. A sales tax that exempts food can result in a more proportionate tax. Taxes on cigarettes and alcohol are regressive sales taxes imposed to achieve a social good (to reduce smoking and excessive use of alcohol).

A progressive tax requires those with higher income to pay a larger fraction of their income in tax. A graduated progressive income tax increases that fraction as income increases. Estate and inheritance taxes are progressive taxes, since those with greater wealth pay a higher portion of their wealth in taxes. Most governments use an "ability to pay" principle and, accordingly, seek to make their income taxes progressive. This is considered more just and equitable.

A progressive tax reduces inequality of income, while a regressive tax increases inequality. Horizontal equity in taxes (equal treatment of equals) requires that people earning the same amount and having the same expenses pay the same tax. If horizontal equity does not exist, people often protest. Because of the many tax deductions and "loopholes" in the U.S. tax code, which are often deemed to be unjust, some advocate a proportionate (or a flat) tax—the same tax rate for all incomes.

Most philosophers (including Aquinas, Rousseau, and Rawls) hold that in justice people should be taxed according to their means—that is, the wealthy should pay a greater portion of their income in tax. Social justice calls for a sufficient income to feed, house, clothe, and educate a family. And those with larger incomes have a greater obligation to help provide necessary government services. Thus, a regressive tax is unjust; it is not a fair distribution of the tax burden. John Locke maintained that private property was a natural right; however, he also acknowledged that an individual does not have as firm a right to wealth beyond what he or she can use. On the other hand, conservatives argue from consequences that it is ethical to impose less tax on the wealthy. When the rich have greater income it benefits all, since their income supplies new investment and purchases goods and services which in turn provides many with jobs and family income.

The ethics of taxation has been described as an uneasy truce between good citizenship and personal greed. Supreme Court Justice Oliver Wendell Holmes said that "taxes are the price we pay for civilization." On the other hand, the U.S. tax code has been interpreted by courts as not requiring an individual to pay more taxes than are absolutely required. Hence, taxpayers self-assess their own tax returns, and they seek to pay as little tax as possible.

The U.S. federal income tax provides examples of various tax strategies. Income tax is a direct tax as it is levied on the individual person. A consensus grew in the United States in the 1930s that the government had an obligation to help those citizens who had lost their jobs and those who were spending their old age in poverty. This consensus shifted in the 1980s with the middle class tax revolt. The middle class, who bore a major portion of those costs, judged that they were not receiving proportionate services in return for their taxes. So many Americans demanded tax cuts, and one effect of this tax revolt is that it has required federal and local governments to reduce services. Corporations and wealthy individuals pay federal and local taxes, but they generally hire tax advisers (all the major accounting firms have tax consulting divisions). These tax advisers interpret the tax code so that their clients pay as little tax as possible. Thus, many firms and wealthy individuals pay little federal income tax. Recently, numerous tax advisers and accounting firms have been indicted for advising fraudulent reports.

In addition to generating revenue for government operations, another goal of tax legislation is to influence citizen behavior. So there are many tax incentives for various activities that legislators deem to be for the long-term public good. Hence, it may be difficult for the taxpayer to decide whether she is engaging in the behavior that is encouraged by the tax code or merely exploiting a tax loophole.

Historically, increases in taxes were made in times of war, because of the need for more resources to pursue the war. In democracies, initially income tax was levied only on the rich, but income tax now is generally levied on all but the very poor. Taxes are higher in European Union countries. But governments of these countries provide many more services, such as universal health care.

—Gerald F. Cavanagh

See also Income Distribution; Internal Revenue Service (IRS); Public Goods; Redistribution of Wealth; Tax Ethics; Tax Havens; Tax Incentives; Tax Reform Act of 1986

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Regulation and Regulatory Agencies

Regulation has been defined broadly as the intentional restriction of a subject's choice of activity by an entity not directly party to or involved in that activity. In its most familiar form, regulation concerns restrictions placed by government on activities in the private sector (although government may also regulate itself). Normally, government acts as an agent for its citizens and, as such, is obligated to give account of its actions. Hence, regulation, as well as other government actions, is normally accompanied by a formal rationale, though the content of the rationale may range from substantive to purely symbolic in character. There are many possible forms for this rationale, but it is generally given the label of "the public interest." Hence, regulation can be defined more narrowly as *the public administrative policing of a private activity with respect to a rule prescribed in the public interest.*

As discussed later in this entry, regulation that is formally rationalized as in the public interest may in fact be the result of a societal group obtaining government protection that steers benefits to the members of the group. Thus, the existence of a public interest rationale for regulation does not necessarily mean that the primary actual purpose of the regulation is to provide general public benefit. Government regulation can be a valuable prize that reduces competition, guarantees enhanced incomes, discriminates against open participation in activities, and so on. Indeed, one of the classic reasons for the existence of government is to provide a legitimate mechanism for the coercive resolution of disputes. Whoever can harness that coercion to serve particular economic and social ends can reap enormous windfalls.

Regulation is traditionally divided into economic and social regulation. *Economic regulation* includes the regulation of market transactions, restrictions on the behaviors of firms and on the behaviors of individuals within firms and markets, regulations on financial and trade practices in particular industries and in commerce at all levels, including international trade, and so on. *Social regulation* is concerned with the impacts of economic and social practices on people and on the natural environment; it is sometimes labeled "protective" regulation. Such regulation can be aimed at reducing pollution, protecting consumers from physical harm from the use of consumer products, ensuring the safety of drugs, keeping the workplace safe, assuring safety in the performance of motor vehicles, eliminating discrimination in employment on such grounds as gender, race, age, or disability, and so on.

There are several standard rationales for regulation in the political economy literature. For economic regulation, these include, among others, the control of cutthroat competition (selling below cost) and other forms of "unfair competition;" the control of monopoly power, especially that arising from so-called "natural monopolies;" the existence of unequal bargaining power and of excessive transaction costs in markets; and the control of economic rents, in which firms possess cost advantages over what prevails in the market by being able to exploit their control of local supply due to technological, legal, situational, or other factors. For social regulation, these rationales include the control of externalities, the unintended by-products of market activities, such as pollution; information, incentive, or public goods problems that are judged to require rebalancing interventions by government; and other public policy concerns where the market works but produces outcomes that are socially unacceptable.

Regulation is a function of governments at all levels, from local to national (and even international). This entry will focus on regulation in the United States, with an emphasis on the federal level.

Origins of Regulation

Quite apart from regulation that is sought to benefit narrow private interests, more broadly based regulation is rarely enacted with deliberative foresight. At least with respect to the development of regulation in the United States, policy makers tend not to act in a precautionary manner, reviewing the economic and social hazards that plague society, and developing government interventions that aim to forestall or ameliorate the detected present or anticipated future hazards. Instead, a number of factors work against such rational, calculative regulatory initiation, that is, rationalized policy formulation and implementation of new regulation. Indeed, the most important precursor to regulation has been a real or perceived crisis in the issue area. Advocacy from a variety of pressure groups has influenced the origin and character of the regulation, taking advantage of or creating the perception of crisis. The resulting pattern of regulatory origin in the United States featured most economic regulation arriving decades before extensive social regulation.

Factors Affecting the Initiation and Implementation of Regulation

Factors that work against systematic planning in the initiation and early implementation of regulation include, among others:

- The extent and character of current economic and social hazards, much less the course of future events, may be poorly understood and initially unpredictable.
- Political consensus supporting regulation may be lacking, especially in the case in which those who would pay the costs of regulatory compliance, such as industry, are aware of the potential future economic impacts, are well represented, and oppose the regulation effectively, and those who would benefit are spread diffusely through the population and lack effective political agents to secure regulatory protection (see the work of James Q. Wilson).
- There may be a technical incapacity to resolve the hazards, for example, the knowledge to produce nonpolluting engines.
- The prospective costs of regulation may deter adoption of the regulation. Regulation may be perceived as costly to administer as well as costly to those who must comply with it, so that resource availability issues may slow adoption, as well as engender opposition from both those who must pay for compliance and those who must absorb the tax burden of administering the regulatory state. The Weidenbaum Center (Washington University) and the Mercatus Center (George Mason University) jointly prepare an annual report of federal spending on regulatory activities by agency and in aggregate. Although the report is perhaps overly inclusive about which federal programs are regulatory and is based in center research programs that tend to be critical of government regulation, the extensiveness and significant cost of regulatory programs in the federal government is apparent.
- Whether or not regulation is approved and the particular design of regulation and locus for its administration can depend on the process of regulatory approval, the distribution of political power, and the design of the institutions that manage such approval. For example, conflict in the legislature may lead it to delegate the locus for choice of specific features of the regulation to the regulatory body, where the mix of pressures from interests concerned about the regulation might be different. And the legislature may wish to shift the burden for design of the regulation, as well as the potential blame for the costs or other negative impacts from the regulation, to the regulatory body. The gatekeeping role of legislative committee process can block or advance regulatory legislation. There is now a growing literature on delegation, the creation of regulatory agents, and the design of regulation, beginning with Barry Mitnick's work and including such scholars as Morris Fiorina; the trio of Mathew McCubbins, Roger Noll, and Barry Weingast; Jonathan Macey; David Epstein and Sharyn O'Halloran; and others.
- The design of regulatory tools remains relatively poorly understood so that the choice of regulatory instrument can be far from systematic. The choice of regulatory means is often based on the availability of traditional tools, such as directive standards, or the influence of political directives to reduce regulatory impacts or serve special interests. Political mandates can filter societal expressions of need for government intervention. Thus, issues with the design and choice of regulation, as well as the design of the administrative process, can present challenges in ensuring that controls are adopted and that they are effective and efficiently administered, as well as provide due process opportunities for public participation. The

treatment of regulatory means as a matter of choice, rather than as predetermined in the form of traditional standards regulation, was introduced largely by Allen Kneese and Charles Schulze with the comparison of incentive to directive means. This evolved into the "tools" approach to the study of regulation, as developed by Lester Salamon, Mel Dubnick, Christopher Hood, John Scholz, Barry Mitnick, Stephen H. Linder and B. Guy Peters, Michael Howlett, and a number of others.

- There can be significant hurdles in implementation, that is, in creating the regulatory system, and in administering that system as an operating regulatory organization. These administrative problems are made even more formidable by the need to operate regulatory controls across a federal system in the United States, that is, to operate across federal, state, and local government settings. The study of implementation as almost a subfield of political science has expanded since the 1970s. The early work of Jeffrey Pressman and Aaron Wildavsky was soon joined by that of a number of scholars, including Daniel Mazmanian, Paul Sabatier, Laurence O'Toole, Kenneth Meier, Keith Provan, Brint Milward, and many others. Implementation was treated as potentially a highly problematic and often critical aspect of the initiation of any new public program, including regulation.
- Finally, regulation can be opposed on normative or ideological grounds as a restriction on private choice and on the uses of private property, no matter the distribution of costs and benefits. In general, scholars such as Paul Quirk and Joseph Kalt and Mark Zupan have studied the influences of ideology on changes in regulatory policy.

Crisis as the Precursor to Regulation

Thus, although industries may actively secure and defend regulation that benefits them, much regulation does not occur unless there is widespread public pressure as the result of a perceived crisis. Such perceived crises may have a real basis generated by an attention-grabbing, catastrophic, and often tragic event. One such case was the sulfanilamide elixir poisonings in 1937, in which many of those who died were children. That incident led to the Food, Drug, and Cosmetic Act of 1938, which required the U.S. Food and Drug Administration (FDA) to determine that drugs are both safe and effective before being allowed on the market.

The circumstances preceding regulation can be manipulated or brokered so that they are perceived as a crisis, though there may be no single precipitating event. Thus, pressure from the labor movement led to the creation of the Occupational Safety and Health Administration (OSHA) in 1970. There were indeed serious issues regarding the level of safety in the American workplace as well as advocacy to ameliorate them for years, but there had been no single, galvanizing event.

Although a crisis may be perceived, there may be no real basis for one. Or, if real, the purported solution to the crisis may in actuality be a subsidy or protection for a particular interest or company. Typically, firms seeking regulatory protection invent rationales claiming great public need for the intervention, even though the public action that is proposed may actually raise costs to the public or divert resources better used elsewhere. Firms may manage to define the public's perception of the crisis in such a way that the solution provides significant benefits to the company. Via adroit use of political influence strategies, such firms can ensure implementation of regulatory interventions that are superficially designed to resolve the crisis but may produce little general benefit other than enriching the firms. Thus, tax incentives to produce ethanol, plus the seasonal mandate to use gasoline mixed with ethanol, were great benefits to Archer Daniels Midland, which had sought the regulation. Some critics argued that there were better ways of achieving essentially the same public ends.

Widespread, severe human harm, such as the sulfanilamide elixir poisonings, tends to be the most effective generator of crisis. The crisis levels political divisions and makes legislative action mandatory. But such crisis is not predictable, of course, and, besides producing such reactions as outrage or widespread horror, it acts as a kind of social surprise. Hence, reform with the creation of new or more stringent regulation staggers forward unpredictably after recurrent crises rather than after rational steps to prevent harm.

Role of Pressure Groups in Regulatory Origin

By generating widespread social and political support for public action, the social perception of crisis provides the opportunity for groups to push policy agendas featuring regulation. In general, regulation can be created in response to pressures from a variety of sources, including consumers desiring protection, industry desiring competitive protection and special advantages, the bureaucrats themselves as a means to extend or defend the bureaucracy or to rationalize existing regulation, and legislative or bureaucratic actors as a good faith effort undertaken in a particular, but authentically held, view of the public interest.

As an example of "public interest" regulation, consider Ann Friedlander's arguments regarding value-of-service pricing regulation by the Interstate Commerce Commission (ICC). Beginning in the ICC's early years, value-of-service pricing appeared originally to be aimed at subsidizing the development of the American West, and, hence, promoting economic development in the United States. Under value-of-service pricing, so-called higher-valued goods, such as manufactures, were subject to higher shipping rates than lower-valued goods, such as bulk commodities. Because the developing West produced lower-valued goods, this form of discriminatory pricing in effect subsidized development in that region. But value-of-service pricing lingered as official regulatory policy long after western development ceased to be a national goal and was for decades supported in Congress and the ICC by those whom it benefited. Indeed, scholars have found strong evidence that regional differences, including regional competition reflecting differential potential impacts of regulation, frequently shape regulatory designs and implementation (see, e.g., historical studies by Thomas W. Gilligan, William J. Marshall, and Barry R. Weingast; Richard Bensel; and Elizabeth Sanders). Thus, whether or not the initiation of the regulatory policy had an authentic public interest basis, history suggests that groups, including those with a regional basis, have interpreted the regulation in light of their self-interest and pursued and defended it chiefly on those grounds.

Historical Pattern of Regulatory Origin

Most economic regulation predated social regulation in the United States. With a few exceptions (e.g., antitrust regulation in the 1903 Antitrust Division of what became the Department of Justice), the model of the ICC (see below) was replicated in other regulatory contexts: the Federal Reserve Board in 1913, the Federal Trade Commission (FTC) in 1914, the Shipping Board (later the Federal Maritime Commission) in 1916, the Tariff Commission in 1916 (becoming the International Trade Commission in 1975), the Federal Water Power Commission in 1920 (becoming the Federal Power Commission [FPC] in 1930 and the Federal Energy Regulatory Commission [FERC] in 1977), the Federal Radio Commission in 1927 (becoming the Federal Communications Commission [FCC] in 1934), the Securities and Exchange Commission (SEC) in 1934, the National Labor Relations Board (NLRB) in 1935, the Civil Aeronautics Board (CAB) in 1938 (beginning as the Civil Aeronautics Authority), and the Atomic Energy Commission in 1946 (becoming the Nuclear Regulatory Commission [NRC] in 1975).

Federal regulation was relentlessly mimetic, replicating earlier models. As noted below, the rationale for those models was created largely post hoc but found widespread support and defense among the legal practitioners who populated the agencies. Regulation was seen as an enterprise in the law, guided and defended by those schooled in the same tradition as those who practiced in the courts. In essence, despite being a delegation from the legislature, regulation in the United States was perceived as an appendage of the legal system and its practitioners. A few social regulatory agencies, mostly in the single-headed agency rather than multi-headed commission structure, were established, including the FDA in 1931 (developing from regulation going back to the Pure Food and Drug Act of 1906) and the Federal Aviation Agency (later, Administration, or FAA) in 1948.

Beginning in the mid-1960s, new regulations were overwhelmingly social in character. Some used the old independent commission form, but many were established as single-headed agencies. The commission model was under increasing attack, and the new regulation was sometimes seen as an urgent matter for executive branch policy making and implementation rather than as something to be investigated and adjudicated in an independent body. In other words, social regulation was sometimes perceived as an enterprise directed at solving pressing social problems, under the execution of the chief executive, rather than as the arbiter of disputes and protections among industries that needed to be governed so as to approximate markets. The new agencies were thus a mix of the old independent commission form and the single-headed executive branch agency. For example, the Equal Employment Opportunity Commission (EEOC) was established in 1964; the Environmental Protection Agency (EPA) in 1970; the Consumer Product Safety Commission (CPSC) in 1972; OSHA in 1970; the Mine Enforcement and Safety Administration in 1973, becoming the Mine Safety and Health Administration (MSHA) in 1977; the National Transportation Safety Board (NTSB) in 1975; and the Office of Surface Mining Reclamation and Enforcement (often referred to more simply as OSM) in 1977. The Commodity Futures Trading Commission (CFTC) saw light in 1974 in a structure parallel to the 1934 SEC, evolving from earlier economic regulation located in the executive branch.

Performance of Regulation

The performance of federal regulation has been criticized almost from its beginning, with the ICC in 1887. Many regulatory performance issues have been rooted in the design of the agencies and their administrative practices, with the original model being the ICC.

Model of the ICC

The ICC took on the modern form of the independent regulatory commission, an entity outside the hierarchical direction of executive branch agencies, in 1889. Early that year, a lame-duck Congress and President Grover Cleveland sought to put the ICC beyond the direct control of incoming President Benjamin Harrison, who was perceived as a "railroad lawyer" likely to weaken the new agency's authority. They passed legislation taking the agency outside the Department of the Interior and making it an independent body. Subsequent legal scholarship sought to reify the value of independence, which is supposed to keep agencies free of political meddling and ensure that they develop and maintain the specialized expertise necessary to regulate effectively. Many critics have observed that independence may have caused more problems with developing consistent public policies than avoided partisan manipulations.

The ICC's procedures were developed by its first chair, Judge Thomas Cooley, who installed an adversarial, judicial-like system in the new agency. These procedures were intended to give the new agency legitimacy, but in practice they led to long delays and significant costs for those who sought to participate in the process. Sometimes those costs actually protected regulated companies from challenges by acting as an entry barrier to companies seeking to enter the industry. Because new entrants often brought cost-saving innovations to the industry, the classic administrative process tended to act as a drag on innovation and efficiency in the regulated industry. Later, the Administrative Procedure Act of 1946 and its amendments attempted to standardize the process across agencies and succeeded in bringing some, though not complete, uniformity across the federal government. But as the Cooley model spread across federal regulatory bodies, so did its problematic characteristics.

Reliance in the United States on an adversarial administrative process mimics the practice of the larger legal system derived from the English model. Such adversarialism stands in marked contrast to the greater use of administrative tribunals in many other countries around the world, including many in the European Union. In an administrative tribunal, a greater burden is placed on the administrative judges to investigate and assemble the case, rather than sit back as arbiters between the advocates representing the parties in the dispute or administrative judgment. One consequence of the U.S. system is that the cases that are assembled via adversarial contest do not necessarily reflect all interests relevant to a case, nor do they necessarily assemble all relevant evidence. What is assembled is what is in the self-interest of the parties to the case to present, not what should be reviewed in the wider aim of serving the public interest in regulation. There is a nominal instruction in U.S. administrative procedure that encourages administrative judges to play a more active role, but the common historical practice has been to allow the record to assemble itself.

Regulatory agencies were set up as government in miniature. The agencies performed all the functions of the larger government but without the checks and balances of separation of powers. Thus, regulatory agencies were administered by an executive (sometimes plural, as in the independent commission), who conducted the legislative function of rule making under delegation from Congress, investigated infractions of those rules, adjudicated whether infractions occurred and how rules should be applied to individuals and firms, conducted enforcement activities, set general policies, and collected data and statistics on the industry. Critics charged that agencies that functioned in this manner could not be truly impartial and could not police themselves effectively by competition among their functional areas.

Rigidity and Capture in a Regulatory Life Cycle

Critics of regulation noted that, over time, many regulatory agencies reached accommodations with the regulated industries. The agencies appeared to become supportive and protective of the industries rather than of the consumer and general public. In a classic analysis, Marver Bernstein argued that independent regulatory commissions tended to follow a life cycle: The regulatory commission emerges from a crisis that, in a compromise, resolves a group struggle that may have lasted for decades. In its youth, the agency is crusading and is opposed by a well-organized industry. The agency lacks experience in the area and has vague objectives and untested legal powers. Its political supporters fade away, convinced the battle was won. In maturity, the agency adjusts to the conflict it faces and begins to act as a manager or umpire for the industry rather than as a policeman. It relies on precedent, maintains good relations with the industry, and soon develops a backlog of slow-moving cases. Bernstein notes that the agency "becomes a captive of the regulated groups." In its old age, the procedures of the agency become sanctified and resistant to change. It acts as if it has a "working agreement" with the industry to maintain the status quo. The agency's staff declines in quality and the agency suffers from poor management. It fails to keep up with societal change and is generally recognized as a protector of the industry. Congress becomes reluctant to fund what is perceived to be a poorly performing agency. Should crisis recur in the industry, however, whether due to technological, competitive, or other changes, new legislation, supported again by activist groups, can return the agency to its youth. The cycle repeats. The life cycle model provides an attractive explanation for some very recognizable behaviors in federal regulation, though a number of scholars, including Barry Mitnick, Robert Chatov, Kenneth Meier and John Plumlee, and others, have analyzed Bernstein's arguments and found them more heuristic than descriptive.

Iron Triangles Protect Industry

Critics of federal regulation observed that the close relationship that developed between agency and industry was often embedded in a network of relationships among industry, the agency, congressional committees, and, later, citizen groups, the federal courts, and the president. Because the public policy that emerged from the interaction of industry, agency, and Congress tended to reliably favor the regulated industry, the trio was often referred to as the *iron triangle.*

The iron triangle is built on a system of incentives operating among the particular institutions of the federal government. To serve their districts and earn reelection, legislators in the House and Senate seek to be members of committees of oversight for industries important in their home districts. To encourage legislators to protect the industries via helpful legislation (and obstruction of threatening bills), the industries take actions that generate flows of campaign contributions as well as organize support and votes from those employed in or dependent on the industry.

In return, legislators produce laws consistent with the interests of the industry and attempt to influence the regulatory agency to bias its discretionary decisions toward the industry. Legislators control agency budgets; the Senate passes on top-level agency appointments. Uncooperative agency administrators can be publicly embarrassed at oversight hearings. Agency heads are political appointees who, according to historical data, tend not to stay in their positions for even the full term of their appointments. Looking ahead in their careers, these administrators do not want their service in the agencies held up to public ridicule. In their jobs, they are dependent on information from the regulated industry. Because the industry depends on receiving favorable regulation, it treats regulators with the respect and attention that these officials can get from nowhere else. Through repeated interaction, the regulators see industry managers as reasonable folks trying to do their jobs rather than as subjects of federal regulation whose compliance must be ensured. Thus, the industry can shape the perceptions of regulators via information and interaction. Finally, when they leave their positions, agency heads often find employment either in the regulated industry or in jobs dealing with the industry, for example, in law firms or lobbying groups specializing in the industry. This rotation of jobs among the actors in the regulatory system is sometimes called the *revolving door.*

Because of this perverse distribution of incentives, mediated by legislators or received directly, regulators tend to be responsive to the industry. In the extreme case, the incentive system leads to regulatory capture. Public policy making in such regulatory systems thus displays the stable outcomes of an iron triangle.

Although regulatory outcomes in some issue areas appear to benefit the regulated industry, and there is abundant anecdotal evidence of many of the behaviors described above that appear to lead to such outcomes, the behavioral and motivational logic of the iron triangle is relatively simplistic. Many practicing regulators would claim that the logic either does not fully apply or is incomplete as it applies to their industry contexts. For example, the classic logic ignores the emergence of professionalism in the staffs of the regulatory agencies and how such professionalism would modify agency outcomes (see, e.g., work by Ted Greenwood, John Mendeloff). Thus, one area for future academic research is whether iron triangles really emerge in the fashion described (as influences on bureaucratic decision making—see, e.g., the recent work by George Krause; Marc Eisner, Jeff Worsham, and Evan Ringquist; B. Dan Wood and Richard W. Waterman; and Richard W. Waterman, Amelia A. Rouse, and Robert L. Wright).

Beginning in the late 1960s, increases in judicial activism along with the appearance of citizen group activism on an organized scale never seen in Washington posed challenges to the old iron triangles of regulation. Even the White House took occasional action to repair regulatory failures. The networks of federal policy making in a number of areas of regulation became more flexible, with outcomes that were no longer so consistently supportive of industry interests. With six significant influential actors rather than three, regulatory policy making looked more like a jelly hexagon than an iron triangle.

The study of the creation and change of policy agendas (see, e.g., the work of Roger W. Cobb and Charles D. Elder; John Kingdon; and Frank R. Baumgartner and Bryan D. Jones; among others), the study of networks of policy making, often labeled *policy subgovernments* or *policy networks* (see, e.g., the work of Hugh Heclo; Edward O. Laumann and David Knoke; among others), as well as the study of networks of policy implementation (see, e.g., the work of Keith Provan; Brint Milward; and others), have been expanding. These approaches suggest that, quite apart from the rational choice or interest-based arguments that seek to explain regulatory origin and regulatory design, path and institutional structure models can offer a powerful descriptive theoretic alternative. Thus, such factors as the particular pattern of decision control in the administrative process in the issue area; approval paths; government-level crossing effects, featuring control loss, policy redefinitions, control delays, and so on; and arena effects as competition occurs among a limited set of elite groups within a particular set of institutions can individually or collectively shape regulatory origin, regulatory designs both formal and in practice, and, of course, regulatory performance (on the extreme case of regulation as a random walk, see the work of David McCaffrey).

Recent Performance of Regulation and the Coming of Reform

A large number of studies in the 1970s and later, both by economists and by public interest activists, established that federal regulation had performed poorly in a number of regulated contexts. Agencies such as the CAB and the ICC had tended to protect regulated companies from competition while raising costs for consumers and retarding innovation. In other cases, protections for consumers, those exposed to environmental pollution, vehicle owners, patients treated with new drugs, and others, were criticized as poorly designed, ineffective, or insufficient. These streams of criticism, together with the acceptance of new ways of thinking about the design and performance of government, led to both efforts to deregulate, chiefly in economic regulation, and efforts to increase or modify social regulation. The rise of public interest activism spurred by the efforts of Ralph Nader, beginning in the late 1960s, led to support for new social regulation. Agencies such as the EPA, OSHA, and the CPSC were established in the early 1970s. For the first time, major regulatory agencies were terminated or replaced with much smaller entities (the CAB in 1978 and the ICC at the end of 1995). Beginning with the Carter administration, there were experiments with new methods of regulation in some agencies.

Despite the problems noted above, social regulation has yielded very significant benefits in the United States in the just over 30 years in which the major statutes have been in effect. Social regulation has resulted in markedly cleaner air and water. Despite some early, conflicting empirical studies, regulation appears to have had some effect in making the workplace safer. It has caused firms to establish significant offices dealing with environment, health, and safety. In many firms, this has translated to a serious and ongoing attention to compliance, with measurable reductions in pollution and increases in employee safety. The development of professional compliance bureaucracies with both a vested interest in the regulation and a high level of professional expertise in designing and performing compliance led many firms to resist the deemphasis on regulatory compliance that characterized regulatory policy during the administrations of Reagan and George H. W. Bush (on response bureaucracies in the financial services industry and elsewhere, see the work of David McCaffrey and his coauthors).

Indeed, some large firms (e.g., PPG in Pittsburgh, Pennsylvania) participated in the development of new regulation. Their expertise in regulatory design, and their knowledge of how regulation affects their costs, permits them to help design regulation that may be less costly for them in compliance than for their smaller competitors. Large, multinational firms have participated in negotiations leading to the establishment of voluntary international standards that make it easier for such firms to do business overseas. Having a uniform standard across international boundaries, even a fairly stringent one, is far less costly for business than adapting products to the multiple standards of different national regulatory regimes. Meeting such international standards can thus be a critical element in the ability to compete. And there can be significant differences across international regulatory regimes. For example, regulation in the European Union is more likely than in the United States to be based on the *precautionary principle,* which places the burden of proof of safety on those introducing a new technology. In the absence of such proof, the technology is tightly restricted. Thus, sensitivity to and the ability to adapt to as well as shape international standards can be essential in being able to compete in many markets around the world. Today's patterns of corporate compliance tend to acknowledge such international differences.

Some Business Complaints Under Regulation

Among the most important factors shaping public agenda discussion over the creation, design, and performance of regulation have been business complaints about the impacts of regulation. Offered sometimes with guile as part of a contest over the definition of regulatory issues and the design or implementation of pending regulation or regulatory reform, at other times they have reflected frustration with inappropriate, counterproductive, costly, and ineffective regulatory tools and administration. There is a huge anecdotal literature on regulatory failures, spanning decades (see, e.g., the historical reporting and fascinating anecdotes in works by Louis M. Kohlmeier Jr. and Cindy Skrzycki; there are many articles in the *National Journal* and in *Regulation* that describe regulatory behavior). Some of the typical complaints include the following:

Stifled Innovation

Regulation tends to freeze industries, protecting the existing competitors against new entrants and slowing the introduction of new technologies. For example, in 1961, the Southern Railway attempted to introduce its new aluminum "Big John" hopper cars, which were capable of competing with barges in transporting grain. The barge lines and a number of other businesses that depended on barge traffic or grain storage complained to the ICC, tying up the regulatory approval process in the ICC and in the federal courts for years, forcing Southern Railway to pay high legal fees and preventing it from earning a swift reward for its innovation. Studies at the time showed that just switching grain transport to the cheaper rates of the Big John cars was sufficient to reduce the prices of many commodities that even indirectly depended on grain, such as milk, beef, and poultry.

Inconsistency in Application; Unresponsiveness to Error

One of the classic cases of regulatory failure concerned the Marlin Toy Company, whose popular transparent plastic children's play balls, the "Birdie Ball" and "Flutter Ball," began breaking unexpectedly. A supplier had substituted an inferior grade of plastic. The balls were taken off the market under the Hazardous Substances Act, then administered by the FDA. The new CPSC took over responsibility for this act in 1973. Under agreement with the CPSC, Marlin had replaced the plastic in its balls by then, but the CPSC inaccurately listed the new balls as the banned ones. The commission was unable to issue a timely correction in its public listing of banned products. As a result, the company was unable to sell its toys and laid off most of its workforce. It required the passage of a private bill by Congress permitting Marlin to sue the government for the company to recover a portion of its damages.

Mindless Proceduralism

A common complaint about regulation is that it can feature procedural requirements that are imposed in a rote way, without effective linkage to any substantive rationales. Such proceduralism is often characterized as *red tape,* or termed *bureaucratic.* Sometimes the proceduralism does have an unstated rationale, such as creating an entry barrier that protects regulated firms from new entrants.

In a classic historical case of regulation from 1965, Tom Hilt, a young employee at his father's trucking company, Hilt Truck Line, became frustrated at having to type and retype tariff schedules—lists of shipping rates between various locations—for submission to the ICC. All new rates as well as rates proposed for change had to be approved by the ICC. After Hilt submitted a lower tariff on frozen potatoes, meat, and grain, railroads had challenged the reductions, claiming that Hilt's rates were lower than its costs. Under ICC regulations, cutthroat competition—selling below cost—was illegal, and had been since the original Interstate Commerce Act of 1887. The railroads mounted such challenges routinely for rate reduction submissions from competing transportation modes to protect their competitive position, and the protest was not based on real knowledge of Hilt's costs. The Hilt Line had decided not to fight the challenge. So, after finishing typing tariffs that raised the rates back up, a disgusted Tom Hilt inserted a new item at the end of one such list, "Yak Fat, Omaha to Chicago. Rate: 45 cents per hundred pounds . . . to be shipped in minimum quantities of eighty thousand pounds . . . Hilt Truck Line would accept yak fat in glass or metal containers, in barrels, boxes, pails or tubs." The ICC clocked in the new tariff, filed it, and "tariff watchers" for the railroads noticed the filing. The railroads filed a formal complaint, complete with supportive data and comparing the shipment to an earlier case dealing with paper articles, arguing that Hilt Line's rate was patently below cost. The ICC reviewed the submissions and suspended the yak fat rate, responding routinely, as it normally did, to such a complaint. The railroads notified the ICC that they had formed a yak fat arguing committee, on which sat representatives of a number of midwestern railroads. Hilt Line never responded, and, after a while, the ICC closed the case, warning Tom Hilt that it had been "afforded ample opportunity" to counter the railroads' case. Of course, the yak fat rate was entirely bogus, borne of impatience with a regulatory system that used procedures originally intended to provide due process to protect a regulated industry from competition.

Excessive Delays

The administrative process often permits intervenors to participate, realizing norms of due process and protecting regulatory decision makers when appeals courts look to see if the required substantial evidence on the record was compiled. The procedures themselves are often time-consuming, with many layers of review. The result is delay. It can take an agency a year or more to issue a single regulation, and challenges to regulations can span years, as they did in the Big John case.

Inappropriate Levels of Standard Specificity

Regulation has operated with vague standards in some cases (e.g., many areas of economic regulation) and overly specific standards in other cases (e.g., some areas of social regulation). Thus a standard such as forbidding "unfair competition" under economic regulation (e.g., by the old ICC) tells us by itself little about what is forbidden. This delegates effective regulatory policy making from legislators to the regulators, who have sometimes implemented their discretion by offering inconsistent, case-by-case interpretations. The other side to such vague controls is directive regulation that entails highly descriptive "design standards" that detail the specific acceptable means of compliance, admitting no adaptations. Examples include the original design standards implemented by OSHA as it got under way in the early 1970s. Thus, the exit sign standard specified every aspect of an exit sign, without regard to the room or setting in which the sign was situated. Many OSHA standards were originally adopted from boilerplate language designed for procurement contracts, not safety regulations, simply to get OSHA implemented quickly. Such standards were pruned from OSHA's rulebook in the late 1970s. In general, standards can be ineffective when they require compliance that is inappropriate to their contexts as well as unnecessarily costly.

Excessive Costs; Costs Exceed Benefits

It is not surprising that so much criticism has been leveled by business at the costs of regulation. Many of the regulatory problems noted in this entry generate questionable costs, whether due to delay, proceduralism, inability to recover savings from innovation, protection of the profits of special interests, or other factors.

Protection of Special Interests

Private interests have sometimes been able to shape regulations in ways that protect them from competition or that provide them with direct, tangible benefits denied others. The iron triangles functioned in this way, of course. The ICC operated for decades in a way that protected each mode of transportation against competition from the other modes. Marketing orders administered under the U.S. Department of Agriculture kept the prices of navel oranges high by restricting the supply of "whole fruit" allowed to go to market, while keeping the price low on excess oranges treated as juice for Sunkist and other juice producers.

Regulatory Paternalism

Too often, regulators assumed that the locus for the design of regulatory standards lay completely in government. The industry was treated as suspect, not to be trusted. This led to unrealistic, overly costly, and often ineffective standards. For example, the original bicycle standard issued by the CPSC was developed in-house and widely criticized by industry as likely to be ineffective and needlessly costly. In recent years, a whole subfield of administrative practice and research has grown under the heading of "reg-neg," *regulatory negotiation,* which aims to involve industry representatives together with consumer and other stakeholder representatives, along with government regulators as facilitators, early in the process of regulation development (see the work of such scholar-practitioners as Philip J. Harter and Daniel Fiorino). Such collaborative development of regulations tries to avoid paternalism, while yielding more effective regulation with a wider base of support from those affected by the regulation.

Conflict Among Regulations

The development of any regulation tends to proceed independently of related or existing regulations. This can lead to the government effectively prescribing opposing mandates. For example, OSHA noise protection rules have required ear protectors for users of noisy machinery, such as drills, and also required backup beepers on workplace vehicles as a warning to pedestrians. How to avoid what may happen when a work vehicle backs up toward an ear-protected worker using a drill is not considered.

Inability to Focus on Cases Where Needed and to Avoid Cases Where Inapplicable; Poor Targetability

Government tends to regulate what can be measured and controlled rather than what is dangerous and can be made safer. Indeed, government too often regulates appearances when it cannot or will not control outcomes. Thus, regulations attempt to control conflicts of interest by requiring reporting of stock ownership by top officials, effectively regulating the appearance of conflict of interest. But they permit lobbyists to flow campaign contributions to legislators who are key to creating or blocking new regulatory legislation. The only conceivable reason such contributions are made, of course, is to influence such actions—the issue is not appearances, but active biasing of outcomes.

Feasibility of Regulating in Some Areas

Just as perfect agency—perfect performance by agents for principals—is only rarely, if ever, attained, so are there limits to what can be controlled by regulation. Regulation of jaywalking is common in American cities, yet, apart from a very few central city locations, is impossible to implement universally and, indeed, is enforced only sporadically. The regulation appears to exist primarily for educational or emergency uses.

Regulatory Agencies in the United States

Unlike some national systems of regulation around the world in which the central government reserves to itself all significant regulatory controls, including direct inspections, regulation in the United States has been adapted for our federal system. U.S. regulation also displays characteristic institutional structures and administrative processes, including the process of judicial review of its decisions.

Regulatory Federalism: The Granting of Primacy to the States

In the United States, regulation is performed by governments at all levels, federal, state, and local. Major new regulatory initiatives usually, though not always, begin at the federal level, but are often implemented via federal to state handoffs. Thus, a new piece of social regulation might create a new federal agency or a new program within a federal agency. Under federal rules set in the legislation, if states pass legislation similar though not necessarily identical to the federal act, provide state funding, and adopt regulations consistent with the federal ones, the federal government can grant states *primacy.* This permits the state to be the regulator of first contact and, of course, primary effect. State inspectors, not federal regulators, are likely to be the ones to visit regulated workplaces. Federal inspectors fall back to support positions, though they may intervene. Some, such as those at OSHA, may concentrate on the most dangerous enterprises. Primacy has usually functioned well and has been pulled back only infrequently. During the Reagan administration, severe cutbacks in federal agency staffing and budgets were implemented in response to White House policy favoring loosened enforcement. When failures in state regulation of mine safety emerged in a few states in the absence of federal assertion of authority, in some cases involving corruption, federal regulators were forced to cancel primacy and reassert full federal control in those states.

Institutional Structures and Practices in Federal Regulation

Federal regulation in the United States is implemented via a mix of institutional structures that do not reflect a consistent design practice or rationale. In addition, although there have been sporadic efforts to combine sector or industry controls in the same agency setting, such controls can still be found split in different locations. Thus, antitrust and competition regulation is split between the FTC and the Department of Justice. Consumer protection in transactions is in the FTC, while consumer safety is in the CPSC. The FDA regulates some aspects of food safety, as do parts of the Department of Agriculture. The stringency of controls is also inconsistent. The CPSC can issue mandatory product recalls; the Department of Agriculture's Food Safety and Inspection Service can ask meatpackers to recall adulterated meat but does not issue mandatory recalls (though it can seize adulterated product from the marketplace).

Institutional forms include the independent regulatory commission, dating to the ICC, which as noted above became independent in 1889, and the executive branch administrative agency. The independent commission has been structured as partly independent of presidential policy, but even this status varies. Presidents can designate a commissioner as chair, but cannot always remove a chair. In the independent commission, commissioners are nominated by the president and confirmed by the Senate but cannot be removed by the president, unlike top-level department appointees. There has been a trend to place new or reorganized independent commissions inside government departments for administrative reasons, while retaining most of their previous independence. Thus the FPC, when reorganized as the FERC, was placed inside the Department of Energy rather than, as before, floating freely in government space. The Surface Transportation Board, successor to the ICC, was placed inside the Department of Transportation. But, apart from the occasional requirement to consider policy initiatives from the department secretary and other relatively minor stipulations, such agencies still function as they did before.

In contrast, regulation by executive branch agencies functions as does the rest of the federal government. The head of the FDA has the title of commissioner, is nominated by the president and confirmed by the Senate, but serves like other executive appointees at the pleasure of the president. The particular regulatory tools used, such as design standards, can be exactly the same whether in a commission or an executive branch agency. The U.S. EPA is unusual in that it is an independent agency, not inside a department, but functions as an executive branch agency. Its top post, the EPA "administrator," serves at the pleasure of the president, like other top executive appointees.

Today, the number of commissioners on an independent regulatory commission varies from 3 to 5; in decades past, the number ranged as high as 11. Most economic and social regulatory agencies in the 20th century were small relative to agencies in the executive branch, with a few hundred to a few thousand employees and budgets in the seven- to eight-digit range. The expansion of federal authority now subsumes many government functions not previously thought of as regulatory. Thus, the annual compilation of regulatory budgets by the Weidenbaum and Mercatus Centers shows a Fiscal Year 2007 total budget for regulatory activities of $44.2 billion and a staffing level at 245,361 full-time equivalent people. The comparable numbers were $43 billion and 241,029 in 2006. Adjusted for inflation, the budget total is actually slightly less. But these totals include many functions that would in the past have been considered as related to defense, such as homeland security, as well as to other functional areas. In 2003, the Transportation Security Administration alone hired more than 50,000 airport screening agents, greatly inflating the apparent size of regulatory staffing.

As illustrations, the estimated outlays by the CPSC for 2006 are $65 million with a staff of 440; for the FDA, $1.875 billion with a staff of 10,164; for OSHA, $484 million with a staff of 2,173; for the EPA, $5.395 billion with a staff of 17,302; for the FCC, $365 million with a staff of 1,886; and for the FTC, $220 million with a staff of 1,080. The SEC budget jumped from $357 million with a staff of 2,841 in the year 2000 to $867 million with a staff of 3,765 in 2006 largely due to extra resources given it after the corporate scandals, with the passage of the Sarbanes-Oxley Act in 2002. It should be noted that some regulatory agencies are funded at least partly by fees or penalties, rather than by outlays from the federal budget, reducing their actual central budget cost.

Political party balance on a regulatory commission is often required by statute. Thus, no more than three members of the five-member FTC can belong to the same political party. In one historical case, the appointment of Joseph Eastman to the ICC in the early years of the 20th century briefly became an issue. With his typical honesty, Eastman notified congressional leaders that he was an independent, not registered to either major party, and so, in his own view, there was an issue as to whether he could be appointed to a seat that would normally go to a member of a party to ensure statutory balance on the ICC. Eastman did this on principle—he did not believe regulatory officials should be partisans. Senator Henry Cabot Lodge is said to have deliberately ignored the observation of his constituent, and Eastman's famous career as an ICC commissioner began.

Statutes also often set up the terms of commissioners to be overlapping to maintain policy uniformity and institutional memory. Thus, on some commissions, one commissioner's term ends each year, though even this is not consistent across all commissions. For example, terms on the five-member FTC are 7 years, not 5. Thus, the five FTC commissioner terms expire in 5 straight years, followed by a gap of 3 years, then five more expirations and a gap of 3 years, and so on. This pattern has existed since 1914. The FCC and the SEC each have five members who serve overlapping 5-year terms, so that one member's term expires each year. But the expiration date of those terms is not the same for each agency. The reasons for the differences among the agencies are historical, not based in some intrinsic agency characteristics.

Judicial Review of Regulation

In general, decisions by the federal regulatory agencies may be challenged in the federal appeals courts, with the possibility of review by the U.S. Supreme Court. A string of federal cases has narrowed the qualifications that any party must have to bring suit against agency decisions, that is, to have "standing to sue." In most cases, that party must at least show that he or she is individually "aggrieved" in a manner covered explicitly by the enabling statute. Review courts look to see if the agency has compiled "substantial evidence on the record," that is, collected evidence on all the decision criteria specified in the enabling statute and in its own rules. There is no requirement that the review court determine that the agency actually weighed all that evidence so as to produce a decision consistent with the content and balance of the evidence. All that is required is that the evidence be there. This decision rule can create an interesting and potentially mindless dynamic, as agencies routinely assure that the evidence covered at rule-making hearings and in adjudications—indeed, in any reviewable context—touches on all criteria mentioned in the enabling statute and in agency regulations. Such procedure is also potentially a recipe both for delay and for manipulation over the content of the record.

Some Tools of Regulation

In recent decades, the tool set of regulation has expanded from the traditional directive standard to include a variety of innovative and sometimes incentive- or market-based alternatives.

Traditional Standards

The traditional tool of U.S. regulation is the standard. The agency promulgates a rule that either incorporates standards specified in the enabling legislation or creates such a standard under authority created by the legislation. The standards amount to mandatory directives for behavior. As noted above, the standards can vary greatly in specificity. In the context of social regulation, standards are sometimes called *design standards* because they fully specify the compliance required, whether it is use of hay bales to control mine runoff under the regulations of the Office of Surface Mining Reclamation and Enforcement or the height of fire extinguishers above the ground under old, now deregulated OSHA rules. Penalties are attached to noncompliance with the directives. The use of standards assumes that the activities that standards specify will produce the outcomes desired under the regulation, such as a cleaner environment or a safer workplace. But the social science on many such regulations that would establish whether the standards actually produce their intended outcomes has often never been done. In fact, some critics argue that such standards often have the opposite effect—by locking in certain compliance technologies, they inhibit the development of innovative, efficient, and more effective means of compliance. On the other hand, when regulated actors strongly oppose the regulations or are likely to game or manipulate regulations that allow discretion in compliance, the standard provides an easier-to-measure and more certain control.

New Regulatory Tools Featuring Incentive Effects and Discretionary Compliance

Beginning in the 1970s during the Carter administration, largely in the context of social regulation, a number of innovative means of regulation were developed that aimed to produce outcomes better than those from old-style directive regulation. The use of tax incentives in the form of tax credits was a familiar and widely criticized tool, and, until that era, incentive regulation had rarely been employed elsewhere. Tax incentives were useful only on those who paid taxes and amounted to an implicit subsidy from the Treasury. In contrast, incentives such as effluent charges, which put a price or fee on each unit of pollution emitted from a plant, tried to create direct incentives for polluters to reduce emissions. A company's total costs for pollution would go down as it reduced emissions.

Other methods sought to make use of a company's own knowledge of costs of compliance to produce both more effective and more efficient compliance. For example, the regulatory bubble placed an imaginary bubble over a plant that had multiple air pollution sources. Old-style standards would have required each smokestack to reduce emissions to a set level, per a standard. With a bubble, the company was able to use its own discretion to decide which sources on the site to reduce, as long as the total emissions met the EPA bubble standard for the site. The company had to worry only about total emissions from the site, combining all the sources. Some sources, in newer facilities, were typically much cheaper to control than those from older plants. Emissions from the bubble could be adjusted by the regulator to ratchet down total site emissions below the total level that would have resulted from regulating individual stacks, leaving both the company, which could do the reductions in the cheapest manner, and the public, which would get, overall, cleaner air, better off.

A similar logic created regional or urban permit auctions. An imaginary bubble was placed over a region and pollution permits issued to all polluters in the region. If any company wished to expand, it would have to purchase permits from other polluters. Such permits might become available (and, indeed, be sold for profit) when plants were closed or equipment upgraded to more efficient, cleaner technologies. Any trade in permits resulted in an automatic reduction in the permitted levels by a certain percentage, for example, 15%. Thus, pollution would ratchet down as permit trades occurred and the total pollution "value" of permits in the regions moved downward. The problem with such markets is that they ignored localized effects. Companies could build very dirty sites, polluting nearby communities, if they could purchase the permits elsewhere in the air shed.

One solution to the problem of design standards was to use *performance standards.* These standards set the outcome levels directly and allowed industry to figure out the best way to reach those outcomes. Like the bubble, the performance standard took advantage of industry expertise and used the discretion it permitted industry to make all concerned better off. One problem with performance standards is simply that it is often difficult to measure outcomes directly in many regulated areas. Unless outcomes can be measured consistently and with high certainty, there may be opportunity for manipulation. But in such contexts as environmental pollution or workplace safety, it is sometimes possible to directly measure such performance success, and so performance standards can be a significant advance. It is likely that future regulatory tools will take advantage of incentive and marketlike effects to reach outcomes above those achieved in the past via traditional standards.

The newer regulatory tools have also tried to shape the decision setting for the respondent. Thus, transparency or information provision has been used to take advantage of consumer choice and reputational factors in encouraging companies to modify their behaviors. And, as discussed above, the administrative process itself has been modified in some agencies to try to involve all regulatory stakeholders early in the rule-making process. If a "reg-neg" process results in a quality regulation supported by both industry and consumers, lengthy court challenges will be avoided and the regulation itself is likely to be more effective.

Strategic Use of Regulation

Despite the development of new, more effective regulatory tools, business may continue as it has done for decades and take strategic advantage of regulation. Indeed, though public discussion might suggest that regulation is a continual burden for business, more often than not the opposite is true: Regulation protects and gives competitive advantages to companies able to exploit its impacts. In general, large firms gain advantages over smaller competitors under regulation. They are better able to handle the demands of compliance. Under newer forms of regulation, such as performance standards, they can afford to employ expert central staffs that can design compliance activities that are most efficient for the firm; smaller firms must contract this out and thus have higher costs and less of an opportunity to develop adapted, customized responses to the regulation.

Of course, a view that treats regulation as a strategic opportunity rather than as a citizen obligation raises serious ethical issues. To the extent to which newer means of regulation achieve both public and private ends, yielding better as well as cheaper compliance, the ethical stress is reduced. But in a society that operates under both the rule of law and a representative democracy in which the choices to impose costs and achieve common benefits are made legitimately, business must act as a citizen and not just a player. Thus, the description below of strategies under regulation is offered descriptively, rather than as a kind of normative guide to what should be done under regulation. When such strategies run counter to public policy, regulators must find innovative means to counter them, much as they developed replacements for traditional regulation. As of 2006, government was widely exploited for private gain by American business, making use of sophisticated lobbying, carefully targeted campaign contributions, relationships with friendly legislators who use the earmarking capability in legislation to divert public benefits to narrow private interests, and other means. Most such mechanisms were not anticipated by the Constitutional designers, and so the work of academics and public policy advocates alike remains to design practical means to ensure that business no longer gets the best government money can buy in the United States.

Many strategies are available to firms that seek to manipulate regulation and gain competitive advantage. The explicit literature on strategic use of regulation is now extensive and goes back at least to the 1970s, but similar arguments have populated the literature on regulatory capture for decades. Early work in the area was done by such scholars as Bruce M. Owen and Ronald Braeutigam, Robert Leone, Barry Mitnick, John Mahon, Alfred Marcus, Richard Harris, Donna Wood, David Baron, and George Stigler, among others. These strategies include the following:

Strategic Use of Information

Firms know their costs and their compliance status better than regulators and can shape information responses, withhold information, or flood agencies with information to gain advantage in compliance.

Strategic Use of Litigation

Larger firms tend to have deeper pockets available to support expensive litigation before regulatory agencies and to challenge regulation in the courts. Just the threat of litigation can be enough to deter small firms seeking to be new market entrants in a regulated industry.

Strategic Use of Innovation

Innovation can be used both to lower the costs of compliance to regulation and to gain competitive advantage over other firms subject to the regulation. U.S. auto manufacturers told Congress that there was no technology to reduce emissions as the original Clean Air Act would require. At the same time, each manufacturer was secretly developing the technology. When a Japanese company introduced cars with such technology, Detroit's car companies were quick to follow, apparently pulling the technology out of thin air.

Exploitation of Cross-Subsidies

Under regulation, firms use funds from a more profitable—"creamy"—part of their business to subsidize an unprofitable segment. Prices in the unprofitable segment are deliberately set low, either for competitive reasons or to build support from the group or groups receiving the subsidized prices. Thus, transportation companies set rates low for senior citizens. If threatened with undesired regulation, these companies can warn that the new regulation will make it impossible for them to keep the low rates for seniors. Lobbies for senior citizens then file briefs supporting the transportation companies. The choice of seniors is no accident—a much higher proportion of seniors vote.

Co-optation of Coalition Partners

Besides cross-subsidizing politically powerful customers to defend against undesirable regulation, firms can provide benefits to their stakeholders to build political coalitions for or against regulation, as desired. For example, in Pittsburgh, Pennsylvania, the city's elected leadership has been hostile to billboards for years, viewing them as urban blight. The city's dominant billboard company has donated empty billboard space to nonprofit organizations for limited periods of time for the cost of the sign and a fee for placing it. Whenever a proposal comes before the Planning Commission for restriction of billboards, a host of the city's largest nonprofits show up to testify against the regulation.

Use of the Agency as a Cartel Manager

By setting prices and policing trade practices in an industry, an economic regulator can act as a cartel manager who stabilizes the industry and protects it from new market entrants. The ICC acted in this role by protecting each regulated mode, railroads, trucks, and barges, against new competition from other modes or new entrants. As in the Big John and Yak Fat cases, the modes gain strategic protections by challenging the actions of transportation competitors, using the ICC to defend and enforce their protected activities.

Effective Lobbying

Effective strategic behavior in regulation often includes the adroit use of lobbying. Legislators depend on industry lobbyists for information on issues, and the literature tells us that lobbyists can perform as extensions of the legislator's staff, helping to write speeches, draft legislation, conduct liaison with groups supportive of issues the legislator supports, and so on. Lobbyists are as important in their roles as shapers of issues, defining the public agenda, as they are in providing tangible electoral support in the form of steering campaign contributions and organizing group support. By developing long-term relationships with key legislators, guaranteeing access whenever major regulatory issues need to be advanced or resisted, lobbyists can play a central role in making policy in regulation.

Co-optation of the Experts

Because the administrative process depends on the building of substantial information on the record, and regulated areas tend to cover issues that are technical to the industry, the use of specialists can be essential to effective participation both in that process and in the judicial appeal process. Larger firms with deeper pockets can afford to have a field's top experts on retainer, denying their availability to competitors. Before deregulation, AT&T provided support to many of the country's top experts on communications regulation, potentially making them unavailable to challengers such as MCI.

Trading Off the Agencies/ Choosing Regimes

Firms can sometimes choose their regulators. State regulatory regimes can differ appreciably, so that location decisions can be influenced by state regulations. Federal law in some areas of regulation allows states to have regulations more stringent than federal ones. In essence, firms can choose federal over state regulations by locating in a state that achieved primacy by closely following federal rules. In addition, the granting of primacy by a federal agency does not generally require that a state's regulations be identical to the federal regulations in every respect. Thus firms can track such differences. Finally, some areas of regulation allow a choice between a federal or a state regulator, for example, between establishment as a state mutual savings bank or a federal savings and loan.

Blowing the Whistle

Firms complain to regulators that competitors are in violation of regulatory standards. For example, there are two competing technologies in solid waste disposal: incineration and burial. The companies that specialize in each regularly complain to regulators that their competitors in technology violate air pollution standards on the one hand and effluent or ground water contamination standards on the other.

Regulatory Pork Barrel

Just as firms benefit from building pork barrel projects steered to their districts by legislators, so can firms obtain benefits in the form of regulations tailored to benefit them against their competitors. Thus, tariffs can be designed to raise the costs of imports from competitors. Standards can reflect bias for domestic or district products over international suppliers or competitors elsewhere in the United States.

Conclusion

Although its performance has been questioned, and though it has sometimes been used to divert public resources to private ends, regulation remains a central and essential function of government. It remains a work in progress, and the tasks of both scholars and policy makers in the future will be to devise increasingly efficient, effective, and just social and economic controls worthy of the democracy in which they are embedded.

—Barry M. Mitnick and Kathleen A. Getz

See also Administrative Procedures Act (APA); Airline Deregulation; Archer Daniels Midland; Asymmetric Information; Auction Market; Barriers to Entry and Exit; Child Safety Legislation; Commodity Futures Trading Commission; Consumer Activism; Consumer Product Safety Commission; Consumer Protection Legislation; Corporate Average Fuel Economy (CAFE) Standards; Cross-Subsidization; Deregulation; Employee Protection and Workplace Safety Legislation; Environmental Protection Agency (EPA); Environmental Protection Legislation and Regulation; Externalities; Federal Communications Commission (FCC); Federal Energy Regulation; Federal Reserve System; Federal Trade Commission (FTC); Financial Accounting Standards Board (FASB); Food and Drug Safety Legislation; International Organization for Standardization (ISO); Interstate Commerce Commission (ICC); Iron Triangles; Market Failure; Market Power; Monopolies, Duopolies, and Oligopolies; National Ambient Air Quality Standards (NAAQS); National Highway Traffic Safety Administration (NHTSA); National Labor Relations Board; National Traffic and Motor Vehicle Safety Act; National Transportation Safety Board (NTSB); Nuclear Regulatory Commission; Occupational Safety and Health Administration (OSHA); Pollution Externalities, Socially Efficient Regulation of; Pollution Right; Public Company Accounting Oversight Board; Public Interest; Public Utilities and Their Regulation; Regulatory Flexibility Act of 1980; Revolving Door; Sarbanes-Oxley Act of 2002; Securities and Exchange Commission (SEC); Self-Regulation; Subsidies; Tax Incentives; Transparency, Market; Unfair Competition; U.S. Food and Drug Administration (FDA)

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Regulatory Flexibility Act of 1980

The Regulatory Flexibility Act of 1980 (referred to here as the Act), Public Law No. 96-354, was signed by President Carter on September 19, 1980. The Act had a major impact on the rule-making activities of government agencies as it attempted to minimize any disproportionate effect of federal regulations on small entities. This Act was part of a stream of legislation and executive acts, beginning in the 1970s, that sought to increase the flexibility and effectiveness of federal regulation. A number of new regulatory tools were implemented, sometimes across regulatory issue areas. The Act reflected a newly proposed regulatory design often referred to as "tiering," in which the burdens of regulation were adjusted for the size of the complying organization, so that the burdens faced by smaller organizations would be reduced. Through tiering, compliance would improve because it would become more feasible for small organizations to comply. This design was also viewed as a more equitable way to regulate, because it removed what some viewed as unjust, unreasonable burdens from small organizations. Tiering was sometimes incorporated into regulation via specific size guidelines, for example, being triggered by a specific number of employees such as 25 or 50. In the case of the Act, this size limit was left undetermined, leaving the agencies required to do regulatory flexibility analyses to indicate the appropriate reach of the regulation in question. The Act required all independent federal regulatory agencies and executive agencies to perform various analyses, calculate cost impacts, and evaluate alternatives with regard to the impact of their proposed regulation on small entities. Enforcement of the Act is performed by the Small Business Administration (SBA).

Passage of the Act resulted from complaints from small businesses that were going broke and drowning in federal forms as a result of federal regulations. Prior to 1980, small entities experienced the same burdens of regulations as their larger competitors, but with fewer resources. The Act recognized that the size of a small entity frequently has a bearing on its ability to abide with federal regulations. Compared with larger entities, a small entity may not be able to absorb the costs of complying with a particular regulation. These costs include staff time, direct compliance costs, record keeping, outside expertise, and others. The burden of these extra costs, which may be manageable for larger businesses, may not allow small businesses to set competitive prices, expend funds on development activities, or even remain in business.

The Act had three main goals. The first goal was to improve governmental agencies' understanding and awareness of the impact of their regulations on small entities defined as small business, small not-for-profit organizations, and small government jurisdictions. The second goal was to require agencies to communicate to the public by explaining their findings through various reports. Finally, the Act encouraged agencies to be flexible and provide regulatory relief by attempting to find an easier, less burdensome way for these small entities to comply with the regulations.

When proposing a new regulation, the Act requires governmental regulatory and executive agencies to publish a general notice, then prepare and make available to the public an initial regulatory flexibility analysis (RFA). The RFA was developed to place the burden on governmental agencies to review all proposed regulations to ensure that they do not unduly inhibit the ability of small entities to invent, produce, and compete while accomplishing their intended purpose. The initial RFA contains the objective and legal basis of the proposed rules and describes the agencies it applies to and the requirements for reporting and record keeping. In addition, it contains significant alternative proposals that could satisfy the objectives of the proposed rule at a cheaper cost to small entities and states any duplicative, overlapping, or conflicting federal rules. An RFA analysis is not required if the agency head certifies that their proposed rule will not have a significant economic impact on a substantial number of small entities.

Small entities are encouraged to participate in the development of new regulations and suggest alternatives by responding to the initial RFA. The Act required all regulatory agencies to solicit input from small entities through various means, such as publishing a semiannual regulatory agenda, publishing proposed rules in the Federal Register public forums and notices in industry trade publications, and making direct notifications. After the comment period for the initial RFA, a final RFA must also be made and published along with the final rule. Federal agencies are allowed to establish different compliance or reporting requirements for small entities, including giving them exemptions to the rule and allowing them different timetables for implementations. The final RFA needs to include a summary of public comments received and the action the agency has taken as a result of the comments. In addition, it must include a description of alternative proposals that were considered and rejected by the agencies with an explanation of why they were rejected.

Finally, the Act requires agencies to publish and implement a plan for reviewing existing rules. On a 10-year cycle, all agencies must examine their rules and make appropriate changes to minimize any economic impact these rules have on small entities.

Despite the passage of the Act, the small business community still complained that federal regulations were too numerous, complex, and expensive to implement. The failure of the Act to produce its intended results was partially attributed to the lack of a provision allowing small entities to directly challenge federal agencies' compliance in court. Without any enforcement provision, several agencies chose to not comply with the intent of the Act by certifying that their regulation did not have a significant impact on a substantial number of small entities. Others chose to do as little as they thought necessary to meet compliance, such as trying to satisfy the advance notification requirement by publishing completed actions in the federal regulatory agenda.

As a result of these concerns, Congress passed the Small Business Regulatory Enforcement Fairness Act of 1996 (SBREFA). The SBREFA gave small businesses a voice in the development of new regulations and provided them with assistance in understanding and complying with them. Under the SBREFA, federal agencies were required to produce small entity compliance guides and be responsive to small business inquiries concerning compliance issues. The SBA established the Office of the National Ombudsman and Regional Fairness Boards to investigate small business complaints about federal agency enforcement actions. The SBREFA also allowed small businesses that were unhappy with administrative decisions regarding the effects of regulations to seek judicial review of those decisions and recover attorney's fees and costs when a federal agency was found to have acted excessively in enforcing the regulations.

—Lois S. Mahoney

See also Regulation and Regulatory Agencies

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Rehabilitation Act of 1973

The Rehabilitation Act of 1973 applies to any program that receives financial support from the federal government. As the act states, "disability is a natural part of human experience and in no way diminishes the right of individuals to live independently, enjoy self-determination, make choices, contribute to society, pursue meaningful careers, and enjoy full inclusion and integration in the economic, political, social, cultural, and educational mainstream of American society" (Section 2(a)(3) of the Rehabilitation Act). To that end, the act's purpose is to provide "comprehensive and coordinated state-of-the-art programs of vocational rehabilitation, independent living centers and services, research, training, and demonstration projects" (Section 2(b)). The U.S. Department of Education's Rehabilitation Services Administration (RSA) is responsible for administering the act. The RSA develops and issues program regulations as well as the policy guidelines that support those regulations. The act is enforced at the federal level.

The Rehabilitation Act of 1973 represented a new approach toward providing individuals with disabilities with greater access to the workplace. One major change in policy was the act's requirement that vocational rehabilitation programs make individuals with the most severe disabilities their first priority. In addition, the act promoted consumer empowerment with the requirement that the consumer be involved in the development of the Individualized Written Rehabilitation Program (IWRP) and sign the final plan as an indication that he or she understood it and agreed with it. The act also supported rehabilitation research and independent living centers. Finally, the act mandated that the RSA conduct regular evaluations of programs that fall under the act.

Title V of the act focused on the civil rights of individuals with disabilities. Section 501 requires executive branches of the federal government to develop affirmative action plans for the employment of individuals with disabilities. Section 502 established the

Architectural and Transportation Barriers and Compliance Board. Section 503 prohibits federal contractors and subcontractors receiving $2,500 or more from engaging in employment discrimination against individuals with disabilities. Those with 50 or more employees or a federal contract of $50,000 or more were required to write an affirmative action plan. Section 504 prohibits any federally supported program (e.g., hospitals, school districts, state offices, colleges, and universities) from discriminating against qualified individuals with disabilities.

Since 1973, the act has been amended several times. The Rehabilitation Act Amendments of 1978 further strengthened the call for consumer involvement with an added focus on peer counseling (from peers with the same as well as different disabilities). The Rehabilitation Act Amendments of 1986 enhanced the support for rehabilitation engineering and provided support for special projects and demonstrations, all of which promote new advancements in rehabilitation. The Rehabilitation Act Amendments of 1992 made it clear that the person with a disability should be able to exercise choice and that competitive employment is the ultimate goal. In 1998, Section 508 was added to make information technology accessible to people with disabilities. The Americans with Disabilities Act of 1990 (ADA) built on the Rehabilitation Act's foundation by expanding protections to employers with 15 or more employees, including private, nonprofit, and government entities.

—Ann Buchholtz

See also Americans with Disabilities Act of 1990 (ADA); Disability Discrimination; Employment Discrimination; Equal Employment Opportunity; Equal Opportunity

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RELATIVISM, CULTURAL

Cultural relativism has been given at least two distinct definitions. On the one hand, "cultural relativism" is the view that an individual's beliefs and attitudes are largely shaped by the culture in which he or she lives. Put another way, a culture is the primary source of an individual's views. On the other hand, "cultural relativism" is the view that different societies accept different moral standards, have different moral beliefs, and thus frequently disagree on how to act morally. Both versions of cultural relativism are descriptive claims about the state of the world. Cultural relativism as a descriptive thesis must be kept distinct from ethical relativism. Ethical relativism is a normative thesis that states that one ought to follow the cultural norms of the society in which one lives. Clearly, a person can be a cultural relativist without being an ethical relativist.

Cultural relativism has a long history. The earliest exponent in the West was the Greek Herodotus, who pointed out that the Callatians ate the bodies of their dead fathers while the Greeks burned the bodies of their dead fathers. Both the Callatians and the Greeks were horrified at the practices of the other. Cultural relativism seemed to get a foothold in social science when the discipline of anthropology was born near the beginning of the 20th century. Anthropologists such as Ruth Benedict, Margaret Mead, and William Graham Sumner, among others, documented the widespread differences in ethical practice that existed throughout the world. In the late 20th century, a number of ethicists criticized the reigning ethical theories of utilitarianism and Kantian deontology for ignoring the influence of culture on our ethical beliefs. As a result of such criticism, John Rawls withdrew his claim for a universal theory of justice and announced that his theory was designed for liberal democracies. Assorted feminists and communitarian moral philosophers seemed to subscribe to both versions of cultural relativism defined above. Alasdair MacIntyre's approach based on communitarian virtue ethics was framed from within a cultural relativist standpoint. This emphasis on the role of culture was also a prominent feature of the advocates of postmodernism—a group of thinkers that went well beyond philosophers. In business ethics, Patricia Werhane, in expanding on the importance of moral imagination in ethical decision making, noted that one of the impediments to moral imagination was the tendency to think that we Americans had discovered the correct version of capitalism and that our form of capitalism could be exported to all other countries around the world. The failure of some prominent American professors to recognize the cultural parameters of American capitalism led them to give the Russians rather bad advice as they transitioned from communism to capitalism. In the context of Russian culture at that time, American capitalism became, in Russia, a lawless kind of capitalism often referred to as "Cowboy Capitalism."

At first glance, the descriptive claims of cultural relativism seem to be true. Even in today's "global society," there are widely different moral beliefs regarding what is right and what is wrong. Terrorists think the killing of civilians is morally justified. "Civilized" societies think that such practice is morally heinous.

But are the claims of descriptive cultural relativism true? There are plausible reasons to doubt the truth of cultural relativism. First, the underlying disagreement may not be a disagreement about ethical beliefs but may rather result from a disagreement about the facts on which the ethical beliefs are based. For example, those who think that the development of nuclear power plants is morally permissible and those who think their development is not morally permissible may disagree on the likelihood of a catastrophic accident at one or more of these nuclear power plants.

Second, the disagreement could be about conceptual issues rather than about moral judgments. For example, both sides in a dispute could agree that it is morally wrong to kill an innocent person but disagree as to what constitutes a person. At least some of the debate surrounding abortion, certain forms of birth control, and certain types of stem cell research are debates about what counts as a person.

The greatest challenge to the truth of cultural relativism is the possibility that there may be underlying principles behind the divergent moral practices and beliefs that might be held in common. If that were true, there would be universal agreement on the fundamental underlying ethical principles even though these universal principles might legitimately be applied differently in different cultural circumstances. This point can be illustrated by taking two of the basic principles from the two dominant ethical theories. Suppose we take the key principle of utilitarianism—that we should adopt the social practices and institutions that create the most good—as the underlying principle. It does not take much imagination to see how that principle could be applied very differently in different cultural circumstances.

The same type of analysis would work for someone who adopts a deontological point of view. Suppose one adopts as a fundamental moral principle the respect for person principle; that principle may indeed be accepted in all cultures, although what counts as respecting persons differs in different cultures. This point can be illustrated by the earlier example concerning the Callatians and the Greeks. Both demonstrated respect for their dead fathers but in radically different ways.

In addition to this theoretical consideration, international organizations have agreed, or are meeting to agree, on international standards. Perhaps the most familiar set of international standards is the United Nations Universal Declaration of Human Rights. Every member of the United Nations has accepted these standards as a condition of membership, and most of the countries in the world are members of the United Nations. Having said this, the member countries of the United Nations often disagree as to how to honor these human rights, and they disagree as to whether a given country has violated those rights. For example, the United States and China often accuse one another of violating one or more of the UN's stated human rights. For example, the United States has accused China of violating Article 5, which stipulates that no one should be subjected to torture or to cruel, inhuman, or degrading treatment or punishment. The basis of this charge is the allegation that China harvests the organs of executed criminals. (It should be noted that many accuse the United States of being in violation of Article 5 because it permits capital punishment.) On the other hand, China takes the existence of the large population of homeless people in the United States as showing that the United States is in violation of Article 25, which provides that everyone is entitled to a standard of living that includes food, clothing, housing, and health care. Whether these disagreements are fundamental or are differences in applying human rights in different circumstances is a matter of controversy.

The United Nations Declaration of Human Rights is not the only example of an attempt to develop universal standards. The International Labour Organization sets international standards regarding the treatment of labor. Other examples include the Rio Declaration of Development and the Environment and the United Nations Convention Against Corruption. These international agreements provide the basis for the 10 principles of the United Nations Global Compact. The UN Global Compact asks companies to embrace, support, and enact a set of core values in the areas of human rights, labor standards, the environment, and anticorruption. There are also a number of international agreements that govern business conduct in certain industries, such as the Fair Labor Association, which sets standards for the apparel industry as members of that industry outsource to "sweatshops." How extensive these international agreements turn out to be remains in doubt. However, it is significant to note that in this era of global capitalism, there is a growing recognition of the need for international standards governing business conduct.

The tendency to develop international standards is not the only challenge to cultural relativism. The very notion of cultural relativism suffers from certain conceptual ambiguities. First, what constitutes a culture? Some might argue that a common language is indicative of a culture. However, consider the United States. Suppose one were asked to identify the characteristics of American culture. What could be said? The United States is considered to be a highly pluralistic culture. This means that there are many cultures within the United States, and perhaps this means that there is no one identifiable culture of the United States. The country is even becoming bilingual or multilingual. For many Americans, Spanish is the language of choice, and in an increasing number of places, public instructions in airports, subways, and so on, are given in both English and Spanish. One of the first items on the menu when you try to conduct business on the phone is whether you wish to speak in English or Spanish. On the other hand, English is becoming the universal language—or at least the universal language of business—worldwide. Thus, identifying a culture is an increasingly problematic activity.

But to the extent that one can identify a culture, it is the existence of a certain minimal morality that makes such an identification possible. Suppose an anthropologist arrives on a heavily populated island and wants to know how many tribes are on the island. One key to answering that question is to ask whether the people on the northern part of the island are permitted to kill, steal, and commit violence against those on the southern part of the island. If they are, then there are at least two tribes. If they are not, you have evidence that there is only one tribe. Thus, what constitutes a culture, at least in part, is that the members of the culture practice a certain minimal morality with respect to one another. Killing, stealing, and wanton acts of violence are not permitted among members of the culture. Thus, rather than simply saying that different cultures have different moral customs, we also need to say that for any culture to be a culture there is a certain morality that must be practiced by members of the culture.

All these considerations indicate that the simple descriptive claim that different cultures have different moral practices is much more complex than it appears.

Despite these criticisms of the simple descriptive claim of cultural relativism, the continued existence of different ethical standards among people reminds us to be cautious in asserting the correctness of our own moral standards in all circumstances. We must also remember that differences in geography, population density, and economic development, among other factors, require that any universal standards need to be applied taking such factors into account. An appreciation of cultural diversity here reminds us that when circumstances such as the global conduct of business seem to require universal standards, then these standards need to be negotiated among the relevantly affected parties. Universal standards are more likely to be created than to be discovered.

—Norman E. Bowie

See also Cultural Imperialism; Globalization; Human Rights; Multiculturalism; Pluralism; Postmodernism; Postmodernism and Business Ethics; Rationality and Ethics; Situation Ethics; United Nations Global Compact

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Relativism, Moral

Definitional Issues

Moral relativism is a theory that can be applied to individuals, to cultures, or to moral theories themselves. At the individual level, individual moral relativism would argue that whatever an individual thinks is right or wrong really is right or wrong for that individual. A popular expression of this view is, "What's right for me is right for me and what's right for you is right for you." In philosophical discussions of ethical theory, this view is either identical with or closely allied to the doctrine of ethical subjectivism. Since most philosophers think that ethical subjectivism results in the very denial of the possibility of ethics as the term is normally understood, it will not be discussed further here. At the level of moral theory itself, moral relativism would argue that there is no ethical theory that is really objective. An ethical theory is objective when there are independent reasons that provide for its truth of adequacy. The key here is justification by reason rather than authority, be it personal charisma or cultural norm. Moral relativism at this level is an example of metaethical moral relativism since it denies the possibility of this form of rational justification. One needs to ask whether metaethical moral relativism is a moral theory (it seems that it is) and, thus, whether it is put forth as an objective moral claim. If so, it seems that metaethical moral relativism would contradict itself. If it is not put forward as an objective moral claim, why should any moralist pay attention to it?

Most moral philosophers discuss moral relativism at the level of cultures, and that is the focus of this discussion. At the cultural level, moral relativism is the normative ethical theory that says that what is really right or wrong is what the culture says is right or wrong. In other words, it is culture that determines the criteria for right and wrong. Thus, if the culture of Sweden has a norm that accepts the moral permissibility of abortion, then abortion really is morally justified in Sweden. If Ireland has a norm that abortion is wrong, then abortion really is wrong in Ireland, and it cannot be morally justified. In matters of right and wrong, culture is the ultimate judge but it is only the judge for that culture.

Moral relativism must be distinguished from cultural relativism, with which it is sometimes confused. Moral relativism is a normative ethical theory that is meant to instruct as to what is really right or wrong. Cultural relativism is a descriptive thesis that says that moral practices differ among cultures. Cultural relativism is a factual claim about the world.

Reasons for Adopting Moral Relativism

In the late 1800s and early 1900s, American politics was dominated by the doctrine of manifest destiny—namely, that America's destiny was to spread democracy, capitalism, and Christianity throughout the world. At about the same time, the discipline of anthropology was born. Early anthropologists included William Graham Sumner, Ruth Benedict, and Margaret Mead. These pioneers and others discovered a great variety of customs regarding morality throughout the world. What was considered moral in one place was almost always considered amoral or immoral in another. As an antidote to the cultural imperialism of manifest destiny, these social scientists and others urged a greater toleration of the moral customs of others. Thus, one reason for adopting moral relativism, some would argue, is that it encourages a healthy toleration of diverse moral customs—a toleration that is pragmatically necessary in a pluralistic world and cosmopolitan business environment.

Another reason for adopting moral relativism is to use it as a counterweight to cultural imperialism. There is a natural human tendency to think that one's culture has the correct morality and that other cultures are either backward or irrational in some way. Ethical relativism is an antidote to this tendency to think that one's culture has all the moral answers and that other countries are mistaken or misguided on matters of ethics. Some would argue that this counterweight is especially required in the United States in the early years of the 21st century. Many believe that when Americans speak of universal standards or universal human rights, they often identify these universal standards or universal human rights with American standards. The adoption of cultural relativism would be a corrective to this tendency. After all, if moral relativism is correct, there is no standard for right or wrong beyond the culture itself, and, thus, there is no basis for Americans to claim that their moral customs are the correct ones for cultures with different views.

Yet another reason for adopting moral relativism is the vast disagreement among moral philosophers and other thinkers about ethics as to which ethical theory is the correct one. Although all the major theories have their partisan defenders, it is easy for one to argue that all this disagreement simply shows that one cannot do better than one's culture as a source of ethical justification. Since the major ethical theories allegedly give different answers as to what is wrong, what is more reasonable than using culture as the default position?

Difficulties With Moral Relativism

Despite the reasons that have been given for adopting moral relativism, nearly all ethical theorists in philosophy reject it. Some defenders of cultural relativism have been tempted to use the alleged fact of cultural relativism to justify moral relativism. Those who attempt this approach argue that since it is true that moral practices differ among cultures, then what is really right or wrong depends on the culture. But the mere existence of cultural difference does not establish the truth of ethical relativism. After all, it is possible for a culture to be wrong about a matter of ethics, and if so, then it would not be the case that what is really right or wrong in that culture is what the culture says is right or wrong. Another way of showing the error involved is that one cannot derive an ought (what is really right or wrong is what the culture says is right or wrong) from a fact (there are differences among cultures with respect to what is right or wrong).

Moral relativism also is inconsistent with how we actually discuss ethical issues. First, if moral relativism is correct, there is no way to settle or even to rationally argue about conflicting moral practices in different cultures. If what is really right or wrong is what the culture says is right or wrong, then that seems to be the end of the discussion. Yet in the many debates among countries regarding matters of ethics, public policy, and business, people talk like objectivists in ethics and not like ethical relativists. If a country practices torture of criminals, the citizens of other countries that have a moral norm against torture do not say, "well, if torture is considered right in that culture, it really is right in that culture although it is surely wrong in our culture." Rather they say that torture is really wrong everywhere, even in countries where it is morally permitted. In other words, moral relativism is inconsistent with how we talk.

The moral relativist might reply that one certainly could criticize another culture. Indeed one might even persuade another culture to change its moral practice in some regard. In other words, there is a place for argument and even a place for moral reform. But notice how strange a discussion of reform would look if one is an ethical relativist. So long as the culture subscribes to the moral norm that the critic is challenging, that norm still really determines what is right or wrong in that culture. The plausibility of the critic's argument does not count until the cultural norm changes. If the critic is successful and moral practice changes, then what was right (wrong) in the culture becomes wrong (right). But this is surely a strange way of talking. Consider the practice of slavery in the Southern United States. If moral relativism is correct, then slavery was morally right in the South until the moral norm changed. But wouldn't we say that slavery was always wrong; it was never right even if it was accepted in the Southern United States.

There are also difficulties with the claim that the adoption of moral relativism would promote tolerance. First, the extent to which we should be tolerant and to which cultures we should be tolerant is controversial. (We should not tolerate cultures that endorse terrorism, for example.) Second, note that appealing to tolerance is to appeal to a cross-cultural moral concept. Not all cultures believe that one should be tolerant, and if ethical relativism were the correct moral theory, then they would be right. Thus, those who defend the value of tolerance and urge that nontolerant cultures be more tolerant are appealing to a moral norm that cannot be defeated by the fact that some cultures are not tolerant.

Moral Relativism and International Business

The leaders of multinational enterprises face genuine business issues when they wrestle with cultural relativism. The variables they must consider include the culture in their home country—the place where they are headquartered, their corporate culture, and all the cultures in the countries where they do business. Should they adopt moral relativism, or, as it is often expressed in business, "When in Rome, should they do as the Romans do?"

One might think that the obvious position to adopt is that of moral relativism. In this way, businesses can adapt to local custom and not be seen as cultural imperialists. In this way, they could be more competitive. But the issue is more complicated than that.

Many multinationals believe that a strong brand gives them a competitive advantage. What makes a strong brand? Obviously the quality of the product is a major contributing factor. But a strong brand depends on more than that. The reputation of the company is important as well. A well-defined set of corporate values, a specific mission statement, and an ethical corporate culture are components of a corporation's reputation, and these in turn contribute to a strong brand. Nike provides an excellent example.

Multinational corporations try to avoid the following dilemma: doing business abroad in a way that opens them up to moral criticism at home. Many of the sportswear and apparel wear corporations such as Nike found themselves in just this dilemma when they were criticized in their home countries because of the labor practices of their suppliers. The suppliers were accused of mistreating their workers and of paying wages that would not provide a minimum standard of living. In other words, these multinationals were using sweatshop suppliers. Companies such as Nike did not respond to their moral critics at home by invoking cultural relativism. They were not content to simply reply that they were merely following the norms of cultures that happened to differ from the home culture. Rather, to protect their brands and to keep a level competitive playing field, they worked together and with their critics to establish a set of ethical standards that would apply to all their suppliers wherever these suppliers might be located. In other words, an industry standard was developed that transcended the norms of the suppliers' cultures.

In the European Union, the guiding principle, if not universal practice, is that corporations should practice sustainability. A corporation's business practices are sustainable if they are financially sound, environmentally friendly, and socially responsible. These are the three pillars of sustainability. For most Europeans, the key element in social responsibility is to be in conformity with and supportive of human rights. Reference here is usually to the United Nations Declaration of Human Rights.

The challenge is especially great when multinationals do business in countries that systematically violate human rights. Certainly, companies themselves should not violate human rights. But many would go further. They would argue that multinationals should not do business in countries that violate human rights. This demand is not new. Many companies left South Africa when that country practiced the form of racial discrimination known as apartheid. Lately, many multinationals will not do business in Myanmar (Burma) because the government of that country systematically violates human rights.

Thus, most multinational corporations do not practice moral relativism. They will not subscribe to cultural norms in host countries when those norms are inconsistent with the fundamental values of their own company. They are also cognizant of critics in their home countries who would condemn business practices that violate home country norms or universal norms as found in the United Nations Declaration of Human Rights.

Nonetheless, multinationals are well aware that they cannot practice ethical imperialism. Multinationals need not insist that business be done in every respect the way the multinational or the home country of the multinational would do it. As two prominent business ethicists have argued, there is a certain amount of moral free space where practices are not in violation of any universal norms even if the practices violate the norms of the home country or the company. Gift giving (as opposed to bribery) in many Asian countries, especially Japan, is a good example of a practice that is morally permissible there even if it is frowned on in the United States. In Japan, it is morally permissible and good practice to participate in the culture of gift giving.

The struggles of multinationals to deal with the "When in Rome, should you do as the Romans do?" problem illustrates the strengths and weaknesses of moral relativism. On some occasions, a multinational should not follow the moral norms of the host country but rather should follow the moral norms of the corporate culture or should follow norms that are considered universal. For these reasons, ethical relativism cannot be the sole guide. On the other hand, multinationals should not be moral absolutists. They should not think that there is one and only one morally correct way to practice the moral life. There is an important place for the universal value of toleration and for moral free space where different moral norms in different cultures are all morally permissible.

—Norman E. Bowie

See also Global Codes of Conduct; Human Rights; Relativism, Cultural; United Nations Global Compact

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Religious Discrimination

Discrimination, in its etymological sense, means the action and effect of making a distinction, or differentiating one person or thing from another. Discrimination itself is not morally wrong. When a company selects personnel, discrimination occurs in accordance with the profile required for the job, and this is not necessarily incorrect in ethical terms. However, in talking about discrimination, this word generally has a negative connotation, meaning “invidious discrimination.” In this sense, the common meaning of “discrimination” includes a judgment based on unacceptable ethical or legal motives, one of which involves religion.

Religious discrimination takes place when one person is treated less favorably than another is, has been, or would be treated in a comparable situation on the grounds of religion. The prohibition of religious discrimination covers most social activities, including business.

Three forms of religious discrimination can be distinguished: (a) *direct,* where this less favorable treatment occurs unmasked, (b) *indirect discrimination,* where an apparent neutral provision, criterion, or practice would put persons having a particular religion or belief at a particular disadvantage compared with other persons, unless such is objectively justified by a legitimate aim and the means of achieving that aim are appropriate and necessary, and (c) *religious harassment,* which occurs when unwanted conduct related to any of the grounds of religion takes place with the purpose or effect of violating the dignity of a person and of creating an intimidating, hostile, degrading, humiliating, or offensive environment.

Many international human rights doctrines have articulated the freedom from religious discrimination as a human right. However, people in many theocratic countries deny the importance of such a right and maintain the criteria of adherence to the official religion as essential in filling leadership roles in society and business. This commitment is founded on a belief in the fundamental rightness of their faith, which overrides the standards of rational ethics, as defined by Western philosophers and political theorists. Freedom from religious discrimination is closely related to another even more fundamental right: religious freedom. Religious freedom is seen as necessary for carrying out the moral duty to search for the truth, especially with reference to God, religion, and a meaningful sense of life. It also provides protection for those who do not believe in God to adhere to their own beliefs.

Religious freedom requires immunity from coercion for individuals and social groups, including businesses, governments, and any other human power, which can be forced to act in a manner contrary to their own beliefs. Religious discrimination impedes or even prevents religious freedom and frequently entails the disdaining of people and lack of respect for individual freedom.

Significant International Texts and Legislation on Religious Discrimination

There are significant international declarations against religious discrimination. In 1948, the General Assembly of the United Nations adopted and proclaimed the Universal Declaration of Human Rights, in which Article 2 states that everyone is entitled to all the rights and freedoms set forth in the Declaration, without distinction of race, color, sex, language, religion, or political or other opinion. Article 16 adds that everyone has the right to freedom of thought, conscience, and religion. In 1981, in a more specific way, the General Assembly adopted the Declaration on the Elimination of All Forms of Intolerance and of Discrimination Based on Religion or Belief.

Prohibitions against discrimination on grounds of religion are also present in the legislation of the United States and other countries. Title VII of the U.S. Civil Rights Act of 1964 makes it unlawful for employers to discriminate against any individual on the grounds of religion. With the Equal Employment Act of 1972, the U.S. Congress amended Title VII requiring that employers reasonably accommodate the religious preferences of employees when this can be done without undue hardship when the employees are conducting the employer's business. In addition, it clarified that the term *religion* includes all aspects of religious observance and practice as well as belief. The Workplace Religious Freedom Act of 2003 also amended Title VII of the Civil Rights Act of 1964 to establish provisions with respect to religious accommodation in employment. In Europe, the Council Directive 2000/78/EC establishes a general framework for equal treatment in employment and occupation prohibiting, among other things, discrimination on grounds of religion or belief. Its prohibitions included the types mentioned above: direct and indirect discrimination and religious harassment. Since 2003, national legislation in European Union member states has been used to develop the implementation of this directive.

From both legal and ethical perspectives in the Western tradition, it can be stated that freedom from religious discrimination is an important right, which should be respected and fostered, but it is not an absolute right and, in certain circumstances, another right may have priority when a conflict arises.

Freedom From Religious Discrimination in the Workplace

The problem is that religious discrimination is a constraint to employers' freedom in hiring, promotion, dismissal, and work conditions within a company, and conflicts can arise. Nondiscrimination on religious grounds requires the employer to provide reasonable accommodation to an employee's sincere religious beliefs, unless this accommodation would cause an undue hardship to the company. From a legal perspective, at least in the United States and in the European Union, this is also mandatory. However, not only the employer but also the employee should make an effort to arrive at a reasonable solution to avoid religious discrimination.

In practice, it is difficult to establish clear rules about what a "reasonable accommodation" and an "undue hardship" are. Determining them requires common sense and practical wisdom to explore imaginative and fair alternatives. Legal cases and empirical information can help to find an appropriate solution in each situation, which is compatible with the employee's religious beliefs without compromising the employment entitlements of other employees and with minimal costs to the enterprise.

Undue hardship is generally evaluated by considering the damage that religious discrimination would cause. It is assumed that avoiding religious discrimination could have a cost, but this cost has to be reasonable. This is not because profits are intrinsically more important than people, but profits are related to other people's interests and rights and perhaps to the competitive continuity of a business, which obviously affects people's well-being. The Workplace Religious Freedom Act of 2003 clarifies that, for legal purposes, the term *undue hardship* means an accommodation requiring significant difficulty or expense, including (a) the costs of loss of productivity and of retraining or hiring employees or transferring employees from one facility to another; (b) the overall financial resources and size of the employer involved, relative to the number of its employees; and (c) for an employer with multiple facilities, the geographic separateness or administrative or fiscal relationship of the facilities. From an ethical perspective, these criteria could also be valid. These legal criteria provide an insight to aid sound ethical judgments in specific situations.

There are some kinds of businesses or organizations in which a certain religious belief could be necessary because a religious orientation is an essential part of the organization's mission. This is the case, for instance, with religious institutions, which require appropriate people to carry out their mission properly. Similar reasoning could be extended to some key positions in educational or medical centers that define themselves as organizations with a religious mission. U.S. legislation explicitly allows religious discrimination for religious institutions. In Europe, this is not so explicit, but it can also be justified.

Some Specific Issues

Religious Feasts, Worship, and Prayers

Most religions have feast days in reverence to divinity, during which adherents pray, worship, and enjoy the day in particular ways. Jews celebrate the Sabbath, as the weekly Lord's day, remembering the seventh day of Creation, on which, according to the Bible, God rested. According to Jewish tradition, Jews shouldn't work on Saturday, and some Jews do not work past sundown on Friday afternoon. Christians consider Sunday as the fulfillment of the Sabbath, because this is the day of Christ's Resurrection. They participate in the Eucharist or other religious services and abstain from working. For Muslims, Friday is the day they meet to pray in mosques.

Apart from this, most religions have special festivals or periods of time with special religious significance. In addition, Muslims generally have to make a pilgrimage to Mecca once in their lifetime. In many companies, it has been not so difficult to accommodate business schedules to holy days or to religious duties on these days, through a sense of comprehension and flexibility and a good rotation system.

However, some managers think that praying five times a day, which is required in Islam, could be more difficult to harmonize with production needs. It could even be disruptive and cause resentment among other employees, especially in societies in which Muslims are a minority. In spite of this difficulty, some companies have found solutions based on goodwill of both employer and employee.

Dress and Grooming Policies

Certain business policies, compulsory for every employee, can pose dilemmas of religious discrimination. Thus, dress requirements in some companies, such as those for people in transportation, security guards, fast-food workers, and so on, can conflict with the practices of Sikh employees who wear headscarves or turbans for religious motives. A successful solution has been to permit wearing headscarves or turbans, while maintaining the rest of the required uniform.

Another conflict could appear when the workplace requires certain clothing and an appearance that may conflict with certain religious beliefs (e.g., that women should keep their legs and head covered at all times). Sometimes, as long as no damage is done to the business, companies admit a certain degree of flexibility in clothing requirements to avoid religious discrimination, but this is not always possible. In such cases, management generally prefers making this point clear when contract conditions are discussed.

Handling Food

Some religious practices, such as wearing a beard or having long hair can conflict with health and safety requirements. Some clear regulations on this point help us to find solutions. Those who handle food need to keep long hair tied back or otherwise restrained. A hygienic head cover for long hair and a net for long beards are generally accepted as a reasonable accommodation.

Training Programs

Some specific training programs, for instance, those based on New Age spirituality, can pose a problem. These programs employ a variety of techniques (meditation, self-hypnosis, altered states of consciousness, and guided visualization) that can conflict with the employees' religious beliefs. These kinds of training programs, which are not too common, have been declared noncompulsory by courts on grounds of religious discrimination.

Religious Symbols

Forbidding discreet religious symbols is generally understood as religious discrimination. A more complex case arises when certain symbols might seriously annoy or offend other employees or customers. In this latter situation, some people suggest employing common sense and flexibility to arrive at the best solution for both sides, and, in practice, it is not too difficult to find solutions that work for all.

Free Speech and Proselytism

Free speech on one's own religion and even respectfully trying to persuade others about religious matters without neglecting business obligations is normally allowed. However, proselytizing using harassment, especially if it comes from a supervisor, is a different matter. Harassment is a form of religious discrimination, as has been mentioned above.

Being aware of situations of religious discrimination, such as those described here, means respecting human freedom. This helps avoid expensive trials, negative corporate image, and loss of reputation.

—Domènec Melé

See also Christian Ethics; Civil Rights; Employment Discrimination; Human Rights; Kantian Ethics; Rights, Theories of

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Religiously Motivated Investing

Religiously Motivated Investing and the Socially Responsible Investment Community

Religiously motivated investing (RMI) is a rapidly evolving core component of the larger socially responsible investment community. Understanding the contextual nuances of RMI and its placement within this community requires a brief overview of socially responsible investing itself. The term *socially responsible investing* (SRI) encompasses an investment strategy whereby financial contributions are placed into investment vehicles designed to combine the traditional investment philosophy favoring profit maximization with values-based component-seeking nonfinancial benefits. Such nonfinancial benefits are often referred to as social returns. These social returns vary in scope but may be broadly defined as corporate policies and actions that enhance a socially responsible investor's specific environmental, religious, or social values. It is important to note that such enhancements may or may not have any impact on the profit-maximization component of the socially responsible investment. Therefore, a successful socially responsible investment portfolio will appreciate in value over a specific time period (when compared with an appropriate financial benchmark or to returns from a traditional and similarly situated investment portfolio) while also significantly advancing an investor's specific social values. A quasi-successful SRI portfolio may earn substandard financial returns but successfully advance an investor's specific social values—a result acceptable to many socially responsible investors. Although *socially responsible investing* is the most common term for this practice in the United States, the concept is also referred to as ethical investing (primarily in the United Kingdom and Australia), moral investing, or values-based investing.

Today, major institutional investment groups such as corporations, hedge funds, insurance companies, mutual funds, pension funds, religious institutions, and universities, along with the environmentally/religiously/socially motivated individual investor, are becoming increasingly involved in SRI. Similar to the traditional investment community, religiously motivated investors take advantage of three distinct investment strategies to advance their investment goals: (1) social screening—the affirmative investment in (or divestment of) companies meeting (or failing to meet) predetermined social investment objectives; (2) shareholder advocacy—a process by which investors choose to initiate discussions with company management, sponsor or cosponsor shareholder resolutions, or boycott company products or services in an effort to induce company management to modify policies in accordance with specific social objectives; and (3) community investment—where investment funds are channeled directly to communities where such resources have been historically scarce with the intention of fostering regional economic development.

At the dawn of the 21st century, the SRI industry claims that more than $2.16 trillion is invested in professionally managed portfolios implementing at least one of the three SRI investment strategies mentioned previously. This figure, touted as representing one out of every nine dollars invested professionally in the United States, grew from $1.19 trillion in 1997 and from $40 billion in 1984. It is important to note that many scholars remain skeptical of the accuracy of these figures and toward the effectiveness and widespread use of SRI. While many peer-reviewed academic studies demonstrate that SRI earns substandard returns and is merely growing in pace with the traditional investment strategies, other studies demonstrate that SRI is becoming more prominent and that socially responsible investors are increasingly able to achieve desired social objectives while also earning competitive returns as compared with traditional investment philosophies.

Three Core Classes of SRI Investors

SRI is an umbrella concept covering three core areas of socially responsible investment: (1) environmentally motivated investing (EMI), (2) RMI, and (3) socially motivated investing (SMI). While investors from all three core groups seek social returns along with capital appreciation, the major difference between these investors stems from the motivations behind their investment practices. Environmentally motivated investors generally seek to invest in companies where corporate policies and actions either benefit, or do no significant harm to, the global or local environment. Issues such as global warming and deforestation often top the agenda of EMI. Religiously motivated investors are generally guided by issues central to their particular religious traditions. Historically, core RMI issues revolved around alcohol, gambling, and tobacco and have recently encompassed human dignity and antifamily entertainment as well. Socially motivated investors, not specifically motivated by environmental or religious issues, generally invest in companies whose policies and practices adequately address key contemporary social issues such as diversity, discrimination, and corporate governance. Although these distinctions make for a clean categorization of investment motivations, they are not perfect representations of the SRI community overall. For instance, the investment strategies of many religiously motivated investors may focus on issues more commonly found in the environmentally or socially motivated investment communities. In fact, at any time, a socially responsible investor may be interested and invested in companies dealing with issues important to all three core SRI groups. While such issue crossovers commonly occur, at any given time the majority of socially responsible investors can be classified as primarily pursuing EMI, RMI, or SMI.

Religiously Motivated Investing: In-Focus

Members of the RMI community hail from diverse religious philosophies; for instance, the Catholic Sisters of Charity of Cincinnati have emerged as effective shareholder advocates, while managers of the Amana Mutual Funds are expanding the practice of investing according to Islamic investment principles. Although various world religions can stake a claim to investing according to their religious practices, the most prominent RMI investors come from the Christian, Islamic, and Jewish religious traditions. Historically, a less sophisticated form of RMI emerged in America during the early 20th century as certain religious groups—specifically the Methodists and the Quakers—expressly avoided investing in companies dealing in alcohol, gambling, or tobacco, also known as the "sin stocks." The contemporary history of RMI began in the 1960s as certain groups of religiously motivated investors, opposed to the Vietnam War, screened from their portfolios companies involved in the production of weapons or military-related products. In the 1980s, religiously motivated investors joined forces with many other socially responsible investors urging divestment from companies involved in supplying products or services to or within the apartheid regime in South Africa. The tobacco-related litigation of the 1990s shed light on this key RMI issue as religiously motivated investors lobbied for additional restrictions on the production, distribution, and selling of tobacco and tobacco-related products. At the turn of the 21st century, areas such as human dignity (sweatshop and child labor) and antifamily entertainment (graphically sexual or violent programming in television, movies, or video games) are beginning to garner the attention of the religiously motivated investment community, while the traditional avoidance of sin stocks remains prominent.

RMI emerged as a specific investment philosophy as religious adherents began to realize that companies included within their investment portfolios were not operating in accordance with their religious beliefs. While continually striving to incorporate specific religious philosophies into their everyday activities, friendships, relationships, and careers, these investors were either unconcerned or unsure what products and services their investment dollars were promoting. To remedy this contradiction, these investors began to incorporate their religious beliefs into their investment philosophies. Today, to make their investment strategies compliant with their religious tradition, religiously motivated investors look to their religious philosophies, sacred texts, and community religious leaders for guidance in determining the issues on which they will focus their investment energies. Once these core issues are selected, religiously motivated investors commonly undertake a combination of the key SRI strategies of social screening, shareholder advocacy, and community investment.

RMI and Social Screening

Similar to contemporary EMI and SMI groups, religiously motivated investors use social-screening techniques to develop their investment portfolios to meet predetermined religiously motivated objectives. While this practice involves a small amount of screening specific companies into portfolios (positive screening), the majority of RMI groups screen from their portfolios companies not meeting their social standards (negative screening). Such negative social screening results in an investment portfolio free from companies whose policies contradict moral principles of the particular investor's religious tradition. Today, issues such as human dignity and antifamily entertainment combine with companies' dealings in alcohol, gambling, and tobacco as the most common negative screens for religiously motivated investors.

RMI and Shareholder Advocacy

Religiously motivated investors also use common shareholder advocacy tactics, including discussions with management, shareholder resolutions, and boycotts attempting to move corporate policies closer to specific religious investment objectives. While alcohol, gambling, and tobacco remain potent issues for RMI shareholder advocacy, the same emerging issues found in the screening process are often subjected to advocacy practices as well. For example, major religiously motivated investors, led by a Catholic group, recently cosponsored a shareholder resolution at the Walt Disney Company urging company executives to analyze and report how the prominent placement of smoking in television commercials and movies negatively influences society—particularly teenagers. Another Catholic investment group recently urged a major Fortune 500 company to report on the economic effects—both foreign and domestic—of its foreign weapons and weapons-related sales.

In addition to the predominantly RMI issues, religiously motivated investors are also concerned with mainstream EMI and SMI issues. A recent example of this cross-interest emerged out of the recession of 2001 and the renewed focus on corporate governance. During 2005, Baptist, Catholic, and Methodist investment groups cosponsored shareholder resolutions alongside socially motivated investment groups advocating for the separation of the chief executive officer and board chairperson roles and an analysis of excessive executive compensation. In addition, allying with environmentally motivated investment groups such as the As You Sow Foundation, the Adrian Dominican Sisters advocated against genetically modified organisms that may allow dangerous substances into the world's agricultural environment. These groups cosponsored a shareholder resolution asking the DuPont Company's board of directors to review the company's internal controls and report to shareholders concerning the potential impact on the worldwide seed market and risk management.

RMI and Community Investment

Religiously motivated investors are increasingly joining the community investment movement by providing financial assistance in communities traditionally underserved by financial institutions in an attempt to stimulate economic development. RMI groups are among the many SRI community groups allocating funds into Community Development Financial Institutions (CDFIs) to provide affordable housing, entrepreneurial microloans, and job opportunities where such opportunities have been historically scarce. In 2001, the Social Investment Forum—a national nonprofit SRI trade association—issued the 1% Mark challenge. This challenge urged the entire SRI community to invest at least 1% of their assets into community investment programs. In 2002, The Mennonite Mutual Aid Praxis Mutual Funds became the first religiously motivated investment group to achieve the 1% Mark challenge goal.

—Corey A. Ciocchetti

See also Christian Ethics; Islamic Ethics; Jewish Ethics; Social Investment Forum; Socially Responsible Investing (SRI); Stewardship

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RENT CONTROL

Rent control refers to laws or ordinances that regulate how much landlords can legally charge for their property. In its simplest form, there are two approaches to rent control. The first approach is that a "fair rent" is fixed for every unit and that an enforcement mechanism is established to ensure that these rents are in fact charged. The second form of rent control is a "control on rent increases," regardless of the current rent level. Rent control was established to protect renters from excessive rent increases, especially if such an increase could lead to renters being forced out of the premises. As such, rent control was intended to help renters, especially indigent ones, by allowing them to continue living in areas which otherwise would be too expensive for them to afford since rents would be too high for their level of income. In fact, rent control is often enacted in times of severe housing shortages and steep rent increases, for example, due to war or hyperinflation. Rent control is an international phenomenon and exists in both developed and developing countries.

In a free market, rent is the result of supply and demand for a rental property. However, rent control fixes this outcome at an artificial level, thus creating an imbalance between supply and demand. Even so-called second-generation rent control, which is when landlords are allowed to escalate rent in certain situations, will lead to such an imbalance. For rent control to achieve its desired outcome of creating more affordable housing for lower-income renters, the market rent in equilibrium would have to be higher in the absence of rent control than it is in its presence.

Factors of supply and demand along with the lack of income constraints often limit the effective matching of lower-income families with restricted income properties. Because of the reduced prices landlords must accept for their investment, new investment in rental properties is discouraged. This resistance to investing in rental property creates a shortage of these properties. Since there are fewer rental properties than the market demands, the landlord has more renters from which to choose.

On the other hand, rent control can create an excess demand for rental properties. This excess demand comes from two groups of renters. The first group consists of those renters who prefer renting over buying since rents are kept artificially low. In some situations, these renters have been known to use their financial resources to buy other property while continuing to live in rent-controlled apartments. The individuals then rent out the purchased property, generating personal income, while maintaining residence in the rent-controlled apartment.

The second group consists of those renters who are attracted to the area with the low rent-controlled prices and are willing to commute. Even with the added expense of commuting, it could be more cost-effective to live in the rent-controlled area. Together, these two groups create an artificial shortage, as shown in Figure 1.

Social and Ethical Implications

However well-intended the concept of rent control may be, empirical studies indicate that it seems to have failed its intended objectives. While some lower-income tenants have enjoyed the intended benefits of rent control, much benefit has gone to those less in need. Instead of creating a fair and equitable opportunity for lower-income renters, there are data that show that rent control has created greater hardships and inequities for all involved. In many cases, it is not the low-income renter who occupies the rental property but someone in a more financially secure position who is profiting from the situation. Since rent control in general does not place constraints on the income levels of prospective renters from which landlords may choose their tenants, they will be drawn to choose those tenants

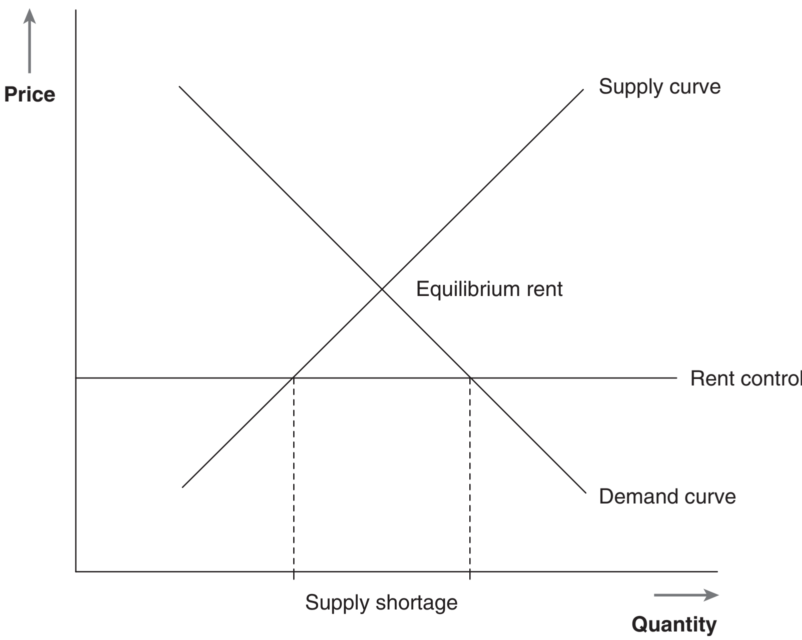

Figure 1 Supply and Demand Graph

who are more likely able to meet their rent payments on a consistent and timely basis. These renters tend to be those in the higher-income brackets.

This often leads to renters occupying too much space for their needs. For example, an elderly couple, whose children have left their home, keep a large apartment, seeing that their costs are low and could go up if they were to move to a smaller apartment. On the other hand, a young couple with children is unable to find a bigger apartment because people enjoying rent control benefits are occupying them. This can lead to another unintended outcome of rent control—namely, it limits the exchange opportunity to the one who values the property rights the most. By definition, the use of a resource is economically efficient when the property rights associated with the resource are held by the one who values them the most.

In addition, rent control may lead to reduced maintenance. Landlords of rent-controlled apartments often delay or even completely avoid maintenance in an attempt to reduce costs and increase their returns to compensate for lost rental income. While the landlord may attempt to withhold maintenance on all rent-controlled properties, those occupied by higher-income individuals will be in a better position to fight this lack of services. They may be able to hire an attorney to sue the landlord to force him or her to do the required maintenance, or they may have the financial ability to make the necessary repairs themselves. However, lower-income individuals will often be at the mercy of the landlord, unable to take the legal action often necessary to force the landlord to comply and make necessary repairs.

—Joanne H. Gavin and Tom Geurts

See also Property and Property Rights; Rents, Economic

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Rents, Economic

Rents have a specific meaning in economic theory. They are equal to any excess payment made to a resource over and above the amount necessary to keep that resource under current employment. This necessary amount is equal to the opportunity cost of the resource; that is, the payment it could receive in its most desired alternative employment. Consider, for example, a famous movie actor who receives a very high salary due to the large revenues generated for movie producers. Of course, if the film industry did not exist, this actor would not be famous and could not, therefore, generate such large revenues. As such, the salary he or she could secure as an actor would be a lot less. The amount he or she would accept to remain an actor is the salary floor on which any excess payment is considered an economic rent. It is obvious, then, that actors earning multimillions of dollars per year are earning a salary that is mostly economic rent. And this rent is paid to them because of their fame that arises from a unique talent that is suited to their current occupation.

The concept of economic rent was originally applied by 18th-century economists, notably David Ricardo, to the agriculture sector. If land is homogeneous and in abundance, it has an opportunity cost of zero; that is, it will either be gainfully used or remain idle and intact. Thus, any payments made to landowners for the use of their land become economic rent in their entirety; in fact, economists refer to it as Ricardian rent. If the land is limited in availability, then any payment above its most gainful use would be the economic rent in that case. But suppose, on the other hand, that land is made up of tracts of different qualities within a market area. Each tract is, therefore, usable for the different activities which are best suited to the qualities concerned. Since the opportunity cost of each tract is different, if a single price were paid to use any of these tracts for some common activity, it would result in what are known as differential rents.

What a tract of land and a famous movie actor have in common is that they both remain available in the long run to be employed in a fashion commensurate with their potential. Their availability for use is independent of any payment offered which is above their opportunity cost. Sometimes, however, rents could be limited to the short run only. In this case they are known as quasi rents (a term first used by the 19th-century economist Alfred Marshall). Quasi rents occur when an economic profit is earned on a resource or activity whose supply is fixed in the short run. In the long run these quasi rents disappear. As an example, consider a business that uses a patented technology and, as such, produces a unique product. This patent gives the business a monopoly situation whereby it can set a price above the economic cost of production so as to earn a profit equal to the quasi rent. When the patent expires, and other businesses are allowed to use the technology, these quasi rents will disappear as the business now faces competition. Unless the producer benefits from long-run barriers to entry, such as economies of scale, its monopoly rents can be competed away by new entrants to the market.

Quasi rents could also become a long-run cost of doing business. As an example, consider a manufacturer who has leased (rather than own) a factory in a particular city. If the city grows in population, the manufacturer's sales may rise and quasi rents could be earned as a result. This analysis assumes that revenues are rising faster than costs (of which the fixed lease payment is but one component). In the long run, when the lease comes up for renewal, the factory owner could raise the required lease payment by the amount of the quasi rents expected to be earned by the manufacturer over the lease period. To the manufacturer, the quasi rent now becomes an opportunity cost of doing business using that factory.

In another setting, the manufacturer could enjoy a government-issued license, which limits the competition faced in the marketplace. When the license comes up for renewal, however, the government could raise the cost of the license by the amount of quasi rents expected to be earned by the manufacturer. On the other hand, the government could make the license available to any business wishing to spend the time and money required to successfully lobby for it. The collective amount of money spent in this rent-seeking situation could dissipate some or all of the quasi rents, with all this wealth being transferred to the government, to lobbyists, to lawyers, and so on.

Economic rents, when they exist in the long run, are not a source of economic waste or inefficiency. It is meaningless to say that a multimillionaire movie actor is "overpaid." While it is true that the actor is being paid multiple times more than the opportunity cost of remaining an actor, the fact is that the employer is willing and able to afford the salary due to the actor's revenue-generating ability. Paying ever-higher amounts for fixed tracts of land is also not wasteful because the rents are a signal that the users of the land expect to generate enough revenue from their production to validate the rent being paid. Thinking about economic rent in this way prevents one from making the error of assuming that high rents lead to high costs of finished goods. It is the demand for the finished goods themselves, and the higher price signals received, that filter down into the costs of employing productive resources such as land.

Quasi rents, on the other hand, do indicate inefficiency because the market has not been able to adjust fully the level of competition necessary to prevent a monopolist from earning them. Quasi rents earned by monopolists generate a deadweight loss in the market. By eliminating barriers to entry, the government eliminates the quasi rents; by instituting barriers to entry, the government creates the environment necessary for quasi rents to be earned. Rent seeking is a phenomenon propagated first and foremost by the governing authority.

The socially optimal situation is one in which there is sufficient competition to prevent quasi rents. The government may need to eliminate barriers to entry to promote competition. Quasi rents signal persistence of inefficient monopoly. Long-run economic rent is in contrast not a signal of persistent inefficient monopoly. The government would, therefore, make a policy error in erecting barriers to entry.

—Darren Prokop

See also Barriers to Entry and Exit; Deadweight Loss; Opportunity Cost; Profit Maximization, Corporate Social Responsibility as

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Reputation Management

Reputation management is a term that has recently gained broad recognition, referring to methodical efforts by business managers to influence perceptions about their businesses. However, the notion that reputation can and should be managed has been around since ancient times. Reputation, which can apply to institutions or to individuals, is analogous to perceptions of character—and while it sometimes is assumed that having a reputation is a good thing in and of itself, an institution can have a good or bad reputation just as a person can have a good or bad character, and reputation measures are as multifaceted as are the purported elements of character. Socrates said that the way to earn a good reputation was "to endeavor to be what you desire to appear," optimistically suggesting a confluence of reality and perception. Although Socrates emphasizes the importance of good moral character to reputation, his remark on its face is not inconsistent with Machiavelli's concession that sometimes political and economic success require a reputation for being heavy-handed and conniving while nonetheless being well respected.

It is clear from these historical views that there is an element of reputation management that is concerned with public relations but that that is not all there is to reputation management. As managers grow more sophisticated about performance management and markets grow more transparent about performance measurement, reputation has become one of those so-called soft characteristics of a business that are believed to have a material impact on market value. Therefore, as analysts, the media, and other stakeholders express interest in corporate reputations, business managers seek ways in which to influence them.

Reputation Indices

What companies have the "best" reputations? Not only is there never full consensus on an answer to this question among the many reputation indices that have been released by the media and other parties, but also, there is no full congruence on what it means to measure reputation. However, there are generally some companies, brands, and individuals that tend to perform well (or poorly) across indices, whether they purport to measure reputation, respect, admiration, brand, or some other variation on a theme. So while reputation indices differ substantially in approach and outcomes, they share the goal of measuring stakeholders' perceptions of business entities.

Most business reputation indices focus on company reputations, although clearly brand reputation influences company reputation and vice versa, while the reputations of individual executives can reflect or less often clash with the reputation of the enterprise. One aspect of reputation measurement methodologies that leads to important differences in results concerns the survey population. Perceptions of the general public tend to differ from perceptions of, for example, chief executives, stock analysts, the business media, or other specific expert populations, while perceptions also vary as a result of other factors, including respondent nationality, economic class, and other demographic indicators. These indices do not always measure a company's internal reputation (among its employees), which may be as important as its external reputation but may be the result of significantly different factors.

These differences among survey populations and methodologies lead to different attitudes about what matters to corporate reputation. Reputation generally is sometimes mistakenly equated with a reputation specifically for corporate responsibility, which in some studies is merely one factor among many that constitutes overall reputation. While the rise of socially responsible investing has increased the potential impact of corporate social performance on corporate financial performance, not all investors (or reputation indices) place equal weight on the importance of social responsibility to corporate reputation. In general, the factors that constitute various reputation indices vary significantly enough from study to study and there is no general agreement even on a typology of factors. Certain factors focus primarily on financial success and efficiency, others on strategy and governance, corporate social responsibility and trustworthiness, product innovation and quality, brand and name recognition, and even on how well the company does with regard to managing its reputation (e.g., through communications and public relations, marketing, or political maneuvering). While a good reputation may be seen as inherently valuable, often these studies seek to make a descriptive connection between a good reputation (however defined) and good financial performance.

As a general rule, the reputation studies that generate wide publicity generally concern companies that have well-established, often global, reputations (such as automobile manufacturers or life insurers). Companies that serve niche markets may have established reputations with their stakeholders but may remain relatively unknown to the broader investing public (such as auto parts manufacturers or reinsurers). Conversely, companies that sell consumer products to a cross section of society tend to be reputation sensitive because they rely on name recognition with consumers who are often also investors. Sometimes, entire industries can be swept up in a wave of excitement or criticism because of their association with external events that may not be entirely within their control: For example, the dot-com boom of the late 1990s led to irrational overvaluation of many Internet start-ups, while energy companies may suffer reputation loss when the price of crude oil leads to a rise in gas prices.

Perception Versus Reality

The debate about the meaningfulness and importance of reputation—and by implication the meaningfulness and importance of managing reputation—links back to an ancient tradition that has often distinguished between perception and reality. From Plato's divided line that helped to explain his theory of forms and form-sense distinction, to Bishop Berkeley's antimaterialist claim that "to be is to be perceived," to Descartes' mind-body division, philosophical epistemology and related psychology have suggested that human beings (and other animals) engage with and respond to the world they perceive, not necessarily the world that is actually out there. Kant's synthesis in a critical philosophy that said that the version we see of reality is inescapably colored by our cognitive hardwiring, and more recently Wittgensteinian and postmodern thinking, to some extent say that the only world that matters is the one we think we are in—that is, the world of perception.

It may be argued that all investment and trading decisions made in the financial markets depend on perception, and the quality of these decisions is a function of the extent to which these perceptions match reality. Recent corporate governance reforms that focus on more comprehensive financial disclosure—in the aftermath of corporate conduct scandals that, not incidentally, adversely affected corporate reputation—are essentially an effort, accepting the traditional perception-versus-reality distinction, to bring perception closer to reality by giving investors more reliable real information on which to base their opinions and decisions.

Even more than other financial market perceptions, however, perceptions of reputation are perceived to be particularly ripe for distortion. That is to say that to the extent that reputation is seen to be important, reputation management has been criticized for being intentionally manipulative of stakeholders' perceptions. Unlike financial statements, which can be reasonably assured through the financial audit process applying generally accepted accounting principles, reputation measures are often more difficult to quantify, sometimes relying on emotional associations with products, brands, and companies. When WorldCom was disgraced by an accounting scandal, one reputation-enhancing step that the company took was to change its name to MCI, the name of one of its legacy acquisitions that had less unfavorable associations for stakeholders (later, the MCI name went away in an acquisition). Johnson & Johnson, a company that has long performed well in many reputation indices, evades the general disrepute of the pharmaceutical industry sector, in part because its most recognizable brand-name products, baby powders and shampoos, have historically sentimental associations for many stakeholders.

These examples suggest simple reputation management techniques from which business managers can learn, but they reinforce the perception-versus-reality distinction and several associated concerns of reputation management, such as the potentially important difference between being a good company (having quality products and services, reliable financial performance, etc.) and being a known (prominent) company. Furthermore, to the extent that a good company is one with a favorable ethical reputation, there is alleged to be an important difference between good ethics (being socially responsible because it is morally right) and good business (which sometimes includes being socially responsible because it is perceived to be strategically advantageous).

Managing Reputation

Another complicating factor in reputation management is the question of what causes what. Does a good reputation enhance financial performance, or does good financial performance enhance reputation? Or is the relationship overstated? In the final analysis, reputation management comes down to giving deliberate attention to the perceptions of stakeholders in making business management decisions, something good managers should be doing anyway. Managing reputation well rarely involves giving equal weight to each stakeholder, but it does require prioritizing, understanding, and then acting to influence the ways in which key stakeholders' perceptions can affect such important business drivers as attracting and retaining human capital, increasing brand distinctiveness and market share, lowering the cost of capital, stimulating favorable analyst and media coverage, and so on.

The business case for reputation management has been said to be a market premium that attaches to a good reputation. Since the market value of a business is not simply a matter of what that business is today but also what investors expect from it in the future, a gap in reputation can distinguish otherwise similar companies' future prospects in the minds of investors. This perspective on reputation management may categorize reputation as an intangible or "shadow" asset, but an asset nonetheless. Reputation has been credited by risk managers as constituting a "reservoir of goodwill" when something goes wrong. However, the value of reputation as an asset is impermanent, and the reservoir is not bottomless. Market perceptions can be fickle, and a single event can transform a reputation, for better or worse. The downside of a prominent reputation is that while it may help in an up market, it can magnify liability in a down market, emphasizing the extent to which a company is vulnerable to events beyond its control—external events, competitor failures, or supply chain mismanagement. All these factors might challenge the perceived value of reputation management, whereas they led to Warren Buffett's famous remark in support of taking steps to manage reputation, "It takes twenty years to build a reputation and five minutes to ruin it."

Machiavelli's pragmatic approach to reputation notwithstanding, Buffett's folk wisdom emphasizes the importance of ethical reputation, because even if certain stakeholders (e.g., shareholders) want management to be aggressive in its bargaining position with other stakeholders (e.g., employees and customers), each influential stakeholder's perception of the business depends on assurances that it will be treated fairly. If management has a reputation for dealing dishonestly with regulators, the negative consequences will extend beyond direct fines and penalties, potentially draining the reservoir of trust the management may once have had with shareholders and the communities in which the company operates. Thus, reputation management experts tend to coalesce around the importance of business ethics and social responsibility to reputation, even if there is no broad consensus on the exact meaning of these concepts in practice. On a related point, they also commonly advise transparency in communications with stakeholders, reasoning that a sound business should have little to hide along with conventional wisdom that when there is something worth hiding, the cover-up usually causes more trouble than the problem itself.

Just as stakeholders' knowledge of the business is important to a fair evaluation of reputation, management's knowledge of who its stakeholders are and what matters to them is critical to effective management of reputation. The benefits of sound reputation management are not separate from sound business performance but rather integral to management's ability to deliver what many stakeholders want—increasing shareholder value, worthwhile products and services, good jobs, social and environmental benefits, and so on. Stakeholder dialogue and monitoring of stakeholders' interests contributes to management's knowledge and ability to balance and, where necessary, prioritize these interests to the extent they cannot equally be satisfied. When there are tradeoffs between product quality and price, cost of production and environmental degradation, local community benefits and low-cost-country sourcing, and other conflicting stakeholder interests, it can be as important for management to have a credible story to tell as it is for management to make an informed decision.

Stakeholder engagement, a term that is often associated with maintaining a dialogue between a corporation and its moral critics, is in fact just a variation on investor relations that recognizes that Wall Street analysts are not the only stakeholders with the media power to express an opinion about corporate management. Stakeholder engagement is a form of reputation risk management that seeks to exert greater management control over the perceptions of others, and managers who view reputation as an opportunity and a risk employ other reputation management techniques that are modeled on risk management techniques, such as identification of key reputation drivers, scenario planning, reputation measurement and monitoring, and the installation of early warning systems.

Finally, in determining how to approach reputation management, it is important for management to ask what kind of reputation it makes sense for the business to have, and how prominent a reputation it needs to have. It is rarely possible to have a reputation for being the highest quality, lowest cost seller of a given product or service, so it makes sense to target reputation to the market the company is best positioned to serve. And given that reputation poses potentially as much risk as reward, it is reasonable to seek that reputation among those that matter to the business while seeking to stay out of the broader limelight lest that bring unwanted attention.

Together, these techniques are valuable reminders that reputation is manageable to the extent that it is based on substantive behaviors but never wholly within any one individual's or company's control. It may be practically useful to distinguish between perception and reality to call attention to the importance of attending to stakeholders' interests, but it is at least as important to recognize that a lasting corporate reputation also requires a grounded sense of corporate purpose that is not buffeted by sometimes ephemeral stakeholder demands and that helps sort out those demands. The notion of reputation management emphasizes the interdependence and potential inseparability of companies from the industries, communities, and markets in which they operate. While this interdependence has led some corporate critics to demand a stakeholder-driven conception of strategic management, it also demonstrates the extent to which capitalist societies rely on business for production and distribution of basic goods. It further suggests that as much as the financial markets are driven by perception, the real exchange of goods and services in the marketplace is evidence that business is integral to social well-being and not just an institution whose reputation is on exhibition for social scrutiny.

—Christopher Michaelson

See also Business, Purpose of; Corporate Social Financial Performance; Reputation Management; Socially Responsible Investing (SRI); Stakeholder Engagement

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Resource Allocation

A resource is any supply or technology input to a productive process to create value or wealth. Resource allocation involves the physical movement or transfer of supply from a point of origin to a destination. Resource allocations may be directed by private owners or by government. Private owners may be motivated by self-interest or by social responsibility. Typically, government requirements regulate these transfers to put social or political goals into practice. For example, government subsidies may direct resource allocations, regulations may govern them, and taxes may raise funds for them. The integrity of procedural justice in legal institutions and judicial systems is critical for the protection of property rights, an important component of the allocation process.

Competition among sellers in a free market tends over time to allocate scarce resources toward the satisfaction of buyers' needs in a process that seemed to Adam Smith as if an invisible hand were guiding the allocation of productive resources for social progress. The for-profit marketplace, however, tends to underallocate resources toward social needs where there is insufficient opportunity for profit. These sectors, such as military defense and public safety services, must be provided by government if they are to be provided at all.

The dynamics of global competition compel businesses today to locate in geographic areas where scarce resources can be acquired and deployed most advantageously. Calls for government regulation on business may become more frequent if their global allocation of resources disrupts traditional lifestyles and sustainability of communities.

Neoclassical economists argue that once the productive possibilities from resource allocations have been maximized, then there will be more wealth to distribute to achieve social goals. For example, some wealth may be taxed by government to reallocate resources toward rectifying the disadvantages of poor segments in society. Many economists recognize the disincentives of such government transfers—the wealthy may work less because their marginal income from additional work is taxed, while the poor may work less because they receive the transfer without needing to work. At the same time, however, economists often compare such government transfers to a leaky bucket—inefficient but still useful.

Owners of private property often contract with managers to act as owners' agents to allocate resources. The resource perspective of management in market-based competitive economies focuses attention on the relationship between resource allocations and financial performance in industries and businesses. Cost-benefit analysis attempts to estimate all the consequences, both adverse (costs) and advantageous (benefits), of a proposed resource allocation and places a money value on the outcomes to allocate as much of the resource as possible to the most beneficial uses. Not all ethical considerations, however, can be monetized, and the costs and benefits may not be fairly allocated.

Competitive marketplaces may not result in resource allocations that satisfy all definitions of justice and social welfare. Competition as a process to allocate scarce resources has been praised for its efficiency but criticized for its amoral focus on short-term self-interest. For this reason, many socialist alternatives to private property governance of resource allocations in competitive markets have been suggested.

Teleological theories of distributive justice focus attention on consequences of resource allocation for individuals and society. The consequential perspective requires comparative measures of well-being and reliable mechanisms to transfer resources from better-off individuals to those less well-off. A sufficiency perspective on resource allocation suggests that all individuals below a certain threshold should receive additional resource allocations. If all individuals' social positions are rank ordered, however, then the transfer from the highest position to the lowest has the greatest impact on equality.

Criteria for justice at the individual level may place the highest priority on resource allocations to those individuals with the least valuable resource stock *ex ante*. Pareto-efficient allocation, for example, is a decision rule that demonstrates fairness by improving the position of at least one individual, while under no circumstance causing any individual to be worse off. When allocation participants view value subjectively, then Pareto efficiency has the practical effect of giving every individual a veto over the allocation scheme.

Some applications of justice theories focus attention on aggregate measures of resource allocation throughout society. Utilitarianism, for example, seeks to maximize the total allocation of valuable resources distributed to the majority. If this social state can be measured, then an equivalent allocation may be found that does not change the total value of resources in society, but does allocate them more fairly or equitably across all members of the community. If such a measure is an additive function, then small amounts of valuable resources allocated to a large population may be calculated to be a greater social good than larger amounts of value allocated to a small population. In the latter situation, the average individual allocation may have higher value, but the total sum of value in the group is smaller.

Whether calculating the social sum or individual average allocation, resources need not be allocated equally for the allocation to be fair. Indeed, one potential criticism of a Pareto-efficient approach to allocation is that there are multiple solutions and not all necessarily have equal resource distributions. There may be variety in tastes and needs that lead to acceptable asymmetric allocations, so that each individual perceives his or her allocation to be a fair response to his or her subjective preferences.

—Greg Young

See also Capitalism; Communism; Consequentialist Ethical Systems; Cost-Benefit Analysis; Justice, Distributive; Pareto Efficiency; Procedural Justice: Philosophical Perspectives; Property and Property Rights; Socialism; Socially Responsible Investing (SRI); Strategic Planning; Subsidies; Utilitarianism

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Restraint of Trade

Restraint of trade, defined broadly, is a contractual limitation on business dealings or professional or gainful occupations, and is legal or illegal, ethical or unethical depending on its effect. If the restraint is in the best interests of both the parties and the public, then it is not illegal. Otherwise, if it is an agreement between or combination of businesses intended to eliminate competition, create a monopoly, artificially raise prices, or otherwise adversely affect the free market, then the restraint of trade agreement violates antitrust laws and is probably illegal. A horizontal restraint of trade is one imposed by agreement between competitors at the same level of distribution, such as a cartel in which rivals agree to restrict output and raise prices. A vertical restraint of trade is one imposed by agreement between firms at different levels of distribution, as between manufacturer and retailer.

Antitrust laws are the United States' embodiment of the British common law's restraint of trade principles and are grounded in the ethics of free market values. Under this theory, technology improves human life because it makes such things as antibiotics available, but it requires constant innovation. For example, as microbes become resistant to penicillin, new antibiotics must be created. Free market economies maximize competition and therefore encourage innovation: They both encourage the creation of new antibiotics and decrease their prices so that they become more readily available to a larger proportion of the population. In contrast, in a planned economy, a monopoly where one company or concern controls the manufacture or sales of antibiotics would provide no incentive for innovation, would raise prices artificially, and therefore would be antithetical to the fundamental values of widespread availability and innovation.

An exception to the principle that a monopoly discourages trade and innovation is the limited monopoly created by patent and other intellectual property laws. Under patent law, the developer of a new antibiotic is granted a monopoly over that product for a limited amount of time, to allow innovators a certain period during which they can recoup the costs of research and development and make a profit. Patents, therefore, are thought to provide an additional positive incentive for innovation.

Development of Restraint of Trade Law

In feudal England, a complex system of guilds regulated relations among master, journeyman, and apprentice. In the first known restraint of trade case, in 1414, a court refused to find the defendant liable for breaching his agreement not to practice his dyer's craft in town for 6 months, finding that the agreement was unfair. Today, this type of noncompetition clause might be found acceptable depending on whether the time and place limitations are found to be reasonable under the circumstances. Thus, the common law of trade restraints originated not so much with notions of competition and protection of the free market but rather in support of fair commercial activity and crumbling guild customs.

Later cases were not so quick to invalidate such agreements, and reflected a respect for freedom of contract principles, until gradually courts decided to uphold such agreements so long as their primary purpose was not to limit competition. The concept was further developed in the U.S. common law such that one line of decisions banned price-fixing agreements and other anticompetitive arrangements when the challenged restraint affected basic necessities. As the 19th century came to a close, however, U.S. courts became more sensitive to unreasonable restraints on competition, positing that where the sole object of both parties to the contract is to restrain competition and enhance or maintain prices, the restraint is unjustified and therefore void.

U.S. courts became more sensitive to unreasonable restraints on competition after the Civil War because rapid industrialization had led to the perceived accumulation of power in the hands of a few robber barons. Public opinion in the United States had always opposed monopolies, because under the original definition, they were despotic powers created by the government. But after the Civil War, large-scale corporate concentration became the norm, and the fiscal power shown by these new trusts led to a widespread perception that so-called private institutions were acquiring coercive power that had formerly been reserved for governments. The result was the passing of the Sherman Antitrust Act in 1890, which made trust agreements in restraint of trade both illegal and criminal. However, this act covered only some abuses of trade. Two other acts were subsequently passed to address other types of anticompetitive behavior. The Clayton Act of 1914 made price discrimination, exclusive dealing contracts, some corporate mergers, and interlocking directorates illegal. The Federal Trade Commission Act created the Federal Trade Commission (the FTC) and made "unfair methods of competition" such as dumping and subsidies illegal. Although they made certain behavior illegal, neither the FTC Act nor the Clayton Act made those behaviors criminal, in contrast with the Sherman Act. The FTC, in addition to investigating unfair trade claims, also prosecutes Sherman Act cases, along with the U.S. Justice Department.

Restraint of Trade as Defined by the Sherman Act

The Sherman Act declares that "every contract, combination, in the form of a trust or otherwise, or conspiracy, in restraint of trade . . . is declared to be illegal." As the Supreme Court describes it, the Sherman Act was designed to be a comprehensive charter of economic liberty and was intended to preserve free and unfettered competition as the rule of trade in the belief that the unrestrained interaction of competitive forces yields the best allocation of economic resources, the lowest prices, the highest quality, and the greatest progress. Violation of the Sherman Act can lead to civil penalties, including injunctive relief and treble damages as well as criminal penalties, including fines of up to $10 million and sanctions for corporations or fines and jail terms up to 3 years for individuals.

The Rule of Reason

Because every agreement concerning trade can be seen as restraining, Section 1 of the Sherman Act prohibits only restraints that *unreasonably* restrict competition. The fundamental test of reasonability is whether the restraint imposed merely regulates competition (thereby possibly enhancing it) or whether it is designed to suppress competition. In determining whether a restraint is reasonable, the court examines all the facts and circumstances peculiar to the business to which the restraint is applied: conditions before and after the restraint was imposed; the nature and effect of the restraint; and the reason why it was adopted. For example, in the seminal "reasonableness" case that allegedly involved price-fixing, the Supreme Court found that a grain exchange rule requiring members to adhere to their closing bid was reasonable because the rule applied only to a small part of traded grain, had no appreciable effect on market prices or conditions, and actually broke up a monopoly previously held by a few warehouses.

Although it is still used in other types of antitrust cases, in more recent price-fixing cases, the Supreme Court has left behind the reasonable test, stating that any agreement whose purpose is to raise, depress, fix, peg, or stabilize the price of a commodity is presumptively illegal (illegal per se) because it discourages competition. Thus, the Supreme Court struck down an agreement among physicians setting the maximum fees they would charge for their purposes. Although the doctors argued that the agreement reduced prices to consumers by lowering information search costs, the Court believed that similar ends could be achieved without maximum price-fixing, which would discourage competition, and, therefore, condemned the agreement per se.

Monopoly Power

The Sherman Act prohibits monopolization, attempted monopolization, and conspiracy to monopolize.

However, the act does not condemn the mere possession of monopoly power, but instead prohibits conduct that excludes others from competition. Thus, a court first determines whether a firm has monopoly power and then determines whether it has exerted exclusionary conduct to prevent vigorous competition.

Because the Sherman Act does not define when a firm is a monopolist for antitrust purposes, three different approaches can be used to measure whether market power has become monopolist power: performance, rivalry, and structure. The performance approach identifies how much a firm's actual performance deviates from the competitive norm. This may involve determining how much a firm's prices depart from its marginal cost, or the amount by which a firm's net profit exceeds the industry average. If the net profit far exceeds the industry average, then it exerts monopoly power. The rivalry test measures how sensitive the firm's sales level or output is to adjustments in buyer behavior. If the firm can ignore buyers' needs without losing a substantial amount of sales, then the firm has monopoly power. The third, most widely used method is the structural approach, which involves counting the number of firms in a market and comparing each firm's share of market activity. An overly large market share indicates monopoly power. Each of the three methods has its advantages and disadvantages.

Exclusionary Conduct and Microsoft

For a firm to be found guilty of illegal conduct under Section 2 of the Sherman Act, it not only must have dominant power but must also have abused that power through unreasonably exclusionary conduct. Competitive measures are not an abuse, but unreasonably exclusionary ones are. In the case of Microsoft in 2001, the Justice Department and 20 states filed a lawsuit against Microsoft alleging that the company had (1) illegally tied Windows to its Internet Explorer, which was per se unreasonably exclusionary against other navigators, (2) attempted to monopolize the browser market, and (3) wrongly maintained its monopoly power in the operating system market in response to a perceived threat by Netscape Navigator. While the trial court found for the Justice Department, the appellate court reversed two of the three findings of violations, upholding only the last.

In reaching its decision, the appellate court gave four ways to distinguish between exclusionary and competitive conduct: (1) The monopolist's act must harm the competitive process and, thereby, harm consumers; (2) the plaintiff must demonstrate that the act had the requisite anticompetitive effect; (3) once the plaintiff establishes a basic Section 2 case, then the defendant may offer a procompetitive justification for its conduct in rebuttal; and (4) if the plaintiff fails to rebut the defendant's justification, then the plaintiff must demonstrate that the anticompetitive harm of the conduct outweighs the procompetitive benefit. Although ultimately the plaintiffs were not able to force Microsoft to divest itself of its browser, after the D.C. circuit court's opinion, the Justice Department and most of the states negotiated a consent order.

International Law and the Long Arm of the Sherman Act

Although some authorities feel it would be helpful, currently there is no international antitrust or "restraint of trade" law, the closest being the WTO rules against dumping and subsidies. Thus, there is no international body that could try Microsoft. The Sherman Act covers restraints that are in the flow of interstate commerce as well as local restraints affecting interstate commerce, which means that it is focused on effects felt or potentially felt in the United States and, necessarily, in more than one state. Where a restraint has purely local effects, it is not in interstate commerce. For example, a board of supervisors' disqualification of an employee from running for the position of county supervisor did not violate antitrust laws, because it had only local effects. Suit would have to be brought under state antitrust law instead.

However, although the Sherman Act is limited to effects or potential effects in the United States, due to a 1982 amendment, it covers acts of firms in foreign countries that have a direct, substantial, and reasonably foreseeable effect on U.S. domestic commerce, U.S. import trade, or the export commerce of a person engaged in such commerce in the United States. Thus, a Mexican sisal monopoly was found to have restricted or adversely affected imports into the United States. In these cases, to have the power to sue a foreign firm in the United States under the Sherman Act, the firm must have intentionally done business in the United States or own assets within the court's jurisdiction.

The lack of an international antitrust law, however, does not mean that a multinational firm won't face substantial antitrust suits elsewhere in the world. While Microsoft did fairly well in its U.S. litigation, it fared much less well in the European Union, which found that Microsoft had abused its near monopoly in operating systems by leveraging that power into markets for media players and for work group server operating systems. The European Union imposed a record-setting $613 million fine, ordered Microsoft to disclose to competitors the interfaces required to permit their products to interact with Windows, and ordered the company to offer a version of Windows without the Media Player. South Korea similarly found that Microsoft violated its antitrust laws.

—Nadia E. Nedzel

See also Capitalism; Competition; Freedom of Contract; Free Market; Free Trade, Free Trade Agreements, Free Trade Zones; Intellectual Property; Mergers, Acquisitions, and Takeovers; Predatory Pricing and Trading; Subsidies

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Revealed Preference

Revealed preference theory holds that consumers' preferences can be revealed by what they purchase under different circumstances, particularly under different income and price circumstances. The concept argues that if a consumer purchases a specific bundle of goods, then that bundle is "revealed preferred," given constant income and prices, to any other bundle that the consumer could afford. By varying income and/or prices, an observer can infer a representative model of the consumer's preferences.

Much of the explanation for consumer behavior, particularly consumer choice, is rooted in Jeremy Bentham's concept of utility. Utility represents want-satisfaction, which implies that it is subjective, individualized, and difficult to quantify. By the early 20th century, substantial problems with the use of utility had been identified, and many of the theoretical replacements of the concept either struggled with the same critiques (often because they retained too much of the heritage of utility) or suffered from being essentially unmeasurable and untestable. In 1938, Paul Samuelson noted that there seemed little reason to believe in the dominant theories of the time other than the fact that the concepts led "to the type of demand functions in the market which seem plausible." As a result, Samuelson offered what became known as revealed preference theory in an attempt to build a theory of consumer behavior that was not based on utility. He argued that his new approach was based on precepts that were observable and relied on a very minimal number of assumptions that many would argue were relatively uncontroversial.

As revealed preference theory has developed, three primary axioms have been developed: the weak, strong, and generalized axioms of revealed preference. The weak axiom indicates that at given prices and incomes, if one good is purchased rather than another, then the consumer will always make that same choice. Less abstractly, the weak axiom argues that if a consumer purchases one particular type of good, then the consumer would never purchase a different brand or good unless it provides more benefit, by being less expensive, having better quality, or providing increased convenience. Even more directly, the weak axiom indicates that consumers will purchase what they prefer and will make consistent choices.

Although relatively simple, the weak axiom provides strong rationality properties that economics requires, including downward sloping demand curves and the dependence of consumption on relative prices. These properties can be developed without resorting to the types of strong assumptions required by utility-based or indifference curve analysis, such as diminishing marginal rates of substitution.

The strong axiom essentially generalizes the weak axiom to cover multiple goods and rules out certain inconsistent chains of choices. In a two-dimensional world (a world with only two goods between which consumers choose), the weak and strong axioms can be shown to be equivalent. Later research built on the revealed preference framework and demonstrated that indifference curves and utility functions can be developed from observations of behavior, even though revealed preference theory explicitly rejects these precepts as a starting point for explaining behavior. As a result, a number of the analytical tools and concepts regarding consumer choice could be preserved, albeit with a stronger theoretical base.

While the strong axiom characterizes the implications of utility maximization, it does not address all the implications—namely, there may not be a unique maximum. The generalized axiom covers the case when, for a given price level and income, more than one consumption bundle satisfies the same level of benefit. Expressed in utility terms, the generalized axiom accounts for circumstances where there is no unique bundle that maximizes utility. This extension is important because it allows for multivalued demand functions and, in the structure of indifference curve analysis, for "flat" indifference curves. Both these implications are important for empirical research.

The two most distinguishing characteristics of revealed preference theory are as follows: (1) It offers a theoretical framework for explaining consumer behavior predicated on little more than the assumption that consumers are rational—that they will make choices which advance their own purposes most efficiently, and (2) it provides necessary and sufficient conditions, which can be empirically tested, for observed choices to be consistent with utility maximization.

Currently, revealed preference theory has been applied to economic theory. However, because the theory is so general and depends on such a small set of basic axioms, as data sets regarding human behavior expand, the contributions to empirical economics, and perhaps other fields, are likely to increase. While more attuned to addressing primarily economic considerations in the formulation of consumer choices, the nonparametric nature of the theory, its flexibility at accommodating a wide range of consumer choices, and its ease at generating testable constructions may allow it to make even broader contributions in other areas, such as ethics or other fields of study.

—James E. Roper and David M. Zin

See also Bentham, Jeremy; Consumer Preferences; Rational Choice Theory; Utilitarianism; Utility

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Reverse Discrimination

For decades, women and various minorities were barred from some of the most desirable institutions and positions in North America. Discrimination persisted in many quarters even after it was declared unconstitutional. Continuing discrimination led to a widespread demand for effective policies of preferential treatment or affirmative action to provide justice for those individuals or groups previously (and often presently) discriminated against. The effect of policies that advantage women and minorities in admission and employment is to decrease opportunities for nonminority males. The direction of discrimination is reversed: The properties of race and sex once used to discriminate against members of groups are now used to discriminate in their favor and against the interest of those not of the right race, sex, nationality, and the like.

Preferential policies that establish goals, timetables, target numbers, and the like have provoked impassioned criticism to the effect that, rather than leveling the playing field, these policies are simply instruments of reverse discrimination. One classic case, known as the "McAleer case," centered on a service representative who handled orders for telephone service in AT&T's Washington, D.C., office. In 1974, he asked for a promotion that he did not receive. Instead, a staff assistant named Sharon Hulvey received the promotion. Although less qualified than McAleer, Hulvey was basically qualified. She received the promotion because of an affirmative action program at AT&T. McAleer claimed that he had been discriminated against on the basis of sex. He then brought a lawsuit against AT&T to ask for the promotion, differential back pay, and $100,000 in damages.

A judge held on June 9, 1976, that McAleer was a faultless employee who became an innocent victim through an *unfortunate but justifiable* use of the affirmative action process. In other words, reverse discrimination was justifiable even though McAleer was a victim of it. The judge ruled that McAleer was entitled to monetary compensation (as damages) but was not entitled to the promotion because the very discrimination that the affirmative action policy had been designed to eliminate would be perpetuated if Hulvey were not given the promotion. The central thrust of the ruling was that AT&T had engaged in sex discrimination, setting back the interest of employees such as Hulvey, who had not been properly trained and promoted. AT&T's prior sex discrimination was judged the root of the problem. Since McAleer had no responsibility for this sex discrimination, AT&T rather than McAleer should bear the financial burden of rectifying the company's previous failure to comply with the Civil Rights Act of 1964. The judge held that an affirmative award of some damages on a "rough justice" basis was therefore required and would constitute an added cost that the stockholders of AT&T should bear.

Over the years, many preferential policies have been backward looking, in the sense that they aim to redress past wrongs. However, proponents need not use only arguments that compensation is owed for *past* wrongs. They can, and often do, argue that preferential policies are required to eliminate or alleviate *present* discriminatory practices that affect whole classes of persons (especially practices of minority exclusion). From this perspective, policies are needed to reach the end of alleviating or eliminating ongoing discrimination that negatively affects groups. Reverse discrimination is judged, by those who believe it is justifiable, to be an unfortunate, but not unjust outcome of the policies. It is said to be justified by a compelling social (or governmental) interest in eradicating pervasive, systematic, and obstinate discriminatory exclusion of minorities or other groups so affected. In other words, reverse discrimination is justified when it is essential to overcome long-term, open, and pervasive discrimination.

Opponents of this position argue that reverse discrimination violates fundamental, overriding principles of justice and cannot be justified. There exist a variety of arguments in opposition to several kinds of preferential policies that have the effect of reverse discrimination. Arguments that have received widespread attention include the following: (1) Some persons who are not responsible for the past discrimination (e.g., qualified young white males) pay the price; preferential treatment is invidiously discriminatory because innocent persons are penalized solely on the basis of their race or sex. (2) Male members of minority groups such as Polish, Irish, Arabic, Chinese, and Italian members of society who were previously discriminated against inevitably will bear a heavy and unfair burden of compensating women and other minority groups. (3) Many individual members of any class selected for preferential treatment never have been unjustly treated and, therefore, do not deserve preferential policies. (4) Compensation can be provided to individuals who were previously treated unfairly without resorting to reverse discrimination.

Few deny that reverse discrimination is sometimes caused by preferential policies, and most agree that cases of reverse discrimination exist in which a white male has unjustifiably been excluded from consideration and has a right to compensation. Unwarranted reverse discrimination is no better than any other form of unwarranted discrimination. But those who believe that it is justifiable to permit reverse discrimination argue that the following should also be considered: Reverse discrimination should be distinguished from what merely appears to be reverse discrimination. Sometimes persons will be hired or promoted who appear to be displacing better applicants, but the appearance is the result of another person's discriminatory perceptions of the person's qualifications. If discrimination against black men, say, is sufficiently entrenched in society, then the effects of this discrimination may simply offset the effects of policies that eventuate in reverse discrimination. That is, black men may be neither better nor worse off even if some are hired or promoted under preferential policies.

Those who tolerate some measure of reverse discrimination argue that many setbacks to the interests of white males negatively affected by a policy may be no more objectionable than a variety of burdens produced by social policies that advantage some members of society and disadvantage others. Inheritance laws, for example, favor certain members of society over others, whereas policies of eminent domain disadvantage persons who wish to retain what is legitimately their property to advance the public good. Such laws and outcomes are warranted by a larger public benefit and by justice-based considerations that conflict with the interests of the disadvantaged parties. The point is that disadvantages to majorities produced by affirmative action may be warranted by the promotion of social ideals of equal treatment for members of groups who were severely mistreated in the past.

Some parties who are either advantaged or disadvantaged by preferential policies are not the parties who, ideally, should be advantaged or disadvantaged. For example, just as young white males may pay the penalty for wrongs committed by older white males (who will likely never be penalized), so the older members of minority groups and older women who have been most disadvantaged in the past are the least likely to gain an advantage from affirmative action policies. Paradoxically, the younger minority members and women who have suffered least (if at all) from discrimination stand to gain the most from preferential policies. It seems much harder to justify reverse discrimination in these cases.

Preferential policies have been alleged to have other shortcomings as well. For example, they may confer economic advantages on some who do not deserve them, lower admission and work standards, heighten racial hostility, and cause continued suspicion that well-placed women and minority group members received their positions purely on the basis of their group affiliation, thereby damaging their self-respect and the respect of their colleagues.

Although reverse discrimination does involve real discrimination, the reasons behind this form of discrimination are notably different from the kind of racial and sexual discrimination that spring from a sense of superiority. Preferential policies seek, ideally, to restore status to a class of persons who have been stigmatized and unjustifiably denied access to employment or advancement. However, there has been and will continue to be considerable disagreement about the best means to rectify the evils of discrimination.

—Tom L. Beauchamp

See also Affirmative Action; Preferential Treatment

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Revolving Door

The revolving door refers to the practice of individuals rotating between working in the private sector and working for the government, often in regulatory capacities, and vice versa. While the government needs individuals with expertise in specific areas, this practice may blur the distinction between the public good and business interests.

There are various types of revolving doors: industry to government, government to industry, law to government and then back to law or working as a lobbyist. Business executives sometimes take positions in government regulating industries in which they were recently employed. The experience the business executive brings to the job could be vital to the government, but it is fraught with potential for conflict of interest. A person who has made a career in a mining company and then takes a mining regulatory position in the U.S. Department of the Interior may appear to be compromised. It is not uncommon for officials to leave government and take lucrative positions in firms that they once regulated or to whom they have awarded contracts. In this case, any interaction the individual had with the company before joining it is suspect, and the integrity of government decisions is called into question. Senior regulators often hold law degrees. When they rotate out of government, they may resume work in a law firm that represents clients in the industry they once regulated. This raises obvious questions of conflict of interest even if the said regulator is not the counsel of record since the former government employee could easily coach his or her colleagues. Government regulators and legislators also frequently leave their positions and work as lobbyists for private business interests. Here concern is raised as to whether they might exercise inappropriate influence over their former colleagues.

The federal government began implementing conflict of interest and ethics laws in the 1950s. The two most important laws enacted are the Ethics Reform Act passed in 1989 and the Procurement Act passed in 1996. Under the current laws, "senior" and "very senior" government officials who make contracting decisions must wait a year before joining a military contractor. A 1-year, and sometimes 2-year, cooling-off period is also imposed on individuals making representational contacts with their former agency or with any high-level executive branch official. The Procurement Integrity Act's two main purposes are to limit contacts related to future employment between current government officials and government contractors and to prohibit high-level government officials who act on contracts worth more than $10,000,000 from accepting compensation, including future employment from the said contractor. The laws are broad, complicated, and overlapping; rules differ by the level of involvement of the government employee as well as by the employee's rank. The laws also allow many exceptions. Many in Congress have called for additional legislation to tighten the laws limiting post–government employment. Also, 29 states currently have their own distinct revolving door policies. California and New Mexico impose a permanent ban on working on identical contracts that the government officer was personally involved in while in public service.

The revolving door has become ubiquitous in both state and federal government from defense contracts to health care to the environment. The practice of rotating work in government and the private sector is not illegal unless unfair advantage is given to certain businesses or individuals, which is what the laws attempt to regulate. Unfair advantage is difficult to prove, but even the perception of it can undermine public faith in the government.

—Lori S. Kolb

See also American Federation of State, County and Municipal Employees; Business Ethics; Conflict of Interest; Corruption; Regulation and Regulatory Agencies

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RIGHTS, THEORIES OF

In general, the term *right* is used to describe a person's entitlement. For example, people claiming an entitlement to say what they think express a right of freedom of speech.

In modern-day societies, it appears that claims to entitlements are proliferating; matters as diverse as liberty, abortion, health care, privacy, human welfare, euthanasia, capital punishment, and suicide are all steeped in claims to certain rights. Indeed, the term *rights* is used extensively in relation to a vast array of contentious matters; debates concerning politics, morality, justice, and fairness are especially peppered with claims to rights. The notion of rights is now also commonly used in relation to claims concerning inanimate objects, plants, and nonhuman animals. It becomes important therefore to consider exactly what we mean by "rights."

The language employed in relation to rights is, however, problematic. Some rights are, on occasion, described as "fundamental." This suggests a hierarchy of rights, some of which are of greater importance, in terms of morality or otherwise, while others are simply rights. It may be that in more developed societies the rights that are seen to be fundamental to civil society have been enshrined in their constitutions. But "fundamental rights" could also refer to those rights that are the minimum entitlement of every person no matter their society's stage of development. The term *natural rights* is sometimes employed in this regard. Life, liberty, property, and equality are often cited as "fundamental natural rights" for the reason that they underlie or are a necessary condition for the enjoyment of all other rights. It is also claimed that natural rights are implicit in human nature.

On other occasions, some rights are described as "inalienable." For example, an individual's freedom, dignity, and choice are commonly described as inalienable rights. These particular rights are also sometimes described as "moral rights." But it is sometimes difficult to determine whether fundamental is one and the same as inalienable or moral or otherwise.

The term *right* is also sometimes used in a more general sense to mean treatment that is just or fair. For example, in relation to being employed, a claim to equal pay for equal work is made in respect of being treated in a just and fair manner. Other times the term *right* is used when some other term may be a more accurate description. For example, the Universal Declaration of Human Rights specifies a right to work (Article 23[1]) and to rest and leisure (Article 24). But whether these are truly rights in the sense of entitlements, as distinct from social/political ideals, is another question that gives rise to debate.

To claim that something is "a right" gives rise to myriad questions that extend from understanding the nature of rights and identifying legitimate claims to a right to concern for their universal acceptance. These questions have in turn generated a literature, grounded in a wide spectrum of philosophical discourse, which is rich in character and long in debate. There is now an abundance of theories endeavoring to answer, or at least clarify, some of the questions posed in relation to claiming an entitlement or a right.

Kinds of Rights

A review of some of the rights commonly upheld in modern-day societies suggests that rights may differ in kind. There are certainly differing ways of expressing rights. Some rights are phrased in terms of the person claiming the right, for example, the rights of a child or the rights of a human being. Other rights are more concerned with certain behavior, for example, claims to the right of freedom of speech. But this distinction may not be of any real importance because a closer review reveals that whether the claim to a right focuses on a person or on behavior, the claims also entail involvement on the part of other persons. That a child has a right to a childhood free from abuse entails those persons who interact with children not abusing them. Similarly, a right of freedom of speech entails that those persons hearing a speech will not censor or silence the speaker.

Certain kinds of rights, thereby, appear to involve a correlative duty, or duties, on the part of other persons. In the examples cited above, the correlative duty is negative in the sense that it requires forbearance from action; a right to a childhood free from abuse requires that other persons will not abuse children. A right of freedom of speech requires that other persons will not censor or silence speakers. In other cases, a right may entail a positive involvement on the part of other persons. For example, a right to work may entail that society ensure job opportunities.

But claiming entitlements as rights, and the imposition of correlative duties, raises questions concerning their legitimacy and enforcement. A person may claim falsely and those persons who are obligated may not act according to the required duty.

A review of some of the rights commonly upheld in modern-day societies reveals that some rights are specified by law, and so we claim them as a matter of legal right, whereas other rights are claimed as a matter of moral right. But while law and morality are both concerned, to some degree, with rights and correlative duties, and employ much the same terminology, there is a considerable amount of philosophical debate concerning the relationship between "legal rights" and "moral rights." It becomes necessary, therefore, to first distinguish what these terms mean.

Legal Rights

Legal rights are recognized and enforced as part of each society's legal system. Such rights will therefore vary depending on the society in which an individual lives; they are created or granted by government, and their being upheld depends on the particular legal system in question. Legal rights may be, but are not necessarily, consistent with moral rights.

Greek societies, for example, developed laws and thereby created legal rights within their city-states. Their laws did not, however, extend to benefit all members of their societies; if you were a public slave, you did not have rights.

In modern societies, legal rights exist for the benefit of all members. They are typically embodied in a written constitution, which also allows for the creation of further rights. Thus, the essential rights affecting U.S. citizens are set down in the U.S. Constitution, while Congress and state legislatures are given powers to a create laws and so to create further rights. A single written document is not, however, a requirement; Britain, for example, has no such constitutional document. Rights determined exclusively by society's legislators and legal system are sometimes described as positive laws.

Moral Rights

Moral rights concern moral standards independent of any legal system. They are rights that, from a moral perspective, we ought to have. Moral rights are often claimed on the basis of their being conventional societal practices. But the nature of moral rights, and the basis for claiming such rights, is problematic. There are also debates as to whether moral rights are culturally specific, and influenced by the society's stage of economic development, or whether they are applicable to all persons everywhere and, thereby, serve as a universal set of moral rules.

In modern societies, moral rights are often enshrined in laws as a means of ensuring their observation and a common standard of enforcement. For example, the rights of owners of private property are protected by laws that, at least in part, reflect the rights that society acknowledges as belonging to such property owners.

Some moral rights are also upheld by the notion of "natural laws." Advocates of natural laws generally argue that the general precepts of natural law are self-evident and discernable by anyone, provided only that their natural reasoning is neither deficient nor degenerate and that natural laws respecting life, liberty, and property are possessed by all persons, simply because they are human beings. Some philosophers advocating natural law argue that such laws have been formulated by human beings because man, by human nature, needs to coexist with others. Natural laws have also been associated with a belief in some form of divine lawgiver, but the discourse concerning natural laws in modern-day societies does not generally rely on such belief.

Other philosophers advocating natural law argue that if there were no governments, human beings would find themselves in a "state of nature" governed by natural laws obliging everyone to respect life, liberty, and property. They also claim that such natural laws are superior to a society's constitution and laws and serve as a standard for evaluating all constitutional and legal endeavors.

Other philosophers deny the existence of such natural laws. Alasdair MacIntyre, for example, asserts that there are no natural laws or human rights on the grounds that there are no good reasons for believing there are such rights. He likens the situation to not believing in witches and unicorns, that every attempt for believing there are such has failed. But he proceeds to discuss natural laws and human rights on the basis that they are a fiction.

Whether natural laws are self-evident and discernable by anyone, whether they have some other basis, or even if they are a fiction, it appears that natural laws are limited in their sphere to matters of "life, liberty, and property" and to what is needed to preserve such matters. Whether a particular claim to an entitlement falls within these bounds will always be a subject for debate. If a claim clearly falls outside these bounds, then arguably some other justification will be needed if the claim to the entitlement concerned is to be regarded as a right.

In modern-day societies, claimants to entitlements that are not duplicated in either legal rights or natural laws argue that such entitlements are imperative. This argument relies on the notion that such entitlements derive their force from the ethical rules, principles, and practices prevailing in a given society. This claim can be likened to the deontological notion of duty and concern for how a person should behave. Immanuel Kant posed that if a rational person's maxim, meaning the reason for carrying out the action, could be willed to become a universal law, the action is morally right. Thus, given a person in a particular situation, if the reason for acting in a certain way is a reason that every person, in any similar situation, would be willing to act on, the action is supported as a moral right.

History of Rights

Whether rights have been claimed as entitlements, and granted as such, since man's existence on earth or whether the notion of fundamental rights is the invention of modern-day societies is a question that remains a subject for debate.

Part of the difficulty in determining the history of claims to rights lies in language. In relation to natural or human rights, Alasdair MacIntyre explains that there is no expression in any ancient or medieval language that correctly translates to what we understand as "a right" until near the close of the Middle Ages; the concept lacks any means of expression in Hebrew, Greek, Latin, or Arabic, classical or medieval, before the year 1400.

However, theories relating to the existence of natural laws, upholding certain fundamental rights, have a long history, reaching back to the ancient

Greek philosophers, including Socrates, Plato, and Aristotle.

It was, however, the Stoics who first stressed the universality of human nature and the brotherhood of man. Their doctrines placed emphasis on man's ability to reason, and they argued that a universal law of nature is ascertainable by reason. At much the same time, the Romans developed laws not only for Roman citizens but also for "foreigners" within the state of Rome and, thereby, recognized the idea of a common law applicable to everyone. The Stoics then had a model on which to develop their concept of universal laws claiming moral superiority over local and conventional rules.

It was in the 17th and 18th centuries that the concept of natural rights became a more prominent issue. This period of so-called Enlightenment is a time when the foundations of the Church, and the Renaissance and the notion of divine, "God-given," law began to be questioned and the order of the so-called natural world began to be seen as a matter relating to society and to justice. The rights of individuals, in relation to sovereigns and governments, came to the forefront in efforts to understand and organize modern-day society.

Hugo Grotius was one of the first scholars to separate the study of rights from theology. He argued that natural law would still apply if God did not exist. He believed that humans have the ability to reason and a social nature and theorized on the basis that mankind desires an orderly and peaceful society. A "right" in his view is a moral quality making it possible to have or to do something lawfully, and he regarded justice as a matter of respecting and exercising individual rights. He, thereby, recognized what are termed *subjective rights*.

Grotius also argued that governments should be understood as compacts among men. However, he rejected the notion of an ideal political state or form of government because in his view there is no single best type of life for all individuals to lead. Thus, while advocating natural laws governing the lives of individuals in society, he introduced the notion of differing forms of government and the recognition of differing social values.

Thomas Hobbes, in contrast, denied man's natural sociability and argued that life without government would be "solitary, poor, nasty, brutish and short." But he developed Grotius's notion of government as a compact among men. In relation to rights, he argued that the inhabitants of the state of nature had the right to do whatever they judged to be necessary for their survival. But given that the world has limited resources, conflicts regarding rights are inescapable unless people agree to surrender their rights to a sovereign Leviathan, the Leviathan being some form of state. In Hobbes's view, having surrendered rights to the state, the individual retains only the natural right to resist being killed or confined.

The Development of Rights in Modern-Day Societies

John Locke is generally credited with developing the doctrine we rely on today when we claim that all individuals have certain natural rights, independent of any human compact or convention. He expressed disagreement with Hobbes's view of man's natural unsociability and, in the absence of submitting to the state, resulting hostility. Locke regarded the state of nature as a state of reciprocal liberty; that each individual has a natural right to preserve himself but not to harm others in doing so (except in self-defense against a violent attacker).

In Locke's view, people ought not to be interfered with in pursuit of life and liberty. These, he said, were the natural rights of man. He also argued that everyone has natural rights to private property that must be respected by others, to compensation for injuries, and to punish anyone who violates the law of nature. In relation to the authority of government, he argued that by the terms of a social contract, the power of government is conceded only on trust by the people to the rulers and that any infringement by the rulers of the fundamental natural rights of the people put an end to that trust and entitled the people to reassume their authority.

Locke's views arguably extended the notion of natural laws to being a source of fundamental democratic rights restricting the freedom of rulers. This view was fully explained in his work *Two Treatises on Civil Government,* which was highly influential in formulating both the American Declaration of Independence in 1776 and the Declaration of Rights made by the French National Assembly in 1791.

The opening statements of the Declaration of Rights made by the French National Assembly claim that the end view of every political association is the preservation of the natural and imprescriptible rights of man to liberty, property, security, and resistance to oppression, and these clearly reflect Locke's views. But there was opposition to such views.

In particular, Jeremy Bentham, a proponent of utilitarianism, was highly critical of these claims. In

Bentham's opinion, there are no such things as natural rights, and he proceeds to describe such rights as "mischievous nonsense" and "nonsense upon stilts." He opined that there can be no rights anterior to the establishment of government and no rights that contradict the laws made by government. He argued that to talk about rights made sense only within a legal framework and that legal rights correlate to legal duties, thereby rendering the notion of legal rights redundant.

While political developments following the French and U.S. declarations caused the notion of natural laws and government as perceived by Locke to be questioned, his legacy remains very much intact.

The Nature of Rights

The philosophical discourse that examines the nature of rights is an attempt to determine what rights are and how they are composed. These are conceptual questions that have given rise to divergent theories and, to varying degrees, invariably unsatisfactory answers.

Arguably, the task of defining what is meant by "rights" is thwarted by the fact that the various claims being examined are too divergent; it may be that the nature of legal rights is dissimilar to the nature of moral rights or the rights created by a particular institution, such as a school or hospital.

Clarity as to the conceptual nature of legal rights emerged in the late 19th century and is generally attributed to the American jurist Wesley N. Hohfeld. He built on earlier juristic work and provided a more rigorous analysis for the proposition that rights comprise four basic components. He described these, the "Hohfeldian incidents," as the privilege, the claim, the power, and the immunity.

Hohfeld maintained that a privilege (which some writers prefer to call a liberty) is a right that does not depend on another person having a correlative duty but requires that other persons have no claim that you either do, or do not, act in a certain way. Thus, you have the liberty to voice your opinion to A only if A has no valid claim requiring you either to voice your opinion or to remain silent. In the context of law, you have a legal liberty in fact of A to perform some action if and only if you have no legal duty to A to refrain from doing that action. Based on Hohfeld's work, but using slightly different language, a liberty right can be explained in terms that B has a liberty (relative to A) to do X, if and only if A has a "no-claim right" that B should do, or not do, X.

A claim, in contrast, is a positive claim right that has a corresponding duty; that duty may be to do or to forbear doing some action. Thus, you have a legal claim against A with respect to some action if and only if A has a legal duty to you to perform that action. For example, a claim right to education has a corresponding duty to provide a system of schools.

Neither a no-claim right associated with a liberty nor a duty associated with a claim right need fall to a particular person or body. For example, a claim to freedom of speech has a corresponding duty not to silence or censor and applies to everyone hearing the speech in question. Similarly, a child has a claim right to a childhood free from abuse, and everyone concerned with that child has a duty not to abuse that child. Such claim rights are also described as general rights because they involve claims against everyone, or humanity in general.

Claim rights can, however, also concern claims against a specific person. For example, the seller of goods has a claim right to payment, and the buyer has a corresponding duty to pay for the goods. Similarly, an employee has a claim right to wages and the employer has the corresponding duty to pay the wages. In both these cases, the claim and corresponding duty can be a matter for the parties themselves and, therefore, be entirely voluntary. In other cases, the law may prescribe certain minimum claim rights. For example, it may stipulate a minimum wage. Such claim rights are also described as specific rights because identifiable persons are involved.

Critics admit that this distinction between A's claim right, which has as its correlative B's duty, and A's liberty, which is A's freedom from duty and has as its correlative the absence or negation of a claim right that B would otherwise have, does provide a clear aid to thinking about rights. But they also take the view that it is problematic.

Hohfeld's other two components of rights, power and immunity, are rather different; they are more about rights involving the ability to change rules. A person has a power right if and only if he or she has the power within a set of rules to alter either his or her own or another person's privileges or claims. For example, a manager has a power right if he or she can alter his or her employee's claim right to wages. The component that Hohfeld describes as an immunity right is essentially the corollary of a power right; if a person does not have a power right to alter another person's privilege or claim right, that other person is said to have an immunity right. H. L. A. Hart defines such rights as "secondary rights," while privileges and claims are in his view primary rights.

Other discussions concerning the nature of rights focus more on the notion of choice and the equal right of all men to be free. Rights are then determined on the basis of a moral justification for one or more persons interfering with and limiting another person's freedom. Hart, an English jurist, and Carl Wellman, an American philosopher, are the principal modern-day exponents of what is commonly termed *the choice theory*.

According to the choice theory, the unifying characteristic of rules that entail or create rights is that such rules specifically recognize and respect a person's choice either negatively by not obstructing it or affirmatively by giving legal or moral effect to it. This theory proposes that no person has an absolute or unconditional right to do or not to do any particular thing or be treated in any particular way.

This right to choose, Hart explains, is more accurately described as "an equal right of all to be free." Every adult human capable of choice, first, is at liberty to do any action that is not coercing, restraining, or designed to injure others and, second, has the right of forbearance on the part of others from the use of coercion or restraint against them. These notions of choice and freedom can also be expressed as a liberty or as an obligation not to do a particular act (*X*): thus A's liberty to do/not having any obligation to do *X* is A's right given B's duty not to interfere.

More recent theories concerning rights have also focused on the notions of liberty and noninterference. Libertarian philosophers maintain that every person is the absolute owner of his or her own life and should not be constrained by others but subject to every person respecting the liberty of others. Robert Nozick, an American philosopher, claims that the only basic right that every person possesses is the negative right to be free from coercion by other human beings. He explains that, in other words, rights are to be thought of as side constraints that limit the actions that are otherwise morally available to everyone. Nozick relies on Immanuel Kant's notion of not treating persons solely as "a means" as the basis for his theories.

Joseph Raz offers a different conception of rights; he argues that people may be said to have a right if and only if some aspect of their well-being (some interest of theirs) is sufficiently important in itself to justify holding some other person or persons to be under a duty. This is commonly termed *the interest theory*. For example, A can be said to have a right to free speech if some interest of A is sufficiently important from a moral point of view to justify some other person(s) to have a duty not to restrict A in speaking freely. The duty in this case rests primarily with the government, but in other cases, the duty may be imposed on some other person or persons.

This theory of rights singles out a certain interest on the basis of its moral importance, but it may be that an interest has sufficient moral importance to justify holding other individuals to be under more than one duty. The interest in question may morally justify endless duties. Thus, if A's interest in speaking freely is sufficiently important from a moral point of view to justify the government to be under a duty not to impose censorship, then others may be under further duties to ensure that A is given the opportunity to speak out, that A has some platform for communication, and even that A has protection as a means to ensure that persons with opposing views do not prevent or disturb A's right of free speech.

In recent times, theories concerned with the proper conception of rights have focused more on the nature of moral rights and claims to rights, as distinct from legal rights. But many of the theories employ, at least in part, the concepts identified in relation to legal rights; whether these conceptions are generally relevant to both legal rights and moral rights, in a like manner, is a question that continues to be explored.

Declaration of Human Rights

Today, it is more usual to employ the term *human rights*, as opposed to natural rights or natural laws, when confronted by apparent abuses of human life. The United Nations Universal Declaration of Human Rights, which was proclaimed following the end of World War II in 1948, was enacted in the hope that an ostensibly universal standard would serve to discourage the sort of barbarous acts witnessed in the first half of the 20th century. The preamble to the declaration explains that such actions had outraged the conscience of mankind.

The Declaration, which is in the form of a charter, generally uses the term *rights*. But the preamble describes the foundation of freedom, justice, and peace in the world as inalienable rights of all members of the human family. It also talks of fundamental human rights, in the context of promoting social progress, in terms of the dignity and worth of the human person and the equal rights of men and women. The use of the terms *inalienable* and *fundamental* does suggest that certain rights may be of greater significance or importance.

The charter also appears to promulgate rights of differing nature. In the first 20 articles, which include the rights of life, liberty and security, free speech, and freedom of worship, the right not to be tortured, the right to a fair trial, and the right to own property, the rights are arguably more concerned with individuals and with the notions of freedom and liberty. The articles thereafter are more communal and concern socioeconomic rights, such as the right to work, the right to just and favorable remuneration, the right to rest and leisure, and the right to periodic holidays with pay.

The first 20 articles of the charter are sometimes described as first-generation rights, whereas the rights that are more concerned with communal rights are said to be second-generation rights. Rights concerning the solidarity of communities are said to be third-generation rights. There is an abundance of modern philosophical and political discourse concerning the relationship between these first-generation rights and the so-called second- or third-generation rights.

The first-generation rights are generally expressed as freedoms. In relation to the people of the United Nations, they are rights to which each and every person is entitled. In Hohfeldian terms, they are privileges (freedoms) because their correlative is a "no-claim right."

Such rights are, however, problematic in that, arguably, a fair degree of material security is required if they are to be exercised. Thus, economic and social well-being, which is addressed in the later articles of the charter, are important in determining whether the freedoms expressed in the earlier articles are actually worth having. It is argued that first-generation rights are predicated on some notion of respect for human dignity and that the neglect of an individual's social or economic predicament is not consonant with that respect. Thus, economic security is necessary if first-generation rights are to be taken seriously. This line of argument ultimately leads to claims concerning welfare and for economic support and assistance.

Modern-Day Issues Concerning Rights

Claiming an entitlement as a "moral right" has become commonplace, and as Waldron explains, the language of rights now appears to be used to refer to any demand that an individual interest should be protected or promoted that is made from the individual's own point of view.

In recent debates, it has been suggested that we need some way of expressing that not all individual interests have sufficient importance to form the basis of rights. Given that rights may also generate more than one duty, we also need to understand whether the duties generated by a right have differing degrees of importance.

To categorize rights based on their moral importance is clearly problematic. John Rawls developed the idea of lexical priority in relation to his first principles of justice. But identifying certain rights as of higher priority and needing attention before others, as Rawls has pointed out, seems ill-suited to principles or moral considerations that are in many cases open-ended. Priority becomes even more problematic if we determine that a certain right is correlated with more than one duty. Such a priority may also result in an overly rigid approach to claiming an entitlement or a right.

Waldron poses a qualitative weighting as a means to determine the importance of different duties expressed as a fraction of the importance of the right from which they flow. But he ultimately dismisses this idea as unsustainable because it also requires prioritizing rights.

There remains a need to clarify exactly what is meant when we claim to have "a right." Theories abound, but they lack a consensus, or at least explanation in language that can be commonly understood by persons claiming entitlements or rights. The basis for making such claims, in many cases, is a "moral right" or a "human right," but modern-day societies have yet to determine what such rights actually comprise.

—Vanessa Stott

See also Animal Rights; Animal Rights Movement; Civil Rights; Communitarianism; Consequentialist Ethical Systems; Consumer Rights; Consumer's Bill of Rights; Corporate Rights and Personhood; Deontological Ethical Systems; Due Process; Duty; Employee Rights Movement; Entitlements; Equal Opportunity; Ethics, Theories of; Feminist Ethics; Freedom and Liberty; Gay Rights; Gender Inequality and Discrimination; Human Rights; Justice, Theories of; Legal Rights; Natural Law Ethical Theory; Normative Ethics; Nozick's Theory of Justice; Ought Implies Can; Paternalism; Patients' Bill of Rights; Pollution Right; Promises; Property and Property Rights; Rawls's Theory of Justice; Redistribution of

Wealth; Right to Work; Self-Ownership; Shareholder Activism; Side-Constraints; Social Contract Theory; Utilitarianism

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Right to Work

According to some accounts, the right to work denotes a basic human right; to others, it aims to remove the limitations to employment imposed by unions or, alternatively, takes away employment protections that unions have fought to attain. More recently, the right to work has been invoked as part of efforts to ensure a just and equitable workplace free from discrimination or hazards. In different ways, each of these interpretations is grounded in an understanding of work as a necessary component of human dignity and human flourishing.

A right is a claim that an individual or group may make against a society or state. The claim is limited by what is morally correct or upholds standards of justice. For every right, there is a corresponding responsibility both on the part of the right-holder and on the part of a second party who either enables or provides for that to which the claimant is entitled (positive rights) or does not infringe in areas of the claimant's life that are protected (negative rights).

Two broad-based categories of rights are civil or legal rights and moral rights. Civil or legal rights are rights that are guaranteed by law; they are created by a state to ensure the proper functioning of that state and the protection of the individuals who reside under the state's jurisdiction. Any given legal right may or may not be informed by a specifically perceived moral right but must be made explicit by the state through legislative or judicial decision making. Moral rights are construed more broadly to be universally applicable but may be divided into categories based on the identity of the rights-holders. A human right is a moral right that pertains to all human beings regardless of their political state or society. Human rights are determined according to widely accepted basic requirements for human dignity.

The Right to Work as a Human Right

Since work allows the individual to strive to achieve his or her fullest potential while also emphasizing a sense of social responsibility, it must be considered one of the requirements for human dignity. Within moral theory, then, the right to work is a positive moral right, thereby necessitating the assistance of others, and is generally understood to be one of the basic human rights.

Broadly construed, work is the exercise of a service, or a skill in the creation of a product, that is valuable to society. Work tends to be thought of as providing a service or skill in exchange for a wage; however, "work" might also include labor that does not receive a traditional wage but is nonetheless valued. Examples include traditionally uncompensated household tasks that are necessary for the running and maintenance of a family as well as other creative or valued tasks that may not always receive a wage, such as tutoring needy students or organizing a community garden. Human rights principles require that individuals have some social support in the form of wages or financial assistance from the state.

In 1948, the United Nations General Assembly adopted the statement of human rights called the Universal Declaration of Human Rights. The UN Declaration is not based on any particular political or religious system but is rather a general statement to which the signing countries can agree. It is an assertion of what the participating nations take to be the basic minimum standards of human dignity, that is, the basic standards by which an individual may not only survive but also thrive. This document is the most comprehensive and widely accepted statement of human rights to date. Article 23 (in four parts) and Article 24 of the UN Declaration assert a universal right to work as well as some of the necessary provisions included in that right.

The first paragraph of Article 23 of the UN Universal Declaration of Human Rights asserts the right to work. The work must be freely chosen rather than coerced or enslaved labor. In addition, the conditions and environment within which a person works must not be harmful to the person's health or dignity.

The second paragraph of Article 23 emphasizes the equality of all persons in work upheld through providing equal pay for equal work. Such a policy would in part mean that it violates basic rights to assign the most degrading or difficult forms of work to those individuals perceived to be already degraded or socially inferior, for whatever reason.

The third paragraph states that workers also have a right to a just wage. The just wage is determined according to the amount necessary to guarantee a family existence worthy of human dignity. Human dignity entails such basic needs as clean drinking water, adequate health care, proper shelter and clothing, a substantial diet, and basic education. If the wage is inadequate to provide such needs, then it is the responsibility of the state or the community to provide supplemental means of social protection.

The fourth paragraph in Article 23 ensures a worker's right to join a trade union or to form collective bargaining bodies. The UN specifies that this right is designed to protect the interests of the individual worker.

Article 24 asserts the importance of limiting work so that individuals may have time to develop other aspects of their human personality as well as spend time with family and friends. Thus, the UN includes a statement about the need for leisure time so as to ensure that while we validate the right to work we in no way validate or legitimate the exploitation of the worker.

Not all work supports or upholds the dignity of the individual; such labor would not satisfy the criteria for the human right to work. Some work may be demeaning or degrading or otherwise detract from a person's sense of self-esteem, autonomy, or responsibility. Additional aspects of assessing forms of work in fulfillment of the human right include the extent to which employees are incorporated into decision-making procedures that affect their work activity, the variety of tasks they perform, the degree of worker input into modifications of work load or production alterations, and the avoidance of hierarchies that dehumanize types of work.

While civil or legal rights generally mean the holder has a claim against another agent or state, as a moral right, the right to work operates somewhat differently. There is no single governmental office and no single person or group of people responsible for finding dignified, nonexploitative work for each and every human being. However, as a matter of public policy the state may be held responsible for unemployment. The right to work may function also to limit other rights and inform other obligations, as when the right to work conflicts with the right to private property.

Most rights also carry a corresponding obligation. In the case of work, there is both an obligation to oneself and to one's community. First of all, work fulfills a personal obligation in that it encourages or even requires that the individual determine certain aims or goals for himself or herself. These aims generally make use of one's unique talents or gifts. Our uniqueness helps determine our obligation to work. We are obligated to develop our talents to actualize our own potential.

In addition, our obligation to work extends to the community. The community provides certain social goods ranging from simple support to more detailed structures of exchange. Membership in a community entails reciprocal relations, whereby one gives of oneself in the form of time, talent, and goods while also receiving from others similar forms of support. These reciprocal relations allow individuals to pursue more specialized tasks precisely because they are ensured that those tasks related to daily living will be reciprocally exchanged for the specialized tasks some other individuals perform. In addition, the communal obligations of the right to work mandate mutual protection of that right. Thus, the right to work at times has been construed as a negative right insofar as individuals ought not to have their right to work infringed.

Right-to-Work Laws

Within civil society, the right to work frequently has been construed to mean a public policy of full employment. In the United States, this took the weakened form of the Employment Act of 1946, which stopped short of advocating full employment, and the Full Employment and Balanced Growth Act of 1974, which aimed at 3% unemployment. The Keynesian model of full employment in the United States contrasts with the predominant model in Western Europe that was influenced by trade unions and socialism. Sweden, for example, crafted an economic policy that recognized the right to work as a human right and emphasized economic security guaranteed by society.

Since the mid-19th century, trade unions have been instrumental in pushing public policy toward the goal of full employment. Ironically, labor politics in the United States during the latter part of the 20th century centered on a different conception of the right to work. Right-to-work laws are state constitutional amendments or legislative statutes that challenge union security or proscribe compulsory participation in a union. They specifically make the closed shop and the union shop illegal, but they also target the preferential shop and maintenance of membership programs. In a closed shop, only union members may be hired; in a union shop, employers may hire anyone, but employees must join the union within a specified time of employment. The preferential shop mandates priority hiring of union members and maintenance of membership requires union members to sustain their membership for the entire time of their employment contract. In contrast, the open shop allows the employer to hire employees regardless of union membership.

Right-to-work laws are based on Section 14(b) of the Labor-Management Relations Act of 1947, better known as the Taft-Hartley Act, and protect an individual's right to refuse membership in a labor organization. Individuals have a right not to join a union and ought not to be forced to pay dues to a labor union as a condition of their employment. The Taft-Hartley Act bans the closed shop, and Section 14(b) permits states to outlaw the union shop through state law.

The first right-to-work law was passed in Florida in 1944. Since that time, 21 other states have passed right-to-work laws, and Congress occasionally discusses a federal right-to-work law. Of course, numerous bills have also been introduced into Congress calling for the repeal of Section 14(b).

In contrast to the human rights account of the right to work, right-to-work laws are negative legal rights because they prohibit the infringement of a person's liberty. Nonetheless, defenders of the right to work demonstrate the link to human rights by emphasizing the individual employee's right to work regardless of union membership. Proponents of right-to-work laws further claim that they protect individual freedom and are neither pro- nor antiunion. Unions, they argue, often use member dues to support political candidates or causes that individual employees would not or may not choose to support. Forcing employees to join a union, then, forces them to contribute to causes they may find morally problematic or politically unsound.

Opponents argue that right-to-work laws or "right-to-work-for-less" laws are part of a systematic attempt to destroy collective bargaining and merely enhance the ability of employers to underpay their workers. Moreover, because unions also negotiate hours and working conditions, opponents argue that right-to-work laws invite unfair or even abusive treatment. Right-to-work laws, they argue, open the door for free riders to reap the benefits of union negotiation without contributing to the costs. Moreover, by appealing to the 1951 Supreme Court ruling in *Railway Employees v. Hanson*, supporters argue that unions protect and strengthen an individual's right to work, and those who benefit from the collective bargaining of unionism ought to contribute dues.

The right to work continues to take on new meanings as traditional workplaces adapt to the changing workforce. Affirmative action policies aim to remove barriers that limited the right to work for women and minorities. Dual-career families challenge traditional conceptions of work rights by demanding flexible schedules, family leaves, on-site child care, and family health provisions. Laws that protect against sexual harassment, gender discrimination, and hostile environment add further layers of complexity and increased importance to ever expanding social conceptions of the right to work.

—Sally J. Scholz

See also Age Discrimination; Dignity; Disability Discrimination; Employment Discrimination; Gender Inequality and Discrimination; Human Rights; Just Wage; National Origin Discrimination; Racial Discrimination; Reverse Discrimination; Wages for Housework

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RISK RETENTION ACT OF 1981

The Product Liability Risk Retention Act of 1981 sought to improve the availability and cost of product liability insurance to businessmen and municipalities across the United States by allowing similar businesses to form risk retention groups (RRGs) who could self-insure to cover product liability exposures. The Risk Retention Act reflects social organization and a decision that continues to evolve as to who bears the risks in society.

In 1986, the Product Liability Risk Retention Act was revised, expanded, and renamed the Risk Retention Act. The revised act established a new entity by which insurance buyers could purchase liability insurance: purchasing groups (PGs). A PG can be any group of persons with similar or related liability risks who form an organization to purchase liability insurance on a group basis. Unlike a RRG, a PG is not an insurance company. PGs are much easier to form and are not required to raise capital to file feasibility studies or to reinsure, as are RRGs.

For the RRGs and PGs to operate cost-effectively and efficiently across state lines, Congress inserted two types of federal preemption provisions. The first prohibits discrimination against RRGs and PGs by the states. On a practical level, once a RRG has obtained a license from its chartering state and has raised its capital, it can begin operations in other states almost immediately. The second prohibits a state from requiring any insurance policy issued to a RRG or any member of the group to be countersigned by an insurance agent or broker who resides in that state. This addresses the issue of states requiring every insurance policy issued in the state to be countersigned by an agent who is a resident of that state and who would be paid a percentage of the commission. RRGs, by definition, provide insurance to persons in the same type of business or industry, not to the general public. Therefore, the state requirement for a resident agent to sell insurance seems to add nothing but cost. Although the Liability Risk Retention Act is a federal law, it has no enforcement mechanism of its own. RRGs are regulated by the state in which they are registered. Regulation of PGs entails not only the domiciliary state of the PG but also the regulation of the PG's insurer.

RRGs benefit from the act because it allows members to control their own program, obtain rate stability over the long term, and implement effective loss control programs. They may obtain dividends for good loss experience and have access to reinsurance markets, all of which improves their ability to maintain a stable source of liability coverage at affordable rates. The major benefit for PGs is the ability to negotiate tailor-made coverage at favorable rates with insurers.

The natural catastrophes of the 1990s drove up the price of commercial property insurance and increased discussion about the need to broaden the act to allow RRGs to cover property risks. Although such legislation would be welcomed by RRGs, the National Association of Insurance Commissioners (NAIC) opposes expansion of the 1986 act on the grounds that a lack of any guaranty fund protection could lead to a disproportionate number of bankruptcies of RRGs. The NAIC also argues that although premiums may be high, there is no actual shortage of property insurance that is not addressed by state-based solutions that are mindful of insurer bankruptcy. At the time of this writing, legislation to expand the 1986 act is being reviewed by a congressional committee.

—Lori S. Kolb

See also Interstate Commerce Commission (ICC); Market Power; Regulation and Regulatory Agencies; Unfair Competition

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Rocky Flats

Rocky Flats Nuclear Weapons Plant (Rocky Flats) in Jefferson County, Colorado, was a nuclear weapons production site. From 1952 to 1989, Rockwell International produced plutonium triggers for the U.S. Department of Energy (DOE) for nuclear weapons. After its cleanup in 2006 (scheduled), the site will be designated a National Wildlife Refuge. Rocky Flats has been controversial regarding issues such as regulation, government oversight, community involvement, use of risk-based analyses, cleanup standards, and disposal of radioactive waste.

Operations were on a 384-acre portion of the 10-square-mile site, 10 miles northwest of Denver. Community groups expressed concerns over contamination and lack of oversight by the DOE. Major sources of contamination on- and off-site were two fires (1957, 1969), an accidental release of plutonium into the air in 1974, leakage of metal-laden oil from barrels stored outside since 1958, and a chromic acid spill in 1989. The use of corrosive and radioactive materials, storage of hazardous and radioactive wastes, and spraying wastewater resulted in contamination on- and off-site. Additional problems included safety issues, decreased staffing, breakdown of controls in the radiation compliance programs, and organizational independence.

Following an FBI raid in 1989, Rockwell settled out of court in 1992 admitting to environmental crimes and paid an $18.5 million fine, the largest environmental penalty ever imposed at that time. In 1989, EG&G Technical Services became the prime contractor for the site. EG&G planned to resume production but stopped due to performance problems. In 1993, the DOE revealed that the site had at least 14 tons of plutonium, 7 tons of enriched uranium, 281 tons of depleted uranium, 65 tons of beryllium, and large amounts of other toxic chemicals. Surface soils had high concentrations of plutonium-239, estimated at almost 380 times the background concentration, or level naturally or previously occurring, and a significant inhalation hazard. Although conclusive evidence of health problems in the community due to exposure is not available, community groups and health studies emphasize the potential risks from accidental releases and continual operations. Studies of the workers' health continue; to date elevated risk of disease and chromosome damage related to radiation exposure has been seen in some plant workers.

The DOE initially estimated that the cleanup would take 70 years and $36.6 billion. A joint venture of Kaiser Engineers and CH2M Hill (environmental and engineering firms), Kaiser-Hill proposed a cleanup that would take 7 years costing $6 billion. Citizen groups called the latter plan a "dirty closure" as it would leave elevated levels of plutonium in the soil and groundwater, and the contaminated building would be buried. When Kaiser-Hill and DOE agreed to a 7-year plan costing $7 billion, community groups were angered over the lack of citizens' input. Debate involved several stakeholders, including DOE-sponsored organizations and grassroots organizations.

By designating the end use of Rocky Flats as a National Wildlife Refuge, the DOE tailored remediation goals to meet less stringent legal requirements, since the risk standard is based on the "maximally exposed individual" on the future site—a wildlife refuge worker. By using a risk-based end state, costs were lower than if the land was to be cleaned up to background concentrations.

—Virginia W. Gerde

See also Environmental Assessment; Hazardous Waste; Pollution

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Role Model

According to philosophers, the relationship between ethics and role modeling extends back to Aristotle, who said that the spirit of morality was awakened in an individual through the witness and conduct of a moral person. Social scientists bear this out, finding that the modeling process is a common means of observational learning and of transmitting values, attitudes, and behaviors. People learn much of what they know, not through direct experience but by observing the behavior and experiences of others. Thus, much learning, of behavior generally and ethical behavior more specifically, occurs in an anticipatory manner as individuals are informed about the benefits of the modeled (ethical) behavior and the costs of inappropriate behavior.

When an individual becomes a role model for others, she or he becomes a target of identification and emulation. Theoretically, anyone (e.g., a coworker) can act as a role model for another, but leaders are likely role models in organizations because of their status, success, and power to affect the outcomes of others. In the organizational literature, role modeling is viewed as essential to leadership and, in particular, to the transformational leadership style.

Empirical research suggests that individuals can become ethical role models by engaging in behaviors that are thought to be altruistically motivated and normatively appropriate (e.g., honesty, fairness, caring). Such behaviors increase the model's attractiveness, credibility, and legitimacy, all requirements for effective role modeling. In an interview study, MBA students at three universities were asked to identify the characteristics of individuals they think of as ethical role models. They identified a number of interpersonal behaviors displayed by their ethical role models, such as care and concern, integrity, trustworthiness, humility, respectful treatment even in difficult times, explanations for negative outcomes, and openness to input and criticism. The interviewees also described ethical role models as taking responsibility for their own ethical failings and accepting the mistakes of others. Ethical role models were described as coaches who focus on improvement and also as having a consistent ethical vision and behavior that play out in all areas of the role model's life. They communicate high standards to others and hold themselves and others accountable to those standards. Ethical role models put ethics above other personal or company interests, sacrifice their own needs for the needs of others, and have a long-term multistakeholder perspective. The researchers found that thinking of someone as a role model requires a close working relationship and, somewhat surprisingly, does not require business success. Rarely were senior executives identified as ethical role models. Rather, interviewees thought of someone with whom they worked closely whose integrity they admired. It remains an open question whether ethical role models can be developed.

—Linda K. Treviño

See also Mentoring

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Roles and Role Morality

The notion of role morality is based on the belief that individuals and groups have certain duties and virtues as a result of the specific roles they occupy within society. A conceptual framework for understanding these specific moral obligations can be found in Greek virtue ethics. Within the thought of Aristotle, virtues were carefully cultivated character traits that were teleologically related to the good life or happiness of the community as a whole. For a community to be happy, or prosper, each individual had to cultivate the virtues specific to his or her role in society. If you were a soldier within the Greek city-state, you had to cultivate the virtue of bravery; if you were a worker, you had to be diligent; and as a ruler, you had to be wise. The communitarian philosopher, Alisdair MacIntyre, argues that duties and virtues are cultivated within certain practices in society and that we cannot understand our moral obligations without reference to such a social context.

A contemporary application of role-specific virtues and duties can be found within professional ethics. As a society, we expect professionals to fulfill their role properly by displaying certain virtues and responding to specific moral obligations. We trust professionals to be custodians of certain specific public goods: Legal professionals serve justice and, therefore, have to be fair; medical professionals protect and nurture our physical well-being and have to display the virtue of care; and accountants vouch for the veracity of financial statements and have to be honest. If professionals fail to protect these basic goods or neglect these virtues, society can no longer allow them to fulfill their specific roles. Arthur Andersen, the auditors in the Enron scandal, exemplifies how a lack of honesty and failure to protect the public can result in the loss of an auditing practice.

Role morality is sometimes contrasted with personal morality. Virtues and duties required in a specific role may conflict with one's personal sense of what is morally appropriate. It was Max Weber's contention that individual morality is subjugated to the functionally specific rules and roles of the bureaucratic organization. The danger that this subjugation presents is that of the compartmentalization of an individual life. Alisdair MacIntyre points out that individuals lose a sense of overriding concern for what it means to be human and stop asking moral questions apart from those required by specific roles. For example, executives may have two radically different opinions when asked about the need for environmental protections in two different capacities. When confronted with this issue in their capacity as parents, executives will typically support environmental protection, but in terms of their fiduciary duties within the corporation, they will often not feel responsible for implementing environmentally friendly business practices.

The phenomenon of amoralization, or the inability or unwillingness to recognize something as a moral issue, has also been linked to the limitations that role morality imposes on one's sense of moral imagination. This problem is exacerbated by the fact that society tends to assign legal responsibility for the avoidance of harm only to those within a specific role and not to human beings in general. For instance, within most jurisdictions, failure to assist a drowning person is not technically illegal, but a mother's allowing her child to die of neglect is. In the business environment, this is manifested in the fact that legal concepts such as the "business judgment rule" assign executives certain rights and liberties to take risks to maximize shareholder value. The flip side of this coin is that legislation like the Sarbanes-Oxley Act of 2002 increases the risk of individual liability of CEOs and CFOs by requiring sign-offs verifying the accuracy of financial statements.

—Mollie Painter-Morland

See also Accounting, Ethics of; Arthur Andersen; Autonomy; *Challenger* Disaster; Enron Corporation; Fiduciary Duty; Professional Ethics; Sarbanes-Oxley Act of 2002; Virtue Ethics

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ROUSSEAU, JEAN-JACQUES (1712–1778)

Jean-Jacques Rousseau, who lived most of his life in France but sometimes identified himself as "a citizen of Geneva," was a philosopher who wrote novels, letters, autobiographical reflections, and essays that advanced positions that were at once provocative and paradoxical. He is remembered most for his political thought, which is both a critique of existing monarchies and a reaction against the Enlightenment and the then revolutionary individualism of Thomas Hobbes and John Locke. His writing first gave impetus to the French Revolution, later lent weight to the Romantic movement, and continues to be studied for its attempt to confront, define, and solve the problem that political societies are inescapably made up of naturally asocial creatures. His several solutions to this problem join in offering a powerful moral critique of the "bourgeois," the sort of person Rousseau sees as being fostered by large, democratic nation-states founded on the rights of the individual to pursue property.

Rousseau accepts Hobbes's view that human beings are not "political animals" but are asocial by nature. The challenge of politics is hence to design institutions that are legitimate and function well with creatures whose primary natural concerns are themselves, not the common good or unselfish virtue. But Rousseau's view of human asociality is much more radical than Hobbes's. Rousseau denies that one can discover human nature simply by observing what happens when enforced law is removed, as Hobbes implied, for the people who live in civil society have been deeply shaped by this experience. Their conduct, with or without enforced law, is a reflection on socialized man, not on natural man. To discover natural man, one must go back much further in the history of the species, and this leads to a much different set of standards by which to guide and assess political life. Indeed, for Rousseau, natural man is scarcely human at all. He lacks language, reason, imagination, and the inflated desires that these nurture.

Because Rousseau's natural man is without pride, religious opinions, or exaggerated desires, he is also free from many of the motives that drive human beings into conflict. True, he is an uncivilized brute, but he is a peaceful brute, a "noble savage," capable of enjoying "the sweet sentiment of existence." Whereas Hobbes used the horrors of the state of nature to underscore the blessings brought by stable government, Rousseau uses natural man's freedom, self-sufficiency, equality, wholeness, goodness, and tranquility to argue that life in civil society has made human beings weaker, less happy, more artificial, and deeply corrupt. For Rousseau, the political problem is not mainly one of keeping the peace and increasing material prosperity; more important, he argues, are political principles that look to human happiness, wholeness, and virtue.

It is a modern political idea to affirm and stress a natural right of individuals to pursue property. Even before this idea takes hold, Rousseau expresses powerful reservations against it. He does so partly on the ground that the inequality between rich and poor is hardly natural or based on natural rights (Locke's argument that labor constitutes a title to ownership to the contrary notwithstanding), but he also stresses the moral changes that accompany this inequality: Avarice and ambition come to be dominant passions, and unhappiness is added to injustice. Rousseau is thus a critic of the sort of human being who is devoted to the pursuit of self-interest, and he sees this sort of person as justified and encouraged by modern liberal institutions. Adam Smith would later show that, under capitalism, it is not from "the benevolence of the butcher, brewer, or baker that we expect our dinner, but from their regard to their own interest." Rousseau would grant this but would be quick to add that if it is not in their interest to feed us, modern principles and institutions will incline others to let us starve. More fundamentally, what if true happiness requires that one be benevolent or good, not merely well fed? Modern liberalism may succeed in producing "the wealth of nations," but only, if Rousseau is correct, by impoverishing the individuals who seek their daily bread within these wealthy nations.

Rousseau openly admitted to writing "paradoxes." Through these, he lent support to the forces that would overthrow the French monarchy, but at the same time he laid a foundation for opposing any liberal regime that might replace it. Rousseau's diagnosis of the problem of natural man in unnatural society went so deep that it could not be followed by a simple solution. He did present "solutions" both for civil society (*On the Social Contract*) and for the individual (*Emile*), but both are so complex and demanding that neither serves as a pattern for easy imitation. In Rousseau, one finds no easy solutions but rather stimuli for romantic longings that cannot be satisfied by getting and spending; for outrage at the callous mistreatment of the poor by the rich; and for the urge to go "back to nature" to live a simpler but happier, more honest existence. Above all, one leaves Rousseau with the sense that the pursuit of luxury and superfluity may bring tangible benefits while yet also coming at an enormously high social and human cost.

—*Wayne Ambler*

See also Hobbes, Thomas; Human Nature; Individualism; Liberalism; Locke, John; Smith, Adam; Social Contract Theory

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Royal Ahold Company

A Dutch-listed company, Royal Ahold NV, was first established by Albert Heijn as a small grocery store in 1887 in Zandaam, the Netherlands. By 2005, it was one of the world's leading food providers with more than 240,000 employees, a customer base of more than 300,000 independent and chain businesses, and sales of more than 44 billion euros in 2005. In 2003, however, Royal Ahold was rocked by a financial scandal resulting in the firm restating its earnings by $1 billion for 3 years ending 2002 and paying $1 billion in December 2005 to settle a class-action lawsuit with shareholders. The former CFO who was fired in 2003, Michiel Meurs, was singled out by a Dutch enterprise court in 2006 as bearing most of the blame for the accounting scandal. The former CEO, Cees van der Hoeven, who resigned when the fraud was uncovered, was also found complicit. The accounting scandal involved overlooking weak internal controls because Royal Ahold emphasized achieving double-digit growth within its recently acquired subsidiary, U.S. Foodservice.

Starting in 1995, Royal Ahold achieved rapid growth by purchasing subsidiaries around the globe. It spent approximately $19 billion in acquisitions over a 6-year period. The Dutch enterprise court in 2006 stated that Royal Ahold knew about the weak internal controls within the U.S. Foodservice subsidiary before it was acquired in 2000 and accused Royal Ahold of failing to act even after warnings of continued accounting weaknesses.

The February 2003 discovery of accounting fraud due to overstatements of income nearly bankrupted the entire firm. Characterized as "Europe's Enron," Royal Ahold has made significant changes in its financial and operating controls as well as increasing transparency with investors. Financial statements for the fiscal years 2000, 2001, and 2002 were restated with significantly lower net earnings and earnings per share.

The U.S. Securities and Exchange Commission (SEC) also investigated Royal Ahold and its various operating companies, including its U.S. Foodservice subsidiary. A final settlement with the SEC was reached in October 2004. Under the agreement, Royal Ahold was not required to pay any fines or admit to any wrongdoing for its actions, which caused it to restate earnings by $1.2 billion over 3 years.

The SEC didn't fine the company because Royal Ahold cooperated with investigators. Royal Ahold reported the misconduct itself and conducted an extensive internal investigation that went beyond U.S. Foodservice. According to the SEC, Royal Ahold also gave up attorney-client privilege, made personnel available for interviews, and fired employees responsible for the irregularities.

After the fraud crisis in 2003, stronger financial controls, direct oversight, better governance mechanisms, and tighter controls on vendor contracts provided additional accountability and transparency of the firm to many government agencies in the Netherlands and the United States, investors, and employees. As part of Royal Ahold's "road to recovery," numerous steps were undertaken to increase trust. Among the steps was the appointment of a chief corporate governance counsel who is a member of the executive board.

One in a continuing line of accounting fraud discoveries, Royal Ahold joined the ranks of Enron, WorldCom/MCI, Tyco, and Adelphia Communications as lightening rods depicting managerial exuberance and accounting fraud. Unlike Enron, WorldCom, and Adelphia Communications, however, Royal Ahold did not declare bankruptcy and emerged 2 years later in stronger financial shape with better operational controls. Today, Royal Ahold continues to operate through subsidiaries and joint ventures of food retail and food service activities predominantly in the European Union (EU) (e.g., operating supermarkets, hypermarkets, and convenience stores, including Albert Heijn, Gall & Gall, Etos, and Albert Zakelijk) and the United States (e.g., owning food service stores, including Stop & Shop, Giant, and Tops and its e-commerce grocery retail delivery service, Peapod).

—*Jennifer J. Griffin*

See also Accounting, Ethics of; Adelphia Communications; Enron Corporation; Fraud; Tyco International

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Rural Electrification Administration

The Rural Electrification Administration (REA) was created during the Depression era to provide electricity to rural areas. President Franklin D. Roosevelt established the REA through Executive Order 7037 on May 11, 1935. In 1939, the REA became part of the Department of Agriculture (USDA). Subsequently, the agency's role was expanded by Congress to include directing a rural telephone program in 1949 and the delivery of rural Internet-based broadband telecommunications programs in 2002. In 1994, the Department of Agriculture was restructured under the Federal Crop Insurance Reform and Department of Agriculture Reorganization Act. This restructuring ended the REA but created the Rural Utility Service (RUS), which was charged with administering rural utility programs, rural housing programs, community facilities programs, rural water and waste disposal programs, and select rural business programs.

The vision of the Rural Development unit (which runs the RUS programs) of the USDA is "a rural America that is a healthy, safe, and prosperous place in which to live and work." Its mission is "to increase economic opportunity and improve the quality of life for all rural Americans." To serve its mission, the agency provides direct loans, loan guarantees, and modest levels of grant assistance in public-private partnerships. The RUS offers its services to rural cooperatives, nonprofit associations, public bodies, and for-profit utilities. The agency estimates that it supports the development of economic opportunity for more than 60 million Americans living in the 80% of the country classified as rural.

The Electric Program is the largest of the infrastructure programs of the RUS, accounting for approximately $28.5 billion of its fiscal-year 2006 loan portfolio. Water and telecommunications projects account for the remaining $12.5 billion of the agency's loan portfolio.

The agency has identified two key strategic initiatives: broadband service access in rural areas to provide for equal economic development opportunity and a grant program for high home energy cost areas. The RUS views affordable broadband as an "essential business tool." The agency is committed to the provision of such technology that will improve distance learning opportunities and telemedicine care for sparsely populated areas. The energy grant program is targeted to pockets of homes in nine states with energy costs exceeding 275% of the national average. This program seeks to improve generation, transmission, and distribution facilities for those communities.

The provision of electrical service to rural America by the government through the REA was not without its detractors; for example, the bituminous coal industry objected to the federal government's entry into the power business through subsidies using taxpayers' money. Although large private power companies may have been capable of generating and delivering electrical power to rural customers during the Depression, few actually provided such service, citing prohibitive costs and customer payment risks. Similar arguments are made regarding current RUS initiatives. However, the RUS essentially serves as a financing agency for infrastructure needs, providing 25-year loans to private companies, cooperatives, and public agencies at interest rates approximating the prevailing rate for government obligations.

—Frank L. Winfrey

See also Great Depression; Public Utilities and Their Regulation

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Sarbanes-Oxley Act of 2002

In response to major corporate accounting scandals at large U.S. companies such as Adelphia, Computer Associates, Enron, and WorldCom, to name a few, the United States Congress passed a sweeping legislation in July 2002 aimed at improving the integrity of financial statements and related audits and mandating certain corporate governance practices within publicly traded U.S. companies. This legislation, called the Sarbanes-Oxley Act of 2002 (referred to here as Sarbanes-Oxley or the Act), has been considered by many to be the most significant new law since the passage of the Securities and Exchange Acts of 1933 and 1934.

The Act is most commonly referred to by its section numbers. Each section has specific requirements, affecting either the external auditor or a company or both, or in some instances, creating additional government oversight of companies and their auditors.

Some of the most important sections of the Act and their related requirements are discussed in the following sections, grouped into related categories.

Enforcement and Penalties

The Act has created new mechanisms to monitor the quality of audits performed by public accounting firms that audit publicly traded companies, establishes accounting standards, and includes penalties to punish officers of companies that attempt to profit from fraudulent activities.

Section 101

It established a newly created and separate nonprofit corporation, the Public Company Accounting Oversight Board (PCAOB; referred to here as the Board) to "oversee the audit of public companies that are subject to the securities laws . . . in order to protect the interests of investors and further the public interest in the preparation of informative, accurate, and independent audit reports for companies the securities of which are sold to, and held by and for, public investors." The Board shall be operated under the auspices of a five-member commission, appointed by the Securities and Exchange Commission (SEC; referred to here as the Commission). The Board may have only two members who have been or are Certified Public Accountants (CPAs). Each member of the board is expected to serve on a full-time basis and may not engage in any other business or professional activity during their term of appointment. Board members are appointed for a 5-year term and may only serve for two terms.

Section 102

Any public accounting firm that desires to be appointed as the auditor for a publicly traded U.S. company (i.e., an issuer or a registrant) must register with the PCAOB to perform such audits. In addition, the firms must pay an annual registration fee and provide periodic reports to the Board. The firms are also subject to an inspection process as defined by the Board (see Section 104).

Section 103

This gives the Board the authority to establish, as it deems appropriate, auditing standards to be used by registered public accounting firms in their conduct of financial statement audits of issuers and in the preparation and issuance of their audit reports. The Board issued PCAOB Auditing Standard No. 1 (AS1), which adopted all the previously issued and existing *Statements of Auditing Standards* of the Auditing Standards Board of the American Institute of Certified Public Accountants (AICPA) in effect as of April 16, 2003. AS1 also provided the standard report format for registered public accounting firms to use when issuing their auditor's report on an audit of an issuer's financial statements. Section 103 also set standards for the retention of the registered firm's audit documentation, requiring firms to maintain their documentation for 7 years from the auditor's report release date, unless a longer period of time is required by law.

Sections 104 and 105

The PCAOB was charged with conducting "a continuing program of inspections to assess the degree of compliance of each registered public accounting . . . with this Act" as well as with any standards or rules issued by the Board or the SEC related to the performance of audits or issuance of audit reports. The inspection program replaced the previous peer review process conducted by member firms of the SEC Practice Section of the AICPA, considered by some to be ineffective at detecting financial statements lacking adherence to auditing standards. These inspections are to be performed annually for all registered firms that audit 100 or more issuers and at least once every 3 years for firms that audit 100 or fewer issuers. A report of the results of the inspection shall be issued, the registered firm shall have the right to respond to the findings of the report, and the information shall be provided to the public, absent any confidential or proprietary information related to the firm. The PCAOB has accomplished this by making the reports resulting from their inspection process available on the Board's Web site (www.pcaobus.org). The Board was also granted the power to investigate and discipline registered firms, including requiring and obtaining testimony, producing documents, and requesting other forms of cooperation. Failure to comply with the Board's requests or provisions of the Act can result in sanctions, temporary or permanent revocation of registration, limitations on activities, and monetary penalties.

Section 107

The SEC shall have oversight and enforcement authority over the Board as specified in the Act. Sarbanes-Oxley requires that the PCAOB submit their proposed rules for registered firms or issuers to the Commission for their approval.

Section 108

The Act allows the SEC to recognize, as generally accepted for purposes of the securities laws, accounting standards that have been issued by a private standard-setting body that has a board of trustees committed to serving the public interest and will be responsive to emerging accounting issues, business practices, and changes in the business environment. This was de facto confirmation of what has already been occurring in practice for many years. The Commission, which was granted the authority to promulgate accounting standards by the Securities and Exchange Act of 1934, has relied almost exclusively on the Financial Accounting Standards Board (FASB) and its predecessor organizations for standard setting.

Section 109

This section of the Act establishes a funding mechanism to provide for the activities of the Board and the standard-setting body discussed in Section 108, in the form of annual accounting support fees paid by issuers. The Board and the accounting standard-setting body establish their annual operating expense budgets, and these amounts are allocated to issuers by a formula based on an issuer's average monthly market capitalization during the preceding year as a percentage of the total average monthly market capitalization for the preceding year.

Section 304

If an issuer is required to restate its financial statements as a result of misconduct with any financial reporting requirement under the securities laws, the chief executive officer and the chief financial officer of the issuer shall be required to reimburse the issuer in the amount of any bonus, incentive-based compensation, or equity-based compensation that the person received during the 12 months following the issuance of the misstated financial statements, and to reimburse the issuer for any gains that they may have realized from sale of the issuer's securities during the same 12-month period.

Section 408

The Act requires that the SEC shall review the periodic filings of issuers (e.g., Form 10-K) no less often than once every 3 years.

Section 906

This section of the Act is part of the "White-Collar Crime Penalty Enhancement Act of 2000" and provides for the imposition of criminal fines and penalties on chief executive officers and/or chief financial officers who knowingly certify that their financial statement filings are accurate when they are not (see the discussion of Section 302 below). The fines and penalties can amount to as much as $5,000,000 and imprisonment of up to 20 years.

Reporting Requirements

The Securities and Exchange Acts of 1933 and 1934 require issuers of publicly traded securities to provide certain periodic filings with the SEC, such as quarterly reports (Form 10-Q), annual reports (Form 10-K), and current reports (Form 8-K). In response to significant misstatements of financial statements by some companies, the Act includes provisions requiring executive officers to certify their company's financial statements and assess the effectiveness of their systems of internal control.

Section 302

The principal executive officer or officers of an issuer were always required to sign a company's periodic reports being filed with the Commission. The Act goes further, requiring the principal executive officer(s) and principal financial officer(s) to certify in each annual or quarterly report filed with the Commission that (1) they have reviewed the report; (2) to the best of their knowledge, the report "does not contain any untrue statement of a material fact or omit to state a material fact necessary in order to make the statements made, in light of the circumstances under which such statements were made, not misleading"; (3) to the best of their knowledge, the financial statements included in the filing present fairly in all material respects the financial position and results of operations for the issuer for the period(s) presented; (4) the signing officers are responsible for disclosure controls and internal controls over financial reporting, have evaluated the effectiveness of the issuer's internal controls as of a date within 90 days prior to the report date, and have presented their conclusions in the report about the effectiveness of internal controls; (5) the signing officers have disclosed to the issuer's auditor and audit committee any significant deficiencies in design or operation of internal controls, any material weaknesses in internal controls, or any fraud (whether or not it is material) involving management or employees who play a significant role in the system of internal control; and (6) the signing officers must indicate whether or not there have been any significant changes in internal controls or other factors that could affect internal controls subsequent to their evaluation date. The wording of the management certification included in Section 302 must be used *verbatim*; issuers are not permitted to adjust the language, and it must be included within the periodic report.

Section 404

The Act requires that the SEC develop requirements that each annual report filed (Form 10-K) by an issuer must include a report on internal control that shall "1) state management's responsibility for establishing an adequate system of internal control and procedures for financial reporting and 2) include an assessment, as of the end of the issuer's most recent fiscal year, of the effectiveness of the issuer's internal control structure and procedures for financial reporting." If management determines that it has one or more material weaknesses in its internal control system, then they cannot conclude that they have an effective system of internal control. In addition, Section 404 requires that the issuer's registered public accounting firm "shall attest to, and report on, the assessment (i.e., of internal control) made by the management of the issuer." The auditor's report on management's assessment of internal control shall be made in accordance with guidelines issued by the PCAOB and shall not be an engagement separate from the audit of the issuer's financial statements. This is referred to as an integrated audit, incorporating the financial statement and attest report on management's assessment of internal controls.

This three-paragraph section of the Act has been the subject of much discussion, criticism, and complaint, and there have been outright calls for its reversal. Many business executives have complained that the costs of Section 404 have far exceeded the possible benefits. Proponents claim that this is the only way to ensure that issuers will devote the appropriate resources to ensure that adequate internal control systems are in place to produce accurate financial statements. Others claim that this section has also rewarded the public accounting firms with additional fees when they were implicit in some of the accounting scandals that have occurred. The first year that companies were required to report under Section 404 was the year ending after December 15, 2004. Moody's, the rating agency, estimates that approximately 6% of companies reported material weaknesses in their internal controls and procedures for financial reporting. While Section 404 of the Act has received the most criticism, a previous law, the Foreign Corrupt Practices Act, which was passed in 1977, already required public companies to maintain an adequate system of internal control. It is unclear how vigorously this law was enforced.

Section 409

This section of the Act requires that the SEC issue new rules requiring companies to disclose additional information regarding material changes in their financial condition or operations on a rapid and current basis. The SEC subsequently amended its rules for the filing of Form 8-K, requiring that it be provided within four business days of the occurrence of the event.

Auditors

Prior to the passage of the Act, it was not uncommon for the auditors of publicly traded companies to provide additional services to their audit clients. These services typically involved various types of business consulting, and in many instances, the fees for these services exceeded the fees charged for the financial statement audit. Many observers believe that this created an inherent conflict of interest for the auditor and that the auditor could not carry out a thorough audit of an issuer's financial statements if the auditor was also concerned with whether or not significant consulting work would be retained. The Act provides specific rules on what services the auditor of an issuer may provide and also addresses the issue of a registered firm's employees becoming employed by an issuer.

Section 201

Registered public accounting firms that perform an audit of an issuer's financial statements are specifically prohibited from performing any nonaudit service, including "a) bookkeeping or services related to accounting records or financial statements of the audit client; b) financial information system design and implementation; c) appraisal or valuation services; d) actuarial services; e) internal audit outsourcing activities; f) management functions or human resources; g) broker or dealer, investment adviser or investment banking services; h) legal services and expert services unrelated to the audit; i) any other services that the Board determines, by regulation, is impermissible." The effect of Section 201 has been to limit the registered public accounting firm who performs an issuer's audit to performing the audit and preparing the company's income tax returns. In addition, the issuer's audit committee must now approve any nonaudit services performed by the registered public accounting firm in advance (Section 202).

Section 203

The Act requires that the lead audit partner of the registered public accounting firm having primary responsibility for the audit and the audit partner responsible for the reviewing of the audit (i.e., the concurring partner) be changed or rotated from the audit every 5 years.

Section 206

Historically, many employees and even partners of public accounting firms accepted employment opportunities with client companies when they decided to make a career change from public accounting. The act makes it more difficult to do this because an employee of a public accounting firm must wait for at least 1 year before he or she accepts a position in a financial reporting oversight role with a client company.

Corporate Governance

Many of the financial statement scandals occurring in the late 1990s and early 2000s have been attributed to lack of proper oversight by corporate boards of directors and, specifically, their audit committees. The Act includes specific rules expanding and clarifying the composition and responsibilities of audit committees. In addition, it provides rules for corporate officers related to transactions that they might engage in related to an issuer's securities as well as other transactions with the company.

Section 301

This section of the Act provides specific guidance on the composition and duties of an issuer's audit committee. The audit committee must consist of members of the issuer's board of directors, and the members must be independent. Independence of the audit committee member means that he or she cannot be a member of management, cannot accept any consulting or compensatory arrangement with the issuer, and must not be affiliated with the issuer in any other way. At least one of the committee's members must be considered a *financial expert* having thorough education and (1) an understanding of generally accepted accounting principles (GAAP) and financial statements, (2) experience in financial statement preparation or auditing, (3) experience with internal controls, and (4) an understanding of the functioning of an audit committee. Audit committees without a financial expert must disclose the reasons why they do not have such a person on their committee.

The audit committee is now directly responsible for the appointment, compensation, and oversight of the registered public accounting firm. In addition, the committee has the right to engage its own advisers to carry out its duties and responsibilities, and the issuer must provide the necessary funding. Furthermore, the committee must establish procedures to receive and address complaints received by the issuer regarding accounting, internal accounting controls, or auditing matters, and it must provide for confidential submission of employee concerns regarding questionable accounting or auditing matters. Many audit committees have established anonymous hotlines to accept these types of complaints and concerns.

Section 204

Traditionally, public accounting firms have met with the audit committees of their clients at the conclusion of a financial statement audit. This section of the Act mandates that certain communications take place between the auditor of the issuer and its audit committee. Specifically, it requires that the auditor report to the committee on all critical accounting policies and practices of the issuer, any alternative treatments of accounting matters discussed with management of the issuer, and any other material written communications between the registered public accounting firm and the issuer's management, such as a letter of recommendations on internal controls or a list of accounting adjustments that were detected during the audit but not recorded (referred to as passed adjustments).

The Sarbanes-Oxley Act has mandated that companies make significant changes in corporate governance, requiring more proactive audit committees and holding senior management more responsible for the information presented in a company's financial statements. The Act has changed the role of the registered public accounting firm as well. Firms now report directly to the audit committees of their clients and are subject to the expectations of their new government regulator, the PCAOB. Many critics of the Act contend that the U.S. Congress has attempted to legislate ethics into the corporate workplace. In addition, there are concerns that implementation of the Act gives U.S. public companies inherent disadvantage in raising capital in international markets, as no other country has such significant laws and regulations regarding financial reporting and corporate governance. Will the changes brought on by the Act improve the integrity of financial reporting, the quality of audits of financial statements, and the behavior of corporate management and directors? Will U.S. public companies experience difficulty in their attempts to raise capital? Only the passage of time will permit a determination of the effectiveness of this far-reaching legislation.

—Robert J. Kollar and Sharon L. Green

See also American Institute of Certified Public Accountants (AICPA); Certified Public Accountants (CPAs); Financial Accounting Standards Board (FASB); Fraud; Internal Audit; Public Interest; Securities and Exchange Commission (SEC)

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SATISFICING

Satisficing takes place when an individual arrives at a decision that is good enough according to the information at hand. When a person satisfices, he or she is not necessarily arriving at the best decision but at one that is considered adequate for the achievement of the current goals. Satisficing is not a process in which the first-fitting solution is chosen but, instead, is a consideration of what has worked well in the past. It is often used during cognitive tasks such as problem solving where the best solution is difficult to establish. An obstacle to satisficing, however, is that individuals do not usually have access to all the alternatives available because they are simply too numerous to contemplate. As a result of these cognitive restrictions, it is sometimes rational to choose an option that may not necessarily be viewed as optimal. In contrast to satisficing, optimizing behavior attempts to determine the best possible way for an individual to attain his or her most desirable goal. Although optimizing can provide the paramount solution for long-term goals, most of everyday decision making is based on the need to satisfice. In business situations, satisficing is frequently seen as cheaper than optimizing because looking for other alternatives would be time consuming and unnecessary when a viable solution already exists.

The term *satisficing* was introduced in the work of Herbert Simon (winner of the Nobel Prize in economics in 1978). Simon believed that human wisdom is bounded or limited by incomplete knowledge and an inability to predict all the consequences of decisions. Since these cognitive boundaries do not allow the processing of all possible information, individuals are forced to pick the most satisfactory solution from those they can envision.

Selling an item (such as a car or home) provides an example of satisficing in a dynamic decision-making environment. Possible options are explored in the form of offers made on the item being sold, and the seller is forced to eventually stop taking offers and finalize the sale. In essence, the seller must arrive at the offer deemed good enough when considering all the offers on the table.

Satisficing also has moral implications that must be considered. Situations that take into account a multitude of people or decisions such as shareholder wealth maximization or stakeholder analysis may pit optimization against satisficing. As a result, it is possible that managers seen as satisficing will be criticized for their lack of insight or ability to see the "big picture," including their duties or obligations to all business constituents. In terms of moral theories, satisficing may be viewed as a form of consequentialist decision making. Satisficing utilitarianism is very similar to classic views of utilitarianism except that it does not necessitate the maximization of total well-being and, instead, believes that coming up slightly short of total well-being is acceptable.

Several criticisms of satisficing exist. Of significance is the theory's elimination of an individual's ability to make impulsive decisions. In addition, there are protests that the constant evaluation of the utility of consequences may be detrimental to a person's capacity to make the best decision.

—Tara L. Ceranic

See also Bounded Rationality; Expected Utility; Rational Choice Theory; Utilitarianism

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Savings and Loan Scandal

During the 1980s, a large number of savings and loan depository institutions in the United States failed or suffered severe financial distress because of changing financial regulations, widespread financial mismanagement, and a surge of financial crimes perpetrated by, in many instances, officers of the affected institutions. This wave of financial failures, unprecedented since the difficult economic years of the Great Depression, came to be known as the savings and loan scandal. Ironically, the earlier success of the savings and loan institutions in fulfilling their intended mission laid the groundwork for this descent into financial ruin.

The origins of the savings and loan scandal in the United States lay in the changing economic and political environment of the 1970s. Savings and loans institutions, also called thrift institutions, existed since the banking reforms of the 1930s (under Franklin D. Roosevelt's "New Deal" administration) as a major source of residential mortgages for single-family homes. During the housing boom in the United States following World War II, these institutions provided low-interest, fixed-rate, long-term loans to a growing consumer base of home buyers. The thrifts in turn funded these long-term loans by attracting deposits that, because they could be withdrawn at any time, were short term in nature. This financial framework succeeded in driving the growth of the post–World War II residential building and home-owning boom, especially in the expanding suburban communities surrounding major American cities.

Savings and loans attempted to balance this difference between their short-term deposits and long-term loan obligations by matching the interest rates of their mortgage lendings to the interest rates offered for savings. Throughout the postwar years and into the 1970s, they accomplished this through three incentives: savings interest rates at levels slightly higher than those available to depositors from commercial banks, customer convenience services and savings bonuses, and the protective umbrella of federal deposit insurance for savings.

During the 1970s, however, the conditions underpinning the thrifts' activities changed drastically. Consumer price inflation caused federally set interest rates to rise dramatically, increasing the cost of funds to all savings institutions and forcing thrifts to increase their savings interest rates to continue attracting deposits. Meanwhile, the assets held by savings and loans in the form of mortgage loans remained at fixed rates of interest that were much lower than the cost for new deposits. This trend created economic pressures that had an adverse impact on the financial profitability of the thrift industry.

Accompanying these economic changes were growing political pressures from free market advocates for reduced government intervention in the marketplace. These advocates cited the financial imbalances faced by thrifts and the growing emergence of market-based alternatives to thrifts (such as commercial banks with expanded powers, mutual funds, and even government-chartered mortgage institutions such as Fannie Mae and Freddie Mac) as proof that the savings and loan industry needed deregulation to compete more effectively. With the United States facing both inflationary pressures (from a combination of economic recession and supplier-created oil scarcity) and increasing mistrust of government (in the aftermath of the Vietnam conflict and the Watergate scandal), the sentiment for change was strong within most sectors of the economy.

Whereas many thrifts lost money during this period of economic and political uncertainty, the regulatory changes of this time also brought expanded opportunities. Governmental actions in the late 1970s and early 1980s succeeded in removing many of the regulations that previously restricted the range of deposit and lending options available to thrift institutions. These actions attempted to offer the thrift industry a degree of flexibility for diversifying their mix of deposit (liability) and lending (asset) offerings. On the liability side, federal legislation approved the expansion of deposit offerings by savings and loans beyond simple savings accounts to include more lucrative, but also higher risk, products such as interest-bearing checking accounts and large-denomination, nationally sold certificates of deposit. These new products also received the protection of guaranteed federal deposit insurance, which was increased from $40,000 to $100,000 per account. Meanwhile, on the asset side of the business, thrifts began to offer both fixed-rate and adjustable-rate mortgages, expanded into a wider range of investments beyond residential real estate, and extended their lending activities beyond their traditional regional locales to a nationwide marketplace. However, even with these structural changes, thrift institutions' primary expertise remained rooted in locally based residential lending, creating the potential for large-scale mismanagement.

As savings and loans moved to expand their lending (asset) and deposit-attracting (liability) activities while returning to profitability, the free market–based philosophy of deregulation proposed that those institutions unable to balance their assets and liabilities under free market competition would fail or be absorbed by more viable competitors. The result would be a stronger, more effective, and more profitable industry sector for both consumers and industry participants. However, this proved not to be the case because of two significant intervening factors: institutional regulatory failures and expanded risk-inducing incentives.

When the U.S. federal government moved to relax regulations for the savings and loan industry, it likewise lessened regulatory oversight of the implementation and consequences of these changes. As thrift institutions lost money and moved toward (or reached) financial insolvency, this reduced level of regulatory oversight allowed many declining thrifts to avoid disciplinary penalties and remain open. Once this process of regulatory failure had occurred, the postderegulation expansion of deposit-attracting opportunities for thrifts provided a perverse incentive for these businesses to engage in increasingly risky lending activities.

All savings and loan deposits were insured by the federal government in full up to $100,000, without regard for the underlying risks or the creditworthiness of the insured savings and loan institution. Thus, once a thrift fell into financial insolvency (where its liabilities exceeded its assets), it could choose to raise additional deposit funds for speculative investments knowing that its liability in the event of failure would be assumed by the federal government. These risky investments, if successful, would then return the business to financial solvency. If these risky investments failed though, the depositors whose money had been put at risk would not lose their funds, because the federal insurance guarantee would presumably protect the full return of their principal.

This combination of potential high return for thrift industry participants with relatively small risk proved very attractive to both experienced managers and new entrepreneurs. From 1983 to 1985, the savings and loan industry grew by more than 50%, just as the underlying real estate values supporting the industry's lending-based growth declined. The result was a tidal wave of financial insolvency throughout the 1980s and the early 1990s among savings and loan institutions, which, because of political pressures raised by depositors and their legislators to ensure federal deposit protection for the entire value of consumer deposits, was ultimately assumed by the federal government. By the end of the 1990s, the taxpayer cost for resolving the problems of failed savings and loans had exceeded $120 billion.

The movement toward financial deregulation in the 1970s that engulfed the savings and loan industry intended to address one growing issue facing the industry: the problem of economic imbalances and inefficiencies in a changing global marketplace. However, by ignoring the critical public service component underlying the creation and success of the savings and loan industry, the reduced levels of governmental oversight occasioned by deregulation invited unscrupulous financial risk takers to exercise unprecedented control over assets previously considered inviolate—the savings and homes of individuals. This deregulation-driven emphasis on financial criteria as the sole justification for the savings and loan industry highlighted a critical trend of political policy making in the late 20th century: a reliance on the economic forces of growth and globalization (Adam Smith's "invisible hand") as the preferred course for ensuring financial well-being and individual security.

—William E. Martello

See also Barriers to Entry and Exit; Competition; Deregulation; Ethical Role of the Manager; Federal Deposit Insurance Corporation (FDIC); Federal Reserve System; Free Market; Regulation and Regulatory Agencies; Smith, Adam

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Scandals, Corporate

Scandals have been a part of the commercial landscape at least since the inception of the corporation. Corporations are created to generate wealth by concentrating economic power and directing it to achieve corporate purposes. Corporate scandals emerge when individuals attempt to seize this power for personal purposes and from their abuse and misuse of it. The form of scandal is shaped by the economic nature of the modern corporation.

The British economist Ronald Coase observed that modern economies are dominated by large corporations run by managers rather than by traditional systems of individuals and small organizations selling goods and services primarily to each other. These managers seek to control their firm's transaction costs (i.e., to manage the costs incurred in acquiring resources and in coordinating processes such as marketing and manufacturing). In *The Modern Corporation and Private Property*, Adolph Berle and Gardiner Means argued that the essence of a corporation is the fragmentation of accountability among its various managers and other related actors. In the modern corporation, professional managers are not necessarily the owners; stockholders and other investors are not generally in charge or even legally liable; and the boards of directors are rarely sufficiently informed or adequately empowered to control their firms. This fragmentation and lack of control tend to encourage an open grab for corporate power as individuals who are involved with these organizations seek to acquire for themselves some of the available resources connected with corporate transactions. There are both morally acceptable and morally unacceptable ways of doing this. In Western societies we tend to praise those who acquire power and wealth by ethical means. But actions that are born out of greed, hubris, narcissism, or arrogance and that abuse corporate power are morally unacceptable. They offend many people's sensibilities.

A scandal materializes when untoward actions are alleged and publicized whether they ultimately prove to be valid or not. The publicity harms some people, if not many. Meanwhile almost everybody is tainted, bringing about general public disgrace. Comparing scandal to robbery, Lord Chesterfield once observed that the victim is generally thought as bad as the thief. Accordingly, it is the very fact that some untoward incident is made public that makes it a scandal. Social systems tend to agree with Molière, the French dramatist who claimed that to sin in secret is no sin at all but to be accused of sin made a scandal.

Corporate power can be abused scandalously in many different ways: using corporate resources for personal gain, excessively hyping an unsound business deal to an uninformed investing public, using false and deceptive advertising or selling methods, indulging in insider trading, paying bribes, making use of influence peddling, paying early investors out of later investors' contributions rather than from income (pyramid or *Ponzi scheme*), selling a phony or nonexistent product, manipulating or colluding on prices, overcharging for products or services delivered, and failing to respond adequately to an accident or natural disaster. Organizational forms that have been used to concentrate power unduly include trusts—units for which the real control of a company is transferred to an individual or small group by an exchange of shares of stock for trust certificates, which are issued by the individuals seeking control—and cartels—organizations formed by producers whose purpose is to allocate market shares, control production, and regulate prices.

In a capitalist economy, the public depends on accounting statements and financial and other information to make its business decisions. In recent years, accounting fraud has been a source of considerable scandal. Among the many shams that have been used recently to pretty up some ugly underlying financial conditions and to deceive investors are channel stuffing (Sunbeam), treating expenses as capital investment (WorldCom), unsubstantiated lengthening of the lives of assets (such as a fleet of trucks) to reduce depreciation charges (Waste Management), and the shams that Enron used par excellence—namely, front-end loading of revenues by using unduly optimistic "mark-to-market" (actually, "mark-to-model") estimates and transferring assets off the books to specially contrived paper organizations such as "special-purpose entities."

Brief History of Corporate Scandals

The modern history of corporate scandals begins with the South Sea Bubble of 1720. In 1711, the British Parliament gave the South Sea Company permission to form a monopoly for trade in the South Seas and South America, including the right to import slaves from Africa. The deal's promotion spawned a frenzy of public speculation. As a result, the South Sea Company share prices soared from about £1 to as high as £1,050. Trading in slaves, however, proved to be unprofitable, and the monopoly in British trade with Spanish America never achieved its original high expectations. In possession of insider information about the forthcoming shortfall, in January 1720, the chairman and some company directors sold their holdings. Widespread financial losses were experienced, and thousands of investors were ruined when the bubble burst and the stock price collapsed. The public, having lost confidence in the entire economic system, demanded explanations and restitution. A parliamentary investigation revealed complicity by several company officials. Two members in the royal court of George I were also implicated in the scandal. Early in 1721, Britain's Chancellor of the Exchequer was imprisoned in the Tower of London on charges of fraud in connection with the South Sea Bubble. A new prime minister and Chancellor of the Exchequer were appointed. Reforms were initiated averting an even greater financial panic.

The South Sea Bubble case illustrates a general pattern for corporate scandal. First, there is a climate of general optimism creating an environment in which significant business opportunities arise or appear to arise. Executives, managers, and others in positions of power succumb to greed and narcissism and embark on grandiose schemes to avail themselves of the opportunities. Some of these schemes are initially legitimate, whereas others are scams from the beginning. Playing on the public's infectious greed (as Alan Greenspan subsequently called it), hype, exaggeration, and clever new instruments (creative financing) are used to secure funds and other resources. The ballyhoo creates a bubble. But the underlying business model proves to be flawed and fails. The executives then conjure up deceptions, illusions, deflections, frauds, and other schemes to hide the shortfalls. Meanwhile, they take action to protect their personal interests. Eventually, however, an investigative reporter uncovers a clue, a whistleblower releases information, or the march of events simply overtakes the firm, and the public learns of the misdeeds. The press runs scathing stories. People learn that the executives' self-aggrandizing actions have deceived investors and other stakeholders and, ultimately, inflicted substantial harm on many other parties. The harm is often widespread. Investors lose savings and retirement funds. Suppliers no longer have customers. Consultants are ousted. Trading partnerships are terminated. Customers and communities are disrupted. Notably, employees lose their jobs. Usually, some of the key parties would have been privileged to inside information and would have cashed out their stock or otherwise protected their interests before the burst. As a result, the public is incensed, disgraced, and morally offended; trust in the economic system erodes; and the public calls for redress and reparation. Allegations are made. Investigations are launched. Culprits are sought out and charged. Two types of social control are implemented. External controls such as laws, sanctions, and imprisonment are put into practice. Internal controls of socialization including programs to promote ethics and more acceptable behavioral norms are propagated. All this is intended to prevent future abuses. The next scheme, consequently, must be created outside the purview of these new controls.

The *Black Friday* incident of 1869 in which the great railroad and telegraph baron, Jay Gould, and another financial speculator, Jim Fisk, attempted to corner the U.S. gold market follows the pattern of corporate scandal. It occurred during a period of optimism following the U.S. Civil War. On September 20, Gould and Fisk began purchasing gold in New York City. The public was led to believe that government officials condoned the purchases. Soon Gould and Fisk controlled enough of the available gold supply to bid the price up from about 140 to 163, thus creating turmoil and confusion at the exchanges. A general panic ensued and the prices of other commodities began to fluctuate wildly. The run on gold was halted when U.S. Secretary of the Treasury George Sewall Boutwell announced that the federal government was making $4 million of its gold reserves available for trading. Many businesspeople were ruined by the panic whereas Fisk and Gould reportedly made a profit of about $11 million. As events unfolded, the press portrayed Gould as a malicious, amoral, unstoppable financial wunderkind, pasting him forever with an unsavory reputation. The incident outraged the public, prompting the U.S. House of Representatives Banking Committee to launch an investigation focusing largely on President Grant's administration. While implicated members of the administration were eventually exonerated—not all scandals end with convictions—the Congress and Wall Street changed their policies and procedures to further protect financial markets from flagrant market cornering by conniving individuals.

As the 19th century morphed into the 20th, opportunities in steel, oil, railroads, finance, and other emerging industries attracted a new group of innovators—men who would not only create great industrial organizations but would also secure massive fortunes for themselves. Today, the names J. P. Morgan, Andrew Carnegie, John D. Rockefeller, and Cornelius Vanderbilt join Gould's as archetypical scandal makers and power magnates of the era. The mere mention of their names conjures up images of the excesses and skullduggery of the time. Their ethical standards for doing business during the heated post–Civil War decades of innovation, capital accumulation, and consolidation shocked almost everyone. In 1902, the muckraking writer, Ida Tarbell, published an exposé of Rockefeller and Standard Oil, concluding that the spectacular growth of the companies had been accomplished by means of fraud, deceit, special privilege, gross illegality, bribery, coercion, corruption, intimidation, espionage, or outright terror. In 1934, the journalist Matthew Josephson appropriately dubbed these people *robber barons.* President Theodore Roosevelt launched a successful antitrust suit against Standard Oil and pursued other robber barons as well, which earned him the title of *trust buster.* Public outrage gave rise to reforms, including the passage of the

Sherman Antitrust Act of 1890 and the Clayton Antitrust Act of 1914.

The 1920s were called the roaring twenties because of the affluence and optimism of the times. Early in the decade, a flamboyant Italian American financial wizard named Charles Ponzi bilked thousands of unsuspecting people out of their savings by claiming that his company had agents buying Spanish reply coupons for 1 cent that could be redeemed at any U.S. post office for a 6-cent stamp. Investors flocked to participate. Early investors were paid off at rates of 50% to 100% with funds raised from later investors, thereby giving the illusion that the deal was financially sound. The pyramid scheme eventually collapsed, at least $8 million were never accounted for, six banks failed, and Ponzi went to jail. The phrase *Ponzi scheme* became a standard part of the corporate scandal lexicon.

Another enduring symbol of scandal occurred in 1929 when a former U.S. secretary of the interior, Albert Fall, was convicted of accepting a bribe of $100,000 for secretly leasing the U.S. Navy's *Teapot Dome* oil reserves to Harry Sinclair's petroleum company. In 1932, Chicago Edison, Commonwealth Edison, Peoples Gas Light and Coke, and several other utilities companies, all controlled by Chicago magnate Samuel Insull, went into receivership. More than 600,000 shareholders and 500,000 bondholders lost most of their investments. Insull, who had emerged from an impoverished childhood to become Thomas Edison's private secretary and then to play a pivotal role in the creation of General Electric (GE) before taking control of the companies, was indicted for fraud and embezzlement. Pyramided holding companies and interlocking directorates were his key deceitful tactics. President Franklin Delano Roosevelt publicly denounced him and his practices and called for regulatory reform leading eventually to the Public Utility Holding Company Act of 1935, one of the most important federal consumer protection laws ever passed.

The Depression and World War II diverted corporate efforts, but by the 1960s, corporate power was on the rise and more scandals were in the making. The climate of the 1960s in the United States was one of social unrest. Civil rights issues emerged, concerns about the war in Vietnam arose, drug use escalated, employees formed more adversarial relationships with management as old values were cast aside, and loyalty shifted from faithfulness to one's employer to belief in personal ideals. In this milieu, several executives in the electrical equipment industry, led by executives from GE and Westinghouse, entered into agreements to fix prices and to allocate market share by a phases of the moon formula that determined which company would make the low bid on a particular job. Learning of this, the public was incensed. In December 1961, the Justice Department sought a court order to make GE subject to unlimited fines if it ever again tried to fix prices or violated any antitrust laws. Several senior GE executives went to jail. The 1960s also witnessed the conviction of the colorful financier Billie Sol Estes from Pecos, Texas, for selling finance companies $24 million worth of mortgages on fertilizer tanks that did not exist. Texas Gulf Sulfur was indicted for issuing misleading press releases about copper deposits supposedly discovered in Canada. A few cases of insider trading led to case law efforts to protect innocent investors. As part of the reformation efforts toward the end of the decade, firms began to establish codes of conduct and publish vision and values statements. This was also the period of the birth of the corporate social responsibility movement. For the most part, corporate legal and human resources departments took the lead in these efforts.

The decade of the 1970s was characterized by recession, oil embargo, unemployment, productivity lag, and heightened concerns about the environment. Its moral tone was set by the Watergate affair. In June 1972, burglary and wiretapping of the Democratic Party's campaign headquarters led to a scandal involving abuse of power by public officials, violation of public trust, bribery, contempt of Congress, and attempted obstruction of justice. President Richard M. Nixon and many of his associates were implicated. The affair culminated in the first resignation of a U.S. president. The Love Canal incident, in which scores of residents were evacuated from houses built over an abandoned excavation site used to dump toxic chemical waste, raised questions of corporate responsibility for environmental safety and disclosure. Defense contractor overcharging, the Lockheed overseas bribery case, and Equity Funding were notable corporate scandals. In February 1976, a Lockheed executive told the U.S. Senate Foreign Relations Committee that the company had paid bribes to Japanese government officials to sell aircraft to the country. The incident led to the arrest of former Prime Minister Kakuei Tanaka on charges of accepting bribes. The scandal was heightened when it was revealed that Lockheed had paid a total of $22 million to Japanese and other foreign government officials shortly after it received a $250 million emergency loan guarantee from the U.S.

government. Senator William Proxmire spearheaded the passage of the *Foreign Corrupt Practices Act*, which President Carter signed into law in December 1977. A company called Equity Funding overstated its revenues by making up phony insurance policy sales supported by fictitious records in their files. The result was a billion-dollar fraud based on thousands of fabricated transactions that outside auditors never caught. An insurance analyst, Raymond Dirks, warned his clients about the massive fraud and encouraged them to sell short. Regulators investigated and uncovered the scandal; but they then rewarded Dirks by prosecuting him for using insider information to tip off his clients who had shorted Equity Funding stock based on his advice. Dirks was convicted but later exonerated by the U.S. Supreme Court. Nevertheless, the case served to warn investors about the impropriety of trading based on an insider's tip. The Ethics Resource Center was established in Washington, D.C., to provide aid to companies on issues of ethics. During this period, the "values" movement in business ethics began. Its mission was to encourage corporate ethics efforts to move beyond legal compliance and become values centered. Nevertheless, compliance with laws still dominated.

During the 1980s, the social contract between employers and employees was redefined. As companies became less loyal to their employees, employees became less loyal to their employers. Additional cases of bribes were uncovered, deceptive advertising methods exposed, and influence peddling revealed. The Swiss company Nestlé Corporation was accused of marketing powdered infant formula, whose safe use required a literate consumer who had access to a clean supply of water, to illiterate mothers in undeveloped countries. Many of their babies died, raising questions of misleading and irresponsible selling practices. Union Carbide's plant in Bhopal, India, exploded emitting poisonous gases that killed more than 3,000 people and injured more than 200,000 others due to a failure to comply with safety practices. The incident raised questions about a multinational corporation's obligations when operating in less developed countries. Dow Corning was accused of covering up evidence linking its silicone breast implants to female patient illnesses, immune system problems, and other disorders, raising additional questions about corporate responsibility for safety and disclosure. Four other scandals stand out: defense contract cost cover-up, the savings and loan debacle, Wall Street insider trading, and the *Exxon Valdez* oil spill. The public was outraged to learn that numerous defense contractors had substantially overcharged the government for minor items—for example, the $1,000 toilet seat—and were submitting misleading, if not false, information. As reports of procurement irregularities increased, investigations into the activities of major contractors began. In July 1985, President Reagan asked David Packard, chairman of Hewlett-Packard Corporation and a former deputy secretary of defense, to chair a specially appointed, independent Blue Ribbon Commission on Defense Management (the Packard Commission). In late spring of 1986, the Packard Commission delivered a report that many companies signed, pledging to implement several reforms: codes of ethics, ethics training programs, internal reporting systems for allegations of misconduct, compliance monitoring systems, Best Practice Forums, and accountability to the public programs. Deregulation of the U.S. savings and loan industry and an increase on the limits on deposit insurance (from $40,000 to $100,000 per account)—actions intended to make savings and loans more competitive with commercial banks—led to a wave of failures that foreshadowed a more general financial crisis. About $150 billion was lost, more than 80% of which was borne directly by the U.S. government and hence the public. Although mismanagement, rising interest rates, fluctuation in real estate values, and failed speculation were contributing factors, the Federal Home Loan Bank Board concluded that fraud and insider abuse were the primary causes. Charles Keating, head of Lincoln Savings in Irvine, California, was convicted of fraud, racketeering, and conspiracy and spent 4½ years in prison until his convictions were overturned and he pleaded to a lesser charge. Also, during the 1980s, financial crime became commonplace on Wall Street as greedy traders struck shady deals, bribed influential people to leak confidential business information, illegally manipulated prices, and secretly accumulated portfolios of prized securities. Drexel Burnham Lambert, Inc., was most infamously implicated. Among the key parties in these insider trading scandals were Ivan Boesky, Michael Milkin, Dennis Levine, and Martin Siegel, all of whom served prison terms but avoided full public trials by pleading guilty to reduced charges. In 1989, a drunken captain ran the *Exxon Valdez* aground, spilling 11 million gallons of oil into Alaska's Prince William Sound and producing a world-class environmental disaster. The public was incensed by the seemingly insensitive demeanor and slow response of Exxon executives.

The 1990s was a period, as described by Federal Reserve Chairman Alan Greenspan, of global expansion and irrational exuberance. The decade ended with the blooming of the dot-com bubble. More global issues emerged as scandals included the Bank of Credit and Commerce (BCCI), foreign sweatshops, financial mismanagement, false reporting, fraud, and a renewed emphasis on board of directors' corporate liability.

The Pakistan-based BCCI built an empire that operated in 73 counties and controlled at least $30 billion in deposits. Portrayed as the first global Third World bank by founder Agha Hasan Abedi, BCCI was based on fraudulent practices from the start, being designed to steal billions of dollars and buy political influence in the United States and around the world. The company devised an array of schemes to rob innocent depositors of their savings, assist government officials in looting their countries' treasures, and finance the activities of terrorists and drug lords. Its major mission was to influence U.S. policy in the Middle East. The BCCI affair highlighted a laxness in international control of banks and raised questions about the morality of governments and individuals that used outlets like BCCI to conduct their own covert activities.

The sweatshop issue came to the public's attention when it was revealed that popular talk-show host Kathie Lee Gifford's line of clothing at Wal-Mart had been manufactured by women laborers in Guatemalan shops under near-slavery conditions. Around the same time, CBS ran a report on the poor working conditions in Nike factories in Indonesia and Vietnam. Whereas the Asian workers, mostly women between the ages of 17 and 25, worked 60 to 90 hours a week and were paid 15 to 25 cents an hour, celebrities such as basketball star Michael Jordan and golfer Tiger Woods were paid handsomely ($45 million and $28 million, respectively) for merely associating with the companies' products.

Beginning on February 23, 1995, the venerable 200-year-old Barings Bank was plunged into bankruptcy within just 3 weeks by the unapproved speculative trading of a 28-year-old named Nicholas Leeson. Leeson's short-term trading losses exceeded $1.4 billion, more than the capital of the bank. He was sentenced to serve 6 years in a Singapore prison for his fraudulent scheme, which included phony hedges, doubling up on speculative investments, and submitting false profit reports to the bank.

Social control responses included the recasting of a set of principles for conducting international business that were originally propagated by Reverend Leon Sullivan in 1977 and known as the Global Sullivan Principles for Corporate Social Responsibility. Representatives of 34 nations under the auspices of the Organisation of Economic Co-operation and Development signed a new Convention on Combating Bribery of foreign public officials conducting international business transactions. New emphasis was placed on the United Nations' Code of Conduct on Transnational Corporations, which among other things, required multinational corporations to engage in arm's length pricing. Corporate executive and board member responsibilities and liabilities were clarified. On November 1, 1991, sentencing guidelines of the U.S. Sentencing Commission for all public or privately held organizations were put into effect. They were intended to ensure just punishment and deterrence and to encourage the installation of effective compliance and ethics programs. In 1996, Chancellor Allen of the Delaware Chancery Court, responding to a plea agreement, decreed in the *Caremark* case that the company's directors still bore personal responsibility for the harm the company had caused by alleged mail fraud and kickbacks to physicians for patient referrals, even though no senior company officials were implicated. The following year, the U.S. Supreme Court decided the O'Hagan case, specifying that a person who trades in securities on the basis of insider information may be held criminally liable even if he is not an insider of the company whose securities he trades. On the corporate front, a few companies that had earlier been implicated in scandals, like Royal Dutch Shell, began issuing annual reports on their companies' ethical performance. During the decade, a collection of start-up companies selling products and services offered on or otherwise related to the Internet proliferated, giving rise to a speculative frenzy of investment in technology-related stocks and enterprises. The questionable business models of these companies typically relied on network effects to justify their losing considerable amounts of money to build market, mind, or eyeball share. As a consequence of hype, accounting artifacts, and investor exuberance, a bubble developed that sent dot-com stock prices soaring to dizzying heights making the founders extraordinarily rich, but mostly just on paper.

The economic growth of the 1990s was followed by some dramatic financial failures at the outset of the 2000s. This decade, during which numerous cases of severe financial mismanagement were uncovered, is also characterized by extended international corruption, exorbitant executive pay packages, cyber crime, intellectual property issues, and privacy issues stemming from the collection and selling of personally identifiable information. The dot-com bubble was blown up to the point of bursting on March 10, 2000, when the technology intense NASDAQ composite index peaked at 5048.62, more than double its value the previous year. Soon thereafter, as the flawed, and in many cases deceitful, business models were exposed, investor confidence plummeted. By year's end, the NASDAQ fell to below 2000, wiping out many fortunes. On December 1, 2001, Enron filed for bankruptcy, launching a period of revelation of numerous scandals. A partial list of companies is startling in its scope: Adelphia Communications Corp. A.I.G., AOL Time Warner, Bristol Myers, Cendant Corp., Computer Associates, Credit Suisse First Boston, Disney, Dollar General, Global Crossing, HealthSouth, ImClone Systems, Hollinger International, Merck, Quest Communications, Rite-Aid, Parmalat, Sunbeam, Tyco, Waste Management, WorldCom, and Xerox.

Enron is the poster child and prototypical case. CEO/Chairman Kenneth Lay, COO/CEO Jeffery Skilling, and CFO Andrew Fastow were the lead executives responsible. By using shams and questionable accounting techniques, executives made it appear that the company was earning money that it really wasn't. For example, Enron allegedly generated 96% of its 2000 reported income of $979 million deceptively. The company also reported having a debt load of $10.2 billion in 2000, when it was really $22.1 billion. One of Enron's largest shams was a $111 million deal with Blockbuster video for video-on-demand that never went through but was recorded as profitable on its books. Although it was once the largest energy trader in the United States, on December 1, 2001, Enron collapsed into the largest bankruptcy in the United States at the time (Worldcom's eventually exceeded it). At least seven former Enron executives faced criminal charges. Three British bankers were also indicted for Enron-related wire fraud in late June 2002, and several Morgan-Stanley executives were convicted of illegally parking investments in barges for Fastow. Fastow's co-conspirator, Michael Kopper, returned $4 million after he pleaded guilty to fraud and money laundering. Fastow was arrested on numerous fraud and conspiracy charges (which could have landed him up to 140 years in jail). On October 2, 2002, he was indicted. Eventually, the grand jury lodged 98 counts against him. Among other things, he was accused of obstruction of justice for his part in the destruction of a laptop on which he and Michael Kopper kept secret records of their illicit deals. Then, on January 14, 2004, Fastow entered a guilty plea as part of a plea bargain, admitting to two counts of conspiracy involving wire fraud and securities fraud and agreeing to testify against Lay and Skilling. He also explained his role in several Enron frauds and in a billion dollar hedging scheme that failed. Fastow's wife, Lea, completed a yearlong sentence in July 2005 on a misdemeanor tax charge for having failed to report the kickbacks Fastow received to the IRS. Former senior Enron energy trader Tim Belden pleaded guilty to conspiring with others to create the California power crisis, a major scandal within the Enron scandal. Former Enron treasurer Ben Glisan was sentenced to 5 years in prison for his role in the scandals. Lay and Skilling stood trial early in 2006. Enron's accounting firm, Arthur Andersen, was indicted for obstruction of justice and went out of business. David Duncan, Andersen's lead partner at Enron, pleaded guilty to obstruction for shredding pertinent documents. In response to Enron and other scandals, on July 30, 2002, Congress passed the Sarbanes-Oxley Act, the most far-reaching overhaul of securities law since the Depression. Subsequently, the Federal Sentencing Guidelines for Organizations were extended.

In Enron, WorldCom, and other early 21st-century scandals, once again a familiar pattern of corporate scandals was played out. New technology and business practices and a favorable climate presented opportunities for unscrupulous individuals to contrive deceitful and self-aggrandizing deals. The deceit was exposed and published. As a result of the scandal, reputations were tainted and investments lost. An incensed public called for more forceful external and internal social controls, some of which were implemented.

—Richard O. Mason

See also Accounting, Ethics of; Adelphia Communications; Antitrust Laws; Archer Daniels Midland; Arthur Andersen; Barings Bank; Bhopal; Boesky, Ivan; Carnegie, Andrew; Consumer Fraud; Corruption; Cowboy Capitalism; Dalkon Shield; Deceptive Practices; Dow Corning; Enron Corporation; Ethics and the Tobacco Industry; Executive Compensation; Extortion; *Exxon Valdez*; Federal Sentencing Guidelines; Firestone Tires; Ford Pinto; Foreign Corrupt Practices Act of 1977 (FCPA); Fraud; Global Crossing; Grasso, Richard; Insider

Trading; Johns-Manville; Long-Term Capital Management; Love Canal; Manipulation, Financial; Merck & Co. Inc.; Milken, Michael Robert; Nike, Inc.; Parmalat; Ponzi Scheme; Price-Fixing; Sarbanes-Oxley Act of 2002; Savings and Loan Scandal; Silkwood, Karen; Stewart, Martha; Sweatshops; Teapot Dome Scandal; Tyco International; WorldCom

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Securities and Exchange Commission (SEC)

The U.S. Securities and Exchange Commission (SEC) is the primary federal government regulator of securities markets in the United States. The SEC was created to administer the Securities Act of 1933 and the Securities Exchange Act of 1934. Since its creation, the SEC has been assigned responsibility for administering other laws and amendments to those laws, including the Public Utility Holding Company Act of 1935, the Trust Indenture Act of 1939, the Investment Advisors Act of 1940, and the Investment Company Act of 1940. The SEC also has responsibility for administering large parts of the Sarbanes-Oxley Act of 2002. These laws were enacted by Congress to achieve the broad policy goals of protecting investors and promoting efficiency and competition in the capital formation process. The SEC's mission is to help achieve these statutory goals. The SEC carries out its mission by issuing rules and regulations based on the authority of the laws it administers. These rules and regulations serve to interpret and implement the laws enacted by Congress. The SEC also carries out its mission by enforcing the nation's securities laws, including the rules and regulations promulgated under the authority of laws enacted by Congress.

To achieve the statutory goal of investor protection, the SEC relies on several regulatory tools. Chief among these tools are rules and regulations promoting the public disclosure of information about key variables influencing investor decisions. Nearly every securities market participant faces some form of SEC mandated information disclosure requirements. For example, securities exchanges, such as the New York Stock Exchange, face SEC mandated transparency requirements promoting the real-time publication of information about market quotations and transactions. Publicly traded firms, like IBM, face SEC mandated disclosure requirements concerning the information contained in the firm's prospectus ahead of its initial public offering. In addition, publicly traded firms are required by the SEC to disclose, through regular reports to investors, information about the firm's financial condition along with any other information that may be important in influencing investor decisions. Brokers and dealers face SEC mandated disclosure requirements related to the handling of investor funds, sources of potential conflicts of interest, and matters related to fees and trade execution. Mutual funds face SEC disclosure requirements concerning investment risk and performance as well as information concerning advisory relationships, investment objectives, and fund governance. The SEC has continued its policy of mandating more frequent and comprehensive information disclosure requirements over the objections of critics who argue that such policies often have unintended consequences and foreclose an otherwise important dimension of competition among market participants.

To facilitate the SEC's information disclosure policy for public companies, the commission maintains the Electronic Data Gathering and Retrieval system (EDGAR). All companies, foreign and domestic, are required to file registration statements, periodic reports, and other forms electronically through EDGAR. Any member of the public can access and download this information for free over the Internet.

To achieve the statutory goal of promoting efficiency and competition in the capital formation process, the SEC adopts rules and regulations prohibiting trading practices that distort prices and degrade the performance of the securities markets. The SEC regulates aspects of market microstructure to promote competition in securities trading. In addition, the SEC regulates important dimensions of exchange competition as part of its administration of the National Market System amendments to the Securities and Exchange Act of 1934.

Sometimes the SEC must choose to sacrifice the promotion of one goal to promote another. For example, rules that prohibit insider trading to protect investors may degrade the quality of securities prices. In other cases, protecting one class of investors, for example, individual small investors, may harm another, for example, mutual fund participants. When facing conflicting goals, the SEC must determine the trade-off that is consistent with the public interest, broadly defined.

In addition to rules and regulations, the SEC imposes self-regulatory duties on market participants who interact with public customers. In other words, market participants themselves must perform a regulatory role. The SEC oversees the entire regulatory structure to make sure that market participants perform their self-regulatory duties. It has the authority to approve the rules of self-regulatory organizations to ensure that investors are protected and that the capital formation process is efficient and competitive.

The SEC maintains an active program to enforce securities laws under its jurisdiction. Each year it brings hundreds of enforcement actions against individuals and companies that violate the securities laws. Typical infractions include insider trading, accounting fraud, and providing false or misleading disclosures about the financial condition of public companies.

The SEC is not the only governmental organization regulating securities trading in the United States. Individual states have their own antifraud laws related to securities issuance and trading, and the Federal Reserve Board sets minimum margin levels for stocks and stock options through its Regulation T. The SEC also works closely with other financial market regulators, such as the Commodity Futures Trading Commission, to define responsibility for products that have economically similar characteristics to security products.

The SEC consists of five commissioners appointed by the president and confirmed by the Senate. Each commissioner is appointed to a 5-year term. The commissioners' terms are staggered, so that each year one commissioner's term expires. No more than three commissioners may belong to the same political party. The president designates one of the commissioners as chairman, the SEC's top executive. The commissioners are supported by a large permanent staff of approximately 3,100 lawyers, accountants, and economists. The SEC is headquartered in Washington, D.C., and has 11 regional and district offices across the country. The SEC's meetings are open to the public unless confidential subjects, such as settlement negotiations related to an enforcement proceeding, are discussed.

The SEC is organized into four operating divisions: the Division of Enforcement, the Division of Investment Management, the Division of Corporate Finance, and the Division of Market Regulation. These divisions carry out the day-to-day regulatory and oversight operations of the SEC. The SEC also has several independent offices that support the operating divisions as well as the commission itself.

The Division of Enforcement investigates alleged violations of securities laws. On completion of an investigation, the Division will recommend Commission action when appropriate, either in a federal court or before an SEC administrative law judge. Often, the Division will negotiate settlements on behalf of the commission. Although the SEC has civil enforcement authority only, it works closely with various criminal law enforcement authorities, such as the U.S. Department of Justice, to develop and bring criminal cases when warranted.

The Division of Investment Management is responsible for administering the Investment Company Act of 1940 and the Investment Advisor Act of 1940. The Division also exercises oversight of utility holding companies under the Public Utility Holding Company Act of 1935. It is responsible for formulating policy proposals governing investment companies and investment advisers. It is also responsible for registering investment companies and advisers and for ensuring that registrants comply with securities laws.

The Division of Corporation Finance forms the SEC's disclosure regulations related to publicly held corporations and ensures that corporations comply with these regulations. This Division determines the types of public disclosures that must be made when a stock is initially sold. It also determines the types of disclosures that must be made to investors on a continuing and periodic basis. Its staff routinely review the disclosure documents filed by companies and provide companies with assistance in interpreting the commission's rules.

The Division of Market Regulation is responsible for regulating the major securities market participants such as broker-dealers, securities exchanges, clearing facilities, and securities information processors. Among other things, it sets regulations governing minimum capital levels for broker-dealers, reviews and recommends SEC approval or disapproval of rules adopted by securities exchanges and other self-regulatory organizations, inspects clearing facilities, and regulates the price of real-time market information charged by exchanges to information vendors such as Bloomberg. It also oversees the Securities Investor Protection Corporation, which is a private, nonprofit corporation that insures the securities and cash in the customer accounts of member brokerage firms against the failure of those firms.

In addition to the SEC's operating divisions, the commission's supporting offices include the Office of Economic Analysis, the Office of the Chief Accountant, and the Office of General Counsel. The SEC's Office of Economic Analysis advises the commission on policy and regulatory issues. The office analyzes the potential costs and benefits of proposed rules and regulations. It also develops economic evidence for use by the SEC's Division of Enforcement. Another mission of the office is to conduct empirical research on issues of interest to the commission. The office works on a consulting basis with the SEC's operating divisions and with other SEC offices.

The SEC's Office of the Chief Accountant advises the commission on accounting and auditing matters. It also works with accounting standards–setting bodies, such as the Financial Accounting Standards Board (FASB), the International Accounting Standards Board, the American Institute of Certified Public Accountants, and the Public Company Accounting Oversight Board. It advises the commission regarding the application of accounting standards and financial disclosure requirements and helps develop evidence for use in enforcement proceedings related to accounting fraud.

The primary duty of the Office of General Counsel is to serve as the commission's legal representative in appellate proceedings or other litigation involving the commission. The office also works on legislative matters and provides legal advice to the commission.

The securities market is changing rapidly, and the rate of change often outpaces securities laws and regulations. New technology for trading and disseminating information, the growing importance of institutional investors, the proliferation of innovative financial products, the restructuring of financial exchanges, increased linkages between markets, financial scandals, and the globalization of markets are all examples of recent developments that are forcing the SEC to reevaluate how it regulates securities markets. The SEC's response to these developments will have important implications for the cost of raising capital in the United States and, more broadly, for the international competitiveness of U.S. firms.

—James A. Overdahl

See also Commodity Futures Trading Commission; Disclosure; Financial Accounting Standards Board (FASB); Insider Trading; Regulation and Regulatory Agencies; Sarbanes-Oxley Act of 2002; Scandals, Corporate; Securities Industry Association; Self-Regulation; Shareholder Activism; Shareholder Model of Corporate Governance; Shareholder Resolutions; Shareholders

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Securities Industry Association

The Securities Industry Association (SIA) is a professional trade organization that represents organizations that are licensed to participate in the securities industry. The association's membership is vast and includes securities entities such as brokers, dealers, exchanges, investments firms, investment counselors, mutual funds, and many others that are involved in securities transactions. The SIA was established in 1972 through the merger of the Association of Stock Exchange Firms (1913) and the Investment Banker's Association (1912), and the SIA recently merged with the Bond Market Association as well. The SIA is a trade association of nearly 800 securities firms. SIA members—including most NYSE member organizations, major firms, Canadian exchanges, the OTC market, investment banks, broker-dealers, and mutual fund companies—are active in all U.S. and foreign markets and engaged in all aspects of corporate and public finance. Membership is open to all qualifying entities on a nondiscriminatory basis. In the United States, SIA members collectively account for approximately 90%, or $100 billion, of securities firms' revenues and employ about 350,000 individuals. They manage the accounts of more than 50 million investors directly and tens of millions of investors indirectly through corporate, thrift, and pension plans. In 2005, the industry generated an estimated $322.4 billion in domestic revenue and an estimated $474 billion in global revenues.

U.S. securities markets are the most transparent, liquid, and dynamic in the world. New forms of competition, technological advances, globalization, and broader investor participation have driven phenomenal changes in the capital markets and the securities industry over the past three decades. U.S. securities markets are grounded on the foundation of a structural framework. Self-regulation—and the historical level of member cooperation in particular—has been a key ingredient in the longevity of this framework. For example, the extensive expertise of members and their involvement in the rule-making process has undoubtedly led to more effective, less costly self-regulatory rules. Members of the regulatory community have noted that self-regulation has been viewed as having certain advantages over direct governmental regulation because industry participants bring to bear expertise and intimate knowledge of the complexities of the securities industry.

SIA provides much of the leadership for Wall Street firms in Washington, D.C., as a representative of the industry on securities and financial services issues. It actively engages in testifying on Capitol Hill before various committees on issues that affect the securities industry. It prepares position papers and presents them at conferences to crystallize issues that will affect the capital markets and plays a significant role in contributing to the development of proactive policies that help perpetuate the longevity and integrity of the securities markets.

Also, SIA takes a progressive role in other related issues affecting the financial services industry. It provides policy guidance to both federal and state policy makers in the following areas. The association has provided specific policy guidance on issues pertaining to savings and retirement, financial services, tax, securities, international transactions, treaties, and privacy. It regularly issues press releases on various actions that the executive, legislative, and administrative agencies take that affect the financial services industry. For example, on May 11, 2006, SIA issued a press release praising the U.S. Senate for extending capital gains and dividend tax rates. SIA is an active voice for its members on issues that affect the long-term interest of financial services in the United States and abroad. Last, SIA-PAC is a federally registered political action committee for the SIA. Its primary focus is to participate financially in the election of candidates to the U.S. Congress who are committed to preserving the sound economic policies on which the securities industry is built.

—Sylvester E. Williams, IV

See also National Association of Securities Dealers (NASD); Securities and Exchange Commission (SEC)

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SECURITY INDUSTRY ASSOCIATION

The Security Industry Association (SIA) is a full-service, international trade association. The security industry was a $130 billion industry in 2005. It is a broad one that offers protective measures to communities, organizations, and people to alleviate risk, danger, doubt, anxiety, or fear. Security is the condition of being protected against danger or loss.

The security industry is concerned with safety, continuity, and reliability. Safety means the condition of being safe and free from danger, risk, or injury. Safety devices include those designed to prevent accidents, such as a lock on a firearm preventing accidental firing. Continuity means an uninterrupted succession or flow. Systems that provide continuity include disaster recovery systems and backups, for example, generators. Reliability refers to the probability that a system will satisfactorily perform its intended function and behave as we expect it to behave.

Many threats to security stem from external forces; so the industry takes into account the actions of active malicious agents attempting to cause destruction. The security industry includes tangible things that give or assure safety, such as security guards, controlled access systems, and alarm systems, as well as intangible things, such as measures adopted by a government to prevent espionage, sabotage, or attack. A secure system is one that behaves exactly as it is expected to even when external forces try to make it behave differently. The security industry is concerned with risk (the possibility that an event that could cause a loss will occur), threat (the method of triggering risk), countermeasures (ways to stop a threat from triggering risk), and assurance (guarantees that a secured system will behave as expected).

Security measures are generally taken around physical security, building and asset security, information security, and computer systems. Recent security efforts include those enacted by transportation systems, such as at airports and seaports, and the food industry (to prevent contamination). A general principle is that one should never rely on one single security measure alone. Often multiple means of security are built in.

Member companies of the SIA deal with numerous ethical issues. The most compelling are those around privacy and surveillance. For example, the technology of radio frequency identification has raised questions about unauthorized reading of one's personal information—although one should keep in mind its beneficial uses, such as law enforcement using it to locate 911 callers. Other ethical issues include the reliance on biometrics. Some biometric identification methods, such as retina scans, are relatively intrusive and could create a loss of a person's sense of privacy and dignity. Also, the public sentiment toward the use of biometrics like fingerprints may have a negative perception—that is, fingerprinting may be associated with criminal behavior. People feel embarrassed when rejected by a public sensor. Some methods (e.g., face recognition in public places) could be used to track someone's movements without their knowledge or consent.

Ethical questions also arise about how data are stored and used. Safeguards and ethics policies are needed regarding limiting how electronic information is moved and duplicated, who has access to this information, and the proper uses of the information.

The SIA's mission is to promote growth, expansion, and professionalism within the security industry. It provides educational opportunities, performs research, participates in setting technical standards, and represents member's interests.

The SIA was formed in 1969. As of 2005, the SIA counted manufacturers, distributors, service providers, integrators, and other companies among its 417-member base. Members represent a variety of market segments, including closed-circuit television (a type of television that does not involve broadcasting for public viewing but rather limits the content to be seen only on specified receivers connected to the television camera); access control (which includes policies and permissions regarding entrance to a property or system and may be implemented via a human agent such as a security guard, mechanical means, such as locks and keys, or through technological means, such as identification card readers); biometrics (the measurement of physical characteristics, such as fingerprints, DNA, or retinal patterns, for use in verifying the identity of individuals); computer security (the authorization of access to hardware, software, and information on a computer or within a computer network; typically, users are assigned ID numbers and passwords that allow them access to information and programs within their authority); fire/burglar alarms (devices that announce the outbreak of a fire or unauthorized access); and building automation (such as lighting controls, intercoms, energy savings, and security).

The SIA serves several purposes. Its first core purpose is education. The SIA issues a certificate in security project management. It works with other organizations to offer certificates in burglar and fire alarm technologies and video security systems. The SIA has also established multilevel apprenticeship programs in low-voltage systems installations with other groups.

The SIA's second core purpose is to provide its members with market trends and intelligence, so they can increase business effectiveness and achieve greater potential within the market for security services. New technologies that have an impact on the security industry include biometrics and Voice over Internet Protocol. Current topics of interest include workplace violence and threat mitigation and technology-enabled terrorism.

The third core purpose is to develop and implement integration and performance-oriented standards. SIA's current standards activities focus on architectural graphics, control panels, security communications, digital video, and sensors.

The fourth core purpose involves government relations and lobbying. SIA is an active proponent of tax-expensing legislation for security and life safety equipment products and services. Members have testified at U.S. congressional hearings about issues such as homeland security, dual-line monitoring, and wireless technologies and are influential in introducing legislation that codifies theft and licensing in the security field.

—Donna M. Schaeffer

See also Computing, Ethical Issues in; Electronic Surveillance; Privacy

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Self-Consciousness

Self-consciousness refers to a person's tendency to focus attention on his or her own thoughts and feelings that results in awareness, control, intention, and self-reflection. Because personal actions and choices are based on what one sees, feels, and believes, self-consciousness is essential to understanding human action and moral development.

The state of self-consciousness, therefore, has fundamental personal, social, and cultural consequences. Its related aspects include self-awareness and self-knowledge—terms more frequently applied in management theories. Integral to understanding self-consciousness are definitions of self and self-concept.

Defining Self and Self-Concept

Broadly defined, the self is an array of self-relevant knowledge acquired through thinking, feeling, and motivation. A unique quality of the self is the reflexive capacity for one to be the object of his or her own attention, likened to looking at oneself in a mirror. The self includes a physical body and a social identity and is the active agent in decision making. In the early history of psychology (the late 19th and early 20th centuries), research focused solely on the individual aspects of the self. In the 1920s, the self was primarily studied from a sociological perspective. This shift indicates that the self derives from the interaction with one's culture and society.

One's self can be categorized as material (tangible objects, people, places designated as my or mine); social (social roles and the way we are recognized and regarded by others); and spiritual (inner psychological self, includes perceived traits, abilities, emotions, and beliefs). Contemporary researchers expanded the concept to include a collective self (social categories in which we belong, including racial, religious, and ethnic identities) and a relational self (family, friends, and coworkers).

A person's self-concept derives from how he or she integrates these categories. One's self-concept performs several functions. As an interpersonal tool, self-concept informs one's identity—a prerequisite for social life and human interaction. A person must be able to understand "you" and "I" to sustain relationships over time. Second, one's self-concept is a collection of values and preferences that influence decision making. Choice is integral to self-definition. Because individuals are diverse and complex, the way to keep order when values and preference conflict is through self-regulation—a third function. Finally, one's self-concept serves as a reference point. The storing and organizing of information that relates to and has an impact on one's personal life is processed and remembered more thoroughly through self-reference.

Thus, a person's self-concept guides and directs action and future-oriented goals. It serves as a fundamental tool of mental and social development. Questions of "Who am I?" "Where do I belong?" and " How do I fit in?" are social in nature. Others' views of us are vital to how we conceive of ourselves.

The social construction of one's self depends on one's immediate environment and on larger sociocultural and historical factors. Our *selves* are created within social contexts that take into account the values, norms, and mores of others in that same environment. Self-concept is the result of what Mead calls social commerce—that which propels the type of social action that sustains societies and ourselves. Therefore, the context of the social environment is central to self-understanding.

For example, in Western culture, the emphasis is on personal identity and how people are different from others. In Eastern cultures, the emphasis is on collective and relational identities and how people are similar. Societies that emphasize individualism value individual rights over the duties or social obligations that define a collectivist society. Individualism places value on personal autonomy and self-fulfillment in contrast to collectivist societies, which place value on group memberships.

Therefore, one's self-concept is tied to cultural influences. For example, a person who came of age in the United States in the 1950s, an era of relative conformity, would tend to define self differently than one who entered adulthood in the 1960s, a time of counterculture and peace movements, or the 1970s with the advent of the women's movement. Today, what is often identified as the modern obsession with selfhood is linked to the desire to find meaning in life, with individual and societal values placed on community building and awareness, volunteerism, and philanthropy. This is also evidenced in business practices such as social venture partnering, social entrepreneurs, and strategic corporate philanthropy.

The field of social psychology continues to expand on how culture influences social interactions. Businesses are social institutions; organizations establish legitimacy through ethical interactions with other social actors. The resulting corporate culture functions as part of and within a larger demographic culture. The process of self-consciousness brings these influences into awareness.

Self-Consciousness Defined

Consciousness as a general state is defined as being awake, alert, or aroused—characteristics aligned with motivation. Consciousness encompasses the processes of awareness and attention. Awareness involves the continual monitoring of the inner and outer environments. Attention involves applying conscious awareness to an event or situation that produces greater understanding.

Self-consciousness is the ability to think, reason, and reflect on one's self. Self-consciousness is difficult to study because it is layered, multifaceted, complex, and not generalizable. It is unique and distinct to the degree to which a person becomes conscious through reflection on his or her life experiences. Therefore, self-consciousness is related to one's unique and particular identity as a person. The concept of person is laden with assumptions of duties and rights, both moral and legal. For example, how would one distinguish between a person versus an individual? Are human rights distinct from individual rights? A corporation is defined as a legal person; how does this affect one's view of self?

The process of being self-conscious is the distinguishing feature that separates humans from other mental beings in answering these questions. For example, I have the capacity to make plans for the future. In doing this, I can pursue questions such as "What sort of person am I?" " Am I the sort of person I want to be? Ought to be?" The state of self-consciousness yields this form of moral reflection and evaluation that is tied to moral self-development.

Kohlberg identified three levels of moral development that enhance this discussion. Right behavior, or morally correct action, differs across the three levels. At Level 1, right action is initiated to avoid punishment and to serve one's own needs. At Level 2, right action is to gain approval from others and to abide by legal authority. At Level 3, right action is the result of respecting individual rights and social contracts based on principles of justice, fairness, and universal human rights. According to Kohlberg's research, people appear to develop sequentially through these levels. As one matures, right behavior moves from being motivated by external standards and rules to taking guidance that results from internal recognition and control. The rationale behind this model is that people move from a self-centered to a principle-centered approach to decision making. Being at a higher stage does not ensure that more ethical decisions will be made. The processes of awareness and self-reflection that lead to self-consciousness allows a person to identify the level he or she is in, which in turn, results in intentional decision making.

The process of self-consciousness is what allows one to distinguish himself or herself from the larger environment in which he or she interacts. From this, self-consciousness gets categorized as public and private. Public self-consciousness is the tendency to be concerned about one's self as perceived by others. Self-monitoring, self-awareness, and paying attention to one's relationships with others are components of public self-consciousness. Components of private self-consciousness are self-reflectiveness and internal awareness. A related construct used to describe private self-consciousness is mindfulness.

Mindfulness has its roots in contemplative traditions where conscious attention and awareness are actively cultivated because consciousness is related to sustaining quality of life and well-being. In management theory, mindfulness is most closely aligned with emotional intelligence—the array of noncognitive skills, capabilities, and competencies that influence one's ability to succeed in managing environmental demands and pressures. Emotional intelligence is becoming a considered and measured factor to include in leadership capability and change management. As an aspect of self-consciousness, mindfulness is important in disengaging individuals from automatic thoughts, habits, and unhealthy behavior patterns. Therefore, mindfulness plays a role in fostering self-regulation and guiding personal understanding of one's own ethics and subsequent response to social issues. A fundamental aspect of mindfulness is the capacity for self-awareness and heightened self-knowledge.

Self-Awareness

Self-awareness is the extent to which an individual monitors and reflects on his or her own behaviors, traits, and accomplishments. The more self-aware one is, the more likely the attempt to match behavior to his or her beliefs and internal standards. For example, if people have norms against stealing and cheating, those who are self-aware are much less likely to engage in these behaviors. Some evidence suggests that self-aware individuals are more likely to assume responsibility for a given action. Research and practice in systems theory cites self-awareness as an integral component to effecting systemic organizational change. Self-awareness can be anything from broad, abstract, and far-reaching (i.e., "How do I uniquely contribute to bettering society?") to narrow, concrete, and short term (i.e., "Do I tell a white lie to get ahead?"). The process of self-awareness requires a person to examine his or her potential actions in light of moral standards.

Self-awareness also has public and private aspects. Public self-awareness is associated with moral approbation, defined as a person's desire to gain moral approval from others. According to this theory, the desire to be viewed as a morally good person influences one's ethical course of action and decision making. Moral approbation characterizes the internal need for approval, and public self-awareness is part of monitoring this process.

Private self-awareness is prominent in theories on self-regulation—how individuals choose and accomplish their goals. It involves an inward focus of one's behavior. Therefore, a person's thoughts and feelings about himself or herself affect goal-directed behavior and motivation.

Psychological theories that suggest that self-awareness is an inherently positive quality are referring to self-awareness as self-knowledge—the mix of roles, traits, values, and relationships and past experiences acquired through social interaction. Individuals come to know themselves through social comparison, observing their own behaviors, and through awareness of how others react to them. Therefore, social interaction and communication play an important role in shaping one's self-knowledge.

At one time, self-knowledge was seen as the most complete and perfect form of knowledge available.

Today, however, the accuracy of self-knowledge is challenged through the construct of self-deception: Are people fooling themselves into believing that they are different and/or better than they really are?

Two distinguishing areas associated with self-knowledge are identity crisis and identity conflict. Identity crisis deals with the difficulties of defining oneself because one's environment and experiences change over time. Identify conflict is often linked to this crisis and occurs when multiple definitions of one's self come into conflict and dictate competing, incompatible courses of action. It is particularly relevant in an organizational setting where a person's values and identity conflict with organizational goals. Unlike cognitive dissonance theory, which says that the inconsistency needs to be resolved, identity conflict suggests inconsistency can be tolerated until one encounters a situation that makes it impossible to sustain both definitions of self.

Identity conflict typically produces passivity, guilt, and feelings of being a traitor. It also precipitates whistle-blowing in an organization—the disclosing of misdeeds of superiors and/or colleagues to preserve ethical or morally acceptable behavior and to prevent and correct wasteful, harmful, and/or illegal acts. The act of whistle-blowing shows an individual is no longer willing to violate a personal code of ethics for the sake of the organization.

The Impact of Self-Consciousness on Society and Ethics

There are four areas that outline the impact of self-consciousness on society and ethics. First, the maxim "Know thyself," as articulated by the Greek thinker Solon, comes through understanding one's culture and sociohistorical context. The reflective and reflexive capacities that are the hallmarks of self-consciousness have an impact on the private and public aspects of one's personal life and significantly influence social actions. It is through the vehicle of social action that one's individual's life and total societies are created and sustained.

Second, the by-products of self-consciousness (i.e., awareness, control, intention, and self-reflection) influence behavior and/or intent to behave. Most notable are studies on conformity, which have found that the more self-conscious/self-aware an individual is, the less apt she or he is to be swayed by group or social norms. This may support either ethical or unethical behavior. The key is that the ethics of business is the ethics of those individuals who make business decisions. The process of self-consciousness shapes individual decision making.

Third, the role of self-consciousness influences the question of workplace distributive justice, defined as reward allocation in situations where more than one person has contributed to the outcome. People whose disposition focused on private self-consciousness tended to allocate rewards on the basis of the privately held principle of equity. That is, people are rewarded as a direct function of their contribution. People with a predisposed focus on public aspects of self-consciousness, which uses a social standard, allocate rewards according to the principle of equality. Specifically, people share evenly in rewards without regard to their relative contributions. The point is not to label one disposition, public or private self-consciousness, as better or to associate self-consciousness necessarily with concrete behaviors. What is worthy of note is how self-consciousness directly influences workplace issues of import, such as determining a just allocation of rewards.

Finally, an Aristotelian approach to business ethics is often applied with its focus on individual character, and not only on impersonal policies and abstract principles and theories. Implicit in this approach is the role of an expanded self that is part of and identifies with the larger community or society. The act of becoming self-conscious creates this enhanced awareness and connection. This integration of one's self with society is a component of integrity—a defining characteristic of ethical leadership.

Conclusion

In *Man's Search for Meaning*, Viktor Frankl says being human means being conscious and being responsible. The concept of self-consciousness has not, to date, been integral when discussing the ethical dimensions involved in the relationship of business to society. However, it is an endeavor worthy of further research.

Individual, organizational, and societal factors affect ethical decision making. Frequently, these factors interact, influencing a business's course of action. Focusing on the role of self-consciousness gives deeper insight to understanding not only one's self but others, all within a social environment of which business is a part. Consciousness is informed by values, worldviews, and ideologies, each of which translate and affect day-to-day business operations. How we define work, the role of corporations, and the responsibility of business to society are examples of changes noted in management theories as requiring paradigmatic shifts in consciousness. Future study and attention to self-consciousness inform this discussion at a deep and sustaining level.

—Michele Simms

See also Aristotle; Cognitive Moral Development; Kohlberg, Lawrence; Nozick, Robert; Self-Deception; Self-Realization; Self-Regulation; Self-Respect

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Self-Deception

Self-deception is the act of leading oneself to believe something is false, and this can occur with varying degrees of self-awareness about the process. The other face of self-deception is denying or ignoring the relevance or importance of evidence and argument that is contrary to our preferred vision of ourselves and our world. A common example would be ignoring chest pains and convincing oneself that all is well even with all the classic symptoms of heart problems. Because self-deception is seen as a barrier to living an authentic and ethical life, from the earliest of times, philosophers have encouraged us to be aware of ourselves and our surroundings—or in the words of the ancient Greek aphorism "Know thyself."

Sources of the Self

In searching to the root of self-deception, the first question becomes determining the source of the self that we are to know. For all philosophers, the essence of being human is to exercise free will—to choose how to live. Whether that choice is to follow an ideal or become fully aware of one's existential self, the central choice we have as humans is whether to be true to ourselves or to live a life of deception.

For much of Western philosophical history, humans had a "self" that existed at birth. That self was a complex being with contradictory motives and actions, elements of human nature that were measured against ideals (Plato), or the exercise of virtues necessary to fulfill one's role in society (Aquinas). People who adopt this notion of self tend to have a transcendental vision of the soul, which is grounded in religious or philosophical commitments. In this tradition, self-deception occurs if one does not ruthlessly measure one's motives and actions against the ideals as one navigates through life.

Another understanding of self emerged with the existentialists and the notion of a constructed self. As individuals are placed in history, they come to understand who they are as they interpret the events of their lives. As meaning is given to the events, people determine their identity in relationship to the rest of the community. For Albert Camus or the early Jean-Paul Sartre, the self constructs itself by free acts of will. For other theorists, the sense of self is constructed as individuals accept or reject information that is given to them about their place in society. For example, for much of history, women "knew" that they were supposed to create households and raise children because that was the role given to them by society. Men "knew" that they were to be the breadwinner and were measured by how well they supported the family. In this tradition, self-deception emerges as one does not accurately evaluate one's position in the social matrix.

Finally, a third school of thought asserts that self-deception is a natural progression of evolution. To survive, all species adopt camouflage to protect them from the enemy. Thus, if a person wishes to succeed in business or marry well, that person must exaggerate personal strengths and minimize weaknesses to be positioned for survival. If one actually believes the rhetoric, one is more convincing and, thus, more likely to succeed. This school of thought asserts that the quest to minimize self-deception may in fact be counterproductive because people will not position themselves appropriately in the marketplace to succeed. However, to the degree that telling the truth will maximize the opportunity for survival, self-deception should be avoided.

In practical ethics, for individuals seeking to fulfill their obligations and have a good life, all three theories about the source of self-identity and the role of self-deception in shaping that identity have the same implication: To be a mature ethical actor and survive in the community, one must be ruthlessly aware of one's self, motives, and place in the community. In the first two traditions, self-deception means that we are avoiding responsibility for ourselves. In the third, self-deception may hinder our ability to survive.

Sources of Self-Deception

While the following list is not exhaustive, eight different sources of self-deception provide insight into the patterns that keep people from seeing themselves clearly.

1. One source of self-deception may be undesirable thoughts or actions that are influenced by the subconscious or the unconsious. Self-interest, including the very basic will to survive, is often raised as a barrier to truth telling. Prejudice, desire, insecurity, and other psychological factors are cited as affecting people's ability to accurately assess a situation and respond authentically. Much of psychology is dedicated to helping people explore and understand their subconscious with the goal of making explict hidden motives and drives. With understanding, the seeker can use his or her will to break habits and make more ethical choices.

Example: A person promotes himself as an "expert" and "star" even though his performance is mediocre. As he does not get the promotions he believes are deserved, in therapy he discovers that his parents always told him that he was wonderful, even when he knew that he wasn't.

2. Social pressure is another source of self-deception. For example, society has very deep commitments to how the genders are to relate to each other. Women who wished to pursue certain male-dominated careers were told that those desires were not "normal" and were counselled out of them. The conversation about essentialism, whether certain traits or qualities were "essential" to one's racial or gender identity, served to underscore societal expectations for the self. Thus, one had to carefully evaluate one's desires and choices against the social fabric of acceptability.

Example: A woman finishing law school has the skills to be an excellent litigator. However, her grandfather, who is also a lawyer, strongly asserts that fighting in the courtroom is unseemly for a woman. That lawyer then settles for another, lesser paid and esteemed branch of the law, convincing herself that she would rather be a "lady," and wouldn't be that good anyway, than follow her talent and passion.

3. Another source of self-deception comes with unthinkingly embracing social roles to achieve calculated rewards. Thus, people climbing a professional ladder will routinely overestimate their abilities to reach a goal or maintain market strength. Those who understate their abilities do not get promoted. Others may not examine whether the roles they have taken on are congruent with their own desires. Thus, people choose careers based on how much money they will make or power they will amass rather than according to ability or desire.

Further, identification with a role may excuse examination of a larger social problem. One who is a "company man" may not believe that he can critique the overreaching of a corporation. As one takes on the identity of a profession, one may be blinded to the cost to the self in terms of authenticity. Thus, lawyers who professes a commitment to justice may balk at seeing themselves as technicians who manipulate the law. Their very identity as public servants would be compromised by clearly seeing the trajectory of their career. Thus, self-deceit can be a function of our wanting to think of ourselves as honest persons.

Example: A son is in line to inherit the family business. Even though he does not like business, he follows the career chosen by his parents and grandparents. As he struggles to perform well, he finds that he is miserable. Telling the truth about his skills and choosing to change professions require a great deal of courage.

4. Humans may be deluded by suggestive propaganda or even a neighbor's back-fence rhetoric. Much advertising is designed to manipulate our understanding of ourselves—strong not weak, rich not poor, right not wrong. Whether it is a question of notions of racial or national superiority or an accurate assessment of

one's own or children's abilities, humans tend to hear what they want to believe. Studies of people find that we routinely overestimate our abilities and our place in the community. Most of us believe that we are more talented, more attractive, or more successful than the average. Clearly, by definition, we cannot all be above average.

Example: Many college graduates who attended a middle-of-the-road school and received middling grades are surprised when they do not command top dollar at prestigious organizations. These students have been told forever that they were "special" and "talented." Whatever niggling fear they might have that they are not "the brightest and the best" is dismissed. Their failure to achieve a highly placed position is someone else's responsibility for failing to recognize their talent.

5. Humans may be misled into addicted behavior where they are unable to see the truth, because their habits are so deeply ingrained that they form virtual blinders. Those who wish to cast off the behavior of alcoholism must begin by acknowledging that they are in fact addicted. As society has identified a whole series of addictions from food to work, recognition and naming of the addiction must precede mastery.

Example: An executive is convinced that she is the only one who can effectively lead the company. That executive works 7 days a week, resisting taking vacations. When forced to leave, the cell phone and computer are constant companions. That executive exhibits all the classic symptoms of addiction to work. However, because diligence is valued, that executive will have to face a personal crisis, such as a divorce, a problem with a child, or physical illness, before admitting the truth: No one is indispensable.

6. Many people surrender their autonomy to create an intimacy that will offset the pains and perils of loneliness. Many who are in abusive relationships, whether personal or in the business world, justify the behavior of the abuser by asserting that the abuse was deserved. Others define abuse as love to avoid the possibility of being alone or rejected. People will also surrender their autonomy to be accepted by a group. The fear of being excluded has kept many people from carefully examining both what was being taught and the behavior that was then expected of the members.

Example: A personal assistant to an explosive executive will put up with the abusive behavior, convincing herself that the stress of the job is what causes the angry outbursts. If another coworker suggests that she should not put up with the behavior, the suggestion will be dismissed.

7. One of the most enticing forms of self-deception is attachment to a closely held belief about the world. Rather than being proved wrong about a situation, we refuse to either accept data that contradict our beliefs or engage in experiences that might enlarge our sense of ourselves or the world. From our perspective at present, white men being terrified by integration of African American children into a school seems irrational. At the time, however, the attachment to the notion of racial superiority transcended evidence to the contrary.

Example: Many Americans believe that our health care system is the very best in the world, even though it is the most expensive and many people do not get good care. Evidence of other health care systems, such as those in Canada, giving excellent care is minimized or dismissed. Then, when someone goes to India for surgery and spends a fraction of the cost for the same service that is provided in the United States, many refuse to believe that those physicians are as well trained and qualified as those in the United States. By definition, any item made or service provided in the United States is better than an equivalent anywhere else in the world.

8. Finally, we can get caught in a frenzy of antireason and be persuaded, by our emotional identification with a certain mood or movement, that we are somehow more important to all other people than we really are. Each person has a seemingly primal need to be included and important. Thus, we misinterpret motives, actions, and events to give ourselves a larger place in the stream of history than we would otherwise deserve.

Example: A talented athlete believes that he is somehow exempt from all the rules of the organization. He believes that his value to the team is such that his "bad-boy" behavior and image will be tolerated. When benched or dismissed from the team, he is surprised that he is dispensable.

Antidotes to Self-Deception

Self-deception has been classified into three types. Cognitive self-deception occurs when one does not interpret data correctly. Learning rules of analysis will often be an antidote to that form of deception. Emotional self-deception happens when one does not accurately name and respond to emotional states. Moral self-deception occurs when one fails to tell the truth about oneself or one's world. This failure can result in either not being true to oneself or not being an ethical member of the community. All three forms of self-deception begin with a failure to pay attention.

A central task of being human is to understand one's self and one's place in the world. If we don't pay attention to what is happening around us and how we interpret that activity, we fall prey to self-deception. We have the capacity to see, evaluate, and ultimately accept or reject the identity given to us by ourselves or others. Thus, the primary source of self-deception is a failure to "notice" the thing that threatens our identity and then not notice that we are blind. We may see economic injustice a thousand times, but if we have not noticed it, that injustice cannot be said to have entered our experience.

According to William James, our consciousness—or sense of meaning, our sense of self—must be constructed out of what we have seen. If we have not seen ourselves as an oppressor, we may be distressed by another accusing us of misusing our power. If we rationalize that experience or deny it, we move into self-deception rather than facing the possibility of changing our sense of self. Thus, the first step to overcoming self-deception is to practice seeing that which we don't expect to see.

Some who practice self-deception have never been taught to see compassionately and accurately. If families do not teach children to accurately assess themselves or their situation, the skill of reflection and truth telling is not learned. Others are not motivated to overcome patterns of self-deception. Telling the truth requires anticipation of possible outcomes, concentration, and effort. If truth telling is not valued, apathy or disinterest will dampen our desire for the hard work required to not succumb to self-deception.

As we learn to see more clearly, we must be careful not to misperceive random data and see patterns where there are none. We must carefully evaluate the data around us, looking both for data that confirm our beliefs and those that do not support our worldview.

Finally, as we learn to see clearly, we will be able to carefully judge ourselves. In the process of evaluating our actions in the community and accurately attributing cause to the results, we can learn to be responsible for ourselves rather than be at the mercy of our community. In the process, we can evaluate ourselves against the standards or goals—whether an ideal or set of virtues—that we believe are essential for us. Countering the entropy that leads to self-deception requires an act of will; but the prize will be an authentic life—one lived according to one's own definition of the good life.

—Catharyn A. Baird

See also Accountability; Aristotle; Authenticity; Darwinism and Ethics; Existentialism; Free Will; Roles and Role Morality; Self-Interest; Self-Regulation

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Self-Interest

Self-interest is the desire to act in ways that promote what is good for one's self. Whether or not human behavior is, or perhaps more importantly should be, motivated by self-interest has been a central theme throughout the history of Western philosophy. The term *egoism* is used to describe a variety of philosophical schools of thought on the pursuit of self-interest. Some Eastern philosophies, notably Taoism and Zen Buddhism, also discuss a form of egoism—solipsism—that argues that one's own existence or at the least the experiences of one's own existence are the only things one can truly verify.

Most religions have codes of conduct that promote regard for others, fearing an inherent danger that self-interest will be pursued excessively. The dividing line between self-interest and selfishness is thin at best. The line is arguably crossed by pursuing one's own interests in ways that knowingly cause harm to others or with disregard for potentially harmful (even if unintended) side effects.

Beyond the realms of philosophical inquiry, the belief that self-interest explains human behavior has had a profound influence on the development of classical and modern political and economic thinking. The idea that pursuing self-interest can simultaneously serve the public interest underpins classical economic theories favoring free markets in production, exchange, and consumption. A belief in the positive power of self-interest is strongly linked to the emergence of individualism as a political force and the enforcement of private property rights under capitalism.

The assumption of self-interested behavior can be extended to the analysis of business and organizations. First, people in organizations may pursue what is good for them rather than what is good for the organization (the principal-agent problem). Second, organizations may pursue interests that conflict with the interests of others (stakeholder theory) and the interests of wider society (corporate social responsibility). This makes understanding self-interest crucial to the analysis of business, ethics, and society.

Egoism

Egoism is the term used to describe the philosophical doctrine that what ultimately matters to a person is his or her own self-interest. The term egoism derives from the Latin word *ego,* meaning *I*. It is important to note that what is in one's self-interest may incidentally be detrimental to others, beneficial to others, or neutral in its effect: Self-interested behavior is, therefore, not inherently immoral, because serving one's own interests does not necessarily imply intentions to harm others or indifference to any incidental harm. Egoism must be clearly distinguished from *egotism*—an excessive or exaggerated sense of self-importance that can manifest as selfishness and narcissism.

A variety of egoisms have been proposed, which can be grouped under two headings: descriptive or psychological egoism and normative egoism.

Psychological Egoism

Psychological, or descriptive, egoism suggests that self-interest fundamentally describes human nature—in effect, people pursue only that which is in their self-interest. In the extreme, accepting psychological egoism implies that even when a person acts in an altruistic way, or with regard for others, the reason is self-interest. According to this reasoning, acts which might appear to be or which some people might interpret as being done out of regard for others, such as helping a stranger, inherently have a self-interested component.

Thus, the belief in psychological egoism is non-falsifiable if truly altruistic behavior is by definition impossible. Critics also argue against psychological egoism on empirical grounds, stating that much psychological research into motivation suggests that it is too extreme to believe that all behavior is motivated by self-interest.

Questions about motivation are crucial to understanding the debate over self-interest as a description of human behavior. The chief question is, of course, whether or not self-interest is the only thing that motivates people; or does self-interest coexist with other motivations? A related question is, even allowing that self-interest is an important motivation, is it the most important motivation? Further, what constitutes self-interest—is it always something one can know? For example, one could argue that there could be a short-term self-interest that may conflict with a long-term self-interest. And assuming we know our self-interest, do we always pursue it to our maximum advantage, or would we moderate our goal of self-interest in any way?

Normative Egoism

Normative egoism suggests that people ought to act in their own interests, either because it is rational to do so (rational egoism) or because it is moral to do so (ethical egoism). In the strongest version of rational egoism, pursuing one's own interests is not only rational, but it is also irrational not to pursue them. In a weaker version, the latter condition is relaxed, and therefore, not pursuing self-interest is not necessarily irrational.

A strong version of ethical egoism holds that it is always moral to promote one's own good and it is never moral not to promote it. A weaker version states that while it may always be moral to promote one's own good, not pursuing one's self-interest could also be moral.

Normative egoism avoids the criticism noted above about psychological egoism because one's motivations are not important. Rather, one should act to serve one's own best interests in the name of logic and/or morality.

Self-Interest in Economic and Political Thought

The belief that self-interest is a fundamental aspect of human nature has had a profound impact on the development of classical liberal economic and political thought. The writing of the renowned Scottish moral philosopher and political economist Adam Smith has been used to support the primacy of self-interest in economic affairs. First, he argued that we should not think that it is because other people are benevolent that they supply goods that meet our tastes, but rather they are driven by their interest in profiting from our demand.

Wicksteed, in *The Common Sense of Political Economy, Including a Study of the Human Basis of Economic Law*, also suggests that people entering economic relationships do not intend to further the interests of the other party in the exchange, although the outcome of the exchange may in fact serve the interests of all parties. This idea is called non-*tuism* to contrast it with *tuism*, interest in the "other" (*tu* in Latin means *you*). However, even though non-*tuism* suggests neutrality about the interests of the "other" in the economic transaction, it is compatible with broader altruistic behavior as well as self-interest, such as a person driving the hardest possible bargain to secure the most food possible to feed the starving in Africa.

Smith argued further that national economic policy should promote competition because, then, the sum of individual self-interested economic decisions can lead to a socially desirable state of affairs—his famous invisible hand metaphor. Smith was asserting a form of consequentialism, sometimes called conditional egoism: Self-interest is morally acceptable if it leads to morally acceptable ends.

Nonetheless, Smith should not be considered an unequivocal advocate of self-interest, having in his philosophical writing extensively discussed what he called sympathy as fundamental to human nature. In his *The Theory of Moral Sentiments,* people exhibit sympathy and listen to their *impartial spectators.* Whereas people may act opportunistically and self-interestedly, they do so within limits dictated by their sympathy, which may compel them to stop short of crossing the line between self-interest and selfishness. Smith also placed great emphasis on the virtues of benevolence and justice.

In his economic writings, Smith warns of the tendency for businessmen to collude against the common interest if allowed, thereby reinforcing his idea that self-interest can easily give way to greed unless competition holds it in check. *An Inquiry Into the Causes and Consequences of the Wealth of Nations* was written to persuade politicians to restrain their desires to hand out governmental favors and create monopolies at the expense of consumers; competition is achieved through a *laissez-faire* policy.

The Wealth of Nations was published in 1776, the same year in which the U.S. Declaration of Independence was signed. Arguably, this was more than a coincidence as there was a symbiotic relationship between emerging classical economic theories and political theories of individualism. Individualism describes a political and social philosophy that promotes the primacy of the individual and his or her right to the maximum degree of liberty consistent with the maximum liberty of others. The American colonies equated their struggle for political and economic freedom with values of "individualism": self-reliance and independence.

Self-interest and individualism became axiomatic assumptions in the neoclassical school of economics that has come to dominate economic thinking during the 20th century. *Methodological individualism* is invoked to reduce economic analysis to the level of the individual person or firm. Economic writers have expressed views consistent with both psychological and normative egoism, but rational egoism is the variant of self-interested behavior that is most commonly used to explain people's economic decision making—people are acting rationally when they seek their own interests. Models of behavior based on self-interested individualism have been applied to wider social settings under the title *rational choice theory*, purporting to explain behaviors such as marriage, divorce, and family formation. A variant called public choice theory examines political settings, such as the irrationality of an individual becoming an informed voter, and the rationality of "pork-barrel politics," where politicians ignore wider public interest to serve their own interests or those of their immediate constituency.

In the late 20th century, neoliberals developed a political movement based on the pursuit of self-interest, bolstered by individual ownership of property and freedom to make (economic) decisions with minimal interference from the state. The concept of a "Nightwatchman" state is equally applicable to economic and political affairs—the state's role is to provide national security, enforce individual rights through a police force and judiciary, and enforce contracts and private property. This analysis of the role of the State vis-à-vis the individual led the neoliberal movement to critique increased intervention by the state in economic and social decisions, championing the cause of the individual for knowing where his or her best interests lie. Individualism is invoked as a virtue, while effectively ignoring the fact that individuals live and operate in societies and, thus, are influenced knowingly and unknowingly by societal norms, expectations, and constraints. The former British prime minister and neoliberal Margaret Thatcher was nearing the end of her reign when she famously declared that there was no such thing as society, only individuals and their families.

The idea that people are egoists is not just an abstract debate among philosophers, economists, and political theorists. The assumption of self-interest is widely held among the general population. The established folklore about self-interest is problematic for two reasons. First, there is evidence that people are more likely to agree that others are driven by self-interest the more they are told that this is the case. For example, studies have found that completing a course in economics is likely to lead to an increase in the likelihood that a student will believe that self-interest is a fundamental description of human behavior, compared with the same student prior to the course and to another student who has completed a course unrelated to economics or business. Second, there is a tendency among the general population to conflate egoism with selfishness; thus, it is unclear whether self-interest in folklore is effectively egotism rather than egoism.

Self-Interest and Outcomes

Belief that self-interest lies at the heart of economic decisions is argued to be justified by empirical observation of aggregate economic behavior. Economists argue that no one has to be explicitly driven by egoism; yet the evidence of economic statistics is interpreted as showing that, on average, people act as if they are self-interested. Thus, while one might never actually bump into *homo economicus* (economic man) on the street, the outcome of economic decisions is consistent with the assumption that people may be motivated by egoism. However, the principle of revealed preference is subject to a nonfalsification critique. If it is rational to only do things in one's self-interest, then everything we observe people doing must be the thing that was in their best interest; otherwise they would not be doing it. We do not need to know motivations in advance because these will be revealed through actions: The desire to maximize self-interest leads people to make the best choice for themselves.

Two situations argue that pursuing self-interest may not always be rational. The first, called the tragedy of the commons, starts from an empirical observation. The second, the prisoner's dilemma, uses a thought experiment to explain the tragedy of the commons.

The tragedy of the commons refers to the fact that in commonly held resource stocks, every person pursuing his or her own self-interest will lead to the over-exploitation of the common pool. In grazing cattle on common land, for example, each individual owner of cattle is trying to capture an increase in value to his or her herd through grazing, whereas any cost in terms of degradation of the land is spread across all grazers. The outcome of each person pursuing private benefit is overgrazing and a worse outcome for all.

The reason for this outcome can be elaborated through the prisoner's dilemma, an example of game theory. Consider the prisoner's dilemma where two women are arrested as suspects in a crime and interrogated separately. The evidence is weak, so the police want to induce the prisoners to confess to the crime. If neither confesses, the best the police can hope for is to convict on a lesser criminal charge. The police offer each prisoner a deal: Confessing to the crime and implicating her accomplice will lead to conviction on a misdemeanor carrying a very light sentence for herself and a very harsh sentence for her accomplice. The dilemma is created because the offer also states that the very light sentence only applies if the accomplice does not also confess. If both prisoners confess and implicate each other, they both face an intermediate-length prison term, more than a lesser criminal charge but less than staying quiet while her partner confesses.

Neither prisoner can be sure of what the other might do. Had they been able to cooperate, the best strategy for both is to stay quiet because they both will receive only a minor sentence. But without the prospect of cooperation, the individual's best outcome arises when she confesses and implicates the other person, who does not confess. If the prisoners are rationally self-interested, each will suspect that her partner will choose to confess in the hope of getting the best possible deal for herself. Thus, the theory predicts that both prisoners, pursuing self-interest, will confess, resulting in a worse outcome than cooperation. Just as in the case of the tragedy of the commons, cooperation would lead to a superior outcome for everyone (the *common weal*), whereas pursuit of individual self-interest would lead to a far worse outcome. The difficulty lies in finding mechanisms to promote cooperation over individualism.

Self-Interest and CSR

The notion of self-interest can be extended directly into the business world through agency theory, also called the principal-agent problem. Agency theory arises in any employment situation when one person (the principal) hires another (the agent) to perform tasks that benefit the principal but may not serve the interests of the agent and where monitoring the agent's performance is costly to the principal. The challenge is to find a way to ensure that the actions of the agent serve the interests of the owners rather than the interests of the managers; a variety of compensation schemes have been proposed, such as stock options for managers who raise the value of the companies they run.

Stakeholder theory goes one step further, suggesting that businesses and the people who own and run them should take into account the interests of a wide range of people who are affected by the decisions of the business. These impacts may be direct (especially when financial interests are involved) or indirect (there may be spillover effects or externalities). Arguments along these lines lay the foundations for theories of CSR, suggesting that companies have economic, legal, ethical, and philanthropic duties to fulfill in society.

Conversely, the Nobel Prize–winning economist Milton Friedman declared that the only social responsibility of business is to increase its profits or shareholder value. As long as profit is achieved legally, business is considered to have met its economic and ethical obligations. Philanthropic acts, or actions that promote societal well-being but reduce profit or shareholder value, are considered theft from shareholders.

The argument made above parallels Smith's argument that self-interested behavior will (under competitive conditions) result in socially desirable outcomes. But whether the unit of analysis is a business or an individual, pursuit of self-interest is not necessarily straightforward. Issues such as acid rain, global warming, and shrinking biodiversity remind us of the global commons in which business operates. In these examples, pursuit of supposed self-interest (represented by profit in Friedman's robust defense of capitalism) may lead to the opposite, though possibly only in the long run. This begs the following question: If profit and shareholder value are not really business's self-interest, what is and how can it be achieved?

—Will Low

See also Altruism; Asymmetric Information; Capitalism; Consumer Sovereignty; Corporate Social Responsibility (CSR) and Corporate Social Performance (CSP); Economic Rationality; Egoism; Friedman, Milton; Game Theory; Individualism; Invisible Hand; Laissez-Faire; Other-Regardingness; Prisoner's Dilemma; Prudence; Rand, Ayn; Smith, Adam; Stakeholder Theory; Taoist Ethics; Tragedy of the Commons

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Self-Ownership

The principle of self-ownership asserts that every person has a property in his or her own person and the labor of his or her body. Ever since the 17th-century political philosopher John Locke argued for self-ownership on the ground of self-preservation, many political philosophers, economists, and business ethicists have debated the meaning, extent, and political implications of self-ownership. The basic tenet of classical liberalism in the 18th and early 19th centuries was the idea that individuals owned themselves. To protect individuals' freedom to develop their talents and life plans without intervention, many classical liberals argued that maintenance of law and order and protection of individual liberty were the unique functions of government. Economic liberals in that era, in particular, argued that individuals should structure their economic life without intervention from government. In the latter half of the 20th century, libertarians adopted many of these arguments to reject most state interventions and to ground the right to private property. There are four general features to the libertarian thesis of self-ownership. First, self-owning persons are the rightful owners of their own person and faculties. Second, persons have the power of disposal and transfer—that is, a right to freely sell, rent, or exchange their labor and talents as commodities in an open market. Third, persons have the right to accrue private ownership of the fruit of such labor and talents and not be forced to dispose of their possessions in the absence of prior contractual arrangements. Fourth, persons who respect the similar rights of others have an absolute right to themselves and their properties.

The idea of having ownership rights over oneself may initially seem counterintuitive, if it suggests that there is a distinct thing, the self, which one owns, since it implies that we can treat ourselves as disposable objects and not as persons with intrinsic value. Many have pointed out that treating ourselves as properties that we "own" and can dispose of may counter the Kantian idea of respecting our own dignity and humanity. The 18th-century philosopher Immanuel Kant argues that freedom is one innate right that belongs to all rational persons, who have inherent value and should be their own masters. Kant does not think that such freedom implies that one is the "owner" of oneself, if that implies one is free to dispose of or exploit oneself. He believes that we have to respect our own humanity and rejects any thesis of self-ownership that denies the existence of self-regarding duties.

The question of when one's action may violate one's own dignity and humanity is a complex one. Some believe that organ sales, prostitution, commercial surrogacy, and voluntary enslavement all treat human bodies as mere means, and a thesis of self-ownership that allows such transactions violates humanity and contradicts the idea of being master of oneself because one is relinquishing control. Some also believe that suicide and euthanasia, which seem to be allowed under the thesis of having ownership rights over oneself, destroy one's life and go against the duty of self-preservation. However, others disagree that commodification of body parts is categorically different from the use of one's labor or mental powers for income. Some believe that it is an expression of being the master of oneself when one transfers the power to others. Other critics also believe that the freedom to end one's life, especially in certain painful and terminal medical conditions, protects and preserves one's dignity.

The metaphysical question of what it means to own ourselves is also an interesting one. Some argue that the thesis of self-ownership does not imply that one has two selves, one of which owns the other. It also does not imply that we can rightfully treat ourselves as mere means. They argue that the "self" has a purely reflexive significance—that is, it is self-referential. What owns and what is owned are one and the same, the whole person.

At a fundamental moral level, self-owning is tied to the liberal idea of being autonomous agents. It signifies having moral authority to decide how to live one's life within the constraints of the rights of others. It signifies that without previous commitments and relevant transgressions, it is wrong for others to make use of the agent's body without his or her permission. It implies an exclusive right with respect to our bodies and the use of our talents and/or skills against any coercive action taken toward us. For example, without consent, coercive sexual advances violate the agent's bodily integrity. It is this idea of defining the boundaries of things others can and cannot do to us that makes a thesis of self-ownership consistent with Kant's principle of treating people as ends in themselves and not as mere means. A thesis of self-ownership that focuses on people's autonomy requires that we respect the bodily integrity of each other by preventing the physical coercion of some persons by others. It brings freedom from others and governments, except insofar as we agree to associate with them.

Robert Nozick, who adopts the Kantian idea of not treating people as mere means, is one of the most prominent political philosophers of the 20th century. He argues for a strong theory of rights that takes seriously the existence of distinct individuals who are not resources for others. According to Nozick, self-ownership is based on the fact that persons possess various characteristics. Persons are rational beings who have the ability to regulate and guide their lives in accordance with various self-chosen goals. They are distinct individuals with separate interests, and Nozick conjectures that it is by virtue of their ability to meaningfully shape their lives that they have a right to choose and realize their ends, as long as they respect others' right to do the same.

Some argue that the freedom to control and use one's own body supports a right to reap the benefits of one's choices and to have private property. Such right implies that others have no legitimate claim to your property without prior agreement. The Lockean idea that one has the right to the fruit of one's labor has led many, particularly libertarians, to argue that taxation of earnings from labor and other forms of redistribution of wealth are equivalent to forced labor. It is enslaving the better off for the benefit of the needy and, thus, is a violation of self-ownership. It condones partial property rights in other people and makes some people mere resources for the lives of others. Self-ownership is a central component of the idea of freedom or autonomy, and coercive redistribution of wealth makes a society less free.

Others argue that control self-ownership is very different from income or property ownership, which is not directly about one's body. The claim that we own ourselves does not imply anything about external resources. Control rights are justified on the individualist grounds of liberty, autonomy, and self-determination, framed by the agent's preferences, values, and life path. They can be supported without reference to the distribution of resources as a whole. Income rights and property ownership, on the other hand, are justified and determined by principles that govern the pattern of distribution of goods in the economy—considerations that are irreducible to individualist interests.

The issues of private property and distribution of resources bring up the question of how to reconcile the principle of self-ownership with other moral concerns such as equality. In the past few decades, libertarian and egalitarian thinkers have focused on the issue of whether the distributive and proprietarian implications of this principle preclude any redistributive measures. Many libertarians argue that to protect self-ownership and individual freedom, resource distribution should be based solely on free transactions in the open market. Others, especially egalitarians, argue that a general acceptance of the thesis of self-ownership still leaves open the question of whether agents are entitled to full benefits of their choices and of their natural personal endowments. Some argue that a plausible thesis of self-ownership ought to acknowledge rights to a fair share of society's resources.

Two related arguments are often evoked. First, some argue that self-ownership does not imply exclusive rights to private properties or does not override all other moral claims. While a strict egalitarian approach that supports joint ownership of all resources by the individuals in the population will inevitably conflict with self-ownership, certain efforts that prevent or minimize massive inequalities that may leave some people vulnerable can be legitimate. Interestingly, even though many libertarians find support for extensive property rights in Locke, he argues that one must be sensitive to others' unmet needs. While Locke believes that we have a right to own things for the purpose of self-preservation by mixing our labor with it, he contends that the natural right to self-preservation demands that our appropriation does not make others' situation worse off. Keeping in mind the importance of having access to basic needs, some argue that a plausible conception of self-ownership cannot imply unlimited property rights for some if others are deprived of access to such necessities.

While it is difficult to ascertain a causal relationship between one's appropriation and others' unmet needs, some argue that the idea of unlimited property rights is self-defeating, since it contradicts the libertarian goal of promoting autonomy. Some point out that people who lack access to basic needs will have less opportunity to pursue their own conception of the good, and thus, their autonomy or freedom is severely compromised. They will not have the same opportunity to live an autonomous life and develop their capabilities. In this way, any conception of self-ownership that is grounded in the idea of autonomy ought to ensure that all persons have access to basic needs so that they can fulfill their self-chosen life path.

The possibility that unlimited right to private property may deny some people the opportunity to exercise their autonomy has led many to point out another difficulty in the libertarian thesis of self-ownership. Liberal egalitarians such as John Rawls have argued that, even though rational persons are the legitimate possessors of their talents and are free to use them in accordance with their chosen projects, natural endowments are arbitrary from a moral point of view. The libertarian thesis of self-ownership fails to recognize the fact that it is a matter of brute luck that individuals are born with different talents and skills, such that severe material inequalities that will likely arise undeservedly benefit some and disadvantage others. While respect for autonomy may imply a right to income from one's choices when there is no differential brute luck among agents, it is unfair that unequal natural endowment through no fault of one's own can lead to disparate income levels and/or different opportunity ranges. Such unequal distribution of endowment has prompted many liberal egalitarians to argue that, while there should be respect for persons' right to exercise their talents and reap benefits from such efforts, compensation is owed to those who are disadvantaged for non-choice-related reasons in their endowment. Some argue that the libertarian argument, which understands the fruit of one's labor to include everything that a person produces through his or her labor, is flawed in the face of unequal natural endowments. A more plausible understanding of self-ownership should identify the fruit of one's labor with the subset of the total product of one's labor that is due to his or her choices rather than luck. Some argue that redistribution of wealth is one plausible way to acknowledge and correct undeserved (dis)advantages that result from differential distribution of natural endowments.

The thesis of self-ownership has important implications in business ethics and other social institutions. For example, it helps determine what types of economic and political systems are just, such as whether or what types and levels of wealth redistribution may be justified. At the same time, this thesis has not answered many foundational questions, such as whether all human relations should be market relations and how we can understand any duty of beneficence to other human beings. Sorting out such issues will help explain whether a right to self-ownership is absolute and what counts as the fruit of one's labor. It will also help explain the connection between self-ownership and private property and clarify the extent to which one has a right to accrue properties that are not direct results of one's labor, such as inheritance and gifting.

—Anita Ho

See also Autonomy; Commodification; Egalitarianism; Equality; Freedom and Liberty; Individualism; Justice, Distributive; Kant, Immanuel; Kantian Ethics; Liberalism; Libertarianism; Locke, John; Nozick, Robert; Nozick's Theory of Justice; Rawls, John; Rawls's Theory of Justice; Redistribution of Wealth

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Self-Realization

Self-realization is defined as the drive to become what one is capable of at his or her fullest potential, often-aligned in management parlance with self-fulfillment. The self-realized person is characterized as having a high level of self-knowledge, an integrated personality that allows for self-expression, an acceptance and tolerance of human nature, and a greater awareness of the human condition. The actualization of personal moral ideals affects participation in socially useful and ethically acceptable work.

To fully understand the essence of self-realization, the corollary concepts of self-actualization and individuation and the interrelated concept of self-disclosure are included. Self-realization, with its focus on human potential and what it means to be human, derives from humanistic psychology.

Historical Underpinnings to Self-Realization

A variety of philosophers, theologians, and literary figures contributed to insights into what it means to be fully human, the cornerstone to humanistic psychology. The texts date back to antiquity, yet continue to shape understanding and influence the teaching and practice of business ethics today.

Prehistory includes the role of the Greek epic, most notably the work of Homer, who created the image of the individual as hero and of life as quest or an adventure. Socrates articulated the practice of dialogue, dialectical conversations that sought deeper truths through examination of daily life. Socratic discourse was both ethical and personal with its focus on achieving character and virtue through knowledge. Plato focused on the values of *true* and *good* as ends in themselves. Justice was the paramount virtue or the sum virtue with regard to one's relations with others. Aristotle's theory of virtue helped define the excellent man as one who excelled in leading a truly human life by adhering to intellectual and moral virtues. The notion of goodness, with its end state of fulfillment or excellence, was found within the context of society. Virtue was regarded as individually and socially beneficial. These philosophers underscored that living a morally good life involved justice, virtue, and character.

The 19th century marked the emergence of existentialist philosophy. Kierkegaard emphasized a humanistic vision of truth where self-consciousness propelled the individual to reach his or her highest potential. Nietzsche focused on awakening, and creating through transformation, an image of a new individual or superman who would create authentic values. Existentialists maintained that individuals had an ethical obligation to self-understanding as part of a purposeful existence. The quest to be fully human was to push the individual to farther reaches with values at the core. The 20th century marked an inclusion of the individual's role as meaningfully understood based on his or her involvement in society. Most notably, Heidegger described the fullness of humanity as the result of being in the world. Buber's philosophy of dialogue and the relationship between *I* and *thou* defined self-development as the result of one in relationship to, and in dialogue with, others.

The focus of humanistic psychology was, and continues to be, on issues that help individuals understand themselves, others, and their environments. The role of self-realization emerged as the foundation to attaining one's fullest potential and becoming fully human. Philosophers and psychologists expanded humanistic psychology to include social interest, community awareness, and spiritual experiences, further supporting the value of pursuing the highest reaches of human achievement and potential.

The single person most responsible for establishing the field of humanistic psychology and most familiar to management studies is Maslow. He identifies a cohesive theory of the self and self-actualization by identifying a hierarchy of five needs. Physiological needs and safety, as low-order needs, are predominantly satisfied externally (i.e., pay, unions, contracts, and tenure). Social belonging, esteem, and self-actualization, as high-order needs, are internally satisfied. Maslow's theory was a psychology of the whole person.

Neither the theory nor the practice of humanistic psychology advocates self-seeking gratification. Seminal researchers of humanistic psychology committed their work to discovering ways to build cohesive relationships and communities. Because self-realization informs one's ethical and moral values and affects the larger society in which one lives, it is important to include its role and influence on business ethics and society.

Self-Realization and Self-Actualization

Psychology is culture bound and often limited by implicit assumptions that create reality. For example, how one manages his or her employees or seeks to establish company stakeholder relationships is embedded in social and cultural assumptions. Such assumptions are often removed from conscious awareness. Thus, the process of self-realization is to make these assumptions conscious.

The best vantage point for understanding behavior is from one's internal frame of reference. Self-realization is a process that brings one to this vantage point. Conscious thought reveals the true self—one unencumbered by the dictates of individual, group, or organizational expectations. Self-realization entails sensitivity to values and raises the question of how individuals prioritize such values, in general and in particular situations. The process involves moral awareness, thought, reasoning, judgment, and intuition. It is not narcissistic self-gratification.

As an ideal, self-realization represents the ultimate actualization of utilizing one's fullest capabilities. A person grows toward this ideal, defined as peak performance and peak experience, through self-discovery. Peak performance is the result of a clear focus on an event that culminates in a more efficient, creative, and productive result than would typically occur. Peak experience is characterized by a sense of profound significance, recognized as the moment of highest happiness and, often, a turning point in one's life. Both terms are cited in management studies as phenomena that leaders, capable of effecting change in groups, organizations, and institutions, experience. Maslow found that self-actualizing people tend to be altruists and their work is equated to a calling or vocation.

Therefore, self-realization is not a goal to achieve but rather a corollary of an authentic life. It is cited in ethical theory because self-realization involves the recognition of one's potential and follows the second formulation of Kant's categorical imperative: that one should treat everyone, including oneself, as an end not merely as a means. This Kantian idea infers that individuals have the capacity for autonomous reasoning, with particular reference to moral judgments.

Second, it is accurate to define self-realization as a continuing process of determining one's role and contribution to society. Classical theories put forward by Plato and Aristotle state that individuals attain self-realization when they achieve their distinctive function—that is, the full development of their unique capacities. Distinctive function can be framed as moral guardianship or stewardship, concepts prevalent in the context of sustainability and the ethical mandate to contribute to sustainable environments. The process of self-realization yields one's sense of responsibility for the improvement of the world as it affects both oneself and others.

Third, implicit to self-realization is individual choice, where a person realizes and acts on his or her distinct capacities. Choosing to engage in society is the basis of individuality. Linguistic expressions of "I am" or "I do" signal ways of entering into relationships with others, the society, and the world. Yet action is personal, and self-realization functions as a tool to help determine what constitutes morally justifiable and socially useful work.

Related Constructs of Individuation and Self-Disclosure

A corollary to self-realization is the construct of individuation. Most aligned with Jung's psychology, individuation refers to a person's awareness of the ways in which he or she is different even though unseen and unrecognized by others. Individuation is a relational process based on one's awareness of his or her social environment.

Characteristics of highly individuated persons include being more creative, exhibiting more leadership behaviors, and displaying a greater willingness to express dissenting and sometimes critical opinions. Highly individuated persons influence social situations by leading others and by generating creative ideas and unusual solutions to problems. Further research, however, is needed to determine more specifically how situational contexts, such as various organizational cultures, differ in the extent to which they encourage individual differences. Given today's global business environment, there is value to assessing how national cultures that differ in terms of individualism and collectivism affect individuation. One can speculate that high individuators may have a stronger social impact in individualistic cultures than in collectivist cultures.

Finally, individuated persons have achieved a high level of self-knowledge. Self-knowledge is often identified as contributing to having insight into the behavior of others and to having a greater awareness and tolerance of the human condition. This capacity of understanding is attributed to the integration of all aspects of one's personality. Self-integration correlates with self-disclosure, the second concept associated with the process of self-realization.

Self-disclosure is explicit communication of self-data that another would otherwise not have access to. Such information exchange is considered a private act that strengthens relationships, expresses emotional experiences, clarifies personal beliefs and opinions, and maintains social control and privacy. Self-disclosure facilitates the movement from self-alienation to self-integration; in other words, self-realization is the by-product of one disclosing himself or herself to another. It presumes authentic dialogue where both parties make themselves vulnerable and available to one another. Elements of trustworthiness, safety, and security are associated with this discourse. The choice to fully disclose and be vulnerable with one person ensures an aspect of mental health that guards against the fragmentation and alienation characteristic of modern life, as also experienced in many business environments. The distinguishing features of self-disclosure include the reciprocal exchange of ideas and using dialogue as the chosen method of communication—two elements cited as part of achieving systems change and organizational learning.

On Ties to Management

Humanistic psychology influences management theories of motivation. It has helped advance the view of the employee as a social, and not a purely economic, being, as evidenced in the human relations model of management practice.

Maslow's Hierarchy of Needs is one of the most enduring theories in management, where self-esteem and self-actualization needs are accepted without question. The ideal of the self-realized person emerged as an implicit and central concept in the seminal management theories of organizational behaviorists Argyris and Herzberg and theorists on work and job design such as Hackman and Oldham. Encouraging participative supervisory and leadership styles, designing appropriate forms of work organization for employees to experience self-actualization, and Theory Y leadership are related to the functions of self-realization.

Examples of self-actualizing behavior include the campaigning for better working conditions for one's coworkers, exposing financial irregularities, and opposing the manufacture of environmentally unfriendly products. The process of self-realization allows one to go beyond the limited context of increased productivity in the immediate job to encompass a wider concern for organizational policy and the role of the organization within a local and global community. Self-realization and individual maturation, which includes moral development, is a central theme that surfaces in the works of Argyris, Herzberg, and Trist, who recognized the relationship between employee development and organizational effectiveness.

In the 1960s and 1970s, there was an upsurge of writing challenging the classical management theories of bureaucracy, the role of autocratic leadership, and viewing employees as economic beings. Behavioral theories of management championed new organizational forms that were more human and facilitative of individual self-realization. Employees were recognized as individuals with social needs, thus linking interpersonal relationships to enhanced organizational performance. In the 1980s and 1990s, although the terms empowerment and self-fulfillment tended to be management parlance for self-realization, meaningfulness of work was deemed important and operationalized as part of one's personal value system. Autonomy in the workplace assumed a position of being a necessary condition for self-realization or personal growth. Today, personal and organizational values are being aligned with those values deemed important in the larger social environment, such as trust, integrity, and security. Ethical business practices are frequently measured against these parameters.

Impact on Business Ethics and Society

The discussion of self-realization, with its roots in humanistic psychology, suggests that the concept be examined at a deeper level to fully realize its role in informing business ethics and society. For one, humanistic psychology emphasizes the role of personal change in self-discovery and in the identifying of one's place in society. There is a continuing need to remind business and society of the dignity and worth of being human—something that gets lost in the day-to-day machinations of doing business. In a broader sense, the question of what it means to be human is quite relevant at a time of assessing the impacts of corporate megamergers and multinational and transnational companies, which can leave employees feeling disenfranchised, adding to the feelings of alienation. Maintaining self-realization as part of management and business practice keeps the focus on human capital as a resource that benefits business and society.

Second, the role of self-realization in workplace autonomy, creativity, and innovation suggests that managers understand that people are not only productive assets but also social beings. There is recognition that employee performance is related to employee achievement of personal effectiveness. The conditions that lead to peak performance and peak experience, associated with high-performing teams and effective leadership, are part of the operationalizing of self-realizing individuals.

Third, inherent in the work of self-realizing is the articulation of those virtues that comprise and guide one's ethical choices. Entering into an understanding of one's own potential reveals the larger network of relationships that has shaped one's worldview. For example, a person's religion, family, ethnic, and cultural affiliations influence and shape his or her attitudes to and behaviors comprising right and wrong. This is not an abstract reality; rather, it shapes the strategic choices that culminate in daily business operations. Since business does not function independent of its social environment, the actions that result from self-realized individuals inform the social contract.

Finally, self-realization is often linked to transformation. Transformation occurs when ordinary perspectives shift and the person gains new insights and self-understanding. Self-realization as a transformative process is about how a person can reach his or her fullest potential and how that potential translates as service to society. Today's social entrepreneurs and social venture partners are examples. Noted as part of the citizen sector movement committed to closing the business-social gap, social entrepreneurs and social venture partners bring entrepreneurial talent to the addressing of social problems. The need for a strong ethical fiber is cited as a necessary ingredient to the success of these ventures. Self-realization is about one's own authenticity and values and how those values influence one's daily ethical approach to business transactions. This is in contrast, and perhaps an antidote, to the excessive greed and egoism evident in many corporate organizations today.

—Michele Simms

See also Corporate Rights and Personhood; Ethics of Dialogue; Existentialism; Human Capital; Human Nature; Individualism; Kantian Ethics; Social Activists; Stewardship

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SELF-REGARDINGNESS

Self-regardingness concerns acts and virtues focused on benefiting the self and is a prominent component of a person's orientation to the world. Its strength in relation to other-regardingness has been disputed, with most accounts of human nature also attributing to us a natural concern for others, whereas some other accounts describe humanity as primarily or even exclusively egoistic (psychological egoism). Most scholars would agree, however, that self-regarding tendencies can and do coexist with other-regarding ones in various ways. Self-regardingness should not be confused with selfishness, because it does not necessarily exclude concern for others.

In modern ethics, the moral legitimacy of self-regardingness ranges from its celebration in ethical egoism to its complete denial in altruism. Self-regarding acts and virtues are frequently classified as nonmoral because many scholars understand morality as essentially other-regarding. Thus, self-regarding acts and virtues are viewed as morally inferior to their other-regarding counterparts. Other scholars, however, view self-regardingness as belonging in the moral realm, especially when considered in conjunction with other-regardingness. Self-regarding virtues like prudence and courage can serve the interests of both self and others, and actions can have multiple motives and effects, again serving both self and others. Apparent self-regarding obligations can also be moral obligations when fulfilling them also benefits others. Kant, in particular, claims that we have self-regarding duties based on proper self-respect and that these duties belong in the moral realm because they sustain our moral worth and provide the foundation for performing our other duties. Among the major ethical theories, utilitarianism very clearly incorporates self-regardingness, tempered with the overarching other-regardingness of the self counting as only one among others. It supports the pursuit of personal good until it conflicts with the good of the many.

In historical religious and philosophical accounts, self-regardingness and other-regardingness are intertwined. Whereas the ethics of most major religious traditions emphasize other-regardingness, there clearly is an element of self-regardingness in those traditions with their concern for a person's salvation and/or liberation. The New Testament, for example, makes a self-regarding appeal when it asks what a man will profit if he gains the whole world but loses his soul. It also accepts love of self, but asks that one also love one's neighbor; proper love of self involves love of neighbor. Ancient Greek philosophy perhaps even more clearly links self-regardingness and other-regardingness through the virtues. Achieving a person's highest good requires developing the virtues, not only the other-regarding virtues like justice, but also the seemingly self-regarding virtues like prudence. According to Aristotle, good people should be self-lovers because self-love commits them to the good of others. Whereas modern ethical theories tend to construe prudence narrowly in terms of self-regarding rationality or else discern morally inferior (self-regarding) and superior (other-regarding) versions, the Greeks did not distinguish between rational thinking and moral thinking. For them, self-regardingness was a key part of ethics.

—George D. Randels Jr.

See also Aristotle; Christian Ethics; Egoism; Kantian Ethics; Other-Regardingness; Prudence; Self-Interest; Utilitarianism; Virtue

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SELF-REGULATION

Self-regulation is the process that determines how one identifies, conceives, analyzes, plans, directs, manages, evaluates, and adjusts what one does. Self-regulation precedes the development of intrinsic motivation, which in turn energizes the appropriate use of reflective judgment. Ethical dilemmas are often personal and paradoxical problems that need to be solved using a decision-making process that frequently involves choosing between two or more viable options. Hence, self-regulation in the ethical decision-making process guides how one processes information that is involved in resolving difficult and complex problems that call into question our values, experiences, and prior learning.

Individuals can either be governed by external forces, such as laws and community norms, or through self-regulation, led by our own sense of values and ethical commitments. To balance between societal norms and personal commitments requires the ability to process well-conceived options and weigh the ethical consequences of various solutions. Failing to develop this skill portends risky consequences for individuals, businesses, and societies as effective leadership and survival requires that all in the community be able to evaluate novel and emerging ethical situations.

The premise of self-regulation in the ethical decision-making process is that one can learn and become better at the evaluation of ethical dilemmas and ways of resolving the problems surrounding the principles of conduct governing an individual or group. Acknowledging that learning to make effective ethical decisions is a developmental process and can be improved through the learning process opens the door to how people utilize self-systems and regulate the way they think about ethical problems. The developmental process allows improvement in the clarity of thinking about the problem, the heuristics about how one solves ethical problems, what values of conscience one will weigh as the problem is solved, and the continued belief that one is competent and consistent in the control of the decision and outcomes of these decisions. The assertion is that the more we develop our ethical decision-making process the more effective we are as leaders, whatever our positions in an organization.

An Ethical Framework Founded on Philosophical Precepts

Research about ethics has centered on the principles that guide our actions and how we evaluate our principles, rules, and goals. The world of ethics is about disciplining the mind through reason to critically apply principles and criteria to a problem to help us select the most ethical act. Ethicists have tried to determine whether we have a set of principles from which we live (deontology) or whether the goals of our lives determine our choices (teleology). This debate is subjugated by considering an ethical framework of four themes that deal with and attempt to balance the juxtaposition of autonomy and equality as well as rationality (following the rules) and sensibility (being flexible). In this way, we can attend to concerns such as hierarchy, compassion, community, and parity. By looking at the ethical issue in terms of balance among competing values, ethicists can acknowledge that we are not guided solely by a set of principles or goals; rather, ethical decision making is deeply informed by how we process information, learn, develop, and regulate ourselves in a world of interpersonal relationships.

Four key philosophies have captured competing notions of what is an ethical act: (a) deontology, which focuses on our duties; (b) utilitarianism (teleology), which focuses on the greatest good for the greatest number; (c) justice theories, which promote integrity-sustaining systems that attend to the needs of the least advantaged; and (d) virtue ethics, where an ethical act is one that is consistent with a good character and reputation. Faced with competing notions of what is an ethical act, in a postmodern, pluralistic community no one reason will be accepted by all as sufficient for action. Because our actions are shaped by the authorities we find persuasive, the traditions that are important, our base knowledge, and our experiences, we often develop a preference for thinking and making decisions based on one of these philosophical threads and call that preference our conscience.

The Role of Self-Regulation and Conscience

As the world evolves and more is known about development and learning, self-systems research begins to highlight the significance of other dynamics in the critical-thinking process. Self-awareness and self-management are often considered the keys to being moral, in that they can inform how individuals use their emotions and empathy as well as their intellect to gather information about how to act in community. Self-awareness includes being sensitive to our strengths and weaknesses—our gifts as well as our blind spots or proclivities for deception. As described by Daniel Goleman in his work on emotions and ethics, self-management involves virtues such as emotional self-control, transparency, and adaptability

Charles Shelton has researched the role of conscience in decisions. Conscience serves as our moral compass, guiding us to do what we ought to do and act how we ought to act. Implementing a conscientious decision involves continuous reflection, discipline, and effort, which are based on observations we make in our childhood and shaped by our environment until we develop a sense of ethical meaning that becomes our code of conduct when faced with ethical dilemmas. Sometimes, to rationalize their decisions based on original beliefs and values, individuals may resort to self-deception if they do not have a disciplined basis for learning new ways of behaving in a changing world, examining the actual issue at hand, honoring the stakeholders involved, and filtering their values in conflict.

Self-systems allow the individual to reassess the "oughts," "shoulds," and "have tos" that have formed absolutist messages that fail when complex issues do not fit into the rigid and demanding templates of viewing oneself and others, when ethical decisions have to be made. Yet conscience reveals personal integrity when we choose to stand up for ideals that can balance questions such as "Who am I as an actor in this process?" "Who is involved?" "What are the possible consequences for myself and others?" How we have developed and continue to develop a sense of conscience influences how we learn and how we regulate our information processing and ethical decision making. An ethically mature person will use both the rational considerations as well as the emotional implications for the key relationships before adopting any course of action. The belief that we can think about, control, and predict the outcomes of our decisions over a broad spectrum of circumstances involving a sense of conscience speaks of the degree to which self-efficacy is involved in the decision-making process.

The Role of Self-Regulation and Learning

Information processing involves how people learn and think through knowledge that is available to them. Common terms that are related to learning are *cognition* (how we think about and acquire knowledge: perceiving, encoding, storing, processing, decoding, and expressing our thinking), *affect* (the emotional interpretation of perceptions, values, and feelings), *metacognition* (the general heuristics that are developed that are overarching strategies for solving problems), and *conation* (the connection of knowledge, affect, and metacognition to behavior and action). It is well known that we are "hard-wired" to some extent by our nature and are born with certain propensities that help us analyze information. It is also clear that skills and abilities are nurtured and developed through the family and culture in which we are raised and that the combination of nature and nurture determines what things we value and how we make decisions based on these values. Enmeshed in the nature and nurture conversation is the degree to which we involve self-determination as well as how we learn and manage information, knowledge, and feelings. Learning is witnessed by a permanent change in behavior, demonstrating new ways of thinking.

Self-regulation is closely associated with the concept of volition and the ability to make choices about what we do through the intentional, deliberate, goal-oriented, and reflective process. Hence, self-regulatory learning processes require that we select and organize information and regulate what we think about, and they are also related to how we process and manage information and how we change our mind about issues given new information and a prescribed way of analyzing information based on a rational and reasonable procedure. The development of self-regulatory learning processes involves meaningful integration of new material and prior knowledge into the information processing networks. Addressing higher-order learning outcomes, such as ethical decisions, are often best formulated and regulated by asking questions such as "Who is the ethical actor?" "Who are the stakeholders?" "What is the context of the issue?" "What values are in conflict?" These questions serve as self-regulation strategies to offer systematic interventions to focus us on the critical issues of making complex decisions. Posing questions offers reflection points that help people consider the interface between rationality and empathy as well as the relationship of individuals within a community, as we seek to make ethical decisions.

The Role of Self-Regulation and Self-Efficacy

Self-efficacy is a related concept that explains how outcomes are dependent on capable and competent action, which creates a sense of causative power. First, self-efficacy influences the sense of personal agency as individuals determine whether or not they are the ones who might be responsible for making an ethical decision. Next, self-efficacy influences to what degree (if any) persons have control over the processing of information, control over making choices about their actions, and the courage to question preconceived ideas and values. As people question their belief systems, they are able to reestablish new values and communicate those new positions. Finally, self-efficacy influences a person's ability to sense that decisions and actions that lead to expected outcomes have a degree of predictability rather than being arbitrary (e.g., based on chance and lacking a pattern for repetition). The development of self-efficacy requires mastery of knowledge and skills. This learning becomes a self-referent belief system that influences one's ability to organize and execute thoughts and actions leading to the evaluation of anticipated consequences and expected outcomes.

Self-regulation and self-efficacy go hand in hand in that people must believe that they themselves can orchestrate knowledge, monitor information, mobilize skills, manage changing situations and emotions, acknowledge perceptions, evaluate alternative courses of action, establish goals and enlist motivation, and direct their actions as well as influence the actions of others who might be involved in the performance of the decision. Self-regulatory capabilities and meta-strategies for solving problems increase the sense of personal efficacy that transfers across different activities and when involved in different settings. Dale H. Schunk and Barry J. Zimmerman found that developmental theorists conceive of self-regulation in terms of incremental and progressive changes in learners that allow them to exert greater control over their thoughts, feelings, and actions.

When Self-Regulation Is Absent

People who lack self-regulation, a sense of conscience, and self-efficacy usually lack the ability to logically think about complex problems in a thorough and regimented fashion. It is difficult for those individuals to formulate a focused frame of reference about the issue at hand. Many skills needed for effective decisions are lacking. They cannot define a problem, develop notions of proof, or evaluate evidence. They are unable to research additional information or develop credible options. Because they lack the foundations for ethical decision making, they cannot use the four primary ethical theories to find a solution that effectively harmonizes competing values. They are unable to balance the rights and responsibilities that must be considered in the decision; explore the results/outcomes that will likely follow their decision (e.g., efficiency, quality); respond to issues of character, virtue, and reputation; and make a choice that will enhance the well-being of the system, organization, community, and global environment.

Recent industry indiscretions like the Enron fiasco highlight the inability of corporate officials to focus on solutions to problems that are well conceived, rational, and made with a conscious effort at understanding the long-term effects for all stakeholders. The inability to process well-conceived options and weigh the ethical consequences of various solutions portends risky consequences for individuals, businesses, and societies. This lack of careful deliberation illustrates the need for self-regulation in the ethical decision-making process. For example, issues concerning stem cell research and terrorism mandate decisions at many levels that involve moral parameters, economic welfare, and personal sacrifice—decisions that do not have familial or societal precedents.

Conclusion

Self-regulation and ethical decisions systematically implement a heuristically designed set of operating principles that allow one to work through a process of decision making. Hence, behavior is predicated on cognitive, metacognitive, affective, and conative mediators. Self-regulation develops from social sources and shifts to self-sources by acquired learning strategies and the ability to guide enactment based on one's own ability to reflect on information, reconstruct knowledge, and determine an outcome. Self-regulation also involves the process of acquiring beliefs and theories about one's own abilities and competencies and how one regulates strategies to solve problems.

Effective decision making requires one to (a) be attentive to the questions at hand, (b) sort out the issues, (c) weigh the values in conflict, (d)generate options to solve a problem, (e) monitor and evaluate the options based on considerations of conscience and self-efficacy, (f) act in a responsible manner correcting for bias and errors of judgment as decisions are confirmed, and (g) reevaluate and learn from decisions made and determine how those decisions should ultimately support the values and goals that hold the most meaning. Using self-regulatory processes in ethical decision making offers a unique approach to solving complex and sometimes paradoxical problems. Self-regulation requires individual accountability and participation in the analysis process based on one's belief systems and conscience.

Self-regulation builds one's self-efficacy so that patterns of analysis take into consideration a disciplined and rational process for considering all the dynamics involved in difficult ethical dilemmas. It allows for decisions to be nuanced by spiritual influences, societal mores, critical thinking about emerging diversities, and new ways of belonging. Self-regulation as it pertains to ethical decision making facilitates reflection of philosophical considerations. In the ethical decision-making process, it allows for adjustments as one learns to reject unconscious arbitrary decisions and embrace conscious and rational choices. Self-regulation encourages people to modify initial values and compare those values to those in question. Finally, self-regulation in ethical decision making allows one to evaluate competing ethical solutions using a broad array of complementary principles and goals. In the process, the ethical actor can move from being right to being responsible.

—Catharyn A. Baird and Kerry McCaig

See also Authenticity; Autonomy; Cognitive Moral Development; Cognitivism and Ethics; Decision-Making Models; Empathy; Empowerment; Ethical Decision Making; Ethics, Theories of; Ethics of Care; Moral Agency; Postmodernism; Self-Consciousness; Self-Deception; Self-Realization; Self-Respect; Values, Personal; Virtue; Virtue Ethics

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SELF-RESPECT

Self-respect is a sense of one's worth. Theorists disagree, however, about what kind of worth it is a sense of. According to various accounts, people with self-respect believe that they have full moral status, try to live up to certain ideals, and have a morally good character. Most agree that self-respect differs from self-esteem, though these concepts are related and are sometimes used interchangeably. Self-esteem and self-respect both involve evaluations of the self, but the latter is a specifically moral evaluation. The concept of self-respect has played a larger role in debates in moral and political philosophy than in debates in business ethics. When self-respect is appealed to in discussions of business ethics, it is usually in the service of an argument for workers' rights, especially the right to meaningful work.

Varieties of Self-Respect

Self-respect and its cognate concepts such as dignity, pride, magnanimity, and honor have figured prominently in the writings of philosophers from Aristotle in the 4th century BCE to John Rawls in the 20th century. Arguably, the most important source for contemporary discussions of self-respect is the work of the 18th-century philosopher Immanuel Kant. According to him, we should treat humanity, in our own person and in that of others, never merely as a means, but always as an end in itself. Many scholars interpret this as a claim that humanity should be *respected.* Since Kant's command applies as much to others as it does to oneself, it follows that for Kant, *self*-respect, in addition to the respect of others, is morally required.

The role of self-respect in historically important moral theories has led to discussions of its nature. According to one view, self-respect is a sense of moral worth that people are entitled to have just because they are people. People with self-respect think they have full moral status and are the moral equals of everyone else. Frequently, the nature of self-respect is elucidated by examples. A familiar one, which illustrates this sense of self-respect, involves an oppressed member of a minority group who is exploited by whites but does not complain. (The Uncle Tom figure is often cited.) Suppose this person passively accepts being fired from his or her job for a less-qualified white person and being given less than his or her fair share of social benefits by a white government. This person is not calculating; rather, the individual thinks that whites are entitled to treat him or her this way because of their superior status. It seems right to say that such a person lacks self-respect (perhaps through no fault of the person's own). The reason is that the person fails to appreciate his or her rights, or more generally, his or her full and equal moral status.

Some theorists have claimed that recognizing one's full and equal moral status is necessary but not sufficient for self-respect. According to them, people with self-respect must also try to live according to standards they set for themselves. Some acts are inconsistent with a person's having self-respect—not because they are intrinsically wrong but because they conflict with deeply held beliefs that person has about who he or she is and what kind of life he or she leads. Imagine a person for whom writing songs that protest private ownership of the means of production is so important that she identifies herself to friends and strangers as a Marxist songwriter. Suppose over time she gets fed up with being ignored by society and—not out of any material necessity—sells her melodies to giant corporations to be used as advertising jingles. There is nothing intrinsically wrong with this. But it seems beneath her—that is, incompatible with the self-respect of a Marxist songwriter. It is incompatible not with her status as a moral equal but with the standards she has set for herself.

The two types (or aspects) of self-respect we have considered so far have been called "recognitional," in virtue of the fact that their basis is the recognition of ourselves as certain kinds of individuals (e.g., as moral persons or as Marxist songwriters). Some theorists have claimed that there is also an "estimative" component to self-respect or a type of self-respect that is estimative. According to them, self-respect is based not only on "important" features of people, such as their being moral persons, but on "good" features of them, such as their being honest, trustworthy, or diligent. The basis of estimative self-respect is thus said to be morally praiseworthy character traits and conduct. For example, we might say of people with many praiseworthy qualities that they are entitled to have more estimative self-respect than people with few praiseworthy qualities. People with no praiseworthy qualities are entitled to no estimative self-respect, whether or not those people actually think highly of themselves.

Self-Respect and Self-Esteem

The concept of self has been described not only in terms of self-respect but also in terms of self-esteem. Philosophers usually pursue the former route and psychologists the latter. Thus, the literature on self-esteem is more empirical, and less conceptual and normative, than the literature on self-respect.

However, self-respect and self-esteem are related concepts, as a consideration of psychologists' accounts of self-esteem reveals. According to them, self-esteem is the degree to which a person approves or disapproves of himself. Persons with high self-esteem think of themselves as, on one hand, significant and worthy, and on the other, competent and successful. Whether one thinks of oneself this way is thought to depend both on, as William James said, the ratio of one's successes to one's pretensions and, as Charles Cooley said, others' appraisals of oneself. The domains that have been found to be important for self-esteem include physical appearance, athleticism, intelligence, social acceptance, and parental support.

Like self-respect, then, self-esteem is a sense of worth that is manifested in a person's attitudes, beliefs, and dispositions. But there are differences between them. One is in the nature of the worth at issue. To have self-respect is to value oneself, whereas to have self-esteem is to think highly of oneself.

A second, and related, difference concerns the source of this worth. The bases of self-respect are *necessarily* morally significant features of the person and may or may not be appraisable (i.e., good or bad), whereas the bases of self-esteem are *necessarily* appraisable features of the person and may or may not be morally significant. The fact that one is a moral person or has a certain identity is morally significant and, therefore, is a source of certain kinds of self-respect. But there is nothing good or bad about being a person or having a certain identity. The fact that one is, for example, honest *is* appraisable; but what qualifies this trait as a basis of self-respect is its moral significance. Now contrast this with self-esteem. In addition to being a basis of self-respect, being honest can be a source of self-esteem because it is an appraisable trait. However, one might have high self-esteem by virtue of being good-looking, athletic, or socially accepted. These traits are appraisable, but there is nothing morally significant about them; that is, a person who is good-looking is not for this reason morally good.

The Normative Significance of Self-Respect

Compared with the amount of discussion about the nature of self-respect, there has been relatively little discussion of its importance. What discussion there has been has focused on the first kind of self-respect, according to which having self-respect entails thinking of oneself as having full and equal moral status.

Kant said conceiving of oneself this way is a rational requirement, but few theorists accept this now. Nonetheless, many are convinced that self-respect is highly morally important. Some theorists claim that the appreciation of things that are intrinsically good is itself intrinsically good. Self-respect qualifies as intrinsically good in this view because it is the appreciation of the intrinsic value of one's personhood. Others claim that self-respect promotes moral behavior, as people who have a proper appreciation of their rights are less likely to tolerate abuses of them by others. Still others claim that self-respect has instrumental value. According to them, self-respect is necessary to pursue one's life plans with zeal.

More work remains to be done on the importance of self-respect, especially as it compares with other moral values. This is important for determining the extent to which self-respect should be promoted in society. We might think of self-respect, as some do, as an individual moral requirement. But whether people have self-respect is determined in part by the nature of the social and political institutions as well as the business organizations in which they participate.

Some political theorists—including many on the "left"—embrace self-respect as a distributive ideal. They endorse policies that promote this value, even at the expense of other values. Some support giving homosexuals the right to marry, on the grounds that being denied this right makes it hard for homosexuals to conceive of themselves as moral equals. Others justify social welfare payments by appealing to self-respect, on the grounds that lacking the resources to pursue one's plan of life is incompatible with living according to standards one sets for oneself. These policies are often opposed by those on the political "right," for a variety of reasons.

Theorists' conclusions about the importance of self-respect have been put to use by activists. The struggles of oppressed groups, including women, blacks, and homosexuals, have been framed in terms of self-respect. It was argued, for example, that denying voting rights to women (or blacks) made it difficult for them to conceive of themselves as having the same moral status as men (or whites).

The concept of self-respect has been given less attention by business ethicists than by political philosophers. When it is discussed by business ethicists, it is usually in the context of an examination of workers' welfare. Self-respect has been connected to the availability of work, to meaningful work, and to a living wage. The argument in each case is roughly the same. It begins with the claim that contributing to society is a source of self-respect and that the way many people contribute to society is through work. Thus, if people lack work, they may feel that they are a burden on society, and their self-respect may be damaged. The same is true, it has been argued, if people do meaningless work or fail to earn a living wage. In the former case, although they have work, they do not have work that is stimulating, complex, and creative; in short, they do not have work that seems worth doing. In the latter case, the low level of compensation they receive for their work communicates to them that their work is not valuable. It will be difficult for them to believe that they are making a meaningful contribution to society in either case.

There is a great deal of empirical evidence, beginning with Arthur Kornhauser's seminal work on the mental health of industrial workers, that people's self-*esteem* is adversely affected by meaningless work and, to a lesser extent, low pay. Given the similarities between self-respect and self-esteem, it would not be unreasonable to conclude that people's self-*respect* is adversely affected by these factors, but more work needs to be done to establish this result.

Self-respect-based arguments for meaningful work and living wage provisions are usually met with objections that these measures are too costly and that they interfere with the rights of owners and workers to contract freely. Whether these objections succeed depends on the importance of self-respect compared with other values—a topic that, along with the nature of self-respect, deserves further consideration.

—Jeffrey Moriarty

See also Kant, Immanuel; Living Wage; Meaningful Work; Rawls, John; Self-Regardingness; Shame; Working Conditions

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Servant Leadership

The concept of servant leadership was developed by Robert Greenleaf, who drew from his 40 years directing management research for AT&T to create a business and leadership consulting practice centered on his ideas about leaders as servants. After retiring from AT&T in 1964, Greenleaf launched his second career with the publication of the 1970 essay, "The Servant as Leader," in which he acknowledged Herman Hesse's *Journey to the East* with providing the key insight for his theory of servant leadership. In this story, a group of men embark on a pilgrimage to the East, accompanied by their servant, the spiritual and charismatic character Leo. Deep into the journey, Leo mysteriously disappears and the men are so confused and disorganized without him that they fail to complete their journey. Years later, it is discovered that Leo was actually the head of the organization that had sponsored the pilgrimage.

Greenleaf's approach to leadership could be described more as a spirituality of leadership than a theory of leadership, anchored in the human quest for meaning, wisdom, and community rather than in a critical analysis of theory or empirical data. In the 1970 article, which became the first chapter of his book on servant leadership, Greenleaf begins with the assertion that prophetic vision and voices are always present in the world but that people do not always listen to their wisdom. Greenleaf saw in the social upheavals of the late 20th century the seeds of a new moral vision of power and authority that would reshape traditional notions of leadership in organizations. In this social context, Greenleaf reflects the widespread emergence of leadership theory as a discursive domain of people and relationships distinctly different from management theory focused on operations, authority, roles, and tasks.

Greenleaf's framework of leadership as service shows similarities to the larger body of developing leadership literature, for example, the charismatic and visionary "new leadership" theories of Burns, Bryman, Kouzes, and Posner or the charismatic theories of Bennis, Conger, and Kanungo. Greenleaf shares with his contemporaries an emphasis on the dynamic, relational aspects of leadership with special attention to the character of the leader and the leader's relationship to followers. His emphasis on the character of the leader is viewed essentially as the desire and choice to serve; the defining moment for the servant leader is in valuing the good of others through service over a personal drive for power or gain. Servant leadership views people and human communities as the ultimate end (telos) of leadership rather than as the means to an external organizational or political end.

With the formation of his Center for Applied Ethics, now known as the Greenleaf Center, a second generation of servant leadership writers emerged from its seminars, lectures, and publications. Hunter, Autry, and Blanchard, for example, apply servant leadership to business, government, politics, churches, and family life by distinguishing leadership from management and emphasizing the spirituality of work and the character of the leader in influencing and inspiring people for the common good. Covey, Block, Senge, De Pree, Wheatley, and Blanchard view servant leadership as compatible with a more holistic approach to the distributed power dynamics of a collaborative organizational model. Servant leadership is seen by some executives and managers as a means of personal leadership and character development. It has also been applied in some settings as an organizing ethos for enabling people to reach their full potential, thus helping them achieve optimal performance. Phil Jackson, for example, applied a servant leadership philosophy as head coach of the Los Angeles Lakers to build a strong, high-performance team. Herb Kelleher adopted a servant leadership organizational development strategy as CEO of Southwest Airlines to build a culture of shared vision and customer-service-focused community among Southwest employees. This approach is especially attuned to the social mission sensibilities of service and nonprofit organizations but may be less suited to the organizational culture of public corporations with profit margins and shareholder expectations to consider.

Servant leadership is sometimes described as a quiet global revolution taking place in the modern workplace, wherein managers relate to workers as persons rather than as tools or cogs in the production process. With its focus on workers as persons, servant leaders are differentiated from authoritarian, hierarchical leaders by skills and practices of empowerment. By devoting themselves to serving the needs of their individual followers, servant leaders build organizational value and quality through people. Eight central qualities of the servant leader identified by Larry Spears, currently the CEO of the Greenleaf Center, reflect a marked departure from traditional managerial leadership literature in their relational, pastoral tone: listening, empathy, healing, awareness, conceptualization, foresight, stewardship, and commitment to the growth of people.

Critiques of servant leadership emphasize its failure to focus on the goals of an organization because of its emphasis on the people of an organization as ends in themselves. Whereas this critique would perhaps constitute a Kantian approbation of servant leadership, it reflects the commonly held utilitarian approach to business leadership. In this view, servant leadership is acceptable as a practice to the extent that it motivates employees to fulfill organizational goals, but it does not offer a sufficiently robust theory of leadership for the performance challenges of a highly competitive business environment. Servant leadership practitioners respond that the Fortune 500 companies applying the servant leadership philosophy outperform their competitors with more productive, loyal, and purpose-driven employees. Servant leadership may also be seen as narrowly sectarian in diverse organizations consisting of individuals who may be uncomfortable with the use of Scripture and Christian exempla by some who apply it in a religious context. Despite its limitations, servant leadership remains a popular leadership model among American business leaders.

—Lindsay J. Thompson

See also Leadership

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Sexual Harassment

Sexual harassment is unwanted verbal or physical conduct of a sexual nature. General Recommendation 19 to the United Nations Convention on the Elimination of All Forms of Discrimination Against Women defines sexual harassment to include unwelcome physical contact and advances, sexual demands, the showing of pornography, and sexually colored remarks. Most reported victims of sexual harassment are women. Sexual harassment is illegal in a growing number of countries, many of which recognize that both men and women can be harassers or victims. In the United States, sexual harassment is a form of gender discrimination prohibited by Title VII of the Civil Rights Act of 1964. Title VII holds both harassers and their employers legally responsible and liable for damages and seeks to protect employees who report sexual harassment from retaliation.

Sexual harassment is both widespread and underreported. Surveys indicated that nearly half of working women in the United States and Europe have experienced sexual harassment. More than 90% of Fortune 500 companies have received sexual harassment complaints, and more than a third of Fortune 500 companies have been sued for sexual harassment. Meanwhile, estimates place the reporting rate for sexual harassment at 15% or lower. Reasons for failing to report sexual harassment include embarrassment and shame, a belief that nothing will be done, and fears of hurting one's career or even losing one's job. The U.S. Equal Employment Opportunity Commission (EEOC) received 12,679 charges of sexual harassment in Fiscal Year 2005, with 14.3% filed by men. Complaints peaked in Fiscal Year 1997, when 15,889 cases were filed with the EEOC.

Both victims and employers suffer harm from sexual harassment. Victims have reported resulting anxiety, depression, and sleep and appetite disturbances. Victims may also lose wages when trying to avoid harassment by taking sick leave or unpaid leave, by transferring to new jobs, or by quitting. Reporting sexual harassment can make matters worse if the harasser retaliates. Since there may be few or no witnesses to the harassment, attention may focus on the victim's credibility, opening the victim's life to intense public scrutiny. Companies where sexual harassment occurs suffer consequences such as lower team productivity, a "poisoned" work atmosphere, higher job turnover, increased sick leave, court costs, and damaged company reputation. The average jury award in a U.S. harassment case is $1 million.

Sexual harassment generates both ethical and legal debates. Confusion abounds over what constitutes safe sexual conduct at work. The power dynamics in sexual harassment are increasingly recognized, as are the synergistic effects of gender bias with racism and other forms of discrimination.

U.S. Legal History

Title VII

Title VII of the Civil Rights Act of 1964 was intended mainly to protect disadvantaged minorities from discrimination based on race, religion, color, or national origin. Gender was added by opponents of the law who had wanted to kill the legislation but failed. As a result, women, a majority group, gained protection from discrimination under Title VII.

Sexual harassment became a specific violation of federal law in 1986, when the U.S. Supreme Court ruled in *Meritor Savings Bank v. Vinson* that a hostile environment created through sexual harassment violates Title VII. The Court said victims were entitled to back pay, damages for emotional distress, and attorney's fees.

EEOC Regulations

In 1990, U.S. EEOC defined unwanted sexual conduct in the workplace as harassment when (1) the employee's response to the conduct affects their employment; (2) the conduct unreasonably interferes with the employee's work performance; or (3) the conduct creates an intimidating, hostile, or offensive work environment.

According to the EEOC, harassers and victims can be of either gender, and a harasser can have the same gender as the victim. Harassers could be not only the victim's supervisor but also other supervisors, coworkers, nonemployees, and agents of the victim's employer. Illegal sexual harassment can occur even if the victim suffers no job loss or economic injury and even if the victim isn't the one being harassed. The EEOC guidelines recognize two types of sexual harassment: quid pro quo and hostile workplace environment.

Quid Pro Quo

In quid pro quo sexual harassment, a job benefit is tied to an employee's acceptance of unwanted sexual behavior. For example, a supervisor may demand sexual favors in exchange for a promotion or threaten to fire an employee for resisting sexual advances. Only supervisors can engage in quid pro quo harassment because only they have, or can reasonably be perceived to have, the power to give or withhold job benefits. A supervisor's sexual advances may be shown to be unwanted even if the employee eventually submits to them. Employers are generally held liable for quid pro quo harassment by supervisors.

Hostile Workplace Environment

Hostile workplace environment harassment occurs when an employee is regularly subjected to sexually offensive speech, behavior, or materials. An ongoing pattern of offensive conduct is generally necessary to show that a hostile workplace environment exists.

In the 1993 case of *Harris v. Forklift Systems,* U.S. Supreme Court Justice Sandra Day O'Connor developed a two-fold test for hostile workplace environment harassment: (1) Is the conduct so severe that a reasonable person would find the environment objectively threatening or abusive? and (2) Does the employee perceive the environment as threatening or abusive? Employers are liable in hostile workplace environment cases unless they can show that they took reasonable measures to prevent or correct sexual harassment or that the employee failed to take advantage of these measures.

Several courts have used a reasonable woman standard for determining whether a hostile workplace environment exists, especially in the less obvious cases where men and women tend to disagree. The reasonable woman standard has been criticized as unfair to men, and most courts have dropped it in favor of a consistent use of the reasonable person standard.

Federal Court Interpretations

Federal court rulings in the 1990s and early 2000s interpreted a number of aspects of Title VII. For example, the 11th Circuit Court of Appeals ruled in *Farley v. American Cast Iron Pipe Co.* that an employer with an effective policy against sexual harassment cannot be held liable for creating a hostile workplace environment unless the employee reports the harassment in accordance with the policy and the employer fails to provide a remedy. The court said that even if the harassment is pervasive, the employer will not be presumed to know about it. Employees lost several cases in federal court because they had failed to use the avenues their employers provided to remedy sexual harassment. In *Slayton v. Ohio Dept. of Youth Services,* the employer was found liable for harassment by nonemployees because employees had encouraged it.

State Laws

All states have some form of sexual harassment legislation. These laws typically resemble federal law but expand protection to employees of smaller firms. State laws vary considerably in the damages and remedies provided for a successful sexual harassment claim. More than a dozen states require or encourage employers to train their supervisors and managers in harassment prevention. In California, supervisors may be held personally liable for harm they cause by sexually harassing employees.

International Perspective

A number of international conventions, reports, and agreements either directly address sexual harassment or include material relevant to it. For example, the United Nations Declaration on the Elimination of Violence Against Women, adopted by the General Assembly in 1993, explicitly includes sexual harassment and intimidation in the workplace. Some international documents treat sexual harassment as a form of violence against women or as a barrier to development. Other documents affirm rights that sexual harassment violates, such as the right to dignity at work.

Sexual harassment is illegal in a growing number of nations. By 1992, according to an International Labour Organization survey, Australia, Canada, France, New Zealand, Spain, Sweden, and the United States had laws on sexual harassment. Other industrialized nations treated sexual harassment under tort law, criminal law, or wrongful dismissal. Members of the European Union were required to have laws against sexual harassment by October of 2005. Also in 2005, the Chinese law protecting women was amended to bar sexual discrimination against women and to empower women to lodge complaints with appropriate organizations. Japan's Equal Employment Opportunity Law includes sexual harassment, and India's Supreme Court has expanded the definition of sexual harassment beyond physical contact.

National laws that recognize sexual harassment generally define it in terms of quid pro quo and hostile workplace environment. Penalties for sexual harassment vary considerably from one nation to another.

Preventing Sexual Harassment

Many companies have developed programs in response to court rulings holding employers responsible for both preventing and remedying sexual harassment. Typically, these programs include the following:

- A strong, written policy prohibiting sexual harassment
- A definition of sexual harassment with specific examples of forbidden behaviors
- Procedures for reporting, investigating, and remedying sexual harassment
- A nonretaliation policy
- Education and/or training, including regular reinforcement of the employees' right to a harassment-free workplace

Experts recommend that training programs not only give information about sexual harassment laws and the company's policies and procedures but also raise awareness and offer strategies for intervention. Some experts emphasize the importance of a company's culture—the informal social system that sets norms in an organization and lets people know "how things are really done around here." Company culture has been shown to influence the effectiveness of formal ethics training programs.

Ongoing Debates

Discussions of sexual harassment from an ethical perspective tend to emphasize the abuse of power rather than the sexual element. At the same time, ethical debates have continued over issues such as the following:

- Do victims have an ethical obligation to resist sexual harassment?
- How is sexual harassment best understood?
- How can organizations and individuals best learn to recognize and eliminate sexual harassment?

Not only sexual harassment itself but also the laws surrounding it have become topics for debate. For example, some scholars see a conflict between sexual harassment law and freedom of speech. Other critics ask whether sexual harassment laws enshrine an outdated view of women or represent overkill in an area long covered by common law and tort law.

—David P. Schmidt

See also Dignity; Diversity in the Workplace; Employee Rights Movement; Employment Discrimination; Equal Employment Opportunity; Hostile Work Environment; Reasonable Person Standard; Women in the Workplace

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Shame

Shame is an important mechanism in much of the world for discouraging unethical behavior. Shame may be defined as public censure and disapproval, whereas honor, its opposite, is public affirmation. Shame and honor may be endowed by one's inherited circumstances or family station, but they also serve as negative and positive reinforcements of behavior. Shame takes many forms, including embarrassment, humiliation, loss of face, ridicule, punishment, expulsion from the family, and exile.

Relationship-Oriented Cultures

Shame-based regulation of behavior is most prevalent in relationship-oriented cultures, which rely heavily on personal supervision. This is because the experience of shame, in the sense intended here, requires that other people take note of one's behavior. A relationship orientation is typically found in non-Western countries.

Direct supervision plays a central role in relationship-oriented cultures because authority resides in persons rather than in rules. Rules may be laid down, but they receive their legitimacy from the persons who lay them down, such as parents, teachers, husbands, bosses, elders, or political leaders. These are also high-context cultures, in the sense that behavior norms need not be spelled out explicitly but are learned from the context of everyday life. Activities that superiors allow to proceed without immediate censure are assumed to be permissible.

Relationship-based behavior regulation can be seen in countless everyday business contexts. For example, department stores in relationship-based countries typically ask customers to pay a central cashier rather than the sales person who showed them the merchandise. The customer then brings a receipt to the sales person to pick up the items purchased. The reason for the central cashier is that direct and constant supervision of persons who handle money is viewed as necessary, and it is easier to supervise one person than many.

Loss of face is a particularly important mechanism for enforcing behavior norms, as for instance in many Asian cultures. Exposure of bribery in the news media, for example, may lead to loss of face that is highly damaging to one's personal and professional life even if there are no legal consequences. Loss of face is a powerful force, however, that must be managed with care in everyday business situations. For example, a boss who criticizes employees in front of their coworkers can cause serious loss of face that could lead to poor morale or resignations. It can also result in loss of face for the boss, and consequent erosion of authority, since the boss exhibited poor management skills. Generally, a boss should not cause employees to lose face unless they have already done so by demonstrating gross incompetence in front of their peers or unless their conduct is truly immoral rather than merely inept.

An Ethic of Care

A relationship orientation tends to be associated with an ethic of care, which in turn stems from a conception of human nature defined by relatedness to others. In Confucian cultures, for example, one scarcely exists apart from the family, and in many African cultures, the village, not the individual, is the unit of human existence. As a result, one's first concern is for those with whom one is connected—the extended family, friends, village, tribe, or ethnic group—since this is in essence concern for oneself. Cronyism and nepotism, frowned on in the Western business world, may represent high moral virtue.

Shame-based cultures do not reject justice but view it as a derivative value when it applies. Justice is important to the extent that it is grounded in the fact that caring for significant others is tantamount to caring for oneself. Shame is the primary form of social regulation because it results from a failure to care.

Shame-based cultures may be susceptible to corruption in the form of bribery and kickbacks, since personal relationships are necessary to getting things done. There is a constant temptation to create a relationship quickly by exchanging favors rather than by going through the long process of building mutual trust.

Shame Versus Guilt

Shame is best understood when contrasted with guilt, which is a private rather than a public phenomenon. It is a feeling of regret for doing something one believes to be wrong. (This should be distinguished from a legal sense of guilt as being responsible for an act.) One can feel guilty for an act that is known to no one else, but one cannot be shamed unless others are aware of the act.

Guilt provides a basis for behavioral regulation in rule-oriented cultures, including many Western cultures, much as shame does in relationship-oriented cultures. In rule-oriented cultures, the rules are seen as having authority in their own right. Behavior norms are explicitly spelled out in laws, government regulations, company policies, and instructions. Activities that are not explicitly prohibited by rules are assumed to be permissible.

Guilt-based regulation relies on the fact that people learn to feel guilty for breaking the rules. It, therefore, requires only intermittent supervision, along with the threat of punishment for violating the rules. The central role of guilt and relief from guilt is reflected in the Jewish and Christian faiths, which profoundly influenced the West.

This is not to deny that shame and honor have historically played a role in Western countries. Miscreants were once placed in stocks and pillories for public ridicule, and gentlemen resorted to duels to preserve their honor. In modern times, however, shame and honor tend to be secondary to guilt in importance, as witnessed by the fact that they seem a bit quaint or old-fashioned.

The example of the department store illustrates the difference between guilt-based and shame-based enforcement. In rule-based cultures, customers often pay the sales clerk directly, and all sales persons have access to cash registers. Guilt-based internal regulation along with accounting controls and fear of punishment if caught are viewed as sufficient deterrence against theft.

If a tendency toward bribery is a weakness of shame-based cultures, guilt-based cultures are susceptible to corruption in the form of cheating—perhaps by understating taxable income or altering the books to obtain a more favorable accounting statement. This is due to the reliance on guilt and relative lack of supervision, making the society vulnerable to a minority who are not deterred by guilt. Recent business scandals in the United States, and to some extent in Europe, illustrate this possibility.

Rule-based cultures are associated with an ethic of justice and equality, which again stems from a particular conception of human nature. Human beings are regarded as rational individuals who are ultimately a law unto themselves and, therefore, equal. Since no one has authority over others except when it is sanctioned by rules, social cohesion requires that one accept the rules voluntarily because they are self-evident and logical. This gives rise to an ethic based on equality, fairness, and logic, which is elaborated in Western ethical theories. Rule-based cultures do not reject duties to family and friends but view them as derivative values when they apply. Guilt is the primary form of regulation because it results from a violation of rules one recognizes as inherently valid.

The distinction between shame-based and guilt-based cultures is very general and glosses over many differences within each category, but it is nonetheless valuable for understanding ethics across cultures.

—John Hooker

See also Rationality and Ethics; Relativism, Cultural; Side Payments

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SHAREHOLDER ACTIVISM

Shareholder activism can be defined as the use of shareholder prerogatives, including but not limited to the filing of shareholder resolutions, to attempt to effect some policy change by a corporation and its managers. Shareholder activism encompasses a variety of techniques that holders of common stock in a public corporation use to affect the behavior of that corporation's managers. Shareholder activism can include the voting of shares for or against particular policy initiatives submitted by managers or other shareholders. The more typical use of the term refers to using pressure techniques—like the filing of shareholder resolutions—that seek to influence corporate and managerial behavior. In contrast to the screening out of bad corporate actors envisioned in "socially responsible" or "ethical" investing, shareholder activism relies instead on maintaining ownership positions in corporations to effect social change. Because shareholders possess voting power, they are often able to influence corporate behavior in ways that other stakeholders cannot. Shareholder activism can focus on issues related to corporate governance, social issues, or some combination thereof.

The History of Shareholder Activism

Shareholder activism has a long history in the United States, where SEC rules allow for shareholder direct involvement in corporate governance processes. In a number of other countries—like the United Kingdom, France, and Japan—shareholder activism has also occurred, albeit less frequently than in the United States. The primary vehicle for shareholder activism in the United States has been the shareholder resolution.

Richard Marens has argued that the history of shareholder activism in the United States dates back to the 1940s and 1950s, when corporate "gadflies," such as the Gilbert brothers, pioneered the use of the shareholder resolution as a means of pressing corporate managers to undertake some sort of policy change. During this period of time, shareholder activism was primarily focused on increasing the transparency of corporate decision making and improving the quality of corporate governance, although there were a number of shareholder resolutions focusing on social issues such as the inclusion of women and members of minority groups on corporate boards of directors.

Later work in shareholder activism addressed social concerns more frequently. In 1971, the Episcopal Church filed a social-issue shareholder resolution with General Motors asking that corporation to leave South Africa, which was ruled by a regime that practiced the racial segregation system called apartheid. Under apartheid, black South Africans could not vote or own businesses, mixed race individuals could own businesses but not vote, and all nonwhites were forced to live in certain areas of the country. The Episcopal Church's action marked the beginnings of religiously motivated shareholder activism, and the Interfaith Center on Corporate Responsibility was founded in the early 1970s to bring together religious organizations interested in using the shareholder resolution as a means of advocating social change. Early religious campaigns focused on issues like apartheid in South Africa, infant formula, and fair-lending practices by banks. In recent years, religious campaigns have addressed concerns like sustainability, environmental justice, global warming, and genetically modified organisms. More recently, socially responsible mutual funds, state and local pension funds, and activist groups like People for the Ethical Treatment of Animals have all used shareholder resolutions to seek policy changes from corporations.

Shareholder activism often focuses on issues related to corporate governance and strategy, as shareholders unhappy with financial performance use their ownership prerogatives to try to force corporations to change how they make decisions or to undertake some sort of strategic change, like an asset divestiture or a stock buyback. In the past 25 years, individuals such as T. Boone Pickens, Kirk Kerkorian, and Carl Icahn have bought significant positions in underperforming companies and sought to pressure company managements to increase stock prices. Sometimes these strategies are successful at causing strategic changes (Carl Icahn causing Mylan Laboratories not to purchase another pharmaceutical company in 2004) and sometimes not (Carl Icahn and Time Warner ca. 2005).

In many other cases, shareholder activism focuses on social concerns, as activists attempt to change corporate behavior in areas like employment practices, environmental responsibility, or community relations. Both broad types of shareholder activism can be observed throughout its history.

The Mechanics of Shareholder Resolutions in the United States

The rules regarding shareholder resolutions vary from country to country; in the United States, these are administered by the SEC. Subject to various form and content restrictions administered by the SEC, a stockholder (or group of stockholders) who has owned more than $2,000 of a corporation's stock for at least a year can file a 500-word shareholder resolution asking the corporation to undertake some action. Most resolutions are phrased in terms of requests that the board of directors of the company do something, whether to conduct a study, report to shareholders, adopt a policy, or some combination thereof. When a corporation receives a resolution, it has a number of options:

- The corporation can ask the SEC for a "no-action letter" indicating that the SEC will not recommend enforcement action if the company omits the resolutions. If the SEC grants the no-action letter, the company will usually omit the resolution from its proxy statement. In the absence of a no-action letter, omitting the resolution would put the company in jeopardy of regulatory enforcement, and companies tend not to omit resolutions in such cases.
- If the company chooses not to seek or does not receive a no-action letter from the SEC, it may seek to engage in dialogue with the proponents of the resolution to determine if there is some possibility of agreement that would allow the resolution to be withdrawn. In many cases, the company will agree to undertake the actions sufficient enough to the proponents so that the resolution is withdrawn.
- If the company cannot endorse the resolution and is unable to come to an agreement with the resolution's proponents (or chooses not to engage in dialogue), the resolution is printed on the company's proxy statement, which is sent to all shareholders in advance of the company's annual meeting. Because in the vast majority of cases very few shareholders attend company annual meetings, the proxy statement is the means by which shareholders vote for board members and auditors, in addition to voting on resolutions submitted by shareholders.

A resolution that goes to a vote by shareholders in the United States must receive an increasing percentage of affirmative votes cast by shareholders to be resubmitted to the same company in subsequent years—3% in the first year of submission, 6% in the second year, and 10% for the third and any following years. Receiving increasing affirmative vote percentages helps place further pressure on corporate boards and managers to respond to the issues raised in the shareholder resolution. Although most shareholder resolutions are advisory rather than binding on managers, a resolution that receives a significant percentage of votes cast will frequently bring about changes in corporate policies and practices.

It should also be noted that a less common method of shareholder activism focuses on elections for corporate boards of directors. When a company is performing poorly, shareholders may seek to influence the corporation by withholding votes from one or more directors to demonstrate their disapproval of its performance.

Shareholder Activism in Other Countries

In countries other than the United States, it is significantly harder to submit a shareholder resolution as a means of engaging in shareholder activism. The United Kingdom, for example, requires that a minimum of 100 shareholders sign on to a shareholder resolution before it can be considered at an annual meeting. The ease of submitting shareholder resolutions or engaging in other communication with corporate managers, therefore, affects the extent to which shareholder activism will occur in other countries.

In recent years, however, shareholder activists from different countries have started to work together to file shareholder resolutions with companies outside the United States. This tactic is particularly popular when a particular social issue is cross-national in nature. As shareholder activism spreads to and expands outside the United States, it is likely that such cooperation will increase. It is also likely that increased demands for corporate transparency and shareholder engagement will have the same effect.

The Effects of Shareholder Activism

Shareholder activism can be effective in bringing about changes in corporate behavior, although the nature of such effects would depend on the issues and companies involved. With regard to corporate governance issues, for example, shareholder activism has been effective at bringing about changes like moving from a staggered board to the annual election of directors. When companies are not performing well, shareholder resolutions focusing on the quality of corporate governance often receive majorities of votes cast, causing corporations to adopt the policy change requested. Shareholder activism focused on changes in corporate governance has therefore made a significant impact in recent years, at least in the United States.

In contrast, the vast majority of social issue shareholder resolutions fail to get even 10% support from shareholders. If this is the case, then why would companies engage in dialogue with such shareholders? There are two reasons. The first relates to the "embarrassment factor." Senior managers prefer not to have the social records of the companies they work for publicly questioned. Printing a dissident point of view in a company proxy statement is often embarrassing and raises the profile of a public issue as it relates to the company, and corporate managers may find it advantageous to try to have such shareholder resolutions withdrawn. The second relates to the value that many corporate managers find when they engage in dialogue with their critics. The Gap, for example, started working in 2003 with a public reporting working group convened by the company and composed of its shareholder-critics; the working group has helped the company develop and improve its social responsibility reports over time. Similarly, large companies like General Motors and Ford are almost continually in contact with shareholder activists; here, the idea is that managerial dialogue with those stakeholders who want you to improve your social performance will help you do so.

The popular perception of shareholder activists is that they are gadflies, sincere but annoying individuals engaged in some quixotic struggle against corporations. Sometimes the gadfly moniker is awarded affectionately but more often derisively. Contemporary portrayals of shareholder activists, particularly members and representatives of religious institutions, tend to portray them as either lonely outsiders railing against corporate policies and practices at annual meetings while being ignored or as dangerously deluded (but sincere) folks who don't understand modern capitalism and whose policies would bring about its ruin if adopted. The reality is more complex. Through research, issue definition, and building coalitions outside of their organizations and relationships with corporations, shareholder activists have been able to bring about social change. But most such social change comes not from the shareholder resolutions themselves, which (with a few exceptions, like some corporate governance resolutions) tend to be voted down overwhelmingly by shareholders, but rather from ongoing relationships and discussions with corporate managers. The shareholder resolution, thus, is not an end in itself but rather a tool to bring a company into a discussion of the issues raised in the resolution and then for the company to take some sort of action that starts to address the shareholder activists' concerns. The effects of shareholder activism, therefore, go beyond the filing of a shareholder resolution that is voted on at a company's annual meeting. The long-term relationships and partnership between corporate managers and shareholder activists are what bring about more substantive change in corporate behavior.

Whereas, in the main, shareholder activists have played an important role in changing corporate behaviors and stakeholder expectations, there are real limits to the effectiveness of such strategies. Roberta Romano has noted that shareholder activists (particularly ones focusing on social issues) do not seem to be able to affect the financial performances of targeted firms. Jon Entine has taken a different tack, suggesting that what such activists call "socially responsible" may not be. In this line of analysis, shareholder activists are viewed as promoters of simplistic ideas of corporate right or wrong or particular political agendas that are out of place in a profit-making enterprise. Entine's analysis points out that shareholder activists themselves are subject to critical and ethical analysis. In other analyses, it is noted that shareholder activists generally do not control critical resources and, thus often, must rely on moral suasion—which has practical limits. In some cases—like shareholder activists asking military contractors to adopt ethical criteria for their core business activities—shareholder activism has thus far failed to create corporate changes or popular support. In this instance, the shareholder activist remains the proverbial gadfly who seeks to promote a position outside of the mainstream because what the shareholder activist is asking for—the adoption of a policy that would have significant financial implications in terms of lost sales—is costly to firms receiving such shareholder resolutions. A provisional conclusion might be that shareholder activism that seeks to impose significant financial costs on a firm or that (implicitly or explicitly) criticizes the legitimacy of a firm's core business activities and strategies is likely to be ineffectual.

How Shareholder Activists Manage Their Relationships With Corporate Managers

One of the main contributions that shareholder activists have made to the debate about corporate social responsibility involves defining new social and public issues. The notion that corporations had an ethical responsibility to the majority population of South Africa—which could not vote or engage in a variety of occupations—represented a difference in views between shareholder activists (and many other stakeholders) and corporate managers.

In addition to defining social issues and engaging in public acts to put those issues before the general public (moving resolutions at annual meetings, writing opinion pieces, engaging in demonstrations), shareholder activists have sought to manage their relationships with corporate decision makers by developing (1) *deeper* relationships with corporations and (2) *wider* stakeholder networks.

Deeper Relationships With Corporations

One way in which shareholder activists have sought to manage their relations with corporations is to use the shareholder resolution (or the possibility of one) as a prod to bring companies into a dialogue on a social issue. In many cases, it is true that the social issue shareholder resolution creates two one-way dialogues in which the proponents and the company tell each other what they think about the social issue without any real interaction between them. But in many other cases, there are substantive dialogues that encompass a variety of social issues and last for a number of years.

Wider Stakeholder Networks

Another tactic that shareholder activists have used to manage their relationships with corporations is to develop wider stakeholder networks that collectively interact with companies. Rowley notes that as the density of ties within a social network increases—density here is the proportion of actual ties in a social network as compared with the possible number of ties—the ability of a focal organization's stakeholders (working collectively) to constrain the organization's actions increases. Applied to the present discussion, dyadic ties between organizations and shareholder activists are often not enough to lead to the latter's being able to affect corporate behavior. But if shareholder activists work together with other stakeholder groups that have similar interests and values, the organization's ability to resist the stakeholder coalition's demands is lower than if the organization was just dealing with activists alone.

This is a particularly important approach with highly technical issues or issues that require significant local community involvement. In the past few years, for example, a coalition of shareholder activists and environmental groups have worked together on the issue of climate change. A shareholder campaign in the late 1990s focused on corporate memberships in the Global Climate Coalition (GCC), an organization believed by many in the environmental community to be in opposition to regulatory action on climate change, and companies like American Electric Power, General Motors, and Texaco withdrew from the GCC as a result of this campaign; the GCC ultimately disbanded in 2002. Shareholder activists and environmental groups have been able to approach companies jointly and to be more effective on this social issue than either group would have been if they had been working alone.

What Shareholder Activism Illustrates About Organizational Relationships With Stakeholders

Corporations have similarly changed how they respond to shareholder activists and their social demands. First and foremost, not all companies actively resist or passively ignore such stakeholders. A significant number of shareholder resolutions are withdrawn every year by resolution proponents after the companies receiving the resolutions make some substantive policy change and/or agree to engage in further dialogue. More interesting—but less visible—for the study of organization-stakeholder relations are the number of resolutions that are not filed because of ongoing dialogues between shareholder activists and companies. As noted previously, the impact of shareholder activists is hidden in part because of the many dialogues that go on outside of public view—unlike a very public social issue shareholder resolution that gets voted down at a company's annual meeting. There has been a shift in the behavior of many companies away from reactive responses to the social demands of shareholder activists and toward more accommodative or proactive responses.

Ongoing dialogues with companies illustrate another response to shareholder activism: the development of ongoing, multi-issue relationships between managers and shareholder activists. A number of companies engage in annual dialogues with shareholder activists and provide progress reports on what they are doing with regard to a variety of social issues. Some companies have gone as far as to involve shareholder activists in the process of developing social polices and implementation practices. In some sense, more accommodative and proactive companies seek to bring shareholder (and other) activists into more collaborative and less confrontational relationships and, in so doing, use the expertise of such activists to shape their responses to social issues. Many of these dialogues—like those on global warming and on human rights standards—have brought shareholder activists together with other stakeholder groups and corporate managers in a way that would not have been possible otherwise.

Finally, even companies that don't want to deal with shareholder activists will try to influence public perceptions of the company's legitimacy with regard to a particular social issue, often by engaging in public relations or issuing reports that try to tell their side of the story. Very few companies, interestingly enough, simply ignore shareholder activists—although some responses may be symbolic and others more substantive. Religious institutions like the Interfaith Center on Corporate Responsibility have developed significant expertise in the corporate arena with regard to defining social issues, working in collaboration with other stakeholder groups and engaging in dialogue with corporate managers. Deeper and more cooperative relationships that seek to bring about dialogue and incremental change, combined with the development of broader stakeholder networks, have increased the effectiveness of shareholder activists. But corporations have changed as well in their approaches to shareholder activists. Some corporations seek to ignore or oppose attempts by such activists to change corporate policies and practices, but many others have found that the expertise and ability of shareholder activists to organize stakeholder dialogues helps improve the ability of corporations to manage social issues. This is not to say that most corporate managers are happy to see shareholder activists but rather that more enlightened managers are able to use dialogues with them to better understand and then manage social issues—and by extension, corporation-stakeholder relations. One lesson from shareholder activism for stakeholder management is this: Conflicts between corporations and their stakeholders need not always lead to discord. Sometimes cooperation and dialogue can bring about changes in corporate policies and practices far more effectively than muckraking and confrontation (although the latter often have their place as well).

In short, despite a lack of direct power over corporations and their managers, shareholder activists have been able to bring about social change. The effects of their activism can be felt in how social issues get publicly defined and then responded to by corporations, in addition to their direct interactions with corporations. As shareholder activism—particularly by religious institutions—more directly addresses corporate governance processes and issues of power in stakeholder-corporation relations, it will be interesting to see if the relatively congenial relationships of recent years between many corporate managers and shareholder activists continue.

Shareholder activism also merits further critical and ethical analysis. Shareholder activists, for example, seek to speak on behalf of particular issues and stakeholders, but such self-appointment might be ethically problematic. Shareholder activists, therefore, are one voice—with a unique position as activists and partial owners—in the debate about the social responsibilities of business.

Conclusion

Shareholder activism has done much to influence the debate about the responsibilities of corporations and their managers. Shareholder activism has prodded managers to become more transparent and accountable with regard to their actions on behalf of shareholders. It has also done much to influence the debate about corporate social responsibility and contributed to increasing stakeholder expectations for corporate social performance. The study of shareholder activism illustrates that stakeholders can have an effect on the behaviors of corporations and their managers.

—Harry J. Van Buren III

See also Agency, Theory of; Corporate Governance; Global Codes of Conduct; Religiously Motivated Investing; Social Activists; Socially Responsible Investing (SRI); Stakeholder Engagement

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Shareholder Model of Corporate Governance

In the familiar Anglo-American model of corporate governance, shareholders have two important rights: the right to ultimate control of a corporation and a right to all its profits. In addition, shareholders are the exclusive beneficiary of the fiduciary duty of management, which is to say that managers have a fiduciary duty to operate a corporation solely in the interest of shareholders. The role of shareholders in corporate governance can also be expressed by saying that maximizing shareholder wealth is and ought to be the objective of a firm.

These features of the shareholder model of corporate governance appear to place shareholders in a privileged position in comparison with employees, suppliers, customers, and other corporate constituencies or stakeholder groups. As a result, this model, which is often called "shareholder primacy," requires some moral justification. Why should shareholders occupy such a prominent role in corporate governance? Since the shareholder model has also become dominant in most developed market economies, there is also the empirical question of why this model has come to be preferred to the alternatives. What explains the origin and prevalence of the shareholder model?

Although many answers have been given to these two questions at different times, a consensus has emerged recently in the study of corporate governance that draws on new developments in the economics of organization. This consensus has been challenged, though, by the movement in business ethics known as stakeholder theory, which holds that all stakeholders and not merely shareholders should be central to corporate governance. Thus, this recent consensus in the study of corporate governance must successfully counter the challenge of stakeholder theory.

Some Preliminary Clarifications

To the questions of why shareholders should have the right of control and the right to profits, there is a very simple answer: Shareholders are, by definition, the group that has these two rights. That is, whichever group has the right to control a corporation—which also allows it to operate the firm in its own interest—and the right to receive the profits of the enterprise is called "the shareholders." The possession of these two rights also defines "ownership": Ownership of a corporation just means having the right of control and the right to the profits. So to say that shareholders are the owners of a corporation is true as a matter of definition.

In most corporations, especially those that follow the American and British model, the shareholders—which is to say the group with the right of control and the right to profits—are investors or, more precisely, equity capital providers. It should be observed, though, that equity capital providers are not always the owners of a corporation. Some corporations are owned by employees, while others, commonly called cooperatives, are customer owned or supplier owned. Mutual insurance companies are owned by policyholders. Still, the investor-owned corporation is the dominant form of corporate governance in the world today.

So the critical moral question is not why shareholders have the rights they do—this is a matter of definition—but why equity capital providers should be the shareholders. That is, why, should one kind of investor and not employees or some other group have the rights of shareholders? There is also the empirical question of why equity capital providers usually are the shareholders. That is, why has the investor-owned corporation become so dominant?

The answers provided by the recent consensus in the study of corporate governance can be stated very simply: The investor-owner corporation arose and endures because it is, under most conditions, the most efficient form of corporate governance. And it is morally justified because every corporate constituency, acting in a market, voluntarily consents to it, and they consent to it because investor ownership best serves each group's interest. These two claims, especially the second one, obviously require further development.

Approaches to Corporate Governance

The shareholder model of corporate governance originated in the 18th century, and in its long history, many different rationales have been developed for it. The original form of the modern corporation was the joint stock company, in which a small group of wealthy individuals pooled their money for some undertaking they could not finance alone. This form of business organization was justified on the grounds that it represents an extension of the property rights and the right of contract that are enjoyed by everyone. In a pure expression of this argument, the Michigan State Supreme Court declared in 1919 in *Dodge v. Ford Motor Co.* that a business corporation is organized and carried on mostly for the profit of the stockholders. The decision further noted that the profit-making end of a corporation is set forth in its charter of incorporation, which represents a contract among the shareholders who have invested their money.

The decision in *Dodge v. Ford Motor Co.* assumes that a corporation is the property of the shareholders. This assumption is true as long as a corporation has relatively few shareholders who actively control the business. However, the 1932 book by Adolf A. Berle Jr. and Gardiner C. Means, *The Modern Corporation and Private Property,* showed that the stock of large corporations had become dispersed among numerous investors who had little involvement in corporate affairs and that the actual control of corporations had passed to a class of professional managers. The result was a separation of ownership and control, and with this separation, shareholders had relinquished both control and responsibility. As a result, shareholders of large publicly held corporations had ceased to be owners in the full sense and had become merely a provider of one of the resources needed by a corporation.

In a famous exchange between Adolf Berle and E. Merrick Dodd, Dodd argued that with the demise of the argument for shareholder rights based on property and contract rights, the modern corporation should be operated to serve other constituencies besides shareholders. Berle replied that even though shareholder rights had lost their traditional foundation, shareholders should still have formal control because only a strict fiduciary duty to serve shareholder interests could effectively constrain managerial power. His argument, then, is that shareholder ownership is good for the whole of society because only this arrangement can assure that corporations are well run.

Today, the main justification of the shareholder model of corporate governance is founded on an economic approach that conceives a firm as a nexus of contracts between a legal entity called the firm and its various constituencies, most notably employees, customers, suppliers, and investors. This approach begins with the assumptions that in a market, all individuals with economic assets—such as employees with skills, suppliers with raw materials, customers and investors with money, and so on—trade with each other to obtain a greater return and that the greatest return will often be obtained by combining individual assets in joint production. That is, individuals will frequently realize a greater economic return by cooperating with others in productive activity than by participating in a market alone.

In his 1937 article "The Theory of the Firm," Ronald Coase noted that cooperative productive activity could take place entirely in a market. So, he asked, why do firms exist? The answer lies in the costs that would be incurred by individuals in coordinating joint or cooperative production in a market. The transaction costs of making and enforcing all the contractual agreements that would be required are substantial. These costs could be reduced by creating firms in which hierarchical authority relations replace the market as the means for coordinating joint productive activity. Thus, for Coase, markets and hierarchies constitute two fundamentally different means for conducting productive activity. The former operates by exchange, the latter by direct control.

As individuals contribute their assets to joint production, they will voluntarily form firms because doing so brings a greater return insofar as conducting business in a firm rather than in a market reduces costs. That is, the transaction costs of organizing productive activity entirely in a market can be reduced by bringing some of this activity into a hierarchical organization, and this reduction in costs will enable each participant to realize a greater return on the assets that are contributed to joint production. Because of this greater return, individuals with assets would voluntarily agree to contribute their assets to production in a firm.

On this economic view, then, the purpose of a firm is to enable individuals with economic assets to realize the full benefits of joint production. Every group benefits from production in a firm. Employees, suppliers, and investors gain by the opportunity to contribute their assets—labor, materials, and capital respectively—in a lower-cost form of production that brings a corresponding higher return. Customers benefit by being able to purchase abundant, low-priced goods, and society as a whole is enriched by the wealth creation firms make possible. Although some of these benefits can be obtained in a market, there is an additional gain or return from deploying assets in a hierarchical form of production. It is this additional gain that a firm provides, and realizing this gain constitutes the reason why it is formed.

The Role of Governance in Corporations

A firm requires many *inputs.* Economists classify these as land, labor, and capital, although they also recognize the need for managerial expertise to coordinate these inputs. Each corporate constituency interacts with a business organization or firm as *input providers*—employees providing labor, suppliers providing raw materials, and investors providing capital. Each input brings a return, such as employees' wages, suppliers' payments, and investors' interest and dividends. It is necessary in a firm for each input provider to *secure* their return—that is, to employ some means for ensuring that wages are paid, supplier payments are made, and so on. Generally, this security can be obtained by contracts or legal rules that obligate a firm to provide the return due to each corporate constituency.

Governance can be understood as the contractual agreements and legal rules that secure each input provider's claim for the return due on that input provider's contribution to the productive activity of a firm. Accordingly, every asset contributed to joint production will be accompanied by a governance structure of some kind, which may vary depending on the features of the asset provided. That is, the governance structure for securing employees' wages and other benefits may be different from those protecting suppliers and similarly for other input providers.

When the protection for each group's input can be provided by fully specified contracts or precise legal rules, the governance structure is relatively uncomplicated. Customers, for example, are adequately protected, for the most part, by sales contracts, warranties, and the like. The market also provides some protection. Thus, customers are protected by the opportunity to switch from one seller to another. The greatest problems of governance occur for *firm-specific* assets, which are assets that cannot easily be removed from production. When assets are firm specific, the providers become "locked in."

Developing governance structures to protect input providers is also more complicated when contracts and legal rules cannot be developed easily due to *complexity* and *uncertainty.* Contracts and legal rules provide protection only when the situations likely to be encountered can be anticipated and the ways of proceeding in each situation can be specified. When planning is difficult because of the complexity and uncertainty of the situations that might arise, other means must be found to protect stakeholder interests. Despite the three problems of lock-in, complexity, and uncertainty, governance structures for the assets of each input provider are relatively easy to provide for each corporate constituency except one, namely shareholders, the providers of equity capital.

The Economic Case for Shareholder Governance

As already noted, shareholders have a certain bundle of rights that includes the right of control and the right to the profits of a firm. To ask why shareholders should have these rights and thus be the owners of a firm makes no sense. The shareholders are, by definition, whatever group has the right to control and the right to receive the profits of an enterprise. The more relevant question is why, in most corporations, this group consists of equity capital providers and not, say, employees or customers or perhaps all groups.

Part of the answer to this question is also a matter of definition. Equity capital is money provided to a firm in return for a claim on profits—or, more precisely, for a claim on residual revenues, which are the revenues that remain after all debts and other legal obligations are paid. Just as customers buy a company's products, equity capital providers "buy" the future profits of a firm; or, alternatively, to raise capital, a company "sells" its future profits to investors. Unlike the providers of debt, who commit only for a fixed term (their contributed capital must be returned eventually as principal payments), equity capital providers invest for the life of a firm. Their investment is never returned, although stock ownership is alienable in the sense that the rights of ownership can be sold to another party. No matter who owns the shares, though, the capital originally provided remains available to the firm.

In addition, since future profits are risky, investors not only provide capital but also assume much of the risk of a firm. The willingness of shareholders to bear this *residual risk*—which is the risk that results from having a claim on residual revenues rather than a fixed claim—benefits all other input providers. As long as a firm is solvent—which is to say that it can pay all its fixed obligations, such as employee wages, suppliers' payments, and so on—then the claims of these groups are secure.

The remaining question, then, is why equity capital providers, who in effect "buy" the future profits of a firm and "sell" their risk-bearing services, should also have control and thus the right to have the firm run in their interest. The answer is very simple: Control is the most suitable protection for their firm-specific asset. If their return on the asset they provide, namely capital, is the residual earnings or profit of a firm, then this return is very insecure unless they can ensure that the firm is operated for maximum profit. In contrast, the right of control is of little value to other input providers or stakeholder groups because their return is secure as long as a firm is solvent, not maximally profitable. In addition, the return on the firm-specific contribution of other, nonshareholder groups is, for the most part, better protected by other means.

That equity capital providers have control is in the best interests of the other stakeholder groups. First, society as a whole benefits when business organizations are maximally profitable because of the greater wealth creation. If firms were controlled by groups whose interests are served only by firms that are solvent, not maximally profitable, then they would create less wealth. Second, every nonshareholder group benefits when shareholders assume much of the risk of an enterprise because their return is all the more secure. Shareholders are willing to assume this risk—in return for some compensation, of course—because they are better able to diversify their risks among a large number of companies. Employees, in contrast, are very undiversified inasmuch as their fortunes depend wholly on the employing firm. Third, without the right of control, equity capital providers would require a greater return to compensate for the increased risk to their investment. This, in turn, would drive up the price of capital, thus increasing the cost of production for everyone.

As previously noted, firms can be owned by groups other than equity capital providers. Some corporations are employee owned and others are owned by customers or suppliers. These forms of ownership are not common, however, because of their relative inefficiency, which is principally due to higher costs of making decisions and obtaining capital. It is only under certain economic conditions that these costs are offset by other advantages such that other forms of ownership would be preferred by the corporate constituencies involved. These other forms are also unstable inasmuch as employee owners, for example, often find it economically advantageous at some point to sell the firm to investors.

The bottom line, then, is that equity capital providers are usually (but not always) the shareholders of a firm, the group with control and the right to profits, because control rights are the best means for protecting their particular firm-specific asset. More specifically, equity capital providers have provided capital to a firm in return for the firm's future profits, and this claim on future profits can best be ensured by having control. Each group has the opportunity to seek the best protections or safeguards for their own interests, which is to say the return on the firm-specific assets they provide to a firm. Usually, nonshareholder groups are better served by safeguards other than control, which is left to shareholders.

This economic case for corporate governance not only explains why investor ownership is, in fact, the dominant form of corporate governance but also why it is morally justified. On this economic account, each corporate constituency—employees, customers, suppliers, and investors—mutually agrees to cooperate in joint production. Each group seeks the highest return on the specific asset that they provide and also seeks means to safeguard this return. Corporate governance is essentially the contract that firms write with equity capital providers, but other groups write contracts that best protect them. As a result, each group voluntarily consents to a mutually beneficial cooperative venture. The investor-owned corporation thus represents the best cooperative arrangement that can be negotiated among the various corporate constituencies in a free market.

The Stakeholder Challenge

Insofar as stakeholder theory advocates a different form of corporate governance that would extend some of the rights of shareholders to all stakeholders, it does so on two possible grounds. One argument is that stakeholder management—in which managers have a responsibility to serve the interests of all stakeholders and not shareholders alone—provides greater protection for each group's interest. The second argument is that stakeholder management results in a more just distribution of the wealth created by a corporation.

The first argument involves a purely empirical claim about the effectiveness of various safeguards. Generally, nonshareholder constituencies are better served by contractual guarantees than by a fiduciary duty to serve a group's interest, which is the main protection for shareholders. That management has a fiduciary duty to serve shareholder interests does not give them a privileged position; rather, it reflects the inability of shareholders to form the kind of contracts that adequately protect other groups. Fiduciary duties, in other words, are a weak substitute for the stronger contractual safeguards that other corporate constituencies enjoy. There is no evidence that any nonshareholder group, such as employees, would voluntarily replace the contractual safeguards they have with the kind of protections that serve shareholder interests.

To the second argument—that stakeholder management results in a more just distribution of the wealth—there are two replies. First, stakeholder theory may underestimate the extent to which shareholder-controlled corporations, in fact, serve the interests of all stakeholder groups. On the economic account, the purpose of a firm is to enable everyone with economic assets to realize the full benefits of joint production. From the wealth created by business organizations, employees earn wages, customers receive products, suppliers make sales, and so on. The profits of a corporation are merely the returns due to shareholders for their provision of capital. Every group benefits from a corporation's activities, and they benefit all the more when a corporation is operated for maximum profit.

Second, the task of distributing the wealth created by corporations is done largely by the market, not management. It is a mistake to infer that because the purpose of a firm is to benefit everyone, that benefiting everyone is a task of management. Wealth must be created before it can be distributed, and wealth creation, rather than distribution, is and ought to be the main task of management. If the market's distribution of wealth is unfair, then the task of altering this market distribution falls primarily to government. Attempting to alter the distribution of wealth by making changes in corporate governance is not likely to be very effective.

—John R. Boatright

See also Agency, Theory of; Berle-Dodd Debate; Coase, Ronald H.; Corporate Governance; Fiduciary Duty; Profits; Shareholders; Shareholder Wealth Maximization; Stakeholder Theory; Wealth Creation

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Shareholder Resolutions

A shareholder resolution is a request that shareholders vote on a recommendation that the corporation and/or the board undertake certain action. It appears in a company's proxy statement to be presented at a company's annual meeting. Resolutions, even those supported by a majority vote, are not binding on management, although the shareholders of some companies have proposed changes in corporate bylaws to make the proposals binding. Shareholder resolutions are governed and controlled by both state and federal law, specifically by Rule 14a-8 of the 1934 Securities Exchange Act. The remainder of this discussion will focus on the mechanics of a shareholder resolution, its history and evolution, the purposes underlying the tactic, and corporate responses to resolutions.

Mechanics

Any shareholder with $2,000 or more invested in a company may propose a resolution, as determined by Rule 14a-8 of the 1934 act. Once a resolution has been proposed and approved for submission to all shareholders by the SEC, it must then receive a certain threshold of support to remain alive for submission in subsequent years: 3% in the first year, 6% in the second year, and 10% in the third year qualify for future consideration.

According to Rule 14a-8 of the Securities Exchange Act of 1934, companies can exclude resolutions from consideration if they relate to or contain (1) personal grievances, (2) self-interested proposals that provide a personal benefit to the person introducing the proposal that would not accrue to other shareholders, (3) ordinary business matters, (4) impermissibly vague or misleading statements, and (5) impractical or overly general proposals that the company lacks the power to implement. As opposed to the conditions for exclusion, the major condition for acceptance is that the resolution relates to a substantial business policy and not just mundane business matters. Courts have included employment and social issues as substantial business policies, and corporate governance concerns easily qualify.

History and Evolution

The first wave of shareholder resolutions started in the 1960s and focused on the social causes of the day, particularly equal employment opportunity, napalm production during the Vietnam War, investment in South Africa, and the environment. Social issues of concern more than 30 years later include global warming, human rights, and corporate political practices.

An early pioneer in sponsoring shareholder resolutions was Saul Alinsky, a community organizer from Chicago who targeted firms like Eastman Kodak on equal employment issues. Ralph Nader then adopted the tactic, as part of his pressure on General Motors Corporation through Campaign GM. It was only through religious institutional sponsorship, however, that shareholder resolutions spread rapidly in the 1970s. The Interfaith Center on Corporate Responsibility, since its founding in 1971, has coordinated 200 to 300 shareholder resolution campaigns annually.

In the 1990s, shareholder resolutions began to focus on mainstream corporate governance concerns, relevant to a greater number of shareholders, and executive compensation has been the subject of many resolutions. Since 1990, support levels have grown dramatically from the 3% to 10% range for most social issues to a much higher 20% to 50% range. Many of the traditional institutional investors, including pension funds and labor unions, have sponsored the corporate governance resolutions.

Purposes

The purpose behind most resolutions on mainstream governance issues is to galvanize shareholder support to force an immediate change in corporate policy, though the passivity of many pension funds and mutual funds is an obstacle to achieving such heavy support. On social issues, where it is virtually impossible to build majority support, the purpose is often to promote incremental change. Such shareholder proposals become part of an overall publicity campaign to expose corporate practices to media and public scrutiny and, perhaps, place the issue on the public policy agenda.

Corporate Responses

In the early days of shareholder proposal campaigns, the typical management response was one of reflexive opposition. Some companies learned that negotiation is a better approach. Even GM, which initially and aggressively confronted Ralph Nader, ultimately accepted his resolution calling for a public issues committee of the GM board. As shareholder resolutions have multiplied over time, companies have observed the positive lessons of negotiations, leading to the withdrawal of resolutions. In some companies, management has even endorsed shareholder resolutions, leading to overwhelming votes for their passage.

In deciding how to vote their shares on proxy resolutions, institutional investors rely heavily on a growing market of shareholder advisory services. Institutional Shareholder Services is the largest of such firms, though new firms and established rating services like Standard & Poor's have injected competition into the field. To combat the practice of brokerage firms voting stock held in street names, with those votes invariably being cast to support management's position on a resolution, the New York Stock Exchange is proposing to bar broker votes on behalf of customers who do not provide instructions on proxy matters. If the SEC approves such a rule, share owners would have to opt in and grant permission to brokers to cast votes on their behalf, rather than brokers retaining that power unless their customers opt out.

—John M. Holcomb

See also Corporate Governance; Shareholder Activism; Shareholder Model of Corporate Governance; Shareholders

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Shareholders

A shareholder is the owner of an equitable interest in a for-profit corporation. A shareholder does not own legal title to the property of the corporation but owns stock or shares in the corporation. Ownership of the shares or stock of a corporation confers the rights to control the company and to receive residual revenues or profits.

In a close corporation, a family-owned or privately held company, a small number of shareholders own equitable interests in the corporation and often also manage the enterprise. State laws permit greater flexibility in the operations of close corporations than in the operations of the traditional publicly held corporation but also impose greater controls on the transfer of shares to protect the interests of all shareholders. Close corporations, for instance, are often allowed to operate without such corporate formalities as a board of directors. The business form of S corporation also exists, restricted to companies with 75 or fewer shareholders. This form affords certain tax advantages to its stockholders but has become less common, given the rise of the limited liability company and of the limited liability partnership.

The overwhelming proportion of shareholders own stock in larger, publicly held corporations. There are two categories of shares: common shares and preferred shares. The vast number of shareholders own common shares, and their rights are subordinate to those of owners of preferred shares when dividends or dissolution payments are paid. However, common shares confer voting rights that preferred shares do not possess, and there is greater upside potential for common share values to grow as corporate earnings expand. Common share owners have an exclusive claim to corporate earnings and assets that exceed the legal claims of creditors and preferred shareowners.

While voting rights attach to most shares on a one-share one-vote basis, some companies have established two categories or classes within common shares, with only one class having super voting rights. Critics condemn the system for preserving a privileged class of owners, but they serve an important purpose of allowing minority shareholders to keep control with the consent of other shareholders. Allowing a family or the original founders to keep control might benefit the brand or culture of the firm and retain customer goodwill.

In a publicly held company, the widely dispersed shareholders are the principals, and they delegate the day-to-day operations of the company to management, their agents. The result is a separation of management from ownership, which can create a misalignment of incentives between the two. Shareholders desire the maximization of shareholder wealth, and their elected representatives on the board of directors owe a fiduciary duty to shareholders to promote that interest. Meanwhile, management serves the overall interests of shareholders and of the corporation as a whole on a de jure basis. In doing so, management may on a de facto basis pursue other goals besides shareholder wealth maximization, whether those goals are altruistic or based on self-interest. The de jure goals of management are aligned with shareholders, but the de facto goals may diverge. To realign shareholder and management interests, some argue that managers' compensation ought to be partially or largely based on restricted stock or stock options.

Based on the identity of shareholders rather than the types of shares they own, the two major categories of owners are individual investors and institutional investors, the latter playing an increasingly important role in investor capitalism. Pension funds and mutual funds serve as intermediaries for most individuals who want to participate as investors. Two thirds of the stocks in the economy are held by institutional investors. Ninety-five million Americans own stock through mutual funds—double the number that own individual company stocks.

Importance of Shareholders

Pooling the investments of many shareholders has also allowed companies to grow and allowed the evolution from an entrepreneurial economy to an industrial economy in the late 19th and early 20th centuries. Since the United States benefits from a widely dispersed shareholder base, versus the concentrated business ownership structure in Germany and other countries, that large source of capital is especially noteworthy in the United States.

Limited liability of shareholders in the American legal system provides added incentive for shareholders to invest. Whereas they assume the possible residual risk of losing their total investment should the company collapse, this is generally the extent of their liability, leaving their other personal assets out of the reach of creditors. Only when a firm is the alter ego of a group of investors, through domination by large shareholders, commingling of assets, or bypassing organizational formalities, might a court "pierce the corporate veil" and hold the controlling shareholders personally liable. If the firm is undercapitalized, a court might also hold controlling shareholders liable for misconduct by the corporation. Assuming the risk of losing just their investment, however, still provides incentive to shareholders to monitor the conduct of the company and to hold management at least indirectly accountable to them through the board of directors.

Problems Concerning Shareholders

One problem associated with shareholders, especially in close corporations, is the possibility that majority shareholders could oppress the rights of minority shareholders. Majority shareholders owe a fiduciary duty to minority shareholders and are legally liable if they deprive minority owners of their full rights of participation, perhaps even in directing or managing the enterprise.

A larger societal problem about shareholders concerns the state of shareholder power. In the late 20th century, a concern arose that management was not sufficiently accountable to shareholders, that the owners actually played a limited role in governing the corporation, and that imperial CEOs were assuming too much power over directors and shareholders. After the corporate scandals of the early 21st century, shareholders became somewhat more active in exercising their rights and powers, leading some defenders of traditional management and director roles to criticize the rise of the "imperial shareholder."

Given the variety of shareholder interests within both the individual and institutional investor communities, some exercise their powers more than others, with both positive and negative effects. Some hold shares for short periods of time, whereas others are long-term value investors. Because of this, some investors are truly concerned about the operations of companies in which they invest, whereas other shareholders are disinterested and concerned only with making money from short-run changes in the market. Hedge funds, decried by some, are notorious for focusing on the short term. Individual investors are too dispersed to have much impact on corporate governance, but some institutional investors are taking an active role, either by energizing the takeover market or by emphasizing director accountability and independence. Meanwhile, mutual funds and pension funds are faulted for reflexively supporting management in most of the companies they hold.

Global shareholder activism is also moving forward, with U.S. institutional investors bringing pressure on companies based in other countries, whereas foreign investors are exercising their powers in U.S. companies. Given the greater accountability of companies to shareholders in the United Kingdom and the disruptive nature of shareholders in Japan, the development of global shareholder activism strikes fear into the traditional defenders of management and directors. Beyond shareholder pressures, investor relations departments must also serve the needs of shareholders for information, and both add to the costs of corporate decision making.

Legal Powers and Rights of Shareholders

Among the typical powers of shareholders are the powers to amend the articles of incorporation or bylaws, to approve a merger or dissolution of the firm, and to approve the sale of corporate assets. They also enjoy the power to remove directors for cause, and some states even empower shareholders to remove directors by a majority vote without cause. Shareholders also enjoy the right to dividends, though directors will not be held liable for failing to declare dividends if they want to invest that money in corporate expansion or some other legitimate purpose. Articles of incorporation might also confer preemptive rights to shareholders to a prorated share of a new issue of stock by the firm. The major legal powers and rights of shareholders discussed below are voting, inspection of corporate records, campaigns for control, shareholder litigation, shareholder resolutions, and shareholder exit.

Voting

Shareholders can vote either as individuals or as a group. They can agree through a written shareholder agreement to vote their shares together on a specified matter. They can also designate an agent to vote their shares through a written proxy agreement. Finally, they can enter into a voting trust, where they transfer the right to vote their shares to a designated trustee.

The power of voting is crucial to a system of shareholder democracy, and shareholders participate in the election of corporate directors on a one-share one-vote basis. A shareholder who owns 10 shares can, therefore, cast 10 votes for each director position open on the board. A system of cumulative voting is designed to favor minority shareholders by ensuring that they may be able to elect at least one director. For instance, in a company with a nine-member board, a block of minority shareholders with 3,000 shares could accumulate 27,000 votes for one candidate rather than casting 3,000 votes on each of nine open board seats. Assuming that majority shareholders controlled 8,000 shares, they spread their 80,000 votes among the eight other board candidates but could not win every seat. However, few companies have adopted this system, and few state corporation laws require it.

The board or governance committee nominates candidates for the board, and few elections are contested. Hence, a shareholder can either vote or withhold a vote for each board member. Given that most companies follow a system of plurality voting rather than majority voting, a shareholder usually accomplishes little by withholding a vote. The candidate will be elected even if few votes are cast. Nevertheless, symbolic campaigns to withhold votes from directors have been organized to protest corporate problems such as undetected accounting fraud or excessive executive pay. Even symbolic campaigns can have results, though, as in the case of Disney shareholders who withheld 45% of their votes for Michael Eisner in his re-election to the board, tripping off an erosion of his support that led to his ouster from the board and eventual resignation as CEO. Occasionally, campaigns will also be launched to remove specific directors from a board through a shareholder resolution. In the United Kingdom, where the balance of power is struck in favor of shareholders over directors, shareholders can actually vote directors off the board.

Institutional investors have also promoted the adoption of majority-vote systems to replace the plurality systems in many corporations. A majority-vote system would require that each board candidate, whether opposed or not, receive a majority of shareholder votes to be elected. Since shareholder resolutions are not binding, institutional investors have instead pressured companies to change their bylaws to allow majority voting.

Even with majority voting, however, shareholder democracy would not be fully realized since shareholders are still presented with a slate of candidates, or a single candidate for each board seat, nominated by the board. To complete the picture, some believe that shareholders should be able to nominate candidates to the board. Efforts by the SEC to implement a rule calling for shareholder nominations to the board have thus far not succeeded, and such a rule has been opposed by the Business Roundtable and other major business groups.

Inspection of Corporate Records

Shareholders have the right to inspect the books and records of the corporation for a "proper purpose," which the various states define differently. Some states are concerned about an abuse of that right and define "proper purpose" to minimize the possibility of shareholders using the tool to go on "fishing expeditions." Most inspection battles surround attempts to obtain shareholder lists, which corporations guard closely. Aggrieved shareholders often want those lists to wage proxy fights for control of the company.

Campaigns for Control

Shareholders can also engage in proxy fights for control of the ownership structure and board of a company. Wealthy investors, such as the "corporate raiders" of the 1980s, have been joined by activist hedge funds in such battles for control. The hedge funds have been supported in these battles by high-powered law firms and leading investment banking firms. A few investment firms have even sought controlling ownership of underperforming firms to turn them around.

A major barrier to proxy fights over both board elections and shareholder resolutions is the cost, since management controls the proxy machinery. Management can pay for its campaign with shareholder assets, but insurgents must finance their own campaigns. To bring more fairness to such contests, it has been suggested that the corporation reimburse sponsors for the costs of successful campaigns.

Shareholder Litigation

When faced with injury from management fraud, shareholders have the legal power to bring derivative lawsuits, wherein they sue management on behalf of the corporation, and all owners may thereby be compensated. To recover their losses, the U.S. Supreme Court held in *Dura Pharmaceuticals v. Broudo* that shareholders must prove that management fraud rather than a general market decline was the actual cause of their injuries. The 1998 Securities Litigation Uniform Standards Act requires that any losses sustained in the buying and selling of stock must be brought in federal court, not state court, and the Supreme Court in *Merrill Lynch v. Dabit* held that federal law also preempts any state law and requires that cases involving losses sustained from the holding of stock must also be brought to federal court.

In the 1995 Private Securities Litigation Reform Act, Congress sought to empower large institutional investors by requiring that the shareholders with the largest financial interest at stake be appointed as lead plaintiffs in shareholder class-action suits, since their interests were best aligned with shareholders in general. In an attempt to prevent abuse of the securities laws, Congress also limited the power of professional plaintiffs who filed lawsuits for their own pecuniary benefit in order to prompt companies to settle cases for nuisance value.

Shareholder derivative suits can be brought only after a shareholder first complains to the board about possible illegal conduct and fails to receive satisfactory results. Securities class-action lawsuits, however, do not require such advance screening by the board and represent the largest number of lawsuits and also the largest amount of damages awarded directly to shareholders rather than to the corporate treasury.

Shareholder Resolution

A shareholder who owns at least $2,000 worth of stock in a company has the legal right to introduce a shareholder resolution at the annual meeting, so long as that resolution has been approved by the SEC as unrelated to the ordinary business of the firm. There is little question that a resolution related to corporate governance would qualify. Shareholder resolutions are more fully discussed in a separate entry in this encyclopedia.

Shareholder Exit

What is often called the Wall Street Rule gives shareholders the obvious power of selling their shares in a company as their ultimate expression of disapproval. This relates to the alienability of shares and the right of shareholders to sell or transfer their shares. Shareholders may prefer to exercise voice, but exiting is always an option. In this way, the market punishes underperforming companies. Shareholders may sell for other reasons as well, including the promotion of social change. Shareholders in the 1970s helped change the system of apartheid in South Africa by disinvesting from corporations doing business there.

—John M. Holcomb

See also Corporate Governance; Market for Corporate Control; Minority Shareholders; Shareholder Activism; Shareholder Model of Corporate Governance; Shareholder Resolutions

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Shareholder Wealth Maximization

The principle of shareholder wealth maximization (SWM) holds that a maximum return to shareholders is and ought to be the objective of all corporate activity. From a financial management perspective, this means maximizing the price of a firm's common stock. In pursuing this objective, managers consider the risk and timing associated with expected earnings per share to maximize the price of the firm's common stock. When this is properly executed, management will also have maximized the future stream of dividends and capital gains that accrue to its shareholders. The most defensible form of SWM looks to long-term rather than short-term maximization.

The maximization of shareholder wealth is described as the "monotonic" view of the purpose of the corporation and, therefore, of the responsibilities of its managers. It is monotonic because it focuses on the interests of a single group, the shareholders, to the exclusion of other groups that may be affected by the activities of the firm or that could benefit from the activities of the firm. It is for this reason that the principle of SWM is controversial. Economic, legal, and moral considerations have been used both to defend and criticize the view that the firm should be managed so as to maximize the interests of a single group, namely the shareholders.

The Justification of SWM

Historically, from a legal perspective, the corporation was regarded during the 19th century as an instrument of public policy with a social responsibility. These social concerns gave way to the idea of managing the firm for the shareholders' profits. Legal theorists began to regard stock ownership as no different from other forms of private property. The corporation was viewed as owned by its shareholders. This legal model is entirely consistent with SWM. The directors' role is to manage the property of the owners, that is, the shareholders. As stewards of the shareholders' interests, their sole responsibility must be to the shareholders, and promoting the interests of other groups would be a misuse of the property entrusted to them. Insofar as private property plays such a powerful role in the American ethos, the argument for SWM, based on the value ascribed to private ownership, has had profound appeal.

At the same time, property rights are viewed as the foundation of a capital-driven economic system, and the principle of SWM also makes sense from the perspective of economic efficiency. The shareholders, as the owners of the corporation, purchase stock because they are looking for financial return. In most cases, shareholders elect directors who then hire managers to run the company on a day-to-day basis. Since managers are supposed to be working in the interests of shareholders, it follows that they should follow policies that enhance shareholder value. Property rights are deemed essential to the workings of the system, and the resulting outcomes are at the same time beneficial to society. Profits are indicative of the fact that an organization has transformed a set of inputs into a productive output of goods or services that have a higher value than the original inputs. Thus, when SWM is properly pursued, the financial benefits are alleged to include the following: efficient, low-cost businesses that produce high-quality goods and services at the lowest possible prices; products and goods that consumers need and want, such as new technologies, new products, and new jobs; courteous service; adequate stocks of merchandise; and well-located establishments.

But one could underline that corporations often have a diversified class of investors with financial claims not only from shareholders but also bondholders and other debtholders. Why is it not more economically efficient to focus on this diversity of financial claimants? It is claimed that SWM remains a more economically efficient *modus operandi* because the maximization of shareholder value requires the initial satisfaction of the financial claims of other investors and interests to secure a profitable return. SWM is, therefore, not inconsistent with the satisfaction of the claims of other investors.

Moreover, defenders of the principle of SWM or shareholder primacy hold that it is not merely consistent with but that it also promotes the interests of all nonshareholders who have financial interests in the firm, such as bondholders and other secured and unsecured creditors. Shareholders are less risk averse than nonshareholders, whereas managing the firm on behalf of interests other than shareholders can lead to greater risk aversion. This will occur if the firm is managed in the interests of its fixed claimants. Fixed claimants, such as bondholders, refer to those financial interests to whom the firm has pledged a fixed rate of return or sum that cannot be varied regardless of the firm's financial success. In contrast, residual claimants are only guaranteed a return after all fixed financial claims have been satisfied, and the amount of the return, if any, will vary according to the financial success of the company. In this situation, bondholders, for example, base decisions on the bankruptcy risk on a firm's cash flows, not the firm's value-maximizing potential from free cash flows. The result may well be that the company fails to invest in new opportunities for growth, innovative products, and new technologies or markets, which in the long run may undermine the capacity to remain competitive. It is argued that shareholders have a greater incentive to induce firms to engage in activities that other claimants such as bondholders may regard as excessively risky. Shareholders, thus, push the managers of the corporation to operate at levels beyond those sufficient to satisfy the interests of fixed claimants. However, it is also true that it is the shareholders who bear the greater loss from excessive risk taking if the firm does badly because, in any case, other claimants have a guaranteed fixed rate of return. At the same time, it is argued that in maximizing shareholder wealth, managers seek to increase market share (insofar as this is compatible with long-term profits), which will increase the size of the pie that is available to all participants in the corporate enterprise. In this way, the success of the company will offer greater security for fixed claimants by ensuring that the firm is in a better position to cover possible future losses and thereby maintain its commitments to its fixed claimants.

Defenders of SWM also argue that attempting to maximize in more than one dimension at the same time may well be impossible unless the multiplicity of objectives can be reduced to an overall monotonic purpose. The resulting loss of direction from pursuing multiple objectives can mean an equally fatal loss of competitiveness. Moreover, managing the firm for a variety of interests including fixed and residual claimants means a diversity of goals in which overall performance cannot be accurately assessed. In contrast, the principle of shareholder value offers an unambiguous standard, which is measurable and observable.

The Contractarian Legal Model and SWM

The earlier legal view of the corporation as a form of property that is subject to ownership rights has given way to a contractarian model, which sees the corporation as a nexus of contracts. This alternative model envisions the corporation as offering an umbrella that allows private parties to contract with one another more efficiently than they could in a market by limiting the transaction costs. This view avoids the ontological issues that result when one regards the corporation as a thing that could possibly be owned. In any case, regarding the corporation and its assets as being owned by the shareholders is highly misleading insofar as shareholders usually have no right to manage these assets or unlimited access to information and records relating to these assets. The corporation is, therefore, more accurately viewed as a device that operates as a nexus for all contracts that various individuals have voluntarily entered into for mutual benefit. Although, theoretically, the activities of the corporation could be carried out by individuals through individual contract in a market outside the corporate structure, the costs associated with enlisting cooperation would be significant. As R. H. Coase argued in 1937, the law in effect offers a standardized form of contract or a set of default rules that facilitate private ordering. This legal entity, which is actually a legal fiction, allows those with money and resources to contract with those who have managerial skills but little money to forge a mutually advantageous cooperative enterprise. Moreover, those with labor to sell but lacking monetary resources or managerial skills can negotiate with the managers acting as agents of the corporation to form employment contracts.

However, according to contractarians, interpreting the corporation as a nexus of contracts rather than a form of property that is owned does not invalidate the principle of SWM. The contractarian perspective describes the corporation as being composed of explicit and implicit contracts held by shareholders and nonshareholders. The interests of nonshareholders, such as employees, suppliers, bondholders, communities, and customers, are protected by contract, law, and regulation. Shareholders are said to be entitled to the firm's residual cash flow. However, the management's obligation to realize and promote this residual cash flow is open-ended because there are no sets of specified actions that can be enforced to realize this objective. In other words, management has a legal obligation to create a healthy residual cash flow, but there are no terms that specify particular actions for achieving this goal. But to give greater definition to the relationship that embodies this particular understanding, the legal system creates a fiduciary duty to maximize shareholder wealth. This fiduciary duty fills the gaps that arise in terms of management's unspecified or imperfect obligations to maximize shareholder wealth.

Moreover, agency theory supplements the contractarian position and adds weight to the view that the purpose of the firm is the maximization of shareholder wealth. Agency problems arise because contracts are not "costlessly" written and enforced. Agency costs include the costs of structuring, monitoring, and bonding a set of contracts among agents with conflicting interests, plus the residual loss incurred when the cost of full enforcement of contracts exceeds the benefits. It is argued that the necessity of a corporate structure in which ownership and control are separated entails that only the residual claimants can provide appropriate monitoring. It follows that the agency costs inherent in a team organization, such as the firm, are controlled, and maximization of output occurs when control rights are assigned to the residual claimants.

We have considered the economic and legal rationales that justify SWM. We will now proceed to consider a normative critique of SWM.

Ethical and Legal Implications of Contractarian and Communitarian Theory

The nexus of contracts view of the corporation also has an underlying ideological basis that embodies a particular moral perspective. We have discussed the view of the corporation as an economic and financial arrangement with an objective of SWM. However, we have not considered whether this particular governance relationship is and ought to be a product of individual choice. Those who advocate SWM argue that we should leave it up to the various participants in corporate activity to specify respective rights and obligations through contract, rather than legally imposing relationships. According to this view, shareholders bargain and secure from management a commitment to a fiduciary duty to direct the corporations so as to maximize shareholder wealth. This is an open-ended responsibility because it is not realistically possible to specify in detail what exactly is to be done to fulfill this fiduciary duty. On the other hand, other participants in the corporate enterprise contract with the agents of the corporation for more specific rights in return for the particular services provided. Accordingly, nonshareholders are free to protect themselves through contracts by bargaining for whatever protections they deem necessary to protect interests that may be threatened by the pursuit of SWM. For example, workers could bargain for protections against a policy of employment at will or seek other legal protections.

The communitarian view stands in contrast to this contractarian position. While contractarians advocate that the law should play a minimal role in structuring relationships, communitarians argue that the law must intervene to prevent harmful externalities that may result from the single-minded promotion of SWM. For example, factories may be closed down and workers laid off to protect profits, but at the same time, this may significantly damage the local community, which depends on this income and indeed may have invested in infrastructure that supports the corporate enterprise. Communities may find it difficult to foresee such events and contract to protect their interests from uncompensated losses. At the same time, public goods that are often essential to the communities in which corporations operate are difficult to secure through the market.

An important difference between the communitarian and contractarian positions is their focus. Communitarians tend to highlight the undeniable social effects of corporate activity, seeing corporations as institutions that have a profound effect on those who are outside the corporation. Accordingly, it is appropriate that the state intervene to enhance the social environment and minimize the deleterious effects of market activity. On the other hand, contractarians focus on the internal relationships. They see the corporation as an organization constituted by private contracts that have been voluntarily entered into. This difference in emphasis sheds light on the important ideological differences that also manifest contrasting and opposing moral values.

Contractarians see society as constituted by autonomous citizens who ought to be free to make the choices that shape their destiny without intervention from outside authority, so long as they are not actively harming other individuals. Governments should not dictate matters involving the type of agreements we make, our individual economic behavior, or the redistribution of wealth. Contractual arrangements are a way in which we express this autonomy and freedom. The latter, they claim, form an important foundational value for our social existence. Communitarians, in contrast, emphasize social interdependence and the fact that individual persons and corporate persons derive many benefits from life in society that have no contractual basis. On this rationale, it is appropriate that the state intervenes to structure relationships that reflect this interdependence and protects constituencies such as workers and the local community from the deleterious effects of unregulated SWM. Although contractarians claim that nonshareholders can always enter into contractual relations to protect their interests from harmful externalities, communitarians point out that unequal distribution of wealth produces inequality of bargaining power. In many cases, nonshareholders lack the resources to bargain and negotiate effectively to protect their interests. In reality, nonshareholder protection from the externalities of SWM depends on people's capability and willingness to pay for contractual guarantees. Communitarians argue that it is unrealistic to believe that unskilled workers have the resources to buy layoff protection from the shareholders or their agents. Ultimately, the existence of contractual relations alone does not ensure that arrangements are fair to all parties or even reflect the individual contributions that are made to the greater social body.

Stakeholder Theory

Many who see a moral dimension to business activities that extends beyond mere contractual obligations and the single-minded pursuit of making money for shareholders propose a stakeholder approach to business activities. Stakeholder theory emphasizes that managers are also moral agents who are responsible to a wide array of groups for their actions. Much of the groundbreaking work is associated with R. Edward Freeman. A stakeholder is broadly defined as any individual or group who can affect or is affected by the achievement of the organization's objectives. If one fails to recognize these responsibilities to other groups, it becomes easy to rationalize a questionable practice that potentially harms nonshareholder stakeholders, such as workers or suppliers, to whom managers supposedly have no moral obligation, in order to realize increased profitability.

The stakeholder theory of corporate responsibility is a developing response to the view that a firm should be run in such a way as to maximize the wealth of the shareholders.

The stakeholder approach argues that it is not only those with a financial claim on the institution who are worthy of consideration, but that there is a multiplicity of groups with a stake in the operations of the firm, all of whom merit consideration in managerial decision making. The word "stakeholder" first appeared in usage in 1963 in an internal memorandum of the Stanford Research Institute and has since become a prominent concept in corporate and academic communities. The theory, which is clearly designed to extend the ethical responsibility of the firm, is an alternative to the monotonic fiduciary model offered by the property rights and contractual approaches. According to stakeholder theory, a person who holds a stake in the activities of an organization, a "stakeholder," is entitled to consideration in some ways similar to shareholders.

Stakeholder theory has also apparently been reflected in changes to the law, especially in the United States. In the 1990s, many jurisdictions in the United States passed so-called "other constituencies legislation" and determined that the directors should consider not only the profit margin in their decisions but also the interests of the employees and the general public. These statutes have been enacted by at least 25 U.S. states. The typical nonshareholder constituency statute authorizes (but does not require) a director of a corporation, in considering its best interests, to consider the interests of persons (often referred to as stakeholders) other than shareholders and frequently also consider generalized factors such as local and national economies, societal factors, and any other factors deemed by the directors to be pertinent. The various nonshareholder constituencies may be seen to include employees, customers, creditors, suppliers, and communities in whom the corporation has facilities. However, whereas some have hailed "other constituencies legislation" as rejecting shareholder primacy, many are far more cautious. It has been pointed out that there is little meaningful case law relating to these statutes and so they still stand in need of interpretation. The American Bar Association's Committee on Corporate Law recommends that constituency statutes be interpreted according to the relatively recent Delaware precedent. This precedent states that courts should not allow consideration of nonshareholder interests without relating such considerations in an appropriate fashion to shareholder welfare. Moreover, constituency statutes apply only to a narrow range of decisions, which essentially involve change of control, that is, takeovers. This means that the range of situations in which boards have the right to consider other constituencies is rather limited. It can therefore be argued that these statutes are really not proshareholder but in fact are designed to entrench management.

Again, many of the arguments used to support SWM can be used to reject the stakeholder model of corporate responsibility. As we pointed out earlier, defenders of SWM would argue that adopting strategies in accordance with the stakeholder view, which means acknowledging the interests of multiple constituencies in addition to fixed and residual financial claimants, may well result in increased indecision and confusion. Satisfying a diversity of interests may well be impossible unless the multiplicity of objectives can be reduced to an overall monotonic purpose. Loss of competitiveness may well follow. As said before, it is not easy to manage on behalf of multiple constituencies when their goals come into conflict, and it may not be socially desirable to give managers unlimited liberty to make choices between competing interests. In contrast, the principle of shareholder value offers an unambiguous standard, which is measurable and observable.

Finally, if the law intervenes and seeks to enforce the stakeholder model, for example, by requiring that investors take on increased liabilities with respect to employees, forgoing employment at will or giving the employees the right to buy the business at less than market value, any benefit to employees might well be short-lived. Investors cannot be compelled to supply capital to the corporation. Shareholders may demand a higher price for capital and thus increase the firms' cost of capital with damaging financial consequences for nonshareholder constituencies. On the other hand, investors may simply look to other forms of investment if the monotonic principle is abandoned and shareholder interests are compromised, resulting in insufficient monetary returns. Alternatively, potential shareholders could invest in real estate, gold, Treasury bonds, or shares in overseas Japanese corporations, to mention a few examples.

Those who disagree with these points and promote the stakeholder model argue that emphasizing the principle of SWM fails to appreciate entrepreneurial risk in the wider, richer context of joint stakeholder relationships. In addition, emphasizing a single responsibility to make money for shareholders fosters a myopic worldview in which managers fail to see themselves as moral agents who are responsible to a wide variety of groups for their actions. In the long run, this monotonic approach may well work to the disadvantage of the shareholder's interests. However, defenders of shareholder value maximization argue that their position does not encompass the exploitation or alienation of the firm's other constituencies. Strategies that do not take into account the morally acceptable relationships with other stakeholders, including effects on the local community, are incompatible with long-term shareholder value creation. In this manner, SWM can be interpreted as an inclusive principle that does not deny that these other interests exist and must be acknowledged in the decision-making process. Ultimately, both those who advocate shareholder value and those who advocate the multi-fiduciary stakeholder approach can make reasonable claims that their preferred approach enhances the interests of all related constituencies. One concludes that the monotonic and pluralistic approaches only become clearly distinguishable in those cases in which managers of a firm, following ethical principles, decide to benefit a particular nonshareholder group in circumstances that negatively affect both short-term and long-term shareholder wealth creation.

—*David Riordon Lea*

See also Agency, Theory of; Corporate Governance; Corporate Social Responsibility (CSR) and Corporate Social Performance (CSP); Fiduciary Duty; Profits; Shareholder Model of Corporate Governance; Shareholders; Stakeholder Economy; Stakeholder Engagement; Stakeholder Responsibility; Stakeholder Theory; Wealth Creation

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Side-Constraints

Side-constraints are anything that acts to confine or restrict. The focus here is on *moral* side-constraints. When we speak of moral side-constraints, we have an understanding of moral rights as requiring that nothing be done to prevent those rights being exercised. So, for example, conceived of in a side-constraint way, a right to freedom of speech requires that nothing should be done to prevent actions qualifying as an exercise in freedom of speech. In short, side-constraints are moral rights conceived of as bestowing an absolute right of noninterference in the exercise of a right.

It is a conception of moral rights that, although variously articulated earlier and elsewhere as part of a long tradition in thinking about rights, finds its definitive statement and first labeling as *side-constraints* in the work of Robert Nozick. There, the conception of rights as side-constraints is presented as the reason for acceptance of an "entitlement" theory of distributive justice. But it could equally well (as Nozick would probably concede) be viewed as a concept constructed to defend such a theory. Either way, conception and theory are intimately bound up together, and accordingly, it is side-constraints in the context of Nozick's theory of distributive justice that will be outlined here.

Nozick's theory of distributive justice is strongly libertarian, uncompromisingly free market orientated, and unflinchingly antiegalitarian. The notion of rights as side-constraints fits in with such an account by making it a violation of rights (specifically, a violation of the right to liberty) to interfere with the workings of free markets to secure a more equal distribution than would otherwise prevail (or, indeed, any sort of predetermined pattern of distribution). The notion of rights as side-constraints does this by coming down on the traditionally free market liberal side of two long-standing disputes over the nature of rights.

First, and perhaps most fundamentally, by making rights absolute, the notion of rights as side-constraints requires rights to be viewed noninstrumentally as things of value in themselves rather than instrumentally as things of value only insofar as they serve a greater good of human welfare and the like. (Clearly, viewed instrumentally, rights could not be absolute, as they could be overridden by the demands of the greater good they are seen as serving.) Second, by understanding rights in terms of requiring others not to interfere in their exercise, the notion of rights as side-constraints understands them in a purely "negative" way as rights to noninterference and excludes from consideration what are contrastingly described as "positive rights," involving a requirement to receive something of benefit from others. (In so doing, it fits in with a free market liberal perspective by excluding a right to welfare provision based on need.)

It follows that acceptance of a side-constraints interpretation of rights is only as good as the above two claims about the nature of rights. Insofar as Nozick offers a defense of those claims (here as elsewhere he cheerfully admits to inconclusiveness), it is by arguing that the alternative of an instrumental and/or positive conception of rights fails to respect the separateness of persons by treating people as a resource to be used by other people. (He presents this as a restatement of the Kantian principle that people should never be treated as means but only as ends.) Such a defense can, however, be questioned at just about any level. Most directly, there is the issue of whether respecting that separateness requires acceptance of the side-constraint interpretation of rights? (Not everyone taking a Kantian approach would agree it does.) In addition, there is the issue of the extent to which that separateness should be respected in the event of conflict with other moral demands: in particular, with the common good. Most fundamentally, there is the issue of the extent to which it should be respected at all. Surely, it can be argued, morality is all about enabling people to live together in collectively advantageous ways, and so the primary focus of moral attention is people as members of society rather than, as seems to be the case with talk of the separateness of persons, the individual in isolation?

Nozick hints at what could be a possible reply to this last and most fundamental objection by suggesting that the separateness of persons should be respected because it is necessary to the fulfillment of individual life plans and, through that, the "meaning of life." But given that any such fulfillment will invariably involve others and require their cooperation, it is an explanation that arguably just brings us back to the primacy of the social over the individual in moral assessment.

—John Kaler

See also Absolutism, Ethical; Deontological Ethical Systems; Egalitarianism; Free Market; Human Rights; Instrumental Value; Intrinsic Value; Justice, Distributive; Kantian Ethics; Libertarianism; Nozick, Robert; Nozick's Theory of Justice; Rights, Theories of; Self-Ownership

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Side Payments

When two parties involved in a transaction exchange money that is not part of the transaction itself, the exchange is a *side payment.* It is typically made to induce the recipient to take part in the transaction.

The most notorious side payments are kickbacks and other types of bribes, but side payments can take many forms, some perfectly legitimate. For example, if several countries join a pact to reduce air pollution, a downwind country that has the most to gain from clean air may make a side payment to an upwind country to give it some incentive to participate in what would otherwise be a losing proposition.

Kickbacks and Commissions

Side payments raise ethical questions when they create conflicts of interest or provide incentives to break the rules. The classic example is a purchasing agent for a firm who receives a *kickback* from a vendor selected by the agent. The vendor "kicks back" to the agent some of the profits gained from the purchasing contract. This normally creates a conflict of interest, because it is in the firm's interest to award the contract to the most attractive bidder, while it is in the agent's personal interest to award it to the firm that will provide a kickback.

Kickbacks should not be confused with commissions. Someone who hires an agent, a broker, or a salesperson may pay that person a *commission* for services rendered. The purchasing agent's kickback is not a commission because it is paid by someone other than the party that hired the agent. Commissions normally do not create conflicts of interest but can do so in some circumstances. Real estate agents, for example, typically receive a fixed percentage of the sales price as commission. This may create a conflict of interest for an agent hired by the buyer, since it provides an incentive to negotiate a higher price than necessary.

There are several related types of payments that may or may not create conflicts of interest. An attorney who refers a potential client to a second lawyer may receive a *referral fee* from the second lawyer. This is not a side payment because it is not external to another transaction involving the lawyers, and there is no obvious conflict of interest. Financial advisers (or, more frequently, the banks that employ them) may receive a *retrocession payment* from a mutual fund when the adviser's client buys shares of that fund. This is a side payment but is not identical to a kickback since it normally goes to the bank rather than an individual. It can create a conflict of interest, however, since the bank may give its advisers incentives to recommend funds that pay retrocession.

Bribes, Extortion, and Facilitating Payments

A *bribe* is a payment that is intended to influence the recipient to make a decision that is not in accord with normally accepted criteria for making the decision. A kickback is a particular kind of bribe. Examples of bribes include payments to police offers to induce them to overlook a violation of law or payments to government officials to obtain a more favorable ruling in tax negotiation. (The former can be viewed as a side payment because it takes place alongside a legal, albeit not a financial, transaction.)

Bribery can be distinguished from *extortion*, which is a payment demanded for something to which one is already entitled. A side payment demanded by an electrical inspector for a permit is an extortion payment when the wiring already meets code specifications. The same is true of payments to police officers, who would otherwise report a more serious offense than actually committed, or customs inspectors, who would otherwise indefinitely delay importation of legal goods. Small or routine extortion payments are often called *facilitating payments.* In many countries, government functionaries are paid impossibly low salaries and are expected to make up the difference by collecting such facilitating payments.

The U.S. Foreign Corrupt Practices Act makes similar distinctions when it forbids U.S. citizens from bribing foreign government officials while permitting extortion payments and facilitating payments. However, the distinctions made here are not intended to correspond precisely with legal definitions.

It is sometimes unclear when gifts or entertainment should be treated as bribes, as when a potential vendor treats a purchasing agent to dinner at an expensive restaurant. Many companies bar their employees from accepting gifts valued at more than a certain amount or bearing no company logo.

Side Payments and Corruption

Bribes and kickbacks can be viewed as corrupting in the sense that they tend to undermine social norms or an economic system. Bribes can distract decision makers from their duty, and kickbacks may encourage agents to make economically inefficient decisions. However, many practices around the world that appear to be bribery, particularly to Western observers, may not be corrupting.

One example is the exchange of favors for the purpose of building a long-term relationship. This type of relationship is important in China, for example, where it is known as *guānxì* (a Mandarin Chinese word for "connection" or "relationship"). The gifts and favors are not quid pro quo and are therefore not bribes. Far from being corrupt, they build long-term, stable working relationships that are essential in a culture where mutual trust is historically more important than rules and transparency. Relationship-based business need not create conflicts of interest, as it often does in the West. A purchasing agent may favor his or her friends, but since long-term relationships are the foundation of business, it may be in the company's interest for its agents to do business with people they trust personally.

In much of the world, gifts may be culturally required to show courtesy, respect, or gratitude. It is important to know when gifts are appropriate so that they are not misinterpreted as bribes. Lavish entertainment may be a way of showing hospitality, which is a central value in many cultures.

Bribery is generally corrupting in both rule-based and relationship-based systems, but for different reasons. While bribery in the former encourages people to break the rules, bribery in the latter undermines the long-term and stable relationships on which a successful relationship-based economy depends. Bribery tends to be more common in relationship-based systems, since there is a constant temptation to take short cuts around the hard work of building mutual trust. Yet this should not be read as a signal that bribery is acceptable, just as the cheating on matters such as income taxes prevalent in the West is no indication that cheating is acceptable.

—*John Hooker*

See also Agency, Theory of; Conflict of Interest; *Guanxi*; Multiculturalism; Shame

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Sidgwick, Henry (1839–1900)

Henry Sidgwick made important contributions to ethics and economics. He argued that intuitive commonsense morality collapses into utilitarianism, comparing as he did so utilitarianism with alternative moral theories. Sidgwick also wrote on economics and argued against socialism.

Henry Sidgwick was born in Skipton, Yorkshire, in 1838; he died in 1900. He was educated at Trinity College, Cambridge, and remained at that university for his entire career. He was highly influenced by the work of J. S. Mill, especially Mill's *The Subjection of Women,* and was a great advocate of female education as well as the education of the working class. He was influential in establishing the all-female Newnham College, Cambridge, in 1871, which was one of the first colleges for women in England. Sidgwick is best known for his first major work *The Methods of Ethics.* His other works include *The Principles of Political Economy, Outlines of the History of Ethics for English Readers, The Elements of Politics*, and *Practical Ethics: A Collection of Addresses and Essays.*

Sidgwick's *Methods of Ethics* was an examination of what he took to be the three most basic methods of ethics to be found in people's common moral reasoning. The three methods of ethics—or ways of arriving through reason at an account of what should be done—were egoistic hedonism (e.g., Epicureanism), intuitional morality (understood mainly as commonsense deontology), and universalistic hedonism (e.g., utilitarianism). (Sidgwick unified both egoistic hedonism and universalistic hedonism under the term *ethical hedonism*.) In assessing these three methods of ethics, Sidgwick argued that intuitive commonsense morality collapses into utilitarianism, in particular a form of indirect utilitarianism by which it would be preferable to keep people ignorant of the utilitarian basis of morality if doing so would result in the greatest happiness for the greatest number in the long term. In addition to the substantive conclusions of *The Methods of Ethics*, this work also secured Sidgwick fame for its methodology, insofar as in it Sidgwick compared utilitarianism with its major alternatives, always ensuring that his account of each theory was historically well-informed.

Apart from his work on ethics, Sidgwick also wrote on economics, having been influenced by Mill's *Principles of Political Economy*, and has become best known for his microeconomic work on human capital and noncompetitive behavior. Although Sidgwick endorsed in broad form the claim of Adam Smith that the common welfare is best secured by each person attending to his or her own self-interest, this claim was qualified when Sidgwick addressed topics such as education, poor relief, child care, and public goods such as national defense and certain types of public works. Such qualifications led Sidgwick to consider the arguments in favor of socialism, a doctrine that he rejected on the grounds that socialistic policies would undermine a person's economic incentives to produce. He did, however, pave the way, through his work on arguments on utilitarian grounds, for a greater degree of state interference aimed at securing the greater good. In addition to his academic work, Sidgwick was also actively involved in promoting religious freedom and education.

—James Stacey Taylor

See also Bentham, Jeremy; Hedonism, Ethical; Hedonism, Psychological; Mill, John Stuart; Self-Interest; Socialism; Utilitarianism; Utility; Utility, Principle of

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Signaling

Signaling refers to market actors' use of visible attributes that convey information to or change the beliefs of other actors in the market. Because signals are under the control of the signaler, they are, at least partially, designed to communicate. Hence, signaling theory essentially captures an economic view of reputation in the market. Signals are observable proxies for unobservable attributes of individuals or organizations. For example, an individual's conspicuous consumption may be a signal of wealth and social status. Organizations may invest in reputation building to signal the greater quality of their products and services. Signals are necessary in uncertain economic environments where sellers know more than buyers (i.e., where information asymmetry exists). In this context, we must distinguish between signals and indices (such as race or gender), which generally are considered unalterable (especially in the short run). A good example of a signal is education, which may, in an uncertain world, communicate to an organization which applicants are the most productive and, thus, who will contribute the most value to an organization.

Michael Spence, whose pioneering work on signaling equilibria won him the Nobel Prize in economics in 2001, used this example of education as a signal in job markets in his path-breaking book *Market Signaling.* In the context of any labor market, the signaling equilibrium is defined as a set of conditional probabilistic beliefs for the employer that, when translated into offered wages, employee investment responses, and new market data, are confirmed by the new market data relating education levels to productivity. Hence, in signaling equilibrium, the employer's beliefs are self-confirming.

Spence showed that usually there are many signaling equilibria, not just one. The simplest case involves comparing two groups of employees where one group doubles the productivity of the other. If education is assumed to function as a signal of differential productivity, the low-productivity applicants will not invest in education at all, whereas rational high-productivity applicants will invest in that education level where the gap between the wage rate and the education cost (= cost of the signal) is maximized. However, Spence also showed that sometimes everyone would be better off if they presented themselves in an undifferentiated pool of applicants. The extent to which the market is able to find a so-called "pooling equilibrium" that still allows differentiation between the two employee groups will depend on the proportions of low- and high-productivity employees and the government's tax scheme on education. Spence showed that with the right tax scheme, such pooling can be made to fulfill the economic criterion of Pareto efficiency.

The standard explanation of signaling and its associated multiple equilibria works because the cost of that signal is negatively correlated with the attribute valued in the market. But even when education costs rise with the valued attribute (i.e., signaling costs vary the wrong way with respect to productivity), a signaling equilibrium may be attained. This outcome will be possible when the attainment of education also raises productivity to a large extent. In other words, when education is productivity inducing enough to justify its costs, the absence of a negative cost correlation does not necessarily destroy a signaling equilibrium (as initially assumed by Spence). Rather, a signaling equilibrium can still be identified. However, in this equilibrium, the private return to education falls short of the social return and hence causes underinvestment in education.

Often, the signaling hypothesis is presented as a contrast to Gary Becker's human capital theory. According to signaling theory, education serves exclusively as a signal and does not contribute to gains in productivity. In contrast, human capital theory is presented as a perspective that holds that educated people earn a return on their investments in education because of productivity gains, which lead to increases in future earnings. However, this contrast is really an oversimplification of the signaling hypothesis. Spence explicitly discussed the case when education serves as a signal *and* enhances human capital. Under those conditions, a Pareto-optimal (fully efficient) equilibrium that accurately distinguishes between high- and low-productivity employees may still exist. But, assuming a particular constellation of net benefit functions to both groups of signalers, the outcome may also lead to overinvestment in education, as was theorized in the simplified no-human-capital model of signaling.

Generally, the signaling hypothesis does not change the private benefits of education for the job applicant. It simply shifts the reason for hiring, promotion, and so on, from productivity gains to (primarily but not exclusively) the signaling function. However, from a social perspective, it may lead some observers to question a lot of investment in higher education because it represents an overinvestment under certain plausible conditions of the market signaling model.

The distinction between education as a signal and education as a way of enhancing human capital may be not only theoretically but also empirically interesting. Some research found that about half the impact of education on individuals' incomes may be due to signaling. Other research shows that education should not be overemphasized as a signaling device only, since employed and self-employed workers tend to acquire approximately equal levels of education. In other words, even groups of employees who do not need education as a signal still pursue it.

The effectiveness of signals in general depends on two attributes. First, a signal that is relatively more costly for the lower-quality types in the market tends to be more effective because this makes it more expensive for the lower-quality types to attain it and, thus, it is more likely to be used as a (valid) signal by high-quality market actors. Second, to the extent that sellers know what types of signals are used by buyers in times of informational uncertainty, they may be tempted to "fake" signals, so that the signals do not validly separate low- and high-quality market actors. This will weaken the value of the signaling device.

Although the examples in the discussion above relied on education in the traditional job market context, signaling applies to many other market contexts. In evaluating credit risk, lending institutions use personal information as signals in their credit-scoring schemes. Because of the high cost of many signals (such as home ownership), though, they de facto become indices in this context. Other contexts in which signaling occurs are selective college admissions and promotions because the informational structure of those markets are usually similar to the job market example. In product markets, warranties can be used to differentiate high- from low-quality sellers. However, in the *private* market for used cars, George Akerlof argued that lemon owners will imitate the signals of non–lemon owners, making the two types of cars indistinguishable to the buyers of used cars. In such a situation, informational intermediaries such as independent rating companies are required to resolve this signaling problem. For this solution to be effective, the signal must cost more with decreasing quality of the car and, in addition, the costs may not exceed the gains from signaling quality to the consumer.

A Business and Society research domain in which signaling was used as an explanation for market behaviors was corporate social performance. Corporate social performance may function as a signal of "employer of choice," which offers superior wages, benefits, work-life balance, and generous training and development opportunities, for example. This way, applicants can use various activities that signal social responsibility to distinguish between good and bad prospective employers. Consequently, over time, better employees who are more highly motivated are likely to migrate to employers high in social responsibility because they signal competitive advantage. Hence, regardless of the instrumentality of social performance in other economic domains, it may lead to positive economic consequences because of its signaling effect (in the minds of the best applicants). If this signal attracts more productive or creative employees that are uninterested in dysfunctional organizational politics, for example, organizations that possess this signal may, over time, outperform other organizations that do not.

Similarly, various socially responsible activities (adopted voluntarily) may serve as signals to government. Firms that deem their compliance costs with potential future government regulation to be high will adopt various self-regulatory policies and practices to secure more lenient regulatory treatment later. This signaling explanation of self-regulation leads to the prediction that the social performance of self-regulators may deteriorate when regulation is imposed.

—Marc Orlitzky

See also Asymmetric Information; Conspicuous Consumption; Corporate Citizenship; Corporate Social Responsibility (CSR) and Corporate Social Performance (CSP); Equilibrium; Game Theory; Human Capital; Information Costs; Pareto Efficiency; Rational Choice Theory; Reputation Management; Self-Regulation

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Silkwood, Karen (1946–1974)

Karen Silkwood, a union activist and whistle-blower, was on her way to submit proof of safety infractions at Kerr-McGee Nuclear Corporation's Cimarron plutonium plant in Oklahoma when she was killed in an automobile accident. Her fight for nuclear plant safety and her death became a rallying point for the fledgling anti–nuclear industry movement.

Silkwood was 26 and a divorcee with 1 year of medical technology in college when she took a job as a metallography laboratory technician at Kerr-McGee's Oklahoma City Cimarron Plutonium Recycling Facility in 1972. She knew little about nuclear power other than that it was thought to be the energy source of the future. That winter, there was a strike by the local Oil, Chemical and Atomic Workers Union, in which she played a part, but the workers were forced to return to work with a more difficult contract.

Silkwood's enthusiasm for the job waned as she learned more about the dangers of plutonium and began to notice the laxity of safety measures at the plant. She resumed her involvement with the union and, because she was outspoken in voicing complaints about plant safety, was elected to the union bargaining committee, the first woman on that committee in the history of the company. Kerr-McGee was behind on production, so employees worked longer hours and carelessness about safety increased. Because the local union did not have much support from the employees and recertification was near, she and two other union officials went to Washington, D.C., to talk with the national union officials and the Atomic Energy Commission. In preparation, she asked Kerr-McGee employees for examples of specific instances of safety violations. She divided these into three major problem areas: (1) lack of training, (2) failure to minimize contamination, and (3) poor monitoring. In Washington, she learned from the national union officials of the link between plutonium and cancer, something never mentioned at Kerr-McGee. She had by this time been exposed and decontaminated twice. She also mentioned that she had seen company employees alter negatives of the pellets to make them look perfect. The officials told her to get proof and that they would arrange an interview with a reporter from the *New York Times.* They also suggested holding an employee meeting with two professors, who talked about the relationship between plutonium and cancer. The recertification vote was held soon after the seminar, and the union won 80 to 61.

After Silkwood obtained microphotographs from Kerr-McGee's files that proved that uranium pellets were altered, she called the national union officials and arranged to meet the *New York Times* journalist. On the way to the meeting, her car crashed into a culvert, and she was killed. The highway patrol called it an accident and did not investigate further. Her folder containing the proof of pellet fixing was never found. Later, a 1984 *New York Times* report implied that the pellets had not been tampered with. Speculations about the cause of the accident and the possibility of foul play were never proven, but a federal investigation of safety and security at the Cimarron plant did take place. Kerr-McGee closed the plant in 1975. An autopsy showed that Silkwood's body was contaminated by plutonium.

In 1976, Silkwood's father, on behalf of her three children, sued Kerr-McGee for personal damages. The trial opened 3 years later in March 1979. Kerr-McGee's lawyers painted Silkwood as a loose woman who had contaminated herself in an effort to cause trouble for the company, while various investigators and company employees testified that she was rightfully concerned about safety at the plant. On May 18, the Oklahoma jury awarded the family $10.5 million. The company appealed, stating that Oklahoma had no jurisdiction because Kerr-McGee was operating under federal regulations set by the Atomic Energy Act. In 1981, the 10th Circuit Court of Appeals agreed with the company, thus reversing the Oklahoma ruling. Two years later, the case was heard by the U.S. Supreme Court. In January 1984, the Supreme Court reversed the Circuit Court's decision in a 5 to 4 vote and returned the case to the Court of Appeals. They did not, however, reinstate the damages. The Court of Appeals sent the case back to the original Oklahoma trial court. The Silkwood family and Kerr-McGee agreed to a settlement of $1,380,000 in August 1986, 10 years after the suit was filed. Kerr-McGee did not admit to liability. Silkwood's three children divided $500,000, her father received $70,000 as co-administrator, and the remainder went for administrative and legal fees.

The case set a precedent in that it allowed state courts to impose punitive damages on nuclear industry companies that were regulated by a federal agency. It also fueled rising concerns about the safety of nuclear power as an alternative source of energy. Karen Silkwood became an icon for antinuclear groups across the United States. A 1983 movie, *Silkwood,* romanticized her and portrayed her as genuinely concerned about nuclear safety. It also showed her as a real human being, warts and all, and implied that she was murdered. However, the real truth remains unknown, about Kerr-McGee's plutonium pellets, Silkwood, and her death.

—Carol H. Krismann

See also Accountability; Bhopal; Chernobyl; Hostile Work Environment; Labor Unions; Nuclear Power; Whistle-Blowing

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Single European Act (SEA)

The Single European Act (SEA) was signed in February 1986 in Luxembourg and The Hague and came into force on July 1, 1987. There were several significant provisions of the SEA that brought important modifications to the foundational treaties that had established the European Communities and were agreed to in the 1950s. The European Communities were built on the agreements of the European Coal and Steel Community (ECSC), the European Economic Community (EEC), and the European Atomic Energy Community (EURATOM). To fully appreciate the central role that the Single European Act has played in the formation of the European

Union (EU), a brief history of how the EU became a governing institution in Europe is necessary.

History of the European Union

For centuries, Europe had been the site of horrendous war and strife between its nation-states. In the 19th and early 20th centuries, for example, France and Germany went into major combat with each other no less than three times. War had become commonplace, and its toll on the area's resources and the attendant loss of life was monumental. So leaders in Europe began to see the overwhelming need to forge some long-lasting harmony and peace in the region.

After World War II, the movement toward European integration began, but it did so in rather halting steps. In the early 1950s, six countries—Belgium, Luxembourg, the Netherlands, West Germany, France, and Italy—created the ECSC, which became the first modern, wide-scale economic coalition in Europe. The ECSC served as a supranational body composed of a high authority that had regulatory powers over member states, a council that exercised legislative power, and a court that was called the "European Court of Justice." The thinking at the time was that if a consortium could be successful in managing European economic rivalry, especially the one that existed between France and Germany, then future wars might be avoided. This move toward economic cooperation was also urged by the conditions made by the United States in its "Marshall Plan," which provided $25 billion to assist Europe to rebuild itself from the ashes of World War II.

In 1951, the Treaty of Paris brought forth the birth of the ECSC. Then, 6 years later, when it was clear that economic cooperation in Europe would be possible, the member states of the ECSC deepened their arrangement and through the signing of the Treaties of Rome set up the EEC and the EURATOM. The EEC's goal was economic harmonization in Europe by the establishment of a common market and the removal of barriers to free trade. Trade restrictions, it was agreed, would be lifted in the course of 12 years, but during this transitional period the economic health of member states was so enhanced that all tariffs between them were dropped in 1968. Also on the economic front, the EEC Treaty called for a common policy on agriculture and transportation, uniform customs arrangements, agreements about the deployment of labor, and a common policy on trading with non-EEC parties. Thanks to these initiatives, the EEC became widely known as the "European Common Market," but this is not to say that Europe was a completely free market as of yet.

The Importance of the SEA

In the 1970s and 1980s, the EEC expanded by adding the United Kingdom, Ireland, Denmark, Spain, Greece, and Portugal. This was a time of economic troubles in Europe, especially with the oil crisis reaching its peak in 1973 and new pressures to compete on a global scale as the United States entered an era of more liberalized international trade. If Europeans were to rise to the occasion, then it would have to do so with a unified front that would streamline the major economic and political differences that stood in the way of a genuine integrated Europe. The SEA can be counted as the step that Europe took toward such a true union.

First, while the EEC had established a European Parliament, its role was limited to mostly advisory powers and its officials were not directly elected. The SEA gave the European Parliament expanded powers to include a veto of agreements made and on the admittance of new member states and its members to be elected directly for the first time. Second, the SEA gave more authority to the European Council that replaced the summits and conferences of the European heads of government that were held at the time. This council had limited powers and can be taken more as a way to create a unified executive branch of government that at the same time supplants the individual power of the member nation-states. Not only did the SEA make such significant institutional changes, it also made strides toward political integration of Europe. But the most important and sweeping aspect of SEA's contributions was the timetable it detailed for the creation of single European market in 1993.

With its economic provisions, the SEA began what is now the world's largest trading area. It accomplished this by permitting a genuinely free movement of goods, capital, labor, and services among and between member states. Before the implementation of the SEA provisions, there was some success toward a single market but there were still many barriers such as the differential rates of a value-added tax, and border crossings still required the completing of much red tape in the trucking industry. The SEA was the first attempt to have a Europe without frontiers by going further to ensure union than any agreement before it. In addition to introducing unitary market mechanisms—it had 272 such provisions—it set up social rights standards for workers' health and safety, set up European research and technology development strategies, and created policies designed to protect the environment as well. Hence, the SEA was a major step in the direction of establishing what we now call the European Union as it made a cohesive and harmonious economy the goal for Europe.

—Peter Madsen

See also European Union; Free Trade, Free Trade Agreements, Free Trade Zones; International Trade; Tariffs and Quotas; Value-Added Tax (VAT)

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Situation Ethics

Situation ethics is a position that holds that moral decision making is contextual or situational. It understands moral rules not as directives but as guidelines that are applicable in most situations but not all and that themselves may change or be modified over time because of their usefulness or lack thereof in varied situations. Ethical judgments must be made within the context of the entirety of the situation, and all normative features of a situation must be viewed as a whole. The guiding framework for moral decision making is stated variously as that of acting in the most loving way or acting to maximize harmony and reduce discord or to enrich human existence.

Situation ethics was developed by an Anglican theologian, Joseph Fletcher, in the mid-1960s as a result of his objections to both fixed, universal moral laws and the view that there are no fixed moral principles at all. The situation ethics of Fletcher was based on the general norm of brotherly love, which is evidenced in different ways in different situations, and he applied this to issues of Church doctrine.

For example, if one holds to the absolute wrongness of abortion, then one will never allow for abortion, no matter what the circumstances within which the pregnancy occurs. Fletcher holds that such an absolute position pays no attention to the complexity and uniqueness of each situation and can result in a callous and inhumane way of dealing with the problem. On the other hand, if there are no principles at all, then the decision is reduced to nothing more than what one decides to do in the moment, with no real moral implications involved. Rather, Fletcher holds, within the context of the complexities of the situation, one should come to the most loving or right decision as to what to do.

This view was influential in Christian communities both in America and Europe for a good number of years, but reached its peak in the 1980s and then began to wane. But while Fletcher is no longer influential, situation ethics is asserting a strong voice within the context of contemporary ethics through the position of American pragmatist philosophy, most notably through its employment of the position of John Dewey. Dewey developed situation ethics in a nonreligious context and as part of a broadly based philosophy, and it is Dewey's position that is most often used in presenting or employing situation ethics in its contemporary form.

Dewey characterizes his position as "instrumentalism" because moral principles are understood as tools or instruments that are used because they work in resolving the conflicts within complex situations in the most harmonious way for all those involved. These principles are experimental hypotheses that are constantly subject to ongoing verification or revision by the demands of the unique conditions of experience.

This view is opposed to the absolutist understanding of fixed rules as inherently valid and universally applicable to all situations, there being no exceptions. It also is opposed to the relativist understanding that there are no normative guidelines but only individual judgments concerning particular cases and that there is no moral justification for evaluating one moral claim as "really" superior to another, with ethical judgments in particular cases coming down to a "my opinion versus your opinion" kind of decision.

For situation ethics in general, moral reasoning is understood as concrete. It is not the "top down" approach of working downward from abstract rules to their application, but the "bottom up" approach of working upward from the full richness of moral experience and decision making toward guiding moral hypotheses.

Morality is to be discovered in concrete human experience where conflicting interests and desires need to be adjudicated rather than in conflicting moral principles or rights that are debated in the abstract.

This position recognizes that rules are often in conflict with each other in concrete cases and offers a way of resolving them by getting beneath them. For example, common sense tells us that in being kind or charitable one must at times "color the truth." Trying to formulate any of these precepts as strictly universal would be impossible because of the endless number of qualifications that would be necessary, many of which could not even be envisioned until they arise in some specific case in its full complexity, and every concrete case is at least a little different from any other—unique in its own way. The relative weight given to any of these guidelines, as well as to a host of other considerations in coming to a decision as to what ought to be done, will depend on the novel and complexly rich features of the situation in which the need for the decision arises. Furthermore, we sometimes have a case where specific rules just are not appropriate and we do not know what should be done, and we have to make a judgment of the individual case in light of our general wisdom of life.

Situation ethics accounts for virtues as emerging through our moral decision making in concrete situations. The most important habits we can develop, according to situation ethics, are habits of intelligence and sensitivity, for neither following rules nor meaning well can suffice. But bringing about good consequences in the contextual richness of different situations through moral decision making helps develop, as by-products, both good character traits as habits of acting and good rules as working hypotheses needing ongoing testing and revision.

According to this position, the past, with its traditions and moral rules, is to be respected, not ignored. Many of our most ingrained rules and traditions have become such because they work remarkably well, and the responsible person will pay attention to them. We make decisions and evaluations within the context of a traditional heritage that gives us a somewhat general consensus about working hypotheses from which to begin our decisions and actions. For example, in our society we tend to agree (to a certain extent, at least, and in a rough general fashion) that lying, cruelty, stealing, killing, selfishness, and so forth are to be avoided in favor of fairness, kindness, freedom, concern for others, and the like. But these can serve only as guides whose meanings are shaped and reshaped by ongoing novel situations and the conflicting values that must be integrated. Rules can change over time, and there are always exceptions to the rules.

Moral reasoning as concrete rather than abstract and discursive incorporates in its very dynamics moral sensitivity and moral imagination. Moral reasoning involves sensitivity to the rich, complex value ladenness of a situation and to its interwoven and conflicting dimensions, the ability to use creative intelligence or moral imagination geared to the concrete situation, and an ongoing evaluation of the resolution. The goal, according to this view, is not to make the most unequivocal decision but to provide the richest existence for those involved. Situation ethics emphasizes that we cannot assign priority to any one basic value, nor can values be arranged in any rigid hierarchy, but we must live with the consequences of our actions within a process of changing unique situations.

—Sandra B. Rosenthal

See also Absolutism, Ethical; Ethical Decision Making; Moral Imagination; Moral Reasoning; Pragmatism; Relativism, Moral

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Slavery

Slavery can be defined as the forced servitude of a person. In the United States, slavery as an institution ended in 1865 with the conclusion of the Civil War. Other countries ended slavery earlier or later than did the United States, and today, no country officially permits slavery. Slavery-like practices, however, still continue in parts of the world, and the effects of prior slavery represent current corporate responsibility issues for many companies. Finally, the idea of slavery is sometimes used as a metaphor by activists to criticize particular labor practices of companies and their suppliers.

It might seem strange to include an entry on slavery in this *Encyclopedia*. Slavery is often thought of as a long-ended practice relegated to history. But there are still slaves, people working in conditions where they lack true choice, and continuing controversies about the historical effects of slavery, all of which continue to this day. We are not likely to see the end of slavery as an issue for business ethics and corporate social responsibility scholarship and for business practice for some time to come.

Slavery in History

Slavery has occurred in many different cultures and countries throughout history. Slaves were often taken after war by the victorious party or as punishment for a rebellion by a colony. In Europe and the United States, slaves were captured in Africa and then exported. Although some slaves were eventually freed by their owners, most others were kept as slaves—as were their descendents—for their entire lives. Slaves have no control over their lives or their treatment.

Various abolition movements freed slaves in most countries by the late 19th century. These movements also sought (before formal emancipation) to free slaves by moving them to countries and regions that did not permit slavery. But slavery in its most formal sense is still practiced today. Robert Bales has argued that there are still millions of people who are held as slaves in many different—mostly poor—countries. In short, the contemporary view held by many people that the practice of slavery is a historical artifact is inaccurate.

Slavery and Corporate Responsibility

There are three main issues related to corporate social responsibility and slavery. The first issue involves reparations for the descendents of slaves. The second issue involves corporations that are profiting (usually indirectly) from the current use of slave labor. The third issue involves how corporations respond to allegations by activist stakeholders that particular working conditions—in their own or their suppliers' factories—are "like slavery."

With regard to slavery and contemporary corporate responsibility, slavery in its literal form is unlikely to be directly observed but is still a possible ethical issue in supplier operations. "Slavery" may also be used metaphorically to express stakeholders' concerns about particular labor practices. At the present time, the historical effects of slavery are still current issues for some corporations, but this manifestation of the slavery issue is likely to dissipate over time.

Reparations for the Descendents of Slaves

One ethical issue regarding slavery that affects corporations is that of reparations or some other compensation for the descendents of slaves. Although this has largely been cast as a public policy issue (governments providing apologies for slavery and direct reparations to the descendents of slaves), there are also calls for corporations with links to the slave trade (such as banks) or corporations that benefited in the past from such labor to pay reparations to the descendents of slaves. In the United States, as in other countries, the connections between current corporations and 19th-century chattel slavery are somewhat remote. There have been a number of lawsuits filed against companies that are alleged to have profited from slavery during that time period, but these lawsuits are not likely to succeed due to various statutes of limitations. However, the publicity that ensues from such lawsuits brings attention to the issue of slavery and its social legacy.

Slavery during the Holocaust of the 1930s and 1940s in Europe illustrates another example of a reparations movement, albeit one in which the harm and its partial remedy are more immediate. German corporations that profited from slave labor before and during World War II, along with the German government, have paid into a fund that compensated slaves and their descendents. The moral effect of such payments is that German corporations have taken some measure of responsibility for workers enslaved during the Third Reich.

The likelihood of a reparations movement succeeding is largely a function of the immediacy of the slavery. Corporations that profited from the use of slave labor in the 20th century, for example, are more likely to pay reparations than corporations that profited from the use of 19th-century slave labor. In short, the more direct and immediate the tie to slave labor, the more likely that a legal and moral case for reparations exists.

Corporations Currently Profiting From the Use of Slave Labor

Another issue affecting corporations with regard to slavery is current business activities that profit from the use of slave labor. One recent example comes from the cocoa and chocolate industries. A number of allegations emerged in 2001 and 2002 that children were being abducted, sold as slaves to cocoa farmers in the western African nation of Cote D'Ivoire, and were harvesting cocoa that was then sold to chocolate manufacturers. Research by a number of nongovernmental organizations provided evidence for such claims, which posed a significant public-image threat to chocolate manufacturers in the United States and Europe. In response, the Chocolate Manufacturers Association in 2002 created the International Cocoa Initiative, which included representatives from industry, labor, and antislavery organizations, to develop ways of eliminating the use of child and slave labor in cocoa farming. The International Cocoa Initiative issues periodic reports on its progress in the area of preventing the use of slave labor in cocoa farming.

Similarly, the oil company Unocal was accused of profiting from slavery with regard to a natural gas pipeline project in Myanmar (Burma). Myanmar, a country that has been ruled by military dictatorships for most of its recent history, was accused of enslaving people adjacent to the pipeline project and forcing them to work on infrastructure projects related to it. Unocal argued that it did not condone the use of slave labor and was not responsible for human rights violations in Myanmar. The company was sued by villagers and by human rights organizations, with some of the lawsuits ultimately being settled. Here, the allegation was neither that Unocal was itself enslaving workers nor that its suppliers were but rather that it was indirectly profiting from forced labor brought out by an illegitimate national government.

The examples of cocoa farming and Unocal illustrate how the slavery issue is likely to manifest itself for corporations today—not as an issue in which corporations are directly employing slaves but rather as a supplier issue or as an issue related to operating in countries with repressive governments. It is hard to imagine a corporation risking its reputation by directly employing slave labor in its own facilities. But in many supplier relationships—whether in commodities or contract manufacturing—the possibility of profiting from labor that is not truly free still exists. Corporations are increasingly developing codes of conduct and monitoring mechanisms to prevent the use of forced or slave labor in their own operations or those of their suppliers. Such allegations are more likely to occur in operations in lesser-developed countries, with suppliers, in commodity-oriented markets, and in politically nonfree countries.

Working Conditions That Are "Like Slavery"

Finally, the idea of slavery is used to criticize particular labor practices that are "like slavery" or "slave-like." Labor activists, for example, have used the term *slave-like* to describe labor conditions in industries such as rubber and toys. When working conditions are inhumane and workers are being mistreated, allusions to slavery by activist groups and members of the media are possible. The use of slavery as a comparative concept is meant to highlight allegations that the labor of some people is not exactly slavery but somewhat like slavery in that there is some level of coercion by an employer or a lack of freedom by an employee to choose his or her employer and working conditions.

Obviously, an allegation that particular working conditions are like slavery is incendiary. Corporations do not want to be tied in any way to allegations that workers—whether their own or their suppliers' workers—are being treated like slaves. Corporations with significant international operations and/or supply chains, therefore, have strong incentives to undertake programs and policies to ensure that workers are being treated fairly and often seek to communicate information about these programs to particular stakeholders such as consumers.

A broader issue involves defining what true freedom in employer-employee relations means. There are relatively few workers who are actually slaves, even in very poor countries. But many workers may feel coerced by economic circumstances to accept poor wages and working conditions or may wish to organize an independent labor union but cannot do so. Defining slavery is easy, but defining its opposite is considerably harder.

Slavery, Business Ethics, and the Moral Consensus

Today, there is a broad moral consensus that slavery is (and indeed always has been) morally wrong. Slavery is generally regarded as either a historical evil consigned to a prior age or a current evil that occurs in a few parts of the world and now must be ended. Most corporate policy statements, codes of conduct, industry standards, and nongovernmental organization statements on business ethics include language proscribing the use of forced or slave labor. No respectable corporation would seek to profit from slave labor, and language opposing the use of forced or slave labor has become a common part of corporate codes of conduct. Corporate and industry statements regarding slavery tend not to deal with topics such as reparations, however.

The ethical debate about slavery and corporate responsibility largely focuses not on the use of slave labor in its literal meaning but on whether particular working conditions can be appropriately compared with slave labor. In many contexts, the ability of employees to make free choices about whether, for whom, and when to work are less than ideal. Corporations' monitoring of working conditions—whether in their own plants or in facilities owned by their suppliers—and reporting are two of the mechanisms used to assure stakeholders that products are not made in exploitative conditions.

Conclusion

Slavery is both a historical issue and a current issue for corporations. The idea of slavery is morally repugnant to the overwhelming majority of people around the world. There are still controversies, however, about how to remedy the historical effects of slavery, how to prevent the contemporary use of slavery (especially in the operations of suppliers), and whether particular contemporary working conditions can be reasonably compared with slavery. Because of the moral import of slavery, corporations should seek to assure stakeholders that they only use labor—directly or indirectly—that is freely given and not coerced.

—Harry J. Van Buren III

See also Colonialism; Global Codes of Conduct; Globalization; International Labour Organization (ILO); Racial Discrimination

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Slippery Slope Argument

Two important versions of the slippery slope argument are the logical slippery slope and the causal slippery slope. The basic form of the slippery slope argument is as follows: A particular action seems to be acceptable. But if this action takes place, then another, less acceptable action, will follow. This is followed by an even less acceptable action, and so forth. For example, someone might argue that legalizing prostitution will cause more marriages to break up, which will in turn cause the breakdown of the family, which will finally result in the destruction of civilization.

The logical slippery slope argument is best illustrated by the example of baldness. Removing one hair from an individual does not make a person bald. Neither does removing two hairs, or 100. Therefore, any line drawn between baldness and nonbaldness will be arbitrary. The problem with this argument is obvious: Just because one cannot specify the number of hairs that must be removed for baldness, it does not imply that we cannot identify a person as bald. It only implies that there may be some cases in which it is a toss-up whether we can label a particular person as "bald."

A classic example of the logical slippery slope argument is found in the abortion debate. Some opponents of abortion have argued that human life must begin at conception, since no nonarbitrary line can be drawn in fetal development between conception and birth. However, this argument cannot stand on its own. It depends on a view of personhood that identifies the body at any point of development as being a person. Those who believe that personhood is present only with the coming of self-consciousness would hold that personhood comes much later in biological development than conception. More relevant to the sorites argument is the fact that just because a nonarbitrary line cannot be drawn in fetal development, it does not imply that no line can be drawn at all.

Most slippery slope arguments in ethics are causal. These are usually predictions: If one course of action is taken, it will lead to another course of action, and so on, until it results in actions that are clearly morally reprehensible. For example, an opponent of companies mining data from those who surf the Internet might argue that retrieving information that is not personally identifiable will lead to companies retrieving personally identifiable information, with the end result being a total loss of Internet privacy. This is a causal claim since the argument is that data mining of such information from Web surfers will *cause* the mining of personally identifiable information. The most plausible way to understand such causality is in a psychological sense. That is, opening the door to mining one class of Internet users' data removes psychological barriers to mining other kinds of data. The difficulty is that the claim is about what data mining companies might do in the future. It is much easier to look back in retrospect at actions and see a "slippery slope" than to make a prediction about future behavior.

However, the psychological version of the causal slippery slope argument is not as weak as it might look. In the data mining, a pollster could survey data mining companies and their workers on their attitudes toward retrieving personal information from Web surfers and whether they would in the future be willing to retrieve data traditionally considered to be more "private." Retrospective studies of companies that retrieved (perhaps illegally) personally identifying information from Internet users might be used to predict what would happen in other companies that have not yet gone that route. It is, therefore, possible that a cogent psychological slippery slope argument could be constructed, although the task would be difficult in practice.

Sometimes, in business ethics, slippery slope reasoning is used as an explanation rather than an argument. The term *slippery slope* has been used to explain how small crimes can lead a businessperson to greater corruption: "John Doe, CEO, began to take small bribes from his clients. He slid down the slippery slope to being bought off by nearly everyone with whom he was in contact." Although such a slippery slope is not an argument, with sufficient empirical support it could be a way to understand the moral psychology of a person's slide into vice, and thus useful to virtue ethics.

—Michael Potts

See also Absolutism, Ethical; Bioethics; Virtue Ethics

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Small Business Administration (SBA)

The Small Business Administration (SBA) is a federal agency whose mission is to strengthen the nation's economy by enabling the establishment and viability of small businesses and to assist communities in economic recovery after disasters. The SBA has three main strategic goals: (1) to improve the economic environment for small businesses, (2) to help small businesses to succeed, and (3) to restore homes and businesses affected by disasters. The SBA assists prospective entrepreneurs, new start-up businesses, and existing small businesses through a variety of programs and with partner organizations. The SBA was established in 1953 by the Small Business Act.

The SBA created size standards by industry type that define the maximum size that a firm, including all affiliates, may be for eligibility as a small business entity for SBA programs. The two most widely used size standards are 500 employees for most manufacturing and mining industries and $6 million in average annual receipts for most nonmanufacturing industries. There are, however, many exceptions to the size standards, and the SBA's Small Business Size Regulations should be consulted.

The SBA's programs fall into the following four categories:

1. *Small business lending:* The SBA provides loans to new and existing businesses that would not otherwise qualify for loans without the government's guarantee. The SBA's current business loan portfolio of approximately 219,000 loans worth more than $45 billion makes it the largest single financial backer of U.S. businesses in the country.

2. *Federal procurement:* The federal government strives to award at least 23% of its purchases to small businesses. The SBA assists small businesses by helping them get access to the federal procurement system. The SBA also helps government agencies use small business sources.

3. *Technical assistance:* The SBA and its partner organizations provide technical assistance programs to more than 4 million existing and potential small business entrepreneurs annually. The SBA assists new businesses by helping them navigate their way through compliance with laws and other issues in starting and running a business. Some of the SBA's partner organizations to which it provides grants include more than 1,100 small business development centers (SBDCs), 389 SCORE chapters (Service Corps of Retired Executives), and 84 women's business centers. SCORE is a network of more than 10,000 retired and working volunteers who are experienced entrepreneurs and corporate managers/executives. These volunteers provide free business counseling and advice. The SBDC offer counseling, training, and technical assistance in all aspects of small business management. The SBDC's services are delivered through a network of multiple centers and satellite locations. The SBA works to promote and assist women business owners through the Office of Women's Business Ownership. There are women's business centers located in each state and territory.

4. *Disaster lending:* The SBA provides low-interest loans to individuals and businesses that are victims of natural disasters. SBA's disaster loans help homeowners, renters, businesses, and nonprofit organizations finance rebuilding and recovery efforts. Since 1953, SBA programs have provided direct or indirect assistance to 20 million small businesses.

Ethical Issues and the SBA

Over the years, the SBA has been criticized over a variety of questionable actions including benefits to not-so-small businesses and affluent minorities. A recent scandal at the SBA involved the Supplemental Terrorist Activity Relief Act (STAR Act) passed shortly after the terrorist attacks of September 11, 2001. A federal loan program was created to help small businesses affected by the attacks. However, money was poorly managed and loans were made to small businesses not at all affected by the attacks and in some cases to small businesses that were not even in existence in 2001. Recent articles in the *Wall Street Journal* report that the SBA has awarded high-dollar contracts to large companies, but reported them as going to small businesses instead.

—Patrice Luoma

See also Entrepreneurship, Ethics of; Small Business Ethics; Social Entrepreneurship

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Small Business Ethics

Small business ethics refers to social issues and business ethics in small and medium-sized private businesses. Despite the fact that by most measures 99% of private business organizations are small or medium-sized enterprises (SMEs), probably 99% of research on business ethics and society is on large firms and multinationals in particular, giving us a very limited understanding of the relevant issues for small firms.

One of the difficulties of this subject area is the varied approaches to defining "small" business. The usual parameters include number of employees, turnover, sector-specific characteristics, and self-definition. The European Union definition is relatively simple, with small and medium-sized firms being defined as having fewer than 250 employees. The Small Business Administration in the United States offers industry-sector-specific definitions, using turnover and employee numbers ranging from 100 (for all wholesale trade industries) to 1,500 (e.g., for the airline industry). In terms of business ethics and society, the most important perspective is the differing processes and character of smaller business organizations compared with their larger counterparts. The most pertinent perspectives are outlined below.

The Freedom to Act According to One's Own Integrity

In most small firms, the person with ultimate responsibility for running the organization is also the primary owner—that is, he or she is an owner-manager. There may be other shareholders, perhaps family members or business partners, but the convergence of ownership and control of the firm means that the owner-manager acts as both principal and agent. Milton Friedman acknowledges himself that his general maxim of "the business of business is business" does not apply in owner-managed firms since the proprietor has the *right* to spend company money as she or he sees fit, including bringing personal integrity to bear (e.g., for charitable donations). There is no guarantee that owner-managers will be inherently ethical, but the frequent (though not universal) requirement to maximize profit for shareholders is less valid in the small owner-managed firm than in shareholder-owned organizations.

Not Seeking to Maximize Profit

Most owner-managers are not seeking profit maximization but are motivated by factors such as the independence of running their own firm, challenge, and providing a standard of living for themselves and their families. Acting as profit satisficers rather than maximizers may enable more ethical behavior, although there is no absolute clear causal effect, or indeed inverse effect, between ethical activity and profit.

Close Moral Proximity

Small businesses are often embedded in local communities, although there are cases that speak against this—for example, firms operating remotely from their business partners or in virtual networks. Nevertheless, for many small businesses and certainly those whose customers are locally based, physical proximity may translate to moral proximity. Furthermore, the size of the firm, lacking anonymous individuals in vast departments, means that there is nowhere to hide. If a mistake is made or a questionable action taken, it will be simple to identify who is responsible, ending very quickly with the owner-manager. This moral proximity with community and customers can focus the mind considerably on ethical behavior. Owner-managers of small firms often cite employees as their most important stakeholders, in contrast to large firms. Informality and a lack of bureaucracy is usual, with familiarity with the personal circumstances of employees the norm. Accordingly, owner-managers personally feel the burden of maintaining employees' livelihoods. Again, there is no guarantee that this results in ethical behavior, but genuine commitment to employees is very high on the agenda of small businesses, not least because the costs of replacing someone is proportionately substantial.

Reputation and Relationships

Since small firms can rarely undercut their larger competitors on price due to scale disadvantages, they have to find other ways to win business. Flexibility and a personal service are often factors on which small businesses can differentiate themselves. Indeed, the maintenance of personal relationships externally is one of the key characteristics of this type of organization because (1) it is possible due to the small number of people involved; (2) the business *is* personal; (3) since owner-managers are usually "alone" in their business, with no real peers, they often seek companionship with external business partners; and (4) cooperation with others through social capital networks is a means of accessing additional resources. Building on the notion of close moral proximity, these personal relationships are sustained by the good reputation of the owner-manager personally and the business more generally, the two being closely linked and indistinguishable in many instances.

Rejection of Externally Imposed Procedures and Standards

Given the desire for independence, the reliance on informal processes, and the sheer difficulty of maintaining a stable small business, it is not surprising that efforts to impose externally validated standards and procedures are rarely welcomed in small businesses. This includes management systems such as those pertaining to environmental, social, ethical, or human rights standards. Accreditation is often a requirement set by larger firms in the supply chain, but rarely suited to the small firm context. The additional bureaucracy is a vastly disproportionate cost for a small firm and runs counter to the usual informal management style. Similarly, the proximity of stakeholders makes mission statements and codes of conduct potentially redundant. Joining external bodies such as ethics groups and institutes also makes little financial sense and again runs counter to the independence issue. Hence, "measuring" ethics by counting up what standards the organization is signed up to or membership to ethics organizations is nonsensical.

The Importance of Sector

The one external group to which SMEs are likely to be affiliated is their sector or trade organization. Owner-managers are notorious for disliking taking advice from any external organization with which they don't have a personal relationship, but if they accept it from any one institution it would normally be their trade association. While small businesses may be relatively invisible in the media and the public eye, in many cases they will not be so in their sector, where trademarks and quality standards are most likely to have meaning and, again, reputation is key. Related to this is the fact that competitors (in similar sized firms) are often seen more as industry colleagues than enemies. As a result, unlike in large firms, small firms often count competitors as stakeholders to whom they have a moral obligation.

Character of the Owner-Manager

There are some who argue that "entrepreneurs" have a more highly developed cognitive moral development than other business managers. Leaving aside the confusion around the fact that not all owner-managers are entrepreneurial in the financial-growth sense and that entrepreneurs need not run small firms, there is some degree of convincing argument that those running their own business often possess a high level of integrity. It may be that the factors mentioned above, in particular moral proximity, independence, the concern for reputation, the reliance on external networks, and ultimately the responsibility of running your own business, could be interrelated with high levels of integrity.

The above is very much a generalized list of the most important issues relating to ethics and society pertinent in smaller firms compared with their larger counterparts. There are a number of factors that would influence this list. These include the stage of the business (some suggest that business start-up is a time when trust and integrity are compromised); the character and presence or otherwise of the founder; whether the business is a family business (in which case a whole host of additional personal responsibilities and obligations come into play diminishing the independence of the owner-manager, although enhancing the support available to them); sector differences; and national, regional, religious, and ethnic community culture.

While the picture painted above is rather positive about the ethics of small businesses and their owner-managers, it should be viewed against a backdrop of the enormous pressure that they are under to simply survive, as evidenced by the high failure rates. Indeed, during start-up phases, it has been found that owner-managers may well exploit trust relationships (such as previous employers) to get established. Unfortunately, the precise connection between external pressures and ethics in small firms is unclear.

Finally, given the difference between large and small firms in relation to business ethics and society, how might they be influenced and encouraged to act responsibly? The indications are that working through trade sector associations will be most effective, but further empirical research is needed that takes into account those most able to comment on small business ethics—that is, the key stakeholders of customers, employees, competitors, neighbors, family and friends, and the owner-managers themselves.

—Laura J. Spence

See also Cognitive Moral Development; Entrepreneurship, Ethics of; Integrity; Small Business Administration (SBA); Social Entrepreneurship

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Smith, Adam (1723–1790)

Adam Smith is one of the most influential systematic social philosophers in the history of Western civilization. He founded political economy (now economics) as an independent discipline. Smith was a quiet radical, arguing against the status quo, whose observations of human nature and economic activity in Scotland and England continues to influence public policy during the current age of globalization. Smith's first book, *The Theory of Moral Sentiments,* provides the ethical foundation for capitalism. His second book, *An Inquiry into the Wealth of Nations,* provides a wealth of empirical evidence justifying the social benefits of a free market economy.

Background

Smith was born in Kirkcaldy, Scotland. His father, the seaport community's Comptroller of Customs, died 6 months before he was born. Smith's mother, assisted by tutors and wealthy guardians, ensured that her only child received a classical English education that emphasized the virtues of hard work and self-control. He was prone to illnesses and suffered from hypochondria as an adolescent and adult.

At the age of 14, Smith entered the University of Glasgow and studied moral philosophy under the guidance of Francis Hutcheson. While living in Glasgow, he observed the negative impact of protectionist policies and the benefits of free trade with the Americas. At the age of 17, he received a scholarship to attend Balliol College, part of England's Oxford University system, where he studied for the next 6 years.

After graduating from Oxford, Smith became a tutor and gave public lectures on rhetoric, moral philosophy, and law in Edinburgh, the capital of Scotland. There he became lifelong friends with the controversial atheistic moral philosopher David Hume, who was 12 years older than Smith. Much of Smith's later work in ethics built off Hume's writings. Hutcheson, Hume, and Smith were central figures in the Scottish Enlightenment (1740–1800). These three creatively systematic Scottish social philosophers helped to construct the ethical foundation of political and economic liberty in Western civilization.

The Theory of Moral Sentiments and *Wealth of Nations*

Smith obtained a teaching position at the University of Glasgow in 1751, where he became Professor of Moral Philosophy. He taught classes in natural theology, ethics, jurisprudence, economics, and politics. His lectures served as the basis for *The Theory of Moral Sentiments.* In this book, Smith develops his own science of morality based on the tensions between individuals' tendencies to be both self-interested and other-regarding. He concluded moral judgments are formulated by taking the role of an impartial spectator.

The immediate popularity of *The Theory of Moral Sentiments* attracted the attention of Charles Townsend, a volatile English politician who had served as secretary-at-war and was the president of the Board of Trade at the time. Townsend would later author the Tea Act, which led to the Boston Tea Party uprising.

In 1763, Smith accepted a lucrative position tutoring Townsend's 18-year old stepson, the Duke of Buccleauch, for 3 years. Together, they traveled to France and Switzerland, where Smith studied their political and economic systems, discussed contemporary issues with leading intellectuals, and began writing *Wealth of Nations.* Smith returned to Scotland in 1767 and continued writing his economic treatise, integrating historical, anthropological, sociological, political, scientific, and economic information; it was published in 1776.

In *Wealth of Nations,* Smith maintained that no society could flourish when a major portion of its population was poor. He concluded that government should not sanction monopolies. Instead, it should provide citizens the liberty to pursue their own economic interests to compete in business and labor markets, so long as they did not harm others in the process. Smith restricts the duties of government to providing a national defense, a system of justice, public works, and education.

Later Years

Smith spent his remaining years revising editions of *The Theory of Moral Sentiments* and *Wealth of Nations.* He also served as commissioner on the Customs Board for Edinburgh, where he dealt with local economic issues, such as determining taxes on imported and exported goods, raising revenue in a fair manner, and smuggling prevention. Smith started writing two other books, one on jurisprudence and the other on a philosophical history of literature, but he destroyed both manuscripts shortly before his death.

—Denis Collins

See also Capitalism; Competition; Empathy; Free Market; Hume, David; Invisible Hand; Liberalism; Self-Interest

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Social Accountability (SA)

SA is the process of assessing and reporting a business's performance on fulfilling the economic, legal, ethical, and philanthropic social responsibilities expected of it by its stakeholders. While corporations have long been held responsible to investors and stockholders, many firms and stakeholders now advocate an expanded view of this accountability, which includes reporting on the role of business within broader society. SA is part of a movement known as SEAAR, the acronym for social and ethical accounting, auditing, and reporting.

Verifying Social Commitment

Social audits, SA reports, and corporate citizenship audits are common names for tools that companies employ to identify and measure their successes and ongoing challenges with social responsibility. Regardless of the name, these reports are important for demonstrating a firm's commitment to ensuring the continuous improvement of its social responsibility efforts. Thus, SA has to be treated similarly to any other corporate initiative in terms of budget, assessment, and executive commitment. Without reliable measurements of the achievement of social responsibility objectives, a company has no concrete way to verify their importance, link them to organizational performance, justify expenditures, or effectively address stakeholder concerns.

Therefore, a key issue with SA is the way in which companies measure, represent, and report on their social responsibility activities and stakeholder relationships. SA reports are currently voluntary, as no law or regulation requires a specific reporting method or verification of the report's claims. Thus, SA is not subject to internal auditing standards and external assurance practices that accompany financial statements and related reports. However, some firms seek independent verification of the SA report. Major accounting firms and other consultants conduct assessments and attestations as to the accuracy and completeness of such reports.

Since this type of verification is rare, critics worry that some SA reports are merely public relations efforts that contain disinformation and distortions. Critics also question the extent to which companies may use these reports to enhance their reputations rather than as tools for sincerely improving stakeholder relationships.

SA8000 Certification

To remedy these concerns and to create a best practices approach, there are several organizations devoted to ensuring SA within the global marketplace. Social Accountability International, formerly known as the Council on Economic Priorities Accreditation Agency, seeks to create and refine consensus-based ethical workplace standards, accredits qualified organizations to verify compliance with these standards, and promotes the understanding and implementation of social performance standards worldwide. SAI developed and supports SA8000 certification for assuring humane workplaces. SA8000 covers eight primary elements: (1) child labor, (2) forced labor, (3) health and safety, (4) freedom of association and right to collectively bargain, (5) discrimination, (6) disciplinary practices, (7) working hours, and (8) remuneration.

Each of the areas includes a number of specific criteria that must be met for a facility to be certified. For example, in the case of disciplinary practices, a facility must demonstrate that it neither engages in nor supports corporal punishment, physical or mental coercion, and/or verbal abuse of employees. The remuneration category requires a facility to compensate employees fairly and legally, communicate clearly about wages and benefits, and ensure wages are sufficient to meet the basic needs and some discretionary choices of its personnel.

In mid-2005, there were nearly 800 facilities certified as SA8000 compliant. These facilities are found in 47 countries, represent 54 industries, and employ more than 450,000 employees. India, Italy, China, and Brazil have the largest number of certified facilities. The industries most prevalent include apparel, textiles, chemicals, and transportation.

AA1000 Process Framework

AccountAbility is another organization dedicated to advancing the area of SA. This group, which was formally known as the Institute of Social and Ethical AccountAbility, performs research to find best practices in corporate accountability, promotes the development of accountability competencies in various professions, works with public policy makers, and promotes effective accountability tools and standards. The AA1000 framework is designed to improve corporate accountability and performance by learning through stakeholder engagement. In this framework, accountability includes transparency, responsiveness, and compliance.

Much like quality control initiatives, AA1000 is focused on processes and principles rather than substantive issues. Thus, AA1000 does not prescribe performance on ethical issues (i.e., child labor) like the SA8000, Coalition for Environmentally Responsible Economies (CERES), Caux Principles, and other issues-based standards. The key process elements of AA1000 include planning, accounting, auditing and reporting, embedding, and stakeholder management. AccountAbility has published a number of other helpful tools, including an assurance standard for assessing materiality, completeness, and responsiveness of an organization's social report and the processes that inform its reporting.

Gap Inc.'s Social Responsibility Report

A number of well-known corporations have published SA reports. Gap Inc. is an international retailer offering clothing and other items under the Banana Republic, Old Navy, and Gap brand names. Along with the traditional corporate annual report, Gap Inc. also published a separate social responsibility report that reflected its activities between February 2004 and January 2005. The 60-page report included a short financial overview and focused on four major social responsibility issues: (1) labor conditions and certification issues within its supply chain and manufacturing sites; (2) core values and ethics training for employees; (3) community involvement and philanthropy through the Gap Foundation; and (4) environmental, health, and safety standards in the firm's manufacturing and retailing operations. To provide assurance for the accuracy of its report, the Gap incorporated specific examples, photographs, the results of stakeholder outreach sessions, and comments from external consultants.

Beyond SAI and AccountAbility, other nonprofit organizations, membership groups, consumer advocates, and companies are devoting efforts to increasing SA. Stakeholders are demanding increased transparency and are taking a more active role in gaining information from companies. Corporations are communicating about their social responsibility via published reports and Web site material. Government regulators are calling on companies to increase the quantity and quality of information disclosed. All these efforts are aimed at increasing companies' SA as well as access to accountability information.

—Debbie M. Thorne

See also Accountability; Caux Principles; Coalition for Environmentally Responsible Economies (CERES); Global Reporting Initiative; Stakeholder Engagement; Triple Bottom Line

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Social Activists

Social activists are people who aim to bring about change in the social, political, economic, religious, environmental, or military policies of an organization or society by staging public protests and rallying social support for their cause. They generally claim to represent the views and concerns of other citizens, thereby acting not only for their own interests but also in the interest of creating a better society for all those concerned. The desired improvement could be more jobs, higher wages, lower prices, safer working conditions, more equitable laws or law enforcement, environmental protection, the end of military action, or any other goal perceived to be vital to the well-being of society. These particular goals were among the motivating forces for significant social action movements that shaped the United States during the past century.

The history of social activists is a venerable one, although those who are willing to publicly challenge contemporary policies and the status quo frequently face derision and harsh criticism, if not loss of livelihood and social acceptance. Arguing for social change inevitably pits activists against those whose interests are vested in the established policies and practices. Some activists have staked and lost their lives while working to achieve their goals.

Notable historical social activists include Henry David Thoreau, who went to prison for a night for his refusal to pay taxes that would support governmental policies he disagreed with. Thoreau's 1849 essay "Civil Disobedience" pioneered the teaching of nonviolent deliberate resistance as a means of reforming objectionable laws. Mahatma Gandhi's independence movement in India against British colonialism involved long marches and hunger strikes in his effort to work collectively for peaceful change. The civil rights movement championed by Martin Luther King Jr. during the 1960s drew guidance and inspiration from Gandhi's methods. Civil disobedience was widely adopted by protestors supporting the racial integration of schools, buses, restaurants, and other social institutions. Despite King's strong advocacy of peaceful change, he was killed by those who hated his message of racial justice.

Other important social activist groups include ACT UP, a group dedicated to achieve lower prices and increased access to AIDS medication, and Greenpeace and Earth First!, two groups of environmental activists willing to engage in extreme acts of sabotage to protect the environment and intimidate those seen to be acting against nature's interests, for example, loggers and oil companies. Antiwar protests during the Vietnam War gathered support across generations and social classes to dramatically influence public opinion and ultimately U.S. policy regarding the war. Subsequent wars have also evoked antiwar protests, albeit on a much smaller scale than the Vietnam protests.

Contemporary businesses have felt the impact of social activists, although the recruiting of public support now occurs electronically more than through street marches. Most social change groups have extensive Internet mailing lists to share information and raise money more quickly and directly. The status of social activists as stakeholders has been debated but is not yet fully explored. Many corporations have learned by experience that they must take the concerns of activists seriously and respond carefully. The protests staged by social activists over the use of child labor, investments in repressive regimes, support or lack of support for benefits for domestic partners, exploitation of environmental resources, and numerous other issues have proved to have an economic impact that cannot be easily ignored. The actions of these groups serve as a vital component in maintaining the balance of power between citizens, governments, and social institutions in market-driven societies.

—Robbin Derry

See also Animal Rights Movement; Boycotts; Child Labor; Civil Rights; Consumer Activism; Exploitation; Gay Rights; Living Wage; People for the Ethical Treatment of Animals (PETA); Shareholder Activism; Sweatshops

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Social Audits

Social auditing refers to the process of identifying, analyzing, measuring, evaluating, and monitoring the impact of an organization's operations on different stakeholder groups. The auditing process is carried out in five steps.

First, an exhaustive enumeration of the organization's social activities is compiled into a social data bank. Since compiling such a data set may prove to be a daunting task, due to the wide range of social activities that the organization performs, a lengthy and well-planned study may be required.

Second, the compiled data are analyzed such that the meaning and cost-benefit ratios of the social activities may be inferred. Analysis is conducted by using sophisticated statistical analysis tools and expert judgment.

Third, the impacts of the organization's activities on different stakeholder groups are measured. Since measures of social effects are not as well-developed as economic measures, proxies such as opinion and attitude measures are usually used.

Fourth, social performance is evaluated. The effectiveness of the organization's social activities is assessed by comparing actual performance to standards developed using norms and goals. The more clear and specific the norms and goals are, the more accurate the evaluation is. Fifth, continuous monitoring of social effects is maintained.

The success of the social audit depends on the accuracy of the steps discussed above. In addition, three recommendations need to be met. First, the social audit needs to strictly adhere to the selected norms and goals used as standards in the evaluation step. Second, the results of the social audit need to be integrated into the decision-making process of the corporation in the form of feedback as an integral part of the management of the company's social activities. Third, the social audit has to be carried out by competent and skilled professionals who are knowledgeable of the relevant social issues and problems.

The Evolution of Social Auditing

As different stakeholder groups, especially interest groups, increased their pressure on business organizations to pursue more socially responsible goals, and as the notion of corporate social responsibility gained more acceptance, business organizations started responding to their stakeholders' demands. Businesses' responses materialized in efforts such as natural environment awareness programs and equal employment opportunity initiatives. However, a suspicious public demanded measures to assess businesses' social impact, similar to the economic measures that assess a corporation's economic impact. Corporate social performance had to be accounted for. Simply portraying a socially responsible image through a corporate public relations office was not enough any more. The need for a rigorous process that accurately assesses corporate social performance and holds corporations accountable for their practices was clear. Time has come for social auditing.

Types of Social Audits

Research and practice produced several types of social audits. There are six major types of social audits: (1) the social balance sheet and income statement, (2) the social performance audit, (3) the macro-micro social indicator audit, (4) the constituency group attitudes audit, (5) the government-mandated audits, and (6) the social process/program management audit. These six types of audits vary with respect to the intent for which they are conducted, the methods used, the scope covered, and the audit report form. In addition, the group conducting the audit varies among the several types. Following is a brief summary of the six major types of social audits.

The Social Balance Sheet and Income Statement

Similar to a financial balance sheet and income statement, the social balance sheet and income statement represent the social costs and benefits in dollar terms. This type of social audit attempts to parallel the methods of financial accounting. However, the lack of generally accepted standards and guidelines represent a major weakness of this type. In addition, in the absence of generally accepted standards and guidelines, assessment of the audit is at best subjective, if at all possible.

Two versions of this audit have been proposed, the first by Clark Abt, of Abt Associates, and the second by David Linowes, a certified public accountant. Two main differences between the two versions are with respect to audit scope and the group conducting the audit. First, the scope of the Clark Abt version of the audit is the whole company. In contrast, the scope of the Linowes version is the company's voluntary activities. Second, the group conducting the audit, for the Abt version, is composed of an external expert team. The Linowes version, on the other hand, is carried out by a team internal to the organization.

The Social Performance Audit

The social performance audit is carried out through a study of select companies in given industries. The audit results in a critical evaluation of the companies' social performance aimed at influencing investment decisions. Social issues such as environmental pollution and minority personnel policies are usually targeted. External critics conduct the audit. The Council on Economic Priorities and the Interfaith Center on Corporate Responsibility are the main two organizations that support and use this type of audit.

The Macro-Micro Social Indicator Audit

The micro-macro social indicator audit is a quantitative audit that uses both social indicators and indicators of the social performance of companies. The macro social indicators reflect the actual and desired general well-being of a community in general. Areas such as health and safety, education, and housing are usually covered. The micro social indicators, on the other hand, assess a single company's performance in any of the areas covered by the macro social indicators. Using these measures, two types of comparisons may be conducted. The first aims at assessing a single company's progress. To achieve this aim, the social performance of the company in a given year is compared with its performance in previous years. The second contrasts a company's performance to the performance of other companies or the industry as a whole. External or internal experts may carry out the audit. The major strength of this type of social audit is the use of quantitative measures that enables the public to systematically evaluate a company's social performance.

The Constituency Group Attitudes Audit

Most suitable for corporations that interact with different stakeholder groups, also called corporate constituency, the constituency group attitude audit identifies and measures the stakeholder attitudes. The information gathered about stakeholder attitudes and preferences is then used to help corporations better manage social pressures from the different stakeholder groups. An external team of experts carries out this audit. The audit may cover the activities of the whole company or activities of areas of concern.

The Government-Mandated Audits

The government-mandated audits, as suggested by its name, are a type of audit that is required by different agencies of the federal government or by local and state governments. The most notable agencies of the federal government that have required this type of audit are the Environmental Protection Agency, the Equal Employment Opportunity Commission, and the safety and health administration.

This type of audit focuses on corporate performance in specific areas such as environmental pollution, minority personnel practices, and workplace safety. Corporate performance is expressed in numerical and statistical terms. The scope is either the whole company or a division. An internal team conducts the audit on behalf of the overseeing government agency.

The Social Process/ Program Management Audit

This type of audit aims at assessing the effectiveness of select organizational programs that are considered to have a significant social impact. The social process audit, also called the program management audit, unlike other types of audits that focus on program outcomes, takes a holistic approach to assessing program effectiveness. First, antecedents and program development processes are evaluated. At this step, the factors that led to the development of the program are the subject of evaluation. Such factors usually are in the form of organizational and environmental forces that affect corporate decision making. Second, program goals are evaluated. Similar to the first step, the effects of organizational and environmental forces are considered. Third, the transformation process where inputs to the program are transformed into outputs is evaluated. Finally, the program evaluation process itself is assessed.

The standard against which the effectiveness of the program is compared is the set goals. In other words, the actual outcome of the program is compared against the set goals. The evaluation process uses both quantitative and qualitative measures. Quantitative measures such as cost-benefit analysis are used. Qualitative measures, on the other hand, are concerned with the description and analysis of program activities. The two main organizations that are responsible for this type of audit are the Social Audit Research Group at the Graduate School of Business at the University of Pittsburgh and Bank of America.

Corporate Social Accounting, Auditing, and Reporting

Concerned with corporate social responsibility and performance, David Hess argues that further steps need to be taken beyond the current state of social auditing. He proposes the Social Accounting, Auditing, and Reporting (SAAR) system. Under SAAR, the corporation will not only be required to disclose select aspects of corporate social performance but will also be required to put in place a systematic process for evaluating corporate performance. SAAR has four general requirements or characteristics. First, it must be stakeholder oriented. Stakeholder orientation is manifested through (1) taking into account the views of all stakeholder groups, (2) developing a dialogue between the corporation and its stakeholders, and (3) handling the competing views of the different stakeholder groups. Second, the SAAR system must encompass a set of established procedures and policies that ensure effectiveness. Third, the report and the findings of the audit must be verified by independent auditors. Fourth, the report must be disclosed to corporate constituencies in an intelligible and accessible manner. Preferably, the report should be published annually, thus allowing for utilization of the feedback in the next auditing cycle.

Challenges of Conducting a Social Audit

Various factors may interfere with the auditing process and, accordingly, affect its success. These factors may be classified into four main categories—attitudinal, organizational, political, and technological challenges. First, attitudinal challenges are posed by individuals within the organization. Their attitudes toward and acceptance of the audit would influence the process and its outcomes. Personnel attitudes may affect the decision of which programs are to be audited, getting permission to audit, gaining access to the data, and determining how the audit results are to be used. Positive attitudes toward and acceptance of the audit normally would facilitate the process and enhance its effectiveness. Second, the organizational challenges that face the audit refer to those organizational forces that would influence the direction and effectiveness of the audit. Third, the political challenges posed by different interest groups might push the audit away from its rational path. Fourth, the technological challenges are mostly measurement problems: What should be measured, how should it be measured, and which standards should be used?

Critics of the Social Audit

Given the above-stated challenges that face social auditing, some critics argue that due to the lack of standards and generally accepted rules and regulations, the social audit is merely a tool that some corporations use to portray a positive image of social responsibility. The legitimacy, accuracy, reliability, and validity of the audit are questionable at best.

Advocates and Supports of the Social Audit

In spite of the challenges and criticisms directed at the social audit, some companies remain committed to this practice. One of the most widely known social audits is that of Ben & Jerry's, an ice-cream company well known for its social responsibility and philanthropic activities. Ben & Jerry's has published its social audits since 1999 on the Internet. Also, the company's Web site clearly reveals its commitment to corporate social responsibility.

—Kareem M. Shabana

See also Corporate Accountability; Corporate Citizenship; Corporate Ethics and Compliance Programs; Corporate Social Responsibility (CSR) and Corporate Social Performance (CSP)

Further Readings

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Social Capital

Social capital can be thought of as the stock of social trust, networks, norms, and generally the interconnectedness and strength of relationships among individuals in organizations and communities. Social capital is important since higher levels of social capital are related to the health and prosperity of individuals, organizations, and communities. Social capital might be thought of as the glue that holds members together and enables members of a community to accomplish their goals and solve their problems.

The dictionary defines *capital* as wealth in any form that can be used to produce more wealth. *Wealth* should be understood here as not just money but any asset that is valued and accumulated, including effective goal attainment, happiness, group stability, and peace, or perhaps friendship, love, and affection among members of a group.

Capital or wealth comes in various forms. We might distinguish the following forms of capital:

- *Physical capital*—physical tools or items that increase productivity (e.g., a computer)
- *Human capital*—the knowledge and skills that improve productivity (e.g., the knowledge resulting from an MBA curriculum)
- *Financial capital*—accumulated money that enhances opportunities (e.g., loans or savings to begin a new start-up business)
- *Social capital*—the stock of social trust, networks, norms, and generally the interconnectedness that enable communities to deal more effectively with common problems and issues (e.g., a quick response of volunteers to assist victims of a flood disaster)

Social capital is as old as human social grouping. Alexis de Tocqueville did not use the term but captured the essence of *social capital* in his famous discussion of the propensity of Americans to form civic associations. As an academic concept, social capital can be traced to early in the 20th century. However, the concept became more widely studied and popularized in the 1990s, in particular from the work of Robert Putnam, who argued through systematic empirical analysis that there has been a steady decline of social capital in the United States since the mid-1960s.

Some forms of social capital bond together members of groups or organizations. Such organizations include informal neighborhood groups, organized sports teams, recreational clubs, social clubs, professional groups, community groups, or business organizations. There are usually relatively clear expectations for behavior among members of the group, and higher levels of social capital tend to result in higher levels of enjoyment and trust for members of the groups. These kinds of groups tend to involve individuals who are generally more homogeneous. They create what has been referred to as *bonding social capital.* In these settings, social capital functions as the bonding agent that holds the members together.

Other forms of social capital bridge differences among groups that may be different in some respects (e.g., language, culture, religion). But members of these groups have relatively trusting relationships for purposes of achieving common community purposes. Thus, these forms of social capital have been referred to as *bridging social capital.* These forms of social capital are particularly important in pluralistic societies, and in these settings, social capital might be thought of more as the grease that allows differing groups to find common ground and acceptable solutions to common issues. Thus, pluralistic and democratic societies depend on bridging social capital, as do global business partnerships and global business dealings generally. These bridging forms of social capital are generally more difficult to create and maintain, but they are extremely important in terms of healthy global business environments.

There are various aspects and implications of social capital. One aspect of capital is that it tends to accumulate with use and increase future capacity and wealth. For example, using the latest technology in farming can increase the amount of land farmed or increase the time available for other productive enterprises, thus resulting in greater wealth and further productive investment. Likewise, using the stock of social capital to deal with community problems (e.g., aiding one another after a natural disaster) may solidify relationships, trust, and a spirit of togetherness that can help produce compromise and consensus related to future community issues (e.g., a proposed school bond issue that may be controversial).

There are other social implications regarding social capital. Strong networks of social capital make it more likely that members will cooperate for mutual benefit, and conversely, weak networks make it less likely that cooperation will be possible, thus reducing their ability to address effectively community problems. Groups with stronger social capital have greater social wealth because their networks foster reciprocity norms. There will be ongoing give and take and hence sufficient trust such that giving will be repaid at a later date. There are also generally effective communication and coordination channels for the effective flow of information and perceived transparency to verify and test behavior. There is also generally a history or tradition of collaboration that establishes a base for future collaboration and problem solving.

Originally developed as an attribute of societies and political communities, social capital can by extension be considered a characteristic of organizations and businesses, as well as individuals. Individuals who have strong or dense relationships in a community or organizations may be said to have more social capital. Such individuals are able to attain more of their goals and contribute more effectively to organizational goals because of the strength of their connectedness.

Likewise, business and other organizations can be described as having greater or lesser amounts of social capital. It is expected that those businesses and organizations with higher levels of social capital will be more effective, productive, and profitable. Such organizations will ultimately be more sustainable. Management can take actions to foster and increase trust and social capital in organizations. Prusak and Cohen have suggested various strategies for management. The first set involves helping employees make and retain connections. Included in this set would be giving employees time and space to bond in person; promoting within the organization; facilitating personal conversations through things such as cafes, kitchens, and libraries and encouraging interactions in nonwork activities. Another category of initiatives would be to enable trust among employees and managers by keeping things transparent and giving no reason to distrust, empowering employees to use their own judgment and thereby showing trust in employees, and translating the trust into reward (such as promotions). Finally, Prusak and Cohen suggest that management foster cooperation among members of the organization by giving people a sense of common purpose, establishing rules for cooperating, rewarding cooperation with cash rewards, and hiring the kinds of employees who are likely to be cooperative players.

—Dennis P. Wittmer

See also Intellectual Capital; Networking; Social Contract Theory

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Social Contract Theory

While there has been a revival of interest in the "social contract," the idea is a very ancient one, with more than a nod given to it in Plato's *Republic* and in the writings of Epicurus, for example, and then again in a great explosion in the 17th and 18th centuries. We also encounter considerable variation, and controversy, in the idea: first, in what it is an idea *about*, and second, in just what the "contractual" element is supposed to consist.

Regarding the first point, the two main options are (1) that it should be exclusively a theory of *politics* in particular or (2) that it should be more generally a theory about moral relations in society as a whole. In the first view, people agree on how they shall be governed by some institutional system of people occupying positions of political power. In the second, however, no one is the "governor"; rather, we agree on a set of *principles* by which we will regulate our interactions. In effect, the second views the social contract device as a means of grounding, and supplying substance to, *morality*.

How different are the two interpretations in this respect? It is difficult to see why we would agree on who would govern us or in what form if we did not also have in mind certain general principles that we expected those forms to exemplify, uphold, or be constrained by. Thomas Hobbes (1588–1676), the first and widely considered to be the greatest of the early modern contractarians, argued that in the absence of government we would all be abjectly miserable, as well as very short-lived, and that the cure for this was to identify some person or small group of people to whom we would turn over our independent liberty of action, thus authorizing a force powerful enough to "overawe" any subgroup of troublemakers and enable people in society to get on with their various projects. That the resulting rulers might prove to be dictators with motives very contrary to what we might like does not seem to have worried him overly. But in light of the 20th century with its Stalins, Hitlers, and Maos, we are all worried about that. And Hobbes, in fact, did supply a remarkably interesting principle: his "first law of nature," which he elaborated into a set of "Laws of Nature" that he supposed the "leviathan" created by social contract would actually fairly well adhere to and enforce among the rest of us as well.

The Hobbesian first law of nature advises us that everyone is to seek peace, as far as possible, and when one cannot get it, then and only then may one proceed to use the methods of war. This powerful idea is closely echoed by most of his successors, including Locke, Kant, and John Stuart Mill. War, reasoned Hobbes, was the problem; peace, therefore, is the solution. War is the problem in the specific sense that if people spend their time and energies fighting, they will be unable to achieve the benefits of cooperation: industry, learning, navigation, agriculture, commodious buildings, arts, letters, or society.

We can readily impute to Hobbes the idea that this first law of nature is itself essentially a "social contract." For it tells us all to seek peace, provided that others do too, and it is recommended as being a good deal for those who participate. Hobbes defines a law of nature as a "precept of reason" that forbids any individual to do what destroys his or her life (meaning the sort of life he or she is trying to live and not just longevity on any terms), or the means of preserving it, and to omit what would best preserve and forward it. This idea of law is purely individual. But its content concerns our relation to all others when those others can be obstacles to the preservation of our life or alternatively sources of support and preservation to it. And they always can be—especially the first—obstacles; so it is in our mutual interests to adopt as a law the forbidding of interpersonal violence, which will be effective insofar as we are rational enough to see the prospect of loss from war and gain from peace.

And why would people be unable to cooperate in the "natural condition?" Why would war break out instead? In Hobbes's account, it is for two related reasons. One is that it could easily appear to people that they could get what they need from those who already have it rather than trying to make it by their own labors. The other is that to cooperate, we need to trust each other, but the nature of cooperation is such that it tends to lay one person open to exploitation by the other, who will "take the money and run" instead of fulfilling his or her part of the bargain. But if agreements can't be relied on, then there's no point in making them—in which case, of course, we couldn't have any of the things that cooperation is necessary for making, which is almost everything valued in society.

Morals to Politics?

The Hobbesian scenario exemplifies the most central ideas of the social contract. First, it embodies the idea that moral restraints are things we *might possibly not have had:* They are not hardwired into the human frame (as they are, he suggested, in bees). So if we are to have them, we must somehow create them among ourselves. And second, there are only our own interests and wants to guide us: Gods and natural laws—as formerly conceived—simply are not in the picture. People are depicted as largely self-interested, so that if we are to have a workable society, it will have to be one that works *in everyone's interest.* Any natural laws will be based on this fact of human nature rather than on any supposed built-in moral features of the world.

Contracts are excellent models for this undertaking. They are made in self-interest: Each party to them is motivated by some interest of his or her own rather than, for example, by love, common feeling, or group identity. And so contracts inherently present a problem of trust that must somehow be overcome. For we each provide something to the other, and this, so far as it goes, is a cost to the providers; in return, we get the benefit of the other part's performance—if that party does in fact perform. But if one performs first, how do we get the other one to do his or her part when the time comes? That is the problem, and Hobbes supposed that the sovereign was the solution: We have the police watching over things to keep both parties in line.

The Political Version

Modern work on the social contract shows that Hobbes was wrong in thinking either that the sovereign would in fact solve our problem or that we could actually create the state to solve it. On the other hand, it has gone far in explaining why Hobbes was mistaken about the extent of the problem as well as the means for solving it. In fact, self-interest will carry us very far under circumstances that are not at all unusual. In particular, when we envisage continued future relations, it is obvious that if we can't be relied on this time, there will be no next time—and yet "next times" are precisely what enable us to advance. And so we stay at the job, even though we could this once rob the till and depart. Furthermore, there are mechanisms for providing enforcement for agreements when needed that can function effectively without the need of a distant "sovereign" or a police state. We can all keep an eye on each other, for one thing, and should. For another, we can always appoint third parties with an interest in seeing to it that our contract is kept: Each of us, for instance, will contribute a bit to pay this third party, who is not otherwise involved, to apply the cudgel to the one who tries to cheat. Yet that same third party can be hired specifically to look after *this* contract; he need not be hired also to look after *all contracts made by anybody* in the society.

Few among modern defenders of government accept any sort of strongly contractarian justification; but, nevertheless, the idea has been enormously influential. Its influence is especially marked in the tendency to regard government as justified primarily by what are called "public goods" problems. These are problems in which some produce, or would like to produce, what would be beneficial if produced, but the benefits cannot be confined to those who produced them. Instead, some can "free ride"—that is, collect benefits without paying the relevant costs. This, in turn, provides a disincentive to the would-be producers, and beneficial actions thus fail to be forthcoming. Advocates of government propose that the solution to this kind of problem is to have an authoritative body that can simply require all to pay, so that there are no free riders. Make peace the public good in question—which it is, after all—and you have Hobbes's argument for the state. Broaden the range of goods of this kind, and you perhaps have modern arguments for the expanded state with its multiplicity of bureaus and agencies.

Contractarianism as a Moral Theory

Jean-Jacques Rousseau (1712–1788) presciently observed that before there could be any sort of specifically political contract, we had to have something like a "contract" to form society itself: Before we elect a government, we need the act by which we *become a people.* For that act must be the true basis of society. Rousseau postulates that we all give ourselves to each other, as it were; and at the same time, he insists that this will be for mutual advantage—that we will each come out of it better off than when we went in, thus mirroring the ideas of Hobbes, despite Rousseau's somewhat alarming language about the total alienation of each to what he called the general will.

Contracting is normally an *act*—but just when could a "social contract" take place? Since, in principle, it is an agreement of all with all, independently of time, it obviously could not be any kind of historical event. It is, then, an abstraction: The idea of the "social contract" is simply a response by any given person to a basic appreciation of our relations to our fellows. We are all different, each with his or her own specific sets of interests and abilities. But we can all do great, even mortal, damage to each other, while, on the other hand, we can also be enormously helpful. Morals will be a "contract" in that each must give something and each must get something—otherwise it would be pointless. What we give up is the liberty to just go ahead and use other people as we like, without thought of what it will do to them. What we gain is the ability to rely on each other so that we can go about our businesses in peace and with reasonable hope of benefiting from our interactions with our fellows. Peace, in short, engenders prosperity, because peace enables cooperation—the source of all wealth and progress. And so, the cost in terms of foregone opportunities for gains from violence is actually meager in comparison with the possible benefits of renouncing that way of doing things. The social contract idea is that rational individuals, appreciating that this is how things are, will be moved to adopt the dispositions to behave along the lines indicated.

Anyone can play, at any time. That is to say, in any situation where we deal with others, we can size up how we stand in relation to them and vice versa, come to appreciate the prospects of a better outcome by both parties if we renounce intentions to benefit at the expense of others and confine ourselves instead to cooperative ways of interacting with them, provided that they do likewise.

Reworking the Contract: Modern Versions

Contemporary adaptations of a contract idea stem largely from the example and influence of John Rawls (1921–2002). Rawls proposes a device, the "veil of ignorance," which we are to pull over ourselves, to ensure that the "contract" will be *fair.* No one is to know what his or her own situation is in the society that is to be regulated by the principles we propose to formulate by unanimous decision. Thus, no one will be able to rig the principles so as to favor himself or herself at the expense of others. Why Rawls should have thought that a contract that had to be *unanimous* among all people would somehow be able to favor any particular person despite that is unclear. Nevertheless, it is a striking and possibly fruitful image.

Complicating matters, however, is what amounts to a measure of mistrust for his device. Not only does Rawls impose the veil of ignorance but he also deviates, to an uncertain extent, from the original idea in positing that we are to allow some influence from pretheoretic moral beliefs in our construction of the theory (the method of "reflective equilibrium"). We also posit that the parties to the deliberation are "equal." That men are in some sense to be regarded as "equal" when we get into the business of assembling principles for all is another old idea, and especially prominent in Hobbes. In the Hobbesian version, however, it is explicit that the equality in question is not one of general abilities, needs, or interests, but rather, it is specific and only with respect to our capability to inflict damage on each other. If this is a reasonable assumption, then it is easy to see why the first law of nature would be what it is: a law requiring all to forego the option of gaining by force and confine themselves to whatever can be achieved by peaceable agreement. In the Rawlsian construction, the parties are asked to ignore all respects in which they themselves might differ from others, and he supposes that the effect of this will be to support principles calling for much more influence on the social structure by political means.

The most important implication of the Hobbesian idea, by comparison with the Rawlsian one, is that society will not be expected to be much more egalitarian in its economic system. People will engage in trades of all sorts, but some will be far more productive than others, for any number of reasons—more intelligent, more energetic, situated in areas more conducive to production, and, of course, sometimes just luckier. In Hobbes's own view, people were to be ready to help those who suffered, say, from industrial accidents or were otherwise really down and out, but this help does not, evidently, extend very far. That implication is still clearer in Locke, who explicitly develops a view of the right of private property, though such a right is certainly lurking in Hobbes as well. With Locke what mattered is our right to the fruits of our own labor, as well as to any results of peaceable commerce thereafter. Thus, inequality of wealth is a perfectly likely, and acceptable, option.

Rawls, however, formulates not one but two principles of justice. The first, at least in some of its versions, was an "equal liberty" principle, more or less similar to Hobbes's second law of nature (which requires us not to insist on any liberties for ourselves that we would not also grant to others). But Rawls's second principle appears to be quite a different matter. According to it, *any* social inequality that we come up with is prima facie problematic. His second principle calls for equal opportunity and "open offices," and all inequalities must be compensated for to those on the downside of the inequality—not just local inequalities in predatory power. In particular, the worst off are to be made as well off as possible, in the sense that if we stuck to equality, then the worst-off people would be still worse off than they would be on the short end of a mutually advantageous exchange.

All such talk of fairness and equality raises a huge problem for the incorporation of the original idea of the "social contract." For that "contract" simply gets us peace and nothing more. Whether there will be what many modern theorists would accept as "fairness" and "equality of opportunity" is entirely up in the air if we suppose that we are only contracting for peace and security. (Hobbes, to be sure, offers germs of the idea, but his later laws of nature, which deal with that, are very narrow in their apparently intended application.) The classical idea was basically that we trade in our ability to make things bad for each other: You don't hurt me, I don't hurt you. That is seen to be the appropriate, fair price of our laying down of our liberty to "invade and despoil," but we don't go further and include a clause requiring mutual assistance. That is, we do not impose affirmative obligations to aid others. In the Hobbes/Locke view, we each retain maximum liberty about everything else, which includes whatever sorts of insurance arrangements we might want to make as privately acting individuals. Their understanding of the social contract, then, seems to be that it will be essentially what is now called a libertarian outcome.

The interpretation of Rawls's second principle has been the occasion for enormous discussion. It is unclear just what the "maximum" principle actually entails. Thus, Rawls appears to allow that considerations of *incentive*, for example, could justify inequality. That is a concession to self-interest that doesn't seem to sit comfortably with his egalitarian tendencies. But if one makes no such concession, it looks as though an all-encompassing egalitarianism of the socialist variety would be forthcoming. Rawls seems to want a sort of safety-net welfare state in the end, but just how that emerges from his principles is impossible to say. Nevertheless, the Rawlsian theory has been very widely accepted, at least in general form, among today's thinkers.

Integrative Social Contracts Theory

Integrative social contracts theory (ISCT) is a recent proposal to use social contract methods to specify the conditions for socially responsible corporate conduct. Here, the idea is to identify the involved parties—stakeholders—and find the basic values of each; then we look for a "hypernorm" capable of uniting all these parties, and we use it to focus on items of local dispute. The corporation is to abide by the results of this kind of reasoning, thus finding its appropriate niche in the relevant social environment. Care would have to be taken to identify elements of preexisting moral norms that are genuinely incompatible with agreement, as is evidently possible with some religious outlooks, for example. And much doubt exists whether this idea can be made to work for this more limited area. It might be, for example, that in the end all disputes would really be resolved on the basis of the property rights of each party, so that it is really just a carrying on of the Lockean idea. But ISCT advocates, generally, seem to think otherwise. At any rate, it appears to be an interesting application of the general idea of the social contract to the important case of business activity.

Conceptual Status of the Social Contract

Besides this question of just what the contract will entail in the way of rights and duties for all, there is a fundamental issue of just how or why conceiving the basic rules of society to be the output of something like a "contract" can actually explain anything or have any normative effect. There are two problems here. In the first place, nothing like a literal contractual procedure can have happened—hence the relevance of the oft-voiced quip that "the social contract isn't worth the paper it isn't written on." And in the second place, there is the criticism advanced initially by David Hume that since the obligation to keep our agreements is itself an important part of justice on any reasonable view of the matter, that obligation can hardly be itself due to an agreement to do so.

To this, the contractualist needs to respond with a very fundamental theory about how morals work. Regarding the first, a distinction needs to be made between the sense of "agreement" in which actual contracts consist and the sense of "agreement" in which they need not involve any sort of contract. The first kind is what social contract theory is about: A and B relate to each other in such a way that A will do something *provided* that B does, and vice versa. The second sense of "agreement" is that in which it merely means that the persons in question are of like mind, that is, they "agree" in what they think, even though they have not *made* an agreement. For example, I think that 2 + 2 = 4, and so do you, but we didn't need to "make an agreement" about it. In this second sense, what I think is not in any way contingent on what you think, and vice versa: It's just that we both size up things in the same way. If we were both to think that we ought to do this or that, then we would in the second sense be in agreement—but not necessarily in the first. Now, the social contractualist does think, very essentially, that it is a central feature of morals that each person constrains himself or herself in a way that makes his or her own behavior *contingent* on the actions of others: A will, for example, refrain from inflicting harm and damage on B *provided that* B refrains from inflicting it on A. Now, if both of them see the wisdom of acting thus—which is agreement in the second sense—then the claim that the resulting situation amounts to a "social contract" in the first sense, even though no literal bargaining led up to it, becomes plausible. The sense is that there is a universal requirement of reason that we refrain from certain kinds of actions *provided* that everyone else does so too. (More precisely, A refrains from doing *x* to B provided that B refrains from doing *x* to A, but suppose that C does *x* to D? A is not then necessarily involved. Each has the right to protect himself or herself from the assaults of all others as best as possible, and each likewise has the right to assist others who may solicit his or her help in warding off such assaults. But none of us is released from the requirement simply because somebody somewhere is breaking it in relation to *someone.*) This shows the way in which the social contract theory is distinctive. It does not require that literal contracts have been made, but it does require that the resulting principles make the conformity of one person specifically contingent on the conformity of others.

It is important to appreciate that any individual person may embrace contractualism, whatever others do.

Any particular person can say, "I'll refrain from doing such and such to others, *provided that* they do the same to me." In so resolving, that person behaves very different from the one who resolves to take maximum advantage of others with no regard for their responses: If they resist his intended depredations, he fights harder—or not, depending on his estimate of his chances of victory; and if they do not resist, he takes them for all they are worth, killing, raping, or robbing as he pleases. The contractarian theorist proposes that the difference between those two is the difference between the moral and the amoral; and in the case where his victims were peaceable folk not expecting this kind of behavior, the aggressor is not just amoral but downright immoral.

The Central Problem of Contractualism: Why Be Moral?

This account just given does, however, retain the basic idea that morality is *generated from our interests.* The main point of contractualism is to supply a real explanation of morality that at the same time provides rational motivation for it. We refrain from killing because if others do too, then our life expectancy is greater than if killing is routinely allowed and practiced; we keep our agreements because if others do so as well, then we (as well as they) can reap the benefits of cooperation. In both cases, the problem is that individuals could benefit from breaking the rules if others respect them. Thus, it seems always in each person's interest to break rather than keep the rules. But, of course, if that is general, then the whole thing is pointless. And also the reason for the word *seems* is clear: That everyone's interest is served by paying no attention to promises and having no regard for others is shown to be false by the fact that general practice of that kind leads to a state of complete misery and desperation for all. To commit oneself to principles with such consequences is arguably irrational, not rational.

This is illustrated by the familiar "game" explored in formal game theory known as the prisoner's dilemma. Mutual cooperation, as in keeping one's agreement or refraining from violence, is the second best of the logically possible outcomes for each. But breaking the agreement is better for either—*provided* that the other does *not* break it. For if both break it, then both come out worse than in the mutual-cooperation case. As Hobbes saw, the big problem concerns the case where the agreement is such that one party acts significantly earlier than the other (the case he calls covenant). Why, then, would the other bother to keep his end of it?

The problem, then, is how to motivate people to cooperate under the circumstances. There have been many discussions of this, but in the main there are two serious alternatives. One points to the fact that in society we do not "play" the "game" just once, but rather we do so over and over again. This is called "iteration." In an iterated game of this kind, things are different. If there are a precisely known number of plays, things will break down, for at the last play, the next-to-last move will be to defect, and the other player will know this, and it will all come unstuck. However, if the last move is not known, the situation changes completely. Then the smart money, as they say, is on cooperation, generally speaking. This has become known as the "folk theorem" in game theory. And it is generally true in real life that there is no known, predictable last play. Self-interest, so long as it involves at least a modest interest in the agent's own future, will generally carry the day in favor of keeping agreements.

A very different idea, proposed by Professor David Gauthier, has it that the rational agent will abandon what he calls "straightforward maximization," in which defection would be seen as the rational move, in favor of what he calls "constrained maximization," which calls for cooperating with those who are ready to cooperate and defecting only against those who defect instead. In this, Gauthier's strategy perfectly embodies the essence of the social contract. But it also raises severe questions about how reason is going to get it installed in the psyche of the would-be cooperator. And, of course, it requires solution of a possibly insoluble problem: How do we tell whether the person we are about to interact with will or will not prove to be a fellow cooperator?

All is not lost, however. In the first place, the folk theorem is very much with us. And in the second, game theorists tend to ignore or sidetrack what we may call the sociology, or perhaps the phenomenology, of morals. People do not just act: They also criticize each other (and themselves). They react to what others do, as well as acting as best as they can themselves. Why not assemble, then, a set of directives for which behavior to reinforce and which to condemn, and then go to it? One can plausibly argue that that is exactly what we do and that it works pretty well if not perfectly.

Some argue that the kind of morality that emerges from the social contract idea is too narrow and self-interested to pass muster. Those who say this may perhaps have insufficiently appreciated the effect of prisoners' dilemma. They may also have insufficiently appreciated our extrarational potential for cooperation: Fellow feeling, love of mankind, and a considerable fund of altruism, rational and otherwise, are encouraged in the social contract along with the narrower requirements of justice. The other point is that it is not, after all, settled just what precisely *will* be the "terms" of an appropriate social contract. Would it, in fact, include more than the classical mutual refraining from inflicting harm and damage? Would it include, perhaps, the panoply of contemporary ideas—gender equality, civil liberties, and extensive welfare services, all understood as going well beyond mere mutual nonviolence? It is arguably too early to say with confidence.

The moral level is primarily the individual level, and it is here that the likely upshot of the social contract is that each person's primary obligation is to refrain from harm and damage and to keep whatever agreements he or she voluntarily makes. However, it is plausible also that a minimal amount of positive concern for others would be forthcoming. Where we can help others greatly at a very small cost to ourselves, the social contract arguably says we ought to. Where the cost is large, however, social contract cannot require performance, since *mutual* advantage will always be its general form. But perhaps things will look different at the political level.

Political Contractarianism

There are two different but related ideas of how the contract idea might feed into the creating and sustaining of political institutions. One stems from the Hobbesian idea that morality is too weak to do the job: People's commitment to moral restraints binds us "in foro interno"—that is, it binds the will to the desire that people behave like that—but does not necessarily extend to practice in the real world, that is to say, it does not bind "in foro externo." So the idea of political contractarianism is that we should now call in the state to do the job: An effective sovereign will keep peace among us by threatening us with much more than "mere words" if we fail to perform. The sovereign, in effect, turns what would have been prisoner's dilemmas into no-brainers: If reneging on my contract will cost me a year in jail as well as the loss of whatever goods I was contracting for, then my motivation to perform is likely to be excellent.

The other strain of argument goes in two directions. First, it raises the question whether the level of mutually beneficial activity might be higher when institutionalized. Supporters of the welfare state, in particular, may argue that collectivizing many concerns, such as for health, economic security, and old-age security, will yield benefits that relying on individual initiative may not. And second, it takes the question of conflicts of individual interests to what may be seen as a wider level, namely, that on which the contending parties embrace not just possibly conflicting *interests* but also conflicting *ideologies*—conflicting philosophies of life.

Concerning the first of these, there is no question but that democratic government, especially, has been accompanied everywhere by a great increase in the level of intervention by the state into the lives of citizens in those respects. The question can be asked whether this is a step in the right direction. In one view of the matter, only misinformation, or the tendency of groups to seize powers to extract benefits from others, or both, is responsible for the belief that collectivization can "work" in these respects. Such theorists hold that we would actually do better without the state and that the original social contract limiting the state to prevention of interpersonal mischief remains the best way for all. In another view, the state's activity enables a much larger "social dividend" than would otherwise be possible, and the way to divide it is, as with Rawls, to pay special attention to the needs of the worst off. The latter is the standard view among social philosophers at present, but it can hardly be said to have been "proven."

The problem of rival ideologies is different and arguably more intractable. Can there be cooperation and mutual benefit among peoples at loggerheads over religion and much else? The various parties who differ in these ways, many of them perhaps ready to resort to lethal weapons to press their ideas on others, may well be tougher customers than individual parties acting in their own particular interests. Sectarianisms of various kinds bring people to intense, prolonged, and profound clashes, historically and in contemporary times. The contractarian proposes that even these deeply conflicting ideologies can benefit from cooperation, enforced by a strong state in which each participates, or at least by the kind of interstate cooperation that, again, is scarcely possible on the individual level.

Not all, but a great many, of historically actual cases of such conflicting group beliefs are religious in nature, and the classic liberal solution—which is surely the solution suggested by the social contract—is the principle of freedom of religion. Why would differing religions accept such a principle? The reasons are pretty strong. Neither can expect to persuade the others of their "errors" in any short term, and meanwhile, if they instead resort to force, there will be war—and war of a particularly vicious kind. Each will have to decide whether the expected costs outweigh any benefits that might derive from subduing the other parties, but the contractarian will argue that it is a plausible bet that they will indeed do so—especially since sectarian war making will also endanger the lives of bystanders, potential trading partners from otherwise noninvolved parts of the world, and so on. History makes it easy to believe that the consequences of uninhibited religious warfare are thoroughly horrible for all—the Thirty Years' War in Germany in the 17th century stands as a classic example. So if what it takes is a strong state to enforce a kind of general treaty that people will refrain from trying to promote their religious ideals by force, the contractarian argues, then we'll all be ahead if we support such a state. Even in strictly religious terms, it may be further argued that no one will lose, since their prospects of genuinely promoting their religions by means of force are virtually nil anyway. This sets the stage, we may suppose, for general acceptance of religious liberty as a principle to be recognized and enforced by governments everywhere—or, at least, everywhere that there is any religious diversity, which is virtually everywhere. The contractarian may also argue, of course, that the level of individual creativity on ideological as well as other fronts is likely to be much higher when people can live without fear that others stand ready to do violence to them for even thinking about these matters. So long as all are free to accept or reject any given thinker's ideas, what do we have to fear? And the major contractarians have, of course, always supported strong principles of religious and other freedoms for these reasons.

—Jan Narveson

See also Game Theory; Hobbes, Thomas; Integrative Social Contract Theory (ISCT); Locke, John; Political Theory; Prisoner's Dilemma; Rousseau, Jean-Jacques

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Social Costs

The term *social cost* refers to the larger effects on society of externalities created through productive economic activity. The theory of social cost attempts to analyze the total cost of economic activity, including not only the cost to those directly involved in the transaction but also to society as a whole. It attempts to allocate responsibility for harm caused by economic activity among the various parties affected. This theory has application across a broad spectrum of economic activities, but it is particularly important in evaluating the environmental impact of certain kinds of production. By attempting to assess the effects of externalities on the surrounding community, it seeks to determine how best to account for and correct for those externalities, with the goal of minimizing the overall harm caused by production.

A common example involves two industries that use the same area, such as a fishery and a factory situated adjacent to one another. The fishery relies on clean water to raise its fish, while the factory uses the lake to dump polluting chemicals. By dumping into the lake, the factory causes harm to the fishery, thus imposing a cost on agents who are not involved in its production process. Social cost theory seeks to determine what kind of compensation, if any, is owed to the fishery by the factory.

One possible approach would be to require that the factory, as the polluter, bear the cost of cleaning up the damage caused by its pollution, restoring the lake as much as possible to a pristine condition. To do so, however, would be to impose a cost on the factory in the name of the fishery, thus making the factory liable for the fishery's loss. Alternatively, the factory may choose to install pollution filters that would prevent the lake from becoming contaminated, but this would still impose a cost on the factory for the sake of ameliorating a cost to the fishery.

Another approach would involve government regulation of the polluting industry to reduce the externalities and the attendant harm to others. This could be done in a number of ways. Government might come in as a neutral arbitrator among the various parties to balance the relative costs and benefits of the various options available. Alternatively, it might require the polluting industry to install the filters that it might otherwise have found to be too costly. It could also choose to levy a fee on the industry—requiring it to pay according to the amount of damage done. In theory, this governmental intervention will allocate responsibility on the basis of the source of the pollution. The most well-known approach to this strategy is a "Pigou tax" (named after British economist Arthur C. Pigou, who developed the idea in which fees are levied on a per-unit basis according to the cost of the pollution, with the goal of "internalizing" the costs of the externalities, creating an incentive for industry to create fewer polluting emissions). In practice, such governmental interventions are often less than optimally efficient and are looked at askance by many economists, particularly those of the more libertarian persuasion.

A variety of market-based solutions has been proposed to deal with social costs apart from (though sometimes in cooperation with) government intervention. One example of such a market-based solution allows firms to trade "pollution credits," through which those industries that find it difficult to bring pollution down to an acceptable level would be able to buy the right to emit more pollution from those industries that are able to reduce their pollution below those levels. This seems to have had some success in reducing pollution in some areas but does not solve the problem of social cost as much as it does relocate it, as those industries that are engaged in heavy pollution are simply enabled to continue doing so through the allocation of a right to pollute. This strategy is similar to, though not identical with, the Coase theorem.

Ronald Coase argued in "The Problem of Social Cost" that the key problem in evaluating responsibility in cases such as this is that the harm caused is not one-sided. It is not simply the case that the factory is harming the fishery through its pollution. It is also the case that by requiring the factory to compensate the fishery, the factory is being harmed. Coase argues that, in the absence of liability for the damage caused by the fishery, the allocation of resources will be identical to what it would be if the factory were made liable. In other words, requiring the factory to compensate the fishery does not produce any more efficient an economic outcome than not requiring compensation.

The Coase theorem states, "If property rights are fully allocated, competition leads to efficient allocations." That is to say, when the right to property is clearly articulated (e.g., who owns the lake in our example above), market forces will determine how responsibility is to be apportioned. Thus, if the fishery owns the lake, the factory may choose to pay it for the right to pollute in its water rather than install filters. Alternatively, if the factory owns the lake, the fishery may pay the factory to install the filters. However, all this assumes that there are no transaction costs associated with the transfer of the relevant rights. Such transaction costs are inescapable, however, and Coase argues that in matters of economic and social policy, it is only by examining the allocation of transaction costs that it can best be determined how responsibility should be allocated.

This theory raises several interesting questions. For example, does the creation of an efficient system for allocating transaction costs according to property rights necessarily address the moral question of whether some form of social justice is thus achieved? Is the economically most efficient solution, in other words, necessarily the fairest?

Furthermore, Coase's theory seems to assume that all property rights are fully allocated and, thus, there exists no "public property," or even any "public goods." All goods are understood as private goods that can be negotiated among private parties. Even in such a set of circumstances, however, there may be public implications to these private transactions that are not accounted for in the transaction costs. In accepting the Coase theorem, are we thereby committing ourselves to a total rejection of the principle of public goods? Is there any way, given Coase's principles, that any conception of "common resources" can be maintained?

Even were one to conclude that the Coase theorem offers the most economically efficient answer to the question of social cost, it does not necessarily answer the moral questions associated with the problem.

Each of these strategies—whether legal, regulatory, or market based—has its pros and cons. It is only on the basis of a pragmatic evaluation of the actual harm done and the actual solutions that are available in a given set of circumstances that it can be determined what course of action should be followed. In some cases, governmental action may be the best course available; in other cases, market forces will do the job better. The moral principle underlying the entire question of social cost is whether those who have not given their assent to be affected in a particular way by a particular industry are entitled to some form of protection from or compensation for the harm to which they are subject. Although the various solutions offered disagree on the answer to the question, and the mechanisms by which protection or compensation may be given, they recognize the question as a valid issue to which economics owes society an answer.

—Scott R. Paeth

See also Coase, Ronald H.; Coase Theorem; Compensatory Damages; Consent; Cost-Benefit Analysis; Economic Efficiency; Efficient Markets, Theory of; Emissions Trading; Environmentalism; Environmental Protection Legislation and Regulation; Externalities; Free Market; Hazardous Waste; Industrial Policy; Perfect Markets and Market Imperfections; Property and Property Rights; Resource Allocation; Rights, Theories of; Transaction Costs

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Social Discount Rate

The discount rate adjusts future benefits and future opportunity costs for accurate comparison with present values. Other entries for "Discounting the Future" and "Net Present Value" explain the mathematics of discounting to net present value. The social discount rate is the discount rate that should be applied to cost-benefit analysis of government investment projects generating benefits and costs over time. In economic theory, such government projects should provide public goods demanded by consumers who will not voluntarily reveal their true preferences in terms of paying for those goods. A prominent example is water resource projects for irrigation and electricity.

A simple illustration demonstrates the role and importance of the social discount rate. Suppose that a specific water resource project yields annually a 7% net benefit above opportunity cost. (In nominal dollars, $100 of cost incurred annually produces $107 of benefit.) Each year out into the future, the net present value of this 7% net benefit declines. The social discount rate determines the rate of that decline in net present value. If the social discount rate for a government project is set at 10%, then the project should not be undertaken because the net benefit of 7% annually is less than the social discount rate for the optimal allocation of the resources to be consumed as opportunity costs. If the social discount rate for a government project is set at 4%, then the project should be undertaken because the net benefit of 7% annually is greater than the social discount rate for the optimal allocation of the resources to be consumed as opportunity costs. Whether to undertake the project or not depends on the proper social discount rate.

In economic theory, the discount rate should equilibrate demand for savings by investors and supply of savings from savers. A saver does not spend his or her full income on current consumption. How much to save involves a comparison of the value of current consumption in relationship to future consumption. The discount rate is effectively a rate of compensation for deferring current consumption to future time periods.

The social discount rate selected for a government cost-benefit analysis is an important decision. It should reflect the true social opportunity cost of public investment. In economic theory, cost-benefit analysis should result in a mix of government and private market investments that maximizes overall social welfare. Government investment choices may displace private investment, reducing the future supply of private goods.

There are two schools of thought concerning selection of a social discount rate. One school argues that the private market rate of interest should be used to evaluate government projects. The argument is that, since government investment may reduce private investment, government projects should show at least the same rate of return as private projects. Otherwise government investment funds should remain in private hands. This argument assumes relatively strong capital market efficiency. In technical language, the market interest rate should equilibrate the marginal rate of time preference by savers with the marginal rate of return on private investment, and the market interest rate should be the same as the marginal rate of social time preference. The other school of thought argues that private citizens are shortsighted in evaluating present consumption of private goods relative to investment in future consumption of public goods. The marginal rate of social time preference is in effect too high. The argument is that government should exhibit greater patience than private citizens to promote the long-term welfare of society. Long-term welfare involves intergenerational equity.

This theoretical debate is of great practical importance. One school argues that the market rate of interest should be used in evaluating government projects. This rate would tend both to reduce the number of projects approved for funding and to favor projects with early benefits. The other school argues that the government bond rate should be used. The U.S. government bond rate is effectively risk free and thus significantly lower than the market rate of interest (which includes a risk premium). This rate would tend both to increase the number of projects approved for funding and to favor projects with highest total benefits independently of opportunity costs. Thus, a related controversy is what risk associates with a specific government project as distinct from the total pool of government investments.

The theoretical debate has marked bearing on competing philosophies of business and society. The libertarian theory of society argues in effect that the social discount rate should be relatively high. Most aspects of society should be left to private voluntary choices exercised by individuals, who are best situated to determine their own best interests. Libertarianism is strongly opposed to government activity. Socialism argues in effect that the social discount rate should be relatively low and certainly well below the market rate of discount. Many aspects of society and markets should be taken over by the government, because individuals are often mistaken about their own best interests and the best interests of the collectivity.

—Duane Windsor

See also Cost-Benefit Analysis; Discounting the Future; Intergenerational Equity; Libertarianism; Net Present Value; Opportunity Cost; Pareto Efficiency; Public Goods; Socialism

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SOCIAL EFFICIENCY

The term *efficiency* is used in a variety of contexts. For example, engineers use the term to denote the ratio of output to inputs for specific physical activities. The engineering concept of efficiency is similar to the economists' concept of technical efficiency. A production activity is technically efficient when the maximum possible amount of physical output is being produced for a given quantity of inputs. These concepts of efficiency imply that there is no "waste" in the production process; however, physical measures of efficiency do not necessarily imply that society is as well-off as it could be given the resources that are being used to produce existing rates of output. This is because physical measures of output do not take into account the value that society places on different outputs. In the extreme, for example, an economy might produce the maximum feasible quantity of a given set of products given existing best-practice technology, even though there was little demand for those products on the part of consumers. Clearly, society would not be well served by an economy functioning in this way. From a social perspective, an economy is performing efficiently when productive resources are used so as to maximize the *value* of output produced. Put differently, social efficiency is defined as the condition whereby it is impossible to reallocate productive resources to different activities so as to create a more valuable set of outputs.

Measuring Value

An obvious question that might arise is, "How are *social* values of different outputs and inputs established?" After all, consumers are unlikely to have identical tastes and preferences, while workers, landowners, and other suppliers of inputs are likely to differ in their skill levels and other endowments. Hence, members of society will differ in their individual valuations of the many different outputs and inputs that characterize economies. In capitalist economies, the forces of supply and demand establish the values of outputs and inputs. Specifically, market-clearing prices, that is, prices that equate supply and demand, ordinarily serve as measures of value. The reliance on market-clearing prices as measures of social value can be conceptually justified by acknowledging that buyers should be willing to pay, at a maximum, what any quantity of a good is worth to them rather than go without that good. This implies that the market demand curve for a good should represent the valuation that consumers, in the aggregate, place on different quantities of the good. Similarly, sellers should be willing to supply to buyers any given quantity of a good only if the price received at least covers the incremental cost of supplying that quantity. This, in turn, implies that the market supply curve for a good can be taken to represent the incremental cost of supplying different quantities of the good in question. Under reasonable assumptions, the market demand curve is presumed to be downward sloping, while the market supply curve is presumed to be upward sloping.

If markets function reasonably well, prices will adjust so as to equate supply to demand. Under several specific assumptions that will be discussed in the next section, the market-clearing price that equates supply to demand can be taken as a measure of the value that society places on the last unit of output produced and consumed. This is because, as noted above, the demand curve is an expression of the monetary value that consumers place on various amounts of a good. At the same time, the market-clearing price also measures the incremental cost of producing the last unit of output sold, since the supply curve is a schedule of the incremental cost of producing various amounts of the good in question. Hence, the market-clearing price establishes the monetary value of the marginal unit of any product and equates that value to the incremental cost of producing the marginal unit. This analysis applies equally to products sold for final consumption or for use as inputs in further processing activities.

The Concept of Social Surplus

If the market-clearing price represents both the value that consumers place on the last unit of output consumed and the incremental cost of producing that last unit, it can be easily shown that society is as well-off economically as it can possibly be at the market-clearing equilibrium. The relevant concepts here are consumer surplus and producer surplus. Consumer surplus is defined as the maximum amount that consumers would willingly pay for any quantity of output (rather than go without the product) less the amount that they actually pay. The maximum amount that consumers would willingly pay is the area under the demand curve corresponding to any quantity purchased. The amount consumers are actually required to pay in the marketplace is the price of the product multiplied by the quantity purchased. The difference between the amount of money that consumers are willing to pay and the amount that they actually pay is a measure of how much better-off consumers are by purchasing any given quantity of a good.

Producer surplus is defined as the amount of revenue that producers realize in the marketplace over and above the minimum amount they require to make their product available to buyers. The former is equal to price times quantity. The latter is the area under the sellers' supply curve corresponding to any quantity supplied. Producer surplus is therefore a measure of how much better-off sellers are as a result of supplying any given quantity of a product. The sum of producer and consumer surplus is called *social surplus.*

The concept of social efficiency is directly linked to the concept of social surplus. Specifically, if social surplus is being maximized at the current market-clearing price and quantity, it is impossible by definition to make buyers and sellers collectively better-off by choosing a different combination of price and quantity. That is, any reallocation of resources that leads to more or less of the good in question being produced will reduce the value that society realizes from economic activity in the market in question. Simply put, it is not possible to reallocate productive resources to create more value to society as represented by consumers and producers. Hence, the existing amount of production can be said to be socially efficient. Moreover, if social surplus is maximized in every individual market, the collection of those markets—that is, the entire economy or society—can be said to be efficient.

Some Caveats

As noted above, reliance on market-clearing prices as measures of social value rests on specific assumptions that should be made explicit. Perhaps the key assumptions are that the demand curve fully reflects the social value (or benefit) of consuming different possible quantities of a good, while the supply curve reflects all costs *to society* associated with producing different quantities of the good. The relevance of these assumptions can be illustrated by assuming the counterfactual, for example, some costs of producing a good are incurred by members of society other than the producers of that good. This situation is often invoked when scientists discuss the phenomenon of environmental externalities.

Externalities

In the presence of cost externalities, the market supply curve will not reflect all costs to society. Rather, it reflects only the costs incurred by producers of the good. As a result, at the market-clearing quantity and price, it is not the case that the value consumers place on the last unit consumed equals the cost to society of producing that last unit. Since producers ignore costs that are incurred by others, at the market-clearing price and associated quantity, costs to society must be greater than the costs to producers or the benefits to consumers. The socially efficient output rate will, therefore, not be produced in the presence of cost externalities such as air and water pollution. Indeed, society would be better off if less of the product in question were produced. If producers could somehow be made financially responsible for the external costs that they impose on society, the producers' incremental costs would increase by the monetary value of the cost externalities that they create. This, in turn, would require producers to charge higher prices and result in less output being produced and sold at the market-clearing price.

Cost externalities are ubiquitous in market activities and their widespread presence provides a theoretical justification for government intervention into the free market. Air pollution from burning fossil fuels such as coal is a prominent example. Steel factories, for example, use coal intensively as a fuel, and the particles from the heated coal were a major source of air pollution in the Great Lakes area where steel plants are located. Federal government requirements for factories to install "scrubbers" in smokestacks have dramatically reduced this source of pollution, as the scrubbers catch much of the particulate released before it can escape into the atmosphere.

Demand externalities are seen by economists as being much less ubiquitous than cost externalities, although the presence of demand externalities provides an equally compelling theoretical rationale for government policy intervention into private sector activity. Put simply, the free market will fail to produce a socially efficient output rate in the presence of externalities. In theory, government intervention can encourage the attainment of social efficiency by ensuring, through one means or another, that external costs (or benefits) are fully incorporated into the production and consumption decisions of private sector participants. Precisely which policy is preferable to best accomplish this purpose is a complex issue that is well beyond extended discussion in this entry. As a rule, economists recommend that public policies infringe as little as possible on free market activities while ensuring that externalities are incorporated into the free market process. As such, economists argue that the absence of clearly defined and enforceable property rights is frequently the underlying source of externality problems and that the establishment of such rights by regulators or courts is, therefore, often the preferred public policy response.

Market Power

Another critical assumption underlying the case that market prices reflect social values and promote the realization of social efficiency is that those prices are determined in competitive markets. By definition, markets are competitive when no single seller or buyer, or any group of sellers or buyers, has the ability to influence prices by the amount he or she sells or buys. If this condition is violated, sellers or buyers are said to enjoy market power. As a general statement, when market power exists, the equilibrium output rate will be less than the socially efficient output rate. The impact on price depends on whether sellers or buyers enjoy market power. When sellers possess market power, the equilibrium price is likely to be higher than the competitive price, while the opposite is true when buyers enjoy market power. Once again, a theoretical argument exists for government intervention into private sector markets. In this case, government intervention would presumably seek to mitigate market power and restore competitive pricing. Antitrust laws are the basis for preventing the accumulation of market power, as well as its exploitation. As in the case of government regulation to address externalities, there is controversy concerning whether the application of antitrust laws moves markets closer or further away from social efficiency, although most economists support government efforts to ensure competition.

Fairness

As noted above, social efficiency implies that the maximum value of output is being produced given the available inputs an economy possesses. An equivalent statement is that a nation's real income is as high as it can be given its productive resources. It does not imply that the distribution of the real income produced is *fair* or even acceptable. For example, free market activities could produce an outcome where a relatively small number of people enjoy extremely high incomes while many others suffer in poverty. Where substantial inequalities in the distribution of income are widely regarded as unfair, policies will be implemented to reallocate wealth from the "rich" to the least well-off. The public policy goal in this context is to accomplish income redistributions while maintaining efficient production, that is, socially efficient output rates, to the greatest extent possible.

A prominent public policy issue is whether there is a necessary trade-off between social efficiency and "equity." To be sure, any analysis of this issue requires a precise definition of what is meant by equity. For example, if equity is defined narrowly as the uniform application of rules of law to all individuals without discrimination, there is no reason to believe that social efficiency will be harmed by the pursuit of equity. On the other hand, if equity is defined more broadly to encompass approximate equality in material standards of living rather than just equal rights under the law, the potential for conflicts between social efficiency and equity is both real and complex.

A consideration of this potential conflict is well beyond the scope of this entry. Suffice to say, economists and other social scientists are uncertain about the precise nature of the relevant trade-off; however, there is some agreement that large divergences across households in material standards of living will lead to social conflict and other pathologies that, in turn, can seriously harm production and the efficient functioning of markets. Conversely, efforts to eliminate income disparities through progressive taxation and social welfare programs can, beyond some point, encourage inefficiencies such as the growth of the "underground" economy, black markets, and long-term unemployment.

Conclusion

The pursuit of social efficiency ultimately reflects the importance to society of maximizing society's overall standard of living where living standards include both material and nonmaterial goods. For example, music and leisure can be as much a part of a nation's standard of living as flat-screen televisions and BMWs; however, social efficiency is not equivalent to social welfare. The latter is a broader concept that encompasses considerations such as equitable distributions of income, natural justice, and morality. Policy makers may need to balance among these different components of social welfare where they are not completely complementary.

—Steven Globerman

See also Antitrust Laws; Capabilities Approach to Distributive Justice; Deadweight Loss; Environmental Protection Legislation and Regulation; Externalities; Opportunity Cost; Perfect Markets and Market Imperfections; Surplus, Consumer and Producer

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Social Engineering

Social engineering is the design and implementation of systems and incentives in a human group, institution, or community to accomplish explicit objectives in its allocations of well-being. Examples of such systems and incentives include socially responsible investing and subsidies, taxes and other confiscations of private property, regulations, and socialism.

Social engineering is intended to bring about a moral and fair society. It focuses attention on an intended just distribution throughout society of basic human rights (e.g., housing, health care, food, etc.) and negative freedoms (e.g., freedom from want). One example of social engineering is the affirmative action programs in the United States. These are government orders and regulations intended to bring about ethnic and racial diversity in the important U.S. institutions of commerce, education, and housing. Other examples include minimum-wage laws intended to reduce the ranks of the working poor and private social entrepreneurship ventures intended to fundamentally change the distribution of well-being in poor social segments.

Social engineering effectiveness depends, in large part, on the integrity of decision makers to act for the benefit of society and without regard for their personal self-interest. Important ethical principles include integrity, honesty, social responsibility, compassion, empathy, the avoidance of conflict of interest, and justice.

There are trade-offs between moral ideals and real-world consequences that call for consideration of positive and negative rights (e.g., freedom for autonomous individuals to make choices vs. freedom from poverty). A consequential, or teleological, approach to social engineering suggests cost-benefit analysis and feasibility issues not likely to be included in deontological, or purely philosophical, approaches. Ethical issues concern the need to balance between commutative and distributive forms of justice. For example, distributive justice principles support a socially engineered society in which people who score well on standard tests receive the same social allocation of welfare as people who score poorly; commutative justice supports engineering society to give all test takers fair access to social institutions where their natural endowments can take them as far as their talent enables.

To ensure smooth functioning of social engineering, government must enforce regulations, raise funds to finance social projects, seize private property that can be put to better social uses (the practice of eminent domain), and monitor the activities of society along dimensions of interest to social engineers. Important ethical issues here are balancing positive and negative rights (e.g., freedom to act vs. freedom from harm), self-interest versus utilitarian benefit, and individual autonomy versus social welfare.

One important issue in the practice of social engineering is that the definition of *well-being* is subjective, that is, based on individual perception. This calls attention to issues of fairness in the process of engineering society. Self-interested individuals want to effectively participate in the group, institution, or community to increase their personally defined welfare, subject to the rights of others. The rights of others, however, may call for personal sacrifice for the gain of others. The ethics of persuasion are important in this process of social engineering.

Adam Smith wrote (*Wealth of Nations*, 1776) that free self-interested exchange most efficiently uses society's resources to bring about social welfare. A laissez-faire approach to social engineering, grounded in ethical principles of economic efficiency, designs and implements systems and incentives to ensure the smooth functioning of free markets. Important ethical principles in this approach include cost-benefit analysis, honesty, trust, contract, autonomy, liberty, compliance with government requirements, and private property.

—*Greg Young*

See also Affirmative Action; Consequentialist Ethical Systems; Contracts; Cost-Benefit Analysis; Deontological Ethical Systems; Egalitarianism; Ethics of Persuasion; Laissez-Faire; Regulation and Regulatory Agencies; Rights, Theories of; Self-Interest; Socialism; Socially Responsible Investing (SRI); Subsidies; Utilitarianism; Utility

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Social Entrepreneurship

Social entrepreneurs create social value through the use of the entrepreneurship model. Social entrepreneurship relates to many business forms but fundamentally exists as a model that organizations are able to use in pursuit of goals directed toward building value for the society within which they are embedded. Organizations built on this model follow closely with the traditional path of entrepreneurship, pursuing perceived opportunities to achieve their goals. The key to understanding social entrepreneurship lies in acknowledging that it transcends traditional business model boundaries and can occur in any sector of business, such as in the private for-profit or not-for-profit sector or in the public sector.

To engage in social entrepreneurship, the organization is typically driven by a social entrepreneur. The social entrepreneur shares many similar skills with the traditional entrepreneur. These shared skills are identified as designing a mission with the core purpose to create and sustain value; pursuing new opportunities to serve the mission; engaging in continuous innovation, adaptation, and learning; acting boldly without being limited by the resources currently available; and exhibiting a level of heightened accountability to the stakeholders affected and for the outcomes as a result of the mission. The distinguishing factor for social entrepreneurs is that they create *social* value through the use of this model to create economic value.

While the entrepreneurial skill set is very similar between the traditional entrepreneur and the social entrepreneur, there is a large difference regarding their individual value orientation. Social entrepreneurs are more likely to have experienced some sort of transformative experience during their life, which pushes social improvement to the front of their core values. Most social entrepreneurs are also very active in the social sector throughout their lives, beginning at an early age. This social activism is then combined with their entrepreneurial skill set to enable them to pursue their social missions through social entrepreneurship.

Social entrepreneurship can often be confused with other business models or practices that are designed to create accountability to society within the business sector. Two other terms that are sometimes misused are *social ventures* and *social enterprises*. Both social ventures and social enterprises are the legal entities that are created as an end result of social entrepreneurship.

It is also useful to distinguish between a social venture and a social enterprise. Most frequently, the term *venture* is used to describe organizations that are the result of a venture capital investment, but with social ventures this is the result of social venture capital. The term *enterprise*, on the other hand, is typically associated not with an organization built on venture capital but with one that secured its financing through other means. Regardless of the methods of financing, both social ventures and social enterprises are two possible outcomes of social entrepreneurship. Social entrepreneurship must also be differentiated from terms such as *sustainable enterprises*, *corporate social responsibility*, and *business ethics*. While it is possible for a social venture, or a social enterprise, to practice social responsibility or sustainability, they are different concepts within the same theoretical sphere of social awareness.

A Brief History

Although social entrepreneurship has only recently received significant academic and professional attention, the fundamental concept has been in practice by individuals throughout the history of business enterprises. Some examples from the past include David Brower (the United States), Vinoba Bhave (India), Florence Nightingale (the United Kingdom), and Jean Monnet (France). David Brower was the Sierra Club's first executive director and built it into a global network designed to serve environmental issues. Vinoba Bhave founded the Land Gift movement in India, allowing the redistribution of more than 7,000,000 acres of land to the landless untouchables, individuals who were low-caste Hindus and viewed as "polluted" and separated from the rest of society. Florence Nightingale revolutionized health care through the foundation of the first school for nurses. Jean Monnet led the reconstruction of France after World War II and established methods to integrate Europe economically.

These individuals pursued their missions and extensively influenced the societies around them through creativity, leadership, and a vision of social improvement. These acts are distinguished from those of other socially conscious individuals by the entrepreneurial methods used to pursue their social goals. These social entrepreneurs paved new paths to pursue these ideas. Individuals such as these, along with countless social advocacy groups and community initiatives, have all set the foundation from which the current identity of social entrepreneurship has been derived.

Social entrepreneurship began to gain visibility and definition through the work of Bill Drayton and his founding of Ashoka in 1980. Ashoka became the first to pioneer into the concept of "social venture capital," providing funding for entrepreneurial individuals in pursuit of social change through innovation. The founding of Ashoka marked the beginning of social entrepreneurship as a functional and practical business theory. As social entrepreneurship continues to gain prominence and validity, it is becoming an increasing popular topic of academic discussion.

With the increase in practical applications of social entrepreneurship, it has become clear that it is a viable model within any of the business sectors. Social entrepreneurship is often categorized as a cross-sector model, in which the organizations applying the model often lie somewhere in the middle of the continuum that runs between the private for-profit and not-for-profit sector and the public business sector, blurring the boundaries of these traditional business sectors. However, as blurred as these boundaries may become, the legal distinctions between organizations in each of these sectors still exists, making it useful to examine the distinctions between each.

The For-Profit Sector

Social entrepreneurship within the for-profit sector references organizations that are legally defined as existing to generate profit, while the organization defines its primary mission as one grounded in social improvement or development. When considering these for-profit organizations, it is important not to confuse the act of social entrepreneurship with the act of stewardship. The stewardship model describes organizations that acknowledge their responsibility to society and act on those responsibilities but still identify their primary objective as that of generating profit. For the for-profit social entrepreneur, the ultimate objective is to design a process that allows the organization to generate profit as a by-product of its improvements to society, as opposed to generating social value as a by-product of profit.

By maintaining the for-profit business model, it is easier for these organizations to achieve long-term financial sustainability. This occurs because the organization is often more successful at obtaining sustainable revenue streams. These revenue streams are more stable because the organization understands that its products must not only be socially beneficial but also just as attractive as a competitor's product, even if the competitor isn't driven by the same social standards. This is the result of consumers who may not know, or care, about the social mission behind the company.

Another variation of social entrepreneurship also occurs frequently within the for-profit sector—social intrapreneurship. Similar to social entrepreneurship, social intrapreneurship has become increasingly popular over the last decade. The distinguishing characteristic of entrepreneurship and intrapreneurship is that intrapreneurship occurs within preexisting organizations, often creating extensions of the same business or expanding into new businesses. One of the attractive features of intrapreneurship is the ability to fund these efforts through the preexisting organization. Thus, often the efforts of intrapreneurship are more successful because the risk of financial failure is smaller when the organization is backed by a secure revenue stream.

Excellent examples of for-profit social entrepreneurship can be found in organizations such as Newman's Own or Ben & Jerry's. Founded in 1978 by Ben Cohen and Jerry Greenfield, Ben & Jerry's began with a single ice cream shop. Explosive growth netted Ben & Jerry's sales of more than $155 million by the year 2000, amid rumors of Ben & Jerry's becoming the target of takeover interest. The rumors were confirmed as Ben & Jerry's was acquired by Unilever, an Anglo-Dutch corporation, in early 2000.

Nothing in the foregoing overview captures the spirit of social entrepreneurship undergirding Ben & Jerry's. In 1985, company founders Ben and Jerry institutionalized their long-standing commitment to social and environmental issues by establishing the Ben & Jerry's Foundation, funded through donation of 7.5% of the company's annual pretax profits. The company has not relegated its social and environmental action to its funding of the Foundation. At every decision point, the leadership of Ben & Jerry's has sought to provide social benefits from the ongoing operation of their primary business. Among many other initiatives, in a successful effort to divert its ice-cream waste from the local wastewater treatment facility, Ben & Jerry's began feeding a pig farm with its ice-cream waste; the company helped establish a nonprofit initiative known as "1% for Peace"; they came out against bovine growth hormone, based on concern about its adverse economic impact on family farming; introduced Rainforest Crunch ice cream through its scoop shops, with sales of the ice cream indirectly benefiting rainforest preservation efforts; and to help combat Vermont dairy farmers' losses during a period of volatile prices in the dairy industry, Ben & Jerry's paid a dairy premium totaling half a million dollars to the family farmers who supply the milk for Ben & Jerry's ice cream.

The Not-for-Profit Sector

Not-for-profit social entrepreneurship is represented by organizations that have legally defined themselves as existing for some other purpose than to generate profit, a direct inverse to for-profit organizations. However, within this model, many of these organizations are engaging in what would typically be classified as for-profit business practices to attain sustainability within their business model.

Within the not-for-profit sector, three primary types of organizations exist—public benefit, mutual benefit, and religious. The most common use of social entrepreneurship within this sector is within those designated for public benefit. This is because of the nature of the models; a public benefit not-for-profit exists to benefit the public. Both mutual benefit and religious not-for-profits are less focused on widespread social improvement and are more focused on providing services for a very specific audience. However, it is still possible for social entrepreneurship to exist in each of these types.

The social entrepreneurship model is often mistakenly associated with social activism within the not-for-profit sector; however, the two concepts are fundamentally different. Social activists pursue a social goal as their main mission but are distinguished from social entrepreneurs because they pursue these changes external to the business environment. The distinguishing factor in social entrepreneurship is that these organizations pursue their social goals while simultaneously engaging in market-driven activities. Organizations acting in this sector are typically less financially independent than those in the for-profit sector. With not-for-profit organizations, the fiscal gains through entrepreneurship act less as a method of profit generation and sustainability and more as a method of offsetting their costs or expanding their programs. While they are not as financially independent as their for-profit counterparts, the offset expenses do allow these organizations to engage in more creative opportunities that may not be possible through grants and donations alone.

However, with the expansion of revenue streams for these organizations, an issue arises with the allocation of these subsidizing revenues. Within the United States, any income a not-for-profit generates that is not substantially related to the social purpose of the organization becomes taxable. This is the result of the competition for the consumer's purchasing power. Many for-profit organizations feel that without the tax an arena is created for unfair competition. For many not-for-profit organizations, this means that becoming entrepreneurial and seeking new revenue streams may not be as effective as hoped.

Ben & Jerry's is again instructive on this point. Perhaps the company's most notable foray into social entrepreneurship has been the establishment of the PartnerShop program, a series of scoop shops that are independently owned and operated by community-based nonprofit organizations. Ben & Jerry's waives the standard franchise fees and provides additional support to help nonprofits operate strong businesses among youth and low-income folks by providing economic development and employment opportunities. It should be noted that social entrepreneurship has been around for centuries in the form of enterprises such as gift shops and thrift shops associated with churches and museums.

The Public Sector

Outside of entrepreneurship in the private sector, it becomes more difficult to engage in social entrepreneurship, often because of inherent political and administrative constraints. Whereas the not-for-profit organization can be burdened with donors and grants who have predefined goals for the organization, the public organization is also held to often more stringent preestablished rules, regulations, and legislation. However, where the public sector has succeeded in engaging in social entrepreneurship, such efforts have enabled the institutions to expand beyond their previous constraints, thereby increasing the effect and reach of their mission. The driving force for entrepreneurship in the public sector has been a combination of a need for increased resources to fund specific programs and for a way to counteract the perceived inefficiencies of government programs.

Given that entrepreneurial activities such as risk taking are often looked down on by the public and government officials, social entrepreneurship often occurs much more frequently than intrapreneurship. Typically, entrepreneurship occurs when tasks are outsourced from local governments to organizations created specifically to coordinate specific tasks for the government outside of the public sector where it is able to function beyond the typical regulatory constraints. These organizations are then able to not only support the programs or entities they were designed to support through their services or products but are also able to generate extra revenue by expanding their programs to other organizations that can derive benefit from them.

There exist numerous examples of social entrepreneurship within the public sector. Following years of developing customized information technology applications for in-house use, the City of San Diego outsourced its information technology function to a standalone not-for-profit entity, the San Diego Data Processing Corporation. One principal goal of this initiative has been to successfully market government-specific technology applications to other California municipalities, all the while continuing to meet the technology needs of the elected officials and staff of San Diego. Product endorsements and "city stores," which sell items such as customized street signs, are becoming increasingly common; at the state and national levels, adopt-a-highway programs represent efforts by governmental agencies to engage in social entrepreneurship that serves to offset the high cost of road maintenance through revenue-generating alliances with private business enterprises.

Securing Funding for Social Entrepreneurs

Similar to profit-oriented entrepreneurship, social entrepreneurship is often a process undertaken by individuals who have a vision and are pursuing that vision. Funding for these ventures can come from grants, donations, or what has been called social venture capital. Social venture capital, first defined by Ashoka, is the process of securing funding to advance the interests of the organization through investors who wish to have a stake in the organization. As such, social venture capital is often focused within the for-profit sector of social venturing; however, it is possible for social venture capital to be invested in not-for-profit sector ventures as well.

An important issue in building social venture capital has been designing a way for investors to receive feedback from the organizations they have invested in to know whether their investment has been successful or if the organization is not doing as well as it should be. In the typical venture, this can be done through simple financial analysis and benchmarking as the organization develops and evolves. With a social venture investment, this is much more difficult because of the difficulty of measuring social impact. The success with developing these social feedback tools is evident through the rising number of organizations that have been created to provide social venture capital such as Ashoka, Social Venture Partners, the Social Venture Capital Foundation, the Schwab Foundation, and others.

Measurement Tools for Social Entrepreneurship

Regardless of the sector social entrepreneurship occurs in, it has become increasingly important to design methods to measure the impact social entrepreneurship has on its stakeholders. Much of the measurement throughout its history has relied on qualitative, case-based research. While this type of research has been able to define the areas that social entrepreneurship affects, it is less effective at measuring the actual level of impact that it has on society. The need for measurement has led to the development of tools that allow organizations to measure both financial and social impact. This is frequently called double-bottom-line (DBL) or triple-bottom-line (TBL) analysis. TBL divides the goals of an organization into three sectors—social, environmental, and financial. DBL divides the goals into two sectors—social and financial. DBL is the more often cited tool within social entrepreneurship, but both attempt to achieve the same goal of dividing the organization's impact into defined areas and measuring the effectiveness of that impact in each area.

To measure the goals of an organization using DBL, they are often redesigned in a way that allows the impact on society to be quantitatively measured. This enables the organization to track the success or failure of its social initiatives similarly to that of a financial initiative. Columbia University's Research Initiative for Social Enterprise (RISE) is one group that has contributed to this research. They have identified and analyzed several methods for identifying and measuring social impact. Their efforts have identified social impact measurement in three key areas of analysis—processes, impact, and monetization. Process analysis allows organizations to measure the correlation of their outputs with their social goals. Impact analysis allows organizations to analyze the effect these outputs have on society and compare them with the next best alternative for their resources, a method that is equivalent to measuring the opportunity costs of the organizations' operational processes. Monetization analysis allows the firm to place dollar values to its social impact and is the most effective in demonstrating a direct correlation between money invested and the social return.

One example of monetization analysis is social return on investment. This method, designed by REDF (formerly the Roberts Enterprise Development Fund), is used to develop a cost-benefit analysis of a social project. Rubicon Landscape Services used this method to analyze the impact their organization made by employing people with disabilities and economically challenged individuals. By calculating the amount of money they were saving the government in social service costs and the amount of additional tax revenue generated through their employment, they were able to measure the impact this program had on society with a precise dollar amount.

All three measurement methods enable the social entrepreneur to gauge his or her success at using the organization's resources in the most effective manner to support the social mission. In addition to the RISE project, many other organizations have also begun developing their own private and publicly available measurement tools, which provide a way for social venture capitalists to measure the impact of their investment, as well as a way for organizations to gauge their own success and make adjustments as they grow.

Criticism of Social Entrepreneurship

Critics of social entrepreneurship, and corporate social responsibility, believe the purpose of business activity is to serve the interests of stockholders, leaving social action to entities existing beyond the private for-profit sector. These critics argue that business leaders are ill equipped to make informed social decisions and that business leaders are solely responsible for acting in a manner that benefits the individuals who have employed them. This stance is grounded in the theory that economic returns and social returns are inherently at odds with one another, causing the pursuit of one return to reduce or eliminate the other.

Social entrepreneurs have found that this stance is inadequate for serving the needs of the community. Entities beyond the private for-profit sector have been unable to provide for many of the needs of the community. Social entrepreneurs have identified this gap in service as a viable business opportunity. The businesses built on these opportunities have a positive link between economic returns and social returns, both within the organization, and in its influence on its stakeholders. Thus, although many critics believe that social responsibility is counter to economic responsibility, social entrepreneurs have found a method that allows the two to act in parallel.

Education

Along with the growing number of social investment and analysis organizations, social entrepreneurship has also become increasingly popular with universities and other educational institutions. Many business schools have not only introduced social entrepreneurship into their MBA curriculum but some have also begun to build centers focused specifically on social entrepreneurship. Examples include Duke University's Center for the Advancement of Social Entrepreneurship, Columbia University's Research Initiative for Social Enterprise, and Oxford University's Skoll Centre for Social Entrepreneurship. In addition, competitions have come up to promote social entrepreneurship within these universities, such as the Global Social Venture Competition held at the University of California, Berkeley. Universities have also begun to reward competitors within traditional business plan competitions for being socially cognizant of their impact on society.

Conclusion

Social entrepreneurship has become an increasingly influential business model. It allows for organizations in all sectors of business to ground themselves on socially conscious missions and goals while still retaining the beneficial traits that have been previously available only to the for-profit sector. Social entrepreneurs are able to do this through recognizing and pursuing feasible business models that provide innovative products and services, allowing it to generate revenue while still serving its primary social goal. Social entrepreneurship has been given the opportunity to grow in impact and popularity due to its increased presence in the business and academic realms and will continue to expand as a viable business model as the global society continues to call for more socially conscious and accountable organizations.

—Lance Schaeffer and Craig P. Dunn

See also Business Ethics; Capitalism; Corporate Social Responsibility (CSR) and Corporate Social Performance (CSP); Deontological Ethical Systems; Entrepreneurship, Ethics of; Market Socialism; Profit Maximization, Corporate Social Responsibility as; Social Accountability (SA); Social Activists; Social Ethics; Stewardship; Strategic Corporate Social Responsibility; Utilitarianism

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Social Ethics

Ethics is the application of normative standards to assess right action. Social ethics focuses on the ethical reflection as it pertains to social structures and communities of persons such as our government, school systems, and church organizations and refers to a set of standards around which we organize our lives and from which we define our duties and obligations. It results in a set of norms that establishes acceptable behavior patterns and is concerned with what people ought to do. Examples of social ethical dilemmas that occur in the business environment are privacy rights; sexual harassment; gender, age, and race discrimination; child labor; and environmental protection.

Who Determines What Is Normative?

From a social constructionist perspective, what a society or organization considers to be "ethical" is a product of dialogue among its members. Dictionary definitions of *ethics* and *ethical* support this view. It is the members of a particular group that define what is or what is not ethical based on the meaning making done in their own processes of dialogue.

Dialogue originates in the public sphere, and those words, statements, and expressions are essentially actions performed with social consequences. Kenneth Gergen argues that dialogue is a form of coordinated action and the meaning of any utterance depends on its functioning within a relational environment. Because meaning is born in relationship, an individual's lone utterance contains no meaning. Rather, it provides the potential for meaning, a potential that can only be realized through another's contribution. This back and forth dialogue is the key building block to creating shared meaning and a shared reality. The central focus of generative dialogue is to bring realities (such as systems of social ethics) into being and bind them to particular patterns of action.

Ethical issues become a domino effect, and the logic of one is used by the culture to frame the debate on the other. One powerful example of this is bioethics. Biotechnology and genetics technology is advancing faster than any other area of our culture. The Human Genome Project, funded by the federal government, mapped the DNA strands to identify every human gene and its function. The results mean a degree of control that the human race has never had before. What will we do with this knowledge and control? Should we clone human beings? How should we think about the issue of using animal organs in human beings? Should we place animal tissue in human beings? Should we use gender selection when parents want to choose whether to have a boy or a girl? All these medical practices are currently being done or can be done.

This same logic is used in the euthanasia debate, where the focus is on the right of the person to die with dignity. Some states now sanction doctor-assisted suicide using the implied right of privacy that formerly sanctioned the practice of abortion. Based on the implied right of privacy, a person who is ill and no longer desires to live can legally receive assistance from a doctor to commit suicide. With the baby boomers getting older, the pressure for widespread euthanasia will grow.

The Impact of Business on Society

This notion of ethics as a product of dialogue is particularly important in a business environment that is increasingly global and cross-cultural. Globalization represents an enormous intensification of ethical conflict; as organizations expand into foreign locales, there is a tendency for the reality within the organization to deviate from the surrounding community. The import of alien constructions of the real and the good may come into sharp conflict with local understandings. Particularly in developing nations, businesspeople face cultures, customs, and norms that may conflict with their own ethical standards. Examples of ethical issues that global managers face, which may be completely new to them, include corruption and money laundering, human rights under totalitarian regimes, workplace conditions, and environmental issues.

Ethical and legal concepts are contextual and culture specific. There is general disagreement on what behaviors or practices are considered appropriate, legal, ethical, or moral across cultures. What is commonly practiced and socially acceptable in one culture is repudiated in another. Ethics and morals differ not only among various countries but also among individuals in the same country. To contribute to the shared sense of what is good in the local community, organizations must discuss and integrate the values of the local community in their business practices. Notions of right and wrong or justice and injustice are validated by the values and attitudes of a given culture.

Large corporations are capable of influencing mainstream societal events. Their power is not only economic but also social and political. A notable example of a corporation weighing legal, financial, and ethical points of view is the case of Johnson & Johnson's response to the Tylenol crisis in 1982. Under the leadership of CEO James Burke, the company made the decision to clear all store shelves in the Chicago area of extrastrength Tylenol after several deaths had been linked to their product. In addition, the company recalled 31 million unsold bottles and was completely candid with the medical community, the media, and the public about the situation.

Privacy has become a major issue in recent years for both government and business. The vast amount of personal information that is collected and the need to protect this information became especially sensitive after the passage of the Freedom of Information Act in 1966. This act was intended by Congress to make the government more accountable for its actions but had the inadvertent consequence of compromising the confidentiality of information about private individuals. With the proliferation of new technologies, some businesses insist that workplace monitoring is necessary.

Supervisors can eavesdrop on the telephone conversations of employees and, for example, call up on their own computer screens the input and output of the computers of their employees. In addition to collecting records of telephone calls such as the number of calls, duration, and destination, some companies are collecting medical data from employee assistance plans, which help in handling personal problems and drug addictions. These data can be used to terminate employees or defend against workplace injury claims. In some cases, hidden cameras and microphones are used to observe workers without their knowledge.

Electronic mail (e-mail) is another area in which the right to read employees' e-mail has been debated. To avoid misuse of the company communication system or to investigate misconduct, some employers claim a right to monitor employees' messages. E-mail stored on company fileservers is often backed up on magnetic tape and can be easily restored, leaving a trail of information. In the event of employee misconduct, e-mail messages as well as voice mail messages have been used to strengthen a case to reprimand or even terminate an employee. Some argue that the evidence left in e-mail messages reveal the true nature of behavioral issues and provide useful insight into an employee's conduct. One recent example is of an employee manifesting erratic behavior including frequent unexplained absences and significant performance issues. On reading this employee's e-mail, it was discovered that she was running a drug dealing operation—selling prescription drugs to other employees as well as outside contacts.

The growth in database marketing has also been facilitated by computer technology, which is able to combine data from many sources and assemble them in usable form. Consumer privacy can become an issue when health information such as prescription data from pharmacies and patient records is shared and used to target a market for direct mailings. Internet users often find data mining "cookies" stored on their hard drives after visiting online stores, which recognize repeat users of their Web site from past visits. Cookies benefit users by eliminating the need to enter information each time, but they can also provide the site owner with data about what pages are visited; how much time is spent on each one; and demographic data such as age, gender, and zip code without the owner's consent.

Another example of social ethical issues facing business organizations is discrimination that may occur in a variety of situations such as age, religion, race, gender, and sexual orientation discrimination. Discrimination is an ethical issue beyond any legal protections because it is at the core of fairness in the workplace. Discrimination can be a subtle or not-so-subtle factor in hiring, promotions, and layoff decisions. People who do not fit the "corporate profile" may be passed over for advancement for a variety of reasons that are not covered in legislation. Some employers create job requirements that could automatically eliminate certain employees, not because of their qualification but because of personal circumstances. An example of this is age discrimination resulting from the benefits that employers perceive in marginalizing or shunting older employees aside to make room for younger employees who may be considered to have more up-to-date skills and innovative ideas. Younger employees are less expensive to employ because older employees generally have higher salaries and make more use of the fringe benefits.

Religious discrimination in employment involves conflicts between the religious beliefs and practices of employees and workplace rules and routines. Employees sometimes request revised work schedules for time off to observe religious holidays or Sabbath observance. Members of some religious groups have special dress or grooming requirements, such as a yarmulke for Jewish men and a turban and a beard for Sikh men. Some employees have religious objections to performing certain kinds of work or to submitting to medical examinations; others request prayer breaks and special foods in the company cafeteria.

Several large corporations such as Intel and IBM have created GBLT (gay, lesbian, bisexual, transgender) business units that work directly with GLBT business units in other organizations. One idea behind the creation of these business units is to provide a safe, nonhostile, open, and inclusive working environment for GBLT employees. Managers within these corporations realize the effectiveness and work productivity that is created when individuals share a social identity.

Increased attention to the problem of sexual harassment and developments in the law has made employers more aware of their responsibilities. Some employers struggle to define sexual harassment as well as determine how serious the problem may be and who is responsible for preventing it. In 1980, the Equal Employment Opportunity Commission (EEOC) issued guidelines on sexual harassment that made a distinction between two kinds of harassment. One is *quid pro quo* harassment, in which a superior uses his or her power to grant or deny employment benefits to exact sexual favors from a subordinate. The other kind is *hostile working environment* harassment, in which the sexual nature of the conduct of coworkers and others causes an individual to be very uncomfortable. Whether a work environment is hostile or offensive is not easily determined, and much depends on the attitudes of the employees involved and the response of management to employee concerns.

Social ethical issues engage our deepest values and beliefs. The ideal of a nondiscriminatory and just society is clear, and finding the proper solutions to such challenging social ethical dilemmas requires an ongoing dialogue. It is imperative that an open and honest dialogue continue where beliefs, values, and opinions about social ethical issues are respectfully considered.

—Anne Kohnke Meda

See also Absolutism, Ethical; Age Discrimination; Family-Friendly Corporation

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Social Investment Forum

The Social Investment Forum (SIF) is a national non-profit trade association, based in Washington, D.C., dedicated to promoting the concept, practice, and growth of socially and environmentally responsible investing. As of January 2006, the Forum's membership included more than 600 social investment practitioners and institutions (private investors are served by joining the SIF partner, *Co-op America*).

Founded in 1981, the SIF conducts and communicates research on socially responsible investment. The Forum provides listings of financial professionals, mutual funds, information sources, and community investments that provide socially responsible investing. With its Web site, annual conference, socially responsible investor mailing list, membership directory, and Listserv, SIF supports a community of committed financial professionals. Furthermore, it offers an annual monetary award, the Moskowitz Prize (named for the pioneer investigator Milton Moskowitz, senior editor of *Business and Society Review,* who first published comparisons of the financial performance of screened and unscreened portfolios). The award recognizes outstanding research on socially responsible investing.

The Moskowitz Prize, begun in 1996, is the only global award recognizing outstanding quantitative work on socially responsible investing. The three criteria for the award include (1) the practical significance to practitioners of socially responsible investing, (2) the appropriateness and rigor of quantitative methods, and (3) the novelty of the results. Beginning in 2006, the prize will be administered by University of California at Berkeley's Haas School of Business. SIF will continue to serve as a consultant in prize awards.

News and trends in the socially responsible investment industry are reported by the Forum on its Web site, at its annual conference ("SRI in the Rockies"), in its quarterly newsletter to members, and in its biennial report on social investment trends (the latest report is titled "2005 Report on Socially Responsible Investing Trends in the United States, 10 Year Review").

A related program, Social Investment Forum Advocacy & Policy Program, provides communication, research, and advocacy on public affairs related to socially responsible investing.

—LeeAnne G. Kryder

See also Corporate Accountability; Corporate Social Responsibility (CSR) and Corporate Social Performance (CSP); Finance, Ethics of; Shareholder Activism; Socially Responsible Investing (SRI); Triple Bottom Line; Values, Personal

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Socialism

Socialism is an ideology that places great emphasis on eliminating, or reducing, the disparity between social classes, largely through the more equal distribution of resources, including property. Variations of socialist thought have existed for hundreds of years, evidenced by Plato's *Republic* and even the Book of Acts in the New Testament. In a socialist society, the means of production are owned and controlled by the community as a whole. In a capitalist society, however, the resources and businesses are owned and operated by private parties. Furthermore, at the heart of capitalism is the belief in a free market that operates with minimal restrictions.

This entry will briefly examine current versions of socialism, followed by a review of socialism through modern history, and will end with an assessment of the status of socialism today.

Socialism Today

Despite the fact that North Korea and Sweden both have socialist governments, they are at opposite ends of the spectrum in terms of their political applications of socialism. In North Korea, a socialist country since 1948, all means of production are state owned. Furthermore, it essentially is a totalitarian dictatorship, where the single ruling party quells all forms of dissent, thus alienating the regime from democratic world powers. North Korea's socialist state has also been plagued with difficulties. It has experienced widespread poverty and famine since the end of Russian subsidies in the 1990s.

Socialism in Sweden, however, is characterized by relative prosperity within a multiparty, democratic state and a mixed economy. Sweden, a socialist country since World War II, differs from North Korea in that most business enterprises are privately owned. Socialism in Sweden focuses more on providing social welfare services than on communal ownership and control of the means of production. Northern European socialist movements are often called "social democratic" to indicate their gradualist social welfare agenda and compatibility with democratic values and institutions. To better understand the variations between countries such as Sweden and North Korea, it is necessary to have some historical background on the socialist movement.

Response to European Industrial Revolution

Socialism emerged in Europe in the early 1800s, largely in response to the failings, or perceived failings, of the Industrial Revolution. The Industrial Revolution began in Great Britain. Technological innovations, such as the creation of the steam engine in the 1780s, were applied to both manufacturing processes and to new means of transportation. The factory system, coupled with the development of large and complex railroad networks by the 1840s, dramatically enhanced Britain's productive and distributive capacity. Britain's competitive advantage was expressed in the rapid expansion of its international trade, both inside and beyond its colonial empire.

While Great Britain advanced into the industrial age, the rest of mainland Europe lagged behind. The French Revolution and subsequent Napoleonic Era (from the 1790s to 1815) fostered political, social, and economic instability, thus impeding industrial development on the continent. The working class, and its defenders, grew increasingly frustrated with the industrialized society that gradually enveloped them. It was in this context of rising discontent with unfettered capitalism that socialism gained popularity.

Early Socialists, Including Karl Marx

Early socialist ideas appeared in post-Napoleonic France, as French thinkers and economists attempted to grapple with the new industrial world that was emerging. For example, individuals such as Count Henri de Saint-Simon and Louis Blanc argued that it was the duty of the government to close the income gap between the propertied and working classes. They advocated government intervention to distribute private property more equally.

Germany also had its share of socialist pioneers. German nation-states (Germany was not a unified nation until 1871) witnessed the influx of the cheaper English-made goods during the 1820s and 1830s, devastating individual craftsmen and German society as a whole. Displaced workers blamed the laissez-faire capitalist society they lived in, which allowed a few wealthy industrialists, bankers, and merchants to prosper while the working class as a whole suffered. It was amidst this dissatisfaction with capitalism that socialism further developed as a concept under Karl Marx, a German-born philosopher.

Marx differed greatly from the earlier socialists. Whereas earlier French socialist advocates had pleaded for help from the middle classes, Marx heaped scorn on the "bourgeoisie," claiming that the middle classes had no interest in helping out the working classes or changing the status quo. Marx thought of socialism as merely a transitional phase between capitalism and communism, a classless and stateless society where property and resources would be distributed equally among all people. In the *Communist Manifesto* of 1848, written by Marx and Friedrich Engels, another prominent German thinker, the authors predicted a bloody socialist revolution between the bourgeoisie (middle class) and the proletariat (working class). In the end, the numerically superior proletariat would triumph and confiscate all private property and distribute it equally among the masses. The state would also regulate all social, political, and economic decisions, and eventually class divisions would erode and the society as a whole would prosper. Once these gains were achieved, the state would wither away, thus creating a communist society where all worked together in cooperation and harmony.

Marx's ideas fascinated many Germans, as many believed that capitalism was clearly flawed, evidenced by the high poverty rate and unequal distribution of resources in the various German nation-states in the 1840s. As a result, socialist radicals and other liberal nationalist reformers rose up in arms and attempted a hostile takeover of Prussia, the most powerful German nation-state, but they were ruthlessly squashed by the ruling class in the failed revolution of 1848. In the wake of the failed takeover, the Prussian government sought retribution against those who had taken part in the revolution and, as a result, many of the participants fled Prussia in terror.

Socialism in the United States

Socialism did not die with the revolution of 1848, as socialist-leaning Germans took their ideas elsewhere in Europe and to the United States. Between the 1840s and 1860s, Germans made up more than 25% of all immigrants into the United States. Socialism's relative popularity can be seen in the U.S. labor movement in the 1870s and 1880s. Socialists, particularly German-American socialists, were active in a variety of labor struggles. Socialists were especially visible in the struggle for the 8-hour workday, which reached a disastrous culmination in Bayview (Milwaukee, Wisconsin) and Haymarket Square (Chicago, Illinois) in 1886, where state militias and local police opened fire on demonstrating, unarmed workers.

Despite the hostility that socialists encountered in America, a socialist party was formally created in 1901, with Eugene Debs as its presidential candidate. Debs received more than 400,000 votes in the presidential election of 1908 and roughly 800,000 votes in 1912.

Socialism lost power in American politics in the aftermath of the socialist-led Bolshevik Revolution in Russia in 1917. The Bolshevik Revolution essentially destroyed the fledging socialist movement in the United States, as all socialists were viewed as proponents of violent upheaval and, therefore, socialism lost most of its appeal.

Bolshevik Revolution

As previously mentioned, the Bolshevik (majority) Revolution occurred in 1917, under the leadership of Vladimir Lenin and other prominent Russian socialists. The Revolution took place because of the severe poverty and unequal distribution of resources in the czarist nation of Russia. Further fanning the flames of revolution was the devastation caused by Russia's involvement in World War I.

Leninism was predicated on the belief that socialist change could only occur through a violent revolution. The Communist Party "vanguard" ruling elite exercised autocratic power in the name of the "dictatorship of the proletariat." Dissidents were eliminated ruthlessly. Lenin's successor, Joseph Stalin, forced Russian peasants onto collective farms and applied a central planning model to develop heavy industry.

The Bolshevik Revolution created deep fissures within the socialist camp. Many believed that the creation of the Soviet Union was merely an extension of what Marx envisioned. Other socialists, however, believed that a socialist society could be created through peaceful means via democratic methods.

Huey Long and the New Deal

Socialism witnessed something of a revival in the United States in the 1930s, largely due to the Great Depression. Many Americans looked at the Great Depression as proof of the failings of unregulated capitalism and, thus, were more willing to embrace other ideologies, such as socialism. For instance, Huey Long, the abrasive Louisiana politician, firmly embraced aspects of socialism within his Share Our Wealth (SOW) society. As part of his SOW plan, Long stated that every American should have a car, a house, a radio, and other basic necessities. Long also spoke of confiscating all incomes more than $1 million a year and using the confiscated monies to support SOW. In addition, Long claimed that the state should confiscate all family fortunes in excess of $5 million.

In the context of the Depression, the SOW program drew widespread support, not only from Louisiana and other poverty-stricken areas in the South but also from around the country. President Franklin Delano Roosevelt (FDR) witnessed the popularity of Long's SOW program and sought to squelch any possibility of Long's ascendancy to the presidency. Therefore, FDR adopted many of Long's ideas and put them forth as part of his New Deal legislation, thus robbing Long of his popularity. The New Deal created many of our contemporary social welfare programs in the United States, such as unemployment insurance and social security.

Socialist Setbacks in the United States

After World War II, socialist-leaning thought once again lost appeal in the United States for two main reasons. First, World War II crippled Japan, Germany, France, and Britain, leaving the United States and the Soviet Union as the two remaining superpowers. Even though the two were allies for much of World War II, they became mortal enemies in the postwar years, as each nation sought to prevent the other's ideology and way of life from spreading across the globe. In essence, the world was reduced to a geopolitical chessboard, on which Cold War moves were played.

With the emergence of the Cold War, countless Americans grew paranoid about a possible communist revolution in the United States. The irrational fear manifested itself in McCarthyism, named after the firebrand senator from Wisconsin, Joseph McCarthy. Any group or individual with progressive leanings during this era was labeled as communist and, therefore, was portrayed as a threat to the internal security of the United States. Labor organizations in the United States, such as the American Federation of Labor, engaged in their own leftist witch hunts, so that no one could levy devastating procommunist allegations against them. As a result, socialism in the United States suffered a crippling blow from which it would never recover, even with the worldwide collapse of communism in the late 1980s.

The second reason for the eclipse of socialism in the United States was the relative prosperity of the American working class in the postwar years. World War II generated unheard of sums of wealth, not only for the leading industrialists but also for their workers. Therefore, where the Great Depression provided a fertile testing ground for the spread of socialism, the "Golden Years" of the 1950s greatly dampened the appeal of socialism in America.

Socialist Success in China and Elsewhere

Though reduced to a fringe movement in the United States, socialism throve elsewhere. China became the second nation to witness a socialist revolution, as socialists came to power in 1949, largely because of the devastation and turmoil caused by World War II. Chinese socialists, led by Mao Tse-Tung, adopted their own brand of socialism that once again focused on the violent seizure of power and redistribution of societal resources, which was viewed particularly favorably by landless peasants. China was also akin to the Soviet Union in that both were totalitarian states.

China was not the only country to undergo a socialist revolution. World War II created a power vacuum throughout the world, as former European imperial powers, such as England, France, and Germany, could no longer afford to maintain their colonial empires. Countless countries in Africa, Latin America, and Asia witnessed liberation movements, some of which were socialist in nature. For instance, many Vietnamese united under a socialist and nationalist movement, led by Ho Chi Minh, to oust the French and form an independent Vietnam.

Socialism also played a prominent role in the Cuban revolution of 1959. The gross social inequality and poverty of prerevolution Cuba provided a perfect breeding ground for socialism. The Cuban revolution was led by Fidel Castro, whose promises of equality and social justice found widespread appeal. Once again, however, the violence associated with this takeover, and the land seizures, was very akin to Leninist socialism.

Numerous African countries experimented with socialism in the wake of their independence movements in the 1950s to 1970s. For instance, Tanzania, under Julius Nyerere, was a socialist nation until the 1990s.

Various Latin American nations, such as Chile, also turned to socialism in democratic elections in the 1970s, only to have their governments undermined by procapitalist forces, led by the United States.

Current Situation

Socialism as a whole suffered great losses in the late 1980s and 1990s, largely as a result of the development of the highly interwoven economic system known as globalization. Advancements in communication and transportation technology allowed for the world to become more interconnected than was ever possible before, thus paving the way for globalization. Leading the globalization revolution was the United States, the sole remaining superpower in the wake of the Soviet Union's collapse in the late 1980s. Therefore, globalization revolves around the United States and the concept of free market capitalism.

Due to globalization, only handfuls of states currently remain socialist, and among these remaining countries, there is a great degree of variation. For instance, on one end of the spectrum are the socialist nations of Cuba and Vietnam. A much different form of socialism exists in Scandinavian countries such as Denmark and Norway. For instance, the socialist governments in Scandinavia are democratically elected, and most businesses and corporations remain privately owned. The governments are responsible for maintaining a very comprehensive welfare state, however. In addition, socialist countries in Scandinavia are characterized by the lack of an impoverished class, as well as high taxes.

In closing, socialism continues to live on in varying forms and is actually witnessing a resurgence in Latin America. For instance, Uruguay, Bolivia, Chile, and Venezuela all have recently elected socialist-leaning governments. The rise in socialism in Latin America can be explained, yet again, by dissatisfaction with extreme poverty and highly unequal distribution of resources. The newly elected socialist governments in Latin America, however, are more ideologically similar to Scandinavian governments than they are to Cuba, as they feature privately owned enterprises, mixed with some level of state ownership. In all likelihood, however, these newly elected governments in Latin America will soon witness more of an integration of free market capitalism, because globalization appears to be inevitable. Yet the world will continue to witness periodic socialist movements in response to the perceived failings of globalization, as developing countries will have difficulty keeping pace with the more developed countries that are already firmly part of a global economy.

—Andrew Witt

See also Communism; Engels, Friedrich; Equality; Marx, Karl; Marxism; Redistribution of Wealth

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Socially Responsible Investing (SRI)

Socially responsible investing (SRI) refers to financial contributions into investment vehicles designed to combine the traditional investment philosophy favoring profit maximization with a values-based component seeking nonfinancial benefits. Such nonfinancial benefits are often referred to as social returns. These social returns vary in scope but can be broadly defined as company policies and actions that enhance a socially responsible investor's specific environmental, religious, or social values. These enhancements may or may not have any impact on the profit-maximization component of the socially responsible investment and may actually cause a socially responsible investment to decrease in value. *Socially responsible investing* is the common term for this practice in the United States but the concept is also referred to as "ethical investing," primarily in the United Kingdom, or "values-based investing."

Today, major institutional investment groups such as corporations, hedge funds, insurance companies, mutual funds, pension funds, religious institutions, and universities, along with the environmentally/religiously/socially motivated individual investor, are entering the realm of SRI. According to the Social Investment Forum (SIF)—the most prominent SRI industry group—more than $2.16 trillion was invested in 2003 in professionally managed portfolios that implemented at least one core aspect of SRI. The SIF claims that this figure, representing one out of every nine dollars invested professionally in the United States, grew from $1.19 trillion in 1997 and from $40 billion in 1984. On the other hand, it is important to note that many scholars and investment professionals remain skeptical of this investment philosophy. Many academic studies demonstrate that socially responsible investors are not able to achieve either their desired social objectives or a competitive return, at least when compared with traditional investing practices focusing on profit maximization alone.

SRI is an umbrella term covering three core investing groups—(1) environmentally motivated investors, (2) religiously motivated investors, and (3) socially motivated investors. While all three groups seek social returns along with capital appreciation, the major difference between the groups stems from the motivations behind their investment practices. Environmentally motivated investors seek corporate policies and actions that either benefit or do no significant harm to the environment—both in the United States and abroad. Religiously motivated investors are guided by specific faith-based issues such ethical treatment of employees. Socially motivated investors, on the other hand, desire company policies and practices that adequately address key social issues such as diversity, HIV/AIDS, as well as corporate governance. The history of SRI demonstrates that all three groups played a prominent role in the establishment of SRI as a major player in the investing landscape of the 21st century.

SRI also encompasses three core subject areas—(1) social screening, (2) shareholder advocacy, and (3) community investing. While social screening is by far the most popular of these categories—with $2.14 trillion invested in this manner in 2003—each of the other areas comprises a growing component of the SRI community.

A Brief History of SRI

SRI has religious roots. In fact, scholars trace the earliest form of social screening of investment opportunities back over 2,000 years to the Hebrew Bible. More recently, socially conscious investors played a major role in the religious communities of pre- and postrevolutionary America. In prerevolutionary America, the Methodists, followed by the Quakers, developed the habit of refusing to support companies involved with alcohol, gambling, or tobacco. Investments in all three of these industries were considered "sin stocks" and were screened out—or ignored—by the commercial practices of early American religious communities. The institution of slavery was also an issue of concern to many early American socially responsible investors, with specific groups avoiding companies dealing in the slave trade.

From the 17th century until the mid-20th century, the concept of socially screened investment remained a small, religiously centered, movement. However, in the 1960s, as movements against the Vietnam War emerged alongside the civil rights, women's rights, and environmental movements, investors took a renewed interest in SRI. Socially responsible investors, in tandem with a multitude of other groups and institutions, wanted to be certain that their investment money was not being used to support the war or to keep minorities in a second-class status. The key issues for SRI advocates in the 1970s were the nuclear arms race and the environment. It was during the 1970s that the first socially responsible mutual funds were created, allowing investors to pool their funds together to achieve greater social returns. In the 1980s, worldwide attention focused on apartheid in South Africa and companies were lobbied by the SRI community—and eventually mandated by the Anti-Apartheid Act of 1986—to stop doing business in South Africa.

The decade of the 1990s saw a renewed interest in the environment and the somewhat tenuous relationship between the corporate mission of profit maximization and corporate policies and practices designed to protect the environment. These issues coincided with the commencement of the major tobacco litigation cases and calls for avoidance of one of the top three "sin stocks"—tobacco. The most relevant SRI topic from the dawn of the new millennium to the present is corporate governance. Originating with the recession of 2001 and peaking with the major corporate scandals that plagued the economy thereafter, corporate governance and business ethics have become major issues in the SRI community as well as in the traditional investing world. Interestingly, a few key issues retained prominence over this half-century period of modern SRI. Issues such as abortion, contraception, HIV/AIDS, sin stocks, and unfair labor practices in Third World countries remain compelling and are always on the radar screen of SRI.

Three Categories of SRI

As mentioned above, SRI is traditionally divided into three core categories—social screening, shareholder advocacy, and community investing. These three categories are not mutually exclusive—for example, a socially responsible investor may practice social screening while also investing in community development projects. The majority of socially responsible investors, however, focus on social screening and shareholder advocacy, although community investing is growing in prominence as the SRI movement itself expands.

Social Screening

Social screening is a means by which investors either divest a financial holding or invest in a particular company based on the company's social record—or lack thereof. The basic premise underlying social screening is the idea that companies that meet the social standards required by SRI screens will be the most profitable and successful companies in the long term. Social screening can be divided into two types—(1) negative screening and (2) positive screening.

Negative screening occurs when an investor divests a specific stock or industry group holding from a portfolio based on a company's practices diverging from some criteria of social investment. Once an investor screens a stock out of a portfolio, the ownership relationship between the company and the shareholder ends and often so does the investor's ability or desire to institute social change at the organization. It is for this reason that many shareholders refuse to sell shares of a company with a poor social record and instead choose the path of shareholder activism, as described below.

Positive screening occurs when an investor seeks out a specific stock or industry group and invests because of positive social policies and actions of the company. Many SRI organizations have created sophisticated software intended to search for just this type of investment opportunity. Companies that produce certain products—such as the sin stocks mentioned previously—have a hard time meeting the criteria required to be included in a positive screen. Interestingly, even a company producing a more socially accepted product will also miss the cut if such a company has poor corporate governance standards or employment practices.

Depending on the volume of shares subject to both negative and positive screening, such screening practices may alter stock prices due to the decreased demand caused by negative screening and the increased demand for a company's stock caused by positive screening. As SRI continues to grow in volume of dollars invested, SRI proponents hope such supply/demand attributes cause companies to become more responsive to the voice of socially responsible investors.

Shareholder Advocacy

While social screening is intended to serve the dual purpose of altering the supply/demand equation for a specific company stock and to satisfy the ethical desires of the socially responsible investor, this category is not the only means at the disposal of socially responsible investors to satisfy their goals. Investors desiring to change corporate practices often turn to the shareholder advocacy category. Shareholder advocacy proponents attempt to take advantage of share ownership and the potential of such ownership to obtain access to management and to other shareholders. This access can be a bit misleading, however, because the purchase of a small amount of stock will create a relationship with the company, but a more significant stake may be necessary to truly obtain access to and attention from company management. A significant ownership position allows shareholders to engage in three primary shareholder advocacy tactics: (1) discussions with management, (2) shareholder resolutions, and (3) boycotts.

Discussions With Management

The SRI community currently rallies around the idea that discussions with management should be the first step taken in efforts to create desired social returns. In fact, certain SRI institutional investor groups state that they will attempt discussions only and exclude other, more confrontational, shareholder activism tactics.

Discussions with management occur when shareholders group together and arrange meetings with high-level executives who run the company on such shareholders' behalf. Often, the issue discussed is a corporate policy or activity that the SRI proponents allege is endangering the environment (such as deforestation) or an issue shedding a negative light on the company's public image (such as excessive executive compensation). Often, if company management feels a change is warranted, these face-to-face encounters result in an amended corporate policy and no further action is necessary. Management is often more willing to engage in these informal discussions because a mutual understanding and compromise often limits the shareholder resolutions that occur under the second category of shareholder activism.

Shareholder Resolutions

Assuming the shareholder and management discussion session proves unfruitful, socially responsible investors often turn to a more structured and persuasive option—the shareholder resolution. A shareholder resolution is a proposal by a shareholder or a group of shareholders recommending a change in company actions or policies regarding a particular social issue. The proposal process and content requirements are governed by the Securities and Exchange Commission (SEC). The SEC mandates that proposals must be submitted to management at least 4 months before the company mails its proxy materials and can be no longer than 500 words. Such resolutions must meet other procedural hurdles as well; the proposals may only be advisory and nonbinding on management, and the proposing shareholder(s) must own at least $2,000 worth of company stock (or 1% of the company's total stock outstanding) and must have owned such stock for at least 1 year. If these procedural hurdles are met, then the proposal may be included in the company's annual proxy statement unless the company propounds one of a few specific regulatory reasons for exclusion. Once in the proxy statement, the proposal must be formally presented at the company annual meeting and then such recommendation is subject to a vote of shareholders present or voting via proxy.

Most shareholder resolutions concerning environmental, religious, or social issues do not garner a majority of shareholder votes. However, a mere 5% to 7% of the total votes cast in favor of a proposal at a company annual meeting may represent millions of shareholders—a large voice against the company practice at issue. Therefore, companies often take even the slightest approval rates as an impetus to enter into discussions previously avoided or to amend current company policy to comply with the desires of the proposing shareholders. Management likes to avoid shareholder resolutions because of the potential for negative publicity and because executives and the board of directors are charged with creating company policy and do not like policy dictated from shareholders who might not have a clear understanding of the complete operational picture. Investors, on the other hand, view this type of advocacy as an acceptable exercise of their power as owners of the company.

Another interesting development in this part of the shareholder advocacy process is that since August 2004, mutual fund managers have been required to publicly disclose their votes on issues that could materially affect their portfolios. Therefore, socially responsible investors holding shares through mutual funds—and therefore not allowed to vote their shares at the annual meeting—are now able to discern whether their particular SRI fund manager is helping them achieve their desired social returns.

Boycotts

Socially responsible investors also use various forms of protest—such as economic or physical boycotts—in an attempt to vie for corporate social responsibility. Although this form of shareholder activism can occur at any stage in the process, usually boycotts are attempted only after the discussion and resolution processes have failed. Many boycotts are purely economic protests whereby consumers refuse to purchase, sell, or handle a company's product or service on a local or a national level while also attempting to enlist more consumers to follow suit. Another form of boycott—the physical protest—is employed less often and resembles a social protest rally at which socially responsible investors might be joined by various other company stakeholders and physically protest outside a company establishment or headquarters. Both forms of boycotts use the publicity from the boycott to garner attention and support from other investors and from the general public for the social cause and against the company policy.

Community Investment

Community investment is the process by which socially responsible investors direct investment funds into lower-income and less economically successful communities that have been historically underserved by traditional financial services. The goal of community investing is to provide access to basic banking services, capital, credit, equity, and health care previously unavailable inside the community. These programs are designed to stimulate the economic growth such areas desperately need. Community development capital is most often used in microlending initiatives to lower-income entrepreneurs, building affordable housing, and assisting in employment efforts within the immediate area. Community development financial institutions—such as specialized banks and credit unions, venture capital community development accounts, and microenterprise loan funds—receive the majority of these funds and serve as the distribution center for the community investment area.

Community investment is the most recent addition to the SRI core categories. The concept, however, is demonstrating its potential based on a plethora of community success stories and a steadily growing resource base. From 2001 to 2003, assets held by community development institutions increased 84% from $7.6 billion to $14 billion. As SRI moves into the future, community investment appears as if it will compete for attention from socially responsible investors with the predominant tactics of social screening and shareholder activism.

—Corey A. Ciocchetti

See also Divestment; Domini Social Investments; Religiously Motivated Investing; Shareholder Activism; Shareholder Resolutions; Social Investment Forum

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Soft Dollar Brokerage

Soft dollar brokerage, or simply soft dollars, is an arrangement in which brokerage firms offer institutional investors products and services other than the execution of trades. Institutional investors, such as mutual funds and pension funds, pay a commission to brokerage firms to execute trades of securities. In addition to executing trades, brokerage firms offer some institutional investors credits for other products and services, most commonly proprietary research. These products and services, which are typically provided by a third party, such as research firms, are paid for by the brokerage firm. The credits for these products and service are called soft dollars.

This arrangement began in the 1950s with the growth of institutional investors during a period of fixed commissions for securities traded on the New York Stock Exchange. Barred from competing for volume customers by offering lower commissions, brokerage firms offered various nonprice benefits, including research services, in lieu of lower commission rates. After the system of fixed commissions was abolished in May 1975, the practice of soft dollars continued. Although commission rates declined after that date and customers could pay for only the execution of trades, soft dollar arrangements continued to be an important form of competition among brokerage firms and a significant source of resources for institutional investment funds.

The legislation ending fixed commissions, the Securities Act Amendments of 1975, reiterated that fund managers have a fiduciary duty to secure the best execution of trades, which includes paying low commissions. However, Section 28(e) created a safe harbor that allows soft dollar arrangements as long as the managers believe in good faith that a higher-than-market commission is reasonable in relation to the value of the brokerage and research services provided.

For such a little-known practice, soft dollars has received a surprising amount of moral concern, with some observers claiming that it did not pass "the smell test." Soft dollars was the subject of a 1998 report by the Securities and Exchange Commission, and in the same year, the Association for Investment Management Research issued extensive guidelines for soft dollar arrangements.

Moral criticism of soft dollars has two sources. First, soft dollars is a virtually invisible process that appears to depart from the ideal of arm's-length economic transactions. In soft dollar arrangements, the managers of institutional investment funds seem to be paying brokers more than necessary for executing trades and receiving other benefits in return. The costs of execution and research are bundled together in ways that other parties (e.g., mutual fund investors) may not be aware of and cannot easily evaluate. Expressed in the terms of agency theory, investors (the principals) have the task of monitoring fund managers (their agents). The lack of transparency and market forces makes the monitoring of fund managers by investors more difficult. As a result, investors either suffer the agency costs of inadequate monitoring or else are forced to incur additional monitoring costs. That transactions should be unbundled and made transparent are key elements not only of sound financial practice but also of effective monitoring.

Second, investment fund managers, as fiduciaries, have a fiduciary duty to act in the best interests of a fund's investors. This includes obtaining "best execution" and using any soft dollars solely for the benefit of a fund's investors. However, soft dollars appears to create incentives for fund managers to advance their own interests or the interests of a fund's adviser to the detriment of investors. This would be not only a violation of fiduciary duty but also an unacceptable conflict of interest. Fund managers might unjustly enrich themselves through soft dollar arrangements by engaging in excessive trading or "churning" designed merely to generate more soft dollars. They might also use soft dollars for purposes other than research that benefits a fund's investors, and finally, the benefit from soft dollars may make managers more careless about monitoring the quality of a brokerage firm's execution. All these possibilities would violate the safe harbor provision of Section 28(e), but critics of soft dollars complain that the vagueness of this law leaves investors with inadequate protection.

Some defenders of soft dollars argue that these moral concerns are misplaced and that soft dollar brokerage is not only morally justified but also economically sound. First, to the criticism that the practice tempts fund managers to violate their fiduciary duty to seek "best execution" and use any soft dollars in the investors' interest, defenders argue that the intense competition in institutional investing would punish fund managers who did not use all resources for the benefit of investors. Second, they argue that instead of increasing the monitoring costs of investors, soft dollars aligns the interests of investors and fund managers because fund managers are in a better position than investors to monitor the execution of trades by brokerage firms.

This agency argument is rather complex, but the debate between critics and defenders can be settled ultimately only by an empirical comparison of fund performance. If funds that use soft dollars produce superior returns to those that do not, then their practices, including soft dollars, would appear to be more efficient. The evidence to date is that soft dollars has a slightly positive correlation with fund performance, which suggests that the practice succeeds in solving investors' agency problems.

Critics of soft dollars generally favor two measures: restricting the scope of section 28(e), thus giving fund managers less of a safe harbor and mandating greater disclosure of soft dollar practices. Defenders of soft dollars would expand the scope of Section 28(e), thus giving fund managers greater discretion in making arrangements with brokerage firms. Although they are not opposed to greater disclosure, in principle, some defenders question the usefulness of this information for investors and whether the cost would exceed the benefit.

—John R. Boatright

See also Agency, Theory of; Churning; Conflict of Interest; Fiduciary Duty; Finance, Ethics of; Securities and Exchange Commission (SEC); Transparency, Market

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Speciesism

Speciesism is a term found primarily in the literature dealing with animal rights. It is used in a derogatory fashion to designate a bias or prejudice analogous to racism or sexism. In speciesism, the bias is in favor of the fundamental interests of humans as opposed to those of nonhumans. A "speciesist" would be someone who favors and demonstrates partiality toward humans over animals and who believes that humans have special traits that animals lack (reason, language, technological skills, etc.), thereby making them superior and more important beings. In this way, speciesism can be seen to be a product of a strong anthropocentrism that holds humans to be the focus of and purpose for the universe.

The first expression and use of the term *speciesism* in a formal way came in 1970 when clinical psychologist Richard Ryder of Oxford University used the term in a leaflet that he had privately printed about the abuses of animal experimentation and animal abuse. Ryder reported that the term came to him while he was taking a bath and contemplating the way humans treat animals. Since Darwin had shown that humans too are animals, Ryder thought that speciesism was just like racism and sexism—a form of prejudice based on morally irrelevant physical differences.

We can find more extended arguments about speciesism in the writings of animal rights advocates such as Australian ethicist Peter Singer. Singer is known as a "preference utilitarian," which means that morally correct action produces the most satisfaction of preferences. But, with respect to animals, Singer holds that they, just like humans, have such preferences or interests and that it would be a moral mistake to overlook their interests even though most people do. The mistake of not granting equal moral consideration to the interests of animals is a form of speciesism according to Singer. An even more egregious form of it would be to give the interests of human beings preference over those of other beings merely because the former interests are those of a human being. Hence, for Singer, it is more appropriate to treat all beings as individuals and not as members of a species.

The issue of animal experimentation in medicine is one that is often pointed to as being biased by speciesism. Animal rights advocates hold that animal experimentation in medicine is morally objectionable and should be discontinued. They argue that just because animal experimentation may lead to advances in medicine and this might be beneficial to humans, such benefit is no good reason to put animals in situations that cause them great pain and suffering as is the case with medical experimentation done on them. The claim that beneficial outcomes for humans is the result of such experimentation and therefore justification enough to continue the practice is nothing more than prejudice in favor of humans because they are humans, that is, a form of speciesism, in the eyes of animal liberationists.

—Peter Madsen

See also Animal Rights; Anthropocentrism; People for the Ethical Treatment of Animals (PETA); Utilitarianism

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Speculation and Speculator

Speculation is investing in some asset with the hope of profiting from a price change in asset. Sometimes speculation is regarded as a form of risky and imprudent investing, and some would contrast speculation with investing. A speculator is one who speculates. Speculation is an action that is the result of *speculare*—in other words, to observe from a height; of considering the signs of the stars to take a specific action at the propitious moment with the best probability of success; and of scrutinizing something intently. Speculation is applied to the environment of investment markets, referring to those operations in which someone—the speculator—buys shares or commodities at a low price in the hope of selling them at a higher price in the future, generally the near future. Those who speculate on the stock market are thus investors who move in the short term. At times, the speculator is associated with the player or the manipulator. However, there are important differences between them that are worth explaining, because "playing the market" and "manipulating the market" are generally considered somewhat unethical activities. Although speculation does not enjoy a good image in the public mind, it merits stating that genuine speculation contributes to the common good. This is because it improves the operation of the markets, while the manipulator always takes an unfair advantage at the margin of ethics by altering the prices of shares and the player operates on the stock exchange like someone who risks money on games of chance, without reflection and without any well-founded reasons to justify his bet. On the contrary, the person who speculates with good intentions, seeking a profit and assuming a risk, does so by implementing decision mechanisms that are quite different.

Speculation requires serious effort to gain a competitive advantage on other investors, anticipating possible future scenarios on which decisions must be taken today. Speculators with technical preparation and experience take detailed notice of the multiple short-term factors that explain the quotation price of a share. They study the direction of the economy, are alert to indicators, and rationally decide with knowledge about the cause on well-founded hypotheses.

The benefits of speculation are to reduce market fluctuations; to provide the market with liquidity; to increase the volume of transactions; and to efficiently place financial resources, through the agility with which speculators react—investing or disinvesting—to new information. In short, if speculation is carried out in good faith—that is, with professionalism and rigor, without any fraud or illicitness—we should consider it as a high exponent of economic intelligence.

However, there are some less desirable effects to speculation: If it becomes an end in itself and is immune to ethical considerations and the end objectives of economic life, it could contribute to increasing the distance between the financial and real economies. Furthermore, this distancing can create economic imbalance at a worldwide level, making the difference between rich countries and poor ones even greater.

—José-Luis Fernández-Fernández

See also Financial Derivatives; Gambling; Insider Trading; Manipulation, Financial; Securities and Exchange Commission (SEC); Transparency

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Spencer, Herbert (1820–1903)

Herbert Spencer was a British philosopher and sociologist who developed and applied evolutionary theory to areas such as psychology and sociology and whose influence at the time was almost as great as that of Charles Darwin. But his evolutionary theory, which accepted the view of Lamarck that organic modifications produced by use and disuse are inherited, gradually gave way to Charles Darwin's theory of natural selection.

Spencer's first book, *Social Statics, or the Conditions Essential to Human Happiness*, in which he argued that what characterizes the development of organisms is the tendency to individuation, presents a defense of human freedom and individual liberties and attacks the utilitarian claims of Jeremy Bentham and John Stuart Mill, with its understanding of individuals as merely the means to the goal of the general social well-being. Spencer held that society was evolving toward increasing freedom for individuals and that as a result the intrusion of government should be kept to a minimum. In his second book, *The Principles of Psychology* (1855), he detailed certain psychological aspects of Mill's position to which he strongly objected.

His nine-volume work *A System of Synthetic Philosophy* provides a systematic account of his views in biology, sociology, ethics, and politics and a synthesis, organized through his evolutionary theory, of a broad range of findings in the natural and social sciences. Synthesis was always important to him. He thought not only that the goal of each science or area of inquiry was to arrive at the fundamental principles that accounted for its data but also that the data and theories of each science affect, and are affected by, the finding of the others.

Spencer held an "organic" view of society, believing that social life was an extension of the life of a natural body and that social "organisms" reflected the same evolutionary principles or laws as biological entities. These principles also provided a natural law basis for moral science and political science. This social evolution did not contradict his individualism, for he held that society was an aggregate of individuals and social change was dependent on prior changes of individual members. Individuals were always fundamental, and the formation of societies was instrumental or contractual, the result of the human motivation to join together to counter tendencies toward war and violence in general. The natural inclination of humans is to preserve their lives, and rational self-interest called for the formation of societies.

Recently, there has been a revitalized interest in Spencer's thought because of a growing interest both in evolutionary principles as operative in society and in his powerful arguments for natural rights and attacks on ulilitarianism.

—Sandra B. Rosenthal

See also Darwinism and Ethics; Evolutionary Psychology; Utilitarianism

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Spontaneous Order

A spontaneous order is a pattern or structure of items or elements whose very regularity is generated by the interaction of the elements themselves. Sometimes referred to as self-organizing systems, endogenous orders, or polycentric systems, such orders are not the result of explicit agreement, legislated design, or a direct outcome of biological instinct. Although spontaneous orders appear in both nature and society, this entry focuses only on the idea of spontaneous social orders. Diverse phenomena such as language, money, the division of labor, the common law, prices, rules and institutions, and society as a whole have been explained as spontaneously generated phenomena. The very possibility of such unintended and decentralized coordination challenges the commonplace assumption that any complex social pattern must be the result of a designing mind.

Order, Spontaneity, and the Invisible Hand

In an abstract sense, order is constituted by relations among parts or elements. So understood, order has less to do with power, authority, or control than with comprehensibility. Within an order, elements are so related, in regularities and patterns, that if one understands some subset of the elements and relations, then one may form predictions, or reliable expectations, about other parts of the whole. Within a society, the elements would include individuals and organizations, including business firms. Society manifests order insofar as relations or interactions among individuals and organizations allow individuals to form reliable expectations about the conduct of others.

There is always some sort of order within any society, but an order is spontaneous insofar as it is unintended. An outcome is intended precisely when that outcome is desired by the acting agent, and the agent performed the act to bring about that outcome because the agent believed that this outcome would be the effect of that action. A paradigm instance of an *intended* action would be when a lawgiver enacts a law and that law has precisely the effect desired by a lawgiver. On the other hand, for any *unintended* result, there is a lack of correspondence between intention and effect. Thus, in an unintended or spontaneous social order, regularities or structures arise as individuals, with particular aims and purposes, respond to their own situations and adjust their conduct in light of what other persons are doing. A series of mutual adjustments occurs among individuals so that common patterns of conduct emerge even though such regularities are not the intention of any particular individual but arise, as Adam Smith suggests, by an "invisible hand." Thus, one may explain such orders by employing, what have come to be called, "invisible hand explanations." Such value-neutral (or descriptive) explanations should characterize a set of initial conditions, describe how individuals interact in those conditions, and specify some principle that explains how the interaction of agents within these conditions brings about patterns that were not part of any one individual's intention. These patterns then allow these same individuals to form reliable expectations. Such orders, whose spontaneity may be a matter of degree, emerge either in a specified slice of time or over longer periods of time (as in the case of cultural evolution).

Significant Theorists

There have been numerous discussions of spontaneous order. Some 18th-century thinkers—including Bernard Mandeville, David Hume, Adam Ferguson, and Adam Smith—incorporated the idea of unintended social regularities into their social theories. Smith's idea of the "invisible hand" points to his understanding of how beneficial outcomes may be brought about by individuals who are motivated by a private, rather than a public, interest. Within the social sciences, the Austrian School of Economics has emphasized the importance of spontaneous orders. For example, Carl Menger, in his *Principles of Economics* of 1871, provides an account of the unintended emergence of a common currency. In *Problems of Economics and Sociology* of 1883, he describes how the essential task of the social sciences is to explain institutions that serve the general good but are not directed by a designing intelligence.

F. A. Hayek, a 20th-century Austrian economist, has delineated an ideal type of spontaneous order that emerges from a legal framework of universal and abstract (purpose-independent) laws. These laws would, in general, proscribe types of actions rather than prescribe specific acts, and they would demarcate and protect private property. Within such a framework, and in conjunction with other moral and social customs, individuals will interact and sometimes innovate and experiment. The underlying legal rules permit individuals to act on their own knowledge and in relation to their assessments and beliefs about what others are doing. Patterns and regularities, including those of the market, will emerge spontaneously. For example, freely moving prices will signal to disparate and anonymous individuals how they might mutually coordinate their expectations. Such a spontaneous order, Hayek contends, allows for greater complexity than could have been wrought by centralized organization or design. The complexity of a society is directly related, therefore, to the degree of spontaneity that is permitted by the underlying legal framework.

Spontaneous Order, Business, and Society

This is one of the implications of the idea of spontaneous order. Yet the conception of the market as a spontaneous order also reveals how the myriad interactions of commerce have no predetermined end or result. If the market lacks a purpose or *telos,* then the attempt to construe markets as goal directed improperly describe commercial societies. Similarly, the attempt to impose, via legislation, an overall goal on markets may disrupt self-coordinating tendencies inherent in society. An additional implication, notably argued by Hayek, is how the complexity of spontaneous order reveals the inherent limits of human reason and social planning. Such complex and beneficial societies, he explains, are achieved by instituting a classical liberal rule of law, as noted above. Nonetheless, it is not entirely clear how the descriptive thesis of a spontaneous order must imply a normative claim about the political order. One may argue, conditionally, that if the goods of a spontaneous order are desirable, then a certain political order ought to be instituted. However, such a hypothetical argument does not justify which kind of order (or kind of goods) is desirable for a society.

This last conclusion suggests a critical puzzle about the very identification of *order.* Some thinkers have suggested that market economies do not, in fact, reflect order but disorder. How could there be such disagreement over the order of the market? Perhaps what counts as an order (spontaneous or not) depends on one's interests or concerns. For any assertion that some phenomenon is orderly, there are other sets of relations that one could have discerned. Whether some specific relations are comprehended as orderly may depend, therefore, on whether those relations cohere with one's interests. For example, the patterns or relations of a society include the commercial but there may exist other relations of interest, such as religious or cultural patterns or structures. It has sometimes been suggested that some relations (such as the economic) may crowd out or diminish other relations (such as the traditional or the religious). Whether this might be the case is an interesting question that relates not only to the very identification of order but also to whether some kinds of patterns predominate over others.

Nonetheless, the notion of spontaneous order has relevance for business ethics. Hayek maintains that the market is a self-adjusting and coordinating force and that a spontaneous order will manifest greater complexity than a designed order. The very dynamism of commerce does not, therefore, preclude stable expectations about individuals, actions, products, and modes of production. This consideration suggests, therefore, that the self-organizing or coordinating forces at work in society ought not to be ignored, whether in descriptive analysis or in normative argument. A second, and corollary, point relates to organization and management. In a large firm or corporation, it may be possible to set in place structures that permit spontaneous orders to develop within the organization or to emerge in relations between the organization and parties external to it (e.g., stakeholders). For example, procedures of interaction within the firm (or within some division of the firm) may permit or encourage employees to cooperate with one another (or with suppliers or customers) in ways that allow for adjustments, changes, and adaptations that are not mandated or otherwise stipulated. The outcomes of such processes could serve the aim of the firm, perhaps encouraging innovation that could not otherwise have been foreseen by management, and may enhance trust and cooperative relations between the firm and other individuals or organizations.

A third point of relevance shifts the focus to more general normative questions. Even though prices serve to coordinate economic (and other) conduct, there will exist, within society, other patterns and structures, including those that manifest moral norms. These moral regularities, perhaps the result of spontaneous emergence, may cohere with the overall market order. An imposition of alternative moral standards from outside these processes might disrupt the coordination endogenous to the society. Whether and how such disruption occurs, or whether it is counterbalanced by the good that such disruption may bring, is a question political economists, political philosophers, and business ethicists must also consider.

—F. Eugene Heath

See also Austrian School of Economics; Competition; Entrepreneurship, Ethics of; Ferguson, Adam; Freedom and Liberty; Free Market; Game Theory; Hayek, Friedrich A.; Invisible Hand; Mandeville, Bernard; Methodological Individualism; Smith, Adam; Stakeholder Engagement

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Stakeholder Economy

A *stakeholder economy* is a social system of production and exchange that is intended to protect the interests of all persons and organizations affected by the activities of buyers and sellers. A stakeholder economy is organized for the participation of stakeholders in its institutional mechanisms to allocate capital resources, to produce goods and services, and to distribute them in response to demand. Thus, a stakeholder economy is intentionally governed for the interests of broad and diverse segments of society rather than for the more narrow interests of the owners of capital and the holders of wealth.

In North America, the term *stakeholder* comes from the colonial era when it was the practice for land owners to mark their property by putting stakes in the ground. Those who did so were said to have a *stake* in the community. In addition to the owners of capital and the holders of wealth, today's stakeholders are composed of distinct and diverse groups in a society. For example, buyers and sellers clearly have a stake in the ethical functioning of a society's economic system. Other affected groups with an interest in the fairness and integrity of economic activities include employees, nongovernmental advocacy organizations, and the populations of local communities. Some also argue that posterity, the future generations yet unborn, are stakeholders whose interests are affected by the sustainability of current economic activities and today's decisions that are likely to affect future financial health, availability of natural resources, and the level of environmental pollution.

Clearly, there are many distinct groups of diverse stakeholders. They have in common, however, their perception that something they value is at risk because of society's actions, or inactions, to produce and exchange goods and services. Commutative justice depends on public-policy-making mechanisms that allow all these distinct and diverse stakeholders, including the stewards of posterity, to participate in economic governance and exchange. Such mechanisms include broad representation of social groups on advisory, legislative, and regulatory committees. Commutative justice in a stakeholder economy also gives voice to the diverse groups in capital allocation decisions for production and distribution.

In a context of scarce or finite resources, decision makers are not likely to be able to simultaneously satisfy the preferences of each and every stakeholder. In this situation, broad inclusion compels each group to use the tools of public persuasion and to exercise its political power to realize its preferences in the governance of the economy. The effectiveness of the stakeholder economy is likely to depend on cooperation, consensus, and coalition building to balance the power of any large group with much at stake. A stakeholder economy requires integrity in the public process for interest groups to influence the activities of businesses and organizations. Principles of procedural justice are important to ensure fairness in the process of making decisions that trade off and balance responsiveness to individual stakeholders.

The World Bank, because of its important role in stimulating the development of economies, has relied on a rigourous approach to stakeholder analysis that focuses on the integrity of government operations and public policy decision making. Central to the Bank's approach is the assumption that the stakeholder groups with the most resources and the most at stake are most likely to realize their preferences in public policy processes governing the economy. Importantly, the World Bank also has found that the positive social effects of a developing economy are significantly diminished in societies where public-policy-making institutions are captured by one stakeholder group to the exclusion of others.

The overall lesson from the experience of the World Bank is that both economic development and respect for human rights depends on working closely with powerful stakeholders while simultaneously giving all stakeholders fair opportunity and access to government institutions that govern the economy. The operational effectiveness of a stakeholder economy, therefore, depends on powerful stakeholders avoiding conflicts of interest as they assert their self-interest and liberty while at the same time responding to the rights of less powerful stakeholders in the community.

Current obstacles to the ability of stakeholders to participate effectively in the functioning of an economy include business consolidation, corruption, and the lobbying activities of interest groups. Businesses grow larger and broaden their scope as they consolidate in mergers and acquisitions. As they grow, their resources increase but the salience, or importance, of many other stakeholder groups to it may diminish in significance. Stakeholder analysis suggests that this situation allows the consolidated business to be most likely to realize its preferences in the economy. This issue is particularly urgent for stakeholders in a global economy in which managers may operate a business system of global proportions while other stakeholders are organized in smaller groups separated by country, culture, and language. Thus, the outcome of consolidation and globalism may be a fragmented and ineffective stakeholder economy.

The justice of outcomes expected from an effective stakeholder economy depends on the honesty and integrity of social institutions. Many have commented, for example, that the pervasive role of lobbyists in the U.S. public-policy-making apparatus is an obstacle to an effective stakeholder economy. Lobbyists are advocates paid to influence government on behalf of a group with a special interest. In the United States, lobbyists are regulated in their activities to protect against the hazards of corruption. Nevertheless, one common criticism of lobbyists is that their effectiveness depends on access to substantial financial resources, but those with such resources may contribute to procedural corruption, and stakeholders without such resources are locked out of the public-policy-making process required for the smooth functioning of an effective stakeholder economy. This criticism is consistent with the stakeholder analysis approach to government operations discussed earlier in this entry.

In sum, the stakeholder economy views business as a production mechanism to improve the welfare of all social groups that have an interest in the allocation of resources in society. The goal of the stakeholder economy is to to apply the principles of commutative justice broadly across all social groups to ensure the fair access of each to participate and to benefit from the functioning of the economy. Key to the smooth functioning of the stakeholder economy is the integrity of the public policy process in which stakeholder groups influence the regulation of the economy.

—Greg Young

See also Accountability; Advisory Panels and Committees; Benevolence and Beneficence; Commutative Theory of Justice; Conflict of Interest; Corporate Accountability; Corporate Social Responsibility (CSR) and Corporate Social Performance (CSP); Economics and Ethics; Motives and Self-Interest; Nongovernmental Organizations (NGOs); Political Economy; Pollution; Procedural Justice: Social Science Perspectives; Public Interest; Regulation and Regulatory Agencies; Stakeholder Theory; Stewardship; Welfare Economics; World Bank

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Stakeholder Engagement

Stakeholder *engagement* is an emerging approach for thinking about and acting on the complex interplay of relationships and responsibilities of business *in* society. It focuses on engaging all stakeholders caught up in a shared problem domain in an interactive dialogic learning process so that the messy, interdependent problem can be understood jointly and addressed cooperatively. It is an extension or, some would argue, a transformation of the theory and practice of stakeholder *management* and the stakeholder theory of the firm. Both stakeholder management and stakeholder engagement arise from R. Edward Freeman's 1984 classic definition of stakeholders as any individual or group who can affect or are affected by the achievement of the organization's purposes or by their unintended consequences. The stakeholder concept dramatically expands the scope of executive responsibilities beyond just the fiduciary duty of a managerial agent to serve the economic interests of the firm's shareholders. Managers are expected to consider the interests of all who have a direct stake in the firm (such as customers, suppliers, and employees) or an indirect stake in the firm (such as interest groups, government, or nongovernmental organizations) because of the firm's operational impacts on the external community or natural environment.

The concept and practice of stakeholder management is *firm centered* and calls on managers to review and exercise unilateral control over a series of bilateral stakeholder relationships. These take on a "hub-and-spoke" configuration, as managers of the corporate hub work to minimize potential threats to the firm's primary objective function of enhancing financial performance for shareholder principals. This management activity involves the negotiation of trade-offs between financial and social performance expectations. This typically will reduce short-term financial returns but may, arguably, preserve the long-term financial viability of the firm by improving its reputation or perceived legitimacy in the eyes of potentially threatening stakeholder groups, such as irate employees, customers, or environmentalists. Such accommodations are justified as being necessary to avoid or minimize the threat of negative stakeholder responses, such as consumer boycotts, pressures for regulatory intervention, or other adverse actions. In contrast, stakeholder engagement is a *network-centered*, learning-based process of manager/stakeholder interactions, which locates the firm within a web of multilateral relationships and explores ways to achieve system sustainability by enabling the firm's managers to work with their stakeholders while addressing complex, interdependent, emergent, and messy problems.

Initiating a process of engagement within a stakeholder network requires a dramatic extension of the responsibilities and capabilities of business managers, as well as the enabling of a variety of stakeholder voices, often represented by nongovernmental organizations (NGOs), such as Greenpeace or Amnesty International. Ann Svendsen and Myriam Laberge, two leading Canadian consultants on "whole system change," have characterized this process as "cocreative engagement," highlighting the emergent role of business managers as conveners and facilitators of multi-stakeholder-learning dialogues that bring the "authentic voices" of stakeholders to the table. They define a stakeholder network as a web of groups, organizations, and/or individuals who come together to address a complex, cross-boundary problem, issue, or opportunity. The manager's role must necessarily be one of facilitation and support rather than control because the firm is just one participant within a problem domain that encompasses multiple perspectives on the nature and extent of the problem, as well as perceptions of how each network member is affected by that problem and by potential solutions. The starting point for the convening of a stakeholder network is the recognition by those who share the messy, interdependent problem that no single party can resolve it successfully without engaging with others in the problem domain.

Svendsen and Laberge characterize the stages of cocreative engagement as proceeding from *outreach* to *collective learning* and finally to *joint action/ innovation.* The driver for the initial stage of outreach, where membership in the stakeholder network is extended, often is a reputation crisis experienced by a major corporation. One such is Nike. This reputation crisis, typically, is triggered by the outraged reactions of activist stakeholders to managerial assumptions, methods, and oversights in addressing a sensitive issue, such as creating environmental damage or threats to human rights through their business operations in developing countries. Thus, Nike managers initially responded angrily and defensively to NGO criticism of working conditions in the shoe and apparel plants of their Asian subcontractors. They felt that such criticisms were overblown and taken out of context, arguing that wages and working conditions in these plants were comparable with or preferable to locally available alternatives. Moreover, they insisted that any abuses of employee rights were the responsibility of the local contractors and government regulators. They represented Nike as being primarily concerned with delivering a solid return to its shareholders, as well as a superior product at a reasonable price to its customers. However, escalating stakeholder/NGO complaints and a spreading consumer boycott, especially on college campuses, forced Nike managers to reconsider their "Go it alone" stance. Thus, stakeholder engagement can, to some extent, be forced on a company. Nike's management team, headed by CEO Phil Knight, grudgingly shifted from an adversarial to a more accommodative stance and joined in a multi-stakeholder dialogue with other apparel companies, labor and human rights NGOs, and some governments, including the Clinton administration. Out of this process of engagement within a stakeholder network emerged a voluntary "No Sweat" apparel industry code of conduct that defined socially responsible business "citizenship" performance. Thus, stakeholder engagement is associated with a trend toward heightened *accountability* in corporate social and environmental, as well as financial, performance (i.e., the "triple bottom line"). This requires increased *transparency* in business operations so that these broadened performance expectations can be monitored and compared. Notably, stakeholder NGOs have become actively engaged not only in helping formulate voluntary industry or business performance standards but also in monitoring and certifying compliance to these standards. Business, government, and NGO representatives have taken on these new roles and responsibilities after they recognized that they could not accomplish their goals acting alone. Other stakeholder engagement success stories are offered by Steve Waddell, in his 2005 study of an emerging interactive, collaborative process of societal learning and change.

Critics of this new approach to stakeholder engagement, and particularly of the call for a new management responsibility to foster stakeholder dialogue, point to the risk of strategic or operational delays from stirring up a senseless cacophony of contending stakeholder voices. This criticism can be met by pointing out that stakeholder engagement and dialogue processes are largely unnecessary when "business as usual" rules and conditions apply. Thus, examples (especially successful examples) of stakeholder engagement remain the exception rather than the rule for management practitioners. Even so, Jorg Andriof and Sandra Waddock, leading scholars of the emerging theory and practice of corporate citizenship, argue that stakeholder engagement processes are an appropriate response to unfolding institutional and competitive developments in the global environment of business. Accelerating environmental turbulence (rapid, unpredictable changes) associated with hypercompetitive pressures in the global marketplace is forcing business organizations to forge new network connections. They do so to enhance their organizational learning capabilities needed to guide rapid adaptive responses and to help manage rising social risks posed by activist stakeholders who feel they should have a "say" in mitigating the impact of corporate actions on internal and external constituents. As the boundary separating the business organization from its external environment becomes more permeable, management assumptions about exercising control within a closed organizational system are giving way to a search for new ways to engage stakeholders within an open-system environment. In effect, managers have to learn how to negotiate this complex, unfolding environment by developing a capacity for cocreative engagement via dialogic interaction within the stakeholder network.

Making sense of network relationships requires a more system-based or holistic approach to learning and doing. Stakeholders and business organizations grappling with a messy, open-ended problem first have to realize that they cannot handle it alone. Before they can learn how to work together, each network member must come to realize that furthering a particular identity and purpose is intertwined with the successful functioning of the whole. A critical aspect of this interactive dialogic learning process is the search for common ground, which provides the shared cognitive (thinking) and affective (feeling) foundation from which cooperation and creative adaptation can arise. Dialogue is an open-ended, interactive mode of inquiry that invites participants to speak with an authentic voice (without guile and reflecting the true self), to listen respectfully, and to question not only others' but also their own initial "mental maps" about the nature of the shared problem and different ways network members relate to it. Dialogue encourages reflective inquiry within a process of collective learning, which can move participants toward a cocreative construction of shared meanings, and codevelopment of ethical norms of behavior to guide trust-based network interactions. Reflective dialogue deepens inquiry into underlying causes, rules, and assumptions to enable the reframing of old problems in new ways, thus opening a path to innovation and system change.

Ultimately, stakeholder engagement is about building and sustaining relationships within a shared problem domain. Whereas conventional management theory characterizes the management of these relationships in terms of exploiting resource dependence or minimizing transaction costs, an emerging theory and practice of open systems or network management calls attention to the need to build trust and invest in "social capital"—the connective glue and lubricant for cooperation and information exchange within networks. While proactive stakeholder engagement may not be needed to guide day-to-day operations, many business managers are coming to recognize that a growing number of complex, messy, and interdependent problems, ranging from failing public schools to urban blight, and even global warming and rising energy costs, are threatening the overlapping economic, political, social, and ecological systems within which business firms operate. The insight that growing systemic problems are impinging on business success may well provide a compelling rationale for a new, more proactive approach to corporate social responsibility. Moving beyond philanthropic and public relations gestures, a growing number of leading corporate citizens are beginning to engage with stakeholder activist groups and other strategic partners to find new ways of relating, learning, and working together to resolve some of the messes that our old ways of thinking and doing have created or failed to address successfully.

—Jerry M. Calton and Stephen L. Payne

See also Agency, Theory of; Corporate Accountability; Corporate Citizenship; Corporate Social Responsibility (CSR) and Corporate Social Performance (CSP); Ethics of Dialogue; Fiduciary Duty; Nike, Inc.; Nongovernmental Organizations (NGOs); Social Capital; Stakeholder Theory; Sustainability; Sweatshops; Triple Bottom Line; Trust

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Stakeholder Responsibility

The primary focus of stakeholder theory has been the proposition that firms have a moral responsibility to take into account the interests of stakeholders other than just stockholders. Given the focus on the corporation within organization studies, this emphasis in theorizing is understandable. The emphasis on corporate responsibility to stakeholders has not to date been balanced by a complementary focus on the responsibilities of stakeholders. Though some models within the stakeholder literature portray a two-way relationship between the firm and the stakeholder, writers predominantly argue that firms are responsible for taking into account stakeholder interests, without noting the reciprocal moral responsibility of stakeholders to consider the interests of the firm in their actions and policies. A focus on stakeholder responsibility compels theorists, corporations, and stakeholders to direct greater attention to the importance of the responsibilities stakeholders have to firms and to other stakeholders who are part of the collective enterprise.

Corporate Responsibility and Stakeholder Theory

With the emergence of stakeholder theory in the mid-1980s and its rapid growth up to the present time, numerous writers questioned the primacy of corporate responsibility to shareholders. Writers building the foundation of stakeholder theory argued for expanding the domain of corporate responsibility beyond shareholders to include a number of critical stakeholder groups.

Over time, the legitimacy of the stakeholder perspective has grown and has influenced the direction of work in business ethics, organization theory, and the strategic management literature. Stakeholder theorists have argued for managers to acknowledge the moral "stake" of stakeholders by paying attention to stakeholders and their interests for both prudential reasons (i.e., it is good for the firm and its profitability to listen to stakeholders) and normative reasons (i.e., they argue that there are compelling moral arguments for considering stakeholder interests).

Corporate and Stakeholder Responsibility

As noted above, there has been a lack of attention to the fundamental question of whether stakeholders have moral responsibilities to firms. This is not to say that the topic of stakeholder responsibility has been completely ignored by business ethics writers. A series of articles and books were published in 2002 to 2003 that attempted to establish a conceptual foundation for stakeholder responsibility. This work emphasized the importance of stakeholders assuming responsibility for negative outcomes associated with actions directed to firms and other stakeholders and reinforced contemporary notions of responsibility in terms of accountability and responsiveness.

There are other ways of understanding responsibility in relation to stakeholders. Tracing the term back to its Latin roots (*respondere*), responsibility literally means to *pledge back*. In contrast to notions of responsibility that focus on an externally imposed obligation, this form emphasizes the idea of people and organizations choosing to pledge things to each other to foster cooperation and a better life for all. This definition of responsibility extends what it means to be a stakeholder beyond the traditional definition of stakeholders as individuals, groups, or organizations potentially affected by the actions and policies of an organization. Stakeholders are not only the recipients of organizational actions but actors as well with reciprocal responsibility for the implications of their actions in relation to firms and other stakeholders.

The idea of stakeholder responsibility draws its legitimacy from fundamental philosophical arguments. There are consequentialist arguments for both corporate and stakeholder responsibility that focus on whether a person, firm, or stakeholder can produce benefits or harms that are of importance to others. Writers have devoted primary attention to corporate responsibility particularly in light of their size and power and the potential significance of harms and benefits associated with corporate actions. From a stakeholder responsibility perspective, attention shifts to stakeholders, who are responsible for reciprocating benefits from firms and other stakeholders and addressing intended and unintended harms, particularly deriving from the role responsibilities of stakeholders and their ability to inflict harm on (or create benefit for) the firm and other key stakeholders. In the same way that responsible corporations must consider how specific actions and policies might harm stakeholders, especially those who are in highly dependent and potentially vulnerable positions, stakeholders bear reciprocal responsibilities as well for taking into account potential harms to firms and other stakeholders.

Beyond an emphasis on consequences, specifically responsibility for negative consequences, there are arguments for stakeholder responsibilities that rely on a deontological or rule-based approach to ethics, particularly those connected to justice and the ethics of interdependence. Notions of reciprocity and responsibility—for benefits and harms—are central to the literature on justice and fairness. The notion of reciprocity is a fundamental element of justice and fairness, and contemporary business ethics scholars have developed a "principle of fairness" to determine whether firms have responsibilities to stakeholders (Does the firm receive benefits from the stakeholder?) and to which stakeholders firms should give primary attention (How significant are the benefits received from a particular stakeholder?).

This literature provides a rich foundation for thinking about firm responsibility to stakeholders and can be extended to consider how firms benefit from their interactions with stakeholders. Employees, customers, suppliers, investors, and other stakeholders benefit in a variety of ways from their relationships with firms and each other. Employees gain in tangible (e.g., wages) and intangible ways (commitments) from their relationships with firms. Customers may come to appreciate the high-quality products a firm offers and value as well the service employees provide in purchasing these products. The receipt of these benefits from firms may generate responsibilities on the part of employees and customers to these firms (and other stakeholders). In drawing attention to the benefits stakeholders gain from specific relationships with firms and other stakeholders, considerations of fairness and reciprocity encourage stakeholders to recognize reciprocal responsibilities for helping others achieve these goals and interests.

In like manner, as agents of the firm, stakeholders have a responsibility to create benefits for the firm that further the firm's and stakeholders' mutual interests. There are strong signs that many firms understand and depend on such responsibility in their operations. For example, firms presuppose and depend on employees taking ownership of customer service and acting responsibly toward them. Many firms take steps to put into place supplier codes of conduct that establish responsibilities critical for suppliers to fulfill for these firms to achieve important goals and commitments to other stakeholders.

As more attention is directed to stakeholder responsibility, there will be opportunities to enrich the business ethics literature and create an understanding of business ethics that emphasizes both corporate and stakeholder responsibility.

—Jerry Goodstein and Andrew C. Wicks

See also Business Ethics Scholarship; Consequentialist Ethical Systems; Corporate Citizenship; Corporate Social Responsibility (CSR) and Corporate Social Performance (CSP); Deontological Ethical Systems; Justice, Theories of; Stakeholder Theory

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Stakeholder Theory

Every company exists in a network of relationships with social actors that affect and are affected by the company's efforts to achieve its objectives. Taken together, these actors are the company's *stakeholders*, implying that they hold a stake in its conduct. Typically, stakeholders of a for-profit company include its customers, employees, stockholders, suppliers, the local community, and many others groups.

Stakeholder theory is the term used to describe broadly the systematic study of these relationships, their origins, and their implications for how companies behave. As used in this context, the word *theory* raises serious problems. Social scientists who study stakeholder relations are interested in many empirical questions, such as why companies and stakeholders behave as they do and why companies succeed or fail. They use the word *theory* to refer to a specific set of cause-and-effect relationships used to answer such questions. The controversy (as explained below) is whether stakeholder theory, as a social science theory, points toward a unique set of causal statements about why organizations behave as they do that no other theory identifies. On the other hand, ethicists use the term *stakeholder theory* to describe a coherent and original answer to the central philosophical question in organizational ethics, How should organizations behave? There is less controversy about whether stakeholder theory is a form of ethical theory, though this does not mean that the theory's content is uncontroversial among ethicists. This entry discusses the development of stakeholder theory in both these contexts (social science and philosophy) and details its answers to both empirical and ethical questions.

Historical Background

The term *stakeholder* is not a new one. It dates back at least as far as the early 18th century, where it sometimes appeared in British legal cases to describe a party holding a stake in a financial transaction. In the narrowest sense, a stakeholder was a neutral party to a transaction or wager who held the money in trust—literally holding the stakes. However, by the early 19th century—as detailed in the *Oxford English Dictionary*—the term had acquired a more expansive definition in two ways. First, its meaning expanded to include all parties to a financial interest, and second, it broadened to describe those parties holding an interest in the broader political system or commonwealth. In some sense, this more expansive use of the term would set the stage for its emergence as a term in the study of business and society.

While the term did not appear explicitly in writing about management for much of the 20th century, the notion that executives must pay attention to the demands of an organization's multiple constituencies has a long history in the early-20th-century precursors to the modern field of organization theory. Mary Parker Follett, an early American management thinker, portrayed the organization as nested in an environment of other actors, each mutually influencing and defining each other. To Follett, the manager's job was to integrate the conflicting interests held by these constituencies, and the success of the company depended, in no small part, on managers recognizing the need to (a) manage all relationships with as much attention as they traditionally paid to personal matters and (b) achieve some degree of creativity in how they dealt with conflicting demands.

Likewise, in his classic book *The Functions of the Executive*, Chester Barnard foreshadowed the eventual emergence of stakeholder thinking. For Barnard, an organization is a cooperative scheme, the result of a conscious effort by many people to work together. As such, an organization's survival depends on its relationship to its environment and its ability to satisfy those individuals interacting with it. The central role, in Barnard's thinking, of executive responsibility—the suppression of personal interest in service of the cooperative scheme—also heralds the eventual exploration of the moral side of stakeholder theory. Barnard introduces notions of balance and touches on questions of whether subordinates should be treated as having intrinsic value (valued for their own sake) or should be treated instrumentally (valued only for what they can do for the executive or the company). These are questions that, today, arise frequently in writing about companies and their stakeholders.

The early works of Follett and Barnard, though often neglected today, played some role in the emergence of the open systems view of organizations in postwar organization theory and, in turn, these authors laid much of the intellectual groundwork for theorizing about stakeholders. Efforts by Peter Blau, W. Richard Scott, William R. Dill, and James Thompson all centered on the nature of the external environment in which organizations existed, paying particular attention to the nature of the *organization set*—the immediate relationships surrounding an organization. In the ensuing decades, the attention of most organization theorists would shift from the study of organization sets to organization fields, a higher level of analysis at which all organizations and their constituents interact to create institutional norms and rules. Yet the initial insight that a company plays multiple roles within a bounded set of actors would lay the groundwork for the advancement of stakeholder theory as a continuing effort to explore the nature of organization set interactions.

The term *stakeholder* emerged in the study of organizations and management in the early 1960s through the work of the Stanford Research Institute, in the work of Albert Humphreys and others. There, efforts to map program management processes and improve long-range planning techniques led to greater attention on the parties to a management process—that is, its stakeholders—and their role in determining the success of a change program. Both Kenneth Andrews and Igor Ansoff, early advocates of the study of corporate strategy, used the term explicitly and suggested that stakeholders might have something to do with the overall strategy formulation process in a company. However, the term did not attract much attention until the early 1980s with the publication of two books, Ian Mitroff's *Stakeholders of the Organizational Mind* of 1983 and R. Edward Freeman's *Strategic Management: A Stakeholder Approach* of 1984. Of the two, Freeman's has made the more lasting contribution to stakeholder theory.

Freeman's Seminal Contribution

R. Edward Freeman's book *Strategic Management: A Stakeholder Approach* (1984) is widely recognized as the first major work in stakeholder theory, though misunderstandings about its contents abound. It is, therefore, worth devoting some attention to the nature of Freeman's argument and its implications for the subsequent development of stakeholder theory.

The starting point for Freeman's book is to trace those previous schools of thought that lay a groundwork for thinking about a company's strategy in stakeholder terms. There are four primary schools—the corporate planning literature, open systems theory, the study of corporate social responsibility, and organization theory. For each, Freeman discusses the contributions made to the stakeholder concept. Chief among these contributors are the organization set theorists cited above, systems theorists such as Russell Ackoff, corporate strategists such as Ansoff, and business and society scholars such as Lee Preston and James Post. This section can, in some ways, be read both as a history of the stakeholder concept and as an intellectual genealogy indicative of the various circles in which Freeman was moving at the time that he was conceiving of and developing his approach to stakeholder management.

Freeman's definition of the term *stakeholder* remains the most commonly used (and is the basis for the definition provided above), despite frequent criticisms of its breadth. He writes, "A stakeholder in an organization is (by definition) any group or individual who can affect or is affected by the achievement of an organization's objectives" (p. 46). This definition also lays the groundwork for the visual figure, a hub-and-spoke diagram with the company at the center and stakeholders ranged around in a circle, most commonly associated with stakeholder thinking. Most subsequent writers, however, ignore Freeman's warning that if stakeholder thinking remains at such a generic level—ignoring the specific groups and complex interrelations that characterize actual company-stakeholder interactions—it would have little practical value.

The most obvious and lasting contribution of Freeman's book is the emergence of what has come, more recently, to be called instrumental stakeholder theory—the idea that companies that manage their stakeholder relationships effectively will survive longer and perform better than those companies that do not manage stakeholders well. (This entry will discuss more recent contributions to this stream of research.) In developing this argument, Freeman also offers what remains the most in-depth description of the actual practices and processes by which a company might be said to manage these relationships well. He suggests that stakeholder management "competence" includes a commitment to monitoring stakeholder interests, an ability to formulate strategies for dealing with stakeholders, sophistication in segmenting stakeholder needs, and the alignment of specific business functions (e.g., public affairs, marketing) to dealing with stakeholder needs. In essence, Freeman's book remains one of the most thorough "recipe books" for managers interested in stakeholder management, and far more than its contribution to theory, this remains its greatest strength.

As for Freeman's role in the emergence of an ethical literature on company-stakeholder relations, the genealogy is slightly more complicated. After all, Freeman's book contains little reference to the question of how companies should treat stakeholders, at least insofar as the question goes beyond merely prudential matters of survival or profit. The book contains only one passing reference to ethical and political theory (a stray citation of the writing of the philosopher John Rawls), and it would be a few years before Freeman would acknowledge that, only in later conversations, did he begin to explore seriously the question of stakeholders as moral agents. Yet Freeman's own training as a philosopher and his relationship to the burgeoning scholarly community of business ethicists probably created the conditions by which the 1984 book serves as a foundational work in ethics-based stakeholder theory, despite the fact that it contains little explicitly intended to kindle such discussion.

Stakeholder Theory in Organizational Ethics

As stated above, stakeholder theory can be looked at as a marriage of two somewhat different theoretical enterprises—ethical and empirical. The first is the search for an ethics-based stakeholder theory. From its onset, in the early 1990s, this project started with several attempts by Freeman and other like-minded philosophers to formulate a so-called normative core from which to deduce the moral obligations of the company in dealing with its stakeholders. Many scholars thus sought to establish a clear philosophical foundation on which to ground statements about how companies *should* treat their stakeholders. Almost every major ethical theory—utilitarianism, property rights, feminist ethics, and Kantian deontology—offered some basis for relevant arguments.

At its heart, the quest for a normative core for stakeholder theory has clear roots in the more long-standing debate over the purpose of the corporation in a capitalist society. Ethicists tend to draw a sharp distinction between stockholder and stakeholder models of capitalism—the central question being "For whose benefit should the corporation be run?" The stockholder model, which received its most ardent defense from Nobel laureate Milton Friedman, holds that the corporation must strive to maximize returns for its shareholders. The property rights of its shareholders, the nature of fiduciary duties, the legal mandates surrounding corporate governance, and public policy considerations all offer some support for the stockholder model.

Set in opposition to this model, however, the stakeholder model holds that a corporation owes obligations to more than just the stockholders. For example, Thomas Donaldson and Lee Preston (in a widely cited article) argue that a more expansive notion of property rights allowed stakeholder groups to make legitimate claims on the value produced by the corporation. Each of the attempts to derive a normative core from some established school of ethical theory arrived at similar conclusions, though often from very different starting points. The object of the corporation, they argue, is to maximize stakeholder wealth—which includes but is not limited to stockholders.

With time, the pursuit of a normative, or ethics-based, stakeholder theory has gone beyond the simple pursuit of a normative core. Today, three major problems occupy ethicists interested in how companies should treat their stakeholders—identification, distribution, and procedure. Each has received attention in existing research but each demands further elaboration.

Identification

The problem of identification seems simple enough: Who should managers of a particular company identify as its stakeholders? Given the potentially vast number of actors claiming a stake in the company's operations, identification involves determining which actors truly have enough moral standing to be considered stakeholders. This is a moral problem rather than merely a question of description. A local business may well pay protection money to a local crime boss, and this person may affect and be affected by a company's actions. However, few ethicists would argue that crime bosses have moral standing vis-à-vis a company. Indeed, companies may well treat any number of social actors as salient (i.e., requiring attention) without considering them to have the moral standing afforded by ethics-based stakeholder theory.

From the earliest days of stakeholder theory, the identification problem has produced a great number of distinctions. Early stakeholder theorists spoke of stakeholders as either primary or secondary, indicating that some groups may have greater or lesser claims to stakeholder status. In a frequently cited article, Mitchell, Agle, and Wood suggest that the characteristics of power, legitimacy, and urgency not only determine who the company is likely to consider salient (an empirical question) but which groups merit this attention (a normative one).

It is, however, Robert Phillips's book *Stakeholder Theory and Organizational Ethics* that offers the most coherent and complete answer to the identification problem. Drawing on a principle of justice as fairness first articulated by John Rawls, Phillips contends that a company should consider as stakeholders all those parties that participate in the cooperative scheme surrounding it. In other words, a company has an obligation to attend to the claims of parties insofar as it willingly receives benefits from them. Based on this notion of fairness, Phillips distinguishes between legitimate stakeholders (i.e., those that possess moral standing based on claims of fairness or reciprocity) and derivative stakeholders (i.e., those parties whose claims on a company are indirect, deriving from their relationship to a legitimate stakeholder). Thus, a company must recognize employees as a legitimate stakeholder because the company willingly accepts benefits from the employees' efforts; however, the company need not consider the labor union acting on behalf of employees a legitimate stakeholder, except insofar as their claims derive from their relationship to employees. In sum, Phillips grounds the debate over identification more firmly in the realm of ethical theory and offers one possible solution.

Distribution

The second and arguably greater ethical question in stakeholder theory is the problem of distribution, "How should a company distribute the value that it creates?" Of course, this is a highly simplified way to express the problem, as businesses tend to generate very different types of value (many of which are incommensurate with each other), operate over long time frames in which seeming trade-offs can worsen or resolve themselves, and generate enormous costs that may well be treated as morally different from the value the company creates. If a company damages the natural environment, for example, it deprives community members of certain intangible goods (peace of mind, quality of life) for which monetary value does not fully compensate. Many of the costs involved manifest over long periods of time, during which the immediate benefits to the company of polluting may place the company in better (or worse) position to remedy the environmental problems that arise. Finally, if the damage leads to deaths in the community, these costs are unlikely to fit naturally into a cost-benefit calculation along with returns to stockholders and employee salaries enjoyed by other stakeholders.

Despite the complexities, stakeholder theorists have continued to wrestle with the distribution problem. To a great degree, solutions to the distribution problem are set in contradistinction to the notion that companies (particularly corporations owned by stockholders) owe all their residual value to their owners. Alexei Marcoux, in an important article in the *Business Ethics Quarterly*, mounts a vigorous defense of this principle. He contends that the notion that a company owes a fiduciary duty to shareholders—a duty to act first and foremost in the interests of shareholders—is the natural moral analog to other situations where fiduciary duties apply. Information asymmetries, the degree of possible harm, and the need for trust all create conditions where the company should acknowledge a fiduciary duty to it stockholders similar to that of doctor to patient or lawyer to client. Of course, this idea—equally present in Friedman's justification based on the property rights of owners—actually offers only an incomplete response to the distribution problem. After all, we may agree that shareholders, as owners of the company, deserve special consideration and still have few answers about the right way to distribute value and costs. Many of the decisions companies make and the trade-offs they address have only incidental impact on stockholder value.

In most such cases, the causal relationships are so tenuous as to make considerations of fiduciary duty and residual wealth not useful, if not altogether irrelevant, for solving the practical moral problems involved. Consider a simple example of an airline deciding how much airline baggage to allow on the airplane. Insofar as a company (rather than regulators) still gets to make this choice, managers must decide between passenger convenience and the well-being of employees—flight attendants are often injured trying to help passengers with oversized carry-on baggage. To say "the company should do whatever is best for the shareholder" is to say very little indeed. There is no evidence that baggage policies are a major determinant of customer preference and little more evidence that employee morale translates directly into financial returns in this industry. Indeed, fuel costs (a very important driver of profit in the industry) are not affected either way, as the baggage will end up somewhere on the airplane regardless of whether it is checked or carried aboard. The company is still left to decide how to distribute the good among two conflicting stakeholder claims. Though this is a trivial example, it may be more representative of the problems faced by management on a daily basis.

The general principle often attributed to stakeholder theory is that companies should distribute value broadly, that the company should be managed so as to create value for all its stakeholders. In specific terms, Phillips offers the clearest interpretation of this general principle. He argues that a company owes obligations proportional to the relative contribution that the stakeholder makes to the success of the cooperative scheme. Of course, by marking out such a specific position, Phillips exposes himself to critiques that the resulting allocations are still too narrow to be morally justifiable. After all, some groups (e.g., local communities) may offer few tangible benefits to a company, contributing little to the cooperative scheme, but still deserve some consideration if, for example, the company decides to erect a particularly ugly building that will destroy property values for miles around. Still, the distribution question awaits a more persuasive argument.

Procedure

The problem of procedure concerns the proper role of stakeholders in the formulation of strategies and policies that affect them: Does a company have an obligation to engage with stakeholders and invite their input into policy decisions? Regardless of the moral issues involved, many companies do offer ways for particular stakeholder groups to express their viewpoints. However, given that companies, especially very large corporations, can exercise a great deal of power (often on a par with governmental power) over customers, employees, and local communities, the question of whether managers owe an obligation to provide due process (e.g., via grievance processes, consultations, etc.) remains an important moral question.

Arguments in this vein tend to find their roots in one of two traditions. On the one hand, ethicists may choose to draw on the work of German philosopher Jürgen Habermas. Habermasian, or discourse, ethics hold that morally right decisions in a political context are only possible insofar as they are created through open public discussion and deliberation. The only way to honor man's nature as a reasoning being is to respect reason's role in the act of communication and deliberation. Applying this principle of communicative reason, Jeffrey Smith has argued that a company has an obligation to consult with its stakeholders so that the resulting decisions will not only be better but more ethically legitimate than those created in a vacuum.

A second perspective on the moral problem of procedure is the emerging discussion of multistakeholder dialogue. Though not necessarily rooted in any particular ethical theory, authors such as Jerry Calton and Stephen Payne, drawing on insights from William Isaacs and David Bohm, argue that dialogue is a natural and important facet of all human relationships and that suppressing dialogue in stakeholder relationships is both imprudent and unnatural. It is not clear, of course, what the extent of this dialogue must be—who should be involved, how long it should last—but Calton and Payne seem to suggest that these considerations should flow organically from the dialogue itself rather than according to any external constraints.

Stakeholder Theory as Social Science

If stakeholder theory is (as suggested above) a marriage between two somewhat different theoretical enterprises—the ethical and social science traditions—the latter has been the more fickle partner. Many social scientists researching these interactions have done so while, more or less, accepting the notion that the normative project remains an essential part of stakeholder research. For these theorists, accepting that stakeholders have intrinsic value is a shared premise for stakeholder theorizing. In other words, the social scientist must accept a fundamental ethical principle and then embark on research that advances understanding either the empirical or the ethical implications of this premise. The ideal outcome, then, is some *convergent stakeholder theory*, a phrase coined by Thomas Jones and Andrew Wicks, in which both efforts combine in a hybrid that includes both a sophisticated morally grounded concept of how companies should treat stakeholders and an empirically robust causal chain linking such moral behavior to desirable outcomes.

A minority of social scientists doing research on stakeholders tend to reject this desire for convergence and see it as a threat to traditional assumptions about how to do proper social science. From this perspective, stakeholder research is merely one domain of scholarly activity that studies how companies and their stakeholders interact, and the relationship between the ethics- and social science–based traditions is, at best, at arm's length. There is, they might argue, no reason to privilege the ethics-based element of stakeholder research (as both ethicists and those seeking convergence have tended to do). Indeed, within this second camp, there is even considerable controversy as to whether there is such a thing as "stakeholder theory," if the term *theory* is interpreted solely in social scientific terms. They ask, Does stakeholder theory refer to some unique set of causal factors that theories of power, resource dependence, networks, and institutions do not encompass?

The interplay between these two camps serves as an intellectual backdrop against which good social scientific investigation of these interactions continues unabated. This section discusses the three main areas of investigation covered to date.

What Are the Effects of Stakeholder Management?

Building on the foundation laid by Freeman's (1984) book, one of the most popular subjects for study in the stakeholder research tradition has been the question of whether it matters (financially) how a company manages its stakeholder relationships. In other words, does stakeholder management actually correlate with widely valued outcomes such as profit or stock price?

In this realm, Jones's influential *Academy of Management Review* article from 1995 on instrumental stakeholder theory remains the central work. Jones argues there that the most important characteristic of a company's behavior toward its stakeholders is its moral quality, the presence or absence of dishonesty and/or opportunism. (It is worth noting, here, that this emphasis on morality as the distinguishing feature of good stakeholder management constitutes a departure from Freeman's original model of stakeholder management as largely concerning the procedures undertaken by the company.) Jones proceeds to argue that opportunism and dishonesty will tend to make stakeholders unhappy and lead to increased contracting costs, whereby stakeholders exact higher costs from the company up-front as a way of safeguarding against future opportunism. These costs translate into lower financial performance for the company. In contrast, companies that are honest and trustworthy in their dealings with stakeholders have more efficient contracting and achieve a competitive advantage. Jones then offers an extended list of specific practices (e.g., disproportionate executive compensation, poison pills, and greenmail) that qualify as opportunism and should, thus, correlate with lower financial performance.

A great deal of empirical research has been done to substantiate, either directly or indirectly, the claims of instrumental stakeholder theory. Much of this research has followed not from the theoretical claims of authors such as Freeman and Jones but from the corporate social responsibility literature that Freeman acknowledged as one of his intellectual antecedents.

Much research, of varying levels of scholarly rigor, has been conducted on the subject of the relationship between corporate social performance and financial performance. They address the rather simplistic question, Does "doing good" lead to "doing well"? Insofar as social responsibility can be taken as a rough proxy for stakeholder management, much research hints at the fact that stakeholder management can have some measurable effect on financial performance.

More persuasive, perhaps, is that genre of empirical research designed to test the specific theoretical propositions advanced by instrumental stakeholder theory. Berman's 1998 study of executive compensation, for example, suggests that companies with abnormally high levels of executive compensation do, indeed, underperform those that do not. Subsequent examinations of similar data also suggest that companies that attend to some important stakeholder issues (e.g., product safety and employee well-being) perform better than those that do not. But there is no evidence to suggest that this relationship occurs because the companies value stakeholders intrinsically; rather, it could occur because of the interaction between business strategy and the treatment of stakeholders.

Of course, it is worth noting that financial performance is not the only outcome variable of interest in stakeholder research. Broader questions of societal welfare may also arise from the ways that companies interact with their immediate stakeholders; however, these remain waters uncharted by stakeholder researchers.

What Are the Sources of Stakeholder Management?

A second interesting area for social science inquiry is the question of why companies adopt certain approaches to stakeholder management. Often branded "descriptive" stakeholder research, this research represents the least promising area of research for those interested in advancing convergent stakeholder theory and the most promising area for those seeking to study company-stakeholder interactions on their own terms. After all, to study how a company manages its stakeholders requires that theorists appeal not to "stakeholder theory" but to more established organization theories to account for a phenomenon (stakeholder management) that is interesting in its own right.

Two contributions to this genre stand out in particular; ironically, both were published in the same issue of the *Academy of Management Review* in 1997. Timothy Rowley's network theory–based account of stakeholder management posits that a company's approach to managing its stakeholders will depend, in no small part, on the company's structural position relative to its stakeholder set. Companies existing in dense networks of stakeholders or who are more central will behave different from those in less dense networks or who have less central positions. Rowley's efforts represent a groundbreaking attempt to conceive of the stakeholder set not as a traditional hub-and-spoke system evoked by simplistic readings of Freeman but rather as a web of interrelated groups tied both to the company and to each other. Yet, as network theoretical accounts of organizational phenomena grow more sophisticated, Rowley's effort seems only a simple first step in what must become a more elaborate model of company behavior.

Ronald Mitchell, Bradley Agle, and Donna Wood's article on stakeholder salience is the second important contribution to the descriptive genre. Mitchell, Agle, and Wood posit that stakeholders possess varying levels of three important characteristics—power, legitimacy, and urgency. Insofar as stakeholders possess more of each characteristic, they will be more salient in managers' thinking, receiving priority in decisions about how to allocate value. This model is a useful integration of important insights from various schools of organization theory (i.e., resource dependence, institutional theory, and social cognitive theories), and the ability to categorize stakeholders using these characteristics is a useful managerial heuristic. However, this account also raises stumbling blocks for those who would seek to build further stakeholder theory based on it. Subsequent researchers have (a) offered various interpretations (and misinterpretations) of the term urgency; (b) overlooked the article's emphasis on managerial perception (it is, after all, not how powerful and legitimate the stakeholder is but how powerful and legitimate managers perceive them to be that determines salience); and (c) ignored the extremely simplistic notion of salience, which serves as a vague proxy for the complexities inherent in classifying approaches to stakeholder management.

Indeed, these two contributions, though exemplary, offer two caveats to those who would understand why companies adopt certain approaches to stakeholder management. First, their appeal to existing schools of organization theory, though well-conceived, exposes the stakeholder research domain to the popular critique that stakeholder research has no theory of its own. Second, their emphasis on the causal factors involved (networks, stakeholder characteristics) rather than on the outcome (stakeholder management) does little to remedy the confusion (which must, by now, be apparent to the reader) surrounding how we conceive of stakeholder management. The practices cited by Freeman, the moral qualities of Jones, and the general orientations envisioned by Rowley, Mitchell, Agle, and Wood are all elements of a many-headed beast, and we have little reason to prefer one to the other, scattering the continued efforts of stakeholder researchers.

Why Do Stakeholder Groups Behave as They Do?

From a practical standpoint, a more interesting question for the manager is the issue of how to predict stakeholder behavior. This question forms the basis of the third and, at present, the most rapidly growing stream of stakeholder literature, asking "Why do stakeholder groups behave as they do?" Marshalling theories of collective action, resource dependence, game theory, and social identity, stakeholder researchers have explored this question in several steps, starting first with the question of why stakeholder groups mobilize and then advancing to the question of why, when they do mobilize, they choose the influence strategies that they do. A final step, as yet relatively unexplored, is what conditions determine whether or not these influence strategies actually succeed.

The question of stakeholder mobilization would, at first glance, seem simple enough. Stakeholders act when their interests are threatened. For many years, students of business and society argued some variant of this thesis, contending that stakeholder action resulted from some violation (real or perceived) of the stakeholder group's expectations. When they did not receive what they expected, they tended to strike, boycott, protest, or otherwise mobilize against the company. This was both an intuitive and, in many cases, entirely adequate explanation, but in many important cases, stakeholders mobilized around relatively small violations of their interests, and in many more instances, groups with clear interest did not mobilize or, at least, did not manage to do so in sufficient numbers to have much impact.

Efforts by Timothy Rowley and Mihnea Moldoveanu represent one attempt, premised on an identity-based account, to explain these phenomena. They argue that interests do play an important role in mobilization; so, too, does the collective identity of stakeholder group members. Groups (e.g., certain activist groups) that see protest as a fundamental piece of their group identity are more likely to mobilize. Moreover, structural conditions can strengthen or undermine a common sense of identity. People who are, for example, both parents and churchgoers may be much more likely to mobilize against television violence than those who occupy only one of those groups. Likewise, some groups will possess more or less of the resources necessary to overcome the considerable barriers to collective action for stakeholder groups. Here, again, previous experience with protest and overlapping identities play an important role. In sum, companies must attend to the constellation of interests and identity that surround them, lest they inaccurately assess the likelihood of stakeholder group mobilization.

A second important step in this stream of literature involves the study of why stakeholder groups, once mobilized, choose the strategies that they do to influence the company. Here, the work of Jeff Frooman, extending resource dependence theory to a stakeholder context, sheds some insight. Frooman maintains that a stakeholder's choice of influence strategy depends on just how dependent the stakeholder group is on the focal company for resources and on how dependent the company is on the stakeholder. Depending on how these conditions combine, stakeholders will choose to act either directly or indirectly and will choose either to coerce or compromise with the company. Subsequent empirical research on the subject suggests that there is much to these insights, though other institutional factors may be at play as well.

The final step in this area remains relatively unexplored: When do these influence strategies succeed or fail to change company policy? Here, as Rowley has argued in his earlier piece, a link can be forged back to the question of antecedents of stakeholder management, yet much works remain to make this connection explicit.

Conclusion

Stakeholder theory remains a high growth field of research in the study of business and society, with numerous articles and books being published each year. With students of business strategy and organization theory now showing renewed interest in studying this subject, this is likely to continue. This entry has only hinted at the complexities of this literature, yet it is hoped that it has shown important steps in our evolving understanding of the empirical and normative dimensions of company-stakeholder interaction.

—Michael E. Johnson-Cramer

See also Authority; Corporate Governance

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Statism

Statism is a term employed to characterize practices, examples, or doctrines of state intervention that are regarded as illegitimate exercises of power. There is no single theory of what constitutes statism. However, since the appellation is negative, the reference of the term *statist* (or the specific example or theory of statism) will depend on what one holds to be an unjustified exercise of state power. For example, an anarchist may view any instance of state action as statism, a businessperson may believe that certain regulations are statist, and a citizen may regard government wiretapping as statist.

The term presupposes a basic distinction between state and society. Max Weber characterized the modern state—emerging only after the Renaissance—as exercising a monopoly of legitimate force over a territorial area. So understood, the state also includes institutional divisions (executive, judiciary, legislative, or administrative branches) and possesses an identity distinct from any particular ruler who wields power. To propose, therefore, that some law (or policy) is an instance of statism implies that the law is an unjustified extension of the state into a realm of society that should be free of such intervention. In keeping with this conception, some, such as the early-20th-century writer and critic Albert Jay Nock, draw an explicit distinction between a government and a state, asserting that a government seeks to provide only the functions necessary for community life. Once a government expands beyond the provision of peace and security, it becomes a state. In contrast, some argue that states are necessary for solving problems of collective action, including the provision of public goods. The state is *necessary* because individuals will not cooperate voluntarily to provide these goods. However, such claims remain contestable; in fact, many governmental activities are not undertaken to supply public goods. Attempts to plan the economy, to construct a welfare state, or to diminish inequalities of wealth require the sorts of programs and policies sometimes deemed statist. Whether or not such laws or policies are statist depends on whether they have a publicly acceptable justification. Of course, justifications of state action vary and will depend, for example, on debated notions of rights or on competing conceptions and evaluations of liberty or equality. If one concludes that a law limits freedom of action, one may deem the law to be statist; on the other hand, if one understands this law as serving to enlarge opportunities for all, then one may conclude the law to be justifiable.

Although few would describe themselves as statists, there have been theorists who have claimed that the state is supreme. In the 19th century, Heinrich von Treitschke characterized the state as an organic unity, the legalized constitution of the nation. This understanding also found expression in some of the 20th-century Italian fascists, who regarded the state as the foundation of the nation and conceived the unification of the individual's will with the state as the locus of freedom. Communist regimes proved totalitarian even though Karl Marx forecast the elimination of the state once class divisions disappeared. However, he also maintained that the proletariat must first assume power (the "dictatorship of the proletariat") to destroy the bourgeois state. Nonetheless, the need to exercise political power was emphasized by both V. I. Lenin, who asserted that state repression was required in the transition to socialism, and by his successor, Joseph Stalin, who continued the repressive structures he claimed were necessary to preserve communism.

Most would agree that the 20th century witnessed a dramatic growth of state power, and not just in those states deemed totalitarian. Even if state action is necessary or justifiable, it may elicit further acts that are not so justifiable. Indeed, a steady increase in statist practices may occur as individuals adopt assumptions or metaphors that excuse (but do not legitimate) state action. For example, the democratic ethos may encourage the idea that whatever the government does, "we do to ourselves." In addition, habits and dispositions may incline individuals to look, unthinkingly, to the state to respond to any economic or social problem, thereby encouraging policies that will be deemed statist. However, the governmental response may be worse than either allowing the problem to continue or permitting an indirect, nongovernmental solution to arise. If one has a disposition to state solutions, then one may be inclined less to make a comparative assessment of alternatives than to assume that the governmental resolution will solve the problem without any costs, side effects, or unintended consequences.

Are there political or social structures that may better ensure that the actions of state will be justified and legitimate and, therefore, less likely to be characterized as statist? There may be four—revolution, secession, a written constitution, and public opinion. John

Locke famously argued that if a government breaches its duty to protect natural rights, then the citizens may revolt. The threat of revolution, a drastic and last resort, may serve to counter dire instances of repression but only if the threat appears probable to the rulers. However, a right to secede from a centralized state poses a different threat to unjustified state power: If a sufficient number of individuals (in states, provinces, or cities) find a policy illegitimate, they could petition to secede. The very threat of secession—whether by right or by revolt—promises a loss of power that may lead rulers to consider carefully their proposed actions. In the third place, a written constitution, such as that of the United States, may provide some security against unjustified actions. However, the efficacy of a constitution depends on its particular clauses and, more important, on public beliefs about the significance of the document, its legitimacy, and its proper interpretation. Perhaps the most significant means of limiting the power of the state and forestalling statist practices lies, therefore, in public opinion. The great insight of Étienne de la Boétie, writing in the 16th century, was that any state secures its power, even a ruthless sort, through public opinion. To provide a brake on statist policies, the public must have knowledge and judgment to discern what is legitimate and the will to resist propaganda.

How might statism relate to the problems and issues of business and business ethics? A statist policy is one that seems, at least to some, to be without justification. Given this understanding, those who seek to enact government policies or to set in place economic or business regulations must be able and willing to justify these policies as warranted and just. In any recommendation for or against a government policy, law, or regulation, the business ethicist must make a comparative argument as to the value, justice, and cost of the regulation (or the overall complex of *all* regulations), weighing the proposal against alternatives (including that of instituting no policy, law, or regulation). A corollary concern is whether an increase in the dimension and reach of the state serves, as the sociologist Robert A. Nisbet counseled, to diminish the significance of nongovernmental associations intermediate between the state and the market, as well as the relations and bonds that have arisen via tradition and custom. To the extent that state action has such powerful effects, so does it weaken the very sinews of society.

—F. Eugene Heath

See also Anarchism; Capitalism; Consumer Protection Legislation; Corporate Social Responsibility (CSR) and Corporate Social Performance (CSP); Freedom of Contract; Industrial Policy; Liberalism; Market Failure; Paternalism; Public Choice Theory; Public Goods; Regulation and Regulatory Agencies; Stakeholder Theory

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Stem Cell Research

Stem cells are found in plants and animals, but most moral issues involve human stem cells. Such cells have two significant properties: (1) they can divide to form other types of cells and (2) they can divide indefinitely—that is, they are potentially "immortal." There are three major types of stem cells. A *totipotent stem cell* can divide to form any kind of bodily cell, as well as an entire organism; an example is a fertilized egg (zygote). A *pluripotent stem cell* can divide to form many different kinds of bodily cells, such as neurons or heart cells. A *multipotent stem cell* can divide to form cells of a specific kind: Blood stem cells can form the various types of blood cells, such as red and white blood cells, but cannot divide to form liver or pancreatic cells.

Stem cells can be harvested from the adult (such as from bone marrow or brain tissue), from umbilical cord blood, from the placenta, and from embryos.

Human embryonic stem cells (hES) are harvested from the inner cell mass of the embryo at the blastocyst stage, about 1 week after conception. The sources of embryos include aborted fetuses, but more often, spare embryos donated from fertility clinics. Stem cells can also be harvested from embryos made through cloning adult body cells.

Stem cell research is promising because stem cells could be used to grow replacements for damaged body cells, such as neurons to treat victims of spinal cord injury, Parkinson's disease, or Alzheimer's disease. Other possible diseases that could be treated include heart disease and diabetes. One day, entire organs may be grown.

There has been virtually no opposition on moral grounds to research on adult, umbilical cord blood, and placental stem cells (the placenta, which like the umbilical cord is part of the afterbirth, is a nutrient-carrying organ joining the umbilical cord to the wall of the uterus). Stem cells from cord blood and the placenta are usually classified as adult stem cells. But many scientists believe that because embryonic stem cells, unlike adult stem cells, are naturally pluripotent, they could be used more effectively to grow many types of cells. In contrast to adult stem cell research, embryonic stem cell research has stirred a storm of controversy, with the lines of debate paralleling the abortion issue.

The Moral Status of the Embryo

Since embryos are destroyed in harvesting hES, a key issue is the moral status of the embryo. Is it a human person, with full human rights? Is it a group of cells with no more rights than an isolated group of liver cells? Or does its status lie somewhere in between? Those who believe in the embryo's personhood hold that harvesting hES is immoral, equivalent to manslaughter. They argue that any line drawn after conception limiting human personhood is arbitrary. They further argue that adult stem cells (including cord blood and placental stem cells) can be used just as effectively to develop treatments for disease.

Those who deny any special moral status to the embryo support harvesting hES. They argue that the embryo lacks personhood due to the early embryo's absence of sentience and a developed nervous system. Some argue that because such embryos, either discarded from fertility clinics or cloned for the purpose of harvesting stem cells, will not develop in the womb (because they will not be implanted), they lack any special status above other body tissues.

Another argument is that the United States could fall behind other countries unless federal funding for hES is approved. Debate over hES remains intense in predominately Roman Catholic countries such as Ireland and Italy. However, other nations, such as South Korea (the current leader in stem cell research), the United Kingdom (which has a bank of hES), China, Australia, and Singapore support hES research.

The third option, defended in 1999 by the National Bioethics Advisory Commission (NBAC), as well as by Geron Corporation's Ethics Advisory Board (GEAB), holds that although embryos have some moral status, they are not human persons. The NBAC, established by executive order in 1995, met from 1996 to 2001 and consisted of members from several professions, including philosophy, theology, medicine, and law. Geron Corporation, in business since 1992, is a company specializing in using telomerase, an enzyme involved in cell life span, in research on cancer and on the aging process, and in using hES to treat chronic diseases. Geron has funded research in harvesting hES.

The NBAC report affirmed that discarded embryos could be used for stem cell research, with adequate informed consent from the donor(s). It recommended a ban on selling embryos and that care be taken not to destroy more embryos than absolutely needed for research. The GEAB agreed that although embryos deserve some respect, they lack personhood. hES research is ethical due to the potential for reducing the suffering of individuals with debilitating diseases. The board also emphasized the importance of informed consent by the donor(s), forbade reproductive cloning and cloning to create chimeras, held that the benefits of research should be available to countries with limited resources and that an ethics advisory board (in addition to an institutional review board) should approve stem cell research projects.

The continuing debate over the moral status of the embryo has fueled the continuing controversy over funding hES research. During the Clinton administration, the NBAC recommended federal funding for hES research. But on August 9, 2001, President George W. Bush, though supporting federal funding on stem cell lines derived from embryos that had already been destroyed, did not fund hES research on new cell lines. The ruling did not affect privately funded hES research. He also supported funding for research on adult and animal stem cells as well as on umbilical cord blood and placental stem cells.

Informed Consent and Justice Issues

Other moral issues surround stem cell research. Questions arise concerning proper informed consent. Many hES are harvested from embryos discarded during the process of in vitro fertilization. Issues have arisen concerning the quality of informed consent by the woman or couple donating embryos for research purposes. Does the donor clearly understand that the embryo will be used in scientific research and that it will be destroyed in the course of such research? Are donors aware of the potential benefits and limitations of research on stem cell lines? In addition, a litany of potential benefits of hES research may overwhelm the donor into feeling she has to donate. Do donors know of the potential profit a company can make from stem cells and whether such profit will be shared in any way with the donor? If there is no financial compensation, is this made clear to the donor? Should donors be made aware of the moral debates concerning the status of hES research?

A second group of issues is related to justice. Who shall have access to the fruits of both adult and embryonic stem cell research? Will areas in the United States underserved by the health care system have the same access as areas with adequate health care? What about Third World nations—should they have equal access to treatments derived from stem cell research? But if they receive treatments free, or at a considerable discount, is this fair to Western consumers who must pay full price?

Business Practice Issues

Moral issues also arise related to business practices in companies involved in stem cell research. Although the Geron Corporation formed an ethics advisory board, the corporation has been criticized for deciding to go ahead with the research before the board released its report. Given its close association with the corporation, the extent of the board's independence has been questioned. The broader issue is whether a company should forge forward into the business of stem cell research (especially hES research) before adequate discussion of ethical and societal implications.

Another set of business-related issues involve a company's property rights over the donated embryos and the stem cell lines derived from such embryos. If financial benefit accrues to a company from research on these lines, should the donor receive compensation? Given the patents over cell lines and other research, will the company freely share information gained through research with scientists outside the company? Should patents of stem cell lines be prohibited by law?

A third business-related issue concerns the relationship between the corporation and the academy. Geron funds researchers at several universities, part of a larger process of corporate funding of scientific research at universities. Is there a conflict of interest between scientists' responsibility to the profession to do basic research and their duties to the corporation?

Finally, issues arise concerning the morality of a corporation's private deliberations over stem cell research and its moral dimensions. Some have argued that deliberations should be made public, so that society as a whole can make more intelligent moral choices regarding stem cell research.

—Michael Potts

See also Genetic Engineering; Genetics and Ethics; Human Genome Project; Informed Consent

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Stewardship

A steward is someone who manages or takes care of another person's property, person, or other assets when those assets are put in trust to that individual.

In most conceptions of stewardship, the steward is supposed to place personal interests below those of other people or below the interests of the collective as a whole. In management theory, the concept of stewardship requires managers to subordinate their own personal interests to those of the organization as a whole.

There are several major theories of stewardship in the management literature. One version of stewardship is that managers are stewards or caretakers for the invested resources of companies' owners or shareholders. In this view, which can be found in economic theories of the firm, managers have a fiduciary or fiscal responsibility to ensure that the investments of shareholders into the company through the purchasing of shares in the firm are wisely used. In this view of stewardship, managers are seen as agents of the owners or shareholders and are responsible for the overall well-being of the firm and all its resources. Members of the board of directors are theoretically elected by shareholders to serve as stewards for the interests of shareholders in major decisions made by companies; thus, directors are also stewards and agents of owners.

Another theory advanced by Peter Block focuses on leaders as stewards, a type of leadership he termed *servant leadership*. The other major conception is stewardship theory, which has been developed by James Davis, David Schoorman, and Lex Donaldson and focuses on subordinates in organizations as being trustworthy and willing to help the organization through their work efforts rather than resistant to organizational initiatives. It too emphasizes the good of the organization as a whole, rather than individual interests, and is positioned to counteract some of the assumptions of agency theory, which assumes that managers in organizations will only act to maximize shareholder returns if appropriate safeguards are in place and will seek instead to maximize their personal gains.

Stewardship and Servant Leadership

Servant leadership, according to Peter Block, writing about the relationship between stewardship and leadership in an organizational context, means that a person is held accountable for the good of the whole organization by operating as a servant leader—that is, in service to others in the organization. This perspective on leadership can be contrasted to leadership based on authority and attempts to control others, where the emphasis tends to be on personal gains and self-interest. The key to stewardship in Block's view is the idea of service or servant leadership. Service needs to be authentic or real to be effective. Block argues that service is authentic when there is a balance of power that allows individuals who are not in formal positions of authority to be responsible for their own actions; when the first commitment is to the larger entity, organization, or community rather than the self; when the purpose of the enterprise is jointly defined; and when rewards are equitably and fairly distributed.

The idea behind stewardship is one of reallocating power and resources and the generation of meaning and purpose in an organization more equitably among all the participants in an organization rather than simply locating it in persons holding positions of authority. This view of leadership suggests that empowerment and individual responsibility are critical factors in creating successful organizations. From the perspective of stewardship, when organizations face crises, particularly economic crises, they should focus not on a wealth maximizing or economic goal but on quality, participation, and service. Rather than calling the way the organization is run management, as is typical, Peter Block says it is best to call it governance. This form of governance is focused on partnership and empowerment rather than more patriarchal or authoritative forms of managing. Partnership in this model has four key elements: exchange of purpose or the capacity for each individual to define vision and values for the enterprise, the right to say no or express one's point of view even when one does not get one's way, joint accountability in that each person is responsible for what is happening in the organization and its results, and absolute honesty.

Governance in a stewardship model emphasizes partnership based on an assumption that power can be balanced among individuals in an organization because there is an underlying assumption that all individuals can be trusted to be responsible for their own performance. This notion of empowerment has four elements. One is that survival is in an individual's own hands and that no one else is responsible for that individual's safety or use of voice. Another is defining purpose or the use of one's voice to define one's own purpose in the organization. Third is commitment or emotional investment to the organization, and fourth is being a steward not just for one's self and individuals below a person in the organization but also for those above that individual in the formal structure.

Similarly, under a stewardship model of leadership, the dependency that is created in a patriarchal system, where subordinates are believed to seek safety and consistency over personal responsibility and democracy, is reduced. Individuals are expected to act autonomously and with a commitment toward meeting the organization's goals. A steward or servant leader is more democratic than typical hierarchically structured organizations because there is an assumption that people wish to be empowered to serve the organization's best interest and are willing to assume responsibility for their own safety and freedom.

Peter Block outlines a stewardship contract based on a set of guiding principles. The first principle is to maximize the choice for those closest to the work, and the second principle is to reintegrate the managers and the doing of the work under the assumption that everyone is doing some management of work and everyone should do some of the work of the organization. Third is to let measurements and controls serve the core workers, and fourth is to yield on consistency across groups and support local solutions rather than seeking a top-down, one-size-fits-all way of organizing. Next is to recognize that service is everything and people are accountable to those they serve as well as to those upward in the organization, which leads to the principle that management as a job title should be deglorified and demystified. Other principles underlying stewardship are the ending of secrecy and enabling of disclosure or transparency and the need for demanding a promise that people will actually commit themselves to acting in the best interests of the organization. The final principle is to redistribute wealth so that the reward system links everyone's rewards to the success of the team and the organization as a whole.

The structure of an organization and basic management practices in an organization using stewardship as its model of leadership may need to shift to emphasize customer relationships first and indeed even organize around customers rather than in other ways, improve products and services, and transparently report results. Work flow and job design shift so that power and responsibility are shared among teams, and discipline is handled by a team of peers rather than higher ups in an organization. Because responsibility is located within the team, it is the team that decides what to purchase and from whom, as well as how to undertake quality control.

Stewardship Theory

Stewardship theory is the second management perspective on stewardship. It puts forward a set of positive assumptions about managers and subordinates in an organization. With roots in psychology and sociology, stewardship theory assumes that leaders' behavior in organizations and other collectives emphasizes the good of the organization over individual interests. Stewardship theory was proposed as a counterpoint to agency theory, which has at its base a model of economic "man" as a self-interested, rational actor interested only in personal gain, who will calculate costs and benefits in taking any action and make decisions that favor the decision maker's self-interest. In corporations, managers, in particular the top management team and the chief executive officer, are seen through the lens of agency theory as agents of the investors or owners, who are called principals. The assumptions of agency theory suggest that agents, that is, the managers, will favor their own as opposed to principals' interests unless there are structural safeguards that prevent them from doing so. Under these circumstances, managers will abrogate their fiduciary responsibility to owners.

Stewardship theory takes the opposite view of managers' actions in organizations. Specifically, stewardship theory assumes that stewards will focus on the goals of the whole organization or collective rather than personal goals or self-interest and that this emphasis on organizational goals will benefit the principals of the organization, that is, the owners whose interests are represented by the stewards. That is, managers will fulfill their fiduciary responsibilities to owners. The basic idea is that the steward will gain satisfaction by closely aligning the steward's own interests with those of the organization, particularly a business firm, so that the principals' or owners' interests will be achieved. The fundamental notion is that corporate governance and ultimately performance will benefit from leaders who are stewards for principals or investors because all stakeholders will benefit from the organization's success. Such leaders are expected to be more cooperative because they believe that cooperation is more productive and useful than other forms of behavior, such as competition, and because they focus on the needs of the collective as a whole.

Stewardship theory has performance implications because the assumption is that when the steward's, typically the managers and particularly the chief executive officer, and the organization's goals are aligned, the interests of principals and other stakeholders will be met because stewards believe that their own needs will be met in the context of serving organizational interests. Stewardship theory also assumes that stewards can be trusted to serve the organization's interests and that they should be granted autonomy to do their jobs without excessive supervision. As a result, the costs of monitoring, creating incentives to motivate managers and subordinates, and competitive behavior are expected to be less when a stewardship model is in place in an organization. Under this line of reasoning, stewards will be granted greater autonomy to do what they believe is right for the organization because their interests are organizationally aligned with those of principals or owners.

The developers of stewardship theory suggest that there are a number of factors that differentiate it from agency theory. The key differentiator is motivation. In contrast to agents, who are supposed to be focused on extrinsic rewards that have specific market value to them, stewards focus on intrinsic rewards that tend to be intangible and not readily quantified, such as the opportunity for personal growth and achievement, affiliation or relationships, and what psychologist Abraham Maslow terms self-actualization. Stewardship theory also proposes that stewards will more closely identify with the organization than those who are not stewards and will be highly committed to its goals. Another area of difference between stewardship and agency theory is in the use of power. Agents use what is called institutional power, which has at its base coercion, legitimate authority, and the capacity to provide rewards and punishments. Stewardship relies more on personal power, which includes what is called referent power in which one person identifies with another person, and expert power or the power that derives from knowledge that is task relevant. Differences in the organizational culture and style also influence the extent of stewardship present, with high-involvement organizations and more community- or collectivist-oriented cultures more likely to foster stewardship than more control-oriented and individualistic organizations. Stewards also view themselves as more equal to subordinates than do agents, who tend to have what is called high power distance.

Stewardship theory is especially relevant in the context of corporate governance, because it focuses attention on the controversy about whether the chief executive officer and chairman of the board should be the same individual or not. Stewardship theory argues that it would be best to combine these functions if the executive is a steward because there will then be alignment between the individual and organization's best interests and the organization will ultimately perform better.

—Sandra Waddock

See also Agency, Theory of; Empowerment; Ethical Role of the Manager; Leadership; Power, Business; Servant Leadership

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STEWART, MARTHA (1941–)

Martha Stewart was a very popular and influential American celebrity in the late 1990s and early 2000s, a virtual media icon who ran afoul of the law and served prison time. Stewart was born on August 3, 1941, in Jersey City, New Jersey, and when she was 3 years old, her parents, Edward and Martha Kostyra, moved her and her five siblings to Nutley, New Jersey. Because of her legendarily strong work ethics and character, she received a partial scholarship to Barnard College in New York City. To pay the remainder of her tuition, she worked as a model for television commercials and magazines. At Barnard College, she met her husband Andrew Stewart, and they married during her sophomore year in 1961, just before she graduated with a bachelor's degree in European history and architectural history. In 1965, she had her daughter Alexis, and within 2 years she became a stockbroker. When recession hit Wall Street in 1973, Stewart decided to leave the brokerage and move to Westport, Connecticut, with her husband and daughter.

Stewart became a writer and columnist for the magazine *House Beautiful,* while simultaneously serving in a similar capacity for the *New York Times.* In 1982, she coauthored her first book, *Entertaining*, and shortly thereafter she started publication of her own magazine, *Martha Stewart Living.* By this time, she was a regular guest on the morning network talk shows, and she even appeared on "The Tonight Show" and "Late Night with David Letterman." In 1993, she began her own syndicated television program, "Martha Stewart Living," and she became a well-known and much-loved celebrity, her empire capped by the creation of Martha Stewart Living Omnimedia, Inc. She was the American guru of housekeeping, cooking, gardening, decorating, crafts, and holiday parties.

However, her period of prosperity lasted only about a decade. In 2004, at age 62, Martha Stewart stood trial on charges of conspiracy, obstruction, securities fraud, and lying to investigators in connection with the sale of her stock in ImClone, a biotechnology company. Standing trial alongside Stewart was her former stockbroker, 41-year-old Peter Bacanovic, who faced the same charges in addition to perjury and falsifying documents. Stewart's troubles stemmed from her sale of shares of ImClone on December 27, 2001, one day before the FDA announced it had rejected the application for approval of ImClone's cancer drug, Erbitux—news that caused the company's stock prices to plummet.

It was Stewart's response to the subsequent federal probe that ultimately proved incriminating as prosecutors claimed that she not only conspired with Bacanovic to cover up evidence concerning the sale but also lied publicly about her involvement in the scandal to protect the stock price of her own company, Martha Stewart Omnimedia. Bacanovic claimed he and Stewart sold her ImClone stock after having a "selling conversation" on December 20, 2001, a week before the sale was executed. During that conversation, Bacanovic said he and Stewart reviewed her entire portfolio, not just her shares of ImClone, and agreed to sell her shares in the company if the price sunk to $60.

Although she made $51,000 by selling her shares in advance of the announcement, Stewart was never charged with insider trading. Stewart, ever the domestic diva, even while facing a maximum of 30 years in prison, would join her daughter Alexis every morning before court to have their hair and makeup done. Stewart was convicted in March 2004 of lying to investigators and conspiring with Bacanovic to cover up the circumstances surrounding the stock trade during the federal probe that followed. On July 16, 2004, Martha Stewart was sentenced to 5 months behind bars and 5 months house arrest, with an additional 2 years probation and $30,000 fine.

Stewart issued statements proclaiming her innocence before, during, and after the trial. Her supporters criticized the investigation as being sexist, saying that federal agents unfairly targeted one of the richest women in the world (whose wealth directly resulted from her reputation, the public perceptions of her) while ignoring far worse criminals. In a sense, one's perceptions of and attitudes about this case reflect the mind-set, background, and perspective of the perceiver as much if not more than the facts about Martha Stewart and her fall from the pinnacle of American society.

—Dirk C. Gibson, Rebecca Warin, and Robert McClain Gassaway

See also Insider Trading; Integrity; Public Relations; Savings and Loan Scandal; Scandals, Corporate; Securities and Exchange Commission (SEC); U.S. Department of Justice

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Strategic Corporate Social Responsibility

Strategic corporate social responsibility is the attempt by companies to link those largely discretionary activities explicitly intended to improve some aspect of society or the natural environment with their strategies and core business activities. While corporate social responsibility has historically referred to a firm's economic, legal, ethical, and discretionary responsibilities to society, strategic corporate social responsibility, in general, represents discretionary activities that form a company's community relations function or foundation, including corporate philanthropy, volunteerism, and multisector collaborations. Corporate social responsibility can be compared with the mere general concept of corporate responsibility, which is a company's complete set of responsibilities to its stakeholders, societies where it operates, and the natural environment, as manifested through its operating practices.

Corporate social responsibility represents the direct efforts by a company to improve aspects of society by the firm as compared with the integral responsibilities that every firm has with respect to primary stakeholders such as employees, customers, investors, and suppliers. The use of the term *strategic* implies that the discretionary socially oriented activities of the firm are intended to have direct or indirect benefits for the firm—that is, to somehow help the firm achieve its strategic and economic objectives. There is a wide range of ways in which companies can use corporate social responsibility activities strategically. These ways range from helping local schools improve so that, long term, the workforce will be better educated, to improving local conditions in the community so that it will be easier to recruit and retain employees, to improving the firm's reputation among customers so that they will continue to use the company's products and services, as well as numerous other examples.

Sometimes termed *enlightened self-interest*, strategic corporate social responsibility initiatives are closely linked to strategic philanthropy and cause marketing. They attempt to help achieve a company's core mission and strategies by providing a socially beneficial foundation for enhanced economic value added. This benefit to the firm happens through improved reputation from the social desirability that key stakeholders, such as customers and employees, feel for being affiliated in some way with a company perceived to be more socially responsible or, more directly, through increased use of the company's products and services that are tied to donations to specific charitable organizations.

Some observers object to strategic corporate social responsibility on the grounds that the company cannot or should not both be doing moral or social good while also profiting financially. Other observers see no necessary conflict in what is called doing well and doing good, because for companies that are under increasing pressure for good short-term results, strategic corporate social responsibility represents a way for them to attempt to meet the needs of multiple stakeholders, particularly investors and societal stakeholders, including customers, employees, and investors concerned with corporate responsibility, simultaneously.

There is significant and growing evidence from a large number of research studies that companies that are more socially responsible, or more responsible in general to all their stakeholders, perform at the same level or somewhat better than less responsible companies. This empirical evidence suggests that there are no necessary trade-offs between profitability in terms of financial performance and responsibility, even explicitly socially beneficial activities. Companies with good corporate social responsibility records, according to employee and consumer surveys, may find it easier to recruit and retain employees, attract and keep new customers, and even attract investors concerned about issues of corporate responsibility, also called socially responsible or ethical investors.

—Sandra Waddock

See also Cause-Related Marketing; Corporate Citizenship; Corporate Philanthropy; Corporate Social Responsibility (CSR) and Corporate Social Performance (CSP); Corporate Social Responsiveness; Socially Responsible Investing (SRI); Voluntarism

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STRATEGIC PHILANTHROPY

Strategic philanthropy is an approach by which corporate or business giving and other philanthropic endeavors of a firm are designed in such a way that it best fits with the firm's overall mission, goals, and values. This implies that the business has a carefully articulated strategy and that it understands how to integrate its philanthropic initiatives with this strategy in actual practice. A major characteristic of strategic philanthropy is that the motivation is not solely altruistic. To understand how strategic philanthropy has become an everyday practice, it is useful to trace this concept as it has unfolded in business history.

Beginnings of Corporate Philanthropy

The concept of philanthropy evolved through business history even before the broader corporate social responsibility movement had taken shape. The concept of business responsibility that prevailed in the United States during most of its history was fashioned after the traditional, or classical, *economic model* of the firm. Dominant in the late 1800s and early 1900s, the economic model of the firm thought of the marketplace as the primary determinant of what business firms did in their communities and in society. The pattern of corporate philanthropy in Europe and other parts of the Western world paralleled its development in the United States. Unfortunately, though the marketplace did a reasonably good job in deciding what goods and services should be produced, it did not fare as well in ensuring that business always acted generously, fairly, and ethically. In addition, business created many social problems and the view was developing that business had some responsibility for these social problems that extended beyond just producing goods and services.

Years later, when laws began to be passed constraining business practices, it might be said that a *legal model* emerged. Society's expectations of business changed from being strictly economic in nature to encompassing issues that previously had been at business's discretion. Over time, a *social model* of the firm emerged. What this social model did, in effect, is embrace both the economic and legal emphases and add yet another layer of expectations by society that business would assume some role in addressing social problems and issues that had arisen.

In the late 1800s and early 1900s, initial indications of business's willingness to contribute to the community were localized efforts toward meeting community needs through philanthropy, or business giving, and paternalistic practices. It is evident that businesspeople did engage in philanthropy—contributions to charity and other worthy causes—even during the periods that were dominated by the traditional economic view. Voluntary activities to improve, beautify, and uplift the community were evident. One very early example of this was the cooperative efforts between the railroads and the Young Men's Christian Association immediately after the Civil War to provide community services in areas affected by the railroads. These initiatives, in hindsight, can now be seen as early examples of strategic philanthropy, because they benefited both the communities and the railroads.

The emergence of large corporations during the late 1800s played a major role in hastening the movement away from the strict classical economic model of the firm in society. As the economy transitioned away from one dominated by small, powerless companies to large corporations with more concentrated power, questions of business responsibility began to be raised. By the 1920s, community service had become much more important for business. The most visible example of this was the Community Chest movement, which received its impetus from business.

One example of early progressive business ideology was reflected in Andrew Carnegie's 1889 essay "The Gospel of Wealth." Carnegie asserted that business must pursue profits but that business wealth should also be used for the benefit of the community. Philanthropy turned out to be one of the best ways in which firms could benefit the community. A prime example of this was Carnegie's funding and building of more than 2,500 libraries for communities.

Corporate philanthropy continued to grow into the 20th century and by the late 20th century had become one of the institutionalized ways by which businesses could aid communities, the growing number of nonprofit organizations, and other national and international groups. Today, corporate philanthropy is considered to be one of the foremost means by which companies fulfill their social responsibilities and come to be regarded as good corporate citizens.

Philanthropy Defined

Before developing the concept of strategic philanthropy further, it is useful first to examine the concept of philanthropy itself. The word *philanthropy* has generally been defined as a concern for or love of humankind. Philanthropy has been linked to efforts to demonstrate this fondness or concern for humankind through charitable gifts, aid, or donations. Though most people would not philosophically disagree with the concept of philanthropy, throughout history some have. Friedrich Nietzsche, for example, objected to it as a concept of universal good because he thought it represented the weak parasitically living off the strong. Ayn Rand is another major philosopher who held a similar view. Political views on philanthropy have also been present. Most governments have been supportive of philanthropic efforts on the part of companies and individuals and have supported these efforts through tax incentives and tax breaks. Though the term *philanthropy* seems to imply some altruistic expression, as in "love of humankind," today the concept more nearly refers to the giving of resources for the benefit of others.

Conceptually, today, philanthropy may be seen as a part of companies' corporate social responsibility or corporate citizenship initiatives. Archie Carroll has argued that philanthropy fulfills businesses' discretionary responsibilities to be good corporate citizens. These philanthropic activities are voluntary, guided only by businesses' desire to engage in social activities that are not mandated, not required by law, and not generally expected in an ethical sense. Philanthropy is "desired/expected" in most societies. The public has an expectation that business will engage in philanthropy, in part because it has become so much a part of business tradition and in part because many believe it is part of the social contract between business and society, especially between business and the local community. Others believe business should engage in philanthropy to partially offset some of the social harm or social problems business has engendered.

By the first decade of the 2000s, philanthropic initiatives include corporate giving, matching programs in which companies match contributions given by their employees, product and service donations, employee volunteerism, partnerships with local governments and other organizations, and any other kind of community involvement on the part of the organization and its employees. These philanthropic initiatives are in response to ongoing needs in the community in areas such as education, culture and the arts, health/human services, and civic and community activities. In addition, special needs arise due to emergencies such as the tsunami in Southeast Asia in 2004 and Hurricanes Katrina and Rita in the United States in 2005.

Strategic Philanthropy Takes Shape and Evolves

The concept of strategic philanthropy has evolved out of traditional forms of business giving. Early on, corporate giving was more focused on the needs that had arisen in the community and so philanthropy was more altruistic in nature—more focused on an exclusive consideration of the needs of others. With the passage of time and the heightened competition and cost pressures that have characterized the business community in the past several decades, corporate executives have begun looking more carefully at the kinds of impacts philanthropic efforts might have. It has become evident that business can not only help others but help itself at the same time, and this germ of thought is what has produced the modern strategic philanthropy emphasis. At the same time, corporate giving has become institutionalized and professionalized, and as it has been turned over to professional managers, top management has come to view the giving function as one that should deliver more specific, direct benefits to the company, and thus, the idea of strategic philanthropy has been born and cultivated in a business climate that has been more driven by profitability and accountability toward the bottom line.

Strategic philanthropy is an approach to business giving that seeks to achieve goals for the community or recipient of the giving and for the business itself as well. Strategic philanthropy is more focused. It does not just address any legitimate need in the community but rather focuses on those needs or issues that are consistent with or aligned with the firm's overall mission, objectives, programs, or products/services. A classic example of strategic philanthropy is the Ronald McDonald Houses sponsored by McDonald's hamburger chain. The Ronald McDonald Houses are facilities usually built near children's hospitals to help families who want to be close to their children who may be receiving longer-term treatment at the hospital. The Ronald McDonald House Charities maintains more than 200 houses in 44 countries around the world where families can stay together for free when traveling for a sick child's treatment and 48 rooms within hospitals for the same purpose. McDonald's, which has long viewed children as one of its target markets, thus is able to generously contribute to children and their families, thus enhancing its own interest or strategy at the same time. The children and their families win and McDonald's as a corporation wins. It should be clarified that McDonald's, as a company, initiated and sponsors the Ronald McDonald House Charities, but many other companies also contribute to the charity. In addition, each chapter also relies on individual contributions. In a sense, then, this is an ideal example of strategic philanthropy in that McDonald's gets high name recognition and publicity for the charity, even though the company is just one of the many supporters of the charity.

In using strategic philanthropy, companies strive to align their corporate giving or community relations initiatives with their own goals, objectives, or markets. The idea is to have a double impact—a positive impact on the recipients of the philanthropy and some kind of positive impact on the businesses' bottom lines or strategies. Two other examples are worthy of mention. The first is Novartis' creation of its nonprofit, Novartis Research Institute for Tropical Diseases. The nonprofit Institute allows it to focus on the discovery of new drugs for treating neglected diseases. The company benefits and the victims of neglected diseases benefit. Second is IBM's On Demand Community Program. This program permits IBM employees around the world to share the company's technology and other resources with the agencies where they sign up for volunteer service. Both parties benefit.

Strategic management expert Michael Porter has argued that the term *strategic philanthropy* has begun to be used to explain virtually any type of charitable giving that has some definable theme, focus, or approach that builds bridges between the businesses that are giving and needs in the community. Porter has been critical of strategic philanthropy, arguing that the link between the companies and the charities are often weak, tenuous, or semantic. He suspects that most of these initiatives really do not have anything at all to do with corporate strategy but are aimed at achieving positive publicity or goodwill for the companies and for improving employees' morale. His belief is that for strategic philanthropy to be viewed as genuine or valid, it needs to effectively integrate social and economic goals in such a way so as to produce legitimate social impact in the community. Of course, his criticisms may be broadened to include any corporate citizenship initiatives on the part of business, not just philanthropy.

Cause-Related Marketing

One of the shapes or variations that strategic philanthropy has taken on is that of cause-related marketing, or cause marketing. Many critics claim that this is more marketing than philanthropy, but others have held that it is an extreme form of strategic philanthropy in that the link between the businesses' interest and some social or public cause is tightly tied together. In cause marketing, each time a consumer uses a service or buys a product, a donation is given by the company to the charity. Thus, cause marketing has sometimes been referred to as "quid pro quo philanthropy."

One of the earliest examples of cause-related marketing was in the early 1980s when American Express Company introduced a program whereby it would contribute 1 cent to the restoration of the Statue of Liberty each time one of its credit cards was used to make a purchase. This initiative generated $1.7 million for the restoration of the historical monument and a substantial increase in the use of the company's cards. Today, American Express coordinates its philanthropic and marketing efforts with its community business program and cause-related-marketing campaign to help small business owners acquire access to the credit and resources they need to start or grow their businesses. So the company now gives a portion of credit card charges to three national nonprofit organizations specializing in community economic development when American Express Community Business Card customers use their cards. Today, many different companies have linked using their products or services to the amount they would then donate to some worthy charitable cause.

Just as Porter has been critical of strategic philanthropy, he has especially been critical of cause-related marketing. He thinks these efforts are more targeted toward improving the companies' reputations than doing good in the community and, thus, fail as authentic efforts toward strategic philanthropy. In his view, the best way to maximize philanthropy's value is to follow a path that effectively combines pure philanthropy with pure business in such a way that genuine social and economic values are created.

The Business Case for Strategic Philanthropy

The impetus behind the movement toward strategic philanthropy has been the expectation by CEOs and top echelon executives that for corporate giving to continue, the "business case" for it has to be established. The business case is the argument or rationale as to how the business is specifically benefiting from the philanthropic endeavors. It is the explication of reasons why business is believed to be benefited by the philanthropy. One of the leading business groups supporting the idea of strategic philanthropy is Business for Social Responsibility (BSR), a nonprofit association of firms and executives who support the idea of integrating business's social role with its economic objectives. BSR has assembled research that indicates that companies, through their philanthropic giving, may

- increase customer loyalty and enhance brand image,
- strengthen employee loyalty and productivity,
- enhance corporate reputation, and
- expand into emerging markets.

In short, specific business advantages that strengthen the companies' bottom lines are achievable through carefully designed philanthropic initiatives.

An interesting aspect of strategic philanthropy is that two firms in the same industry may decide to pursue divergent philanthropic projects and initiatives while both are focusing on the bottom-line benefits to the company as well as helping the community. In the home improvement/products industry, for example, The Home Depot supports sustainable forestry, community impact grants, and volunteerism, while Lowe's, its major competitor, supports Habitat for Humanity, sponsorship of American Red Cross disaster relief, and community college scholarships. Executives in these two firms made strategic choices to engage different philanthropies but with doubtless similar objectives in terms of strategic impact on the company's profitability and reputation.

Since strategic philanthropy is a part of corporate social responsibility initiatives, it follows that these same benefits accrue due to these efforts. Also, it can readily be seen that most of these reasons are business related, not philanthropy related. Thus, the business case is strengthened. Finally, it is worth noting that Paul Godfrey has developed and presented an analysis of literature and research that supports the idea that (a) corporate philanthropy can generate positive moral capital among stakeholders and communities, (b) this moral capital can provide business owners with insurance-like protection for a firm's relationship-based intangible assets, and (c) this protection contributes to shareholder wealth. Thus, through logic and research, he has added to the business case for corporate philanthropy, especially strategic philanthropy.

—Archie B. Carroll

See also Cause-Related Marketing; Corporate Philanthropy; Corporate Social Responsibility (CSR) and Corporate Social Performance (CSP); Strategic Corporate Social Responsibility

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Strategic Planning

Strategic planning is a periodic, typically annual process in which organizations' top managers review the organization's strategy, which is its overall direction, competitive positioning, and the resources needed to achieve its short- and long-term goals and objectives. Strategic planning has several phases: formulation, analysis of the strategic environment internally and externally, development and selection of strategic alternatives, and implementation, with feedback from results incorporated as necessary changes in the plan. Strategic planning is part of the overall strategic management process and represents a formal opportunity for the management team to review, assess, and redirect, if necessary, the company's plan of action for a specified period of time into the future. One criticism of the strategic planning process is that it is based on a rational and logical view of the management process, which may not be realistic in today's competitive and highly dynamic environment, so many strategic planners recognize the need to constantly revise the strategic plan as new information is received or conditions facing the organization shift.

Strategic planning begins with specifying an organization's long-term vision or mission, that is, its purpose for existence; focusing on the development of goals and objectives that will enable the organization to achieve that vision; and identifying the means through which the vision will be achieved, typically through the major business units and functions of the enterprise, such as marketing, operations management, finance and accounting, technology and information systems, and human resources. The analytical phase of strategic planning focuses internally on the company's resources, capabilities, core competencies, and its strengths and weaknesses, in what is called the resource-based view of the firm. External strategic planning focuses on the organization's positioning within its industry using industry and competitor analysis. Most often, strategic planning is undertaken by the chief executive officer of an organization and the top management team, including the top managers of any business units. Sometimes many others are involved in the process as well so that the process is inclusive and the goals developed are well understood and agreed to by all the people who will have to implement the plan.

Internal Analysis for Strategic Planning

Strategic planning teams generally focus on a number of key questions focused internally. A basic question tends to be, "What business are we in?" Answering this question helps define the basic mission or purpose of the organization and suggests some boundaries to its activities, as well as indicating the priorities for management attention. Defining what business the company is in provides a solid basis for the determination of the company's vision—that is, how it hopes to affect the world through its business operations.

Another useful strategic planning question is, "What is our strategic intent, coupled with, how or through what strategies or means are we going to achieve our vision?" Strategic intent is a future-directed focused assessment of what you will do to make your definition of what business you are in real. It should be focused, crisp, and clear to everyone to be effective and is based on an analysis of the internal strengths and weaknesses of the firm, combined with an assessment of external opportunities and threats. Analyzing the combination of strengths, weaknesses, opportunities, and threats is sometimes referred to as SWOT analysis. Sometimes SWOT analysis is accomplished by looking at the various business units; at other times, there is an assessment of the core functions of the organization, such as marketing, finance and accounting, operations and logistics, distribution, supply chain management, human relations, and other important areas.

Another important question focuses on what makes this organization unique or different from similar organizations. This uniqueness, which sets that organization apart from others, provides a basis for competitive advantage and is called the organization's distinctive or core competency. Core competencies are built on internal organizational resources, analyzed through a perspective called the resource-based view of the firm. Core competencies are defined as the things that an organization has that are rare, valuable, difficult to imitate, and not easily substituted.

Having identified the internal strengths and weaknesses of the organization, the management team then can ask, What are the critical success factors that we have or need to satisfy? Identification of critical success factors, which are those skills or resources that are necessary for success in a given industry or competitive situation, helps managers focus on next steps.

External Analysis for Strategic Planning

External analysis focuses on the current and expected competitive, societal, and political situation of the organization. External analysis includes industry and competitor analysis, as well as evaluation of trends that might affect the company's performance. Industry analysis, which is based in the thinking of economist Michael Porter, allows the management team to assess the company's position with respect to its competitors, suppliers, customers, threats of new entrants into the industry, or threats from potential substitutes for the company's products or services.

External analysis also involves an assessment of the ways in which the general environment facing the organization affects it. For example, many management teams gather data on demographic trends that might affect the firm, the sociopolitical climate of countries where it operates, technological shifts, local cultures in places where it has facilities, and related issues. External analysis includes stakeholder analysis, which helps a company identify the status of critical relationships that it has with its primary stakeholders, investors, employees, customers, and suppliers, or its secondary stakeholders, such as communities and governments, depending, of course, on the nature of its business.

Focus, Implementation, Evaluation, and Feedback

A key part of any strategic plan is selecting from among the various strategic alternatives open to the organization, which should have been revealed through the internal and external analysis phases. The next step is to implement the plan, which is typically carried out by business units or functional managers responsible for specific divisions, products, and functions in the enterprise. Implementation also involves the allocation of resources among the business units if the organization has multiple divisions or among functional areas such as marketing, sales, operations, and human resources if there are no divisions. Priorities identified in the evaluation and analysis process help managers determine how to allocate resources most effectively.

Critical to the success of any plan is evaluating the outcomes or results of initiatives taken, gathering feedback from key stakeholder groups as well as operating results, and feeding that information back into the strategic plan so that revisions can be made. The key is to think about strategic planning as an ongoing process that evolves with the adaptations that the organization needs to make to continue to perform effectively in its environment.

—Sandra Waddock

See also Market Power; Shareholder Model of Corporate Governance; Strategy and Ethics

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Strategy and Ethics

Strategy is commonly understood to be a plan of action adopted by an organization to attain its goals, while ethics can be described as a system of moral values and principles that govern the conduct of an individual or a group. In a business enterprise, strategy reflects a company's pattern of decisions, commitments, and actions undertaken by the company to improve its competitiveness and generate profits for its owners. However, earning a profit is not the only goal of a business. It must provide quality products for its consumers, continued jobs for its employees, and taxes for its government. In the process of formulating and implementing strategies, potential conflicts arise in the goals of the company's various stakeholders such as stockholders, managers, employees, suppliers, government, and society at large. It is while dealing with these conflicting goals that managers face ethical dilemmas in prioritizing the demands of various constituents that form the core of the strategy-ethics interface, which we address in the following paragraphs.

Ethics in business strategy has gained renewed focus due to the scandals that have unfolded in recent years at several major corporations in the world including Enron, Arthur Andersen, Tyco, and Adelphia in the United States; Parmalat in Italy; and Livedoor in Japan. As a consequence of these business debacles, numerous employees lost jobs, shareholders lost wealth, governments lost taxes, and society as a whole suffered. To prevent future occurrences of such widespread harm, the U.S. government enacted the Sarbanes-Oxley Act in 2002 to ensure governance mechanisms to protect the interests of shareholders and other stakeholders of the firm. The U.S. Corporate Sentencing Guidelines also provide a strong incentive for businesses to promote ethics at work. Tort laws, contract law, intellectual property law, and securities law all govern business behavior. However, while the law can regulate the basic actions of the firm, it tends to be reactive in nature and contains several ambiguities that present opportunities for unethical practices. Therefore, merging company strategy with an ethical framework can guide managers in their task of strategy formulation and implementation. We briefly describe the concepts of strategy and ethics as commonly understood and then discuss the role managers play in the interface between the two.

Strategy

Companies try to pursue strategies that will help them remain competitive and earn superior returns. While formulating a strategy, a company thoroughly analyzes its external and internal environment. The external environment includes general or macroenvironmental conditions such as global trends, industry conditions, and competitive environment. The internal environment includes the company's internal resources and capabilities such as knowledge, technology, physical assets, manpower, and capital. Based on the perceptions of its environmental opportunities and threats, and internal strengths and weaknesses, a firm will consider different strategies and implementation approaches. A company achieves sustained success only if it has an astute, timely strategic game plan, revises its strategies according to changes in the environment and company situation, and implements the strategies with proficiency. Competitive success requires companies to position well in the existing market space, develop and use distinctive competencies to support their strategy, and design internal systems and practices to effectively implement the strategy. The industrial organization (I/O) model suggests that companies should first assess the external environment, select industries with high potential for superior returns, and then develop strategies as called for by the industry. I/O theory suggests that internal resources and capabilities should be developed as called for by the external environment. On the other hand, the resource-based view suggests that the primary basis for strategy and sustained advantage are internal resources and capabilities of the company. Companies, thus, need to develop resources that are valuable, rare, nonimitable, and nonsubstitutable and craft strategies that will help both exploit current resources and develop new resources. Strategy formulation, therefore, involves analysis of both external and internal aspects of a company and developing an appropriate course of action or strategy. Strategy implementation involves developing internal organizational structure, systems, and processes to execute the strategy and matching them to the strategy.

In a large company, strategies exist at multiple levels and, correspondingly, ethical issues also arise at multiple levels. Corporate-level strategy relates to the decisions and priorities of corporate managers of large diversified corporations (such as General Electric), which may include the choice of the mix of different types of businesses it will have under its corporate umbrella, that is, whether to acquire, merge, or sell off individual business units. Each of these decisions will have ethical implications such as should employees be laid off, or will the merger stifle competition? Functional strategies relate to the pattern of actions and priorities of various functional areas such as production, marketing, human resources, and finance. Again, ethical issues can arise in each functional strategy. Production of defective products can injure innocent people, toxic production processes pose a threat to the environment, misleading product information and deceptive advertising can misguide buying decisions, excessive monitoring can invade employee privacy, and so on.

Ethics

To understand ethics and its relationship to strategy, it is important to briefly consider some philosophical underpinnings. The utilitarian approach espoused by John S. Mill and Jeremy Bentham in the 18th and 19th centuries evaluates action based on the following maxim: greatest good for the greatest number of people. Many businesses adopt this approach to evaluate a course of action by using a cost-benefit analysis. However, costs are often hidden. For example, damage to the environment cannot be readily quantified. Besides, utilitarianism as a framework does not consider the rights of all parties concerned and, therefore, can be unfair to the minority. A small number of employees may be laid off to garner greater profits for many investors, so while this action may be consistent with the utilitarian approach it may be unfair to those few employees affected by job loss. The Kantian or rights approach framework advocates that people be treated as ends and not as means and that basic individual rights of all should be respected. Moral theorists argue that fundamental human rights are the base of the moral compass managers navigate by when making decisions that have an ethical impact. However, the rights approach is not useful when the basic rights of two groups of individuals are in conflict. The justice approach propounded by John Rawls evaluates a strategy based on the impartial and equitable distribution of benefits and harm among stakeholders. This framework suggests that managers should weigh a course of action behind a *veil of ignorance* of the particular characteristics of the people involved, and economic goods and services should be so distributed as to be just and advantageous to the least advantaged groups in society. The virtue approach developed by Aristotle is based on virtues such as honesty, fairness, trust, and toughness. According to this framework, moral virtues and habits enable a person to live according to reason and, thus, make ethical decisions. Moral education aimed at improving moral reasoning and debate and the ability to summon courage to take a principled stand regardless of pressure or punishment are considered very important.

Viewed as a continuum, a business strategy can range from being egoist to altruistic, drawing again on the philosophical underpinnings of ethics. Ethical egoism suggests that each person ought to pursue his or her own self-interest, and an action is considered right when it serves one's personal goal. Ethical egoism does not forbid actions that may help others when interests of the self and others coincide. In contrast, altruism is devotion to the interests of others. It is "other directed" behavior at the cost of one's own self-interest. Altruism emphasizes loyalty, devotion, and the subordination of self to a cause, a person, or an ideal. Put in the context of business ethics and strategy, egoism suggests that a business should focus on its primary goal of providing returns to its owners, the challenge being, however, to find the path that aligns the interests of a firm and its managers with those of all stakeholders. An altruist strategy, on the other hand, would have the firm forgo some of its immediate gains and profits to benefit some constituent, say employees or even society, by investing resources in providing health care or education or in mitigating poverty.

Strategy-Ethics Interface and Role of Managers

Strategy and business ethics are inseparable from each other. While the corporation is a separate entity for legal purposes, it cannot act on its own will. The behavior of the corporation is the result of decisions made by the managers and top executives of the firm. Managers act as agents of the shareholders, who are one set of the stakeholders of the firm. Agency theory postulates that managers, instead of acting in the interests of their principals (owners of the firm), will act opportunistically in their own interests when not properly monitored. Such managers are ethical egoists who focus on self-interest and self-promotion. Indeed, the recent scandals of fraud mentioned earlier have been attributed to the failure of adequate monitoring of executives entrusted with the task of making decisions for the benefit of the corporation. The managers put their own personal welfare ahead of others' welfare. In an alternative view, managers are perceived to be stewards of the distinct stakeholders of the firm, acting altruistically to promulgate ethical strategies that create value and meeting the needs of all constituents of the firm. Stewardship theory is based on the premise that managers will act in a manner consistent with the long-term interests of all stakeholders basing their decisions not on short-term gains for themselves but on corporate principles that enable their firm to be viable through actions that promote sustainable profitability. Sustained profitability of the firm requires long-term investments that may not bear immediate returns. High emphasis on short-term economic returns may be detrimental to the interests of several stakeholders and the society at large. Yet employees are evaluated every year, and companies need to meet stock market's quarterly performance expectations—both short-term horizons. While the notion of "performance" is multidimensional and includes social, environmental, and economic performance, the economic dimension generally supersedes others. Some argue that strategy is at odds with ethics primarily because of the overriding concern of strategy with instant economic performance and the inability of managers to find the point of equilibrium between long-term investment and short-term reward.

While the notions of egoism and altruism described above are the two ends of the continuum to evaluate strategy with the perspective of ethics, a practical "middle" perspective is often used to balance the needs of multiple stakeholders. The notions of corporate social responsibility, corporate citizenship behavior, and corporate accountability are more appropriate to explain the interface of strategy and business ethics. As corporations are members of society, they should engage in socially responsible actions in a manner consistent with fundamental social, moral, philosophical, and ethical principles. The corporation should play an active role in benefiting society, even helping solve problems such as environmental degradation. Even from the extreme economic perspective of strategy, enlightened self-interest dictates that pure business interests are best served by being intertwined with social interests. A company enhances its business when various stakeholders support it. Employees are likely to be more motivated and committed when they perceive their employers to be just, transparent, and doing the right thing; customers are likely to be loyal when the company has a reputation for fair dealing and providing safe products; suppliers are likely to be consistent and reliable when they are treated with consideration; lenders are likely to extend credit readily when they have confidence in the governance and accounts of the firm. In sum, the costs of doing business will be reduced for a firm that follows an ethical strategy that is responsive to the needs of all stakeholders, which eventually leads to better economic performance ensuring greater shareholder returns.

Strategy and Ethics in the Global Context

Modern corporations operate in several competitive environments, national boundaries, societies, and cultures. The notion of ethical standards varies across countries and cultures, and managers are faced with many ethical dilemmas globally. Practices that are illegal and certainly unethical in the United States may be acceptable in some other countries. While gift giving is common and might be expected in the Japanese, Oriental, and Middle-Eastern cultures, it is unacceptable in the United States as it can be construed as bribery. While labor laws in developed countries ensure a minimum level of ethical behavior toward employees, absence of such laws in developing nations have led multinational corporations to adopt sweatshop labor conditions, use of child labor, and unsafe working conditions to reap cost efficiencies. Countries that do not legislate or have environment protection laws find themselves dumping grounds for toxic or hazardous waste by corporations following a strict wealth maximization strategy for shareholders to the exclusion of other objectives. Corporations, thus, are confronted with a great number of strategies and contextual conditions that contribute to their facing ethical dilemmas.

Several international organizations such as Social Accountability 8000, Global Compact, International Labour Organization, and United Nations Commission on Transnational Corporations provide uniform guidelines and codes of conduct to multinational corporations. These guidelines are not mandatory laws and cannot be enforced. However, many companies have found that when they have swerved away from following an ethical strategy, they have become a target of negative media attention leading to loss of customers, as Nike did when their sweatshop labor practices in developing countries came to light.

Strategizing Ethically

As noted earlier, strategy and ethics are intertwined. Higher ethical standards and practices improve a firm's image and reputation, and this intangible resource is likely to provide a sustainable advantage to the firm. While violating basic ethical norms may provide temporary benefits and short-term economic gains, long-term financial performance is likely to improve when firms consider the interests of all stakeholders, which results in a positive image of the company. Even investors and shareholders seek out companies that implement ethical strategies that ensure profits by following principles, as evidenced by the growth and popularity of social investing in portfolios such as domini social investments.

Strategizing ethically would mean that businesses should deeply embed ethical principles and standards in their mission, strategies, and day-to-day practices. Managers need to set high ethical standards, need to be cognizant of ethical principles while formulating and implementing strategies, and need to recognize and reward employees who follow ethical standards and penalize those who do not. Statements about the long-term direction and strategy can include a company's philosophy and values, key corporate values can be incorporated in the company's mission statement and then translated into the employee code of conduct, and the code of conduct could be strictly followed and reinforced. Similarly, the design of the organization and formal reporting systems can ensure enforcement of ethical standards and practices at all levels and in all functional areas of operation. Besides formal mechanisms, informal mechanisms such as organization culture, shared norms, values, and beliefs can be very useful in fostering an ethical climate within an organization. Human resource practices, such as recruitment, compensation, training, and promotion decisions, can also be geared to explicitly value and emphasize ethical standards. A well-developed whistle-blowing policy that allows benign disobedience and encourages constructive criticism can also be instrumental in cultivating an ethical climate. Many firms have trained ethics officers whose job is to monitor ethical behavior and counsel managers when the need arises. Above all, managers as leaders could set an example by their own behavior and serve as referent models to employees throughout the organization.

—*Devi R. Gnyawali and Manisha Singal*

See also Adelphia Communications; Agency, Theory of; Altruism; Codes of Conduct, Ethical and Professional; Corporate Social Responsibility (CSR) and Corporate Social Performance (CSP); Domini Social Investments; Egoism; Fraud; Poverty; Stakeholder Theory; Sweatshops

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Stress, Job

Job stress is a harmful physical or emotional response employees experience when they have expectations that they cannot fulfill because of their capabilities, resources, or needs. Stemming from stressors in the workplace, such as time pressure and role overload, job stress may result in harmful consequences for both individuals and organizations. Outcomes of job stress may be physiological, psychological, or influence an individual's behavior at work. For example, an individual's health may be affected, burnout may occur, and productivity levels may also suffer as a result of job stress.

Early signs of job stress include headache and stomachache, difficulty sleeping and concentrating, short temper, and low morale. Research also suggests links between job stress and cardiovascular disease, musculoskeletal disorders, and psychological disorders. Stress in the workplace is linked with increased absenteeism, tardiness, and turnover intentions. A further understanding of the causes of workplace stress, as well as preventative measures, would benefit both individuals and organizations. Although many believe that both individuals and organizations should share the responsibility for preventing and alleviating job stress, many organizations believe that the responsibility for stress management rests solely with employees. Organizational change efforts targeted toward stress reduction can impact the bottom line.

Causes of Job Stress

Job stress is widespread and rising for many reasons, some of which include the working conditions and expectations of employees. Workplace stressors may lead to job stress, which in turn may lead to outcomes of stress. Different individuals respond differently to job stressors, and some employees do not experience job stress. Yet most people find certain working conditions stressful.

In a model illustrative of the stressors-strains (outcomes) relationship, work environment stressors, such as role conflict and time pressure, are common characteristics of the work that may adversely affect an individual (cause human strains). These work roles encompass conflicting or ambiguous job expectations, too much responsibility, and role overload at work. Additional job stressors stem from economic conditions that pressure organizations to make rapid changes to their workforces, including restructuring and downsizing; these changes often lead to increased work expectations and longer working hours on the part of the surviving employees. U.S. employees now work longer hours than employees in most other countries. Other common stressors include job insecurity, inability to deal with rapid change, and lack of career opportunities. In addition, management styles and organizational cultures that limit participation by employees, do not foster communication throughout the organization, and do not support family-friendly policies are other common sources of job stress. When coworkers and supervisors do not support employees, increased levels of stress and increased outcomes of stress may be experienced. How tasks at work are designed can also influence stress levels of employees. Task design is concerned with workload expectations, as well as work hours, shift work, rest breaks, tasks with little meaning to employees, and tasks that do not use employees' skills and provide little feeling of control. Finally, unpleasant and dangerous working conditions may also lead to increased levels of stress.

Prevention and Reduction of Job Stress

One recent survey reported that 40% of workers felt that their jobs were either very or extremely stressful. Individuals can lessen the effects of job stress in several ways. These include balancing work and personal life, having supportive friends and coworkers, and maintaining a relaxed and positive outlook. Stress management programs offered by organizations for their employees can also be helpful in alleviating and sometimes preventing job stress as well. A healthy work environment may be created and maintained by organizations that offer such programs, if they also aim to reduce stress through organizational change efforts.

To determine the changes that organizations need to implement, the underlying causes of stress need to be diagnosed. Some examples of changes that may be implemented include limiting employees' workloads, clarifying roles and responsibilities, designing meaningful jobs, encouraging participation in decision making, and allowing for social interaction among employees. Organizations that recognize good performance and provide career development for employees, among other things, demonstrate both high levels of productivity and healthy, low-stress work. Any stress-reduction process must include problem identification, intervention, and evaluation.

—Margaret Posig

See also Occupational Safety and Health Administration (OSHA); Participatory Management; Work-Life Balance

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Subsidies

In the broadest sense, a subsidy is a grant or other financial assistance given by one party for the support or development of another. However, in a business environment, the kind of subsidies most likely to raise legal and ethical issues are those given by a government or a philanthropic foundation to a person or association for the purpose of promoting an enterprise considered beneficial to a specific subsection of the public or the public in general. A subsidy can be legal, illegal, ethical, or unethical, depending on its effects. The first British subsidies were grants given by Parliament to the King in the Middle Ages to replace taxes formerly collected by the Crown. Now, however, subsidies are granted for reasons such as to keep prices low, to maintain income, or to preserve employment. Governments grant subsidies for several reasons. A governmental subsidy can help eliminate a region's industrial, economic, or social disadvantages, or it can facilitate the restructuring of an industry, especially when changes have become necessary because of changes in trade and economic situations. In addition, a subsidy can be used to sustain employment, to encourage retraining and change in employment, to encourage research and development, or to redeploy industry to avoid congestion and environmental problems.

For example, the U.S. government subsidized Amtrak in an effort to maintain passenger service where it might not otherwise be profitable. Metro transit systems are often subsidized, as is agriculture, housing (the HUD program), regional development, medical care and treatment (the Medicare Prescription Drug Program), and educational development. In addition to federal subsidies, individual states may grant subsidies. For example, Pennsylvania has subsidized medical malpractice insurance for doctors, and Montana grants subsidies to help parents provide for special needs children. As an example of a private (nongovernment) subsidy, Patrick Taylor, an oilman and philanthropist, developed a subsidy scholarship program (the TOPS program) for all Louisiana high school graduates with B+ grade point averages who attend Louisiana public colleges and universities. Corporations may similarly subsidize new ventures, supporting them until they show a profit or prove to be unprofitable.

In addition to different kinds of subsidies, subsidies can take many different forms. Although governments sometimes make direct payments such as cash grants, many subsidies are indirect. They may take the form of research and development support, tax breaks, provision of raw materials at below-market prices, insurance, or low-interest loans or low-interest export credits guaranteed by a government agency.

Subsidies, while intended to support the public interest, can violate ethical or legal principles if they lead to higher consumer prices or discriminate against some producers while benefiting others. Domestically, subsidies granted by individual states are unconstitutional if they in any way discriminate against out-of-state producers, thus violating the Privileges and Immunities Clause or the Dormant Commerce Clause of the U.S. Constitution. Subsidies, while immediately beneficial to an industry, may in the long term prove to have unethical, deleterious long-term effects. Internationally, subsidies that affect global prices, especially export subsidies of agricultural products, are controversial, regarded as both harmful and unethical by developing nations, and depending on their nature and effects are discouraged by international trade agreements such as the World Trade Organization (WTO).

Domestic Subsidies and the U.S. Constitution

The U.S. federal government has given subsidies to its farmers since the Great Depression of the 1930s. In 2005, U.S. farmers received $14 billion yearly in production and support subsidies. The main thrust of such agricultural legislation has been to support farmer income and ensure abundant production. The most subsidized U.S. farm products include wheat, corn, rice, cotton, sugar, peanuts, soybeans, and milk products. Milk subsidies, in particular, have led to some famous Supreme Court decisions.

In most of the 50 states in the United States, federal marketing orders guarantee a uniform minimum price for producers of raw milk. In the 1990s, however, Massachusetts dairy farmers were apparently facing a particularly difficult time even with the federal minimum, so state legislation was passed authorizing a tax assessment of all milk sold by dealers to Massachusetts retailers. These tax funds were then distributed to Massachusetts dairy farmers. A side effect of this subsidy was to make it more expensive for out-of-state farmers and dealers to sell milk in Massachusetts, as compared with in-state farmers and dealers. An out-of-state dairy farm brought suit. The Supreme Court ultimately ruled that the Massachusetts subsidy violated two clauses of the Constitution. First, because it benefited in-state farmers at the expense of out-of-state farmers, it violated the Privileges and Immunities Clause, which mandates that “the Citizens of each State shall be entitled to all Privileges and Immunities of Citizens in the several states.” Furthermore, the Massachusetts milk subsidy violated what has come to be known as the *Dormant* or *Negative* Commerce Clause.

The Commerce Clause provides that Congress has the power to regulate commerce “among the several states.” Sometimes the Supreme Court decides that a law passed by Congress (a federal statute) violates the Commerce Clause, but the Supreme Court has also found that a logical consequence of the Commerce Clause is to make it illegal for states to regulate interstate commerce. A state regulation that is illegal and unconstitutional because it affects interstate commerce is described as a violation of the Dormant or Negative Commerce Clause. Thus, in addition to violating the Privileges and Immunities Clause, the Massachusetts milk subsidy was unconstitutional because it interfered with interstate commerce.

Long-Term Effects of Subsidies and Ethical Controversies

In addition to being illegal because it violates the Constitution, a subsidy can be regarded as unethical if it weakens an industry economically. For example, the arguments in favor of agricultural subsidies are several. Proponents argue that government support is necessary to achieve the goals of supporting the farm economy and ensuring a low-cost food supply. Farmers are at risk because demand for agricultural products is inelastic, meaning that consumers continue to buy similar quantities of food regardless of price increases or decreases, yet as storage is limited farmers have to sell regardless of the price they receive. In addition, farmers are particularly vulnerable to weather and changes in market conditions. Thus, to stay in business, it is argued that farmers need to be protected from the risk of low prices. Furthermore, even though only 2% of Americans live on approximately 2 million farms, culturally Americans identify themselves with farmers and feel it is in America's interest to preserve small farms. Finally, because more than half of U.S. Senators come from largely rural states, the farm states have very strong representation in Congress.

Arguments against agricultural subsidies are also strong. Farm subsidies for crops such as cotton are often granted on the basis of how much acreage was planted the previous year. As a result, it has been argued that these farm subsidies, rather than helping farmers survive, have acted as a "cancer" on rural America: They raise land prices significantly, making it hard for young farmers to get started because farms that benefit most from such subsidies are large, established, consolidated farms, not small family farms. In addition, subsidy programs generally encourage monoculture—raising the same crop year after year on the same plot of land—because benefits are tied to crop yields on a specified acreage planting base. Large-scale monoculture contributes to soil erosion by depleting nutrients in the soil because planting the same crop drains a particular nutrient from the soil year after year without any opportunity for replenishment. Furthermore, it has been argued that farm subsidies have kept marginal land in production, resulting in overproduction and lower prices, and have discouraged farmers from switching to crops that have proven more profitable based on market pressure rather than subsidy potential. Thus, while some subsidies are very beneficial and make possible things that might otherwise be difficult to achieve, they can have long-term complicated unethical or illegal effects that were not anticipated when they were first conceived.

Subsidies and Global Commerce

In addition to raising domestic legal and ethical issues, subsidies raise legal and ethical issues in a global context. Subsidies are considered to be unfair trade practices when they affect a second country's industry: Government A's subsidy of a particular industry puts comparable products produced in Country B at a competitive disadvantage when A's products are imported into B. While competition and lower prices usually benefit the public, when low prices are the result of subsidization, their export into a second country may cause serious economic disruption of the domestic industry, including lost profits, an excess of available goods, layoffs, and even widespread bankruptcy. In addition, the artificial advantages to consumers in the second country gained from subsidization lead to a misallocation of domestic resources. Manufacturers of a product selling primarily in the home market will make decisions concerning expansion based on their perception of how their product competes in the marketplace. If the cost of an imported competing product is low due to subsidization, domestic manufacturers may perceive that their company is not competitive even though it remains the low-cost producer in his market.

WTO Controversy Surrounding Agricultural Subsidies

The WTO is a global international organization dealing with the rules of trade between nations. Although WTO was created in 1995, the heart of the WTO is the General Agreement on Tariffs and Trade (GATT), negotiated and signed originally in 1948 by the bulk of the world's trading nations and ratified by their governments. Although GATT was first passed in 1948, it has been modified in several rounds of negotiations. The Uruguay Round, which ended in 1994, culminated in the creation of the WTO. The nature of GATT is that of an agreement, a contract among nations, and the WTO helps implement that agreement. The WTO is not an international government and cannot itself sanction governments, but its members can sanction each other for unfair trade practices by raising duties against members who do not follow GATT rules. The WTO's stated goals include encouraging countries to liberalize trade, ensuring that individuals, companies, and governments know what the trade rules are around the world, and thus helping producers of goods and services, exporters, and importers conduct their business.

The rules of the WTO prohibit some subsidies and allow countries to increase duties when they find that a subsidized imported product is harming a domestic industry. However, those rules have long made an exception for subsidized agricultural products because many countries, including the United States and the European Union, the two largest agricultural exporters, have long subsidized such products and repealing such subsidies would have serious political implications. As recently as 2002, the U.S. Congress raised farm subsidies. In 2005, U.S. farmers received $14 billion in agricultural subsidies and European Union farmers, $47 billion. European dairy subsidies were such that each cow reportedly received the equivalent of $2.20 per day, an amount greater than the daily income of many people in developing countries.

The ethical implications of such subsidies are as complex in a global perspective as they are domestically. Cotton growers in the United States reportedly received half of their income from the U.S. government under the Farm Bill of 2002. The deficiency payments stimulated overproduction and resulted in a record cotton harvest in 2002, much of which was sold at low cost on the world market. This depressed world cotton prices to a level far below the break-even price of most growers around the world: African farmers received 35 to 40 cents per pound for cotton, while U.S. cotton growers, backed by government-deficiency payments that made up for market prices, received 75 cents per pound. African nations, like other developing countries, argued that they must be able to export their principal commodities to survive but subsidies such as the U.S. cotton deficiency payments were crippling Africa's chance to export its way out of poverty.

Members of the WTO have long since agreed in principle that agricultural subsidies should be scaled back. However, it has been extremely difficult to reach specific agreements on how and when members should reduce such subsidies. The original Uruguay Round of negotiations produced the first multilateral agreement dedicated to subsidies and was implemented over a 6-year period that began in 1995. Under this scheme, measures that support domestic prices or subsidize production in some other way such that they have a direct effect on production and trade must be cut back. Measures with minimal impact on trade can be used freely. They include government services such as research, disease control, infrastructure, and food security. They also include payments made directly to farmers who do not stimulate production, such as certain forms of direct income support, assistance to help farmers restructure agriculture, and direct payments under environmental and regional assistance programs. Direct payments to farmers to encourage them to limit production are also permitted, as are government assistance programs encouraging agricultural and rural development in developing countries.

Despite implementation of the Uruguay Round, international discussion on whether these subsidies should be discontinued remains highly emotional with concerns about food security, past food shortages, and the special place that farms and farmers have in a society's history. The Doha Round of WTO negotiations in 2001 resulted in an agreement that members would work to phase out all forms of export subsidies and reduce trade-distorting domestic support of agriculture. Nevertheless, the subsequent September 2004 round of talks in Cancun, Mexico, collapsed in an impasse between rich and poor countries—particularly over the issue of subsidies provided to farmers in the United States, the European Union, and Japan. A coalition of 21 developing countries, led by Brazil, India, and China, urged developed countries to quickly eliminate the use of trade-distorting agricultural subsidies, but most of the developing nations were unwilling to budge on their own protectionist measures. Furthermore, a group of West African cotton-producing nations challenged the United States to make cotton a test case, but the United States was then unwilling to meet the West African demands.

In the December 2005 Hong Kong Round of negotiations, however, in an effort to avoid replication of the Cancun stalemate, the United States agreed to terminate cotton subsidies in 2006, without demanding a similar concession on the part of other members. The meeting concluded with an agreement to eliminate all forms of export subsidies by the end of 2013. Whether this agreement will result in decreased friction between developed and developing countries remains to be seen. As of January 2006, the anticipated effect of the U.S. cotton concession is an immediate global rise in price of 10% to 15%.

WTO Discouragement of Trade-Disrupting Subsidies

Under the WTO agreements, countries periodically negotiate and state the duty rates on various products they will charge all other WTO members, with the ultimate goal being the progressive lowering of those rates and the liberalization of trade. They cannot normally discriminate between their trading partners. If one country is granted a special favor, such as a lower customs duty rate for one product, then all other WTO members must be given the same rate. This principle is termed *most favoured nation treatment*. Some exceptions are allowed. For example, countries can set up a free trade agreement that applies only to goods traded within the group—discriminating against goods from outside (such as the North American Free Trade Agreement and the European Union). Or they can give developing countries special access to their markets. Or a country can raise barriers against products that are considered to be traded unfairly from specific countries. The GATT contains an Agreement on Subsidies and Countervailing Measures (SCM Agreement), which has been used increasingly by both developed and developing countries in recent years.

The SCM Agreement addresses both the subsidies countries may grant to various domestic industries and the use of countervailing measures to offset injury caused by subsidized imports from other countries. The GATT defines subsidy very broadly as anything given by the government that confers an economic benefit on the recipient. However, only two categories of subsidies are prohibited under the SCM Agreement: subsidies that support products to be exported and subsidies that prefer domestic goods over imported goods.

In addition to prohibited subsidies, the SCM Agreement specifies actionable subsidies. These are subsidies that are not prohibited, but can be challenged if they injure or seriously prejudice a member's domestic industry or if they nullify the benefits that GATT was created to confer. Under the SCM Agreement, a member country is not allowed to impose a countervailing duty unless it has investigated and found subsidized imports, injury to a domestic industry, and a causal link between the subsidized imports and the injury.

These rules apply to WTO members that are considered to be developed countries. However, exemptions are provided for developing countries. The lower a member's level of development, the more favorable the treatment it receives with respect to subsidies. Thus, for example, least developed countries and members with a GNP per capita of less than $1,000 are exempted from the prohibition on export subsidies.

Members must notify the WTO of all specific subsidies that they grant and must also update those notifications every year. Members are also required to notify the WTO of their countervailing duty laws and regulations and any countervailing actions they take. If a member objects to a subsidy or a countervailing duty imposed by another member, or otherwise believes that trade rules have been violated, that party can file a complaint and the dispute will then be resolved through the WTO's dispute resolution process, which is much like a trial conducted by a panel of experts from member countries. If it is unhappy with the panel report, the subject country has a right of appeal to the WTO's Appellate Body.

If the country that is the target of the complaint loses, it must enter into negotiations with the complaining country (or countries) to determine mutually acceptable compensation—for instance, tariff reductions in areas of particular interest to the complaining side. If no satisfactory compensation is agreed on, only then may the complaining side ask the Dispute Settlement Body for permission to impose limited trade sanctions ("suspend concessions or obligations") against the other side. The Dispute Settlement Body must grant this authorization unless there is a consensus against the request. Thus, the ultimate consequence for not following GATT rules is the *possible* imposition of higher import duties by other members.

—Nadia E. Nedzel

See also Cross-Subsidization; Developing World; Development Economics; Doha Development Round of 2001; Dumping; Duty; Efficient Markets, Theory of; European Union; Federal Trade Commission (FTC); Free Trade, Free Trade Agreements, Free Trade Zones; International Trade; Most Favoured Nation Status; Tariffs and Quotas; Unfair Competition

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Sunset Laws

A "sunset law" or "sunset provision" is a law that provides for the automatic termination of a government program, agency, or law on a certain date, unless the legislature affirmatively acts to renew it. Sunset laws were widely promoted in the United States in the 1970s as reform measures to eliminate bloated and unresponsive government bureaucracies. Political theorist Theodore Lowi, for example, touted sunset provisions as diminishing interest-group power over government programs and as promoting more active legislative oversight. Legislators would have to be convinced of the independence and efficacy of programs facing sunset provisions if these programs are to survive, and they would presumably not renew programs that were failing or that served only a few special interests.

In spite of support from prominent politicians and government reform groups such as Common Cause, no comprehensive federal sunset law was passed in the United States. A majority of states did create sunset programs, however, and a large number of individual federal statutes were drafted with sunset provisions. These generally provided for formal review of agencies, boards, and commissions, with program termination looming for those that could not persuade sunset audit staff (and the legislators to whom they reported) of their efficacy.

The 1970s sunset provisions were not terribly successful in practice, however. From the beginning, many of them exempted larger agencies from any review. Moreover, by the early 1980s, it was widely recognized that the de facto burden of proof had shifted from agencies undergoing sunset review to the staff conducting it. Program renewal was commonplace, and actual sunsets were rare. Agencies—supported by the powerful interest groups that sunset laws were supposed to disempower—successfully defended the status quo. Since the 1970s, a large number of laws passed with sunset provisions have had those provisions removed by technical amendment well before any audit or review takes place. Nonetheless, some scholars have argued that while few state programs are actually threatened by sunset provisions, sunset laws have to some extent encouraged more active legislative oversight than previously existed.

In current political practice, sunset provisions are used tactically in at least two ways. First, they are used as a bargaining chip in gathering votes in favor of controversial legislation. The presence of a sunset provision can persuade a wavering legislator (or that legislator's public) of the "purely temporary" nature of a controversial law. Thus, for example, sunset provisions are thought to have been partially responsible for the bipartisan support for the USA PATRIOT Act, which greatly enhanced federal prosecutorial powers in the wake of the September 11, 2001, terror attacks on the United States. Sunset provisions can also be used cynically to reduce the projected costs of a new program, tax, or tax reduction. Public statements can be based on estimates that only forecast costs out to the sunset date, even if it is expected that the program will eventually be renewed or have its sunset provision repealed.

—Stephen R. Latham

See also Interest Groups; Regulation and Regulatory Agencies

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SUPEREROGATION

A fundamental question in business ethics is whether organizations have a responsibility, or even a right, to engage in activities—perhaps aimed at betterment of society—beyond their formally designated roles of providers of goods and services. For example, should firms pay more attention to the environment than is required by law? Should they provide better pay and working conditions than law and market conditions demand? If they do engage in such acts, what are the associated costs to shareholders and others? Similarly, at the individual level there has been growing emphasis on individual actions that exceed formal role requirements to assist others in the firm, meet deadlines, protect the organization, or otherwise "go above and beyond the call of duty." These issues have deep roots, founded in the concept of supererogation.

The combination of two Latin words (*supererogare*), supererogation essentially means "to pay over and above" or "to do more than is required by duty." Supererogatory acts combine elements of optionality and praiseworthiness. The term first appeared in the Latin translations of the scriptures; a New Testament reference is found in Luke 10:35, in the parable of the Good Samaritan. It was later adapted by ecclesiastical writers for the "excess of merit" attributed to saints—works or good deeds over and above what is required for their own salvation and the merit of which is transferable to others in need of indulgence.

According to this view, actions of "superabundant merit," typically collected by the works of Jesus and the saints who greatly exceeded what was required for their own salvation, are deposited in the Spiritual Treasury of the Church to be disposed by the Pope and the bishops for remitting the sins of others. The institution of Indulgences, by which sinners could buy remission of their sins if they "took up the cross" against the infidel in the Crusades or, later, through contributions to the coffers of the Catholic Church, developed in the late Middle Ages. Indulgences were even offered to markets, taverns, and brothels if they gave a substantial portion of their profits to the Church.

The concept of supererogation drew fierce attacks during the time of the Reformation. Luther, Calvin, and Anglican theologians condemned the idea of "super-meritorious" actions and the corruption associated with the commercialization of the system of indulgences that it justified. They argued that no person can do all that is strictly required as a duty, much less exceed it.

This antagonism toward supererogation, coupled with the cessation of the institution of indulgences in the Catholic Church, led to a sharp diminution in interest in the concept of supererogation. In fact, the concept did not appear in nonreligious ethical theory until Urmson's seminal 1958 article "Saints and Heroes" (though Urmson did not actually use the term). Urmson argued that, in addition to the traditional threefold classification of moral actions as obligatory, permitted, and prohibited, there were acts that were praiseworthy though nonobligatory (actions that are good to do but not bad not to do). Since then, supererogation has again been widely discussed and hotly debated. While the context has shifted from theological to ethical, the terms of debate often remain similar.

Heyd wrote that supererogation is a characteristic of attributes of acts rather than persons. According to his analysis, an act is supererogatory if and only if

- it is neither obligatory nor forbidden;
- its omission is not wrong and does not deserve sanction or criticism;

- it is morally good, both by virtue of its intended consequences and by virtue of its intrinsic value (being beyond duty); and
- it is done voluntarily for the sake of someone's good and is thus meritorious.

McKay added the notion that the act should have a potential cost to the agent. In undertaking the task, the agent risks losing something to which he or she might normally be entitled. Because of this cost, the permission not to perform the act despite its moral goodness is normally granted to such acts. Examples of supererogatory actions might include a nurse rendering aid to plague victims or a soldier sacrificing his or her body to a live grenade to save colleagues. At the organizational level, an example might be the actions of Aaron Feuerstein, CEO and owner of Malden Mills. When a 1995 fire burned most of Malden Mills to the ground and put 3,000 people out of work, most employees thought Feuerstein would build overseas to cut labor costs and their jobs would be lost forever. To the surprise of almost everyone, Feuerstein—feeling it would be unconscionable to put 3,000 people on the streets and devastate the local communities—rebuilt the plant and continued to pay his idled workers during the months until the plant was again operative.

To most people, the idea of actions that are "above and beyond the call of duty" seems intuitively reasonable. However, standard forms of ethical theory seem unable to accommodate supererogatory acts. Deontological ethical theories relate to what ought to be done, to duties and obligations, and to justice and right. According to this perspective, since all morally good action is obligatory, there cannot be a separate class of morally good actions the omission of which is not wrong. Teleological ethical theories argue that there are just two categories of acts: obligatory (if they maximize the highest good) and forbidden (if they do not). As such, pure teleological theories such as utilitarianism grant supererogatory acts no unique status, placing them in the general class of acts that are obligatory because they maximize the overall good.

Although the term *supererogation* rarely appears in the organizational literature, its central idea—performing beyond requirements—is now widely discussed and researched using terms at the individual level such as *organizational citizenship behavior*, *extrarole behavior*, and *prosocial behavior*. The common theme of these terms is a sense of going beyond what is strictly required in one's formally designated role. For instance, organizational citizenship behaviors consist of those actions such as helping coworkers, protecting the organization, and giving extra effort as needed that are not in one's job description but contribute to the maintenance and enhancement of the social and psychological context that supports task performance. With growing emphasis on teamwork, flexibility, and collaboration in modern organizations, such behaviors are increasingly crucial.

As with supererogation, the concept of *organizational citizenship behavior* and associated terms highlights a variety of thorny issues. For example, if extrarole behaviors come to be recognized in performance appraisals and rewards, can they reasonably be considered supererogatory? If extrarole behaviors become expected, do they truly remain extrarole? For example, employees of Nordstrom's are known for going beyond what is strictly required in their roles. Nevertheless, such behavior is now generally expected of those employees and failure to display them may be viewed as a deficiency. And, at the organizational level, there is fierce debate over whether acts that go beyond legal requirements to help society are in the best interests of shareholders and other parties dependent on the firm. In the Malden Mills case cited earlier, for example, the company filed for bankruptcy in 2006, and many wondered whether Feuerstein's benevolence was partly the cause.

In sum, the concept of supererogation raises many provocative questions, and there are certainly no comfortable conclusions regarding its ethical status. Nevertheless, the notion of supererogation "makes sense" to most people; is clearly important; and poses fundamental challenges to conceptions of the nature and limits of duty, the role of ideals and rationalization in ethical judgment, and the connection between actions and virtue.

—Ramon J. Aldag

See also Altruism; Benevolence and Beneficence; Consequentialist Ethical Systems; Duty; Kantian Ethics; Utilitarianism; Virtue

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SUPPLY-SIDE ECONOMICS

The origins of the supply-side economics school of thought can be traced to the 1970s as a conservative reaction against postwar Keynesian "demand-side" economic policies associated with changes in government spending levels to smooth out business cycles and to fund social spending programs. The central idea in this framework is that government can stimulate growth in aggregate supply through suitable tax policies, which in turn will result in an expansion of gross domestic product, accompanied by a decline in inflation.

The policies associated with supply-side economics are typically tax cuts. A prime example of such a policy is a cut in the top marginal income tax rates, which has the greatest effect on the highest income earners. According to the theory, a reduction in the marginal income tax rates will raise the after-tax compensation of the income earners. Since they will get to keep more of their earnings, individuals will now have an incentive to work harder and thus raise their earnings. Furthermore, some individuals who may have previously opted to stay out of the labor force may now be enticed back into the workforce. Consequently, the supply of labor increases, which in turn will cause an increase in the aggregate supply of goods and services in the economy. The projected results are higher output, lower unemployment, and lower inflation.

One variant of the supply-side argument asserts that the reduction in tax rates will result in increased tax revenues for the government. This argument is encapsulated by the Laffer curve (Arthur Laffer reportedly drew the curve on a restaurant napkin), which depicts the effect of tax rates on revenues. Initially, as tax rates rise, so do revenues, but after a certain point, any further increase in tax rates is accompanied by declining revenues as the higher tax rates begin to exert a stultifying influence on work effort. Furthermore, higher tax rates may also encourage increased use of tax avoidance measures; in some cases, these measures might include illicit efforts to conceal income. Under these circumstances, a reduction in the tax rate will not only engender greater work effort but also reduce the extent of tax evasion, leading to a robust increase in economic growth and an overall increase in tax revenues.

Proponents of a flat tax also make similar arguments. Notably associated with Steve Forbes, flat tax proposals seek to levy the same (low) tax rate on all incomes, thereby effectively providing a sizeable tax cut for high-income earners. To prevent large increases in the budget deficit, some versions propose outlawing the myriad tax deductions currently enjoyed by the middle class and upper-income groups. These include eliminating the mortgage interest deduction, a particular favorite of homeowners and the real-estate industry. Stiff resistance from those who would be affected by the loss of such tax breaks has frustrated proponents of the flat tax.

The empirical evidence on the relationship between tax rates and revenues is mixed, at best. Most studies show that cutting tax rates leads to less revenue, not more. The Reagan administration's tax cuts of the early 1980s resulted in a decrease in tax revenues. Between 1980 and 1984, a period when average incomes (per person, adjusted for inflation) rose following the tax cuts, revenues from personal income taxes (per person, adjusted for inflation) fell. The decline in revenues continued throughout the decade; by the end of Reagan's second term, the record of large budget deficits had been firmly established.

Another example of a supply-side policy is a cut in the capital gains tax. The argument here is that such cuts, by raising the after-tax return on stocks, will encourage greater savings by households. The consequent fall in real interest rates will stimulate investment by firms, which in turn will lead to increases in the country's capital stock, eventually causing the aggregate supply to rise and economic growth to accelerate. A related argument is that lower income and capital gains tax rates will stimulate entrepreneurial activity, thereby creating new jobs while also expanding personal and aggregate income from the sale of new goods and services.

The empirical evidence on this, too, is mixed. Effecting changes in consumer behavior regarding savings decisions is not an easy task. Cutting capital gains taxes might simply reward those who might have invested in stocks anyway, without attracting any significant new savings. And even if savings and investment rise, the attendant changes in the capital stock and, thus, economic growth will occur after several periods. The growth effects of such tax cuts, then, may be seen as manifesting themselves in the long run; in the short run, the likely effect is reduced tax revenues and larger budget deficits.

The policies associated with supply-side economics rest on the assumption that consumer behavior (and, in some cases, producer behavior) will change in a predictable manner when consumers are presented with certain tax cuts. More precisely, the assumption is that supply-side tax cuts will lead consumers to work more (increase labor supply) and save more (increase capital stock). In each case, however, the presumption may be turn out to be unduly optimistic or, worse, faulty.

The empirical evidence suggests that the effects of tax cuts on labor supply and savings decisions are modest. Thus, these policies are unlikely to deliver significantly faster economic growth and even less likely to produce an increase in revenues that will offset the initial tax reduction. The likely result—larger budget deficits.

Cuts in taxes may also have perverse effects. For instance, a cut in the income tax rate, by leading to an increase in the after-tax earnings, might encourage individuals to work less and save less. Individuals may work less because they might wish to enjoy a greater amount of leisure, which they can now do without sacrificing any income. Similarly, an increase in after-tax earnings may induce consumers to save less in the current period, since they are now in a position to maintain a higher future consumption level without sacrificing current consumption. If these effects prevail, the results of the tax cuts will be contrary to those anticipated in the conventional thinking on supply-side policies.

Supply-side policies also mainly benefit the affluent. The reduction in the highest marginal income tax rates will raise the after-tax compensation of the highest income earners, leaving those at the lower-income strata largely unaffected, thereby exacerbating income inequality in society. Similarly, cuts in capital gains taxes (and estate taxes) will also predominantly leave the wealthy better-off, since they are the ones with large holdings of stocks (and estates). Thus, supply-side policies tend to militate against an equitable distribution of income while constraining public spending on social programs, such as health care and social security.

—Sanjay Paul

See also Economic Growth; Economic Incentives; Flat Tax; Gross Domestic Product (GDP)

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Surplus, Consumer and Producer

In economics, *consumer's surplus* refers to the difference between what a buyer actually pays for a product and the maximum that he would have been willing to pay. If one would have been willing to spend $40 on a shirt, but find it on sale for $10, one would realize a consumer surplus of $30 on the purchase. *Consumers' surplus* is used to refer to the aggregate difference between what consumers would be willing to pay for a given good or service and what they actually do pay (the market price).

Producer's surplus, inversely, is the difference between the price actually received by a seller (or sellers) for a product and the minimum price at which the seller (or sellers) would have been willing to sell. *Producers' surplus* is the equivalent aggregate measure. Thus, consumer's surplus is a demand-side welfare measure, and producer's surplus is a supply-side welfare measure. *Social surplus* is the sum of consumer and producer surplus and is a measure of the total welfare gain from market transactions.

Surplus Under Price Competition

Within any given market, price competition tends to minimize producer surplus and maximize consumer surplus. (The exact nominal value of producer and consumer surplus in any given market depends on the cost and demand structures of that market.) According to economic theory, producers are forced by price competition to sell their products at marginal cost (roughly, the cost to them of producing the last item to be sold). Every consumer—even those who value a product very highly and would be willing to pay much more for it—will be able to buy that product at its marginal cost and, thus, realize substantial consumer surplus. Producers in a competitive market also realize some producer surplus, however. The amount realized will increase to the extent that the producer's average production costs are below the market price.

Price Discrimination and Surplus

Price discrimination is the sale of identical goods to different buyers at different prices. Price discrimination on the part of sellers can shift social surplus from consumers to producers. A seller who can price-discriminate perfectly will charge each of his buyers exactly the highest price that that buyer is willing to pay. Such a seller will sell the same amount of goods as would be sold in a competitive market, but no buyer will realize any consumer surplus, and the seller will realize the maximum possible producer surplus. Perfect price discrimination, in other words, gives all the social surplus to the producers.

Perfect price discrimination is difficult to achieve, since it involves knowing each individual customer's willingness to pay. It is also difficult to maintain: It is undercut by price competition and, even where there is little competition, by arbitrage among customers. But even imperfect price discrimination transfers some social surplus from consumers to producers. This is why retailers commonly use various tactics (e.g., airline "Saturday overnight stay" rates that create differential prices for business and nonbusiness flyers) to charge their different customers prices closer to their maximum willingness to pay.

Monopoly and Surplus

A perfectly price-discriminating monopolist would, in theory, be able to sell the same number of goods as would be sold in a price-competitive market, while keeping all the social surplus on the producer's side rather than on the consumer's side. In practice, however, because price discrimination is difficult to achieve and maintain, monopolists have to set a single price for all their customers. In these circumstances, monopolists famously maximize their profits by producing fewer goods, but charging more for each. This strategy ends up splitting the social surplus. Some—more than in a competitive market—is kept by the monopolist as producer surplus. Some—less than in a competitive market—is kept as consumer surplus by those buyers who value the monopolist's product most highly. Importantly, however, the total amount of social surplus produced in this situation is less than would be produced either in a regime of perfect price competition or in a regime of perfect price discrimination. Social surplus is reduced because the monopolist's uniform high price displaces some transactions entirely. Some potential consumers are simply priced out of the market, so some goods are never sold—and no surplus is ever realized on those absent sales. (The economic loss due to these absent transactions is what economists term *deadweight loss*.)

The same thing occurs when groups of sellers band together in an attempt to transfer social surplus to themselves from their consumers. Cartels, price-fixing agreements, geographic market division, and other illegal competition-limiting techniques have the effect of making the allied sellers behave like a single monopolist. The upshot, again, is increased prices and decreased production, a transfer of social surplus from consumers to producers, and a reduction in total social surplus.

Antitrust and competition laws generally aim to prevent this kind of reduction in social surplus from the level that would be realized by competitive markets. An important secondary goal of antitrust and competition laws is the transfer of as much social surplus as possible from producers to consumers. The latter goal is not pursued everywhere: Retail price discrimination, for example, shifts surplus away from consumers and toward producers, but is not illegal under American antitrust laws. Several factors may explain this, including the difficulty of policing price discrimination schemes (which makes enforcement challenging) and the historical inability of sellers to price-discriminate effectively (which makes enforcement relatively unimportant).

Marketing and Consumer Surplus

A number of advertising schemes make use of the notion of consumer surplus, though not by that name. Marketers on televised infomercials, for example, regularly ask viewers how much they would be willing to pay for a given product, before actually displaying its price. The (hoped for!) contrast between what the consumer would be willing to pay and the actual price eventually displayed is designed to impress the viewer with the amount of consumer surplus he stands to realize by purchasing the product. A similar tactic involves displaying the presale price of an item next to its new, on-sale price; here, the old price is meant to represent what consumers have historically been willing to pay for the product, and the contrast between the nonsale and sale prices is an indication precisely of consumer surplus (assuming, of course, that both prices are honestly displayed).

—Stephen R. Latham

See also Antitrust Laws; Cartels; Competition; Cost-Benefit Analysis; Deadweight Loss; Externalities; Marginal Utility; Monopolies, Duopolies, and Oligopolies; Price Discrimination; Price-Fixing

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Sustainability

Sustainability is an evolving concept that expresses holistic thinking integrating society, economy, and ecology. This concept has been advanced to guide actions within present society to ensure continued existence and prosperity into the foreseeable future. Therefore, *sustainability* can be defined as an integrated understanding of the interconnectedness of human activity with all related man-made and naturally occurring systems. The goal of sustainability is often conflated with the approach needed to attain the goal—*sustainable development.* Understanding these two terms is an essential first step for addressing a set of global challenges embodied by sustainability. To that end, the Brundtland Commission, created through the United Nations, published a report in 1987 in which *sustainable development* is defined as seeking to meet the needs and aspirations of present society without compromising the ability to meet those of future generations.

Because of profound changes to our shared ecological systems, the question of sustainability is being considered around the world. From advancing ozone depletion, which leads to progressively higher levels of life-damaging radiation, to accelerating greenhouse gas emissions, which contribute to complex climate change, to habitat destruction, which results in decreased biodiversity, shared ecosystem resources are being depleted or damaged. Among the consequence of ecosystem damage and loss are that it can threaten and create social unrest in the future, while at the same time drive numerous species toward extinction. Abject poverty that attends the growing gaps between the rich and the poor is a proven driver of environmental degradation and fuels resource, trade, and policy disputes. This type of economic unrest has provided a source of motivation to address sustainability issues not only in organizations such as the United Nations but also at the World Bank and the World Trade Organization.

As our society wrestles with the meaning and actions implied by sustainability, it is helpful to consider that more than 400 years ago the Haudenosaunee (also known as the Iroquois) had their "Great Law," which, in part, requires that leaders consider the impact of their decisions on the seventh generation following that decision. There are other such examples of statements regarding sustainability from the past that very clearly define our collective responsibility to protect and plan for the future. Understanding the recurrence of this theme in human society helps us to understand the centrality of sustainability. It is also instructive to note that thinking about sustainability is not the same as achieving a sustainable outcome. Many civilizations have risen only to prove unsustainable, the Haudenosaunee being among them. What is very different today is the accumulating metrics and resulting data that confirm the impact of human activity on global ecosystem services, such as water cycles, carbon cycles, and resource renewal cycles to name a few. Climate scientists are in general agreement that global warming is real, and it is the product of human activity. The main questions now are as follows: How bad will the consequences be? How fast will they manifest? What can be done to mitigate some of the damage already done?

Sustainability explores how we collectively and individually move into the future while learning to understand how global ecosystem services underpin the social and economic activity on the planet. Business organizations are human society's most efficient resource concentrators, transformers, and distributors; thus, they create what might be called a "corporate ecology" and, therefore, business-oriented solutions central to any working and attainable definition of sustainability.

A few business organizations have viewed increased emphasis on sustainability as an opportunity. If environmental and social costs are included as additional performance metrics, then those firms that comply early and set new standards may be able to create a basis for competitive advantage. For instance, when the California Environmental Protection Agency found that two-stroke engines (the type often used in lawn mowers and gas-powered gardening equipment) were causing a large amount of air pollution, it began to demand more stringent emissions standards for these machines. At first, these new standards were opposed by industry, but a few innovators not only were able to meet the new standards but exceeded them and used 33% less fuel with their more efficient motors. In this case, a sustainability effort, once embraced by these companies, provided the compliant companies with a competitive advantage and achieved a social and environmental objective simultaneously. Sustainability, when pursued by businesses with creativity and purpose, can achieve financial, social, and environmental objectives in an integrated and positively reinforcing manner.

The concept of sustainability is not without its detractors. Some notable scholars, such as Julian Simon, feel that the combined mental power of more people will solve whatever environmental or social problems further human activity produces. The Cato Institute in 2002 concluded that sustainable development is a dubious solution in search of a problem or that it is simply a restatement of a commonsense position of taking care of one's own productive resources that is already well addressed by the current free market policy. It has also been argued that the cost of taking action to comply with sustainability initiatives such as the Kyoto Treaty on Climate Change would cost the U.S. economy a disproportionate amount. These arguments were central to the Bush administration's refusal to become a signatory nation to that agreement on "greenhouse gas" reduction. Some climate scientists and ecologists argue that greenhouse gas damage to ecosystems services may be irreversible and this damage has real costs now that will grow in the future. A concept as complex and far-reaching as sustainability will always present business and society with very conflicted and ambiguous trade-offs.

Because business organizations are uniquely transformative institutions in modern society, how business approaches the concept of sustainability is of primary importance. This central role of business in modern society is also discussed in such topics as corporate social responsibility, corporate citizenship, and corporate ecology. A number of management efficiency approaches have been suggested for business organizations that could make important contributions to our societal goal of sustainability. Some of these include ISO14000, triple-bottom-line accounting, the balanced scorecard approach to strategic management, natural capitalism, the natural step, industrial ecology, Zero Emissions Research Initiative (ZERI), ecological foot printing, and ecoeffectiveness (cradle-to-cradle model). In the following sections, these approaches will be discussed briefly.

ISO14000

ISO stands for the International Standards Organization. It is a nongovernmental organization that has grown out of the General Agreement on Tariffs and Trade. As the World Trade Organization pursues agreements on global trade, quality standards have become increasingly important. One of the outcomes of the 1992 Rio Summit on the Environment was the creation of ISO14000 to create a comprehensive set of standards designed to address the most pressing environmental issues for organizations in a global market. As it currently stands, these standards are voluntary for organizations to abide by. However, the ISO14000 is building on up-to-date environmental health and safety standards. These are important standards and make significant contributions to our understanding of sustainability. However, the ISO does not make specific mention of sustainability and states as its primary focus the application of best practices that are geared toward helping organizations come into compliance with globally accepted standards on environmental health and safety. Depending on the application, the ISO approach to standardized reporting and efficiency measures can lead a company to improvements or to follow an industry to the lowest common denominator of acceptable practice.

Triple-Bottom-Line Accounting

This term and approach originated with the publication of John Elkington's 1998 book *Cannibals with Forks: Triple Bottom Line of 21st Century Business.* In it, Elkington argues that accounting practice should be expanded to include environmental and social costs as well as financial costs. Some scholars argue that corporate social responsibility, or corporate social performance, must measure the social, environmental, and economic performance of the corporation for a firm to be consistent in its approach to these commitments to good practice. There are obvious problems associated with assessing the costs to society for various corporate actions. According to Elkington, the price of a product should include the cost of the ecological services consumed in the production of the product and embodied in the use and disposal of the product. Great strides in ecological economics and research in social capital have helped create metrics to fill in these gaps. The triple-bottom-line approach would have a substantial impact on how organizations operate and may advance our understanding of sustainability. But there are many scholars and practitioners who oppose this type of approach, arguing that it confuses the division of labor and would make firms inefficient and uncompetitive.

Balanced Scorecard

This systematic approach to enterprise management was developed in the early 1990s, by Robert Kaplan and David Norton, as a way to remove some of the vagueness out of strategic management. This approach was not developed specifically as a tool to achieve sustainability, but it has promise as such. Like the triple bottom line, the balanced scorecard approach requires that management look beyond financial measurement; it incorporates a more holistic systems perspective into organizational management. This system uses what has been referred to as a double-loop feedback: One loop is business process focused, and one loop is strategic outcome focused. Both loops are intended to use measurements to provide managers with data on which decision making is based. The application for sustainability comes from the reliance on internal and external data collection and an inherent acceptance of a systems approach.

Natural Capitalism

In 1999, Paul Hawkins, Amory Lovins, and L. Hunter Lovins published a book proposing the redesign of industry based on biological models. They argue that the living systems of the earth are in decline and that the next industrial revolution will be driven by corporations. Natural capitalism is built around the idea that business opportunities become more abundant as entrepreneurs recognize environmental resource limitations. Those that can do more with less will prosper. The advocates of natural capitalism propose four interlinked principles to unlock and ultimately restore natural capital: (1) radically increase resource productivity; (2) adopt closed-loop systems and zero waste in industry; (3) sell services in place of selling products; and (4) recognize that natural capital is the source of future prosperity, thus that businesses will be incentivized to invest in its maintenance. This approach is not only an explicit plan for the concept of sustainability but also a vision of what sustainable business practice might look like.

The Natural Step

This approach is the outcome of a series of studies initiated by Karl-Henrik Rob, who established principles for sustainable society based on thermodynamics and natural cycles. Since 1989, the Natural Step Foundation has been refining and promoting its four-phase program. These phases are (1) aligning key decision makers and stakeholders around a common understanding of what it takes to be a sustainable society, (2) creating baseline data that detail the resources necessary for an organization to be sustainable, (3) creating a vision-driven strategic plan based on the data gathered through the study of the organizational system, and (4) recognizing that success depends on step-by-step implementation and continued support. While this approach is comprehensive and holistic, an organization's implementation of this approach seems dependent on the Natural Step Foundation and may be self-limiting because of restrictive access. Here again, as in natural capitalism, the emphasis and essence of the approach to sustainability is on systems thinking, confronting natural resource and cycles dependence, and creating strategies to support the health and continuation of these processes.

Industrial Ecology

The idea of industrial ecology, which has grown rapidly over the past decade, originated in a 1989 publication by Robert Frosch, and a book by this title was published by Graedel and Allenby in 1994. Very simply, industrial ecology is the idea that an industrial system should function like an ecosystem. There is no waste product in nature; the end of one process is the beginning of another. Some scholars have defined industrial ecology as the science of sustainability. Yet others would argue that this overreliance on science is the weakness of industrial ecology. It has been said that the answer to the question of sustainability will not be engineered; society must come to an understanding of the interdependence of natural systems and their limitations. These writers advocate caution regarding industrial ecology and suggest that technological fixes help human populations extend their overconsumption of resources, whether they are renewable or fixed in quantity. However, all would agree that industrial ecology will be at least part of the solution, because it provides the engineering solutions that can teach us to do much more with less consumption and helps eliminate waste and pollution.

Zero Emissions Research Initiative

ZERI is a concept and a network started by Pauli and deSouza at the United Nations University in Japan. The ZERI network has more than 50 projects worldwide that are applying the ZERI sustainability ideas regarding biodiversity, waste elimination, creativity, and efficient design. ZERI is similar to the Natural Step in that it employs systems thinking to address business, production, and consumption problems. ZERI seeks to create a global network of participants to create alternative organizations that produce goods and services in ways that alleviate poverty and reduce environmental degradation. ZERI is another holistic, systems-based approach to sustainability—one that seeks to model human organizations based on our understanding of naturally occurring systems.

Ecological Footprint

Ecological Footprint is a tool created in 1993 by Mathis Wackernagel and William Rees to help quantify human demand on natural systems relative to the planet's ability to meet those demands. By showing that these demands are consistently in excess of the planet's ability to sustainably provide for these demands, the Global Footprint Network seeks to get business, government, and communities to adopt more sustainable behaviors. Unlike most of the other approaches presented here, the footprint concept is a tool that helps individuals and organizations get a sense of what their actions cost in terms of ecological services. This is an important place to start when considering the meaning and application of sustainability. Our current global ecological footprint overshoots ecosystem capacity by almost 20%, which can be absorbed for a time but not without damage and not indefinitely. Tools such as ecological foot printing are important for people to map our current trajectory and to be able to measure change when action is taken.

Eco-Effectiveness (Cradle-to-Cradle Model)

This is a management consulting and sustainability model that is similar to the approach of natural capitalism. It was developed by Michael Braungart and William McDonough in 1995. The idea of eco-effectiveness is not simply doing more with less but designing products and services in ways that are systemically appropriate. Such products and services are designed to produce no waste and to support rather than disrupt natural systems. By studying the industry as a natural system, this concept seeks to design business processes that mimic metabolic systems both biological and mechanical. Like natural capitalism, this approach envisions the next industrial revolution as one where the end of a product use cycle is the beginning of the next nutrient cycle—where waste equals food and ecological intelligence drives profitability and competitive advantage.

As this brief survey of approaches for addressing sustainability illustrates, many scholars and practitioners have expressed urgency and insight about the global need for sustainability. A successful approach to sustainability will not be engineered. Simply building better, more efficient products will not on its own yield a sustainable future. Along with the efficient use of resources, sustainability requires some fundamental changes in how organizations work on all levels, from the individual action to international coordination. These are not insignificant changes. This fact alone captures the profound difficulty in even defining sustainability—sustainability will have different meanings depending on the level of analysis; ultimately they must all contain the understanding that a sustainable world cannot support irresponsible and inequitable resource use.

—David H. Saiia

See also Biodiversity; Consumerism; Corporate Citizenship; Corporate Ecology; Corporate Social Responsibility (CSR) and Corporate Social Performance (CSP); Deep Ecology; Invisible Hand; Natural Assets (Nonuse Values); Natural Capital; Productive Efficiency; Recycling; Resource Allocation; Social Efficiency; Transparency, Market

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SWEATSHOPS

By common agreement, a sweatshop is a workplace that provides low or subsistence wages under harsh working conditions, such as long hours, unhealthy conditions, and/or an oppressive environment. Some observers see these work environments as essentially acceptable if the laborers freely contract to work in such conditions. For others, to call a workplace a sweatshop implies that the working conditions are illegitimate and immoral. The U.S. General Accounting Office would hone this definition for U.S. workplaces to include those environments where an employer violates more than one federal or state labor, industrial homework, occupational safety and health, workers' compensation, or industry registration laws. The AFL-CIO Union of Needletrades, Industrial and Textile Employees would expand on that to include workplaces with systematic violations of global fundamental workers' rights. The Interfaith Center on Corporate Responsibility (ICCR) defines sweatshops much more broadly than either of these; even where a factory is clean, well organized, and harassment free, the ICCR considers it a sweatshop if its workers are not paid a sustainable living wage. The purpose of reviewing these varied definitions is to acknowledge that, by definition, sweatshops are defined as oppressive, unethical, and patently unfair to workers.

Sweatshops exist in all countries, including the United States, and have a lengthy history. One finds sweatshops in certain countries where there are no laws protecting workers from oppressive working conditions, as well as in those countries where the conditions allowed by the local laws remain substandard according to international laws. However, if by definition sweatshops involve the violation of laws, then no *legal* sweatshops can exist in those jurisdictions where there are significant worker protection laws. In fact, a 1994 U.S. Department of Labor spot check of garment operations in California found that 93% had health and safety violations, 73% of the garment makers had improper payroll records, 68% did not pay appropriate overtime wages, and 51% paid less than the minimum wage. For example, in 1995, labor officials in California uncovered a garment operation where more than 80 Thai workers were laboring behind razor wires and under armed guards making less than $2 per hour. In 1996, Labor Department officials found minimum wage violations in 43% of the firms sampled and overtime violations in 55% of the firms. Inspections of U.S. garment factories in 1999 continued to find wage and hours law violations at 61% of the factories in Los Angeles and 63% of the factories in New York.

However, strict labor laws, effective labor unions, and the growth of employee mobility and opportunity have attempted to eliminate sweatshops in developed countries. The vast majority of sweatshops currently are found in economically underdeveloped countries, especially those with large pools of unskilled labor, high unemployment, and few regulatory constraints. In an unregulated environment, the more broad definitions apply to include workplaces where the owner is not violating any local laws but instead is perhaps violating international standards of human rights, such as provisions found in the United Nations Declaration of Human Rights. But in those developing countries, the incentives and circumstances arguably leave employers with few options. To attract purchasers for their goods, suppliers must keep labor costs low and, therefore, pay workers on a "piece rate" basis rather than hourly, where workers' wages are based on the number of items they produce during a particular time period. Consequently, the longer and harder an employee works, the more he or she will be paid. In some circumstances, since the piece rate is so low, workers have no choice but to contribute extraordinary hours to merely survive, hence the ICCR's emphasis on subsistence wages as the primary element of a modern-day sweatshop.

Why do sweatshops exist, if their mistreatment of workers is so unquestionable and where countries in the developed world have put into place significant worker protections? In fact, there remain persuasive reasons why we have them in our global economy and even why we should permit them. Though some are present simply because there are those in human society who will abuse their power at the expense of those without power, there are far more that exist because they play a role in the economic cycle of development. There are two fields of thought in connection with their continued existence.

First, free market economists suggest that sweatshops represent the cheapest and most efficient means for developing countries to expand export activities and to improve their economies, benefiting stakeholders, including the employees subject to the challenging conditions. In fact, they would argue that the *only* path to economic development for these poorer countries may lie in their ability to compete effectively—perhaps exclusively—on a world scale. This economic growth brings more jobs, which will cause the labor market to tighten, which in turn will force companies to improve conditions to attract workers. In fact, several commentators argue that encouraging greater global production will create additional opportunities for expansion domestically, providing a positive impact on more stakeholders. Moreover, if the suppliers raise wages to at least subsistence levels, they will need to raise their prices to the contracting retailers, who will then arguably seek lower prices elsewhere—and find them, otherwise known as the "race to the bottom." Though an unpopular sentiment with the general consuming public, and often characterized by the polarizing and volatile name "prosweatshops," many economists argue that the maintenance of sweatshop conditions is therefore supported by economic theory.

The second field of thought with regard to the continuation of these conditions is based on the contention that the current situation is perceived as "bad" only when considered through the perspective of those in developed economies. Where individual workers are faced with the choice of no job or a job that pays a subsistence wage, the workers will opt for the job. Similarly, when parents are faced with wages that do not allow them to feed, clothe, or house their entire family, they do not consider child labor to be unethical. Instead, it is often the only means by which the family can reap sufficient income with which to feed that child. Accordingly, if regulations or other strictures are imposed that demand conditions similar to those in developed countries, the multinationals will have no incentive to house their operations or to seek suppliers in developing countries, and will accordingly remain in their home countries, depriving the workers in the developing countries these positions.

Similarly, along this line of thinking, some philosophers assert that, as long as the worker has freely chosen the position, it is ethnocentric, paternalistic, and imperialistic to then impose alternative values. No one is forcing the worker to work under these conditions; therefore, the conditions should be permitted. If no worker would accept these conditions, the employer would be forced to ameliorate them.

On the other hand, labor advocates state that this argument contains a fallacy of choice. A worker forced to choose between accepting a position under substandard conditions to feed his family or declining the position and watching his family starve does not have true freedom of choice. They contend that it is precisely the imposition of Western expectations of free choice and the empowered worker that create a false analysis of the circumstances under which these workers accept the positions. While those in developed economies might be able to envision declining a job if the position described is unsuitable, in those environments where unemployment is exceptionally high and no public system of welfare or education exists, workers may not perceive that they have that option. The learned helplessness, whether actual or perceived, prevents the workers from impacting their environments to proceed down the route described by the economists.

Moreover, the traditional concept of free trade fails to provide social clauses for the protection of workers serving that trade environment and should therefore be curtailed. While free trade agreements encourage multinational companies to do business with developing economies, thereby increasing the gross national product of those economies, it is argued that these agreements are at the expense of (or "on the backs of") the workforces involved. In addition, these advocates suggest that allowing this economic process to take its course may not necessarily lead to the result articulated by the free market economists and, similarly, voluntarily improving legal compliance, wages, and working conditions will not inevitably lead to the negative consequences the free market advocates threaten.

There are innumerable examples of questionable sweatshop labor practices. Included below are discussions of four major areas of concern—child labor, wage rates and work hours, worker health and safety, and worker constraints and treatment—to provide a taste of the nature of sweatshop problems. To avoid confusion throughout the above debate and to raise the discussion above mere terminological discussions, it therefore remains critical to develop a deeper understanding of the meaning of the term *sweatshop* and the conditions to which it refers, even if the resulting definition remains a stipulative one.

Basic Human Rights

Any exploration of sweatshops would be incomplete without a discussion of the basic human rights that ethicists contend to be inalienable, though the determination of which rights would so qualify is far from resolved. To effectively consider the definitions mentioned above, it is important to stipulate the standards to which one should hold a multinational and its product or service supply chain. Yet the identification of global fundamental workers' rights is a challenge not only because of the debate that rages with regard to universalism versus relativism but also because of the challenge of determining the degree of protection. For instance, even if there was agreement that employers should pay a living wage to their workers, there is no agreement with regard to the determination of how to determine what that wage should be.

One scholarly analysis reviewed a variety of global labor standards to determine whether in this array of emerging standards there existed any such norms with respect to labor standards. The following basic labor rights were determined to have *relatively* universal acknowledgment in the range of codes and documents reviewed for that study:

- Just and favorable working conditions, including a limit to the number of hours a human should have to work each day and a healthy working environment
- Minimum age and working conditions for child labor
- Nondiscrimination requirements regarding the *relative* amount that a worker should be paid and the right to equal pay for equal work
- Freedom from forced labor
- Free association, including the right to organize and to bargain collectively in contract negotiations

Thus, there is an argument that, at least in theory, there is some agreement about what rights *ought* to be respected. On the other hand, however, as mentioned above, there remains broad disagreement with regard to the parameters of fundamental human rights and this study suggests but one option for their identification. A cursory review of conditions around the world reveals that, though perhaps accepted by some as basic human rights, these standards are not necessarily respected as such.

Child Labor

As discussed briefly, there may be persuasive reasons why parents might encourage their children to work. However, in developing countries, children may begin work at ages as young as 3 years and often in unhealthy conditions. The labor that exists almost always precludes children from obtaining an education, as children often work on a full-time basis. In extreme cases, children are forced into slavery, often in the guise of indentured servitude or apprenticeship training. When referring to the nature of children's work, the International Labour Organization (ILO) Bureau of Statistics reports that most children working as paid employees are paid much less than the prevailing rates in their localities, even when compared with the legal minimum wages—receiving only one sixth of the minimum rate in one survey finding; also the younger the working child, the lower the wage payment.

On average, girls work longer hours than boys but are paid less than their working brothers doing the same type of work, and children are generally not paid for overtime work. The ILO reports that, in the Philippines, more than 60% of working children are exposed to hazardous working conditions and 40% of those exposed experience serious injuries or illnesses including those that result in amputations and loss of body parts. Because work takes children out of school, more than half of the child labor force will never be literate. And because of substandard working conditions, child employees will grow less than those who didn't work as children and the child workers' bodies will be smaller, even into adulthood. By the time child laborers reach adulthood, most will irrevocably be sick or deformed; the children are unlikely to live to be 50 years old.

As horrendous as these conditions appear, many ask whether there are always better alternatives. Free market economists point out that, in many circumstances, the wages these children earn are what pays for their food each night. If the children are denied jobs in communities where welfare systems are not in place, their very existence may be threatened. Often suppliers respond to multinational corporations' concerns by summarily and immediately terminating young workers, even when the local law would allow their employment. The impact of this dismissal on the children's survival may be devastating. In addition, if children are not permitted to work in mainstream ventures, they are often forced into the underground professions involving drugs and prostitution to help support themselves and their families. Until such time as welfare systems become prevalent throughout the developing countries, the answer to the question of children in the workplace is not an obvious one.

Wages and Hours

Sweatshop employees are often paid very low wages and are required to work very long hours, sometimes with no provision for overtime. Alternatively, if they refuse to work overtime in some circumstances, they may lose the pay already earned. The piece rate production quotas are often so high that workers are unable to leave the work floor to eat or use the restroom for fear of falling below quota, which often results in a loss of pay for those pieces submitted. The wage levels are far below the wages paid for similar types of employment in developed countries, even after restating wages in terms of country-specific purchasing power. An example of very low wages comes from a study of Honduran labor. In Honduras, workers earn only an average of $24.27 per week. However, basic necessities for a Honduran family cost $22.75 per week, which leaves an average family's wage earner with only $2.05 for transportation, school expenses, clothing, and other items. According to the National Labor Committee, El Salvadoran workers producing NBA jerseys make fewer than three jerseys per hour at $0.24 per jersey, which then sell for $140 in the United States. This $0.60 per hour is only about one third of the Salvadoran cost of living.

Under some extraordinary circumstances, workers are expected to pay for the opportunity to work; at some factories, workers must pay work deposits and monthly tool deposits. Recovery of deposits generally depends on how long workers stayed at the factory. In one factory, workers lost their deposits if they did not stay at the factory for at least 2 years. Similar conditions have existed in Saipan, where workers were forced to pay a recruitment fee of $2,000 to $7,000 before they could begin working.

Frequently, minimum wage and maximum work hours laws have been enacted but have not been effectively enforced. In China, workers at one factory reported that they regularly work 16-hour days, 7 days a week during peak production times, despite Chinese labor laws that establish a maximum 49-hour workweek.

Health and Safety

Working conditions in sweatshops may seriously threaten worker health and safety. The ILO and the World Health Organization have concluded that the shift of industrial production to developing countries will *increase* the global occurrence of occupational disease and injury. In El Salvador, for example, workers at one factory had to endure intense heat, poor ventilation, contaminated drinking water, and a limit on bathroom breaks of one per day. As punishment for breaking rules, workers were forced to stand in direct sunlight. Children who work often encounter some of the worst health and safety conditions. Workers in sweatshops are often missing key pieces of safety equipment such as face masks to ensure safe breathing or work in environments with insufficient means of emergency exit since employers may lock the doors and windows to prevent theft during working hours.

Sweatshop employers frequently impose and brutally enforce rigid constraints on their workers. Neil Kearney, the general secretary of the International Textile, Garment and Leather Workers' Federation, explains that in the garment industry workplace management by terror is standard practice. Workers are routinely verbally abused, shoved, beaten, and kicked, even when pregnant. Kearney claims that attempts to unionize are met with the utmost brutality, sometimes with murder. Although illegal, Mexican *maquiladora* factory (operations that assemble imported materials for export) operators require women to take pregnancy tests or prove they are menstruating as a condition of employment, and women thought to be pregnant are not hired. In El Salvador, women who work in manufacturing industries have been required to take company-provided birth control pills daily in the presence of their supervisors.

Finally, forced labor continues to exist in certain countries. A 2005 study from the ILO reports that at least 12.3 million workers are trapped in situations involving forced labor around the world. Forced economic exploitation occurs in sectors such as agriculture, construction, brick making, and informal apparel and footwear manufacturing and does not seem to discriminate between men and women as does much of traditional apparel and footwear manufacturing, where one finds significantly more women and children involved than men. Forced labor also includes forced commercial sexual exploitation, which involves almost entirely women and girls. In addition, children younger than 18 years make up 40% to 50% of all forced laborers.

International Nongovernmental Response

International nongovernmental organizations (NGOs) have attempted to step into this fray to suggest voluntary standards to which possible signatory countries or organizations could commit. For instance, the International Labour Office has promulgated its Tripartite Declaration of Principles Concerning Multinational Enterprises and Social Policy, which offers guidelines for employment, training, conditions of work and life, and industrial relations. The "Tripartite" nature refers to the critical cooperation necessary from governments, employers' and workers' organizations, and the multinational enterprises involved. These guidelines are not legally binding yet one can see the very clear need for such a document from the introduction to the Declaration, which explains the following:

- Multinational enterprises play an important part in the economies of most countries and in international economic relations. This is of increasing interest to governments as well as to employers and workers and their respective organizations. Through international direct investment and other means, such enterprises can bring substantial benefits to home and host countries by contributing to the more efficient utilization of capital, technology, and labor. Within the framework of development policies established by governments, they can also make an important contribution to the promotion of economic and social welfare; to the improvement of living standards and the satisfaction of basic needs; to the creation of employment opportunities, both directly and indirectly; and to the enjoyment of basic human rights, including freedom of association, throughout the world. On the other hand, the advances made by multinational enterprises in organizing their operations beyond the national framework may lead to abuse of concentrations of economic power and to conflicts with national policy objectives and with the interest of the workers. In addition, the complexity of multinational enterprises and the difficulty of clearly perceiving their diverse structures, operations, and policies sometimes give rise to concern either in the home or in the host countries, or in both.
- The aim of this Tripartite Declaration of Principles is to encourage the positive contribution that multinational enterprises can make to economic and social progress and to minimize and resolve the difficulties to which their various operations may give rise, taking into account the United Nations resolutions advocating the establishment of a New International Economic Order.
- This aim will be furthered by appropriate laws and policies and measures and actions adopted by the governments and by cooperation among the governments and the employers' and workers' organizations of all countries.
- The principles set out in this Declaration are commended to the governments, the employers' and workers' organizations of home and host countries, and to the multinational enterprises themselves.
- These principles are intended to guide the governments, the employers' and workers' organizations, and the multinational enterprises in taking such measures and actions and adopting such social policies, including those based on the principles laid down in the Constitution and the relevant Conventions and Recommendations of the ILO, as would further social progress.
- To serve its purpose, this Declaration does not require a precise legal definition of multinational enterprises;

this paragraph is designed to facilitate the understanding of the Declaration and not to provide such a definition. Multinational enterprises include enterprises, whether they are of public, mixed, or private ownership, which own or control production, distribution, services, or other facilities outside the country in which they are based. The degree of autonomy of entities within multinational enterprises in relation to each other varies widely from one such enterprise to another, depending on the nature of the links between such entities and their fields of activity and having regard to the great diversity in the form of ownership, in the size, and in the nature and location of the operations of the enterprises concerned. Unless otherwise specified, the term *multinational enterprise* is used in this Declaration to designate the various entities (parent companies or local entities or both or the organization as a whole) according to the distribution of responsibilities among them, in the expectation that they will cooperate and provide assistance to one another as necessary to facilitate observance of the principles laid down in the Declaration.

- This Declaration sets out principles in the fields of employment, training, conditions of work and life, and industrial relations that governments, employers' and workers' organizations, and multinational enterprises are recommended to observe on a voluntary basis; its provisions shall not limit or otherwise affect obligations arising out of the ratification of any ILO Convention.

The UN Declaration of Human Rights

On December 10, 1948, the General Assembly of the United Nations adopted its Universal Declaration of Human Rights, calling on all member countries to publicize the text of the Declaration and to cause it to be disseminated, displayed, and read. The Declaration recognizes that all humans have an inherent dignity and specific equal and inalienable rights. These rights are based on the foundation of freedom, justice, and peace. The UN stated that the rights should be guaranteed without distinction of any kind, such as race, color, sex, language, religion, political or other opinion, national or social origin, property, birth, or other status. Furthermore, no distinction shall be made on the basis of the political, jurisdictional, or international status of the country or territory to which a person belongs. The foundational rights also include the right to life, liberty, and security of person and protection from slavery or servitude, torture, or cruel, inhuman, or degrading treatment or punishment.

Articles 23, 24, and 25 discuss issues with immediate implications for sweatshops. By extrapolation, they provide recognition of the fundamental human right to nondiscrimination, personal autonomy or liberty, equal pay, reasonable working hours and the ability to attain an appropriate standard of living, and other humane working conditions. All these rights were reinforced by the United Nations in its 1966 International Covenant on Economic, Social, and Cultural Rights.

Next Steps

These are but two examples of standards promulgated by the international labor community, though the enforcement of these and other norms is spotty. In the apparel industry in particular, the process of internal and external monitoring has matured such that it has become the norm at least to self-monitor, if not to allow external third-party monitors to assess compliance of a supplier factory with the code of conduct of a multinational corporation or with that of NGOs. Though a number of factors affected this evolution, one such factor involved pressure by American universities on their apparel suppliers, which resulted in two multistakeholder efforts—the Fair Labor Association, primarily comprising and funded by the multinational retailers, and the Worker Rights Consortium, originally perceived as university driven. Through a cooperative effort of these two organizations, large retailers such as Nike and Adidas have not only allowed external monitoring but Nike has now published a complete list of each of its suppliers.

As discussed above, a common response to the criticisms of these types of labor practices is to note that, no matter how well-meaning and accurate the criticisms, there is simply no viable alternative for people in many developing nation labor markets. Free market or neoclassical economists contend stridently that this is not necessarily the case. They concur that attempts to redress sweatshop conditions must take into account the pressures of globalization and the poor economic conditions of developing nations. But as long as significant global disparities in wages and working conditions exist among nations, labor practices that are unacceptable in one nation may be used in other nations to secure contracts with multinational corporations (the race to the bottom). Second, in the current global regulatory environment, nations are not permitted to impose import bans on sweatshop-based goods since the World Trade Organization's (WTO) current interpretation of its rules declares such practices protectionist.

Multinational corporations such as those discussed above seek to avoid these negative outcomes by embracing the positive consequences to a proactive response to questions regarding global labor practices. Employees who are treated with respect tend to be more loyal and productive workers; consumers in industrialized countries increasingly prefer to purchase goods and services from companies that treat workers with respect; and potential employees increasingly care about the ethical reputations of the companies with whom they take a job, raising the cost of low-reputation companies to hire high-quality employees. These forward-thinking organizations can be categorized as exhibiting "positive deviancy" with respect to their labor practices.

Nike and Adidas represent several examples of positive ethical deviancy among firms that have been subject to previous criticism by the media or NGOs for their treatment of workers. In actuality, intense media scrutiny often forces firms to be creative in their responses to common globalization challenges. For example, after years of sustained criticism of supplier labor practices by NGOs, Nike CEO Philip Knight accepted responsibility in 1998 at the corporate level for the poor treatment of workers by Nike suppliers. Knight explained that, as of the day of his pronouncement, Nike was committed to increasing minimum age requirements for workers in factories, improving factory health and safety conditions so that they comply with U.S. standards, expanding worker education programs, increasing support for microenterprise loan programs, and involving NGOs in the factory monitoring process.

Though these and other multinational corporations—including Dow Chemical, Chiquita, and Levi Strauss & Co.—are often viewed as positive deviants from the current norms among their peers, their efforts have not only garnered attention but will also serve as models for other organizations with regard to the appropriate treatment of their workers and of those of their suppliers, while remaining sustainable from a long-term perspective. There is no *one* solution to sweatshops and other labor challenges posed by contemporary corporate globalization. However, the programs and initiatives that have successfully been implemented by positive ethical deviants can be used as a basis for other multinational corporations to develop their own economically enhancing and ethical labor programs and initiatives that demonstrate respect for the most basic human rights while remaining profitable.

—Laura P. Hartman

See also Absolutism, Ethical; Alien Tort Claims Act; Child Labor; Developing Countries, Business Ethics in; Economics and Ethics; Fair Labor Association (FLA); Global Codes of Conduct; Globalization; Human Rights; International Labour Organization (ILO); Nike, Inc.; Normative Ethics; Outsourcing; Relativism, Cultural; Reputation Management; Scandals, Corporate; United Nations; Worker Rights Consortium (WRC); World Trade Organization (WTO)

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Moreover, the traditional concept of free trade fails to provide social clauses for the protection of workers serving that trade environment and should therefore be curtailed. While free trade agreements encourage multinational companies to do business with developing economies, thereby increasing the gross national product of those economies, it is argued that these agreements are at the expense of (or "on the backs of") the workforces involved. In addition, these advocates suggest that allowing this economic process to take its course may not necessarily lead to the result articulated by the free market economists and, similarly, voluntarily improving legal compliance, wages, and working conditions will not inevitably lead to the negative consequences the free market advocates threaten.

There are innumerable examples of questionable sweatshop labor practices. Included below are discussions of four major areas of concern—child labor, wage rates and work hours, worker health and safety, and worker constraints and treatment—to provide a taste of the nature of sweatshop problems. To avoid confusion throughout the above debate and to raise the discussion above mere terminological discussions, it therefore remains critical to develop a deeper understanding of the meaning of the term *sweatshop* and the conditions to which it refers, even if the resulting definition remains a stipulative one.

Basic Human Rights

Any exploration of sweatshops would be incomplete without a discussion of the basic human rights that ethicists contend to be inalienable, though the determination of which rights would so qualify is far from resolved. To effectively consider the definitions mentioned above, it is important to stipulate the standards to which one should hold a multinational and its product or service supply chain. Yet the identification of global fundamental workers' rights is a challenge not only because of the debate that rages with regard to universalism versus relativism but also because of the challenge of determining the degree of protection. For instance, even if there was agreement that employers should pay a living wage to their workers, there is no agreement with regard to the determination of how to determine what that wage should be.

One scholarly analysis reviewed a variety of global labor standards to determine whether in this array of emerging standards there existed any such norms with respect to labor standards. The following basic labor rights were determined to have *relatively* universal acknowledgment in the range of codes and documents reviewed for that study:

- Just and favorable working conditions, including a limit to the number of hours a human should have to work each day and a healthy working environment
- Minimum age and working conditions for child labor
- Nondiscrimination requirements regarding the *relative* amount that a worker should be paid and the right to equal pay for equal work
- Freedom from forced labor
- Free association, including the right to organize and to bargain collectively in contract negotiations

Thus, there is an argument that, at least in theory, there is some agreement about what rights *ought* to be respected. On the other hand, however, as mentioned above, there remains broad disagreement with regard to the parameters of fundamental human rights and this study suggests but one option for their identification. A cursory review of conditions around the world reveals that, though perhaps accepted by some as basic human rights, these standards are not necessarily respected as such.

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Next Steps

These are but two examples of standards promulgated by the international labor community, though the enforcement of these and other norms is spotty. In the apparel industry in particular, the process of internal and external monitoring has matured such that it has become the norm at least to self-monitor, if not to allow external third-party monitors to assess compliance of a supplier factory with the code of conduct of a multinational corporation or with that of NGOs. Though a number of factors affected this evolution, one such factor involved pressure by American universities on their apparel suppliers, which resulted in two multistakeholder efforts—the Fair Labor Association, primarily comprising and funded by the multinational retailers, and the Worker Rights Consortium, originally perceived as university driven. Through a cooperative effort of these two organizations, large retailers such as Nike and Adidas have not only allowed external monitoring but Nike has now published a complete list of each of its suppliers.

As discussed above, a common response to the criticisms of these types of labor practices is to note that, no matter how well-meaning and accurate the criticisms, there is simply no viable alternative for people in many developing nation labor markets. Free market or neoclassical economists contend stridently that this is not necessarily the case. They concur that attempts to redress sweatshop conditions must take into account the pressures of globalization and the poor economic conditions of developing nations. But as long as significant global disparities in wages and working conditions exist among nations, labor practices that are unacceptable in one nation may be used in other nations to secure contracts with multinational corporations (the race to the bottom). Second, in the current global regulatory environment, nations are not permitted to impose import bans on sweatshop-based goods since the World Trade Organization's (WTO) current interpretation of its rules declares such practices protectionist.

Multinational corporations such as those discussed above seek to avoid these negative outcomes by embracing the positive consequences to a proactive response to questions regarding global labor practices. Employees who are treated with respect tend to be more loyal and productive workers; consumers in industrialized countries increasingly prefer to purchase goods and services from companies that treat workers with respect; and potential employees increasingly care about the ethical reputations of the companies with whom they take a job, raising the cost of low-reputation companies to hire high-quality employees. These forward-thinking organizations can be categorized as exhibiting "positive deviancy" with respect to their labor practices.

Nike and Adidas represent several examples of positive ethical deviancy among firms that have been subject to previous criticism by the media or NGOs for their treatment of workers. In actuality, intense media scrutiny often forces firms to be creative in their responses to common globalization challenges. For example, after years of sustained criticism of supplier labor practices by NGOs, Nike CEO Philip Knight accepted responsibility in 1998 at the corporate level for the poor treatment of workers by Nike suppliers. Knight explained that, as of the day of his pronouncement, Nike was committed to increasing minimum age requirements for workers in factories, improving factory health and safety conditions so that they comply with U.S. standards, expanding worker education programs, increasing support for microenterprise loan programs, and involving NGOs in the factory monitoring process.

Though these and other multinational corporations—including Dow Chemical, Chiquita, and Levi Strauss & Co.—are often viewed as positive deviants from the current norms among their peers, their efforts have not only garnered attention but will also serve as models for other organizations with regard to the appropriate treatment of their workers and of those of their suppliers, while remaining sustainable from a long-term perspective. There is no *one* solution to sweatshops and other labor challenges posed by contemporary corporate globalization. However, the programs and initiatives that have successfully been implemented by positive ethical deviants can be used as a basis for other multinational corporations to develop their own economically enhancing and ethical labor programs and initiatives that demonstrate respect for the most basic human rights while remaining profitable.

—Laura P. Hartman

See also Absolutism, Ethical; Alien Tort Claims Act; Child Labor; Developing Countries, Business Ethics in; Economics and Ethics; Fair Labor Association (FLA); Global Codes of Conduct; Globalization; Human Rights; International Labour Organization (ILO); Nike, Inc.; Normative Ethics; Outsourcing; Relativism, Cultural; Reputation Management; Scandals, Corporate; United Nations; Worker Rights Consortium (WRC); World Trade Organization (WTO)

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T

Taoist Ethics

Taoism (or Daoism) is one of two major Chinese philosophies of life and stems from the writings of Lao Tzu. Rooted in living a life characterized by balance and harmony, Taoism focuses on the significance of the individual life, spontaneity, and being tranquil. Confucianism, the dominant philosophical system throughout much of Chinese history, focuses on society. It promotes the value of social order, responsibility, and being active. On the surface these two wisdom traditions appear to be contradictory, but in actuality they are complementary. Both have greatly shaped Chinese civilization and its social structure, family traditions, and business culture and practices.

During the latter part of the 20th century, Taoist and Buddhist thought became a popular alternative to Western religious traditions that were seen as rigid and constraining. They provided a personal spiritual approach to life and self-development that was liberating and not rule based. Over time, Taoist thought also influenced business concepts, particularly management, leadership, and mentoring. Some even used it in understanding organizational behavior and business forecasting. With the notion of globalization being the foundation for many 21st-century business strategies and marketing efforts, understanding and respecting Taoism and its ethical principles is important for developing effective working relationships with business professionals in China and other parts of the East.

Background

Lao Tzu, the attributed author of the *Tao Te Ching* and the founder of Taoism, is considered to be a contemporary of Confucius (551–479 BCE). While some say that he was born in 604 BCE, little is known about him. It is uncertain if he was a historical person or merely the preeminent "Grand Old Master," as his name implies. Unlike other major Chinese thinkers such as Confucius and Buddha, Lao Tzu was not a preacher nor an active organizer or promoter of a social or spiritual tradition.

The *Tao Te Ching* (*The Way and Its Power*) is one of the central writings of Taoist philosophy. It is a mere 81 chapters—short poetic sayings and proverbs—reflecting on how people can become one with the Way of the universe (*Tao*) and live a harmonious life. Legend holds that Lao Tzu, a well-respected sage, when leaving to live in Tibet, jotted down a few pages recounting his thoughts on the request of a gatekeeper at the Hanko Pass. These pages became known as the *Tao Te Ching* and have been used by both rulers and common folk. The text in its present form, though, is the work of several individuals.

The other core Taoist writing is *Chuang-tzu,* written by Chuang Chou around 300 BCE. Chuang Chou was a Taoist scholar sought out by the king to be his adviser. He declined, choosing not to serve any specific ruler. He focused on spiritual and social liberty, encouraging people to seek freedom from all forms of tyranny and oppression, even death.

Today, Taoism has three primary forms: philosophical, religious, and programmatic arts to vitalize the human person. Philosophical Taoism is concerned with maximizing *te,* or power, by conserving it, while the programmatic arts seek to expand its quantity. The former promotes thoughtful reflection to preserve power. The latter strives to energize human beings by using herbs and movement (e.g., the practice of *t'ai chi* *chuan*), as well as breathing exercises and yoga to increase or unblock *ch'i,* the essential and vital energy that flows through human beings. Religious or Church Taoism helps individuals deal with life issues, illness, and daily problems by invoking deities and accessing their power by performing various rituals.

Fundamental Taoist Concepts

The following discussion of Taoist principles and ethics focuses on its philosophical form.

Life is not uniform but filled with diversity. Characterized by the symbol of *yin/yang,* the universe is constituted by male and female, light and dark, good and evil, beauty and ugliness, active and passive, and so forth. Opposites are aspects of the whole, the *Tao,* each complementing and balancing the other.

The boundary between opposites is not rigid, for each partially resides in the other. Each component of the opposite is necessary, for, in essence, each is a phase of the continuous cycle of life, one flowing into the other. They are like one season turning into the next.

While the source of life cannot be known, its attributes can be discerned by reflecting on nature, particularly water. The goal of life is to become aligned with the *Tao,* the Way or Path, draw on its animating power (*te*), let actions flow spontaneously, and take pleasure in the *Tao's* graceful flow. An individual's strength and capabilities come from the *Tao.*

The notion of *Tao* is multifaceted and has three core meanings. It can be understood as the way of ultimate reality, the way of the universe, and the way of human life. The first understanding refers to the eternal *Tao,* that is, the ineffable, transcendent source and end of all life. The next meaning pertains to the rhythm and power in nature, the immanent, life-giving principles that structure life itself. The last interpretation refers to human existence when it is grounded in the eternal *Tao* of the universe. All these understandings are interconnected.

Besides the *Tao* and *te,* the other central principle of Taoism is *wu wei,* the stillness and quiet that gives rise to effortless, creative action. In light of *wu wei,* life is a dance characterized by suppleness, simplicity, and freedom. Individuals are relaxed and adaptive, wasting no actions. Human action and work become appropriate and effective through attunement with the *Tao* and inaction, not personal skill, control, and force. Effective actions receive their power from the *Tao's te* flowing through the individual.

Thus, just as water is soft but can move and wear away hard stones, life is paradoxical. The *Tao* and *wu wei* are like water, for they flow, are soft, and have a power to overcome great obstacles.

Taoist Ethics and Values

While Taoism is an overarching philosophy of life, it does not have a delineated set of ethical principles like some Western philosophical systems. One reason is because it does not subscribe to contrived morality, since one of its central tenants is to let go of control. Embedded, though, in its views are particular ethical perspectives and values.

As discussed, central to Taoism is the embracing of the *Tao* and accepting it as the source of personal power. Stillness and suppleness give birth to appropriate and effective action. These concepts are fundamental to the Taoist notion of ethics. From these principles stem ethical values that guide how individuals live and work. Key ones are harmony, balance, selflessness, humility, simplicity, and detachment.

Taoist ethics focuses on being, not doing, on living a life characterized by harmony with the world, not on striving to identify correct decisions and actions. Therefore, decisions are to fit with the natural flow or order of things. Women and men are to perform what is required by the particular situation and nothing more.

To see the universe's rhythm and be in balance requires self-knowledge. Being self-aware enables women and men to let go of personal worth and desires that hinder them in making room for the Tao and others in their lives. Therefore, people are encouraged to be selfless and not to be self-assertive or competitive.

Aggressiveness, position, and possessiveness too often lead to violence, harming both people and nature. In this manner, individuals are to develop lives characterized by simplicity, humility, and detachment. Life's three treasures are mercy or compassion, frugality, and not being first. Lao Tzu holds these virtues as being vital and transformational.

People are to be authentic, unobtrusive, and simple. Life is to be uncluttered and lived in moderation. Worldly position and possessions have no ultimate value. Often they disorient and distract people from their primary purpose and lead to strife, disunity, and oppression.

Taoism, Business Organizations, and Leadership

A Taoist approach to business and organizational operations focuses on balance, diversity, creativity, and the meaningfulness of work. As with all of life, companies are characterized by *yin* and *yang* aspects. Administrators are challenged to be aware of these qualities, developing policies, practices, and work environments that respect each quality and unleash its power. In this manner, the organizational structure and culture, along with the established work values, allow individuals, and the company as a whole, to move with the natural forces of the universe. The company reaches its mission and goals by promoting understanding and harmony instead of creating adversarial relationships and competition.

In such a workplace, the overarching organizational culture stresses operating for the sake of a larger purpose, and creating value for all stakeholders. There is a balance between strategic goals and work meaning, between corporate achievement and work satisfaction, between financial profit and employee well-being. Administrators seek to both lead and manage, aiding organizations to continuously evolve and adapt to the market environment while being consistent with their philosophy and traditions. When issues need to be addressed and problems resolved, the root cause—that is, cultural belief, leadership style, operational practice, corporate policy, and so forth—is identified and altered, as needed.

Taoist thought also holds much wisdom for women and men who are modern business professionals working in a highly competitive environment driven by market share. Many of the *Tao Te Ching's* sayings are specifically directed at leaders.

In Taoism, leaders learn how to guide and manage by first being followers. Through mentoring they learn how to live simply, be flexible, work from creative stillness, and not become caught up in the allurement of success, power, and money.

Being self-aware, reflective people, leaders try to understand and be sensitive to what is occurring at any given time. They trust the process and let things unfold naturally. Unless necessary, they do not intervene. They strive not to be coercive or manipulative, for the less a leader interferes, the more freedom others have and the more responsibility they will take.

Leaders are humble professionals who do not manage by power and authority. Nor do they consider themselves better or more privileged than others. They value all staff members, respecting them as talented people with dignity and recognizing their vital contributions to the organization. Not prizing position and status, leaders do not seek recognition or take credit for organizational accomplishments.

Leaders embrace diversity, seeking to understand and draw on the strengths of polarities instead of trying to get rid of them. They mentor by example rather than by mandates, rapprochements, or punishments. Leaders motivate and empower their employees, enabling them to discover their talents, reach their potential, and be successful. Above all, leaders guard their integrity and do not let anything compromise it.

—Charles F. Piazza

See also Confucianism; Normative Ethics; Virtue Ethics

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Tariffs and Quotas

Tariffs are taxes imposed on foreign-made goods (imports) coming into a country. The tax (also referred to as a duty) raises the price of the good. This has the immediate effect of shielding domestic manufacturers from some of their foreign competitors, and thus tariffs are referred to as protectionism. The tax protects domestic producers (and the labor employed by those domestic firms) from foreign competition by allowing relatively less efficient domestic producers (who must charge a higher price than more efficient firms if they are to recoup their costs) to remain in business. Simultaneously, the product price rises, and the government collects tariff revenues from its domestic consumers, who must pay both the original price of the import and the amount of the tariff. Thus, the winners from tariffs are the government imposing the tariff and the domestic firms and labor whose products receive tariff protection, while the losers are domestic consumers, who pay higher prices for the product and consume less of that product than they would at the free trade price.

While a quota has the same impact as a tariff, it differs in the government action taken. With a quota, the domestic government does not impose a tax on imports but rather restricts the *number* of units of a product that may enter the country from foreign manufacturers. And, as with a tariff, the price of the good increases and the amount of the good supplied by domestic firms increases. However, unlike with a tariff, the government does not collect any revenue.

Tariffs and quotas are examples of a redistributive policy, where the *costs* of the policy are broadly distributed among domestic consumers and foreign competitors, while the *benefits* are concentrated with the protected industries and their labor. Conversely, the economic benefits of free trade are broadly distributed among all consumers and foreign producers, while the costs are concentrated in the noncompetitive domestic firms, making the incentives to fight free trade often stronger than the incentives to fight trade protection.

Political economists recognize beneficial reasons for imposing tariff or quota protections, beyond just job protection. First, many nations protect militarily important industries to ensure that national firms retain the ability to manufacture or innovate products deemed critical to national security; industries such as electronics, computers, aerospace, and even agriculture have been protected using national security rationales. Second, since it is virtually impossible for new entrants in some industries (particularly those with steep learning curves) to compete successfully against established firms from abroad, some countries protect "infant industries" in the hope that sheltering new domestic firms from the full onslaught of competition will enable the domestic companies to become viable long-term global competitors and thus provide the country with important employment and technological benefits. The commercial aircraft (particularly Airbus in the European Union) and semiconductor industries (particularly in Japan) are among the more celebrated examples of infant industry protection. Finally, some countries respond to foreign nations' imposition of tariff or quota protections by retaliating with their own protectionism; this "tit-for-tat" tariff-setting sometimes prompts the first-tariff-imposing nation to lift its tariff.

More recently, the arguments for imposing trade protection have focused not just on broad national benefits that may flow from protection, as in the above examples, but rather on advancing important social goals. Thus, activists have increasingly sought trade restrictions in the past decade to keep domestic firms from exporting manufacturing activities to foreign countries that have fewer or laxer labor and environmental protections (such as allowing child labor or prohibiting unionization). Critics of globalization argue that multinational firms can gain competitive advantage by exploiting national differences in health, labor, and environmental regulations and that this puts pressure on domestic firms and results in a socially destructive "race to the bottom." In short, as is seen in the popular press's coverage of trade policy, the topic of tariffs generates much controversy and disagreement over its winners and losers.

Welfare Effects of Free Trade and Tariff Protection

Microeconomic theory has demonstrated that free trade (the absence of tariffs or quotas) is unambiguously good for consumers and the overall efficient allocation of resources within a country. Free trade makes consumers and a nation better off in two ways. First, consumers are able to purchase more goods due to differences in which nations have a comparative advantage in producing. For example, Central American nations can grow fruits more cheaply than can northern European countries. Thus, if these countries can trade, then the Central American nations will produce more fruit than just what their domestic consumers demand, because they have export markets for the fruit; similarly, northern European countries will have access to far more fruit, and at substantially lower prices, than if fruit was grown only domestically. In this way, free trade enables consumers to purchase more units of a product, at cheaper prices, and often greater varieties of products than if they were restricted to products only sold by domestic firms.

There is also a second benefit from free trade to a country. Firms in a free-trade country will use the resources of that country most efficiently when they produce the goods that the country produces relatively more efficiently than other countries—this is the heart of David Ricardo's theory of comparative advantage. Firms in northern European countries will create more wealth-producing, say, cell phones (as does Nokia) than they would by using the same resources of capital, land, and labor to grow fruit since the growing conditions for fruit are much better in Central America than in northern Europe, while northern Europe has the highly educated labor force necessary to design cell phones. In short, international trade theory concludes that the competition that comes with free trade encourages the most efficient allocation of resources.

Tariff protection has the opposite effect. Domestic consumers and the economy as a whole in a protected country are worse off. This can be seen in Figure 1, which illustrates the various impacts of a tariff. First, under a tariff, the price of the good increases from P to $P + t$, where t is the percentage amount of the tariff. Unsurprisingly, since demand generally drops when the price of a good rises, the amount of the good consumed under the higher tariff price decreases from Y_1 to Y_3. The amount of imports consumed also changes under tariff protection. Under free trade, consumers purchased Y_2 units of the good from domestic producers; these producers had costs that were less than the cost of foreign producers (as can be seen by the fact that the domestic supply curve—which is also the marginal cost curve for the firm—is under the world supply curve). In other words, consumers fill demand from domestic suppliers as long as doing so costs the same or less than buying imports. Consumers purchase from domestic suppliers until the domestic supply curve intersects with the world supply curve (without tariff); at that point, consumers will fulfill the rest of their demand from imports, which are cheaper than the products offered by the higher-cost domestic suppliers, for a total amount of imports from Y_2 to Y_1.

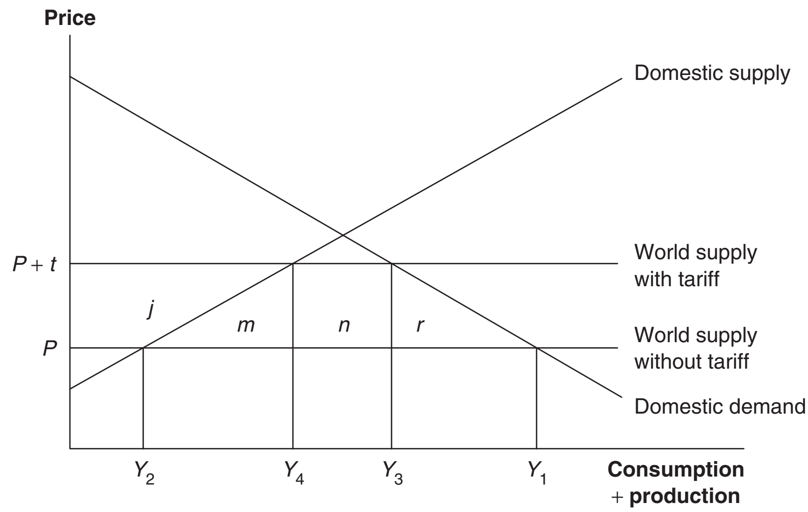

Figure 1 Welfare Effects of a Tariff

When the tariff is imposed, it shelters higher-cost domestic producers from lower-cost import competition by raising the price. Thus, domestic producers supply Y_4 units of the product under tariff protection, or to the point where domestic supply intersects with the world supply (with tariff) curve. At that point, consumers will buy Y_4 to Y_3 units of exports until their demand is fully filled by Y_3 total units. The amount supplied by domestic producers has increased under protection, and the amount supplied by imports has decreased. The total amount consumed has declined from Y_1 to Y_3 because the price of the good has increased by the amount of the tariff.

The effects of a tariff are further characterized by transfers and deadweight losses. There are two transfers associated with a tariff or quota. First, area j represents the *redistribution effect,* or a transfer from consumers to protected domestic producers, in the form of the higher price, $P + t,$ paid by consumers to domestic producers in the presence of the tariff. Second, area n represents the *revenue effect,* or a transfer from consumers to the domestic government in the form of the tariff duty. Under a quota, however, area n does not go to the domestic government, but rather to the foreign country. Recall that with a quota, the country is restricting the amount of imports; the policy emphasis is thus on moving from Y_1 to Y_3; with this restriction in supply, the price increases. Since no tax is imposed with a quota, the domestic government does not collect the money; instead, the higher price paid for the product as a result of its restricted supply goes to the foreign firms.

In addition, there are two deadweight losses associated with a tariff. First, area m represents the *production effect,* or national welfare lost through inefficient domestic production. One way of thinking of this effect is by imagining how less efficiently a domestic firm that is not competitive in global markets, such as a large, integrated U.S. steel company, uses productive resources such as capital and labor, compared with a highly competitive firm in the United States, such as Microsoft. The country would be wealthier with Microsoft using the steel company's resources because Microsoft sells so much of its product abroad, in addition to at home. Second, area r represents the *consumption effect,* or the loss of welfare to consumers for no longer being able to obtain units Y_3 through Y_1 of the good at the free trade price of P. These consumers are made permanently worse off. Conceptually, they can be thought of as people who could have afforded a cheap, imported car at the free trade price but who with the price increase of a tariff or a quota must continue to ride the bus.

The industrial adjustment that accompanies free trade, via the removal of tariff or quota protection, for example, is not without real costs. Since tariffs are unambiguously good for protected firms and the labor working for those firms, the loss of tariff protection is unambiguously bad. Moreover, labor and firms in declining, globally noncompetitive industries have a powerful incentive to lobby politicians for tariff protection since their firms and jobs are being threatened by competition from foreign firms. The incentive to save one's job or firm is typically much more powerful than the incentive for consumers to lobby to prevent a tariff from being imposed on tomatoes, for example. Most people know when their job is threatened by foreign competition, and are sufficiently motivated by this potential loss to exercise their political voice to save their livelihood. On the other hand, few people are aware of the tariff on tomatoes and, even when they are, are unlikely to take the time to exercise their political voice to oppose a tariff that adds only a few cents to a relatively inexpensive purchase. Thus political economists agree that it is generally much easier politically to obtain protection than to reverse it.

Economic models of international trade generally ignore the human costs of free trade that result in political opposition to it. The costs can be the transition costs of moving from a traditional economy (usually agrarian) to an industrialized economy—a transition that is often very harsh (as Karl Marx famously observed of England's industrialization in the middle 1800s). The global economic integration that occurs with free trade is also criticized for homogenizing formerly distinct countries and cultures. Thus, there is concern that as countries industrialize, such as China is doing currently, they lose much of their unique culture and traditions. Some countries impose tariff and quota protection on goods in an attempt to preserve their national identity; the French, for example, do this by limiting the number of American-made films that can enter the country. Despite such criticisms of free trade and global economic integration, there are still many observers who feel the benefits of trade expansion and liberalization are greater than the costs. What these supporters most often point out is that no country that has allowed relatively free trade to operate since World War II has experienced a famine—for the first time in human history. Moreover, basic living standards appear to increase sharply in countries practicing free trade, after the initial adjustment to import competition, whereas countries practicing tariff and quota protection often lag behind in national wealth creation and in innovation.

Tariff levels have declined dramatically in the United States (and most other industrialized countries) since the 1930s, when the U.S. Congress gave the authority to negotiate trade agreements to the president; this authority enabled the United States to champion the Global Agreement on Tariffs and Trade (GATT), beginning in 1947, the precursor to today's WTO (see Figure 2). Increasingly, trade agreements are focusing on nontariff barriers since GATT and the WTO have been so successful in reducing overall tariff levels. Nontariff barriers to foreign goods are practices such as domestic content laws, health and safety regulations that discriminate against foreign producers, and preferential taxes, subsidies, and contracts. While these are currently the biggest barriers to trade, they

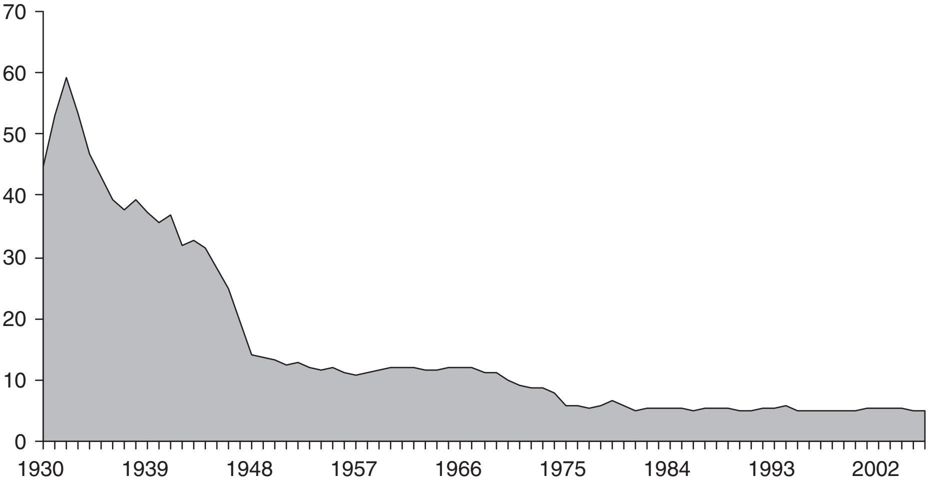

Figure 2 U.S. Average Tariff Rate (%), 1930–2006

Source: U.S. Statistical Abstract (various issues), U.S. Department of Commerce.

are also more difficult to negotiate than are straightforward tariffs or quotas.

—*Karen Schnietz*

See also Comparative Advantage; Competition; Deadweight Loss; Development Economics; Doha Development Round of 2001; Dumping; Duty; Economic Efficiency; Free Trade, Free Trade Agreements, Free Trade Zones; Globalization; International Trade; Most Favoured Nation Status; National Origin Discrimination; North American Free Trade Agreement (NAFTA); Omnibus Trade and Competitiveness Act of 1988 (OTCA); Smith, Adam; Subsidies; World Trade Organization (WTO)

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Tawney, Richard Henry (1880–1962)

Richard Henry Tawney was born in Calcutta, India, and died in London. Educated at Balliol College, Oxford, he held academic appointments at Glasgow, Oxford, and the London School of Economics. He was a founder of the Workers Education Association, an educational venture providing university-level courses for workers that eventually became an extension college within Oxford.

A prominent socialist, Tawney was a prolific writer with numerous books, pamphlets, and newspaper articles to his name. As a member of the British Labour Party, he served on major public commissions and committees that addressed policy issues in labor and education. Trips to China in the early 1930s and the United States in 1941–1942 brought him into contact with laborers in a very social context and resulted in articles and a book comparing their situation with that of English workers.

Tawney was a major figure in the development of the field of economic history and social history. He maintained that the historical endeavor must move beyond simple narrative accounts to an integrative examination of the complex web of social forces surrounding the economic system. Searching for the historical foundations of the English economy, he studied the 16th-century conflict between large landholders and small farmers over the issue of enclosure (*Agrarian Problem in the Sixteenth Century*). In the process, he discovered the important role of the English Church, which laid the groundwork for his subsequent historical examination of the relationship of economics and religion (*Religion and the Rise of Capitalism*). While acknowledging Max Weber's insights into the Protestant work ethic, Tawney disputed his conclusion that the foundations of capitalism can be traced solely to the internal, spiritual aspects of early English Puritans.

Tawney's intellectual search focused on two major issues: why rich and poor continue to coexist in a capitalist system and how to organize a new society built on economic and political equality. His critical analysis of industrial capitalism (*Acquisitive Society*) revealed what he understood to be its devastating impact on society. He argued that the dual focus of capitalists on profit and wealth unhinges the economic system from its primary purpose, to contribute to society's growth and welfare. He concluded that capitalism uncouples property rights from social purpose, diminishes the role of the industrialist as a member of a profession, and taints the working class by infecting it with a desire to acquire wealth.

Carefully weaving a path between Marxist advocates and opponents, Tawney accepted a modified market system as appropriate for the emerging new society. He advocated governmental intervention to channel the behavior of industrialists, protect workers, and eliminate poverty. He envisioned a classless society built on full equality in relationships in a community built on human fellowship (*Equality*). As a democratic socialist, he also advocated the dispersion of political and economic power to individuals to ensure the embodiment of the principle of equality.

—*D. Jeffrey Lenn*

See also Business, Purpose of; Capitalism; Economics and Ethics; Equality; Market Socialism; Protestant Work Ethic; Socialism; Weber, Max

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TAX ETHICS

Tax ethics concern the values, practices, and consequences of taxation as a means of distributing the benefits and burdens of citizenship, including evaluation of the conduct of taxpayers and their accountants and financial advisers in determining and taking responsibility for their fair share of the tax burden. The moral framework for evaluating taxation considers both ends and means in the apportioned tax burden, an accounting of the economic distortions caused by taxation itself, and an assessment of the impact on the economy of public goods and services, their impact on the larger economy, and their impact on social equity. Ethical concerns about taxation center on the proper integration of competing claims: social justice, individual freedom, economic productivity, and efficiency applied to the tax system itself as well as to the instrumental value of taxation in achieving broad social policy goals. Ethical concerns about individual responsibility concern the willingness of taxpayers and tax practitioners to discern and honor the moral claims and financial obligations of citizenship.

In democratic societies, tax ethics are often viewed in terms of simple justice: What is fair? The modern democratic view of tax equity is viewed progressively: Taxpayers of equal means should bear an equal tax burden, and taxpayers of unequal means should bear a proportionally unequal tax burden. The consideration of what is fair taxation and the development of the progressive theory of tax equity has a long history that is still in the making. In recent years, a "postprogressive" approach to taxation has developed with a focus on the role of taxation in economic growth and productivity as a means of achieving social and economic justice. During that time there has been an increased use of tax mechanisms, such as taxes and surtaxes on utilities, travel, alcohol, and tobacco, that shift the tax burden away from income toward consumption.

Historical Approaches to Tax Equity

As Cicero observed 2,000 years ago, taxes are the mainstay of the state. Governments must collect revenues to provide even minimal public services; the challenge is to create a tax system that optimally distributes benefits and burdens. Modern approaches to tax equity began with the introduction of Enlightenment principles of equality and the notion of the social contract into the political economy. Philosophers, economists, and social theorists have been debating the principles and methods for achieving a just system of taxation ever since. Thomas Hobbes believed that people would cooperate with others in sharing the burdens of civil society to achieve its benefits. Recognizing that some public services are more effectively and efficiently provided to all citizens through government agency, Adam Smith established the equitable pricing principle of taxation. Although all citizens enjoy the benefit of public services (e.g., they are protected by the military and have access to the court system without regard to their tax contribution), the underlying approach of equitable pricing derives from economic benefit; people should pay proportionally for the benefit they receive from public services. Smith argued that justice is achieved when wealthier members of society pay a greater share of taxes because they also enjoy greater economic benefits from their membership in society.

John Locke argued that property rights and earnings entitlements constitute a more compelling approach to distributive justice than taxing according to benefits received. In this view, people are entitled to the use and usufruct of their wealth and taxation. Accordingly, the competitive economics of the marketplace is considered the best mechanism both for satisfying people's needs and for achieving equitable distribution of goods and services. Proponents of property entitlements as the foundation of tax equity exert a continuing influence in appeals for limited government and marketization of public goods and services. Contemporary libertarians such as Robert Nozick regard property rights as sacrosanct and advocate a minimal role for government in provision of core public services such as defense and public safety, with some arguing that taxation itself is an unjust taking of private income and wealth.

Critics of this approach, however, are quick to point out that the market of public goods and services does not function exactly like the private market. First, there is little or no competition. Although some elements of public sector competition might be desirable, it is unlikely that the free market benefits of competing police forces, courts, or military forces would outweigh the negative consequences of inefficiency and destabilization. Second, John Stuart Mill's lighthouse example illustrates that many public services are nonrival; the light is available to all, and it would be inefficient (if not impossible) to restrict its rays only to those who pay for it. Third, a society that values human worth and dignity is morally obligated to make some public accommodation for people in dire cases of poverty and hardship, which means that the cost of their public benefits will be paid by someone else. Most theories of optimal taxation have attempted various arguments to justify the assumption of a progressive tax burden for the wealthy.

Utilitarian theories have been influential in the development of modern approaches to tax equity. Mill originally posited the principle of "equal sacrifice," arguing that everyone should sacrifice equally to provide the benefits of public goods and services. Since people are positioned differently on the wealth and income scale, an equal tax cannot be imposed fairly on all. Mill theorized that the marginal utility of income falls as income rises, therefore reducing the amount of sacrifice imposed by tax increases proportioned to wealth. In this view, wealthier people can assume a greater share of the tax burden while still maintaining an equal share of sacrifice. Similarly, the tax burden imposes an equal sacrifice on people positioned together horizontally at various points on the vertical income and wealth scale, and therefore they should pay the same amount of tax. Jeremy Bentham believed that communities of rational people would willingly choose a social contract with egalitarian distribution of burdens to achieve the social good of a civil society as a benefit for themselves.

Economists joining the debate in the past century questioned the basic assumptions of the utilitarian case for progressive tax equity. Economic models could not substantiate either the decreased marginal utility of income as it rises or the derivation of equal utility from public benefits by people of equal income. With the theoretical underpinnings for progressive taxation threatened, economists sought to formulate an economic model of social welfare function to demonstrate the optimal distribution of resources. Economic modeling was incorporated increasingly into the public policy process, shifting the focus of tax structure from equity to efficiency and to the broader relationship between tax policies and economic growth. By the middle of the century, the case for progressive taxation, so firmly entrenched in the social conscience of democracy, could no longer be grounded on utilitarian arguments. Marginal personal income tax rates climbed to a high of 90% and corporate tax rates reached more than 75% in the early 1950s; the economic impact of progressive taxation had political consequences. While Americans have consistently favored progressive taxation, they also understand the value of economic growth generated from less progressive taxation. Widespread calls for tax cuts for business and the wealthy to stimulate the economy have often been met with concerns about shifting the tax burden down the income scale and spurred renewed theoretical attention to tax equity. Economists have succeeded, however, in promoting a public awareness of tax equity within a broader context of the economy as an essential asset of the commonweal. This understanding has helped reframe public discourse about tax ethics as a means of actualizing a civil society of distributive justice and equal opportunity and protection of human rights.

One of the thorniest problems in theorizing tax equity is the problem of reconciling political equality with the natural inequality of human endowments. How can people born with a wide range of innate abilities that position them with greater or lesser comparative advantage be treated fairly in the distribution of social benefits and burdens? John Rawls's theories of human rights and distributive justice have had a strong influence on contemporary approaches to this problem. According to Rawls, the premise of equal worth is best realized if individuals choose among various options of distribution benefits and burdens without regard to their own status, imagined as a veil of ignorance. From this position of impartiality, people would make choices to maximize the good for everyone, and inequalities would only be tolerated if they served to improve the status of the least advantaged.

Applying Rawls's theory to tax equity, progressive tax rates would be just if devised from behind the "veil of ignorance," with the intent of maximizing benefits for all and permitting only inequalities that benefit the least advantaged. With the justification for tax equity based on the premise of equal moral worth rather than incalculable assumptions about comparable utility, sacrifice, or ability to pay, the moral debate of distributive justice shifted more toward the social and economic impact of various tax mechanisms and the constitution of the social safety net as a foundation for public affirmation of equality. The concept of distributive justice developed by Rawls has been influential in justifying and explaining the legitimacy of taxation as an instrument of the public good in the modern state.

Taxation as Social Policy

In the broadest sense, taxation is an instrument of social policy. Tax revenues fuel the political will of the citizenry through programs and initiatives that foster the type of society they value. The basic social policy questions are the following: (1) What should government do for its citizens? (2) What should government expect citizens to do for themselves? In a free, democratic society, it is expected that government provide goods and services that not only meet the expressed needs of its citizens but also spur the economy and promote the values of democracy and freedom for the flourishing of a civil society. Most tax scholars would agree that the American system of taxation has been effective when measured against these social goals, but there are admittedly some glaring failures. As tax policies in recent decades have shifted the tax burden away from the wealthy and focused on stimulating economic growth and efficiency, the income and wealth gap between rich and poor has become a matter of increased attention and moral concern.

One of the most elusive social policy goals is the elimination of extreme poverty, with its devastating effects on children, families, and neighborhoods. There are certainly intractable social inequities that draw the attention of those who advocate increased investment in a social safety net. For example, the United States, the wealthiest nation in history, does not have a universal access health system; its infant mortality rates and children's school achievement scores do not compare favorably with other wealthy, industrialized nations. Although some argue for a dramatic shift in public spending toward more substantial investment in programs that serve poor children, families, and neighborhoods, others claim that poverty is not itself the problem but the result of other social problems people have created for themselves; individuals who have made poor choices or squandered their opportunities should not be bailed out by the majority of citizens, who have worked hard to be productive members of society. Others who agree that poverty is a problem argue that the benefits of economic growth eventually trickle down to benefit all.

Recent public policy initiatives reflect a social goal of fostering initiative and productivity among the poor rather than reinforcing dependence. Keeping holes in the social safety net may make it a less attractive destination—and perhaps motivate people to become taxpayers rather than recipients of tax-funded programs. In contrast, the premise of equal human worth, the foundation of modern civil societies, presents the human capabilities of each citizen as a moral claim on society; in this view, it is the corresponding duty of a civil society to develop the capabilities of its citizenry. These concerns are amplified in examining the moral implications of the global political economy. One ethical measure of taxation is the degree to which a society has effectively developed the human capabilities of its citizens and cultivated the corresponding political will to pay for the investment in its human capital. Human societies are also ethically responsible for the way they care for their citizens when they are not able to be productive: during childhood, sickness, or other periods of frailty.

The mechanisms of taxation (e.g., tax on personal and corporate income, property, consumption, gifts, and wealth transfer; user fees, licensure fees, and social security tax; special levies for public works, services, and projects; rate structures; exemptions and allowances) are as important morally as the goals they are intended to achieve. For instance, critics of consumption tax object to its heavy burden on people of lower means who spend a proportionately greater share of their income on necessities, advocating instead a focus on the higher incomes, inheritances, property, and luxury items of wealthier citizens. And critics of the "sin taxes" on alcohol and tobacco insist that such tax mechanisms unfairly single out certain classes of people for a disproportionately heavy tax burden.

History has shown that the equity intended by taxation policies and mechanisms is not always achieved. Well-intentioned tax mechanisms can shift benefits and burdens to distort relative economic positions or to stabilize the position of a corporation. For instance, legal tax shelters designed to achieve specific public policy goals can relieve some wealthy taxpayers of their entire tax burden. The alternative minimum tax (AMT), established decades ago by the U.S. Congress to ensure fair tax payment from wealthy taxpayers with creatively legal tax shelters, was not indexed for inflation and has imposed a dramatically heavier tax burden on middle-income earners several decades later. A consumption or luxury tax may drive the wealthy to external markets. Arguably, high corporate tax rates can be passed on easily to individuals.

Raising property taxes may spur short-term revenues but create a disincentive for home ownership, depress the real estate market, and slow long-term property tax revenues. These consequences are important ethical considerations in evaluating the long-term effectiveness of tax mechanisms in achieving desired ends.

Tax mechanisms may also disrupt the public economy of revenues, goods, and services. For example, a "flat tax" is often proposed as a simplifying tax mechanism without examining the resulting downward shift in tax burden away from upper-income earners toward middle-income earners. Since the 1960s, the economic consequences of steeply progressive tax structures have been understood as negative for the poor and middle-income earners as well as for the wealthy; tax mechanisms have since shifted to stimulate economic growth, productivity, and efficiency rather than to transfer wealth directly down the economic scale. Advocates of postprogressive tax policies insist that the continued strength of U.S. economic performance can be attributed, at least in part, to this change of tax structure. As discussed earlier, however, a tax structure focused on the social goal of economic efficiency and productivity may not be effective in addressing the moral claims of citizens who are unable to be productive and may inhibit the productivity of citizens who need special supportive services to participate fully in society.

Ethics for Taxpayers and Tax Practitioners

Individual taxpayers and tax practitioners are inevitably influenced by their personal views of society, the role of government in society, and the proper use of public funds in achieving social goals. Taxation takes money from people who have earned it for purposes often defined by others as desired social policy. How does the individual respond to the moral obligation of taxpaying, especially when the social policy goals of taxation conflict or do not coincide with his or her own view of the good society? What is the ethical framework for justifying the payment of taxes? How does this framework support the personal choices of taxpayers and the professional conduct of tax practitioners?

Citizens, as individuals and corporate entities, are morally obligated to pay their fair share of taxes as defined by law. The ethical legitimacy of government taxation has been well established on the grounds of social contract and distributive justice theory. Citizens who object on moral grounds to specific social policies or programs funded through tax revenues or to the fairness of tax mechanisms may express their views through transparent engagement in the policy process rather than through refusing to comply with the tax system. In cases where tax law could be legitimately interpreted or applied with different tax consequences, the taxpayer is morally obligated to make what she considers a fair judgment with attending disclosures and payments. It is reasonable to expect that a taxpayer with complex business interests and transactions would seek the counsel of a tax practitioner in discerning a rigorous interpretation of fair tax. Taxpayers are morally obligated to be truthful about their financial status and operations but not to pay more than a reasonably determined fair share of tax based on truthful financial disclosure.

In addition to the moral obligations outlined for taxpayers, tax practitioners who advise taxpayers and prepare taxpayer returns operate under professional obligations to their taxpayer clients, their professional colleagues, the government, and society. Tax practitioners are obligated to advise their clients truthfully in full knowledge of the tax code and its legal obligations. They are obligated to maintain a current level of professional knowledge and seek the counsel of colleagues when unique circumstances of their clients exceed the range of their own knowledge and expertise. They are obligated to perform their duties honestly and transparently while guarding the privacy of their clients and their sensitive financial information. Tax practitioners are also obligated to participate through their professional associations in the development and clarification of standards for upholding the professional competence and integrity of tax practitioners. Tax practitioners should be mindful of their influence on the conscience of their taxpayer clients.

—Lindsay J. Thompson

See also Justice, Distributive

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TAX HAVENS

A tax haven is a nation other than your own that has lower tax rates and more confidential banking procedures than are found where you reside or normally do business. These havens are made up of about 70 countries and jurisdictions (generally small in size) that provide no-tax or low-tax status and offer a variety of taxation-related incentives to individuals and organizations who wish to bank, incorporate, or headquarter their business within the country in question.

Tax havens are controversial, especially since much of the world's wealth (up to one third) is held "offshore" in such entities. Opinions also differ as to their overall impact, so it is helpful to distinguish between the legal, illegal, and unethical practices associated with tax havens. After all, tax collectors have been unpopular as far back as biblical times. In the Middle Ages, Robin Hood and William Tell were romanticized for fighting against oppressive taxation. A number of serious researchers have also argued that the American Revolution was a successful scheme of tax resistance.

Tax havens are part of the ongoing development of global financial markets. The offshore banking phenomenon began as a legal way for bankers to avoid the taxes and lending restrictions associated with highly regulated national financial markets. Deregulation of national financial markets arose in the 1980s in part as a response to the loss of business in international lending to offshore banks. National (as well as state and local) governments also play the game of offering tax-break incentives to attract foreign investment. Lobbyists also work overtime in the halls of Congress to create or hang on to various legal (if perhaps not always ethical) tax shelters and loopholes.

Tax haven countries offer their services in exchange for service fees and being enriched with assets that help make them politically and economically stable. Foreign corporations, trusts, and partnerships may have valid business purposes for using offshore entities and accounts. Most, however, do so for illegal rather than legitimate reasons.

Lack of transparency (noncooperation with banking regulators of other countries) is one of the major criticisms. Wealthy foreign individuals and enterprises often use these offshore nations as financial centers to disguise business transactions and hide assets. In this context, the world of offshore finance is one of dummy companies, shadow bank accounts, untraceable post office boxes, foreign registries, and other questionable activities. One example involves the substantive role of tax havens in disguising and sheltering illegal drug profits.

Growing resources are being devoted to identifying transactions that are blatantly illegal attempts to defraud creditors, investors, and taxing entities. Such use of tax havens generally serves no business purpose other than to divert income and conceal assets for taxpayers who have no actual operations in the foreign tax haven. Scams are rampant.

The size of the problem is staggering for those nations witnessing a flow of resources overseas through electronic money transfers and other means. In his book *Offshore: The Dark Side of the Global Economy,* reporter William Brittain-Catlin estimates that one third of the world's wealth—or $7 trillion—and 80% of international banking transactions take place in the shadowy offices of banks in the Cayman Islands or the Islamic financial center of Labuan, Malaysia. As much as half of world trade might be routed through tax havens, with huge chunks of capital in the world's stock exchanges "parked" offshore at some point. Furthermore, London's Tax Justice Network (TJN) in 2003 reported that rich individuals worldwide had hidden more than $11.5 trillion of their assets in such hideaways.

Annual tax losses through legal and illegal capital flight to the havens are projected at $225 billion. It is estimated that the United States loses a minimum of $60 billion, although the numbers may be much higher due to lack of effective oversight. Taking advantage of these international markets is a veritable "who's who" roster of very large corporations such as Wal-Mart, Citigroup, BP, and others who are alleged to be hiding their profits in tax haven institutions, away from the eyes of investors, regulators, journalists, and the public.

U.S. persons are taxed on their worldwide income regardless of where it is earned or sourced. Thus, the incentive for using a tax haven is to convert a U.S. taxpayer who is supposed to report all his worldwide income to a "nonresident alien" reporting no income and thus paying no income tax.

A corporation's earnings are taxed twice—once at the corporate level when initially earned and then at the shareholder level when dividends are distributed. The use of a foreign corporation can be beneficial because it can result in deferral. If a foreign corporation has no U.S. trade or business and earns only foreign source income, the corporation's earnings will not be subject to U.S. tax until they are repatriated in the form of dividends to U.S. persons who are shareholders.

Tax havens work by taking advantage of their sovereignty to attract foreign businesses by deliberate public policies. Resident lawyers work with these governments to legally set up a system of little or no income tax in the jurisdiction under their control. They also offer the ability to form entities quickly. This is coupled with a veil of secrecy created through strict laws against disclosure of banking and business records. In effect, tax havens typically refuse to enter into treaties or information agreements with other nations that might open up their records to independent scrutiny. At the same time, these states also take advantage of modern international banking, communication, and transportation facilities. Once up and running, they promote their services with a "wink and nod" about undertaking transactions for clients even though there often is no economic substance other than to evade taxes.

Legislation introduced in the U.S. Senate in April 2005 recognized certain countries as tax havens (see Table 1).

Categories of Tax Havens

Zero Tax Haven

A zero tax haven is a country where there are no income, capital gain, or wealth taxes of any sort and in which there are facilities and legislation under which one can incorporate and/or form corporations, foundations, and trusts. The governments in these countries earn revenue from charging fees on documents of incorporation, valuing corporations' shares, and registration fees.

No Tax on Foreign Income Tax Haven

These countries do impose income taxes on individuals and corporations but not on foreign-sourced income. Countries in this category include Hong Kong, Liberia, Panama, the Philippines, Venezuela, Jersey, Belize, Guernsey, the Isle of Man, and Gibraltar.

Low Taxation Tax Havens

These countries generally tax a small amount on corporate income and have double-taxation agreements with many high-tax countries that when structured

Table 1 Major Tax Havens

Andorra	Grenada	The Netherlands
Anguilla	Guernsey	Niue
Antigua and Barbuda	Isle of Man	Panama
Aruba	Jersey	Samoa
Commonwealth of the Bahamas	Liberia	San Marino
Barbados	Principality of Liechtenstein	Federation of St. Christopher and Nevis
Belize	Maldives	Saint Lucia
Bermuda	Malta	Saint Vincent and the Grenadines
Cayman Islands	Marshall Islands	Republic of the Seychelles
Cook Islands	Mauritius	Tonga
Cyprus	Monaco	Turks and Caicos
Commonwealth of the Dominica	Montserrat	Republic of Vanuatu
Gibraltar	Republic of Nauru	

Source: Congressional bill introduced in the U.S. Senate in April 2005. See http://thomas.loc.gov/cgi-bin/query/z?c109:S.779.IS.

correctly work to reduce the overall degree of taxation. These include Cyprus, the British Virgin Islands, Liechtenstein, Oman, Switzerland, Jersey, and Guernsey.

Special Incentive Privileges

These countries give special incentive privileges to offshore companies and qualified holding companies. These countries include Luxembourg, the Netherlands Antilles, and Singapore. In addition, *international business company tax reductions* are offered by Antigua, Barbados, Grenada, Belize, and Jamaica.

An offshore scheme must assist in moving money or property outside the host country, operating offshore assets to produce further untaxed income and bringing the money home to spend. At their lowest level, offshore financial promotions are simple frauds and another way of inducing victims into phony investment schemes. At the other extreme, they involve a complex series of offshore entities designed to conceal the true ownership and control of assets and income. The following steps are common to them:

- Creation of the offshore structure: Promoters introduce people to offshore structures and use professionals such as attorneys, accountants, and private bank departments of both domestic and foreign financial institutions.
- Concealing transfers of money or other property to the offshore entity: Due to money-laundering laws, the transportation of currency is not widely used. Devices commonly used to get money offshore include (1) creation of an offshore business banking account, (2) fictitious invoicing for payments characterized as legal, consulting, or management services, (3) loans and gifts, (4) interest paid on loans, (5) insurance premiums, (6) transfers of assets in exchange for private annuities, (7) deferred compensation structures, (8) factoring of accounts receivables, and (9) use of a domestic trust so that diverted income can be disguised as deductible expenses or as distributions to an apparently unrelated beneficiary.
- Sales and transfers of property: People structure phony sales of property to a foreign entity, in exchange for a note they do not expect repayment on. The foreign entity with the note immediately sells the assets to a third party who remits the proceeds offshore. This gets title to the property—and its future earnings—offshore. Nonexistent equipment may be purchased from a person's foreign trust and depreciated over a 5-year period even though the payments being made are to the individual himself.
- Maintenance of control of funds while offshore: Banks and trustees virtually give the taxpayers full control of their assets. Many trustees offer various forms of secured communication so that the U.S. person can communicate without fear of detection. Trustees can easily create front corporations inside and outside the United States to carry out instructions.
- Determining a safe way to move money back onshore: People who were not willing to pay tax on the money when it was moved offshore do not want it taxed when they bring it back. Some popular ways of repatriating funds include (1) using credit cards to draw funds from an offshore account; (2) gifts from foreign relatives; (3) loans from mystery offshore lenders; (4) loans from domestic lenders secured by offsetting deposits of offshore funds; (5) use of property titled to offshore entities at zero or below-market rental; and (6) bogus transactions such as purchases, sales of property, and leasing that have no real business purpose or economic substance.

Tax shelter sales are no longer just the province of shady promoters but have become big business assigned to talented professionals at the top of their fields and able to draw on the vast resources and reputations of the country's largest accounting firms, law firms, investment advisory firms, and banks.

Over the past 10 years, federal statues and regulations prohibiting illegal tax shelters in the United States have undergone repeated revision to clarify and strengthen them. Today, key tax code provisions not only prohibit tax evasion by taxpayers but also penalize persons who knowingly organize or promote illegal tax shelters or who knowingly aid or abet the filing of tax return information that understates a person's tax liability. Additional tax code provisions now require taxpayers and promoters to disclose to the IRS information about certain potentially illegal tax shelters. Nevertheless, the system is flawed. Attempts have been made to introduce much tougher legislation, but there are many interests benefiting from the havens, who are quietly opposing efforts to beef up regulation.

While the attempt to minimize government payments to do business is not unlawful or outside ethical boundaries per se and may even offer some benefits within the global economy, tax havens raise a number of social and ethical issues. The secrecy that tax havens provide encourages corruption. Generally, individuals, corporations, and trusts are taxed on their worldwide income. It follows that if tax havens are used, ethical individuals, corporations, and trusts would report this income and pay tax on it. Unethical individuals, corporations, and trusts use tax havens for the illegal purpose of disguising their true income and evading taxes. This has a particularly damaging effect on developing countries because the use of tax havens undercuts their efforts to secure funding and development assistance.

Those promoting "virtue of selfishness" and "looking out for number one" values may applaud such outcomes, but most ethical systems would have difficulty with the current tax haven phenomenon. Deontological (duty-based) ethical approaches generally would be concerned about falsity and the failure to be even-handed in providing information to the variety of stakeholder audiences that depend on honesty in financial reporting. John Rawls is neo-Kantian in that his "veil of ignorance" deductive device works like Kant's categorical imperative in deriving universal normative principles based on fairness. This encourages equal treatment of all without regard to status—not secrecy to defraud.

More recently, Donaldson and Dunfee have argued that social contracts exist. Their hypothetically derived macrosocial hypernorms are similar to Kantian and Rawlsian universal ethical norms, but their extant microsocial community norms for defining "moral free space" could well be helpful in clearing up the moral ambiguity, as well as the legal laxity, of tax havens. Even many utilitarian (outcome-driven) ethicists would tend to find the hidden nature of tax haven practices rather unsavory, especially when such transactions are illegally disguised to evade lawful taxes.

—Richard Alan Nelson

See also Consequentialist Ethical Systems; Deontological Ethical Systems; Fraud; Free Market; Global Business Citizenship; Internal Revenue Service (IRS); International Business Ethics; Kantian Ethics; Rand, Ayn; Rawls, John; Rawls's Theory of Justice; Social Contract Theory; Tax Ethics; Tax Incentives; Utilitarianism; Virtual Corporation; Wealth

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Tax Incentives

A tax incentive is a special provision of the tax code designed to foster particular behavior on the part of tax-paying firms or individuals with the intention of encouraging some particular behavior that is believed to be socially beneficial. There has been a move toward designing specialized tax incentives that encourage saving for particular activities or spending on special goods and services. Unlike other tax provisions, which define the amount or transaction subject to tax and the rate or rates at which the tax applies, tax incentives represent deliberate departures from otherwise applicable taxes to encourage the activity at which the incentive is directed. For this reason, these subsidies are described as tax expenditures. These can take many forms, such as permanent exclusions from income, deductions, deferrals of tax liabilities, credits against tax, or special rates. These departures from the normative tax structure represent government spending for favored activities or groups effected through the tax system rather than through direct assistance.

Corporate Tax Incentives

Especially since 1960, the United States has relied on tax policy to direct private investment toward social objectives. The use of business tax incentives—that is, the adoption of particular features of the tax code as instruments of public policy rather than merely as revenue-raising devices—goes back at least to 1954, with the introduction of accelerated depreciation. Business tax incentives have been justified above all as a stimulus to capital formation. Even when the rationale is job creation, it is job creation via capital investment. Incentives have been provided for areas as diverse as the continued use and rehabilitation of older structures in an effort to arrest urban decay, research and development costs to encourage innovation, and employment subsidies to increase employment among the poor.

Tax subsidies often favor larger firms within an industry and can alter industry structure. Even if the price of products is not affected, the larger firms receive an advantage by having more earnings after taxes and consequently more resources for investment and greater growth potential. On the other hand, if these larger firms do pass the full tax savings on to consumers, they may be able to lower product prices below the average costs for smaller firms facing higher effective tax rates, potentially driving some of the small companies out of business and increasing industry concentration.

Individual Income Tax Incentives

A number of tax incentives are available to individuals. These can be in the form of deductions from taxable income, gifts, or savings accounts that can grow either tax-free or tax-deferred. Some examples are given below:

- Deductions: Expenditures for home ownership, excess medical expenses, state and local income taxes, property taxes, and gifts to charity can be used to reduce taxes.
- Gift and estate taxes: Under current law, individuals are permitted to make gifts of $12,000 per recipient, per year, free from any gift or estate taxes. This allowance permits a substantial sum to be transferred to heirs free of tax. While yearly amounts may be small, consistent use of this annual exemption can lead to the tax-free transfer of large amounts of wealth.
- Education savings: The Coverdell education savings account (ESA) and Internal Revenue Code Section 529 savings plans are structured so that after-tax dollars grow tax-free. Earnings are never taxed if withdrawals are used for qualified education expenses.
- Retirement savings: Individual retirement accounts (IRAs), 401(k) plans, and 403(b) accounts all offer incentives to save for the future. Closely related are employee stock purchase plans (ESPPs), which are employer-sponsored programs that permit employees to save by purchasing company stock, while contributions to them and accumulations within them are subject to favorable tax treatment.
- Health savings accounts: Several options are available for saving for future qualified medical and retiree health expenses on a tax-favored basis.

Tax Credits

A tax credit is an amount subtracted from the gross tax to determine the net tax due. Credits, then, are similar to prepayments of the tax and are not a part of the computation of taxable income, the tax base. Therefore, tax credits are more beneficial to taxpayers than tax deductions. There are three general groups of tax credits. First, there are credits related to business operations and investments. These consist of credits for expenditures such as for historic rehabilitation, research and development costs, hiring individuals from targeted groups, environmental remediation costs, development of renewable resources, and low-income housing developments. Second, there are credits allowed to individuals only because of some special need, such as the child care credit or the credit for the elderly and people with disabilities, or for purchasing certain targeted products, such as electric and clean fuel vehicles. The third group consists of credits related to prepayments and includes credits such as those allowed for income taxes paid to foreign countries and off-highway use of fuels. The availability of such tax credits provides behavioral incentives for taxpayers above and beyond other tax incentives specifically written into the tax code as deductions against income.

State Tax Incentives

The effects of variations in states' corporate income tax regimes can have a significant impact on new capital investment by business as state governments attempt to encourage job creation or capital investment that would not have occurred without such incentives. A key structural feature of the state income tax in the United States is the apportionment formula used to subdivide a multistate firm's income among jurisdictions with which they have sufficient contact (nexus). In general, a corporation's business income is apportioned among the states based on what portion of its sales, payroll, and property occur in each state. The theory is that these factors will fairly reflect the tax attributable to each state. While the Tax Reform Act of 1986 did away with the federal investment tax credit, a number of states have not only preserved their investment tax credit but have also enacted new or expanded investment-related tax credits, such as enterprise zone credits, new facilities credits, and corporate headquarters (relocation) credits. The effect of such incentives is to lower the tax cost of doing business in that state. Thus, these incentives act as substitutes for or complements to tax rate changes or apportionment formula changes designed to accomplish similar objectives. In addition to these credits, many states offer income tax exemptions, property tax exemptions, sales and use tax exemptions, and supplemental accelerated depreciation options to attract businesses to locate within their borders. Some economists consider state tax incentive programs, which seek to influence corporate plant location decisions, to be state-based "industrial policy" initiatives, which can distort free market mechanisms for allocating resources toward their "highest and best use," thereby triggering potentially adverse economic and social welfare consequences. If competing states are overly aggressive in offering location tax incentives, they may bid away most of the social gains from the investment, thereby benefiting the corporation, but not necessarily society as a whole.

International Tax Incentives

Issues of tax competition among nations have become controversial with the globalization of the economy. Many countries have established extra tax incentives for domestic businesses, as well as tax incentives promulgated for the purpose of attracting foreign businesses. A number of organizations, including the United Nations, the World Trade Organization, and the Organisation for Economic Co-operation and Development, have established special dispute resolution procedures allowing nations to air their grievances and resolve them amicably, as international consensus is needed as to where income should be taxed. Historically, active income has been taxed at its source and passive income at a taxpayer's place of residence. Thus, the country where the income is generated has the primary right to levy taxes; the country where the recipient of the income resides has a residual right to tax passive income. However, nations allow varying profit calculating methods and transfer pricing rules in an effort to find universally applicable means of attracting inbound investments while at the same time protecting domestic businesses from unfair competition. Multinational corporations (MNCs) use internal transfer pricing policies to allocate income among their subsidiaries to take advantage of some lower host country tax rates. Host country governments monitor MNC transfer pricing practices in an effort to minimize such tax avoidance behavior. The legislative objective is typically to focus on long-term goals, such as the economic health of the country, the substantial increase of internal revenue, and the protection of national economic interests. Some critics of MNCs regard such shopping for preferential tax treatment to be an abuse of economic power, which has the effect of shifting welfare gains away from the host country and toward the corporate interest.

—Paula J. Thielen

See also Employee Retirement Income Security Act of 1974 (ERISA); Individual Retirement Accounts (IRAs); Industrial Policy; Pensions

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Tax Incidence

The incidence of a tax is the distribution among taxpayers of that particular tax's economic burden (i.e., the sacrifice of taxpayer utility or welfare). Tax incidence ignores distribution of any benefits received from government expenditures. Tax incidence, tax burden, and tax shifting are closely related notions. Statutory incidence is the initial distribution among taxpayers of a legal obligation to remit tax receipts to the government. Economic incidence is the final burden of that particular tax on the distribution of economic welfare in society. The difference between initial incidence and final incidence is tax shifting.

For example, the government may levy a tax on gasoline sales, typically as so much per gallon. Initially, this tax falls on the retail seller of gasoline, who is responsible for remitting tax receipts. The retail seller commonly passes this tax fully to the purchaser of gasoline, who bears the final burden. The government intends that the final user of gasoline bear the economic incidence of the tax, and uses the retail seller as a tax collector.

Tax analysis dates back to the French Physiocrats, who immediately preceded Adam Smith's *The Wealth of Nations* of 1776. Economists study incidence and shifting using tools of partial equilibrium analysis and general equilibrium analysis. Tax incidence concerns fairness or justice of impact of taxes. Equal sacrifice theory argues that each taxpayer should make the same sacrifice of utility or welfare. There are three competing principles of equal sacrifice. Absolute equal sacrifice argues that each taxpayer should bear the same degree of burden. Proportional equal sacrifice argues that each taxpayer should sacrifice the same proportion of welfare. Marginal equal sacrifice argues that each taxpayer should give up the same utility from the last (i.e., marginal) dollar of income or wealth yielded to government.

It is typical to divide taxpayers into incidence groups by income or wealth to measure the degree of progressivity or regressivity. Taxes levied on an ability to pay principle can be classified as regressive, neutral, or progressive. A regressive tax places a higher burden on taxpayers of lesser means. A progressive tax places a higher burden on taxpayers of greater means. A proportional tax with an exemption for taxpayers of low income or wealth exhibits some degree of progressivity. The personal income tax is typically levied using graduated rates rising with the taxpayer's income; and an exemption can be applied for taxpayers of low income.

The burden or sacrifice of a tax, whether levied on the ability to pay principle or the benefit principle of taxation, can be measured as the money amount of tax receipts collected. All taxes other than the poll (i.e., head or capitation) tax exhibit some excess burden, defined as an economic burden greater than those receipts. All other taxes destroy more economic value than the government collects, because taxpayers change their economic behavior in response to the taxation. An excess burden of a tax is a form of deadweight loss of consumer welfare. Only the poll tax cannot be shifted.

The concepts of incidence and economic burden can be applied more broadly than to taxes. Any effect, such as injuries or illnesses, may be distributed unevenly and generate economic burden. Tariffs, monopolies, and theft can be treated as taxes on consumer welfare.

—Duane Windsor

See also Deadweight Loss; Desert; Justice, Distributive; Marginal Utility; Regressive Tax; Surplus, Consumer and Producer

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Tax Reform Act of 1986

The Tax Reform Act (TRA) of 1986 was the most extensive review and overhaul of the Internal Revenue Code by the U.S. Congress since the inception of the income tax in 1913 (the Sixteenth Amendment). The purpose of the TRA was to simplify the tax code, broaden the tax base, and eliminate many tax shelters and preferences. The TRA was intended to be essentially revenue-neutral though it did shift some of the tax burden from individuals to businesses. Although often described as one of President Ronald Reagan's (a Republican) greatest legislative legacies, the TRA was officially sponsored by two leading Democrats, Representative Richard Gephardt of Missouri and Senator Bill Bradley of New Jersey, and was strongly supported by the House Ways and Means chairman, Representative Dan Rostenkowski of Illinois (a Democrat). The legislation was signed into law on October 22, 1986.

The TRA reduced the number of individual income tax brackets from 14 to 2. The TRA also lowered the top tax rate for individuals from 50% to 28% and raised the bottom rate from 11% to 15%. The TRA removed millions of low-income citizens from the income tax rolls. The TRA ended tax code provisions for individuals to deduct interest on consumer loans; however, it increased personal exemptions and standard deduction amounts and indexed them to inflation. The TRA revised tax credits for amounts that individuals could contribute to certain types of individual retirement accounts (IRAs). The TRA strengthened the "alternative minimum tax" provisions of the income tax code for individuals, which were first created in 1978. The TRA passive loss limitation provisions reduced the use of certain tax shelters by wealthy individuals.

The corporate tax rate was reduced from 50% to 35%. The TRA repealed corporate tax preferences for the investment tax credit for the purchase of depreciable assets, lengthened certain asset lives for cost recovery, and limited bank deductions for loan-loss reserves in a given year. It also reduced the allowances for certain business expenses, such as business meals, travel, and entertainment, and restricted deductions for certain other expenses. One provision of the TRA created an alternative minimum tax for corporations (at a rate of 20%) to replace an existing corporate add-on minimum tax.

Since the passage of the TRA in 1986, tax code revision has become virtually a perennial event, resulting in the return of many tax breaks and an increase in the number of tax brackets. Of particular note were the Revenue Reconciliation Act of 1990 under President George H. W. Bush, the Revenue Reconciliation Acts of 1993 and 1997 under President Bill Clinton, and the Economic Growth and Tax Relief Act and Reconciliation Act of 2001 under President George W. Bush.

—Frank L. Winfrey

See also Cato Institute; Flat Tax; Individual Retirement Accounts (IRAs); Internal Revenue Service (IRS); Justice, Distributive; Regressive Tax; Tax Incentives; Value-Added Tax (VAT)

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Teaching Business Ethics

Teaching business ethics at universities involves delivering instructional material on the social value of commerce aimed at helping students understand society's expectations of business responsibilities and the responses of corporations and their agents. Although investigation into the role of commerce in society has been a topic of discussion throughout recorded history, teaching ethics in university business schools is largely a product of the latter part of the 20th century. Specifically, interest in teaching business ethics grew in the 1960s as a result of business school reform spurred by the publication of the Ford Foundation study *Higher Education for Business* and the Carnegie Corporation report *Education of American Businessmen.* This development was reinforced in the 1970s when the American Assembly of Collegiate Schools of Business (now the Association to Advance Collegiate Schools of Business) revised its accrediting standards to grant business and society course work common-body-of-knowledge status in business schools. This revision occurred around the same time that Social Issues in Management became a separate division of the Academy of Management and a partnership was established between philosophers and business and society scholars to explore a common interest in business ethics. As a scholarly enterprise, teaching business ethics has been shaped by a cross-fertilization of ideas from this partnership, as well as by insights from the social, political, and management sciences.

While the number of stand-alone business and society and ethics courses peaked in the late 1980s, interest in teaching business ethics was rekindled by an unprecedented eruption of corporate scandals around the turn of the new millennium. As news of corporate malfeasance and indictments of corporate executives for breaching their fiduciary responsibilities unfolded, many knowledgeable observers called for business schools to do more in educating students about their future responsibilities to society. While there are many methods for doing so, a common challenge for business ethics educators is to blend philosophical notions of right and wrong with the practical realities organizational decision makers face. One approach is to begin instruction with a broad notion of a social contract between business and society as a backdrop for helping students understand the social value of commerce and how ethics relates to it.

Levels of Analysis for Teaching Business Ethics

Before students are exposed to a detailed knowledge of business ethics, many instructors find it helpful to address the value of commerce with a social contract approach to the legitimate role of business in society. A utilitarian interpretation of this contract is that society grants legitimacy to business as an institution because of its potential to serve the greater good by producing goods and services that society otherwise would not have. According to Archie Carroll, this foundational economic responsibility is attenuated by the requirement that firms adhere to the law and the expectation that they embrace important ethical norms not embodied in law. In addition, some members of society want corporations to carry out discretionary responsibilities by giving back to the community in the form of contributions to charities or other worthy causes.

Framing business ethics in terms of the social value of commerce and corporate responsibilities makes it possible for students to grasp early on that society's expectations of business are informed largely by two major ethics traditions: utilitarianism, which emphasizes the social consequences of corporate actions, and deontology, which focuses on the various duties or responsibilities corporations have to constituent groups or stakeholders. In the first case, business actions might be deemed ethical by a consequential evaluation of the distribution of harms and benefits to stakeholders. Stated simplistically, if the benefits, especially economic gains, outweigh the harms, then the greater good is said to be served by the role of corporations in society. In the second case of deontology, business conduct may be evaluated as ethical if corporate agents carry out various duties to stakeholders, motivated by respect for the dignity and intrinsic value of these constituents. Both utilitarianism and deontology can be invoked by the instructor to reinforce the understanding that the social value of commerce depends on business using its considerable power wisely for community flourishing, which amounts to some mixture of economic, legal, ethical, and discretionary responsibilities under the terms of the social contract.

While utilitarianism focuses on the ends or consequences of action, the deontological approach eschews treating people merely as means to ends. Hence, on the stakeholder level of analysis, teaching business ethics in terms of corporate responsibilities involves imparting knowledge of the rights that various stakeholder groups may assert and notions of justice and fairness that support such rights and concomitant expectations of duties from corporations and their agents. For instance, an instructor could ask students to consider that consumers who pressure firms for safe products may assert their right to be protected from harm, buttressed by the claim that to pay for a product that causes harm is unjust or unfair. This assertion of a right to fairness implies that corporations have a duty to ensure the safety of their products, even when not required by law and ideally out of respect for the inherent dignity of their customers, which is consistent with the duty-based perspective. At the same time, the instructor can encourage students to grasp that the cost of product safety may adversely affect the economic performance of a firm, its ability to compete with other firms in the industry, and financial returns to shareholders, all of which affect a utilitarian calculus of desired outcomes from a firm's point of view.

This type of example delivered early on in business education can help students realize the role that public policy can play in balancing business's pursuit of economic ends with various duties or responsibilities to stakeholder groups shaped by views of rights and justice. In the case of consumer safety, students can be encouraged to comprehend that consumer protection laws and the role of federal and state agencies in enforcing such laws are a vital part of the social contract between business and society. At this juncture, students are in a position to consider the power that corporations have to influence the laws that govern them through lobbying and other forms of political advocacy. On this macro level of instruction, it is also appropriate to emphasize the importance of the natural environment, the responsibility business has to preserve this host environment, and the critical role that public policy and government agencies, such as the Environmental Protection Agency, have in protecting the public interest in this area.

In other words, the social contract can be a logical starting point for conveying that the social value of commerce can be analyzed in terms of corporate responsibilities that are shaped by normative traditions, including utilitarianism, deontology, rights, justice as fairness, and environmental ethics. Concurrently, students can be introduced to some descriptive or factual elements of the business and society relationship, such as specific laws and regulations and corporate political actions that affect them.

After students have been exposed to this big picture or macro view, they are in a position to consider how corporations can facilitate the social value of commerce. This involves delivering instructional material at the organizational or midrange level of analysis as corporate social responsibilities or an organization's ability to respond constructively to stakeholder expectations that firms adhere to the law as well as ethical norms over and above the letter of the law. A key topic for teaching ethics at this level is moral leadership or the influence that executive leaders have in conjunction with their boards of directors in establishing socially responsible business practices, which might include some level of corporate philanthropy or discretionary responsibility. A learning goal in this area of corporate governance can be for students to understand the boundary-spanning mechanisms available to executives who seek to enact moral leadership, such as the office of public affairs for tracking and attending to stakeholder expectations of responsibilities and industrywide "best practices forums" aimed at instituting and maintaining collective ethical self-governance among peer firms.

A logical extension of this discussion is for the instructor to point out that an executive can work with his or her board of directors and an ethics officer to formulate and implement ethics compliance and training programs defined by an ethics code of conduct in conjunction with hiring procedures that screen potential employees for ethical standards consistent with socially responsible goals. At the same time, a classroom exploration of moral leadership can consider the role of the executive in establishing an ethical culture or climate in which employees or internal stakeholders are treated fairly, not only out of a respect for their inherent dignity as humans à la deontology but also because a firm's ability to respond constructively to external stakeholders and survive economically in that environment may depend on an internal culture of solidarity and commitment to such goals. It is at this level of instruction that the strategic, consequential, or instrumental aspects of ethics in corporate life can become clearer to students, especially since they can identify with their future roles as employees or managers.

Finally, business ethics instruction should illuminate how ethics in individual decision making relates to the social value of commerce and corporate responsibilities. For example, an instructor can explain the nature of ethical dilemmas individuals can face in organizations, as when whistle-blowers experience internal conflict in balancing a commitment to social responsibility with loyalty to their firms. Whereas the instructor can emphasize ethics as utilitarianism, duty, rights, and justice in the societal and organizational domains, it is appropriate to highlight virtue or character ethics and integrity at this individual level. Virtue ethics implies that moral managers and employees are those who have imbibed certain character traits, such as fairness, honesty, and benevolence, while the literature on integrity suggests that decision makers are able to use such characteristics coherently to establish publicly their trustworthiness and ability to make balanced judgments in the face of moral complexity. According to a dialogic perspective, this ability depends on being able to respect, listen to, and give voice to various stakeholder concerns. Perhaps the most important thing for students to appreciate at this level is that ethics in action depends to some extent on the cognitive ability of individuals to factor values and ethics consciously into decision making that is responsive to societal interests.

Lawrence Kohlberg's widely applied model of moral development can be used to reinforce this point. According to this model, there are three levels of moral development, each embodying two sequential stages of learning. Specifically, the preconventional level involves a focus on self based on a reaction to punishment and seeking of rewards, in Stages 1 and 2, respectively. If individuals learn to move beyond this self-centeredness to consider the expectations of others, then they are able to reason at the conventional level, conceptualized as Stage 3, or conformity to family and peer group conceptions of right and wrong, and Stage 4, or an adherence to the rule of law and custom. In comparison, a person who can reason at the postconventional level of Stage 5 is able to focus on humankind in terms of moral principles, including human rights, social contracts, and constitutional precepts that are broader than those embodied in immediate referent groups or a particular society's customs and laws. Stage 6, the apex of moral reasoning in Kohlberg's framework, is denoted by an ability to define right and wrong in terms of principles of justice, fairness, and rights that can be generalized to all humankind. Students exposed to this material may be able to grasp not only the other-regarding perspective that marks socially mindful decision making but also that they themselves should seek to develop the ability to reason beyond the confines of habit and legal custom. A consideration of this ideal may help prepare them for the dilemmas in international business environments where multinational corporations operate in developing countries that lack the legal or customary protections afforded workers and consumers in more advanced industrial economies. In other words, teaching business ethics involves preparing students for cultural variations in the social contract between business and society that define stakeholder expectations of corporate responsibility.

Delivering Business Ethics in the Curriculum

Methods of delivering ethics in business schools vary. Some schools require a stand-alone business and society or ethics course, some rely on infusing ethics across the curriculum, and others do both. In addition, schools can augment ethics content with extracurricular initiatives, such as hosting guest speakers, offering service learning projects, and establishing endowed chairs in ethics. As of this writing, most business ethics professors have gone on record as preferring that some kind of stand-alone ethics course be required in the curriculum. Their rationale is that a common body of knowledge delivered in a stand-alone course is the most effective way of ensuring that students are exposed to ethics material holistically in terms of consistent learning goals, which include the goal that students understand society's expectations of business responsibilities and the responses of corporations and their agents. The stand-alone course can then serve as a fulcrum for infusing ethics into other courses in specialized ways. Consider, for instance, that a discussion of the social contract in an ethics course can inform and give context to a presentation of socially responsible investment funds in finance. A stand-alone ethics course can also be foundational to extracurricular activities. For example, students who compete in national ethics case competitions will be better prepared if they have previously demonstrated a basic knowledge of ethics conveyed rigorously in a stand-alone course. Delivering such a course in the curriculum can also help ensure that students are able to discuss ethics knowledgeably with recruiters who increasingly expect potential employees to understand the evolving compliance environment for business shaped by Sarbanes-Oxley, Federal Sentencing Guidelines for Organizations, Securities and Exchange Commission rules, and other regulatory measures relevant to the social contract between business and society.

In terms of classroom pedagogy, there is a growing interest in teaching ethics with interactive learning techniques, including actual or simulated cases, computerized assignments, written assignments, and films or film clips. Notably, actual cases can be used to highlight corporate conduct on the societal, organizational, and individual levels so that students can inculcate an integrated understanding of how business ethics relates to practice. Another development in teaching ethics is the increase in courses offered in continuing professional education programs, particularly in accounting, which has experienced an exponential growth in states requiring ethics coursework as a condition for Certified Public Accountant (CPA) license renewal. As of this writing, a continuing education course in accounting ethics is required by a majority of states, whereas prior to the outbreak of corporate scandals and the demise of the accounting firm Arthur Andersen, only a few states mandated such a course. This development may prompt new teaching material designed specifically for the specialized needs of accounting practitioners.

Support for Teaching Business Ethics

There is no dearth of textbooks and support material for teaching business ethics. After new business ethics textbooks appeared in the 1960s in tandem with interest in reforming business education, a preponderance of textbooks became available. Whether labeled "Business and Society," "Corporate Citizenship," "Social Issues in Management," or simply "Business Ethics," these textbooks typically relate ethics to the societal, organizational, and individual domains described previously. In addition, many supplemental materials for delivering ethics in the curriculum are available, such as course or curricula descriptions and resources that lend themselves to interactive learning, including case studies, simulations, and films and film clips.

Journals devoted to the subject of teaching business ethics include the *Journal of Business Ethics Education* and *Teaching Business Ethics,* while other pedagogically oriented journals, such as the *Journal of Management Education* and *Academy of Management Learning and Education,* include ethics as a topical area. Other journals address the teaching of business ethics more indirectly by serving as a repository for research that can influence the content of textbooks and resource material over time. Examples in this category include *Business & Society, Business Ethics Quarterly,* the *Journal of Business Ethics,* and, to a lesser extent, *Academy of Management Review, Academy of Management*

Journal, and *Academy of Management Executive* and other journals geared to broader management topics. Publications such as *Business Ethics Magazine* and *Compliance and Ethics* are especially timely resources for teaching ethics in the classroom, given their focus on current events. Examples of associations that sponsor conferences that include presentations relevant to business ethics pedagogy are the International Association of Business and Society, Society for Business Ethics, and the Social Issues in Management and Organizations and the Natural Environment Divisions of the Academy of Management.

—*Diane L. Swanson*

See also Academy of Management; Accounting, Ethics of; Arthur Andersen; Association to Advance Collegiate Schools of Business (AACSB International); Certified Public Accountants (CPAs); Codes of Conduct, Ethical and Professional; Cognitive Moral Development; Corporate Citizenship; Corporate Social Responsibility (CSR) and Corporate Social Performance (CSP); Corporate Social Responsiveness; Deontological Ethical Systems; Descriptive Ethics; Dilemmas, Ethical; Duty; Economics and Ethics; Enron Corporation; Environmental Ethics; Ethical Culture and Climate; Ethical Decision Making; Ethics, Theories of; Ethics of Dialogue; Ethics Training Programs; Fairness; Federal Sentencing Guidelines; Integrity; Justice, Theories of; Kohlberg, Lawrence; Moral Education; Moral Leadership; Moral Reasoning; Normative Ethics; Power, Business; Professional Ethics; Regulation and Regulatory Agencies; Sarbanes-Oxley Act of 2002; Scandals, Corporate; Securities and Exchange Commission (SEC); Social Contract Theory; Socially Responsible Investing (SRI); Stakeholder Theory; Virtue Ethics; WorldCom

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Teapot Dome Scandal

The Teapot Dome scandal occurred during the administration of President Warren G. Harding. Albert B. Fall, secretary of the interior, secretly leased three federal oil reserves to several oil company officials in 1921 and 1922 and received personal compensation from them. This scandal and accusations of influence peddling and corruption by several of President Harding's political appointees resulted in congressional investigations and court cases that extended throughout that decade.

Underground petroleum reserves on federal government lands had been set aside for possible use in a national emergency by several previous administrations. Two of these oil reserves were located in California, and a third was near Casper, Wyoming. The property in Wyoming was called Teapot Dome due to the shape then of a rock formation on that land. Legislation in 1920 gave control of these federal oil reserves to the secretary of the navy. President Harding issued an executive order in 1921, though, transferring authority over these naval oil reserves to Fall, his secretary of the interior.

Without taking bids, Fall issued exclusive leases to Edward L. Doheny of the Pan American Petroleum Company for the two California reserves and to Harry F. Sinclair of the Mammoth Oil Company for the Wyoming property in 1921 and 1922. Rumors and accusations were raised concerning these transactions, and Senator Robert M. LaFollette of Wisconsin called publicly for action on these allegations. The U.S. Senate authorized an investigation in April of 1922 by its Committee on Public Lands. During the political tension over this scandal in 1923, Fall resigned as secretary of the interior in March, President Harding died in August, and Senator Thomas J. Walsh presided over a Senate investigation that began in October. After accounts of Fall's personal financial gain resulting from the oil leases began to emerge in Senate testimony in January 1924, President Calvin Coolidge announced his plans to nominate two special counsels, one Republican and one Democrat, to investigate further and prosecute. The Senate shortly thereafter passed a resolution charging delays and obstructions by the attorney general, Harry M. Daugherty, another Harding appointee, for his handling of the Teapot Dome investigation and for corruption and influence peddling within the Justice Department. Daugherty resigned in March 1924.

The three oil reserves were returned to the federal government by Supreme Court decisions in 1927. Fall was eventually convicted of bribery, was fined $100,000, and served less than a year in prison. Although oil company officials Sinclair and Doheny were not convicted of conspiracy, Sinclair was found guilty of criminal contempt for jury tampering in a later and related investigation. He also served a short prison sentence of less than a year.

The implications and significance of this scandal have drawn mixed comments from historians. Supporters of conservationist policies and critics of excessive business influence on government officials could claim to have prevailed in this controversy, but questions related to the appropriate roles of business and government in natural resource development and planning remain unresolved.

—Stephen L. Payne

See also Corporate Political Advocacy; Enron Corporation; Metallgesellschaft; Savings and Loan Scandal; Scandals, Corporate

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Telecommunications Act of 1996

The Telecommunications Act of 1996 attempted to bring more competition to the telephone market for both local and long distance service. It permitted firms that served competitive local markets to enter the long distance market, and it attempted to implement a single layer of regulation at the federal level. However, some state and local regulation will exist for years to come.

The deregulation that was brought about by this act enabled competition within the local exchange areas that had been effectively monopolies for many years. It also provided new regulations such as forcing the local carriers to share their communications facilities with competitors at rates established under the act's guidelines and ensuring that each competitor was treated in a fair and equitable manner.

Additional provisions of the act removed restrictions on media ownership and resulted in immediate consolidation within that segment of the industry. Yet another provision provided guidelines for Internet indecency, but the Supreme Court ruled that provision was unconstitutional under the First Amendment. Another significant provision also protected Internet service providers from liability for content of third parties on their service.

This act had many far-reaching effects. It eliminated the firmly entrenched monopoly that had been in existence on local and long distance telecommunications services. This provision effectively opened the local markets to long distance carriers, cable television providers, and other local carriers. The act permitted local telephone companies to provide long distance services when they could prove that local competition existed in their existing markets.

As a result of this legislation, many direct benefits are being realized today. Businesses have seen a reduction in communications costs as they have leveraged the competitive environment to restructure their communications platforms and services. Along with the reductions, these businesses have purchased new tools and services to increase productivity. These new services have forced the adoption of and adherence to many new standards. These standards make it easier for consumers to move between carriers and to be assured that mobile devices can work wherever the user is located, even worldwide.

The act has addressed some ethical implications as well. It has restricted advertising and marketing campaigns by the larger companies to foster competition. Another stipulation required that services between carriers be provided on a cost-plus basis and that those costs be the same to all carriers in the area. It also required wholesale services to be unbundled, which forced the local carriers to provide only the specific service needed. To ensure a truly competitive environment, carriers were required to allow the consumers to take their phone number with them as they changed carriers. Other provisions required reciprocal compensation for calls between carriers.

Finally, the act called for all carriers to maintain equal quality and timeliness or parity among all carriers in providing local services including directory assistance, operator assistance, E911, new telephone number access, installation time frames, repair services, and repair time frames. All have to be provided under the same conditions as the incumbent will provide these services to direct customers. Violation of this provision results in heavy fines and potentially the denial of the right to provide other services.

—Deborah Britt Roebuck

See also Adelphia Communications; Mergers, Acquisitions, and Takeovers; Public Utilities and Their Regulation; U.S. Department of Justice

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Teleopathy

Teleopathy is the unbalanced pursuit of purpose by either individuals or organizations. This mind-set or malaise has been described as an occupational hazard of business life and the key stimulus to which business ethics is a response. Its three principal symptoms are fixation, rationalization, and detachment.

Fixation

Unlike determination, perseverance, and tenacity, which are often considered positive traits of both individuals and organized groups, fixation is usually regarded as a negative trait, akin to obsession, addiction, and dependency. This negative trait involves the domination of a person's consciousness (or an organization's culture) by a persistent goal, objective, or desire—out of proportion to its importance in the larger scheme of things. Fixation is a kind of misplaced devotion or loyalty that in philosopher Immanuel Kant's language ultimately entails treating the self as a means, not an end.

Rationalization

Often when fixation is present, rationalization is not far behind since rationalizing means offering superficial reasons for behavior when more honest reasons might elicit criticism. Rationalization is typically a temporary form of self-deception or "denial," allowing individuals or groups to suspend normal moral inhibitions when taking action. Two broad types of rationalization are common in business settings: One departs from fiduciary obligations to shareholders (market rationalization), and the other departs from law and regulatory permissibility (legal rationalization).

Detachment

When fixation and rationalization are repeated on a regular basis, they become habitual (or cultural), resulting in a kind of indifference to the human impacts of decision making. Head and heart become disconnected. Objectives become idols; obstacles become threats; second thoughts are silenced—and eventually, second thoughts disappear.

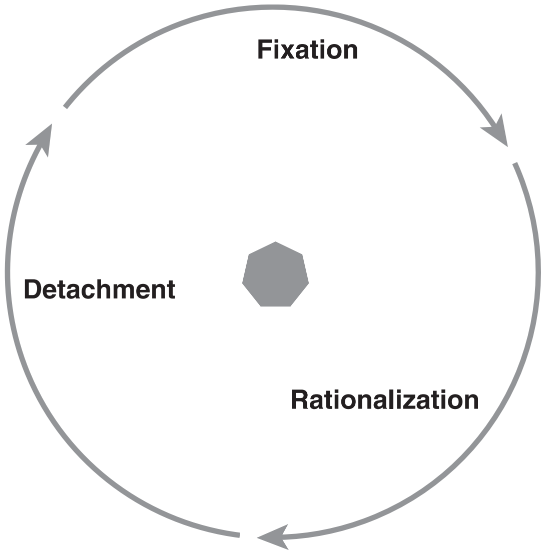

Figure 1 Teleopathy Manifested in Three Symptoms: Fixation, Rationalization, and Detachment

Illustrations

Examples of teleopathy in the behavior of both individuals and organizations are not hard to find (e.g., Jeffrey Skilling and Andrew Fastow, senior executives of Enron; Bernie Ebbers, CEO of WorldCom; and Dennis Kozlowski, CEO of Tyco). The corporate scandals of 2002 resulted in the Sarbanes-Oxley Act, aimed at mitigating abuses in accounting and financial reporting. In the wake of the 2003 crash of the *Columbia* space shuttle, the Columbia Accident Investigation Board (CAIB) indicted the organizational culture, accusing NASA of shortening the launch schedule for a critical section of the space station to meet an overarching goal. The presence of fixation, rationalization, and detachment in these cases is apparent. Less apparent is the antidote to the malaise. Market forces, laws, and regulations are necessary but not sufficient. The prevention of teleopathy must ultimately be personal and cultural. This means moral awareness and corporate conscience, two essential requirements of business leadership.

—Kenneth E. Goodpaster

See also Amorality; Authenticity; Autonomy; Business, Purpose of; Conscience; Corruption; Enron Corporation; Free Will; Human Nature; Loyalty; Moral Agency; Moral Leadership; Scandals, Corporate; Vice; Virtue; WorldCom

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Terrorism

Terrorism is the exercise of unconventional violence to achieve political objectives. What fits this simple definition is a matter of considerable dispute. Often, those in positions of political power characterize as terrorism those challenges to their established political authority that—rather than employing conventional means to political change, from peaceful discourse to declared warfare—employ violent, frequently surprise, attacks, in some cases on innocent civilian targets. Those who incite, endorse, or commit such attacks may defend them on ideological or religious grounds as the most expedient way to make a statement and effect change against a more politically, economically, or militarily powerful adversary. They may contend that the real terrorists are those in political power who engage in overt or covert military action and political maneuvering to defend and consolidate their authority.

Anywhere it is a threat, terrorism disrupts the ordinary rhythms of life, causing the mother to worry about the safety of her children in public places and the business traveler to second-guess the necessity of a trip, resulting in large-scale consequences for human well-being and economic welfare by infecting daily behaviors with fear and uncertainty. In contemporary, developed markets, it is asymmetric terrorism that is most economically disruptive and which is therefore the primary focus of this entry—especially the September 11, 2001, attacks on the United States. The politics of this kind of terrorism are largely motivated by global economic inequality and associated resistance to perceived cultural imperialism. In a broad sense, the victims of terrorism are not only those whose lives and interests are lost or harmed by terrorist attacks, but also all those whose well-being is at risk as a result of conditions that breed terrorism.

History, Forms, and Economic Impact

Terrorist acts are committed by isolated individuals, one of the hypothetical profiles of the anthrax murderer who sent the global postal system into hysteria with a few contaminated letters in the weeks after September 11, 2001; by well-coordinated, multinational networks, such as al-Qaeda—the organization responsible for the September 11 attacks using airplanes to destroy the World Trade Center and part of the Pentagon; and by the many possibilities in between. Undoubtedly, terrorism dates back to unrecorded history, but there are early examples of terroristlike behavior in the *Iliad*, for example, in Hektor's threatened desecration of Patroklos's body and Achilles' treatment of Hektor's body in revenge—notwithstanding that both deaths occurred in the course of declared warfare. Both the state's violence against its enemies in the French Revolution and the secessionists' violence against the state in the American Revolution have been raised, not without controversy, as examples of how, in modern times, terrorist tactics have effectively tipped the balance of power relations to advance political aims. In recent decades, political factions described as terrorists by the reigning political powers have managed to cause persistent political agitation over the course of decades, leading to neither outright victory nor failure. Examples include Hamas in Israel, Hezbollah in Lebanon, the Shining Path in Peru, Tamil Tigers in Sri Lanka, Euskadi Ta Askatasuna in Spain, and the Irish Republican Army in the United Kingdom.

Violence or threats of harm to human beings can be committed by terrorists, using means from primitive weapons and makeshift explosives strapped to suicidal agents to rare chemical and nuclear materials. Other terrorist means may include spreading computer viruses and attacking critical infrastructure elements such as power and transportation, disrupting the flow of economic and other human activity without direct injury to persons. Characterizing terrorism as exercising unconventional violence raises the question of what form of violence is conventional and what makes it more acceptable than the unconventional kind. Along with the political controversy over defining terrorism, there is philosophical controversy around why precisely it is bad and whether, if all nonterrorists agree that it is bad, it can ever be morally justified—even as its perpetrators often cast their activities as fulfilling moral and religious obligations.

Given the variety of its forms and the dispute about what it is, it is not possible to estimate reliably what the economic costs of terrorism may be. However, they are indisputably monumental, and growing, as social tolerance for uncertainty decreases while the potential damage that a single act can cause increases. One conservative estimate suggests that the insured losses caused by the September 11 attacks were greater than $40 billion, while the direct costs of increased security for risk mitigation will be, over time, orders of magnitude greater, not even factoring in the indirect costs of economic disruption.

Economics, Ethics, and Terrorism

It is evident, then, that there are difficult economic problems regarding the costs of terrorism, as there are troubling ethical problems about the moral status of terrorism. Setting those problems aside for resolution elsewhere, our focus here will be particularly on the intersection between all three—economics, ethics, and terrorism. For although terrorists tend to foment passions about political unfairness, religious irreverence, and military injustice, in many cases, the conditions that produce the kind of extreme communal anger that drives groups of terrorists to collective action—which can cause sustained damage, economic and otherwise, over time—have much to do fundamentally with global economic inequality, in which privilege and poverty coexist. This is not at all to say that poverty always leads to terrorism, that poverty is the only cause of terrorism, that poverty ever justifies terrorism, or that terrorism is always an effective equalizing measure. However, social scientists and political commentators have noted repeatedly that the contemporary terrorist movements that pose the greatest threat to the global economy today are fueled by extreme anger among primarily young men from failed states who are hopeless about their communities' chances of achieving relative material self-sufficiency on earth in the shadow of perceived Western, especially American, interference. Recruited from all elements of society for the promise that their anger can be cultivated into extremism, they may conclude that their prospects of being an antiestablishment hero or of being rewarded in an afterlife paradise outweigh the risks of being a terrorist.

Not that all terrorists are materially destitute. Another way in which economics, ethics, and terrorism intersect is in financing for terrorism. While material well-being may be a general disincentive to engage in terrorism, some leaders of terrorist factions have themselves been quite well off. Much of al-Qaeda's early funding, for example, is said to have come from the economically successful family construction business of its leader, Osama bin Laden, who left the peaceful comforts of upper-class Saudi society to become the world's most wanted terrorist. Moreover, bin Laden and his followers have been able to raise funds for their continued operations, much of it coming from the business profits of wealthy sympathizers whose resentment, like bin Laden's, is directed at the culturally and militarily imperialistic effects of Western economic dominance. Although al-Qaeda and its allies justify their actions with the rhetoric of religious *jihad*, it is doubtful that their popular following—which enables them to recruit martyrs, raise funds, attack, and continuously hide from capture and destruction—would be as strong without the accompanying conditions of poverty, unemployment, and lack of material hope.

Even as bin Laden's enemies sought to isolate him physically and economically, the continued pipeline of funding for al-Qaeda raised concerns that al-Qaeda's targets—especially, the United States—were funding both sides of the war on terror. As the United States spent money to mitigate the terrorist threat, its dependence on oil from countries with ties to al-Qaeda meant that some of its spending circuitously reached the hands of terrorists. With similar historical irony, the United States once supported the cause of bin Laden's *mujahideen* allies in Afghanistan when their common enemy was the Soviet Union.

Clamping down on funding for terrorists has led political powers to enlist businesses in the war on terror, creating a legal obligation for business to expend resources on mitigation of terrorism risk. For example, shortly after the September 11 attacks, the U.S. PATRIOT Act was signed into law, imposing costly preventive and detective activities to support prohibitions on transacting with terrorists. The surveillance provisions in such legislation led to controversy about the balance between national security and citizens' privacy rights. Further blurring the lines between public interests and private spending, lawmakers in various jurisdictions have enlisted the cooperation of business regarding the security of global supply chains, safety of citizens, and other public goods touched by private enterprise.

While such security provisions have imposed substantial costs on business, terrorism has also created economic opportunities in some industries. Demand for terrorism insurance ebbed and flowed after September 11, creating an uncertain market in which some insurers sold policies without having to pay claims, while the uneven demand made affordable pricing troublesome without government intervention. Immediately after September 11, faced with ethical questions about whether to pay out life and property claims to victims given the extraordinary nature of an event that was not contemplated or documented in most policies, the insurance industry was generally credited with responding honorably. Meanwhile, the demand for defense contractors' products and services increased with growing warfare and the need for new security technologies, leading in a few cases to the age-old misbehavior of overcharging governments in times of great chaos. Some manufacturers responded to the perceived terrorist threat with necessary innovations, such as improved airline baggage screening equipment, while others exploited public fear and sentimentalism, with products ranging from questionably effective skyscraper parachutes to questionably tasteful memorabilia.

One idea that tragicomically illustrated the complicated balance between economics, ethics, and terrorism was a proposed predictive market sponsored by the U.S. Defense Advanced Research Projects Agency. The market was purportedly based on sound economic theory and practice, that market mechanisms can have predictive value when individuals place monetary bets on future events, insofar as they are more likely to risk more capital on the probability that something will occur when they are in a position to render an educated hypothesis. Applying predictive markets theory to terrorism, the policy analysis market came to be caricatured as a "terrorist futures" market. Once its details were disclosed to public figures, it was cast as so ethically repugnant as to be shut down almost immediately, leading to the resignation of the head of the Terrorism Information Awareness program.

September 11, 2001

Nearly 3,000 people from all levels of the economic pyramid died on September 11, 2001, in most cases because that day they had shown up for work. In the "Portraits of Grief" published by the *New York Times* in the weeks and months after the attacks, there were recurring sentiments expressed by survivors of how work was in many cases a means to the end of a better life—more time with family, pursuit of education, enjoyment of leisure and play, and in numerous cases, helping others, at home and abroad, who needed material support. The September 11 Victims Compensation Fund, established by the U.S. government to provide monetary benefits to victims' families roughly commensurate with anticipated future earnings, raised ethical questions about what a life is worth and whether the wealthy bond traders at the top of the World Trade Center deserved more than the firefighters who climbed the stairs from the bottom to try to save lives; than the wait staff at Windows on the World, who searched in vain for water to comfort suffocating patrons; or than the homeless man who wandered the ground floor corridors as though they were sidewalks.

Within the "city in the sky" that was the World Trade Center, where tens of thousands of people worked and thousands more visitors coursed through each day from nearly every nation, the specter of economic inequality was ever present but not immediately evident to the typical, hurried office worker. The Twin Towers had been attacked by terrorists once before, on February 26, 1993, vulnerable because of their symbolism of American economic might. When they came down in 2001, virtually shutting down with them the global economy, some responded that they should be rebuilt as soon as possible. The argument continued that the economy should remain open for business to demonstrate that terrorists could take down buildings but could not fundamentally alter the way of life they were attacking. Others, no less critical of terrorism waged on innocent people, responded to the tragedy by reflecting on that way of life. They explored the meaning of work within the good life and sought ways in which to share the economic benefits of world trade beyond the economically privileged nations and economically privileged classes within those nations. Terrorism is not to be credited with motivating solutions to the problem of global economic inequality; however, eliminating the extreme inequality that persists today will go a considerable distance toward future elimination of extremist terrorism, which threatens global well-being.

—Christopher Michaelson

See also Economics and Ethics; Income Distribution; Meaningful Work; Poverty; Public Goods; USA PATRIOT Act

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Tobacco Industry

See Ethics and the Tobacco Industry

Tort Reform

Tort reform encompasses the litany of legislative attempts to limit the extent of civil liability in tort cases, particularly product liability cases. Manufacturing businesses, doctors, and their insurance companies are the major proponents of these efforts to limit expenses related to product liability injuries. Employment law, securities fraud, medical malpractice, and environmental issues also constitute the area of tort cases and their related reforms. Both federal and state legislatures have passed a variety of statutes that attempt to modify the alleged imperfections of the court's tort system.

History of Tort Reform

As a developing United States sought economic stability, *caveat emptor* (let the buyer beware) was the guiding legal principle in civil liability cases. The Industrial Revolution, with its ability to distribute products to a vast array of consumers, required a rethinking and extension of product liability laws through warranties in contract theory and under the doctrine of negligence in tort. The latter proved significant in that privity of contract was not required so that nonpurchasing users and bystanders could recover for injuries caused by a certain product. In the early 1960s, strict liability in tort was recognized and led to an explosion in lawsuits, including class actions in relation to asbestos and other products. As the economy and particular industries such as insurance struggled during the 1980s, affected businesses, doctors, insurance companies, and their political representatives called for tort reform as a remedy. Subsequently, legislative debate and reform has occurred at both the state and federal levels in a number of areas of concern in tort actions.

Current Legislation

Current tort reform legislation exists at both the state and federal levels. The American Tort Reform Association provides an updated sampling of state reforms in the primary areas of punitive damages (32 states), noneconomic damages (23 states), joint and several liability (40 states), collateral source rule (23 states), prejudgment interest (15 states), product liability (16 states), class action (8 states), attorney retention (7 states), appeal bond (33 states), and jury service (12 states).

Federal legislation has focused on civil liability protections (via limited liability and federal jurisdiction) for industries most susceptible to economic risk. For example, the insurance industry, air security companies, air transportation businesses, the financial securities industry, medical device providers, Amtrak, credit unions, vaccine providers, the nuclear power industry, and coal mining companies all receive some sort of federal protection. The federal government seems to justify the legislative shelters granted these specific industries because of their significant economic vulnerability in the current commercial climate. For example, insurance companies (mid-1980s), air transportation (post 9/11), and the financial securities industry (early 21st-century accounting frauds) have each faced a major financial crisis recently. The federal legislation was enacted to ensure that these industries would not be completely devastated by their respective predicaments and could continue providing their invaluable services to society. Other federal laws protect teachers, principals, volunteers, donators of food, and federal drivers to make certain that they may keep on offering their socially desirable and essential services without interruption. The economic rationale for these legal safeguards is to compensate for the inability of the listed service-oriented enterprises to generate any significant self-protecting income, more than it is to address any extreme crisis. Stricter controls on class-action suits is the most recent tort reform to find favor in Congress as of 2005.

Tort Reform Proposals

Proponents of tort reform suggest a variety of methods to reduce the costs associated with product liability cases. Obvious examples include implementing a limit to the amount of damages one may receive in any case and the elimination of strict liability (responsibility regardless of fault), returning to the negligence standard in all cases. Other recommendations include placing limits on the amount recoverable for pain and suffering, restricting lawyers' compensation (with greater correlation to the actual recovery of clients), requiring losing plaintiffs to pay defendants' legal fees (with even greater punishment for frivolous lawsuits), ending joint and several liability (ability to recover the entire amount of damages from any one of the culpable defendants), and abolishing or limiting punitive and other noneconomic damages, especially for products approved by regulators. Procedural suggestions hope to diversify and broaden jury pools, restrict the collateral source rule so that insurance or workers' compensation recovery will be both admissible and an offset of damages, limit the amount of appeal bonds and prejudgment interest, reduce the statute of limitations and statute of repose, increase the burden of proof, use more stringent evidentiary rules, and establish an efficient form of alternative dispute resolution. To avoid political partiality and inflated fees, attorney sunshine laws seek to require legislative approval of large contingency agreements when states sue for reimbursement against certain businesses (e.g., the tobacco lawsuits).

Arguments in Favor of Tort Reform

The protection of business from the sometimes overwhelming legal costs of product liability is the major argument in favor of tort reform. These costs then have a negative ripple effect on dependent businesses, consumers, and other stakeholders in society. The argument states that prices increase, innovation decreases, jobs are lost, and all citizens are essentially taxed by the costs to support the inefficient tort legal system. Tort reformers believe that frivolous lawsuits burden business and impair the economy and that even legitimate lawsuits disproportionately benefit the lawyers instead of the actual victims. The tort system itself is criticized for an inefficiency that spends billions of dollars without awarding a significant percentage of that amount to injured parties. The tort system, tort reform advocates say, benefits trial lawyers more than the actual victims, especially in class actions where the percentage of successful claimants who receive their awards is surprisingly low. In addition, personal injury claims seem to vary in value from one state or jurisdiction to another, creating inconsistencies in insurance rates and jury awards. A uniform federal tort reform law arguably rectifies such irregularities. Finally, tort reform would prohibit the controversial effort to "legislate through litigation," that is, the attempt to bring about regulatory changes and objectives through litigation instead of through the legislative process. The increase in the number of tort cases, the number of attorneys, and the amount of monetary awards are all cited as causes for the escalation in overall costs to the tort system.

Arguments Against Tort Reform

Plaintiffs' trial lawyers (and consumer advocates) opine that businesses should be held responsible for their products so that they are motivated to make better and safer products over which they have ultimate control. Businesses are also in a better position to absorb and assume the costs associated with injuries caused by their products. They can also pass on those costs to consumers. Also, to truly stimulate companies to manufacture safer products, be more forthcoming, and respect the environment, the monetary damages for injurious products and the risk of placing such products in the market need to be appropriately high. The entire litigation process lends itself to an increase in information and punishment that leads to safer products and practices. Thus, the tort system regulates business in a manner that efficiently complements the functions of official governmental regulatory agencies. Furthermore, enormous debilitating verdicts against business are indeed rare and often reduced on appeal even when they do occur. Tort reform, according to its critics, would simply insulate businesses from their legal and social responsibilities.

Conclusion

Both federal and state legislatures have passed a variety of statutes in an attempt to rectify the imperfections of the tort system. The remedies consist primarily of methods of reducing the overall costs related to such litigation. There also exist some procedural rules designed to promote more equitable resolutions. Because tort reform is essentially a recent historical development (since the 1980s), it will naturally take a little time to discover its most effective manifestation. Both the positions in favor of and against tort reform testify to its legislative immaturity.

One major challenge to the current tort reform debate is the dearth of agreed-on data that would provide a starting point for a constructive discussion between the advocates and dissenters. Verifiable statistics about legal costs, job losses, safety benefits, and attorney and claimant rewards seem to be a must before real headway can be made in the controversy.

Tort reform also indirectly raises the question of federalism versus states' rights. If reform is really the solution to tort liability concerns, should the federal or state government be the primary conduit of implementation? And is the primary role for business regulation incumbent on the legislature or on the free market system itself? In a real sense, tort liability and tort reform mirror the current question about corporate social responsibility: To what degree shall business be held responsible for injuries to the public in connection with unsafe products, financial fraud, deceptive advertising, and environmental degradation? And is tort law a desirable form of legal insurance for social mishaps, or is tort reform a necessary guardian for economic prosperity? Tort reform seems to be in an awkward stage of requiring companies to fairly compensate injured claimants without burdening businesses to the point of bankruptcy and allowing a minority of overzealous lawyers to exploit the imperfections inherent in the system.

—Mark R. Bandsuch

See also Compensatory Damages; Contracts; Due Care Theory; Duty; Liability Theory; Negligence; Product Liability; Property and Property Rights; Punitive Damages; Torts

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Torts

Torts are civil wrongs in violation of a protected interest or right (and its related duty), other than a breach of contract. Intentional torts, negligence torts, and strict liability torts make up the three primary classifications of torts. Assault and battery, automobile accidents, and faulty consumer products are a few of the many sources of torts. Torts usually involve the violation of an individual's right to bodily security or property interests, the legal guarantee to engage in (or refrain from) certain conduct, or the right to receive (or be protected from) specific treatment from another. The infringement of a said noncontractual right and violation of its related duty is a civil wrong or legal tort (derived from the same French word, which means "to twist"). The same action may be both a civil tort and a crime (e.g., an assault). The courts and law remedy civil torts with monetary damages and injunctions.

Social and Ethical Implications

The most basic social and economic relations require a respect for one's bodily safety and for one's property interest. Tort law has traditionally provided a moral minimum of behavioral guidelines toward a variety of personal and property rights. The enforcement of torts has historically protected said rights, deterred infringement of related and future interests, and compensated for violations thereof. Besides the obvious rights and utilitarian foundation for the protection of such tort interests, the structure of tort law advances both compensatory and distributive justice.

Tort protection of property and bodily rights advances the economic efficiency on which society depends for its overall development. Tort law tries to reduce the costs associated with the injuries connected with the violation of said rights and with the expense inevitable in preventing them. This goal is achieved partially by a tort system designed to award damages in a manner and through an amount that promotes precautionary protection of important personal rights and property interests. Tort law awards monetary damages to individuals whose rights have been violated by the intentional destruction of their property, the accidental injury to their physical person, or their sickness caused by a defective product. Greater security in said rights is a natural outgrowth of the tort system's fair process and substantial sums afforded to the injured and of the compensatory and punitive damages inflicted on both present and future perpetrators. The freer flow of information and increase in safety are said to further testify to these benefits. Plus, the opportunity to have one's day in court protects the notion of justice inherent in the legal system and the nation for which it was founded.

However, many argue that the compensation is overly punitive, that it essentially results in a tax on consumers, and that it discourages technical innovation. Strict product liability in tort is the starkest example of these criticisms since it imposes legal liability on businesses even if they exercise ordinary care. Thus, under the notion of distributive justice, strict liability places the costs of both the injuries and the prevention on the businesses in part simply because they are arguably better situated to insure against them and redistribute said costs to a large number of consumers.

Intentional Torts

Intentional torts derive their name and classification from the fact that the perpetrator (or *tortfeasor*) intended to commit the wrongful act or intended to bring about the wrongful consequences (or knew with substantial certainty that such consequences would occur). Intentional torts are committed against either a person or a person's property. Intentional torts against a person's right to bodily security consist of assault (creating apprehension of immediate harmful or offensive contact), battery (unwelcome, offensive contact), false imprisonment (restraint of another's freedom without good reason), and intentional infliction of emotional distress (caused by an extreme and outrageous act). Common examples include physical altercations between coworkers and the prolonged and uncomfortable detainment of shoplifters.

Other intentional torts against the person, but not the person's bodily rights, include malicious prosecution, defamation (false, negative communication that damages a person's reputation through written libel or oral slander), invasion of privacy (by intruding into a person's individual affairs, publicly disclosing private facts or information that places a person in a false light, or misappropriating a person's name or likeness), and fraud (knowing misrepresentation of material facts). Celebrity gossip magazines occasionally give rise to these torts. Newsworthy public figures relinquish part of but not all their privacy in the eyes of the law.

Intentional torts particular to business include wrongful interference with contractual or business relationships and trade disparagement. Conversion (civil theft), disparagement of property, private nuisance (inhibiting enjoyment of one's property), and trespass on land or personal property encompass a few of the intentional torts against a person's property. Although the violation of the protected rights by itself is enough for receiving compensation for an intentional tort, damages will be awarded in relation to the severity of the injury to the person or the person's property.

Defenses to intentional torts include consent, defense of self, others, or property (with the degree of force limited to what is reasonably necessary), recovery of wrongfully taken property, merchant's privilege to detain, and private and public necessity (in cases of emergency). These defenses excuse legal responsibility for the intentional transgressions of individual rights.

Last, it should be noted that torts committed in cyberspace are a growing phenomenon. Although traditional media such as television, radio, magazines, and papers could be held responsible for defamation, the same is not true for Internet service providers (ISPs). The Communications Decency Act of 1996 essentially insulates ISPs from liability for defamatory postings, destructive viruses, spam, and e-commerce gone awry. Conversely, the originator of these injurious actions could be held liable under traditional tort theories.

Negligence

Like intentional torts, negligence involves an act that wrongfully violates a protected right in one's property or person. However, contrary to intentional wrongs, negligence describes unintentional tortious acts that violate one's duty to exercise ordinary care under the circumstances (also referred to as due care or reasonable care). The degree of care required varies in relation to a reasonable person under the circumstances. For example, legal responsibility for a delivery person's driving accident will depend in part on whether she was driving reasonably under the circumstances of the road, weather, and traffic. Most jurisdictions will hold professionals (like doctors, lawyers, and accountants) to the reasonable skill and knowledge level of someone in that profession. Thus, malpractice is negligence by a professional. Another difference between intentional torts and negligent torts involves the requirement that the duty-breaching act cause the injury to the protected right. This "causation" condition is automatically satisfied where intent is found because intent includes the desire to bring about the consequences. But negligent acts are unintentional by their very nature in that they do not anticipate or intend the harmful consequences. Yet, the law imposes liability for such behavior to hold people responsible for their actions, to promote a certain standard of care within society, to compensate individuals injured by the actions of another, and to influence others to guard against future possibilities of negligent indiscretions. Most states enforce responsibility for negligent actions that "proximately cause" the injuries in question. Proximate cause has been defined by most courts as existing when the consequences were reasonably foreseeable; that is, a reasonable person should know that the action could result in the potential injurious consequences. A minority of states find legal causation when the act is a "substantial factor" in bringing about the injury. If a driver is speeding or driving haphazardly, injuries resulting from such driving would most likely satisfy causation since it is reasonably foreseeable that that type of driving would result in an accident and injuries to another.

To receive compensation for another's negligence, an actual injury to one's person or property must have occurred. This requirement further distinguishes negligence from intentional torts, which allow recovery for the intentional violation of the right itself without requiring an accompanying physical injury (intentional infliction of emotional distress being an exception in some jurisdictions). The amount of damages awarded will, of course, depend on the seriousness of the injury and the level of negligence. Punitive damages may be awarded when the *tortfeasor* is found to have been malicious or grossly negligent, that is, exhibiting a reckless disregard or indifference to the rights of and consequences to others. Punitive damages are usually given in an effort to discourage any similar future wrongdoing by the particular or potential defendants.

Defenses to Negligence

The primary defenses to negligence, those circumstances that excuse legal liability even though one failed to exercise ordinary care, include assumption of the risk and comparative negligence (with contributory negligence also remaining in a minority of states). Although technically not a defense, exercising ordinary care under the circumstances (and thus not being negligent) is the most obvious way a defendant avoids liability. Since proximate cause is needed to impose negligence liability, a superseding or intervening event that breaks the chain of causation is a defense to any additional damages subsequent to such an intervening event. For example, a driver who negligently injures a person in a car accident is not responsible for any additional injuries resulting to that individual during the subsequent ambulance ride that results in a second accident.

Assumption of the risk, which can be express or implied, relieves liability when and because the injured party is aware of and assumes an ordinary risk (but not a peril that is extraordinary). For example, a worker may venture into a construction area that she clearly perceives as containing some degree of danger. She will usually be precluded from recovering for any injuries resulting therefrom since she was or should have been aware of the risk and thus assumed it voluntarily.

Comparative negligence is a defense that reduces the amount of damages recoverable from an act of negligence by the percentage of negligence apportioned to the injured party's own careless actions. For example, if an injured party who suffered $100,000 worth of injuries is found to have been 20% responsible for his own harm, then he will only receive $80,000, his overall recovery being reduced by his comparative negligence. Some states honor this proportional reduction all the way to 1% (which obviously raises the possibility of the plaintiff being liable to the defendant). Other states, meanwhile, permit the plaintiff to recover only if the plaintiff's negligence is not more than (or sometimes not equal to) the defendant's. Maryland, Alabama, Virginia, North Carolina, and the District of Columbia do not yet follow comparative negligence, still adhering to the doctrine and defense of contributory negligence, which precludes any recovery whatsoever by the injured party when his or her own negligence contributed in any degree to the injury (unless the defendant still had a last clear chance to avoid said injury).

Particular Negligence Doctrines

Most of the following special negligence doctrines impose (or excuse) legal responsibility under very specific circumstances. *Respondeat superior* holds an employer vicariously responsible for the tortious actions of its employees or agents while they are acting within the scope of their employment. *Res ipsa loquitur* creates a rebuttable presumption of negligence when the circumstances surrounding the injury indicate that negligence occurred. The injury resulting from a violation of a statutory duty results in *negligence per se* when the statute designates it so. The *danger invites rescue* doctrine holds the negligent party additionally responsible for any injuries suffered by someone trying to help the party originally hurt by the negligent individual. *Good Samaritan* statutes protect people who try to help others in need from actions of negligence unless their efforts were reckless. Each of these special doctrines represents public policy decisions made to compensate society for (and protect it from) harmful events that need to be more precisely addressed within the context of negligence theory.

Strict Liability

Strict liability (or no fault) in tort essentially imposes legal liability for certain types of actions and their resultant injuries on the actor, regardless of his or her lack of negligence or intent to injure. A presumption of responsibility is placed on individuals in certain legally identified circumstances (e.g., abnormally dangerous activities and the distribution of defective products) because of the seriousness of the potential injuries (as to quality or quantity) and because the primary ability to prevent such injuries seems to reside with the actor. Strict liability is imposed on these individuals even if they exercised ordinary care under the circumstances and would not be legally responsible for negligence because the belief is that with their primary control over the situation or injury-inducing subject matter they have both the duty and the ability to prevent such injuries. In formalizing the legal obligation under strict liability, policy makers endeavor to persuade potential plaintiffs to take appropriate safety precautions.

Strict liability in tort was originally (and continues to be) applied to ultrahazardous or abnormally dangerous activities involving dynamite, chemicals, radioactive materials, and wild or dangerous animals. The high risk, potential seriousness, and uncommon nature of these activities led logically to legal liability irrespective of fault. More recent public policy concerns have led to strict liability being applied to certain types of copyright infringement cases. But by far, the most significant and controversial areas of strict liability are found in strict product liability.

Strict Product Liability in Tort

Although contract warranty and negligence law had methodically been chipping away at the doctrine of caveat emptor (let the buyer beware) since the beginning of the 20th century, it was not until the mid-1960s that the law seriously eviscerated most historical protections when the doctrine of strict liability in tort was extended to a variety of products during the consumer protection movement. Section 402A of the Restatement (Second) of Torts, issued in 1964, articulated that strict liability awaited sellers of products in a defective condition that was unreasonably dangerous. In 1997, the Restatement (Third) of Torts: Products Liability clarified the meaning and application of defective products to include defects in manufacturing, design, or warnings, which together encompass packaging, instructions, testing, and pretty much everything else surrounding the production and distribution of a product. Because the doctrine is based on tort theory and not on contract law, every party in the chain of distribution (manufacturers, assemblers, packagers, wholesalers, distributors, retailers, and lessors) is strictly liable for its role in the distribution of a defective product to anyone injured (i.e., every consumer, user, purchaser, lessee, family member, guest, employee, indirect beneficiary, or bystander) by its use and foreseeable misuse (including accidents reasonably foreseeable from any use). The business community and its insurers, realizing the potential breadth and severity of this liability, have proposed reforms in strict liability laws since the 1980s.

Defenses to Strict Product Liability

As "strict" as product liability law may appear, the doctrine does not impose absolute liability. Defenses against strict product liability do exist, providing protection from legal responsibility under certain circumstances. For one, the seller is not responsible for commonly known dangers found in an obviously and unavoidably dangerous product. This defense protects businesses from responsibility for injuries related to things such as knives and hammers but does not excuse liability for ultrahazardous activities. Another defense applies when the defective product is bought by a sophisticated purchaser since this person is expected to be especially aware of the product's risks. Also, protection from strict liability may exist if the product (like certain medicines) is considered safe according to the best scientific knowledge at the time since the law does not desire to hold someone responsible unfairly for an unknown danger. Comparative negligence is still technically a defense against strict liability in that it can reduce the amount of damages recoverable.

Conclusion

The three primary categories of tort law are intentional torts, negligence torts, and strict liability torts. Each plays a significant part in moderating the social and economic relationships among society's stakeholders. Although all three doctrines, like most laws, have a strong ethical basis in rights, duties, consequences, and compensatory justice, it is the more recent development of strict liability that seems to use Rawlsian distributive justice as a justification.

Business has realized an inordinate amount of benefits in postindustrial age society, while workers and consumers have borne the brunt of its burdens. Strict liability in tort seems to be one way the legal system tries to protect society from further potential injustices. Or restated more benignly, the tort system promotes protection of important personal and property interests by redistributing the cost of prevention primarily on the businesses because they are better positioned to protect against such injuries with their expertise, control, and financial resources. But the final distribution of responsibility has yet to be fully determined as tort reform endeavors to redefine strict liability and the framework of justice it establishes.

—Mark R. Bandsuch

See also Compensatory Damages; Contracts; Due Care Theory; Duty; Liability Theory; Negligence; Product Liability; Property and Property Rights; Punitive Damages; Tort Reform; Warranties

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Total Quality Management (TQM)

The goal of total quality management (TQM) is for an organization to realize continuous improvement in its business processes for the benefit of its end customers. These processes involve the procurement of material, the production process, and the distribution of final goods to the customers. As an integrative process, TQM requires the use of both information and human resources to foster continuous improvement. It may also be considered the philosophy supporting modern supply chain management. Since today's firms often find it advantageous to establish flexible contractual relationships, as opposed to inflexible mergers, it is important for potential supply chain partners to demonstrate a mutual commitment to raise quality. Despite a lack of agreement on a precise definition, TQM has been used as a clarion call to initiate a change in process—which may or may not conform with any other type of organization's attempt to raise quality. Therefore, TQM is best understood as an intention to achieve something rather than something subject to a strict definition.

Quality itself may have different definitions; therefore, it should come as no surprise that any technique sought to manage it would be limited in terms of the assumed definition of quality. One view is that quality comes from uniformity and conformity of the product to the demands of the marketplace. Another view is that quality is evidenced from the product's availability and ultimate usefulness. These definitions have an important difference in terms of customer service. The first purports a strong form of consumer sovereignty, while the second recognizes that the producer has a role to play in educating the consumer as his or her demands in the marketplace form and evolve.

TQM, as a systems approach, seeks to lower costs and increase customer service at the same time. While these twin goals may be looked on as a trade-off, the focus on all the people within an organization, and along its supply chain, brings to the fore the need to work toward a common goal (i.e., customer satisfaction) by the sharing of information. What is required is a consensus over what defines quality along the supply chain and what is necessary to maintain it over the long run. Of course, market realities such as changes in technology and customer tastes mean that the process must be subject to change and adaptation. As such, TQM must be part of the long-term strategic vision of any organization wishing to practice it.

TQM may be looked on as a business philosophy applicable to all facets of manufacturing and service provision. Its roots may be traced to the pioneering work of quality theorists such as W. Edwards Deming and Joseph M. Juran in the late 1940s and early 1950s. Both took notice of the Union of Japanese Scientists and Engineers, formed in 1949, to improve Japanese productivity and quality. While both Deming and Juran developed their ideas through studying U.S. firms, it was the Japanese manufacturing sector that took most strongly to their work. Deming began his work with the Japanese in 1950 and Juran followed in 1954. At first the emphasis was on methods of statistical quality control; that is, randomly sampling output to estimate the likelihood of defects. But, through Deming and Juran, the emphasis soon expanded from collecting statistics to the wider task of examining organizational processes. In other words, a paradigm shift was occurring beyond merely controlling defects to one where defects were to be prevented. Quality was now seen as part of efficiency. Customer satisfaction was to be sought as opposed to profit in and of itself. While TQM, as a concept, grew out of this work, it must be noted that the pioneers themselves never used the term. Referring to TQM in 1994, Deming himself noted that it was a buzzword, that there was no such thing, and that the term carried no meaning. Typical of buzzwords, and as noted above, there is no standardized definition of TQM since the term has been adopted in a wide variety of ways over several decades. The actual term *total quality management* was coined in 1985 by the Naval Air Systems Command, which adopted its own version of quality management.

Models for achieving quality in business processes are suggested, for example, by the International Organization for Standardization (ISO) and the British Standards Institution (BSI). It should be noted that while firms enjoy signaling their certification by such auditing organizations, the signal does have its limitations. For instance, ISO certification merely attests that the firm in question has a process in place for quality control that was validated under audit conditions. One should in no way infer from this that the firm's final product is defect-free and of consistent quality. It was the process quality that was vetted, not the product quality.

As an example of this long-term process, TQM would not require the firm's purchasing department to simply look for the lowest cost vendor; rather, the firm should seek the vendor offering the best cost-quality combination. Of course, issues such as vendor longevity and flexibility would be a part of the assessment of quality. If the firm operates within tight time frames (e.g., just-in-time supply and lean manufacturing), then vendor flexibility would be particularly important.

Once the goal is determined and quality defined by all organizations along the supply chain, these organizations have to be aware of their particular competitive advantages and how to maintain them. They must be willing to outsource and in-source to control overall supply chain costs and enhance the logistical flows of inputs, outputs, and financial capital.

TQM reached the height of its popularity in the 1980s when many U.S. firms came under the belief that they needed to compete more effectively with their Japanese rivals in the area of quality. The results were mixed in that some firms found it difficult to deploy such a fundamental change in process, while others began to question TQM's return on investment. The main issue was that the cost side was easier to measure than was quality, with its inherent subjectivity. Over time TQM came to be viewed as a necessary but not sufficient program for maintaining competitive advantage.

Social concerns have also entered into the discussion of product quality. For example, ISO 14000 is a program that audits specifically for environmental impact, while ISO 26000 is intended to audit for "social responsibility" on the part of the firm. In other words, the practice of TQM has expanded beyond the business processes and continuous improvement initiatives contained strictly within the organization and its supply chain partners. Positive spillovers to external organizations may now be considered a part of quality management. As with all variants of TQM, education and training is very important for all employees to feel that they have a part to play in the organizational changes that are to be engendered.

In summary, TQM may be seen as having three principles: focusing the organization on its customer; continuously improving business processes; and promoting teamwork internally and externally through supply chain integration. Techniques must be used to measure success in these three areas and aggregated in some way to manage quality. Therein lies the challenge for organizations today.

TQM requires a change in business culture at all employee levels as much as it does a change in business activities. All employees must be involved. Indeed, the right cultural attitude is necessary to recognize the need for continuous improvement. Focusing on activities alone is not sufficient; TQM requires a long-term process of lowering costs, increasing revenues, empowering employees, and satisfying customers. Systematically increasing quality may indicate a commitment to business ethics as well. Empowered employees and satisfied consumers are raised by TQM to a strategic level commensurate with profits and market share.

—Darren Prokop

See also Consumer Sovereignty; International Organization for Standardization (ISO); Outsourcing; Productive Efficiency

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Toxic Waste

Toxic waste is waste material that can cause death or injury to living creatures. Waste is considered toxic if it is poisonous, radioactive, explosive, carcinogenic (causing cancer), mutagenic (damaging chromosomes), teratogenic (causing defects in the unborn), or bioaccumulative (accumulating in the bodies of plants and animals and thus in food chains).

Toxic wastes result from industrial, chemical, and biological processes. In the early years of the 21st century, U.S. factories released 3 to 4 million tons of toxic chemicals into the air, land, and water annually, including more than 70 million pounds of known carcinogens. Toxins are also found in household, office, and commercial wastes, such as batteries and pesticides, and in cell phones and computers. Five hundred billion gallons of U.S. groundwater are contaminated with uranium and other toxic chemicals. Another 800 million gal of uranium waste is buried in landfills, trenches, and unlined tanks.

The "dirty dozen"—12 of the world's worst chemical toxins—comprises nine chemicals used as pesticides (aldrin, chlordane, DDT, dieldrin, endrin, heptachlor, hexachlorobenzene, mirex, and toxaphene), two by-products of chemical production and the burning of chlorinated substances (dioxins and furans), and a group of industrial pollutants known collectively as polychlorinated biphenyls (PCBs). Toxins such as arsenic, beryllium, cadmium, copper, lead, nickel, and zinc are chemicals known as persistent toxins because they linger in the environment for long periods.

The Dangers of Toxic Waste

In 1962, Rachel Carson, a biologist, ecologist, and writer, penned *Silent Spring.* The book described how DDT entered the food chain and accumulated in the fatty tissues of animals, including human beings, and caused cancer and genetic damage. Carson wrote that a single application on a crop not only killed targeted insects for months but also destroyed countless more and remained toxic in the environment even after it was diluted by rainwater. Carson argued that DDT and other pesticides had contaminated the entire world food supply. A powerful chapter titled "A Fable for Tomorrow" portrayed a nameless American town where all life—from fish to birds to apple blossoms to human children—had been "silenced" by the insidious effects of DDT. *Silent Spring* provoked widespread public alarm. Carson's conclusion that pesticides had contaminated the entire world food supply raised awareness of the dangers of persistent bioaccumulative toxins.

Well before *Silent Spring,* the risks of toxic wastes were evident. For example, lead was a known toxin in the 19th century, with reformers documenting lead poisoning in the workforce and leading cleanup efforts. Nevertheless, auto companies, oil companies, and the government authorized the manufacture, distribution, and use of tetraethyl lead in gasoline in the 1920s. Health officials warned against depositing millions of pounds of inorganic lead dust onto the streets from car exhaust. However, the lead industry pointed to lead's importance to the automotive and petrochemical industries, calling tetraethyl lead a gift from God.

Similarly, despite evidence of lead paint's toxic effects on children as early as the 1920s, the lead industry campaigned for decades to deter concerns. The National Lead Company, manufacturer of Dutch Boy paints and lead pigments, produced children's coloring books, including *The Dutch Boy's Lead Party*, extolling the benefits of lead paint. The federal government finally banned lead in paint and gasoline in the 1970s and 1980s.

In the 1950s in Minamata, Japan, deformed fish floated in Minamata Bay. Cats "danced" in the streets, often falling in the sea and drowning. Townspeople began to tremble, stumble, shout uncontrollably, and experience paralysis, hearing and vision problems, and body contortions; at least 3,000 died. Children were born with the "disease." The ailment was later diagnosed as mercury poisoning resulting from the Chisso Corporation's manufacturing of acetaldehyde. Mercury from the production process spilled into the bay and entered the food chain, including seafood, which was the town's primary protein source. Concentrations increased dramatically at each level of the chain. While mercury was long known to be a toxin—the neurological degeneration caused by mercury used in hat-making in the 19th century led to the phrase "mad as a hatter"—Minamata vividly highlighted its dangers in the food chain.

Hooker Chemical and Plastics Corporation used an empty canal in Love Canal, a section of Niagara Falls, New York, in the 1940s and 1950s to dump 20,000 tons of toxic waste in metal drums. After the canal was filled and the land given to the city, houses and an elementary school were built on the site. By the late 1970s toxic chemicals leaked through their drums and rose to the surface, resulting in high rates of birth defects, miscarriages, cancer and other illnesses, and chromosome damage. Families were evacuated and a national emergency was declared. Tensions ran high; on May 19, 1980, Love Canal activists took two government representatives hostage overnight.

The September 11, 2001, terrorist attacks raised concerns about potential sabotage of toxic waste. Eighty thousand tons of highly radioactive waste awaiting transportation from U.S. nuclear power plants to storage facilities could be targeted by terroists when it travels through 39 states on roads and railway lines. Also, 15,000 chemical plants and refineries nationwide could be terrorist targets, with more than 100 of them putting at least a million people at risk. An attack on a single New Orleans refinery, containing 600,000 pounds of hydrofluoric acid, could jeopardize the city's entire population. Related to this, three Superfund toxic waste sites in and around New Orleans were flooded in 2005 by Hurricane Katrina, and some experts argue that toxic chemicals released into New Orleans floodwaters will make the city unsafe for full human habitation for a decade.

The devastating 2004 Indian Ocean tsunami washed vast amounts of toxic waste—including radioactive waste, lead, heavy metals, and hospital wastes—onto the shores of Somalia and other nations. The legacy of decades of illegal dumping by European and other nations, that waste has already been linked to acute respiratory infections, abdominal hemorrhage, skin reactions, and sudden death after inhalation. These and other high-profile examples—including the *Exxon Valdez* oil spill, the Chernobyl disaster, the Bhopal gas leak, and the Three-Mile Island scare—have raised public awareness and concern.

Costs

Toxic wastes result in huge costs in terms of economic expenditures, human health, and the ecosystem. By one estimate, exposure to toxic substances costs industrialized countries $300 billion annually. The U.S. Geological Survey projects cleanup costs for existing environmental contamination in the United States of as much as $1 trillion.

Toxic waste has been implicated in deaths and health problems such as cancers, birth defects, miscarriages, low birth weight, neurological disorders, liver disease, developmental disorders, hypertension, and heart defects. An estimated 50,000 to 100,000 Americans die annually from the effects of outdoor particulate pollution alone. Cancer rates have risen each year since 1970, with growing levels of environmental toxins cited as a primary cause. Children under 5 years of age, who represent 10% of the global population, bear 40% of the environment-related disease burden, and childhood cancers have increased dramatically.

Toxic wastes also cause massive damage to the ecosystem, endangering or destroying animal and plant life. Such wastes overwhelm natural restorative processes, destroy habitats, kill off sensitive species, and reduce biodiversity. The bald eagle population's decline as a result of DDT use is a vivid example. Similarly, PCBs and other toxins are blamed for many whale deaths.

Laws

Many U.S. laws regulate toxic waste. The 1970 Federal Clean Air Act, last amended in 1990, forms the basis for the national air pollution control effort. Its elements include hazardous air pollutants standards, stationary source emissions standards, and other standards and enforcement provisions. The Toxic Substances Control Act of 1976 requires the Environmental

Protection Agency to regulate potentially hazardous industrial chemicals, including halogenated fluorocarbons, dioxins, asbestos, PCBs, and vinyl chloride.

The Resource Conservation and Recovery Act (RCRA) became law in 1976 and regulated the safe handling and disposal of hazardous wastes. It created the "cradle to grave" system to keep track of such wastes.

The Comprehensive Environmental Response, Compensation, and Liability Act (CERCLA), enacted in 1980, created the Superfund Program to deal with toxic waste dumps. CERCLA provided liability for those responsible for illegal waste dumping and a trust fund to clean up sites when the responsible parties could not be found or determined. Releases of CERCLA hazardous substances in amounts greater than their "reportable quantity" must be reported to the National Response Center and to state and local government officials.

The Emergency Planning and Community Right-to-Know Act amended CERCLA in 1986 to require mandatory public disclosure of release of toxic substances. The annual report of the Toxic Release Inventory (TRI) continues to provide detailed information to communities about the types and amounts of toxins that are legally released into the environment.

In addition to such regulations, toxic waste producers are facing growing numbers of "toxic tort" cases. A "toxic tort" is personal injury or property damage from exposure to toxic substances due to the fault of another party. Victims can sue for medical expenses, lost wages, and pain and suffering.

Dealing With Toxic Wastes

Approaches to dealing with toxic wastes include prevention, disposal, and bioremediation.

Prevention

The ideal would be to eliminate toxic waste production. Toxins can be reduced though substitution of nonpolluting alternatives. For instance, chlorine, which is used to bleach wood and results in the formation of dioxins, could be replaced with oxygen. Efficient production processes and proper maintenance of machinery also reduce toxins. Recycling of some wastes, such as expensive heavy metals, can cut both toxins and costs.

The aim of the "green chemistry" movement is to use chemistry for the design of chemical products and processes that reduce or eliminate the use and generation of hazardous substances. Chemicals may also be added to waste to reduce their toxicity.

Disposal

Disposal forms include land disposal, incineration, and bioremediation. With land disposal, waste is buried in landfills that should be permanently sealed to contain the waste. Landfills may be lined with clay or plastic, or waste may be encapsulated in concrete. However, leaks may occur. Incineration may be at low temperatures, used primarily for urban refuse, or high temperatures, best for many industrial wastes such as tar, paint, pesticides, and solvents since they prevent the formation of dioxins.

Bioremediation

Bioremediation is the use of living organisms to degrade hazardous organic contaminants or transform hazardous inorganic contaminants to environmentally safe levels. Some microorganisms use oil as a source of food, producing compounds that can emulsify oil in water and facilitate the removal of the oil. Successfully applied following the *Exxon Valdez* oil spill, bioremediation treats contamination in place, thus avoiding removal-disposal costs, harnesses natural processes, and reduces environmental stress associated with conventional cleanup efforts. Gene-splicers are also now working to engineer the genes of one radiation-resistant bacterium to produce a "superbug" to decontaminate the world's most intensely radioactive wastes.

Phytoremediation uses plants to remove hazardous substances from soil. For example, genetically altered trees containing the *merA* gene can be planted on contaminated sites, draw in heavy metals such as mercury, and then either transform them into less toxic forms that are dispersed into the air and diffused or trap them aboveground for later harvest.

Social and Ethical Issues

Some social and ethical issues relating to toxic waste, such as illegal dumping of wastes and cover-ups of dangers, have already been identified. Several others deserve consideration.

Negative Externalities

Negative externalities are costs imposed on society at large but not borne by the organization that generates the costs. When toxins generate societal costs that producing firms do not bear, such externalities exist. This shifting of costs raises fundamental questions of fairness. Negative externalities are also a major source of market failure since they encourage firms to overproduce goods and services with external costs.

For example, the Superfund program relied on a trust fund to pay for so-called orphan sites, for which parties potentially responsible for the wastes can't be found or no longer exist. The fund was initially supported by a tax on chemical and oil companies, which generated about $2 billion annually for remediation of contaminated sites. However, the tax expired in 1995, and Congress has not reinstated it. As such, citizens are bearing an increasing percentage of cleanup costs.

Trading Credits

With cap-and-trade, industry is given a capped number of "credits"—an amount of pollution that companies can emit legally. Firms producing less than their allotted quota can sell the remainder to other companies. For example, the 2005 Clean Air Mercury Rule established "standards of performance" limiting mercury emissions from coal-fired power plants and created a market-based cap-and-trade program aimed at reducing nationwide utility mercury emissions.

Advocates say that once limits are set that reduce overall levels of pollutants, market forces can most efficiently deal with allocation of pollutants across firms and industries. However, critics note that this lets some companies pollute more than others, subjecting nearby communities to disproportionately intense levels of emissions and creating dangerous "hot spots."

Exporting Toxic Waste

One approach taken to dealing with toxic waste is to send it elsewhere. Harvard University president Lawrence Summers, then chief economist and vice president of the World Bank, wrote in a now-notorious internal memo, "I think the economic logic behind dumping a load of toxic waste in the lowest wage country is impeccable and we should face up to that."

An estimated 50% to 80% of U.S. electronic waste is shipped to developing countries, risking spillages. Receiving countries often lack expertise and technology to safely deal with toxic waste, thus putting locals at risk. Greenpeace estimates that 90% of obsolete ships—many containing toxins such as asbestos and PCBs—are broken up in India, Bangladesh, Pakistan, China, and Turkey. "Shipbreakers," many of them children, often lack protective gear.

The Basel Convention seeks to control the transboundary movement of hazardous wastes and hazardous recyclable materials and to promote their environmentally sound management. The Stockholm Convention on Persistent Organic Pollutants (POP) aims to eliminate the dirty dozen of persistent organic pollutants.

The Rotterdam Convention on Prior Informed Consent requires exporters to notify of any export of potentially hazardous substances. Exporting countries must also comply with decisions of importing countries and those countries through which waste will pass. Critics of prior informed consent argue that future generations inheriting the costs of toxic waste, including disease, death, sterility, and birth defects, have no voice in that consent.

Environmental Racism

A nationwide study found race to be the most significant predictor of location of commercial hazardous waste facilities and uncontrolled toxic waste sites, an even greater influence than poverty. Differential access to power and decision making among black and white communities institutionalizes disparities in site location. Sixty percent of black or Hispanic Americans live near an uncontrolled toxic-waste site. A growing grassroots movement has developed in response to this "environmental racism."

Environmental Activism

Along with grassroots movements, environmental activism may take other forms. For example, Greenpeace, with offices in 41 countries, spends $360 million annually on environmental activism. Its mission statement says it "uses nonviolent, creative confrontation to expose global environmental problems and to force solutions for a green and peaceful future." Greenpeace members have, for instance, interfered with the dumping of toxic waste at sea and invaded nuclear facilities.

More extreme activist groups, such as Earth First!, use "ecotage," blockading roads, sinking ships, bombing power stations, or engaging in other forms of "monkeywrenching," the illegal sabotage of industrial development efforts. To advocates, ecotage is a generally nonviolent and productive means of responding to oppressive groups and practices. To critics, it is vandalism, potentially life threatening, and better termed *ecoterrorism.*

Conclusion

Current stocks and future production of toxic wastes raise critical social issues worldwide. These issues are complex and interrelated, pose difficult trade-offs, and often involve conflicting economic, social, and political forces. Failure to successfully address them will lead to disastrous human, economic, and ecological consequences. Success will depend on public awareness and pressure, corporate social responsibility, sound governmental policies and practices, and international commitment and cooperation.

—Ramon J. Aldag

See also Bhopal; Chernobyl; Environmentalism; Environmental Protection Legislation and Regulation; Externalities; Hazardous Waste; International Business Ethics; Love Canal; Monkeywrenching; Pollution; Silkwood, Karen

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TRADE ASSOCIATIONS

A trade association is an organization created by a group of individual businesses or business owners to promote, enhance, and protect the mutual interests of its members. One type is the *industry association,* which comprises companies operating within a specific industry or sector (e.g., National Restaurant Association, Motion Picture Association of America, Securities Industry Association). In Europe and Japan, these may be organized into a national representative body called an *employers' organization or federation* (e.g., Federation of German Employers Association, Industry Club of Japan). Another is the *business* or *peak* association, which comprises a variety of companies and business owners within a local, regional, or national geographic area (e.g., Business Roundtable, U.S. Chamber of Commerce, National Association of Manufacturers, National Federation of Independent Business, Japan Chamber of Commerce, German Chamber of Industry and Commerce).

Trade associations are differentiated from other groups according to their purposes and membership. A *professional society* or *professional association* comprises individual members who join together to protect and further the aims of a specific profession (e.g., American Medical Association, American Institute of Architects). *Labor* or *trade unions* are member organizations designed to provide benefits to, and represent the interests of, individual workers, particularly in relationship to business management (e.g., United Auto Workers, Teamsters). In Europe, these are called an *employee association* or a *craft trade association* and are organized into a national entity (e.g., Central Association of German Craft Trades).

Trade Association History and Development

The evolution of trade associations is interwoven with the growth of modern nation-states, particularly those with a democratic capitalist system. They were formed to provide a bridge between government and business in shaping national economic policy as countries grew into industrial giants. Their growth in the United States, Germany, and Japan illustrates the differing impact of political and economic systems on their development.

Voluntary associations in the United States in the late 18th and early 19th centuries were organized to solve myriad social problems not being addressed by democratically elected local, state, and national governments. Voluntarism captured the imagination of many individual traders and shopkeepers who joined a complex network of associations to promote the public good. They recognized the power of collective action for protecting their own commercial interests and organized local business associations. The American pluralistic political structure also forced the associations to promote their economic views as political interest groups. Led by prominent industrialists in the late 19th and early 20th centuries, new national associations were organized with the objective of ensuring the smooth operation of cartels within and across industries. The populist movement forced these associations to curtail "antitrust" activities and to refocus on ensuring competition within individual industries. Concurrently, local associations cooperated to build national organizations (e.g., U.S. Chamber of Commerce and National Association of Manufacturers) to represent business in Washington, D.C.

The European context, with its strong, traditional institutions, set the stage for a different path of development. Government took the responsibility for organizing and guiding the growth of emerging national economies. Public officials encouraged powerful industrialists to organize business associations to aid in these coordination efforts, particularly in mobilizing for World War I. These new national associations, decimated during World War II, were reactivated as government and business partnered to rebuild devastated societies. The German government incorporated both industry and employer associations into a national structure that included employee associations to shape economic policy. Membership was mandated by law with companies joining either a business or employer association. The coordinated market model gave trade associations a stronger role than those in America, with its free market model.

Japanese governmental officials requested prominent business executives to organize voluntary business associations similar to the American chambers of commerce in the late 19th century. The creation of new industry trade associations accompanied the growth of heavy manufacturing companies. Membership for all businesses in the Chamber of Commerce was mandated by government at the turn of the century. The industry associations became cartels to protect individual industries, leading to a split with the Chamber and the formation of the Industry Club of Japan prior to World War II. Major industries, through their powerful associations, fueled the war effort and then assumed leadership in the creation of the *keiretsu* in the postwar period. Research associations and export promotion associations have also emerged to assist businesses in technology development and entry into world markets. Both chambers and industry associations are closely related to the national government in the development and implementation of economic policy.

Trade Association Activities

Trade associations engage in two primary sets of activities—providing member services and influencing governments. Activities designed to benefit members directly or indirectly include the following:

- Sharing information on industry production levels, sales, costs, and new products and services to provide a foundation on which members can plan and operate more successfully
- Promotional advertising about an industry or business in general to enhance its public image or to shape an opinion on public policy issues
- Meetings of executives to discuss issues and determine policy that will enhance member companies
- Research and development of operations, products, and issues, an especially important service to European and Japanese companies
- Standard setting for best practices to encourage state-of-the-art operations and ethical conduct
- Training and education to ensure that managers and employees are better equipped for business operations, an extensive set of programs in many European countries
- Advocacy for capitalism as the preferred economic system through advertising to the public, funding of economic research institutes, and organizing public events

Activities designed to influence government include the following:

- Indirect activities
  - *Issue research* to determine the impact of public policy issues on member companies
  - *Grassroots organizing* to encourage constituents to contact elected or appointed government officials about specific issues on legislative or regulatory agendas
  - *Issue advertising* to inform the public and shape their opinions on specific public policy issues
  - *Coalition building* with other associations or groups to organize ad hoc groups for advocacy of a position on a public policy issue
- Direct activities
  - Governmental officials are lobbied to exert influence on their decisions. In the United States, associations

have offices in Washington, D.C., as well as key state capitals to gain access to, and maintain contact with, elected and appointed governmental officials. Associations build a network of personal relationships with officials that can be used by member companies. They coordinate with member company offices in campaigns to influence the legislative and regulatory processes. Lobbyists contact individual policy makers to provide information and present the position of the association on specific public policy issues. They also make presentations at governmental hearings, host meetings, and organize public events about these issues. They work with the legislative branch to draft new legislation and the executive branch to develop new regulatory rules. Exerting influence on government policy makers is different in other countries. In Europe, associations are quasipublic so that government officials must use them for advice on economic issues. Company and association executives meet regularly with governmental officials to shape economic policy and work closely with labor associations on labor and social policy. In Japan, associations play a major role in public policy development through consultation with governmental officials and political parties. The lack of transparency often makes it difficult to identify the extent of their influence.

– Efforts are made to aid the election and reelection of governmental officials. Associations focus on candidates who are sympathetic to the needs and views of business in general or a specific industry. They maintain an independence from political parties, although they may work closely with them during an election. In the United States, associations form political action committees to help individual candidates fund election campaigns. They may also contribute to national and state parties for each election. Recently, they have been instrumental in creating ad hoc organizations to develop and issue advertising campaigns to differentiate candidates and parties. By law, these campaigns may not be coordinated directly with the candidates. In Europe and Japan, political parties are pivotal to the shaping of public policy, so associations rely on member involvement with the parties to exert influence. They make financial contributions to parties but avoid being visibly connected with individual candidates. Electoral activities are secondary to the more direct strategies for influencing public policy makers.

The public policy process includes two types of voluntary member associations: (1) *special interest groups*, which focus on the promotion of the narrow interests of their members, and (2) *public interest groups*, which coalesce around a public policy issue(s) to inform the public and influence governmental bodies for the good of society. Trade associations are criticized for their attempts to unduly and inappropriately influence the public policy process for their special, narrow self-interests, for example, tax breaks, deregulation, barriers to entry into an industry, and governmental contracts. Business leaders counter this criticism by attempting to portray trade associations as operating in the public interest through promoting a healthy business climate while protecting the market from unnecessary governmental interference.

Globalization and Trade Associations

Trade associations are awash in the waves of globalization with proliferation around the world. While they are structured differently in each country, they typically provide usual member services and act as a collective voice for business interests in relationship to national governments. The U.S. Chamber of Commerce was a pioneer in organizing chapters throughout the world, first to cater to American companies engaged in international ventures but now to cater to domestic firms. These associations allow multinational enterprises (MNEs) to establish contacts in host countries and act as a collective voice for business in the public policy process.

Globalization has posed new issues for trade associations. The friction between large firms operating in global industries and small and medium-sized firms focused on domestic markets has grown. For example, the advocacy by major American associations for the North American Free Trade Agreement and major European associations for the European Union has come under criticism by those weakened by the influx of foreign competitors. This differential impact has accentuated member demands that associations become more attuned to individual company needs, provide new services, and develop positions on public policy with greater care.

Associate leaders face a number of other challenges: whether to grant membership to foreign-owned firms, how to represent the interests of both domestic and foreign-owned firms to national governments, which firms to include as members with industry boundaries blurred by technological advances, and how to deal with strong public interest groups. The current structure of employer, business associations, and employee associations in partnership with government for shaping economic policy is a special challenge to European association.

The growth of regional and international governmental organizations has triggered the development of comparable associations to represent business interests. BUSINESSEUROPE, (formery Union des Industries de la Communauté Européenne [UNICE]), the peak association of European business, has been organized to represent business in Brussels. However, European industry associations continue to be nationally focused, with only loose coordination across borders. The World Trade Organization and key United Nations agencies have heightened the concern of MNEs about the need for a collective business voice on world economic and trade policy. International associations have been organized (e.g., Association of International Automobile Manufacturers, World Coal Institute), although they are not truly representative of all firms in an industry.

—D. Jeffrey Lenn

See also American Medical Association (AMA); Barriers to Entry and Exit; Business Roundtable; Capitalism; Consumer Federation of America; Corporate Political Advocacy; European Union; Free Trade, Free Trade Agreements, Free Trade Zones; Globalization; Interest Groups; *Keiretsu*; Mixed Economy; National Federation of Independent Business; Nongovernmental Organizations (NGOs); Political Action Committees (PACs); Power, Business; Securities Industry Association; Transparency; Voluntarism; World Trade Organization (WTO)

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Trade Balance

The trade balance is a number that compares the monetary value of a country's flow of exports with its flow of imports over a specific period of time. The number is calculated exclusively from the current account of the country's balance of payments. If the number is positive, it indicates a trade surplus in that the monetary value of the exports sold exceeds the monetary value of the imports purchased; in other words, the country's international trade activity has generated a net inflow of monetary value. If, on the other hand, the number is negative, a trade deficit exists because the value of exports sold is not enough, by itself, to generate the funds necessary to finance the value of the imports purchased. In this case the country's international trade activity has generated a net outflow of monetary value to its trade partners. Theoretically, the trade balance could be zero, but independent pricing of exports and imports, combined with the timing of the millions of international transactions taking place, makes it nearly impossible in practice for the value of a country's flow of exports to equal the value of its flow of imports.

The precise structure of the trade balance is not generally agreed to beyond the fact that it is made up of certain items that can be either exported or imported by a country over the time period in question. Pairings of a variety of items as exports and imports are found in the current account of a country's balance of payments. Any or all of these may be used to calculate a trade balance. The items in question are goods (tangible items), services (intangible items), current transfers (gifts and charity), and income (business profits).

In terms of goods and services, it is obvious that value may enter or leave the country as a result of receiving payment for exports or making payment for imports, respectively. Similarly, if more charitable donations are made abroad, value leaves the country. However, value can be similarly transferred abroad when it is the result of income generated on an asset situated in one country but owned by someone in another. Investment income is, therefore, another component of the trade balance. Profits transferred home when generated by assets (e.g., stocks and branch plants) owned abroad indicate a monetary inflow in the same way as when an export is sold. When a foreign entity transfers abroad the profits it generates in the host country, an outflow of monetary value occurs in the same way as when an import is bought.

It should be obvious that care must be taken to understand which items from the current account are being used in any reported trade balance statistics and which are not. For example, if a country has a trade deficit in goods alone, the current account itself could very well be in surplus. In this way, the problem of how the trade deficit, as reported, is to be financed is not really an issue because of the narrow way in which the deficit was defined. Of course, if the country's goods trade is taken to be a key indicator of its economic health, then a trade deficit in goods is informative in that particular regard. However, since the service sector has been gaining in importance in many advanced economies, a trade balance that includes services becomes a more descriptive measure of international trade activity.

The social implications of the trade balance depend on how the country wishes to be perceived economically by its trade partners. The structure of the trade balance, and whether it is in deficit or surplus, will have a lot to do with that perception. A trade deficit is often perceived domestically as a sign of weakness supposedly leading to a loss of sovereignty since the country is in debt to others. This is simplistic because it depends on whether or not the debt is sustainable. If these excess imports are used to invest in the society, then the future economic growth expected would be a means of financing the debt. On the other hand, if the imports are merely fueling a consumption binge, there is little chance that this would generate future economic growth.

A trade deficit may also be perceived as an unfair outcome especially if the country's trade partners use protectionist policies to shut out the country's exports. Trade barriers distort normal trade flows and require negotiation among the affected countries so that barriers are taken down in ways that create reciprocal benefits and yet do not destabilize key industries. For example, in many countries the agriculture sector has grown dependent on government subsidies. Removing these too quickly can displace farmers and add uncertainty to their crop production plans. Therefore, while trade barriers can be enacted quickly, the process of removal is much more complicated because of vested interests that form around them.

Protecting key sectors against unfair trade competition is duly sanctioned by international law. However, countries are often tempted to protect those sectors that wish not to adapt to the pressures of globalization. The developing world has a competitive advantage in the form of low-cost labor; and this tends to attract companies looking to lower their costs of production. Keeping out the imports generated in these countries will indeed protect domestic jobs but has the effect of maintaining higher production costs and denying export income to them. If a trade deficit did occur because of the prevalence of low-cost imports, the development process in the emerging economy would, over time, lead to a higher demand for items from the more advanced countries.

In general, the trade balance does indeed have social implications, but it is unwise to make social policy based on it because it is something which, in many ways, merely reflects social policies. The trade balance is merely a scorecard and not a social tool, notwithstanding the pressures by various interests to treat it as such.

—Darren Prokop

See also Developing World; Economic Growth; Globalization; International Trade

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TRADEMARKS

A trademark refers to any word, name, symbol, or device used to indicate the origin, quality, and ownership of products and services. The scope of a trademark is broad and includes design, sound, smell, color, product configuration, or groups of letters, numbers, or combinations thereof, which are used to distinguish or identify goods or services made, sold, or provided by others. The primary purpose of a trademark is to provide accurate information to a consumer about the origins of a product. A service mark is the same as a trademark except that it identifies and distinguishes the source of a service rather than a product. As consumers become familiar with trademarks and service marks, and the products and services they represent, their definitions may acquire a secondary meaning, as one denoting quality or reliability. This meaning may also qualify a product or service for trademark status, even though it might not be considered distinct or unique, because it has allowed the consumer to identify with a particular good or service. However, not all words or symbols are eligible for trademark protection. For example, one could not get a trademark for certain generic terms, such as pizza. Yet the name "Pizza Hut" represents not only the sale of a product (pizza) but also a unique brand identification denoted by name and logo, which is well known to the public.

Protecting a Trademark

Trademarks are protected through registration, maintenance, and enforcement. Trademarks are protected by federal and state trademark laws, as well as by common-law rights that arise from the actual use of a mark. Although it is not necessary to register a trademark or service mark, there are important benefits to be gained from doing so. If a trademark has federal registration, it serves official notice that the trademark belongs to the registrant. Other benefits of federal registration include the evidence of ownership of the trademark, the invoking of jurisdiction in federal courts, the ability to obtain registration in foreign countries, and allowing the owner to file with the U.S. Customs Service to prevent importation of infringing foreign goods. These benefits have significant meaning to a trademark owner in the event that another company or entity in a different geographic market decides to sell competing products under the registrant's trademark, which may not only create customer confusion but also damage the registrant's reputation if the registrant decides to enter the same market. So long as the registrant can provide official documented information proving that registration of a trademark predates the disputed trademark, the registrant has the right to demand that the other party discontinue the use of the trademark, as well as the right to institute civil proceedings for possible damages or lost profits.

Because common-law trademark rights are grounded in actual and prior use, even federal registration does not give a registrant a right to stop others who have used the same mark in their local markets prior to a registrant's application.

Since trademarks identify the origins of products and services, it is of critical importance that a trademark maintain its uniqueness. Failure to maintain a trademark may lead to loss of product or service identity, rendering the trademark generic. Once this occurs, products or services lose their identity and move into the public domain to be used freely by anyone. Major causes of identity loss, such as misuse of the trademark or abandonment of the trademark, may encourage other parties to use the trademark for their own needs. This may not only result in consumer confusion regarding the origin of goods and services but also result in brand damage as customers turn to other sources to fulfill their needs since they no longer feel this product represents the qualities or services that led the customer to purchase it in the first place.

Issues Affecting Trademarks

A general issue facing the trademark is infringement. Since all trademarks can be infringed on, an issue has arisen regarding the "dilution" of a trademark that is considered famous, as opposed to trademarks that are not. The Federal Trademark Dilution Act addresses this, but this is quite subjective. So the bulk of the responsibility falls on the trademark owner, with limited government support for detecting, pursuing, and bringing actions against the trademark violators.

The universal rise of the Internet has added a further dimension to trademark enforcement because violators can now infringe on a global basis to such a degree that the trademark owner cannot possibly keep up with all the violations. The issue here is that there are limited mechanisms for global regulation of the Internet, so it is difficult to track down and enforce violations of jurisdictional standards.

The issue of "likelihood of confusion" is a major issue since there is no statutory guide or uniform rule of case law. The federal courts have developed tests for this definition but nothing that is uniform. The burden of proof falls on the mark owner, who must show that some significant amount of confusion happened but not that anyone was actually confused. All the above-mentioned issues will have an effect on trademarks and trademark owners; however, the social and ethical issues need to be addressed to bring an awareness of these problems to the forefront.

There are certain social and ethical issues that revolve around trademarks, which include subliminal influences of a trademark representing an item deemed harmful for use, for example, tobacco products.

Looking at ethical issues from another viewpoint, it is necessary to address the issue of trademark damage that can be done quickly, sending erroneous information throughout the world via the Internet and other electronic mediums. Other well-known trademarks represent various items in which the familiarity of the trademark is paramount to company profits, regardless of the potential harm that may be caused by constant overuse of the products.

A major producer of consumer products with a global presence had its famous trademark tarnished when a competitor used electronic media to link this particular company with satanic cults. The amount of damage done to this company's reputation was substantial, and the amount of time and money spent to disprove the allegations was quite expensive. Litigation has gone on for more than 10 years. A small company could never afford this type of legal action and would be ruined. The issue here is not who won or lost the case but the future damage inflicted on a company and its trademark. The company in question was able to survive this because of its sheer size and brand recognition, but it did suffer from loss of business, from customers who believed the allegations and have continued to boycott the company's products. This is a prime example of the power and scope of the Internet and its influence on global business.

These examples show the influence that trademarks have on the public; they also show how vulnerable trademarks are to the various information-bearing vehicles available to the world. The enforcement of trademark protection, although well-meaning, is far from comprehensive or fair. The smaller trademark owners have a difficult, if not impossible, time trying to go after trademark infringers on a global basis. They are constrained by finances as well as industry clout, as opposed to the large multinationals, which have the assets and clout to go after parties who attempt to use or infringe on their trademarks. This in itself is a moral and ethical issue of the haves versus the have-nots and needs to be addressed to maintain fairness in the world of trademarks.

—Tom Marini

See also Global Codes of Conduct; Intellectual Property; Patents

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Trade Secrets, Corporate Espionage and

Trade secrets consist of information not generally known or easily ascertainable that provides the owner with a competitive advantage because the information is secret and the owner has taken steps to keep it secret. Corporate or industrial espionage occurs when one company spies on another to steal its trade secrets or proprietary information. Every business has proprietary or confidential information, some of which may be protected as trade secrets. In an information economy, where ideas and innovation have value, trade secrets are an important form of intellectual property. They constitute the largest class of assets and the most valuable property for most U.S. corporations. Trade secrets may involve technical information, such as details for a new manufacturing process. Secret recipes for a cola, cupcake frosting, and cookies can also be trade secrets. Courts have found nontechnical information to be trade secrets, including plans for new products, methods of doing business, competitive studies, and nonpublicly available information about customers.

A large number of both civil cases for trade secret misappropriation and criminal cases for corporate espionage involve insiders. This might occur when an employee downloads trade secret information from the company's server to take to a new employer. Recently, cases of corporate espionage, involving competitors using improper or illegal methods to gain access to trade secrets, have been on the rise. These cases have included the use of technology to try to steal trade secrets from a competitor's computer systems and a college student employee of a copying service photocopying trade secrets from a civil litigation case. Trade secret law protects proprietary information. It also regulates competitive business conduct that amounts to unfair competition. Trade secret law seeks to draw the line between lawful competitive intelligence and unlawful commercial espionage. As one Supreme Court justice put it, the purpose of trade secret law is to maintain the "standards of commercial ethics and the encouragement of invention."

Sources of Trade Secret Law

Trade secret law in the United States is a complex mix of state and federal law. Civil liability for misappropriating a trade secret is primarily the province of states. This makes trade secret law different from laws protecting other intellectual property. Comprehensive federal statutes provide nationwide protection for patents, copyrights, and trademarks. These statutes define the owner's rights and provide criminal and civil remedies for infringement. Because trade secrets are protected on a state-by-state basis, variations in the law occur from one state to another. Although there are common elements, this means it is possible that information protected as a trade secret in one state may not receive protection in another. To create more consistent trade secret protection, in 1979 a national law conference created the Uniform Trade Secret Act (UTSA). Most states and the District of Columbia have adopted all or part of the UTSA. But because not every state has enacted every section of the UTSA and because interpretation of provisions may differ, there is still not uniformity in civil protection for trade secrets in the United States.

Although there is no federal statute providing for civil liability, in 1996, Congress passed the Economic Espionage Act (EEA) to make stealing trade secrets a federal crime. A recent report to Congress indicated that private or public actors in almost 100 countries have targeted sensitive U.S. technologies. The EEA seeks to combat this by making international economic espionage, when the theft of the trade secret is for the benefit of a foreign government, a crime. It also criminalizes corporate espionage, when the theft can't be linked to a foreign government but when it benefits a third party.

Civil Liability for Trade Secret Misappropriation

To receive trade secret protection, confidential information must meet the definition of a trade secret. Once that has been established, a determination must be made as to whether a particular use or disclosure is a misappropriation or a proper means of gaining access to the trade secret.

Definition of Trade Secret

Precisely defining which confidential information is or is not a trade secret is difficult. Part of the reason stems from differing definitions and tests under state laws taking different approaches to trade secrets. One of the most widely accepted definitions of *trade secret* is found in the Restatement (Second) of Torts, which defines a trade secret as any formula, pattern, device, or compilation of information that is used in one's business and that provides an opportunity to obtain an advantage over competitors who do not know or use it. Courts applying this definition consider a number of factors to assist in determining whether a particular piece of information qualifies as a trade secret. These factors include the following: (1) the extent to which the information is known outside the business, (2) how many employees or others involved in the business know the secret, (3) how extensive the measures taken to guard the secret have been, (4) the value of the information to the business and its competitors, (5) the amount of time or money involved in developing the information, and (6) how easy or difficult it would be to properly acquire or duplicate the information. This definition and test highlight the three elements necessary for trade secret protection: The information must be secret, it must have value, and the owner must make reasonable efforts to keep the information secret.

Trade secrets must be secret. The UTSA definition of *trade secret* requires the information to be not generally known and not readily ascertainable by proper means. Thus, information that is publicly known, generally known in a particular profession or industry, or part of the general skill an employee needs to do a job cannot be a trade secret. An invention that begins its life as a trade secret will lose that protection when it is made public in a patent application. Although trade secrets must be secret, no state requires absolute secrecy. Providing trade secret information to key employees whose work depends on using the trade secret will not disqualify the information from protection. But once the secret is available in public sources or is disclosed without protection, it is no longer a trade secret.

Trade secrets must also have value. Depending on their approach to trade secrets, states define *value* differently. Those following the Restatement (Second) of Torts require that the trade secret's value come from the actual, competitive advantage it provides. The UTSA protects more. Like the Restatement, it protects information that provides actual competitive advantage. It goes further by protecting information that has the potential to provide economic value, as well. In other words, it protects information that is valuable because it is secret.

It isn't enough that the information is secret and valuable. Trade secrets only receive protection if the owner treats the information as valuable and takes steps to protect the information from public disclosure. The law doesn't require heroic efforts to protect confidentiality. The UTSA requires that the owner's efforts be reasonable under the circumstances. Because a court will determine whether an owner's efforts were reasonable, it isn't always clear how much security is required. Depending on the nature of the trade secret, reasonable measures could include physical measures, such as restricting visitors from areas in which trade secrets might be observed, requiring special passwords to access trade secrets on company computer systems, stamping files "confidential," and shredding papers containing the trade secrets. Businesses also use nondisclosure contracts with employees, independent contractors, and potential business partners to create contractual obligations regarding disclosing trade secrets. Courts have found that conforming to the ethical and security standards of a particular industry are evidence that the security measures are reasonable. As a general matter, the more valuable a trade secret, the more extensive the efforts must be to protect it.

Misappropriation of Trade Secrets

Misappropriation occurs when an individual uses or discloses a trade secret without permission or learns about the trade secret through improper means. The UTSA defines *improper means* by listing bad acts. Theft, bribery, fraud, illegal wiretapping, and computer hacking are all improper means by which to acquire a trade secret. However, conduct that is otherwise lawful but that a court finds does not meet generally accepted standards of commercial morality and reasonable conduct may be misappropriation. In one case, a court found that flying over a construction site and taking aerial photographs to ascertain a secret process in a new plant's layout, while it did not violate the law, was improper and found this to be misappropriation.

A properly obtained trade secret may be misappropriated if it is improperly used or disclosed. This can happen if a person uses or discloses a trade secret in violation of a duty of confidentiality or by breaching a nondisclosure contract.

Civil Remedies

A trade secret owner may bring an action for a court order preventing disclosure or use of a misappropriated trade secret. If a trade secret has been disclosed, the court may order the wrongdoer to stop using the trade secret and to pay money damages. Damages could include profits lost by the owner, profits the defendant obtained by wrongfully using the trade secret, the amount of a reasonable royalty for use of the trade secret, or the loss of the value of a patent because the trade secret was disclosed before the patent application. In cases in which the misappropriation was willful and malicious, the court may award double the actual damages and, in some states, attorney's fees.

Criminal Liability for Trade Secret Theft and Economic Espionage

Illegal trafficking in stolen trade secrets costs American companies billions of dollars every year and affects small businesses as well as the Fortune 500. In addition to civil remedies for misappropriation, some states make theft of trade secrets a crime. Prior to enacting the EEA, federal prosecutors had few legal options for combating commercial and economic espionage. At that time, there were reports of various governments placing moles in American companies, breaking into hotel rooms to copy documents, hiding listening devices on national airlines, and wiretapping to gain access to secret information for the benefit of their domestic companies. The EEA remedied this by making economic and commercial espionage federal crimes, and these crimes are among the most important prosecuted by the Computer Hacking and Intellectual Property Unit of the U.S. attorney's office. Section 1831 criminalizes economic espionage and applies when an individual knowingly acts on behalf of a foreign government or an agent of a foreign government. Section 1832 applies to commercial theft of a trade secret and applies regardless of who benefits. The majority of cases are prosecuted under Section 1832 because proving a foreign government's involvement may be difficult. This happened when two defendants, originally from China, were indicted on both conspiracy to commit offenses of economic espionage and possession of stolen trade secrets allegedly stolen from four Silicon Valley companies. The trade secrets were seized at the San Francisco airport when the defendants were attempting to fly to China. The EEA prohibits theft of trade secrets and obtaining a trade secret by fraud. Because the value of trade secrets can be stolen without physically taking an object, downloading and duplicating them is criminal. A recent case indicted a departing employee who downloaded proprietary information and e-mailed it to a new employer. Receiving, buying, or possessing the trade secret is also a crime, as is attempting or conspiring to commit these offenses. The EEA will apply to actions done outside the United States if the acts furthered a criminal offense in the United States as long as the individual involved is a U.S. citizen or permanent resident. Given the serious nature of economic espionage sponsored by a foreign government, an individual convicted of violating Section 1831 may be imprisoned for up to 15 years and fined $500,000 or both, and an organization may be fined up to $10 million. An individual convicted of Section 1832 trade secret theft can be imprisoned for up to 10 years, fined up to $250,000, or both, and an organization can be fined up to $5 million for a violation.

—Susan J. Marsnik

See also Copyrights; Intellectual Property; Patents; Trademarks; Unfair Competition

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Tragedy of the Commons

A "tragedy of the commons" occurs because people take something out of or put something into a resource because each individual who has a right to the resource perceives that the benefits derived from doing so outweigh associated costs. In the familiar example, a commons may be a field on which sheep can graze, and all those in a village may use such a field to feed their sheep. The "tragedy" occurs because rights to use the resource are widely assigned or collectively owned, with no one person having the right to exclude the others. Each person or entity that has a right to use the resource does so without regard to the actions of others or the value of the resource, and eventually the resource is wasted or depleted. In the above example, the result is overgrazing of the commons. Each villager who owns sheep will seek to maximize the benefit he or she derives by using the resource. Other examples are familiar as well. They include the use of aquifers, hunting territories, and fishing grounds.

The cause or logic of the tragedy is easily described. Each person with ownership rights derives some benefit from using the commons. For instance, in thinking about adding another sheep to his herd, our villager will consider how this benefit is affected by the costs. But the costs of adding one more sheep are spread across all villagers using the commons, so the costs accruing to the individual villager will only be a fraction of the real costs of increasing the herd. Thus, the individual villager perceives that the benefit he derives is increased by more than the costs of adding one more sheep to his herd. Since we assume that our villager will act rationally, he will add another sheep to his herd. And since all villagers who have herds will perceive the same low costs, additional sheep will be added to the herd of each villager, and overgrazing of the commons will be the result.

In this case, the tragedy is occurring because people are taking something away from the commons. But a tragedy of the commons can also occur by dumping or putting something into the commons as opposed to taking something out of it. Again, examples are familiar. They include pollution of the air, land, oceans, and waterways. In each case, something is dumped or put into the commons.

Garrett Hardin, in a remarkable essay published in 1968, argued that "technical solutions" when applied to a subset of problems such as population growth and the environment will not work. He defined a technical solution as one that required a change in the techniques of the natural sciences, which demanded little or no change in human values or ideas of morality. For instance, in the above example, a technical solution may be the fertilization of the field. Since no technical solution is available in this subset of problems, a solution might be found in an appeal to the morality of resource users. But Hardin argued that appealing to the conscience of resource users will not work because self-interest will trump other considerations and that a solution can only be found coercively.

Theoretically, a tragedy of the commons *can* be solved by legal or administrative means. For instance, solutions could include sole management of the resource—and assigning rights to use on the basis of some idea of "fairness," for instance, first come, first served. Another frequently suggested solution is to privatize the commons. Resource owners then bear the full costs of depleting the resource, and in an effort to minimize costs, resource owners might husband it. Or the resource usage could be regulated. For instance, government can restrict the total number of sheep grazing on the commons. But Barton Thompson observes that even with available solutions and even though participants in a commons problem know that sooner or later the tragedy will occur, the problem persists. Thompson uses fishing, groundwater extraction, and global warming to illustrate the difficulties of preventing the tragedy and asks why even in the face of abundant evidence that a problem exists resource users have proven to be not only unreceptive but actively hostile to solutions.

Thompson posits that resource users resist solutions to the commons problems due to three reasons. First, a solution will require resource users to use less of the resource than they have enjoyed. Second, each problem is characterized by significant scientific or social uncertainty, and third, each problem involves an intertemporal trade-off between a loss today and a greater loss tomorrow.

Thompson argues that solving the tragedy is not simply a matter of enjoining resource users to give up some present consumption to preserve the resource in the future. Rather, resource users see the potential solution as constituting a sure loss rather then a restricted gain—and Thompson observes that most people are willing to risk much to avoid a sure loss. Since a sure loss is involved with a solution, resource users avoid it.

Associated with a commons problem is uncertainty—both scientific and social. In all three examples that Thompson discusses, there is a great deal of scientific uncertainty as to how the commons is affected, what the impact might mean in the future, and whether or not a technical solution is available. When there is uncertainty, people commonly engage in wishful thinking—that the resource is in better shape than it actually is. Moreover, even if resource users believe that there is a problem, they must determine a fair means of allocating the burden of solving the problem. Thus, even if a technical solution is available, there remain problems associated with social uncertainty. There are multiple fairness rules, and most people perceive that the one that benefits them the most is the fairest. For instance, talks on reducing greenhouse gas levels are plagued by differing interpretations of fairness. Developed countries insist that developing countries share the burden of solving the problem because they will benefit, but developing countries see developed countries as being "at fault" and so they believe that developed countries should assume more of the burden of solving the problem.

The third barrier to preventing a tragedy has to do with intertemporal trade-offs. Thompson avoids the debate about what discount rates are appropriate for making these sorts of trade-offs, focusing instead on his observation that people have difficulty making *any* sacrifice to avoid uncertain future loses, assuming instead that they may be able to avoid or reduce or ameliorate future risks.

But Thompson doubts the problems he has discussed can be solved coercively through the courts. Most of the remaining commons problems are international in scope, and there is no outside entity that can impose a solution. (Even internal commons problems require a cause of action to support a lawsuit.

Often this is lacking, as in the case with aquifers where resource users own the land above the aquifers. Moreover, it is difficult to get non–resource users sufficiently interested to expend the political and legal capital necessary to impose an outside solution.)

Getting an effective solution will, in Thompson's view, require three steps. The first is convincing persons that a problem exists and that it warrants coercive action. The second step is getting resource users to agree on the general structure of the problem's solution, and the third step is allocating the burden required for the solution among resource users.

Reducing scientific uncertainty about the problem may help convince persons that a tragedy will occur. But even with evidence, there are difficulties associated with all three steps. As Thompson points out, all three steps are intertwined. For instance, convincing persons that a problem exists might remind persons that the solution will entail a loss. And we have discussed above the ways in which people commonly react to the prospect of a certain loss. But given that most commons problems are international in scope and that there exists no outside mechanism to impose a solution, he sees negotiation as the only solution.

The problems associated with the tragedy of the commons are associated with natural resources and the "right" to use them because they are somehow perceived to be without cost. Rights can be assigned through law to protect property—and thereby promote social or economic goals. But the policies and laws that are formulated to protect property can achieve results that are unintended or that are diametrically contrary to the desired social or economic goal. One such instance is the assignment of rights that give rise to a "tragedy of the anticommons."

Tragedy of the Anticommons

The tragedy of the commons refers to a problem in which multiple ownership or usage rights results in a resource being depleted or overused. In this model no one person has the right to exclude others. The mirror image of that problem is when exclusion rights prevent persons from using a resource so that the resource in question is underused. This is known as the tragedy of the anticommons.

Michael Heller first identified the problem when he observed that in postsocialist economies, in contrast to the expectation that new entrepreneurs would fill the stores, many privatized storefronts remained empty while kiosks, stocked full of goods, proliferated in the streets. He speculated that new or transitional governments were failing to assign or endow any one individual with a bundle of rights that represented full ownership of the resource. Instead, fragmented rights were distributed across a variety of stakeholders, and the burden of collecting these rights prevented usage of the resource. Heller noted that a full economic model had not been developed to describe the anticommons.

Heller and Rebecca Eisenberg subsequently applied the anticommons model to biomedical research, arguing that privatization of biomedical research may result in a proliferation of intellectual property rights that may prevent life-saving innovations downstream in the course of research and development. (*Upstream* refers to research relatively far removed from a commercial end product; *downstream* refers to research that is relatively close to being translated into a commercial product).

The problem that they identify is distinct from the problem of underusage inherent in a patent system, whereby society confers a monopoly for discovery that raises prices and restricts usage. This cost is willingly borne by society to promote invention and disclosure. The problem they identify arises when a user needs access to multiple patent inputs to create a single useful product. The resulting high transaction costs associated with obtaining the rights to use multiple patent inputs may result in inhibiting rather then facilitating the transfer of technology from the labs for ultimate commercialization and use by society.

In some instances, these transaction costs can be avoided or minimized. For instance, there is an industry-wide trend in the biomedical research industry to "vertically" or "horizontally" integrate. In the former case, one company can simply buy another company, acquiring in the process the rights to any patents held by the acquired company. In the latter case, companies can form strategic alliances or joint ventures. Furthermore, companies can ignore existing patents and the associated costs of licensing them. It is possible, although we have not seen them emerge in this area, that a "patent pool" of complementary knowledge is created. Other strategies include some form of collaborative arrangement such as cross-licensing, where two companies enter into an agreement to essentially share agreed-on patents (which may or may not involve cash payments). Or companies may decide that it is in their interests to defensively patent, hoping that a substantial portfolio of patents will give them some leverage in future negotiations. In addition, the industry has acted to put specific information in the "public domain," making it free (or at least affordable) and accessible to anyone.

But these solutions generally rely either on the market or on a willingness to break the law. Heller and Eisenberg caution against relying on either to avoid a biomedical anticommons. First, the potential value of upstream patents is speculative and it is likely that owners will overvalue their discoveries. Second, antitrust laws might inhibit the formation of patent pools. Third, intellectual property rights belong to a large, diverse group of holders in both the public and private sectors, whose agendas may conflict. Fourth, owners are likely to diverge in their willingness to infringe or to put information in the public domain. Moreover, recent court decisions have reminded researchers that substantial penalties exist for deliberate infringement. James Buchanan and Yong J. Yoon, in demonstrating the formal symmetry between the two models, noted that inefficiencies introduced by competing and overlapping regulatory bureaucracies are widely known and illustrate the pervasiveness of the anticommons setting in many areas of modern economic interactions.

Summary

The tragedy of the anticommons is the mirror image of the tragedy of the commons. Theoretical solutions to both problems exist. But in both situations implementing a solution is likely to be marred by the internal logic of the models, and the rationality of the actors, which even if it is biased, demands that self-interest trump other considerations. More realistically, some kind of solution will be found to both problems only when society is willing to spend the political and economic capital to enforce a solution. Unfortunately, this is likely only after some cataclysmic event or series of adverse events that make society aware of the consequences of a "tragedy."

—Ann E. Mills and Patricia J. Tereskerz

See also Resource Allocation

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Transaction Costs

Transaction costs are the costs of exchange incurred when firms engage in economically motivated relationships. There are four distinct forms of transaction costs: search, contracting, monitoring, and enforcement costs. Search costs are the costs of gathering information for identifying and assessing potential trading partners. Contracting costs are costs of negotiating a mutually beneficial contract or agreement. Monitoring costs are the costs of ensuring that each party to the contract or agreement fulfills his or her obligations. Finally, enforcement costs are the costs of sanctioning the party not performing according to the terms of the contract or agreement. All forms of exchange are subject to different levels of transaction costs. They are socially important, in addition to being economically unavoidable, because they represent a deadweight, or nonproductive, cost of doing business. Transaction costs are unavoidable, but they also decrease efficiency and are often areas where one party can take advantage of another.

Transaction Cost Economics

The best-developed articulation of the impact of transaction costs on business and society is a branch of economics (and increasingly law) known as transaction cost economics (TCE). TCE focuses on comparing the transaction costs associated with different institutional means of completing a transaction, thus explaining why some economic transactions occur within hierarchies, such as firms, rather than between individuals across a market. The most fundamental claim of TCE is that transactions will be governed by institutions that minimize their associated costs. Two main types of institutions are identified. First are markets, in which the identity of the transacting parties is irrelevant because there is no dependency between them; if one party reneges on the terms of the transaction, the other party is not significantly worse off, typically because the "aggrieved" party can seek legal redress through classic contract law and because the assets can often be redeployed at low, or little, cost. However, in some transactions, the identities of the parties do matter, or courts cannot realistically enforce contracts. This, of course, raises the issue of institutional morality: The governance of economic exchanges by contract reduces opportunism only if there is a well-developed, efficient, and noncorrupt legal system to enforce contracts. In places where lawsuits take decades to resolve, or where judges decide cases based on cronyism rather than legal merit, the threat of suing for breach of contract does not constrain an opportunistic party from taking advantage of their "honest" partner.

The second institution is a hierarchy, or an internal organization, where responses to unanticipated disturbances to a transaction are resolved internally, by fiat. Fiat is the power exerted by the central authority in the organization to ensure smooth and efficient transactions. In addition, hierarchies can also control behavior through organizational culture. For example, Enron had a well-known culture of risk taking and pushing legal limits in pursuit of new markets and profits prior to its downfall. Conversely, Starbucks has a strong corporate culture of social responsibility and integrity and thus is less likely to become a future corporate malfeasant.

The main costs associated with hierarchies are bureaucratic and organizational costs. The market will be used to govern transactions where the parties are not vulnerable to reneging; conversely, hierarchies arise when the parties would be made significantly vulnerable or worse off if one of them were to pull out of the transaction. TCE emphasizes three sources of vulnerability: bounded rationality, opportunism, and asset specificity.

Bounded Rationality, Opportunism, and Asset Specificity

Unlike traditional economic theory, TCE does not assume that people are rational. Indeed, TCE explicitly states that while people *intend* to behave rationally, they are *actually* incapable of doing so. For example, in a contract between two firms for a joint venture (JV), the partners can probably predict in advance some of the ways in which the JV may become unstable, but they could probably never predict all the ways in which one or the other partner could be harmed. Since economic actors are not all-seeing, they cannot foresee everything that may occur. This view of limited rationality is, of course, a feature of many decision-making theories, not just TCE.

In addition, some economic actors behave opportunistically—they will take advantage of the other party to advance their own interests. Examples of opportunistic behavior include making false promises, misrepresenting intentions, reneging on a deal, or changing the terms to benefit oneself. Such behavior leaves the "honest" party worse off. Opportunism can come from two sources. Most obviously, an economic agent may intend to take advantage of its partner from the outset. On the other hand, an economic agent may sincerely intend to fulfill its end of a bargain but become incapable of doing so. For example, Firm X contracts to buy a product from Firm Y for an agreed-upon price. Firm X has every intention of paying Firm Y on delivery of the product but goes bankrupt before Firm Y can finish manufacturing the product, and Firm X is unable to pay Firm Y. This example is not a case of opportunism (self-interest seeking with guile) but rather a case of bounded rationality—neither firm could foresee that Firm X would become unable to pay. TCE thus predicts that governance structures arise to protect against both uncertainty and opportunism. There is the uncertainty of often not knowing which economic agents are opportunistic, as well as not knowing which trustworthy economic actors may become incapable of performing as promised. To manage the second type of uncertainty, asset specificity becomes a critical factor.

Finally, parties to a transaction are made vulnerable not only by their own bounded rationality and the potential for opportunistic behavior but also by the amount of irreversible investment they have made to support the transaction. For example, a developer building a house in the large, virtually uninhabited California desert area of Death Valley for a client is very vulnerable to that buyer potentially reneging on the deal. Why? Assume that the developer has sunk 6 months and $250,000 into building the house—who else would pay for it, in the middle of a desert? Moreover, the developer cannot pick up the house and move it to a populated area without being made worse off since it will be quite costly to move and reassemble the house. While many transactions are highly asset specific, some have virtually no asset specificity. For example, if I invest in a pencil-making facility to supply pencils to one customer, and if that customer pulls out of our contract, so many other buyers of pencils exist that I am unlikely to be significantly harmed because I can recoup my investment in the pencil-making factory by selling the pencils on the open market. A partner's vulnerability as result of asset specificity is closely related to the condition of small numbers. When the number of parties with whom one can potentially contract is large, then opportunism can be lessened or eliminated by switching contractual partners. However, if the number of parties with whom one can contract is limited, then the party's vulnerability to opportunism is elevated. Since most economic exchanges expose the parties to some form of vulnerability, safeguards arise. Specifically, TCE predicts that when bounded rationality and opportunism are present, but asset specificity is not, then market exchanges will arise. When bounded rationality, opportunism, and asset specificity are all present, then hierarchies such as vertically integrated firms will arise.

Safeguarding Transactions

With respect to the prediction of TCE about when markets will govern transactions, there are countless situations in which economic agents make investments, but they are not specific to one transaction or client, and thus the agent is not vulnerable. This is the pencil factory example: If I cannot sell my pencils to my original buyer, I can find other buyers, thus limiting my losses. What protects me is the strength of competition in a market (which stems from the many buyers for a product with standard features) that allows me to be "made whole" by some other economic agent. Under these circumstances, the transaction costs associated with searching for the original or a different buyer, monitoring buyers, writing a contract, and investing in enforcement are minimal. However, this is not the main case TCE seeks to explain; exchanges across competitive markets are already well explained by microeconomic theory.

Rather, the case TCE seeks to shed light on is what happens when bounded rationality, opportunism, and asset specificity are all present. Under these conditions, TCE predicts that various forms of economic hierarchy, such as vertically integrated corporations, will arise. Rather than specializing in one aspect of the business's value chain and outsourcing other components to specialized agents across a market, which is comparatively efficient, we see firms internalize some of these components by forward or backward integrating (i.e., specializing in multiple portions of the value chain). For example, if a gasoline retailer were to backward integrate, it might go into exploration for crude oil and refining of that crude. Conversely, if an oil company that has historically only drilled for oil begins selling refined gas at gas stations, it has forward integrated into retail operations. Despite the increased administrative costs of taking on more of the functions in the value chain, the firm no longer has to incur monitoring costs of potentially dishonest suppliers, contractors, or JV partners; it has made itself less vulnerable to opportunistic outsiders by internalizing many functions. What it has lost in productive efficiency it has gained in decreasing its transaction costs.

Influence and Critics

TCE has been applied to a number of business phenomena such as buyer-supplier relationships, mergers and acquisitions, joint ventures and alliances, employment contracts, and debt versus equity financing. The most famous, recent proponent of TCE has been Oliver E. Williamson, an economist at Berkeley's business school. However, TCE also has detractors. Many sociologists question its assumptions: Are all economic exchanges subject to transaction costs? Are all economic exchanges free from the realities of social norms of exchange? Are all parties to an exchange subject to the assumption of opportunism?

Critics argue that TCE overlooks many social incentives that people have to be trustworthy: concern over reputation, the likelihood of working with someone again, motivations other than maximizing profit. Many motivations tie economic actors to one another in beneficial ways. However, the embedded assumption about business behavior in TCE is that loyalty, honesty, and integrity are less powerful human motivators than short-term self-interest and profit seeking and that governance of exchanges by contract is a necessary substitute for trust. Many sociologists argue that human qualities such as trust, compassion, integrity, and justice help control transaction costs and that the governance structures TCE focuses on are unnecessary because the parties in many exchanges will not behave opportunistically. For example, although the search costs associated with identifying a trustworthy trading partner may be high, the costs related to contracting, monitoring, and enforcement will be significantly lower, thus allowing exchanges across a market between trustworthy partners to occur smoothly, even in the presence of opportunism, bounded rationality, and asset specificity. Moreover, partners with a reputation for trustworthiness are generally more highly sought after than economic actors known for cheating. Consider, for example, the Seller and Buyer ratings that eBay employs: All buyers and sellers are asked to provide feedback that is then publicly posted for future parties to consider prior to making or accepting a bid from someone. Sellers with a poor reputation for shipping paid-for items will soon have far fewer bidders than sellers with a reliable reputation. Trust and integrity thus do serve as governance mechanisms in many transactions, but these are not the governance mechanisms that TCE is centrally interested in.

Conclusion

Transaction costs are a powerful and robust way of understanding exchange relationships from both an economic perspective and a social perspective. From an economic perspective, few theories explain so many economic relationships as TCE. However, by understanding that transaction costs associated with economic relationships are subject to social realities such as trust, integrity, and justice, we can understand the conditions under which transaction costs are mitigated, thus allowing a more general transaction cost perspective to explain a larger spectrum of exchange relationships.

—Karen Schnietz and Ariff Kachra

See also Agency, Theory of; Antitrust Laws; Bounded Rationality; Coase, Ronald H.; Coase Theorem; Economic Efficiency; Economic Rationality; Opportunism

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Transfer Pricing

The American Marketing Association defines transfer pricing as "the pricing of goods and services that are sold to controlled entities of the same organization, for example, movements of goods and services within a multinational or global corporation." Transfer pricing is an *intra*firm transaction that affects costs and profitability at the subsidiary level and overall after-tax profitability for the firm at the corporate level. How the firm accounts for its various intrafirm transactions is therefore of interest to host governments, who would understandably want to investigate any suspicions of tax evasion through transfer pricing practices.

Host governments are naturally concerned to ensure that multinationals are not using creative accounting to avoid paying taxes. As a result, host governments may impose restrictions and enact laws that curtail such practices if the intent is to avoid taxation. While different governments may have different laws prescribing how transfer pricing is to be accounted for, in general the principle of "arm's-length" transaction is the approach least likely to violate legal requirements. By *arm's-length transaction*, it is meant that a "fair" price is charged between subsidiaries as though these subsidiaries were unrelated. We should note, however, that such fair prices are often allowed to contain additional charges for technology transfer, R&D, other overhead expense allocations, and the like. The upshot is that even arm's length is not necessarily clear-cut or straightforward. For instance, the IRS's *Treasury Regulations Section 1.482,* which is one of their publications pertaining to transfer pricing (among other things), runs to 103 pages.

If multinational or global corporations were few in number and minimal in economic impact, the issue of transfer pricing would be of only passing interest to most. However, multinational companies (MNCs) are becoming more and more pervasive, and mergers and acquisitions serve to make them even more powerful and omnipresent than ever before. Consequently, what these companies do to avoid taxes is of major import to most national treasuries and by extension to the economies of those societies. Corporations have always tried to minimize their tax obligations, and few would question any entity's (individual or otherwise) attempt to legitimately reduce its tax burdens. However, transfer pricing as an instrument to reduce or eliminate a multinational's taxes sometimes resembles "creative accounting" and corporate malfeasance. Especially in situations where an MNC is operating in a developing country and uses transfer pricing as a means to minimize its taxes payable to that country, such practices may be criticized as a blatant attempt to exploit a developing country's resources.

Global or multinational companies can manipulate transfer pricing to their advantage in at least two common ways—by adjusting the prices being charged intracompany, and by deciding what and how much of intrafirm goods and services will be bought. In an MNC, a lot of purchasing and selling take place within the boundaries of the firm itself. For example, say the Singapore subsidiary of XYZ Oil Company sells its lubricants to the Australian subsidiary for resale in Australia. The price that Singapore charges is the cost that Australia pays. Yet in the final analysis the funds stay within the firm. If not for taxation, the price being charged by Singapore (the transfer price) does not have an impact on the overall profitability of XYZ Corporation worldwide.

Contrast this with a scenario where multinationals do not exist. The "same" transaction is undertaken by an independent Singaporean company selling to an independent Australian entity. The funds change hands in this new scenario. Price matters here, regardless of tax implications.

It is obvious that transfer pricing decisions within the firm can have significant income tax consequences for the corporation as a whole. Consider a simple illustration, where the firm only has two international subsidiaries, A and B. If A has lower income tax rates than does B, then it makes sense for the company to make more profits in A (and pay less taxes) than in B. One way to do this is through transfer pricing, in which case the company would want A to charge higher prices (and make more profits), which adds to B's costs (and thus lower profits). In so doing, the company minimizes the amount of taxes it has to pay.

The multinational firm can also manipulate transfer pricing to its advantage by deciding to buy more (or less) of certain intrafirm products and services. Even if the price itself was based on an arm's-length evaluation, the fact remains that subsidiary A may be buying something from subsidiary B that it does not really need, but which it still has to pay for. The following example illustrates this point.

Exxon in 2002 sold its Disputada de las Condes copper mine operations in Chile to Anglo American for U.S.$1.3 billion. In the mid-1970s, Exxon had bought the mine for U.S.$80 million. Since that time, Exxon reported operating the mine at a loss every year, never paid taxes in Chile, and even accumulated gross tax credits of more than U.S. $0.5 billion. Further, to avoid paying Chilean taxes on capital gains from the sale, the sale was to be consummated in a foreign country.

Questions arose over the nature of these losses that Exxon suffered over the 23-year period of ownership. Apparently, Exxon's Disputada subsidiary borrowed heavily from Exxon's Bermuda-based financing arm and other Exxon entities, and the interest payments on these loans caused Disputada to operate continuously at a loss, resulting in a negative net worth and no income tax. Exxon was able to withdraw funds from Disputada not in the form of profits (taxable at a 35% rate) but as interest payments (taxable at a maximum rate of 4%). Furthermore, since a large share of the interest payments went to Bermuda, where the financing arm was located, Exxon paid no income tax on those profits either.

The subsequent public outcry and Chilean government investigations resulted in an agreement by Exxon to pay the Chilean government U.S. $27 million in taxes (a relatively small amount relative to the magnitude of the operations and the sale). Partly because of incidents such as this, moreover, the Chilean government subsequently passed a law requiring large mining companies to pay a 3% royalty on copper sales regardless of profitability. Transfer pricing is, and will continue to be, an issue that various governments have to wrestle with as MNCs get even bigger and more numerous.

—Ed Chung

See also Accounting, Ethics of; Multinational Corporations (MNCs)

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Transparency

Transparency has two general meanings with regard to ethical behavior in business. The first meaning relates to a business's openness to making information about its policies and performance (both financial and social) available to stakeholders. The second relates to corrupt behavior (generally some sort of bribery) with regard to interactions between a business and the government officials with which it interacts.

Three Questions Regarding Transparency, Openness, and Business Ethics

Three key questions regarding transparency with regard to openness to stakeholders merit examination:

1. About what should businesses be transparent?
2. To whom should businesses be transparent?
3. How should businesses communicate with their stakeholders to demonstrate transparency?

About What Should Businesses Be Transparent?

There are two broad categories of information about which businesses should be transparent: financial and social. A lack of transparency with regard to either can reduce trust for an individual business, an industry, and the institution of business.

In the United States, many of the business scandals of the 1990s and 2000s can be understood in terms of a lack of financial transparency. Many companies engaged in accounting fraud to make their financial results look better, and many such examples of fraud have been linked to a desire to increase executive compensation through stock options. George Staubus notes that accounting failures represent breaches of fiduciary duties that one party owes others. A lack of financial transparency—whether understood in terms of overt fraud by company managers or some other failure to disclose relevant information about the true financial state of a company—violates some of the most fundamental duties that managers owe their stakeholders, especially stockholders.

A second area of information about which businesses are expected to be transparent is social performance. In the past 30 years stakeholders have expected more and more information about a variety of social performance indicators, including environmental performance and treatment of employees. Transparency about financial performance has a direct effect on stockholders and may also affect other stakeholders, such as employees who lose their jobs and pensions. Transparency about social performance, however, affects nonshareholder stakeholders such as employees and communities directly, with a secondary effect on stockholders.

Transparency expectations for businesses, it should be noted, are likely greater for public corporations than for privately held firms. The ethical duties owed to nonshareholder stakeholders with regard to social performance transparency, however, accrue to all organizations no matter what their ownership structure is.

To Whom Should Businesses Be Transparent?

A stakeholder perspective on transparency would suggest that businesses owe duties of transparency to a variety of stakeholders. Because stockholders have ownership interests, public corporations owe fiduciary duties to them that include financial transparency. Nonstockholder stakeholders do not own the firm but have interests (jobs, a clean environment) that would be furthered by financial and social performance transparency. Expectations about financial and social performance transparency have increased recently, as stakeholders are increasingly demanding more and more timely information about a variety of performance indicators.

Stockholders can use financial transparency to decide (1) whether or not to remain invested in a corporation and (2) if changes in the corporation's strategy or practices should be sought (the latter mostly useful to large stockholders). Nonstockholder stakeholders similarly benefit from transparency with regard to social performance, which they can use to advocate for changes in corporate policies and practices.

How Should Businesses Communicate With Their Stakeholders to Demonstrate Transparency?

There is an extensive literature on financial and social performance transparency. Much of this literature has addressed how corporations can and should make such information available to their stakeholders.

Financial performance measurement and transparency has received considerable regulatory attention in the United States (through the Sarbanes-Oxley Act of 2002 and other legislation) and in a variety of other countries. Expectations for reporting financial performance include more timely information, information about future business prospects, and full disclosure of adverse information.

For social performance, there are a number of standardized reporting regimes—such as the Global Reporting Initiative—that address what and how often corporations should report publicly. Much recent attention with regard to social performance transparency has been focused on the relationship between social performance reporting and transparency. Of course, when a business engages in social reporting in an effort to improve transparency, it opens itself to questions about whether its performance indicators are sufficient and whether it is adequately monitoring social performance (including independent verification thereof).

One interesting recent development in this regard is the establishment of industry-level codes of conduct and reporting regimes that attempt to standardize reporting and expectations for transparency. Such initiatives seek to reduce the potential competitive advantage of poor social performance by some members of an industry. The International Council of Toy Industries and the Electronics Industry Code of Conduct are two examples of industry-level cooperation that improves social performance transparency.

Transparency and Accounting

Any discussion of transparency would be incomplete without a discussion of the role of accounting in furthering transparency. Many corporate scandals have implicated public accounting firms that aided corporate managers trying to hide information about the true financial performance of their firms. Some are examples of actual fraud, such as intentionally misreporting revenues or expenses. Others are not examples of illegality but rather of attempts to apply generally accepted accounting principles and accounting regulations in ways that ultimately were misleading. In obeying the letter of an accounting rule, many corporations and their accounting firms violated the spirit of the rule—to increase transparency.

Organizational managers owe ethical duties to their stakeholders that include financial transparency. But other stakeholders—like accounting firms—similarly owe such ethical duties as well. Accounting education and professional practice have focused increasingly not just on the content of accounting rules but on broader ethical duties owed to users of accounting information.

Transparency and Corruption

A second meaning of transparency focuses on corruption with regard to a business's interactions with governments. In the United States, the Foreign Corrupt Practices Act (FCPA) was passed in 1977 and amended in part by the Omnibus Trade and Competitiveness Act of 1988 and the International Antibribery and Fair Competition Act of 1998; this body of legislation deals with bribery and other forms of corruption, coming about after a number of scandals involving U.S. businesses during the 1970s. Other countries have similar kinds of legislation, although enforcement is often weak.

Transparency in this regard is important because of the effect that bribery has on countries; bribery transfers public wealth to private hands in a corrupt way—and in poor countries takes away from other needs—while contributing to a poor climate for economic growth and activity. A number of studies have shown connections between public corruption and slow economic growth. Furthermore, a lack of transparency in this regard increases public cynicism toward business.

Transparency in this regard is a problem in many countries. In many commodity-rich countries (oil would be one example), poor national-level governance is both a symptom and a result of corrupt behavior by businesses seeking an advantage. When a business bribes a public official to secure a contract or to overlook an environmental or human-rights violation, both the business and the government official are engaged in immoral behavior that ultimately hurts the people in that country.

Transparency and Trust

Another essential issue with regard to transparency is trust. In the same way that personal relationships between people rely on openness, so do relationships between organizations (whether nonprofit organizations, governments, privately held businesses, or for-profit corporations). Increased transparency can increase trust, and reduced transparency decreases trust.

There is considerable cynicism about businesses in many countries. Much of this cynicism focuses on the supposed secrecy and dishonesty of businesses. Lying to one's stakeholders—whether stockholders, governments, local communities, suppliers, or employees—is morally wrong, of course. But engaging in undue secrecy similarly violates ethical duties that organizational managers owe stakeholders.

There is a need for businesses and industries—and indeed the institution of business—to counteract public cynicism about business through increased transparency. When organizations are transparent about social and financial performance, public trust in business increases. When businesses are seen to be less than fully transparent, trust declines—and pressures to control the behavior of business through regulation increase. In the United States, the FCPA and the Sarbanes-Oxley Act of 2002 are direct results of a lack of business transparency. Trust is essential for not just the institution of business but for any organization. Transparency and trust are highly correlated.

The Future of Transparency

Generally speaking, it is reasonable to expect that businesses will face expectations for greater transparency in the future. Groups such as Transparency International have been addressing issues related to bribery and corruption, bringing attention to how business activities affect good and bad government behavior. Businesses will also face increased expectations for disclosure regarding financial and social performance.

The relationship between transparency and corporate governance will likely be the subject of increasing academic and practitioner attention in the future. Boards of directors—as stewards of shareholder interests—will have to think through what sorts of financial and social performance data should be disclosed and how.

Another interesting topic to consider is the effects of industry-level norms and initiatives that focus on social performance disclosure. As previously noted, industries as varied as petroleum and electronics are starting to develop industry-level codes of conduct that include expectations for transparency regarding elements of social performance. Corporate endorsement and involvement in such programs will increase transparency, although stakeholders such as activist groups will continue to push individual companies and industries to improve still further in this regard.

Conclusion

Demands for greater transparency—whether from stockholders, consumers, governments, employees, or other stakeholders—are likely to increase over time. With regard to financial performance, corporations have legal and ethical duties to disclose information to their stockholders and other stakeholders. Businesses will have to weigh when it makes sense to withhold information about social and financial performance and when openness is necessary. The bias generally should be toward more transparency from businesses with regard to various aspects of performance to their stakeholders.

—Harry J. Van Buren III

See also Accountability; Accounting, Ethics of; Asymmetric Information; Black Market; Corruption; Developing Countries, Business Ethics in; Finance, Ethics of; Fraud; Sarbanes-Oxley Act of 2002; Scandals, Corporate; Social Audits; Stakeholder Engagement; Transparency, Market; Trust

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Transparency, Market

The word *transparency* can mean different things to different people. In the corporate finance world, people use the term to refer to the degree to which a firm's accounting choices help investors understand the valuation of items on the firm's balance sheet. In the banking world, *transparency* often refers to the banker's knowledge of credit characteristics associated with a loan customer or a trade counterparty. In the world of futures and securities markets, the word *transparency* refers to the degree to which financial exchanges publicly disseminate real-time information on transaction prices, quotations, order flow, and other market variables. It is this case that is addressed here.

A completely transparent market would be one where all relevant market information is instantly and freely available to all potential investors. Some observers distinguish between pretrade transparency, that is, information disseminated ahead of a trade, and posttrade transparency, that is, information disseminated after a trade.

In the United States, the United Kingdom, and other domains, the level of government-mandated market transparency has become a source of contentious public debate. A central element of this debate is the extent to which market forces can be relied on to supply the level of transparency demanded by the public. The debate has intensified due to recent innovations in trading technology that allow for the capture and dissemination of vast amounts of market information at low cost. Government-mandated transparency requirements are often based on the premise that complete transparency is a desirable goal.

Economists have been more circumspect in opining on the desirability of complete transparency. Some observers have argued that complete transparency may actually result in investors having access to less information. This is because mandated transparency sets up a paradox: As securities prices become perfectly known, there is less individual return to discovering new information. Requiring complete transparency can reduce the incentives of individual investors or analysts to gather fundamental information and incorporate it into market prices. If the incentives for gathering information are reduced, prices will be less informative.

The provision of transparency involves both social benefits and social costs. Therefore, identifying the socially optimal level of transparency, that is, the level of transparency that balances social benefits and social costs, is an important consideration in the public policy debate on the subject. Optimal transparency may not be consistent with complete transparency, a concept that implicitly assumes that transparency provides benefits at no cost. The public policy debate on transparency hinges on the question of whether financial exchanges, such as the New York Stock Exchange, possess sufficient private incentives to provide the socially optimal level of transparency.

The provision of transparency is costly because for financial exchanges to disseminate market information, this information must first be produced. Producing market information, what economists refer to as "price discovery," is a costly activity requiring considerable investment by a financial exchange. Restrictions on the use of market information can be viewed as a means of protecting the exchange's investment in producing accurate prices. Under this view, exchanges hold property rights to the information they produce, analogous to a trade secret. Exchange-imposed restrictions on the dissemination of information can reduce the externality problems associated with information production; that is, exchange-imposed restrictions serve to limit the use of information by off-exchange traders who do not contribute to the price discovery process at the exchange. Government-mandated transparency reduces the exchange's return on its investment in information production (because information is given away for free to rivals who have not paid the costs of its production). The result can be less accurate prices, higher costs of trading, or both.

Mandated transparency may also have distributional consequences. Mandated transparency may redistribute benefits from information producers to information consumers and from some classes of information consumers to others.

In the absence of government regulation, transparency can be viewed as one dimension of competition between competing marketplaces. By choosing to make information widely available at low cost, financial exchanges can attract order flow to their trading venues from customers who value transparency. By attracting order flow, markets become more liquid and trading costs decline. Financial exchanges will choose the transparency level consistent with profit maximization. Choosing the appropriate level of transparency will necessarily involve trade-offs. On the one hand, too little information provided to market participants can result in a reduction in trading volume as fewer investors are attracted to the trading venue. On the other hand, too much transparency can also lead to a reduction in trading volume. For example, if a dealer's inventory position can be discerned from the contemporaneous dissemination of transaction prices and volume, other traders may be able to take advantage of this information at the dealer's expense. Thus, the willingness of dealers to make a market will in part be determined by the level of transparency selected by the exchange. In addition, too much transparency helps facilitate off-exchange trading that can reduce liquidity on the transparent exchange. Liquidity can also be reduced if higher transparency leads to higher price volatility.

Other traders may not value transparency as highly and may prefer to trade in more opaque environments where their trades can take place in greater secrecy. For example, an institutional trader contemplating a large market-moving transaction may prefer secrecy to reduce the price slippage that would result from having other traders know his intentions. If transparency is mandated, traders who value secrecy may trade less often or search for venues in other jurisdictions that offer greater secrecy. A reduction in trading volume from large transactions can reduce market liquidity and reduce the information contained in that order flow from reaching the market.

The analysis of the effects of transparency becomes more complex when traders can trade in multiple jurisdictions, each with a different policy governing market transparency. Consider two side-by-side jurisdictions, one with a low level of market transparency (the opaque market) and one with a high level of transparency (the transparent market). Traders in the more opaque market can monitor prices in the transparent market, but traders in the transparent market cannot see prices in the opaque market. This means that the opaque market will have better information: its knowledge of prices on the transparent market and at least some portion of the order flow to the opaque market. This informational asymmetry allows members of the opaque exchange to exploit price differentials between exchanges, causing bid-ask spreads in the transparent market to widen in anticipation of the arrival of informed order flow. Requiring a high level of transparency may result in the unintended consequence of creating higher trading costs (e.g., higher bid-ask spreads) for customers because of the informational asymmetry with less transparent markets.

An important set of players in the provision of transparency are information vendors such as Bloomberg. These vendors form contracts with financial exchanges to receive flows of real-time information. The revenue received by financial exchanges from vendors helps offset some of the costs associated with offering transparent markets. Information purchased by information vendors is then disseminated to subscribers of the vendor's services. This thriving market for real-time data reminds us that an important dimension to transparency is price. Financial exchanges are willing to provide high levels of transparency for a price. Debates about the appropriate level of transparency can be recast as a debate about the price of transparency. In fact, in markets under the jurisdiction of securities regulators, the price of market data is regulated to ensure that the administered price is "fair and reasonable." For markets under the jurisdiction of futures market regulators, the price of market data is determined by the market.

Ultimately, competing views concerning the effects of mandated transparency can best be analyzed with empirical evidence. Currently, little evidence exists. In the absence of empirical evidence, regulators must decide which entity is in a better position to judge the appropriate level of transparency, and its price: the exchange or the government. Advocates of mandated transparency believe that the government is in the better position to make this determination. Opponents of mandated transparency believe that the exchange is in the better position. Ultimately driving these competing regulatory views is a philosophy about the nature of the exchange itself. Advocates of mandatory transparency tend to believe that exchange-imposed restrictions on information dissemination are the result of anticompetitive conduct. Opponents of mandatory transparency tend to believe that exchange-imposed restrictions on information dissemination are the result of financial exchanges acting to protect their private property, and simply a reflection of one form of competition between competing market centers. Under this view, market forces can be relied on to efficiently determine the appropriate level of market transparency—for a price.

—James A. Overdahl

See also Disclosure; Property and Property Rights; Transparency; Transparency International

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Transparency International

Transparency International (TI) is a nongovernmental organization (NGO) based in Berlin that cooperates with business, government, and civil society to combat corruption around the world. TI works at the national and international levels to lessen both the supply and demand of corruption, which it defines as the abuse of entrusted power for private gain. Launched in 1993, TI began because most world business and government officials were ignoring corruption. Yet some people in both developed and developing nations were concerned about the large-scale bribery by businesses as they "bought" officials and politicians in the developing world; such corruption hurt economic development and undermined human rights.

TI raises awareness about the damaging effects of corruption, advocates policy reform, works toward the implementation of multilateral conventions, and subsequently monitors compliance by governments, corporations, and banks. TI estimates that the amount lost to bribery in government procurement worldwide is more than $400 billion each year. TI has chapters in 95 countries, which work to increase accountability and transparency in their own nations. In addition, there are regional networks of TI chapters that cooperate on regional issues in Latin America, South Asia, Southern Africa, and Central and Eastern Europe. China and Saudi Arabia do not have chapters because independent chapters there are not possible, and TI will not accept a mere government-sponsored chapter. TI does not expose individual cases of corruption; however, it does train journalists to investigate and expose cases of corruption in their countries. Thus TI works to make long-term gains against corruption by focusing on prevention and reforming systems.

TI has worked with the leading industrialized nations of the world, through the Organisation for Economic Co-operation and Development (OECD), in establishing an antibribery convention for its member states. Chapter members in European nations, especially in Germany and France, pressured their own governments to support the pact. Moreover, TI insisted that there be effective monitoring systems. Earlier, Latin American TI chapters cooperated to enact an antibribery convention in that region.

A principal vehicle for combating corruption is providing information or transparency, hence the name. TI has received much media attention and therefore has been effective with its annual Corruption Perception Index (CPI). The CPI is a list of countries (146 in 2005) in rank order from least corrupt to most corrupt. To compile this index, TI uses 18 surveys of businesspeople and country analysts that inquire about a country's corruption; they will not list a country unless they have at least three polls. Statisticians at TI then average these polls to arrive at their annual list. TI held its first annual meeting in 1994 and began publishing the CPI in 1995. In the current CPI ranking, the least corrupt are Finland, New Zealand, Denmark, Iceland, and Singapore; the United States is number 18 out of 146 countries. The most corrupt are Chad, Myanmar, Nigeria, Bangladesh, and Haiti. For the current CPI, the annual ranking of countries, and much other valuable information on TI, see TI's Web site (http://www.transparency.org).

TI found that corruption is rampant in 60 of the 146 countries that it ranked and that the public sectors of those countries are plagued by bribery. These 60 countries scored less than 3, compared with a clean score of 10 on the TI list; a total of 105 countries scored less than 5 on that list. TI also measures the countries in which corruption seems to be decreasing, and those countries in which it is increasing. TI challenged the myth of the northern moral superiority of the industrialized nations when it developed data showing that private firms from wealthy northern nations were principal agents undermining governments in developing nations because of their bribes.

TI responded to criticism that in its index it was only listing the countries that receive bribes and that those bribes often come from people in wealthier countries. Thus, they now also publish a Bribe Payers Index (BPI). The BPI is a rank order list of those countries from which it is perceived that bribes are initiated. TI was also appointed the Secretariat for the International Anticorruption Conference, and it has organized conferences in Peru, South Africa, the Czech Republic, and South Korea.

TI also provides information in its annual *Global Corruption Report* (GCR), which presents an overview of the state of corruption around the globe. The report brings together news and analysis. The report focuses on reforms, along with national and regional trends, in articles by journalists, NGOs, and academics from around the world. The 2005 edition focuses on *Corruption in Construction and Postconflict Reconstruction.*

The Business Principles for Countering Bribery is a cooperative initiative of TI and Social Accountability International. It is offered as a benchmark for business firms in designing their own anticorruption principles. Developing these principles followed TI's approach of cooperating with other groups, and it is seen by TI as the first step of a long-term process of working with the private sector to raise the standards of practice to counter bribery. The principles were drawn up in partnership with representatives of business firms, universities, trade unions, and other nongovernmental bodies.

The World Bank and its lawyers initially opposed the work of TI. However, in 1995, a new World Bank president joined the effort to combat corruption because he saw that corruption was thwarting the bank's development programs. Some political and business leaders from around the world have supported TI's efforts, often at considerable cost to themselves. When TI examined institutions in various countries, it found that again and again political parties are the most corrupt institution; this was also true in the United States.

A search of business articles (e.g., one conducted through LexisNexis) on the subject of TI shows the widespread and profound impact TI is having on countries and firms worldwide. Local news organizations around the world publicize the TI index, either praising their country's high ranking or publicizing and perhaps making excuses for a country's low ranking. For example, Nigeria was ranked third from last, and commentators said that it is unfair to compare the bribery in poor countries with that in wealthy countries, which have a developed social welfare system that cares for people's needs. In another incident, the national president of Kenya's chapter of TI in 2002 was asked by a new president to help clean up corruption in the country. But he resigned 2 years later because there had been so little progress in combating corruption.

—*Gerald F. Cavanagh*

See also Caux Principles; Disclosure; Global Codes of Conduct; Global Reporting Initiative; International Organization for Standardization (ISO); Organisation for Economic Co-operation and Development (OECD); Transparency; Triple Bottom Line; United Nations Global Compact; World Bank; World Economic Forum

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Triangle Shirtwaist Fire

The Triangle Shirtwaist Factory is best known as the site of a deadly fire that blazed for 18 minutes in the late afternoon of March 25, 1911. On the ninth floor of the Asch Building, which housed the factory just off Washington Square in New York City, hundreds of young women and girls were trapped by fire. Thirty or more workers jumped to their death on the pavement below, while more than 100 working girls burned on the factory floor. The resulting public outrage prompted the creation of the New York Factory Investigating Commission. This commission launched an era of remedial factory legislation.

Throughout the late 19th and early 20th centuries immigrant girls and women were recruited to work in the garment industry sweatshops. Italian, Jewish, Polish, and Slavic women worked long hours in these unventilated and minimally heated factories. Although female workers were actively recruited into the recently organized International Ladies' Garment Workers' Union (ILGWU), the founders of the union believed that women had neither the ability nor the commitment to sustain leadership roles in the union.

The garment industry was thriving as working women became eager consumers of ready-made clothing. As profit opportunities grew for factory owners, they cut wages, put more workers in smaller spaces, and introduced strict workplace monitoring to reduce pilferage and wasted time. Firsthand accounts of life in the factories describe them as cramped and filthy. In November 1909, a mass meeting of factory workers convened in New York to demand better wages and improved working conditions. When the male leaders hesitated to commit to a plan, a 15-year-old Ukrainian-born girl stood up and called on her fellow workers to strike. The response to her call began the Uprising of the Twenty Thousand.

Within 2 days, 20,000 to 30,000 factory workers in New York went on strike. The walkout quickly spread to Philadelphia and became an important milestone in the women's labor movement. For 3 months the workers picketed in the cold, withstanding the hardships of weather and lost wages in hopes of improved conditions, hours, and wages in the sweatshops. In February 1910, an arbitrated settlement was reached with most of the factory owners, although some refused to sign the agreement. One of these was the Triangle Shirtwaist Factory, where Clara Lemlich, the instigator of the Uprising, worked.

Triangle's ninth-floor factory rooms had inadequate fire escapes, no sprinklers, and exit doors locked from the outside to prevent worker theft of materials. When fire broke out, spreading quickly through hanging fabric and paper patterns, 500 women and girls were trapped inside. A few escaped by running to the roof, or getting the last run of the elevator downstairs, but many resorted to jumping out the windows, crashing to the ground as appalled observers watched. By night, 146 corpses were piled on the 26th Street pier.

In December 1911, the owners of the Triangle Shirtwaist factory went on trial for manslaughter. Despite enormous public outrage and grief, the all-male jury returned a verdict of not guilty, in response to the judge's insistence that the owners could only be found guilty if the jury believed that they knew the workshop exit door to the stairway was locked. However, over the subsequent 3 years, 36 new laws were enacted following the recommendations of the Factory Investigating Commission to reform the state labor code and mandate safer working conditions in factories. One commission member was Frances Perkins, who later became secretary of labor in the Roosevelt administration.

—Robbin Derry

See also Employee Protection and Workplace Safety Legislation; Employee Rights Movement; Industrial Policy; International Labour Organization (ILO); Labor Unions; Occupational Safety and Health Administration (OSHA); Sweatshops; Working Conditions

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TRILATERAL COMMISSION

Founded in 1973 with the support of David Rockefeller and other notable private citizens, the Trilateral Commission has sought to create a forum for substantive contact between corporate and other social leaders concerned with more closely aligning business and governmental actions in three regions of the world. The Commission hosts an annual meeting and also publishes studies and reports (*Triangle Papers*) that cover a wide range of topics.

The Commission is one of a number of major organizations whose members influence public policy discussion and formulation, especially in terms of international affairs. *Trilateral* refers to the three major geographic areas of democracy and wealth: Pacific Asia (particularly Japan), Europe (especially the European Union countries), and North America (the United States and Canada, with Mexico recently added).

Membership in the Trilateral Commission is by invitation. Currently there are about 350 high-level individuals from business, public service (excluding current political officeholders), media, academia, labor unions, and other nongovernmental organizations. Leadership consists of the regional chairmen, deputy chairmen, and directors, along with an executive committee of approximately 40 other members.

The Commission's mandate has been to encourage its members to build institutional linkages within the major democratic industrialized areas of the world that focus on international collaboration. The Trilateral emphasis on the importance of geopolitical interdependence has in fact borne fruit—helping mitigate friction on a number of issues such as trade between nations—and the Commission is among the leading proponents of greater global integration.

Because so many Trilateral members are also active in similar international business groups working outside the glare of regular news reporting, the organization has been subject to much criticism. For example, the Commission has been seen as a front for large corporate interests more concerned with setting up a global state than in protecting national sovereignty. Thus it is not uncommon to see the Trilaterals linked with the Council on Foreign Relations and the Bilderberger group, among others, as part of a loose-knit "family" of foreign policy conspirators. This, of course, is a matter of dispute. However, a continuing ethical concern involves the substantial amount of behind-the-scenes corporate power-wielding that occurs without much publicity or democratic accountability.

—Richard Alan Nelson

See also Bilderberg Group; Council on Foreign Relations; Global Business Citizenship; Globalization; International Business Ethics; United Nations; Vatican Bank

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Triple Bottom Line

The "triple bottom line" captures the three ways in which a company's performance can be conceptualized and measured. John Elkington refers to these three domains as economic prosperity, environmental quality, and social justice. The concept of the triple bottom line implies that a company's effectiveness cannot be judged by financial performance alone. To become more sustainable, a company needs to meet the requirements and expectations of most, if not all, of its stakeholder groups, which include shareholders, employees, customers, suppliers, the local community, and the natural environment. Performance with respect to all these stakeholder domains is reported, for example, in Global Reporting Initiative (GRI) measures, on which an increasing number of companies rely. However, some observers argue that even future generations must be considered in such stakeholder measures since the UN's Brundtland Report defined *sustainable development* as "development that meets the needs of the present world without compromising the ability of future generations to meet their own needs." The concept of the triple bottom line pays tribute to the interdependence of the aforementioned three broad areas, in the sense that there is no social progress without economic development and there is no economic or social prosperity without ecological sustainability. Furthermore, the concept acknowledges the interrelationships between these three areas, which are in constant flux due to social, political, economic, and environmental influences.

Economic Prosperity

This element of the triple bottom line represents, to some extent, a company's conventional financial bottom line. Usually, profitability is used as a proxy of the financial strength and value of a company's physical and financial assets. As per standard accounting practice, profit figures are expressed as earnings per share (EPS) or return on assets (ROA). However, under the triple-bottom-line nomenclature, economic prosperity is a broader concept than financial performance because it takes into account a company's direct and indirect economic impact on various stakeholders (e.g., in the form of investments, dividends, or wages). For example, to achieve economic prosperity, companies use and deploy human capital or knowledge-based assets. To achieve economic prosperity, companies must constantly evaluate their employees' skills, experiences, and knowledge. These elements are often dubbed *intellectual capital,* which companies must maintain, develop, and enhance to achieve economic prosperity.

Hence, the concept of the triple bottom line requires that companies think more broadly about economic prosperity than just ROA. Particularly the sustainability agenda pushes toward long-term business planning. For example, Porter and van der Linde argued that, especially in the long run, there is no trade-off between environmental protection and economic competitiveness. Furthermore, a psychometric meta-analysis by Orlitzky, Schmidt, and Rynes showed that the empirical links between the economic, social, and environmental dimensions of corporate performance are, on average, positive and strong or moderately strong. In contrast, conceptualizing social and ecological improvements as in "natural" opposition to business success may only hinder the implementation of the triple bottom line. Therefore, in line with the empirical evidence, corporate executives must be persuaded that this broader thinking about company performance (as explained by three complementary, or synergistic, rather than contradictory forces) will, in the final analysis, pay off for the companies that they lead.

Environmental Quality

Environmental quality addresses the ecological bottom line. It focuses on a company's impact on the natural environment. Environmental resources consist of renewable resources (e.g., wood, fish, corn) and nonrenewable resources (e.g., soil quality, fossil fuel). The natural environment also provides so-called ecosystem services, such as climate stabilization and water purification. Many of these services are presently invaluable, that is, either no known substitutes exist or there is one available only at a prohibitive price. To achieve environmental quality, companies should consume natural resources at a rate below either their natural reproduction or the development of substitutes. They should not emit pollution that is greater than that which can be absorbed by natural systems.

This argument running opposite to conventional economics is that not all types of natural resources and ecosystem services have substitutes in the form of economic capital or technological innovations. In the short run at least, many resources and ecosystems are irreplaceable. Complex combinations of various natural resources in an ecosystem restrain their substitutability. Forest ecosystems, for example, offer raw material for paper (which is substitutable), but forests also absorb carbon dioxide (CO_2), regulate the flow of rainwater, and provide protection for native plants and animal species. Hence, in many ways, environmental quality and economic prosperity are complementary. Companies have to improve or maintain the quality of natural resources to provide for their long-term economic prosperity. This improvement or maintenance represents the aforementioned investment in *natural capital,* which is likely to explain the performance of future, sustainable organizations.

One of the foremost goals in achieving environmental quality is eco-efficiency. According to the World Business Council for Sustainable Development (WBCSD), *eco-efficiency* is achieved by the delivery of competitively priced goods and services that satisfy human needs and bring quality to life, while progressively reducing ecological impacts and resource intensity throughout the life cycle, to a level at least in line with the Earth's estimated carrying capacity. More specifically, eco-efficiency can be achieved through (a) dematerialization, which involves the substitution of knowledge flows for material flows or product customization; (b) production loop closure, which returns every output to natural systems as a nutrient or as an input to future manufacturing; (c) service extension, in which customers lease rather than buy goods, especially durable goods (such as interior furnishings); and (d) functional extension, which enhances the functionality of products, often in the form of additional service delivery.

Social Justice

Social justice refers to the company's human and social bottom line. This element of the triple bottom line is often called "corporate social responsibility" (even though many scholars would consider social responsibility to include environmental responsibilities as well). Social justice concerns a company's impact on knowledge, skills, motivation, and loyalty of employees and business partners. Proxies for this impact might be turnover, training opportunities, and occupational health and safety within the company. More broadly, social justice also refers to how a company may influence social aspects in its relationships with various external stakeholders, such as involvement in community projects, entrepreneurial culture, and encouragement of innovative suggestions furthering social progress.

To accomplish social justice, companies need to add social value to the communities within which they operate. They can do this by effectively communicating with their stakeholder groups, involving their stakeholders in learning and development opportunities, increasing the number of choices available to customers, and respecting property rights.

A problem with such an aim is that a company typically cannot satisfy all stakeholders simultaneously. Some decisions in favor of certain stakeholders may require trade-offs (e.g., capital invested in state-of-the-art recycling technology will prevent this money from being invested in workers' training and development), which makes these types of business decisions inherently distributive. However, an acknowledgment of this balancing act does not necessarily imply an inevitable erosion of *social capital,* which is a capability that arises from the prevalence of trust in a society (or in certain sectors of society). Because the level of trust between a company and its external stakeholders is a key determinant of long-term survival, a company must clearly identify the status of certain stakeholder claims and, more often than not, engage in a variety of stakeholder dialogues and partnerships.

Like natural resources, social resources are not always substitutable. Companies can introduce economic incentives (e.g., lower prices of products or higher salaries) to substitute for dissatisfaction of their stakeholders. However, economic substitutes have their limits in a social context. Certain social resources such as community spirit, innovative culture, or reputation have no traditional economic substitutes. Hence, in many ways, social justice or social responsibility can be seen as a precondition for a company's economic prosperity and environmental sustainability.

The triple bottom line emphasizes the need for integration of these three dimensions of economic prosperity, environmental quality, and social justice. The concrete measurement of these dimensions aids in this integration in practice.

Triple-Bottom-Line Reporting

The metaphor of the triple bottom line highlights the importance of measurement and reporting in all three domains of company activities and impact. In line with the increasing popularity of the triple bottom line, many corporations shifted from reactive, accounting-based reporting to proactive, value-added, and comprehensive reporting of a company's performance. Triple-bottom-line reporting is supposed to address both primary stakeholders (e.g., employees, investors, business partners, customers) and secondary stakeholders (e.g., governments, social activists, communities, the media) and provide these stakeholder groups with valid, comprehensive, and reliable data about a company's economic, environmental, and social performance. Apart from financial indicators, a company's triple-bottom-line report typically includes narrative statements (such as an explanation of equal employment opportunity policies and programs) and environmental impact measures (such as amount of waste by type and destination).

Although there is at present no universally accepted reporting model, the GRI is a comprehensively developed framework that is widely used. Established in 1997, the GRI sought to bring together business executives, accountants, social and environmental activists, labor organizations, the United Nations Environmental Programme (UNEP), and governments to enhance the comparability and legitimacy of triple-bottom-line reporting standards worldwide. The GRI elements are (a) CEO statement; (b) key indicators; (c) profile and financial performance; (d) policies, organization, and management systems; (e) stakeholder relations; (f) management performance; (g) operational performance; (h) product performance; and (i) sustainability statement. However, so far, integration of these different domains of the triple bottom line has proven elusive. Triple-bottom-line principles similar to the GRI have been promoted by the Caux Roundtable (a coalition of European, U.S., and Japanese business leaders) and the Clarkson Centre for Business Ethics & Board Effectiveness, as well as a number of private organizations, such as SustainAbility, Trillium Asset Management, and KLD Research & Analytics, Inc.

Reporting about the traditional bottom line (i.e., the company's financial performance) is a well-established practice grounded in standard methodology and common systems. Yet, as mentioned before, under the triple-bottom-line approach, economic performance is more broadly defined. Therefore, a step toward more comprehensive reporting on companies' economic prosperity has been made by replacing the conventional financial performance indicators, such as ROA or return on earnings (ROE), with economic value added (EVA), an indicator promoted by several U.S. investors. Application of EVA shows whether a company is adding or destroying value. Within this reporting approach, profit figures are adjusted for the expenses of the environmental resources (natural capital) employed.

The 1990s saw a tremendous growth in environmental reporting. However, the practices of environmental accounting and reporting have been inconsistent and varied across industries, regions, and governmental requirements. To improve the situation, the International Chamber of Commerce has developed the Charter for Sustainable Development, which consists of 16 principles for environmental management. The Charter has provided a common basis for improving business environmental performance, thereby minimizing reporting differences. By the end of the 1990s, a majority of large corporations in the United States (more than 50%) and the United Kingdom (more than 75%) issued environmental reports.

Social accounting and reporting began to gain advocates and practitioners a few years after environmental reporting. Social accounting measures the quality of stakeholder relationships and social performance of a company. In 1997, the U.S. Council on Economic Priorities developed a code of conduct named Social Accountability 8000 (SA 8000), which defines both the criteria for workplace conditions and a system of independent verification of factory compliance. Then, in 1999, UN Secretary-General Kofi Annan announced the proposal to create the UN Global Compact at the World Economic Forum in Davos, Switzerland. The Global Compact provides nonbinding recommendations related to corporate social performance. In another effort, the Institute for Social and Ethical Accountability (ISEA), formed in 1995, created accounting and auditing standards in a comprehensive framework that is called AA1000. Companies such as The Body Shop, British Telecom, and Royal Dutch/Shell, together with organizations from the nonprofit sector, joined up to be proactive in implementing the AA1000 standards with independent assurance. These developments suggest that in only a few years social reporting evolved from a marginal to a central activity of many large companies.

One of the major challenges with respect to triple-bottom-line reporting lies in the integration of environmental and social reports in the company's conventional accounting systems. Environmental and social reports are qualitatively different from financial accounting and auditing. In the case of the former two domains, there is currently an absence of standard methodology as they are more open to subjective opinion or interpretation. Some areas of environmental and social performances, such as the level of trust or employee morale, are measured by collecting stakeholders' perceptions of performance. Information is usually collected through interviews, focus groups, surveys, and stakeholder meetings. For example, the AA1000 framework provides guidance on the selection and administration of these data collection techniques. Some other areas of performance, such as sponsorship and gas emissions, can be measured through the use of more "objective" data. In short, economic performance is assessed with standardized systems and protocols, whereas environmental and social accounting systems still suffer from an absence of standard methodology and lack of accounting and auditing experience. Because of this ongoing debate about environmental and social reports, though, it becomes essential for business to assess these domains internally—via regular *responsibility,* or *social audits.*

Critiques

The concept of the triple bottom line has attracted a few critics, who claim that the concept is synonymous with *corporate social responsibility* and is not novel. Furthermore, the aforementioned lack of standardized, aggregate measurement has been criticized. Critics often contrast the triple bottom line with the concept of the financial bottom line, which they consider internally consistent. Yet, as argued by Meyer and Gupta, there is empirical evidence that different measures of economic performance not only *can* contradict each other but also are in fact *likely* to do so. In fact, financial measures may be as prone to measurement error and deliberate distortion as other organizational performance variables. There have been several important developments that represent clear attempts to bring triple-bottom-line measures (e.g., GRI) in line with the concept and thus enhance construct validity. Given the relatively brief history of this comprehensive model of organizational effectiveness, it may be unrealistic to expect perfect measures. Different business contexts militate against a "one-size-fits-all" model of the triple bottom line for any firm of any scale in any industry.

Motivations

Since 1997, the concept of the triple bottom line has gained tremendous currency, especially among managers of large international corporations whose reputation is on the line on a daily basis. Of course, companies adopt the triple-bottom-line principles for a variety of reasons. Some do so because their executives believe in and espouse these principles. Other managers embrace the concept (at least publicly) because they are expected to comply with stakeholder values or because they regard this approach as a useful marketing tool. In short, there may be all kinds of "motivations" of triple-bottom-line accounting. As the triple bottom line can be conceptualized as an inherently moral-normative concept, the second-guessing of ulterior business motives is understandable. However, raising questions about company motives is confused for two main reasons. First, some authors regard Elkington's notion of sustainable development as inherently utilitarian. This means it is primarily concerned with business contributions to social value and minimization of environmental impact as two *outcome* measures, or *consequences,* of company performance. Second, more generally, attributing "motivations" to organizations ascribes human features to these social entities at the collective level. Talk of some "corporate motivation" may misapply a fundamentally individual-level concept to higher levels of analysis in social theory. Hence, in the end, such ethical fault-finding in organizational motives might often be counterproductive because, ultimately, motives can only be inferred at individual levels of analysis, whereas outcomes can be measured and evaluated at higher levels.

Conclusion

The triple-bottom-line concept, in general, addresses the evolving relationships between business and society. Such relationships involve complex issues of measurement and assessment of a company's performance through three different lenses. It also requires careful consideration of various aspects of stakeholders' perceptions of business processes and outcomes. Therefore, the main challenges continue to lie in the operationalization of the triple bottom line. The implementation of the triple-bottom-line philosophy requires integrative dialogues between stakeholders that seem to be in opposition—for example, companies and environmental groups, shareholders and employees, industries and local communities, and governments and businesses. These stakeholder groups need to develop various partnerships to reconcile tensions between their goals and achieve integration of economic prosperity, environmental quality, and social justice. Some recent empirical research indicates that many of these tensions and oppositions may be dysfunctional social constructions that are, in the final analysis, more apparent than real.

—Marc Orlitzky and Ljiljana Erakovic

See also Caux Principles; Clarkson Principles for Business; Consequentialist Ethical Systems; Corporate Accountability; Corporate Citizenship; Corporate Social Financial Performance; Corporate Social Responsibility (CSR) and Corporate Social Performance (CSP); Global Reporting Initiative; Internal Audit; Motives and Self-Interest; Natural Capital; Social Audits; Social Capital; Stakeholder Engagement; Stakeholder Responsibility; Stakeholder Theory; Sustainability; United Nations Environment Programme (UNEP); Utilitarianism

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TRUST

Trust is essential for establishing and maintaining mutually advantageous, even amicable, relationships in business or other cooperative social arrangements. A violation of trust will severely test and may end the relationship. There is an old saying that trust arrives on foot but leaves on horseback.

The Definition Problem

Despite nearly unanimous agreement on the importance of trust as a lubricant for expediting market exchanges and as a glue for cementing cooperative relationships in that market, scholars have failed to achieve consensus on its definition. They have tended to focus on different aspects of trust observed through different disciplinary lenses in a wide variety of contexts, from individual (micro) to organizational (meso) and even societal (macro) levels of analysis and at different stages of development.

Virtually all definitions of trust include two conditions. (1) *Vulnerability*—The person who trusts someone else voluntarily places valued assets at risk when entering into a one-time exchange or an ongoing relationship with another party. (2) *Expectation of reciprocal regard or treatment*—The prospect of mutual gain from cooperative behavior gives rise to an obligation to treat each other fairly, that is to say, without opportunism or guile, and with some expectation of goodwill in the face of vulnerability. Even where trust may appear blind, as in the case of an infant's dependence on its mother, there is an implicit expectation of unqualified goodwill. Blind trust of a stranger may be either foolish or saintly, but it is hardly rational. Consider the case of hiring a babysitter. Parents place their children at some risk when they invite a stranger to serve as a caregiver while they are away. They can mitigate this risk by investigating the background and qualifications of the sitter. They might check on the certification of the candidate by a professional babysitters' association. In the absence of such macro-level institutional assurance, they could ask for letters of reference, either from previous clients or from reputable persons who could attest to the candidate's sterling character and love of children. References from known parents in the neighborhood would weigh more heavily than the word of strangers. Hiring a relative would be even more reassuring, given the strong ties of family feeling. Direct evidence of the sitter's qualifications could be gathered once employment commenced. Especially cautious parents might set up a secret "baby cam" to monitor electronically the sitter's behavior in their absence, possibly providing a live feed to a security firm. However, this kind of covert monitoring would seem better suited to allaying distrust. Trust is most likely to arise from the sitter's personal interactions with the family while providing impeccable care. This history of trust-based behavior can cement a long-term employment relationship and even develop the affective bonds of friendship. Thus, trust arises both from the prospect of vulnerability and from efforts to mitigate that risk by forging bonds of reciprocal benefit and regard.

Different Disciplinary Perspectives on Types and Levels of Trust

In general, psychologists have tended to focus on the internal cognitive attributes of those who confer and seek trust, primarily at the interpersonal (micro) level of interaction. Economists have tended to think of trust in terms of ways of minimizing mistrust in economic transactions at the interpersonal or firm (meso) level of analysis. Sociological treatments have focused primarily on the meso (network) and macro (societal) levels of analysis, where trust is treated as an organizational or institutional variable embedded in relationships. Philosophers have devoted remarkably little attention to trust, other than as a desirable indirect outcome of principled action after considering what is right, just, and fair in governing relationships. The recent emergence of turbulent, hypercompetitive market conditions has stimulated considerable cross-disciplinary interest in finding ways of mobilizing trust over time within knowledge-creating networks. A convergence of perspectives on trust across disciplines and at different levels of analysis points to the need for better understanding of the role of ethical, trust-based governance within networks in efforts to develop and sustain a dynamic competitive advantage over time. Thus, much of the definitional confusion can be resolved by recognizing that different disciplines tend to focus on the trust phenomenon at different levels of analysis and from either static or dynamic (stages of development) perspectives. Special attention will be devoted to the treatment of trust within the discipline of economics since this treatment underlies transaction cost assumptions about the role of corporate governance mechanisms for minimizing mistrust in hierarchical relationships.

The Transaction Cost Economics Perspective on Trust

When complete contracts govern discrete market transactions—where the terms of one-time economic exchanges are specified, costs and benefits to both parties are measurable, and the contract is enforceable under the law—there is little need for trust. Under such circumstances, valued resources of the buyer and seller are hardly at risk. Trust has potentially greater scope when contracts are "incomplete" or "relational." Such contractual relationships are open-ended and emergent over time, where the terms are not specified fully and thus are subject to learning-based clarification or renegotiation as the exchange relationship unfolds. Institutional economist Oliver Williamson argues that incomplete or relational contracting is much more common than is complete contracting, particularly at the meso level, where business firms are engaged in ongoing economic exchange relationships. This insight gives rise to the "transaction cost-based" theory of the firm, whereby Williamson and others argue that managerial monitoring of underspecified relational contracts, backed by corporate governance mechanisms to control for potential managerial opportunism, tends to minimize transaction costs of hierarchical relationships inside the firm.

Since Williamson defines opportunism as the pursuit of self-interest with guile, it becomes quickly apparent that trust is severely circumscribed within the transaction cost-based theory, as well as in the closely associated "agency theory" of corporate governance. Agency theorists, such as Michael Jensen and William Meckling, argue that the innate opportunistic, self-serving inclinations of human nature must be taken into account by the design of managerial control and incentive systems within the firm. They propose dealing with the "agency problem" (where managers are inclined to serve their own, rather than the ownership, interest) by more closely aligning the interests of managerial agents and shareholder principals. Taking maximization of shareholder value as the unitary purpose of the firm, agency theorists seek closer interest alignment between agents and principals by improving transparency in financial reporting, minimizing conflicts of interest, and designing executive compensation schemes weighted toward bonuses and stock options that pay for superior *financial* performance. Managers are paid to think and act like owners. Such structural remedies seek to recognize and compensate for the inherent *untrustworthiness* of human nature. Many economists are inclined to regard trust as more of an irrational, idiosyncratic, emotional state of mind, which cannot assure efficient and profitable market transactions. Indeed, most of the control and incentive schemes offered by agency theorists and transaction cost economists seem more intent on deterring outbreaks of self-interest with guile, rather than on enhancing trust. Thus, deterrence-based "trust" is the outgrowth of efforts to diminish distrust by controlling for the potential of opportunism, rather than a form of trust, per se.

Trust as an Embedded Source of Social Capital

Alternatively, a growing number of scholars have come to argue that trust has real economic value because it not only reduces monitoring and control costs in business transactions but also encourages cooperation, information sharing, and the joint creation of new knowledge, generated within or among firms—hence the recent interest in a "knowledge-based" (similar to a "resource-based") theory of the firm. The work of Janine Nahapiet and Sumantra Ghoshal is especially helpful in developing this argument. If the firm is a social community specializing in creating and transferring knowledge with speed and efficiency, then the key to developing the dynamic competitive capabilities of this network must lie in efforts to invest in and improve returns on a community's *social capital.* This term first appeared in studies of how and why some urban or regional communities developed networks of strong and weak ties that enabled trust and cooperative enterprise to emerge, innovate, and flower into collective action. The operative word here is *developed*—drawing attention to learning processes that enable forms of trust to evolve over time, strengthening and becoming more *embedded* in social relationships. As trust in social relationships builds, social capital accumulates from the cohesiveness and solidarity of strong ties and from the new information and multiple perspectives available in weak ties.

A Developmental Perspective—From Calculative to Relational Trust

Efforts across scholarly disciplines to arrive at a comparative and developmental framework of trust focused on aspects of *calculative* and *relational* trust. Calculative (sometimes called calculus-based) trust arises from the context of shallow or short-term dependence or interdependence between trustor and trustee, primarily at the interpersonal or organizational level of analysis. It is associated with treatments of rational decision-making processes in economic exchanges. A potential exchange relationship is evaluated to determine whether the likely return from cooperation outweighs the risk to valued assets placed in the hands of the trusted party. A positive evaluation of risk and return is based not only on the strength of deterrence safeguards (to reduce distrust) but also on the availability of evidence attesting to the credibility and competence of the trusted party. Given the shallowness or absence of a direct personal connection, trustworthiness is determined from indirect evidence, such as letters of reference or credit reports that attest to a person's or an organization's reliability, competence, and reputation for fair dealing.

The evolutionary stages of trust are mirrored in changes in the terms and conditions of the "prisoner's dilemma" game—a classic role-playing simulation of game theorists in which each "prisoner" must evaluate the costs and benefits of a self-interested or a cooperative strategy. When neither prisoner has any information about the motives of the other, then the winning strategy is to rat out the other prisoner in exchange for a reduced sentence. In the absence of information about the other prisoner's intentions, blind trust is foolhardy. However, Robert Axelrod has shown that a cooperative "tit-for-tat" strategy based on trust followed by verification of reciprocal regard offers more gains or, at least, reduced losses for both parties over time. By extending this game to an infinite number of plays, others have shown that a tit-for-tat strategy of building trust and cooperation over time has a higher payoff than do strategies of either unconditional opportunism or one-sided altruism. Thus, over the long run, self-interested rationality discovers the net benefit of at least some degree of cooperation with others. It is at this point of learned self-awareness of the value of working and living together with others over time that calculative trust begins to fade into relational trust.

Relational trust builds from a history of direct, personal interactions over time, where both parties demonstrate a willingness to forego the possibility of short-term gain from a default of contractual or moral obligations. Relational trust can arise out of the earlier stage of calculative trust, though some authors prefer to think of these as discrete forms of trust. The initial rational assessment of costs and benefits associated with an opportunity for cooperative exchange can be enriched by the growth of more emotional ties of friendship. Thus, relational trust is also known as "affective trust," where a handshake, or even a hug, can take on new meaning as the relationship deepens. Relational trust may evolve into an even deeper form, frequently called "identity-based trust." Over time, the reciprocal perception of "I" and "thou" can be transformed into the shared identity of a "we" relationship. Under conditions of deep interdependence, equivalent to a marriage, partners feel that they can act with the other party's interests in mind since their interests are virtually synonymous. Such deep emotional ties are not irrational since they typically are built over time from a history of mutual advantage and shared regard. Moreover, a violation of trust in a marriage or a friendship can be devastating to the relationship. Even so, a violation of calculus-based trust tends to be more damaging since shallow relationships built on rational calculations and indirect evidence tend to be more fragile when they are not supported by subsequent facts on the ground. Relational trust is more resilient because emotional bonds tend to stretch before they snap. An act of contrition followed by sincere efforts to renew commitment to the other can restore relational trust over time. Trust, but verify. In other words, honesty is the best policy, both in personal relationships and in business dealings, over the long or short run.

What is the connection between ethics and trust? Social scientists have been reluctant to trace a link between behavioral manifestations of trust and the normative realm of ethics. They prefer to describe and predict what "is" in the "real world," whereas moral philosophers are more concerned with deriving normative rules that point the way toward achieving an idealized "good life." The failure of philosophers to agree on a set of decision rules (Kantianism, utilitarianism, pragmatism, virtue ethics, and social contracting, among others) for deriving ethical norms has not improved prospects for integrating the realms of "is" and "ought." Economists, as reluctant and partial converts to the possibility that trust (as opposed to the deterrence of distrust) may have some economic value, are even more reluctant to confer on ethics a role in economic decision making. Business ethicists ask corporate executives to suspend their laser-like focus on profit whenever an ethical dilemma arises that requires consideration of the rights, values, and interests of nonowner stakeholders in the firm. When the bilateral obligations of principal-agent relationships are supplanted by the more complex, multilateral demands of a multistakeholder network, prospects for enacting a straightforward economic "rationality" dim. Economists resist normative calls for a more comprehensive corporate citizenship practice, to the extent that such calls appear to be driven by emotional appeals to altruism, rather than to the "rational" pursuit of self-interest. Management scholars, noting the growing role of intra- and interorganizational cooperation in leveraging competitive capabilities, have drawn attention to the importance of trust in developing and sustaining productive relationships. However, they have been less successful in showing how management practices that create and maintain trust relate to ethical governance.

Remarkably, even moral philosophers have not considered the trust/ethics connection very carefully. LaRue Tone Hosmer, a notable business ethicist, observed that philosophers tend to regard trust in relationships as a fortuitous by-product of the responsible application of ethical judgment. However, trust becomes a central concern and an essential output of ethical decision making in the "good life" when all members of a community come to realize that they can't achieve their own ends without taking into account the rights and interests of others. Ultimately, ethical norms guide the actions of men and women of *goodwill,* who voluntarily assume the risks and responsibilities of working out productive relationships according to the principles of fairness and justice. Thus, trust necessarily arises from an amalgam of self-interested and other-regarding motives, neither of which is sustainable separately for long in the real world.

Trust in Ethical Governance Processes

In the *Academy of Management Review* special issue on trust, Blair Sheppard and Dana Sherman relate different processes for producing trust to the kinds of risks associated with the shallowness or depth of dependent and interdependent relationships. Thus, in a context of shallow dependence, a calculative trust assessment of the risk of a party's unreliability in living up to the terms of a short-term exchange relationship is reinforced by deterrence-based safeguards against opportunistic violation of a reasonably complete contract (a lawsuit, regulatory action, etc.). In a context of deep dependence, however, such as one in which risk to the welfare of a child is involved, deterrence threats are reinforced by claims of obligation that are binding, not only on the party who may harm the child but also on those in a social network who may be aware of the potential for harm. When harm does occur, blame is placed not only directly on the perpetrator but also indirectly on anyone who should have exercised an oversight responsibility. Thus, in situations of deep dependence, the expectation of procedural justice to minimize the risk of harm is closely associated with the condition of trust. Expectations within such relationships take the form of psychological contracts, which are tested periodically, followed by occasional clarification or renegotiation to assure that all parties understand and live up to their obligations. Relational trust may well develop in this context, but the vertical relationship tends to be stable over time. In situations of shallow interdependence, parties in ongoing horizontal relationships must engage in active discovery through exploratory dialogue, often facilitated by contiguity (such as the colocation of parts suppliers and assemblers) and electronic communication linkages. This is the equivalent of prisoners confronting the dilemma of whether to cooperate by opening a communication channel to explore ways to cope with uncertainties in their relationship. Such exploratory exchanges tend to forge the affective bonds of relational trust, which facilitate coordination and cooperation within an open-ended, emergent relationship. In the context of deep interdependence, identity-based trust is produced when parties in an ongoing relationship have internalized each other's values and preferences to a point where the risk of mistaking each other's intentions is controlled by discursive construction of a shared meaning.

Conclusion

The above analytical and developmental framework has powerful implications for the role of ethical governance processes in building and sustaining trust. In situations of shallow dependence, rational calculations of the risk of unreliable or incompetent behavior, backed by institutional mechanisms for deterring distrust, leave a relatively modest scope for ethics as an auxiliary tool for minimizing transaction costs in short-term exchanges. Ethical considerations have a larger role in reinforcing the normative obligations associated with deep dependency in more lasting vertical relationships. Ethics has a critical role to play in generating affective and identity-based trust within learning processes that govern interdependent relationships, particularly at the meso level of intra- and interorganizational alliances. To the extent that capability building (especially knowledge creation) supplants cost reduction as a rationale for cooperation, the production of relational trust via dialogic interactions is essentially an investment in social capital, from which increased cooperation in the production of new knowledge flows. While deep dependence obligations can be embedded within hierarchical relationships, sustaining both shallow and deep interdependence requires a collaborative, consultative style and open communication for managing near-horizontal relationships among network partners. To the extent that knowledge creation in interdependent networks supplants transaction-cost reduction in hierarchies, the scope for ethical interactions among managers and stakeholders of value-creating networks will grow. When value is defined more broadly, to encompass social and environmental as well as economic measures, the management of complex stakeholder networks must take into account more fully the role of trust and ethical obligations of fairness and justice to govern cooperative efforts to realize the promise of the good life.

—Jerry M. Calton

See also Cognitivism and Ethics; Corporate Governance; Economics and Ethics; Prisoner's Dilemma; Self-Interest; Social Capital; Stakeholder Theory

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Trustees

A trustee is a person who safeguards the assets or property of a trustor for the benefit of a third party who is the beneficiary. In law, a trustee is someone who has the legal authority to manage money or property on behalf of another person. However, the trustee, the trustor, and the beneficiary may be the same person or multiple persons. A trustee can also be a member of a group of people, known as a board of trustees, which is responsible for managing the financial affairs of an institution or organization. The first section of this entry presents specific examples of trustee appointments and their general roles. The second section reviews a trustee's fiduciary duties. The final section offers a brief history of trustees.

Types of Trustees

In its simplest form, a trust is nothing more than an agreement between a trustee and a trustor by which the trustor places assets in the hands of a trustee who then minds them for the trust beneficiaries. A trust is used when a person is unable or unwilling to manage his or her own assets and, thus, places them under the direction of a trustee. A trustee is expected to manage the assets as the trustor would if he or she were willing and able.

Trusts have become increasingly common and popular because of the flexibility they offer in estate and tax planning. Trusts can be used to avoid the expense of probate proceedings, save on estate taxes, support a favorite charity, provide for children, or take care of a pet after the death of a person. Trusts can be used to shield assets from lawsuits and creditors. Trusts can operate during the life of the benefactor and after his or her death. A trustee can be a responsible family member, a friend, or an adviser. Trustees can be changed at the discretion of the trustor.

Trustees may be designated by a trust agreement or by a will, or they may be named or appointed by a court. A corporate charter may enable a bank or trust company to act as a trustee. Trustees may be elected, as in the case of a township trustee, who acts for the benefit of the public. Township trustees provide essential services to the residents and businesses of a township. Areas of responsibility include the township budget, fire and police departments, parks and recreation, zoning and planning, small-claims court, emergency medical service, schools, community centers, shelters, and libraries.

Trustees may be persons who are charged with managing or disposing of the property of a debtor. Trustees may also be any group or board of persons elected or appointed to manage the affairs of an institution such as a college, hospital, library, or other not-for-profit organization. In some cases, the board of trustees is also known as the board of directors. Three examples follow of prominent types of trustees.

Trustees in Bankruptcy

The U.S. Trustee Program is provided by the Department of Justice to promote the efficiency and to protect the integrity of the federal bankruptcy system. The primary role of the U.S. Trustee Program is to serve as the "watchdog" over the bankruptcy process. To further the public interest in the just, timely, and economical resolution of cases filed under the Bankruptcy Code, the program monitors the conduct of bankruptcy parties and private estate trustees, oversees related administrative functions, and acts to ensure compliance with applicable laws and procedures. It also identifies and helps investigate bankruptcy fraud and abuse in coordination with U.S. attorneys, the Federal Bureau of Investigation, and other law enforcement agencies. A trustee may be appointed by the U.S. Trustee Program. A bankruptcy trustee may also be elected by creditors or appointed by a judge to administer the bankruptcy case.

The bankruptcy trustee's duties include (1) collecting and reducing the assets of the bankruptcy estate to cash, (2) operating the debtor's business with court approval if that is necessary to preserve the value of the business assets, (3) examining the debtor at a meeting of creditors, (4) filing inventory reports and making periodic reports to the court on the financial condition of the estate, (5) investigating the debtor's financial affairs, (6) examining and validating proofs of financial claims for and against the business, (7) furnishing information relating to the bankruptcy to interested parties, and (8) opposing discharge of debts through bankruptcy if advisable.

A trustee is appointed or elected in every bankruptcy case under Chapter 7 and Chapter 13 involving personal bankruptcy and under Chapter 12 for the reorganization of family farms. In most Chapter 11 cases involving businesses, the bankruptcy case is administered by the debtor or person going through bankruptcy, rather than by a trustee. The role of the trustee varies depending on the type of bankruptcy case.

Trustees of Not-for-Profit Institutions

Not-for-profit entities are organized to fulfill social or public service objectives rather than to generate profit for investors. The social objectives may be religious, charitable, educational, medical, research-oriented, artistic, or literary in nature. Not-for-profit entities rely on external funding rather than accumulated profits to maintain their operations. Funding may come from multiple sources including private donations, grants from government and foundations, revenue from the organization's activities, and income from the organization's endowment. Fund-raising is an aspect of trusteeship that differentiates trustees of not-for-profit organizations from board directors of for-profit corporations. In the case of arts institutions, trustees often act as both donors (trustors) through the money they provide and as trustees in supporting the values and goals of the institution. Trustees of arts boards are most often recruited from the ranks of the affluent who possess valuable skills, financial resources, or the ability to raise funds.

College and university trustees may be elected by voters or invited to serve as representatives of various constituencies. Universities operate through a system of shared governance, meaning that the trustees concentrate on the overall mission of the organization, while faculties take care of academic matters such as curriculum, teaching, and hiring and promoting professors. The overall mission is decisions about finance, physical planning, fund-raising, and hiring and firing presidents. The traditional roles of the trustees are to defend and promote the interests of the institution and to represent the concerns and needs of the public, which subsidizes and sustains higher education.

Trustees in Companies or Corporations

Managers of corporations may be trustees with a fiduciary duty to serve not only shareholders but also other parties. Corporate managers are trustees primarily in the administration of company-sponsored pension plans. Under the Employee Retirement Income Security Act of 1974 (ERISA), anyone who exercises discretionary control or authority over plan management or plan assets is a trustee (fiduciary) with obligations to the exclusive benefit rule; prudent person rule; diversification rule; and adherence to plan documents rule. The fiduciary may not get involved in a prohibited transaction—transactions involving plan assets, transactions involving employer real estate or securities, and transactions involving self-dealing. Acting in the interests of the employer and acting in the interests of the plan participants may create a conflict of interests.

Fiduciary Duties of the Trustee

Generally, a trustee's duties are to protect and preserve the trust property and to ensure that the property is used solely for the benefit of the beneficiary. Use of the property must be in accordance with the directions contained in the trust agreement.

A trustee has a fiduciary duty to the beneficiary or beneficiaries. A fiduciary duty requires one to subordinate all personal interests while acting for the benefit of another person. It is the highest standard of duty implied by law. Specifically, a fiduciary duty includes acting in good faith, disclosing information in all matters relevant to the trust relationship, loyalty to the beneficiary, obedience to the terms and instructions of the trust agreement, due care in making decisions, and acting for the express benefit of the beneficiary.

The fiduciary duties developed from a need to control the great amount of discretion available to trustees in the absence of the grantor or trustor. However, over the years fiduciary duties have expanded to situations unconnected to a trust. In addition to trusts, fiduciary obligations are found in many different types of relationships including principal and agent; doctor and patient; executor and beneficiary; banker and customer; lawyer and client; and board director and company. Thus, a trustee is a special type of fiduciary. Trustees are involved in fiduciary relationships, but not all fiduciary relationships involve trustees.

A fiduciary relation is a very broad term including both technical fiduciary relations and those informal relations that exist whenever one person trusts in or relies on another. The fiduciary relation is founded on trust and confidence invested by one person in the integrity and fidelity of another person. Such a relationship arises when one person depends on or is especially vulnerable to the actions of another, resulting in an uneven distribution of power and control in the relationship. The relation can be legal, social, domestic, or merely personal. A breach of fiduciary responsibilities makes the trustee liable to the beneficiaries for any damage caused by such breach.

Professional Expertise

The status of being a fiduciary gives rise to certain legal obligations, including the prohibition against investing the money or property in investments that are speculative or otherwise imprudent. In some states, the Prudent Man Rule states that a fiduciary such as a trustee for pension funds may invest the trust's money only in a list of approved securities designated by the particular state. In other states, the trustee may invest in a security if it is one that a prudent man of discretion and intelligence would buy to provide a reasonable income and to preserve the capital investment. In New York, the Prudent Man Rule applies to a trustee who is bound to employ the high degree of diligence and prudence in the care and management of a fund that prudent men of discretion and intelligence in such matters employ in their own affairs. A federal Prudent Man Rule that governs the investment of pension funds is found in ERISA. ERISA Section 404(a) requires a trustee to exercise the same care, skill, prudence, and diligence that a prudent person would use under the circumstances if he or she were acting in a like capacity.

The Prudent Man Rule is also known as the Prudent Investor or Prudent Person Rule. This principle applies to a fiduciary (trustee) who must invest in only those securities or portfolios that a reasonable person would buy. The origin of the rule is an 1830 case involving Harvard College versus Amory that stressed two points for a trustee to consider when making investments—probable income and probable safety. The trustee must consider both.

However, history has shown that a trustee's obligations extend beyond following the Prudent Man Rule that refers to an ordinary prudent man of business. In 19th-century England, complaints and cases brought against trustees were decided not by juries but by chancery judges whose decisions had the effect of setting precedents for increased responsibility and legal liability for the trustee. As a practical matter, trustees in England and also in the United States need to possess greater financial and professional expertise than an ordinary businessman to avoid violating the standard of due care in making decisions.

Personal Attributes

A trustee's personal attributes of integrity, loyalty, and setting aside self-interest in acting on behalf of a beneficiary are equally important. The classic case of *Meinhard v. Salmon* demonstrates that a trustee may not use his or her superior position of power and expertise to make a secret profit at the expense of a beneficiary. Justice Benjamin Cardozo made the following statement in 1928 upholding the importance of fiduciary duties (*Meinhard v. Salmon,* 249 N.Y. 458, 164 N.E. 545):

> Many forms of conduct permissible in a workaday world for those acting at arm's length are forbidden to those bound by fiduciary ties. A trustee is held to something stricter than the morals of the marketplace. Not honesty alone, but the punctilio of an honor most sensitive is then the standard of behavior. As to this there has developed a tradition that is unbending and inveterate. Uncompromising rigidity has been the attitude of the courts of equity when petitioned to undermine the rule of undivided loyalty by the "disintegrating erosion" of particular exceptions. . . . Only thus has the level of conduct for fiduciaries been kept at a higher level than that trodden by the crowd. It will not consciously be lowered by any judgment of this court.

Current Issues

Among the fiduciary duties that may be the most commonly neglected is the duty to provide to the beneficiary disclosures, information, and an accounting of trust transactions. Legal scholars and practitioners recommend changes to the U.S. Trust Code that would provide for resolution of trust beneficiary complaints about the absence of information about management of the trust; understandable accounting summaries of the transactions used to manage the trust; the size and nature of trust management fees; timely responses to inquiries made by the beneficiary; and the desire to be informed of or involved in the decisions made involving the trust's affairs.

Brief History of Trustees

Managers (trustees) were used to administer the Islamic *waqf* in the ninth century. The *waqf* consisted of property, land, farms, or oases that generated revenues for religious or charitable purposes. A *waqf* could also be used for private purposes. By declaring his estate as *waqf* and his descendants as trustees, a rich man could provide an income for his surviving family.

Other examples include the Knights Templar, who acted in a fiduciary capacity (as trustees) sanctioned by English royalty in the 12th century. The Templars were successful in circumventing religious objections to the lending of money for interest. Acting as fiduciaries, the Templars organized the payment of pensions, mediated transfers of funds from England to the Middle East, and provided international banking services.

Some authorities trace the origin of trusts and trustees to the medieval practice of knights leaving a trusted individual to safeguard their families and their land while fighting in the Crusades. Other legal historians claim that the modern trust has its roots in 13th-century England. At that time, the feoffee (pronounced "fee-fee") acted as a trustee for land held for the benefit of a third party. The term *feoffee* continues in use in the modern-day United Kingdom.

Trustees in Medieval England

The feoffee's (trustee's) role was to ensure that family assets were maintained intact for the benefit of the family. The need to place the protection of the beneficiary family and its interests above the interests of the trustee arises from the medieval idea of chivalry. The original protection for the beneficiaries was only the trustee's solemn oath to act properly to protect the beneficiary and the interests of the beneficiary in accordance with the instructions given by the trustor or the grantor. Originally, trustees could not accept payment for their good deeds, and only individuals could serve.

In some cases, feoffees held land and buildings for the benefit of Franciscan friars, who were forbidden to own any kind of property. Land was conveyed to a suitable person in the area to hold for the use of the friars. At the time of the trustee's death, the responsibility passed on to his heirs as successor trustees.

In the 13th century, the feoffee had title to the property, and the beneficiary was intended to have the possession of the property. Between the 13th and 15th centuries, no legal mechanism existed by which a beneficiary could seek action against a feoffee or trustee who did not perform his fiduciary duties. However, by the early 15th century, courts of equity, acting on behalf of the king, began to play a role. The primary means of resolving complaints by the beneficiaries about the feoffee was to appeal to the English chancellor, who enforced the obligation to protect the beneficiary and his interests.

As a consequence of the Statute of Uses in 1536, two types of trustees emerged. The passive trustee simply passed on the title to the property to the beneficiary. The active trustee assumed the imposed duty to manage the property as intended for the benefit of the beneficiary. In spite of the recognition of the obligation to protect the beneficiaries and their interests, the success of the trust in achieving its purpose to benefit a third party depended heavily on the character and integrity of the trustee. To the present day, fiduciary duties are an important social and ethical issue. Heavy emphasis is placed on the responsibility of the trustee to the beneficiaries.

—Eleanor G. Henry

See also Common Law; Conflict of Interest; Due Care Theory; Fiduciary Duty; Fiduciary Norm; Nonprofit Organizations; Prudent Investor Rule; Trusts

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Trusts

The trust, or more accurately, industrial trust, is a legal structure that emerged in the 1880s and 1890s in the United States as a mechanism for consolidating industries. A trust is a legal arrangement where property owners transfer control of their property to a separate entity—the "trust"—that manages the collected properties for the benefit of another party, which can be the original owners or someone else. Legal title to property is held by that one person or entity, the trustee, for the benefit of another, the beneficiary or beneficiaries. The trust structure was employed by industrial companies in the United States to establish economic monopolies over goods and services: All (or substantively all) participants in an industry would exchange their property for dividend-paying ownership shares in the trust, which would then be able to act unilaterally when setting prices, regulating output, and maintaining collective unity among the trust's member entities. Trusts attempt to circumvent conditions of free competition by uniting industry players into a single entity for the purpose of controlling the economic activities within the industry.

After the U.S. Civil War (which ended in 1865), the second half of the 19th century witnessed a substantial expansion of the railroads and the subsequent emergence of national networks for the transportation and distribution of goods. These changes transformed the U.S. economy from a collection of agrarian-centered, localized markets to a national marketplace dominated by large-scale industrial production. Meanwhile, the growing pace of innovation in numerous industries led to increasingly complex, automated processes that created higher capital and fixed costs for business firms. With the greater economies of scale occasioned by large-scale production, businesses focused their efforts on increasing profits by controlling the entire productive process from raw materials to finished goods. The increasing volatility of financial markets during this period, as demonstrated by the panic of 1873 and subsequent national economic depression, further stimulated business efforts to consolidate industries, lessen the economic risks of what was termed "ruinous competition," and provide increased economic stability in the new environment.

These economic forces spurred industries to initiate attempts at coordinating activities among competing firms. However, the initial efforts at forming and maintaining economic monopolies or oligopolies foundered on several legal and practical issues. First, pooling agreements and cartel arrangements to fix prices and divide markets not only violated common-law restrictions on restraint of trade but also proved unenforceable in court. In addition, corporate laws—which under the principle of states' rights resided within the power of the states rather than the federal government—often prevented corporate entities from owning shares in other corporations and even from doing business outside their home states. Finally, competitive pressures among involved firms often tended to produce incentives for participating enterprises to violate coordinating agreements, regardless of their economic efficiency or statutory legality.

Businesses searched for new legal structures that could organize economic activities in ways deemed favorable to their growth and profitability. The trust (industrial trust) was the culmination of their efforts to develop a legally acceptable and economically beneficial framework. Standard Oil Company, founded by John D. Rockefeller, pioneered the industrial trust in 1882. In adapting the legal concept of the trust to an industrial setting, Standard Oil persuaded the stockholders of 30 companies in the economically critical oil industry to turn control of their corporate stock over to nine trustees, who then could exercise all voting rights for this stock in a coordinated fashion. In return, these previous stockholders received shares in the newly created entity—the trust—which entitled them to receive financial returns based on the overall performance of the new combined entity. This legal framework enabled Standard Oil to centralize economic and managerial control over all the participating companies without developing illegal agreements or cartel arrangements. Furthermore, the trust structure allowed the combined entity to coordinate activities across state boundaries, thereby expanding its geographical reach, while eliminating the incentive to cheat by ensuring the distribution of profits based on the overall performance of all firms in the industry.

A wide range of industries, among them sugar, linseed oil, cottonseed oil, cordage, cattle, and whiskey, quickly followed Standard Oil's lead and adopted the trust form. Industries creating trusts possessed several elements in common: All were process-based industries with newly developed technologies for handling large batches of goods; all encountered variable market demand for their products, while facing onerous storage costs for unsold goods; all had experienced serious recent imbalances between supply and demand leading to cutthroat competition; and all had tried in the past to control these situations through the use of collusive agreements and pools.

Trusts could be either "horizontal" or "vertical" in nature. A horizontal trust, such as the Sugar Trust, united industry participants who performed similar economic tasks—such as producing specific goods—into a single source for such products. This combination eliminated competition among the different firms in the marketplace as under the trust structure they functioned as a single firm in the performance of their activities. A vertical trust, such as the Standard Oil Trust, combined under one controlling entity the various functions required for the production of goods or services in an economy—for example, from the provision of raw materials through manufacturing to distribution and sales—to eliminate competition and possible conflict along any phase of the production process. In addition to these monopolization motives, trusts also facilitated the rationalization of firm activities: the standardization and regularization of business processes, and the elimination of duplicate activities.

The business concept of the trust bore similarities to both cartels and monopolies. Trusts tended to be national in their scope, whereas cartels often function internationally. Furthermore, prior to the passage of antitrust legislation, trusts were legally created entities; monopolies, on the other hand, can develop through several means, such as active interventions in the market (where one business entity gains control over supplies of a good or service) or statutory action (where government grants a business entity a regulated position of dominance). After the passage of the Sherman Antitrust Act in 1890, the industrial trust was superseded by mergers as the legal mechanism for creating combinations of industrial entities.

—William E. Martello and Jeffrey Gale

See also Antitrust Laws; Capitalism; Cartels; *Chaebol*; Collusion; Efficient Markets, Theory of; Free Market; Industrial Revolution; *Keiretsu*; Monopolies, Duopolies, and Oligopolies; Price-Fixing; Regulation and Regulatory Agencies; *Zaibatsu*

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Truth Telling

Truth telling refers to the communication of complete and accurate information to another individual or group of individuals. Telling the truth is generally considered to be a positive act, often associated with character traits of honesty and integrity. Most human interactions involve the communication of information in some fashion, and if asked, we would state that we would like others to be "honest" and "tell the truth." When engaging in interactions with others, human beings rely on truth telling as a fundamental element in determining the outcome of the interaction, the relationship, and the larger fabric of society. These determinations are largely based on the value and protection of trust as a social good. It would be hard to maintain relationships as the foundation of society without trust. Thus, the maintenance of trust through telling the truth has individual, organizational, and societal implications.

Honesty

Telling the truth is widely associated with the concepts of both honesty and integrity. As noted above, honesty and integrity are considered desirable or virtuous characteristics. In fact, many moral philosophers have suggested that honesty and integrity are crucial to achieving the cardinal virtues. A number of scholars in the field of business ethics have also described telling the truth as the opposite of lying or as a dimension of dishonesty. In her book on lying, Sissela Bok suggests that telling falsehoods destroys social trust and creates unfairness in relations with others. She argues that Aristotle's initial perspective on telling the truth should be adopted as a means to a more stable and fulfilling society. Aristotle suggested that the truth is noble and full of praise, while falsehood is, in itself, mean and culpable. Bok points out that telling a lie requires a reason, while telling the truth does not. She and other scholars have argued that honesty is required for trust since a society based on lies or dishonesty will collapse.

Empirical research done on honesty has also examined truth telling. For example, a study conducted in the late 1990s showed that the construct of honesty comprises three different dimensions. The researchers found that honest behavior consists of respect for ownership of property (a dimension they called possession); giving complete information, not keeping secrets or omitting information (a dimension they called omission); and giving truthful or accurate information without misrepresentation (a dimension they called commission). Truth telling, then, typically embodies giving both accurate (commission) and complete (omission) information. Lying is considered to be the opposite of telling the truth and, thus, is considered dishonest behavior because it conveys either inaccurate or incomplete information to another person. Note that this would include behaviors such as bluffing, communicating outright falsehoods, and even communicating a false impression through dissembling or impression management.

Integrity

Telling the truth is also widely linked to the concept of integrity. Integrity has been interpreted to mean wholeness or strength of character and is often associated with fairness and trust, like honesty. Truth telling, or being honest, as a behavior is a foundation for establishing the characteristic of integrity. Integrity is considered to be a cornerstone for creating and maintaining relationships with others because it inspires trust, the foundation of such interactions. For example, in their work on integrity, Kathlyn and C. Gay Hendricks suggest that authentic speaking and resonant listening form one of four pillars of integrity in human organizational interactions. What they call "authentic speaking" is, in essence, truth telling. They argue for telling the truth as a means of increasing the degree of integrity in business organizations and destroying the myths that support lying to coworkers. Others have argued that honesty, courage, and respect are three components of integrity and that to create rich and meaningful communities in work organizations, we need to learn how to be more honest, courageous, and respectful of other human beings.

Many scholars have suggested that honesty is a foundation for creating a community within organizations where long-term relationships are based on trust and engagement of the whole person at work. Thus, truth telling begins with individual behavior but has organizational and societal implications as well. When we talk about lying or telling the truth, we are almost always concerned with the behavior of an individual. However, we also talk about bluffing, impression management, deception, and fraud (as forms of lying) when we examine the implications of these behaviors for business, social organizations, government, and society in general. It is helpful to look at the implications of truth telling, or the lack thereof, for individuals, organizations, and society as a whole.

Individual Implications

There are both psychological and physiological implications for individuals who don't tell the truth. Several practicing psychologists have noted a resurgence of ethical therapy in clinical psychology. Ethical therapy is used in treating mental illness. It is based on the perspective that such diseases can be treated by removal of unethical values or behaviors. (Note that dishonesty would be considered an unethical or undesirable value in this case.) Of course, it has long been known that lying is associated with increased stress, an increased heart rate, and perspiration. These physiological changes are what lie detector tests are based on. Many argue that such stress is unhealthy. For example, James Pennebaker has conducted studies that suggest a clear connection between truth telling (and openness) and increased well-being. His work shows that open and honest expression of feelings in communication strengthens an individual's immune system and overall health. This physiological improvement, in conjunction with the psychological improvement, suggests that individuals can benefit from telling the truth. Furthermore, other scholars have pointed out that an ongoing problem with practicing deceit is that the deception must be maintained. This takes a significant psychological toll on individuals engaged in this process.

Benefits can also be obtained in relationships with others through telling the truth. Individuals engage in interactions with others as the basis of relationships. Such interactions, many have argued, cannot be maintained or allow for collective action without truth telling. These authors suggest that if everyone expected everyone else to lie, there could be no trust and therefore no relationships with others. This leads to some perspectives on the implications of truth telling for relationships and organizational or institutional interactions.

Organizational Implications

Organizations are formed to accomplish tasks with more efficiency and effectiveness compared with individuals acting alone. Much of the research on increased effectiveness and efficiency has centered on group or team interactions and performance. Several researchers have found that increased truth telling and trust among team members has led to improved team performance due to strong, cooperative relationships. The other side of strong, cohesive team membership is a tendency to exclude outsiders and potentially create circumstances for groupthink. However, most of the research suggests that organizations with strong relationships based on trust are more successful on a number of dimensions. Others have suggested that the creation and maintenance of a culture within an organization is a function of the relationships, behavior, and norms established by the members. Organizational cultures based on truth telling have been suggested to provide a more solid basis for creating a community of cooperative members engaged in collective action. Even Peter Senge's powerful work on organizational learning suggests that it isn't defensiveness that is harmful in organizations; it is the concealment of defensiveness that harms the success of the business.

In short, many scholars have noted that organizations are microcosms of society as communities formed by relationships among the internal members and external constituents. This perspective leads to substantial overlap between organizational implications and societal implications of not telling the truth. The maintenance of community relationships requires telling the truth for creating the trust necessary for improved performance and success. The success of an internal organizational community has been measured by effectiveness, efficiency, and even assessments of providing meaningful work, while the success of the organization in relationships with external constituents has most often been measured by accomplishment of organizational goals via exchanges with such constituencies. Many researchers have examined the impact of stakeholder relationships on the successful accomplishment of organizational goals and have suggested that truth telling, honesty, integrity, and respect are key components in creating and maintaining such critical relationships.

Societal Implications

While some suggest it would be impractical, and perhaps even uncompetitive, to have all information in business organizations shared, others have noted that transparency in the form of clear and accurate communications can lead to successful long-term relationships in the market. Early writing in business, such as that of Albert Carr, suggested that bluffing should be considered acceptable in business interactions. He argued that bluffing (as a form of deception) is appropriate because everyone knows and understands that it is occurring. This might include behaviors such as exaggerating in a résumé or in advertising material or creating a false impression during an interview. Later scholars such as Sissela Bok have taken issue with this perspective to suggest that interactions based on deception create relationships that are unstable and cannot be sustained. In fact, Donald McCloskey, in his article on bourgeois virtue, reminds us that moral sentiment must ground a market since trustworthiness is required for exchange. Collective action in society, like that in organizations, cannot be accomplished without trust, as a result of honesty and truth telling.

When we discuss the implications of deception in business arrangements such as marketing or advertising information, we are often concerned with how this will affect the level of trust and the long-term relationships between buyers and sellers in the marketplace. For example, almost anyone who has had an experience as a victim of deceptive or false advertising describes the outcome in terms of loss of trust as well as loss or discontinuation of the relationship. Experiences and outcomes such as these led to the creation of the Caux Round Table of business organizations, interested in promoting more ethical business practices around the world. The Round Table developed a set of principles to guide organizations in achieving ethical business activities. In fact, the third of the Caux Principles links truth telling (as sincerity and transparency) to trust as a critical cornerstone of the ethical behavior of business.

Conclusion

In conclusion, truth telling, as a dimension of honest behavior, is generally considered to be a critical component for successful accomplishment of individual health and well-being. It is also key to creating and maintaining relationships with others as the means to collective action and successful and continued societal exchanges and interactions. It remains such a key component due to the role it plays in creating trust as a cornerstone for human interactions at an individual, organizational, and societal level. Without the establishment of such trust, interactions of a variety of natures would not be possible and the nature of human behavior and interactions would be irrevocably changed.

—Dawn R. Elm

See also Authenticity; Ethical Decision Making; Honesty; Integrity; Trust

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Tyco International

During the 1990s, Tyco International, under the leadership of CEO Dennis ("Deal-a-Month-Dennis") Kozlowski, had become one of the most admired publicly owned conglomerates on Wall Street. The electronics and medical supplies company achieved $36 billion in annual revenue, consisted of more than 2,300 subsidiaries, and employed more than 270,000 people. Kozlowski was among the highest paid corporate executives in the United States, receiving more than $286 million in compensation from 1997 through 2001, including $137.5 million in 2000 alone.

But beginning in 1995, Kozlowski and Chief Financial Officer Mark Swartz started stealing what would amount to $170 million from Tyco in unauthorized loans and bonuses and defrauding investors of an additional $430 million through tainted stock sales. Kozlowski and Swartz filed materially false annual reports and proxy statements with the SEC, lied to auditors, and falsified accounting entries to conceal secret compensation arrangements. In 2005, both executives were convicted on 22 of 23 counts of grand larceny, conspiracy, securities fraud, and falsifying business records and sentenced to up to 25 years in prison.

Stealing From Tyco

Kozlowski, born into a working-class New Jersey family, joined a Tyco subsidiary as an auditor in 1975. He progressed to the top of the corporate ladder, becoming CEO and chairman of the board of the $3 billion company in 1992. Five years later, Tyco changed its charter to be incorporated in Bermuda to avoid paying U.S. taxes. Over the next 3 years, Kozlowski achieved 20% annual growth rates by acquiring 700 companies. Kozlowski, as chairman of the board, handpicked board members and dominated board activities.

As CEO and CFO, Kozlowski and Swartz had a strict fiduciary duty to act at all times honestly and in good faith with a view to the best interests of company shareholders. They breached their fiduciary duties and treated company resources as their private bank account by engaging in the following illegal activities.

Abuse of KELP Loans

In 1983, Tyco established a "Key Employee Loan Program" (KELP) to provide low-interest loans to Tyco executives and employees for the purpose of paying federal income taxes on vested shares of Tyco stock. From 1997 to 2002, Kozlowski improperly borrowed $242 million from the loan program to pay for the purchase of art, antiques, yachts, automobiles, jewelry, a New York City apartment, a Massachusetts mansion, business investments, and more than $1 million toward a $2 million private birthday party for his new wife on an exotic Italian island. During the same time period, Swartz improperly borrowed $72 million from the loan program to fund his personal investments, business ventures, real estate holdings, and trusts. Kozlowski and Swartz failed to disclose their improper use of KELP loans to the board of directors, the SEC, or shareholders.

Abuse of the Relocation Loan Program

In 1995, Tyco established an interest-free loan program for employees relocating from corporate headquarters in Exeter, New Hampshire, to new corporate offices in New York and, subsequently, Boca Raton, Florida. Beginning in 1996, Kozlowski improperly borrowed $28 million in relocation loans to purchase personal properties in New Hampshire, Massachusetts, and Connecticut, and a $7 million New York City apartment for his soon-to-be ex-wife. During the same period, Swartz improperly borrowed $9 million in relocation funds, purchasing a yacht and funding real estate investments. Kozlowski also gave these interest-free loans to other key employees, including $10 million to Tyco's chief legal counsel, who purchased a ski chalet in Utah.

Self-Engineered Forgiveness of Tyco Loans

Without board knowledge, Kozlowski forgave his repayment of $57.9 million in KELP and relocation loans and loans of $29.1 million to Swartz. Both executives avoided paying taxes on this economic windfall by not claiming the loan forgiveness as compensation. Kozlowski also forgave the more than 40 loans given to executives who relocated to Florida. The employees signed confidentiality statements that hid this benefit from shareholders.

Concealed Related Party Transactions With Tyco

Kozlowski sold to Tyco his New Hampshire estate for $4.5 million, three times its fair market value. Tyco also significantly overpaid Swartz for some of his real estate holdings.

Secret Bonus Plan

Following the acquisition of the security company ADT, Kozlowski paid himself a $700,000 cash bonus, 148,000 shares of Tyco stock, $700,000 cash, and $16 million in loan forgiveness, without board knowledge. Swartz received a $350,000 cash bonus, 74,000 shares of Tyco stock, and $8 million in loan forgiveness. Other executives received smaller bonuses. The board was not informed of any of these transactions.

Undisclosed Accelerated Stock Vesting

Kozlowski improperly accelerated the vesting of Tyco common stock, resulting in personal gains of $8 million. He did the same for Swartz, though for half the amount.

Concealed Perks From Shareholders

Kozlowski had Tyco purchase a New York City apartment for $17 million and pay an additional $14 million for renovations and new furnishings, including an infamous $6,000 shower curtain; then he lived in it rent-free. He also donated more than $40 million of Tyco funds in his own name to various charities and flew the corporate aircraft for personal use. Swartz enjoyed similar perks, also without board knowledge.

Fraudulent Stock Sales

Kozlowski and Swartz secretly sold hundreds of millions of dollars worth of Tyco stock to company subsidiaries.

Discovering the Scandal

In July 2001, Kozlowski authorized a $20 million finder's fee to board member Frank Walsh, a personal friend and chairman of the board's Compensation Committee, for helping to initiate the acquisition of the CIT Group. Kozlowski instructed Walsh to hide the finder's fee from the other board members. Six months later the board found out and demanded that the extravagant fee be rescinded. Walsh refused to give the money back and Kozlowski defended his actions. The board's Audit Committee then began an investigation of all transactions between Tyco and senior managers, including loans, charitable contributions, and use of apartments and other assets.

With the internal investigation under way, but unknown to the board, Kozlowski was subpoenaed by the New York County District Attorney's Office on May 3, 2002, for suspicion of sales tax nonpayment on art purchases. Kozlowski had evaded paying New York City's 8.25% sales tax by having empty boxes shipped to Tyco headquarters in New Hampshire for invoice signatures, while the $13.1 million paintings, which he inappropriately purchased with a low-interest company loan, were being delivered directly to his Fifth Avenue apartment. Kozlowski was arrested for tax evasion a month later and forced to resign. Only then did the board learn about Kozlowski's illegal use of company funds over the previous 6 years.

On September 18, 2005, Kozlowski and Swartz, after an initial mistrial due to jury problems, were found guilty, given prison sentences of up to 25 years, and ordered to pay restitution and fines. As with Enron, Tyco's stock price declined significantly as a result of the scandal. But unlike Enron, Tyco had a solid business plan, and an internal investigation concluded that the fraud did not affect the company's prior financial statements. Shareholders elected an entirely new board and made executive severance contracts subject to shareholder approval. A Tyco executive is no longer able to serve as board chairman.

—Denis Collins

See also Fraud; Manipulation, Financial; Sarbanes-Oxley Act of 2002

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Tylenol Tampering

One of the most significant examples of business ethics and corporate crisis management involved the actions of Johnson & Johnson (J&J) during the Tylenol tampering crisis. In the fall of 1982, a subsidiary of United States–based J&J, McNeil Consumer Products, learned that seven people in Chicago had died from taking Extra-Strength Tylenol capsules that had been laced with cyanide. The management was convinced that the tampering did not occur at its plants, meaning that it must have taken place once the product had reached Illinois. J&J faced a dilemma, how best to handle the crisis without damaging the reputation of the company, when the company had quickly established that it could not be held liable for the tampering.

Reports on the firm's decision-making process during the crisis indicate that the company placed the safety of its customers first, before considering profit implications. A nationwide voluntary recall took place, involving approximately 31 million bottles of Tylenol, representing more than $100 million in sales. Consumers were told not to use any type of Tylenol product until the cause of the tampering had been established. Production and advertising of Tylenol ceased. The company offered to exchange all Tylenol capsules that had been purchased for Tylenol tablets. Relations were quickly established with the Chicago police, the FBI, and the Food and Drug Administration (FDA). A toll-free crisis phone line was set up for concerned consumers. Senior executives, including CEO James Burke, were readily accessible to the media. As part of a longer-term response, the company reintroduced Tylenol capsules with new triple-seal tamper-resistant packaging. Despite the firm having its market share drop from 33% to 18%, it wasn't too long before the company was able to recover its position. Following a second tampering incident in 1986, J&J made the decision to offer Tylenol in a caplet form, as opposed to a capsule form. No one was ever convicted of the tampering incidents and subsequent deaths.

Probably the most significant aspect of how J&J handled the crisis was the apparent corporate culture that existed at the time. According to J&J executives, turning to the firm's credo enabled them firm to make the right early decisions that led to the comeback phase. The credo, initially written in 1943, stated that the firm had obligations to society beyond merely profit maximization or enhancing shareholder value.

As a direct consequence of the Tylenol murders, U.S. Congress approved in 1983 a new "Tylenol Bill" that made maliciously tampering with consumer products a federal offense. In 1989, the FDA set national requirements for all over-the-counter products to be tamper-resistant.

Unlike many other firms, which often fail to react quickly on discovering potential danger to their stakeholders, J&J is remembered as a company that possessed an ethical corporate culture enabling the firm to handle the Tylenol tampering crisis quickly, openly, and honestly. By doing so, J&J was able to protect and enhance its corporate reputation into the future.

—Mark S. Schwartz

See also Codes of Conduct, Ethical and Professional; Consumer Protection Legislation; Crisis Management; Enron Corporation; Scandals, Corporate; WorldCom

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Underground Economy

The underground economy encompasses any economic activity not reported to the government and, therefore, beyond the reach of tax collectors and regulators. The term may refer to either illegal activities or to ordinarily legal activities performed without the securing of required licenses and payment of taxes. Synonymous terms, especially when applied to these latter activities, are shadow economy and working off the books. Examples of legal activities in the underground economy include unreported income from self-employment, barter, do-it-yourself work, and neighbor help. Illegal activities include drug dealing, trade in stolen goods, smuggling, illegal gambling, fraud, and theft.

The size of the underground economy in the United States has been estimated to be $1 trillion in 2005. This represents about 9% of the total U.S. GDP. If taxes could be collected on these trillion dollars, the federal budget deficit would be wiped out. The underground economy is even larger than many other countries', accounting for up to 40% of economic activity in developing nations. Unreported economic activity tends to occur when excessive taxes, regulations, price controls, or state monopolies interfere with market exchanges. Failure to recognize or enforce private property rights and contractual agreements may also encourage underground economic activities.

Measurement of the underground economy is difficult because, by definition, its activities are not included in any government records. Its size may be extrapolated from sample surveys and tax audits or estimated from national accounting and labor force statistics. One of the most commonly used indicators is the demand for currency, especially bills of large denomination. Hundred-dollar bills, for example, are seldom used in legitimate business transactions. Increased demand for these bills indicates a rapid growth in the underground economy since 1970. Although the dollar has long been the currency of choice in the underground economy, the euro is gaining popularity.

Motivation of Participants

People work in the underground economy for a variety of reasons. Most people working off the books do so to supplement their mainstream jobs. The mainstream job provides benefits, such as health care and pensions, and the work off the books provides additional income. The mainstream job is needed also to provide a visible source of income if the worker should attract the attention of the authorities. This unreported moonlighting is especially prevalent in European countries, where holding a second job is often illegal. In the United States, working off the books is usually motivated by a desire to avoid income taxes. As income and social security taxes have increased because of the "bracket creep" effect of inflation, the incentive to avoid taxation has also increased.

Some workers in the underground economy have no mainstream jobs. Most of these are people who lack the skills, social networks, or documentation necessary to obtain jobs in the mainstream economy. The jobs held by these people, many of whom are undocumented immigrants, often pay less than minimum legal wage and fail to comply with government standards of health and safety. Some full-time underground economy workers with marketable technical skills choose this type of work because the jobs may pay more than mainstream jobs. A third category of workers prefers the underground economy jobs because of the personal freedom provided by temporary, irregular work.

Employers in the underground economy also have a variety of motives. Nonpayment of income, excise, and payroll taxes is a major motivation. Avoidance of labor laws and licensing requirements and fees is also a factor.

Ethical Issues

Whether the underground economy is seen as more harmful or helpful depends on one's values and political philosophy. Those who look to the state as the guarantor of fair wages and labor practices see the growth of the underground economy as a major threat to social welfare. The nonpayment of taxes from this sector reduces the money available for social programs, and the workers do not enjoy the legal protections afforded to mainstream workers.

Mainstream companies complain of unfair competition from underground enterprises that do not have to pay taxes or minimum wages. Where there is significant underground economic activity, as in construction, the wage standards of the entire industry may be lowered over a wide region.

Defenders of the underground economy tend to come from either a utilitarian or a libertarian perspective. The utilitarian argument is that the underground economy is the ultimate safety net for people who cannot find work in the mainstream economy. As undesirable as many of these jobs are, they are better than nothing, and they may provide entry-level work in many fields for recent immigrants and other disadvantaged workers. Advancing technology makes many workers redundant, and for these surplus workers the underground economy may be the only work available. The low-cost goods produced by the underground economy may also improve the welfare of those who cannot afford mainstream products. For moonlighting workers with mainstream jobs, the income from the underground economy may be what enables them to maintain their families while paying the taxes on their reported wages. For these reasons, some economists argue that the government should support the existence of a thriving underground economy as a complement to mainstream activity.

Libertarians may see the underground economy as the last bastion of free enterprise, where the buyer and the seller or the employer and the employee may meet and contract freely without outside interference or restriction. Libertarians argue that it is only in the underground economy that the true value of a product or service may be found. The underground economy may also be viewed as a natural correction to overly centralized and bureaucratic economic systems. When legal restrictions make it impossible for consumers to satisfy their desires through the mainstream economy, the underground economy offers a bypass, a direct connection between buyer and consumer. As such, it may be seen as both a safety valve and an alternative path for the mainstream economy.

—Allen Hall

See also Black Market; Social Costs

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Unemployment

When a resource is not being used in conjunction with other resources to produce either a tangible or intangible product, it is said to be idle or unemployed. Unemployment may be either voluntary or involuntary.

Unemployment is a state in which any type of productive resource or factor of production, for example, labor, land, capital, or entrepreneurial ability, may find itself, although the social problem of unemployment is considered more acute for labor than the other resources. Consequently, governments and private sources collect and report more information with greater frequency on the employment status of labor than the other resources, and governments often design and implement policies to reduce unemployment of labor.

Statistics are calculated and reported on capital employment, which is provided in terms of "capacity utilization" rates and land-use data are also kept.

Determining the state of employment or unemployment of machinery and land is problematic given their multiple uses and the need for repair, replacement, and regeneration. Government policies can also enhance and encourage the use of capital and land and make some use choices more or less favorable—for example, through land-use zoning laws.

Due to problems of measurement, an unemployment rate for entrepreneurs or others self-employed does not exist. Measuring and observing entrepreneurial ability and capacity independent of the individual involved are currently impossible.

Treating unemployment as a yes-no or binary variable may also obscure the fact that some resources at some time may be underemployed—that is, working, but either not in their preferred field or occupation or not working for the number of hours per week they would prefer, or both.

Defining and Measuring Unemployment of Labor in Practice

For purposes of the most commonly reported statistical definition, at any time, a productive resource like labor may fall into one of three categories. Labor may be employed, unemployed, or not be in the labor force. At this point, definitions become somewhat arbitrary and may differ by country and even within a country; however, the Organisation for Economic Co-operation and Development (OECD) reports standardized unemployment rates for its 27 member countries including 22 European countries, Australia, Canada, Japan, South Korea, and the United States.

To be considered unemployed for purposes of the monthly household survey conducted by the U.S. Bureau of Labor Statistics (BLS)—whose definition is broadly consistent with that used by the OECD—a respondent must have actively, albeit unsuccessfully, sought work within the past four calendar weeks. Respondents are considered employed if they have worked at least 1 hour for a wage or 15 hours or more in a family business within the past week. The data are self-reported, and the issues of part-time employment versus desired full-time employment and working in a second-choice occupation are unaddressed in the monthly reported unemployment rate. However, supplementary surveys are taken by the BLS to gauge these different measures.

Those who are neither employed nor unemployed by the BLS definitions are considered to be out of the labor force. Those in the first two categories, employed and unemployed, constitute the labor force. One might be out of the labor force for any number of reasons including age, incarceration, retirement, full-time school attendees, those choosing to work in the home at household production, and so on.

The household survey is supplemented by the payroll survey where the BLS surveys employers on the number of wage/salary–earning employees they have in their firms in the survey month. Typically, the household survey shows a larger number of people employed relative to the payroll survey, as the self-employed (and those working in small family businesses) self-report as employed in the household survey, while they are missed in the payroll survey of firms. This difference in the data and how the data are collected and reported often becomes a political issue. Typically, a challenger will focus on the smaller number of employed as reported in the payroll surveys, and incumbents will highlight the higher reported employment in the household survey.

Sources of Unemployment

There are three major sources of unemployment: job losers, job leavers, and new entrants/reentrants into the labor force. These sources of unemployment result from the choices and behaviors of employers, employees, and those who seek to become employed. Employers laying off or firing workers create job losers. Employees who leave employment in search of better jobs are job leavers. Those who enter the labor force in search of employment are unemployed until they secure a job.

The measurement concept is similar for the other productive resources. A capital good, for example, a robotic welder in an automobile assembly plant, may be laid off—thus be a job loser—with a concomitant loss of income for its owner. Owners of capital may move machinery in search of a better job; thus, that capital becomes a "job leaver." The owner of physical capital has to bear the consequences of capital unemployment in the same way that individual employees have to bear the cost of labor unemployment. The same analysis applies to land, with farmers having to make decisions on crop rotation and letting land lie fallow (Is it unemployed or out of the land "force"?) in some growing seasons.

In any given month, the flow between these three pools of employed, unemployed, and out of the labor force creates the "measured unemployment rate." By the BLS definition, the unemployment rate in percentage terms is the ratio of the number of unemployed divided by the labor force times 100.

$$\text{Unemployment rate} = (\text{\# unemployed}/\text{entire labor force}) \times 100$$

Thus, if there were 100 people in the labor force with 90 being employed and 10 unemployed, the resulting unemployment rate would be $(10/100) \times 100 = 10\%$ for that month. Critics have pointed out that this measure, in addition to treating all employment as full employment, also ignores the discouraged worker, those persons who have withdrawn from the labor force after futile search for employment. Thus, the measured unemployment rate may well understate the true unemployment rate. Using the example from above, if there were two people who had exited the labor force due to becoming discouraged, then the measured unemployment rate of 10% would understate the true unemployment rate of $(12/102) \times 100 = 11.76\%$. The BLS also does supplementary surveys that attempt to capture this effect.

To examine, albeit briefly, the impact of changing flows from category to category on the unemployment rate, return to the original example. If two employed individuals flow to unemployed status the measured unemployment rate rises from 10% to $(12/100) \times 100 = 12\%$. Of course, if that flow were reversed the measured unemployment rate would decline. If workers flow from employed to out of the labor force, then the unemployment rate rises and vice versa. Finally, if individuals flow from unemployed to out of the labor force, the measured unemployment rate declines and vice versa.

Thus, mere observation of the unemployment rate does not always give one a good indication of the state of the economy, and the measured unemployment rate must be used with care if interpreted in this way. If one takes the position that less unemployment is better than more, one would view a declining unemployment rate as always being good. However, as outlined above, a declining measured unemployment rate may be consistent with a falling level of employment (e.g., if it is also accompanied by an increase in the discouraged workers exiting the labor force). One must look at the underlying flows to gauge the economic condition of a country.

Causes of Unemployment

There are four main causes of unemployment: cyclical, frictional, seasonal, and structural unemployment. These are associated with different economic situations and different economic concepts.

Cyclical unemployment is that unemployment that arises due to changes in the level of macroeconomic activity—termed *the business cycle*—because economic activity tends to rise and fall, not change in one direction only. When macroeconomic activity slows, we are said to be entering a recession, and unemployment results. This type of unemployment is most often viewed as being involuntary in that employers, in times of a recession (meaning lower sales and profits), are forced to lay off employees. So the flow from employed to unemployed rises, and the unemployment rate also rises. However, the process is probably better understood as one of lower sales in firms leading to layoffs that go into making the business cycle, which is an epiphenomenon of these individual results.

When macroeconomic activity increases, we enter the expansionary phase of the business cycle and unemployment tends to drop as firms, selling more than anticipated, now hire more employees. This process of firms responding in recessions (expansions) to lower (raise) employment lowers (raises) sales of other firms and creates more layoffs (hiring). This process is sometimes referred to as the multiplier process.

These adjustments are also known as quantity-adjustment processes, where the volume of employment of resources adjusts to cyclical conditions, in contrast to a price-adjustment process, whereby employment may stay relatively stable if the prices of resources (in labor's case, the real wage) were immediately fully flexible downward and upward. Reasons for inflexible or sticky prices abound and may not be inconsistent with individual choice. Thus, changing employment and unemployment may represent an optimal response given the underlying constraints on the costs of price changing, information, and other economic considerations.

The issue of whether or not cycles have to occur or what causes (and what ameliorates) cycles is still a hotly debated topic in economics. The idea of underconsumption as a cause of cyclical downturn, thus leading to unemployment, is associated first with Thomas Robert Malthus; it was further stressed by Marx, and the thread was later picked up by John Maynard

Keynes. It is not clear that Malthus had a recurring cycle in mind, but both Marxian and Keynesian analysis is the analysis of cycles, with Marxian cycles becoming ever greater and more destructive. Keynesian cycles can be either explosive or convergent depending on values of the multiplier and the investment accelerator and admit a role for government stabilization of the economy.

Frictional unemployment is that unemployment associated with the "frictions" in an economy analogous to the frictions in the physical world (e.g., air resistance, friction when surfaces move across one another) that lead to deviations from the theoretically predicted result. For example, in the physical world, air resistance causes a feather to fall slower than a bowling ball, though in a perfect vacuum they fall at the same rate. In the same way, in an economy, if there were no economic frictions, the unemployment rate would be lower.

What are these economic "frictions"? Perhaps the most serious is trying to match the skills and number of employees across jobs and the requirements of employers. While in the frictionless state there may be the perfect employee and the perfect job for everyone, it takes time in the real world for these employees and employers to find each other, if in fact they ever do. This search process takes time, and over that time period frictional unemployment results. As employees leave jobs in search of better opportunities, and as employers lay off one employee in search of a better one, the coefficient of "labor friction" or imperfections in information causes the unemployment rate to be greater than zero. Frictional unemployment may always be a feature of the economic landscape, though policies that encourage the production and dissemination of labor market information certainly lower these frictions.

Structural unemployment deals with those causes of unemployment relating to the changing structure of the economy. As the business mix of an economy changes, so too does the mix of skills and abilities required from resource markets. The information "revolution" is rewarding those with skills in information generation, manipulation, dissemination, and interpretation. Those with skill sets that do not match these changing requirements are relatively disadvantaged, reflected in the falling numbers of jobs (this may be either relative to the size of the economy, or in absolute terms, or both) and/or falling real wages.

While changing real wages may address this structural unemployment problem over time, it has been noted, at least since David Ricardo made the argument (stimulated by his correspondence with Malthus), that technological change may lead to unemployment, and in the case of older, less flexible workers, this may cause earlier labor market separation through early retirements.

Seasonal unemployment is that unemployment associated with jobs that are highly dependent on weather or other seasonal considerations. Agriculture, mining, forestry, fishing, even construction are examples of industries that tend to have a strong seasonal component, or what Adam Smith referred to as constancy or inconstancy, and the real wage adjusts to reflect this pattern.

Voluntary Versus Involuntary Unemployment

From Smithian, classical economic theory through the early 1800s, unemployment was viewed as a matter of individual choice. From that perspective, it may not always be preferable to be fully employed constantly. For example, the wage might be too low for the effort required, or at times, other alternatives such as schooling (a form of investment) might be more attractive. As people make these decisions based on a life cycle or intertemporal trajectory, and conditioned by their alternatives, wages would adjust to provide the signals guiding labor and other resources to their highest valued uses. Therefore, the observance of unemployment is not necessarily viewed as suboptimal or inefficient.

Adam Smith wrote famously of the wage or expected wage as a compensating differential that gave a tendency for all jobs to be similar when adjusted for their different requirements of innate ability, risk tolerance, tolerance for drudgery, specialization, constancy or inconstancy, luck, and so forth. Smith did not consider unemployment a social problem in the sense that workers might be involuntarily unemployed. The observed pattern of employment or unemployment was caused by individuals making their choices given the conditions, real wages and requirements of labor, in the markets. If there were an imbalance, say, not enough bakers and too many brewers, real wages would adjust to cause workers to flow from brewing to baking. Thus, in this view, unemployment is always voluntary and markets could be relied on to create incentives to balance workers with jobs.

This view from classical economics has many adherents today in the form of new classical economics (NCE) that embodies the "rational expectations" view. Though, it should be noted that there are several variants of NCE with differing ideas of how fast markets adjust, most NCE models yield results that indicate the observed level of unemployment is optimal.

In NCE, the existence of measured unemployment is not denied, but its involuntary nature or disequilibrium cause is. That is, given the NCE assumption that markets are always in equilibrium given our state of knowledge allows for no involuntary unemployment. Then, what is it that we observe? Only unemployment that is too costly to avoid given the frictions and changing nature (structure, seasons, and cycle) of the economy. Cyclical unemployment is the result of errors, realized ex post but not ex ante, that are caused by "mistakes" made by labor and employers in forecasting price levels and inflation or deflation rates when setting wage bargains denominated in nominal terms that span more than one period.

If the price level falls over the period that nominal wages are fixed by contract, the real wage rises and unemployment results. Had labor known about the falling price level before it occurred it might have agreed to lower nominal wages to keep employment constant, but the price level fluctuates in ways that are not perfectly predictable. Thus, observed unemployment may result.

Only when the anticipated inflation rate is actualized will cyclical unemployment vanish. This level of unemployment, termed infelicitously the *nonaccelerating inflation rate of unemployment* (or NAIRU), would be consistent with that level derived from the combination of frictional, seasonal, and structural factors prevailing at any given time. These factors, however, are considered givens in the short run, therefore outside the control of individual decision makers.

It is in the writings of later classical writers, for example, Malthus and Ricardo, that the idea of involuntary unemployment is introduced. John Stuart Mill also developed these lines of reasoning. Yet even in the writings of Malthus, Ricardo, and Mill, the persistence of involuntary unemployment is questioned.

Of course, Karl Marx most famously argued against the classical notion of a stable, classical, equilibrium (or equilibrium process) that always led to (or at least pointed in the direction of) full employment of resources. Marx's critique relied on class differences and imbalances in power relations that disadvantaged labor relative to capital leading to labor's residual status in the production process resulting in capricious unemployment of labor for reasons beyond its control.

Keynes, picking up on the classical economists' reasoning more than Marx's, brought back the underconsumptionist ideas of Malthus and added informational gaps (Keynesian uncertainty) that resulted in coordination failures in markets. Keynes oriented his critique at those classicists, for example, A. C. Pigou, who argued in the late 1920s and early 1930s along Smithian lines that labor markets were best left to themselves to solve unemployment through changing real wages.

Keynes did not question that markets would clear, but he questioned the speed at which this would take place, answering the long-run results promised by the classical model with the famous retort that in the long run, we will all be dead. Involuntary unemployment, in Keynes's view, results from coordination failures (e.g., "sticky" prices and wages) that prevent markets from continuously clearing at full employment.

Keynes's analysis has been added to and extended, and Keynesian interpretations of labor markets abound. "New Keynesians," "neo-Keynesians," "post-Keynesians," and many more groups or schools based (sometimes only very loosely) on Keynes's ideas are extant. Macroeconomics, influenced by both classical and Keynesian ideas, remains a very vibrant area within the mainstream of economics.

Policy Responses to Unemployment

If one believes, as most Keynesian-influenced economists do, that unemployment can be involuntary, and that involuntary unemployment is a social problem or burden (i.e., inefficient or suboptimal), then any number of government policy responses are deemed appropriate depending on the sources and types of unemployment existing. For cyclical unemployment, Keynes called famously for governments to act to overcome market uncertainty and pessimism through aggregate demand management policies, altering government spending and taxation, to boost sales and profits and thus encourage firms to hire more labor. Aggregate demand management is aimed at smoothing or eliminating the business cycle.

Structural unemployment calls for policies that provide information on the changing labor market, providing incentives to labor to make the transition from one skill set to another (e.g., education, retraining, reskilling) and in general trying to make labor markets more efficient through time. Notably, some commentators have argued that maintaining a given industrial structure may be the best response to forces creating structural change, for example, preventing or slowing firms from closing down plants or from laying off workers.

These policies, however, may have unintended and negative consequences for employment in that firms will be less likely to form and less likely to hire in the first place in the face of higher, governmentally imposed, costs of responding to changing economic circumstances. Some have argued that these types of polices, which are more prevalent in Western European countries such as France and Germany, explain some of the differences in the unemployment rates in those European countries versus the U.S. economy.

Classically oriented economists, who believe that markets generate the optimal pattern of resource use both at a point in time and through time, are less likely to call on governments to do anything other than allow markets to work more "freely" through enhancing price and wage flexibility, encouraging voluntary exchanges, and protecting property rights. These goals would be consistent with lowering frictional unemployment. Classically oriented economists are especially scathing of government policies that are seen to introduce or reinforce market inflexibilities, for example, wage and price controls and/or minimum wage laws.

Policies aimed at ameliorating the consequences of unemployment, for example, unemployment insurance programs, may have inbuilt moral hazard problems that encourage behavior that creates some unemployment (e.g., through reducing the incentive to finding a job thus lengthening the average duration of unemployment), but provides assistance through periods when wage income falls to zero. Differences in the design of these programs across countries have been shown to explain some differences in countries' unemployment rates.

—David L. Hammes

See also Auction Market; Chicago School of Economics; Economic Efficiency; Economic Growth; Equilibrium; Human Capital; Marx, Karl; Minimum Wage; Smith, Adam; Unintended Consequences, Law of; Wage and Price Controls

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Unfair Competition

Unfair competition refers to a wide range of laws dealing with economic injury to a business due to the wrongful actions of a competitor. For example, a competitor using another business's trademark for the purpose of deceiving customers would violate unfair competition laws. These wrongful acts include common-law causes of action (e.g., disparagement), as well as state (e.g., the Uniform Deceptive Trade Practices Act) and federal (e.g., the Lanham [Trademark] Act) regulation. This entry provides a brief overview of some of the different types of unfair competition claims.

Some of the most common unfair competition claims involve intellectual property. Intellectual property refers to the creations that flow from a person's mind, such as an invention or a fictional novel. The law grants the creator rights over the use of certain types of intellectual property, such as trademarks, trade secrets, copyrights, and patents. For instance, the example given above of a competitor using another business's trademark involved the intellectual property claim of trademark infringement. Trademarks (including trade dress and service marks) are the unique words and symbols that a business uses to distinguish its products in the marketplace (e.g., its brand name or product packing design). A business establishes its right to a trademark simply through its use in commerce, but registering it with the Patent and Trademark Office grants additional protections. The law grants a business the exclusive use of a trademark to allow customers to easily determine the party responsible for a product and to allow businesses to build goodwill (i.e., customers recognize the level of quality behind the trademark over time). A trademark holder has an unfair competition claim when another party infringes on his or her trademark. That is, the other party creates confusion in the minds of consumers as to the source of a product by using a confusingly similar trademark. Even if there is no customer confusion, a trademark infringement claim may be based on "dilution." Dilution is the use of another's trademark in a way that lessens the ability of the trademark holder to identify and distinguish goods through the use of that trademark.

A second unfair competition claim involving intellectual property is the misappropriation of trade secrets. A trade secret is any compilation of information (e.g., a formula or manufacturing process) that provides a business with a competitive advantage by virtue of the fact that it is not generally known and is not readily ascertainable by others. Perhaps the most famous trade secret is the recipe for Coca-Cola. As long as a business takes reasonable steps to protect its trade secret, it is misappropriation (and thereby unlawful) for another to use that information if it was gained through improper means (e.g., industrial espionage or the breach of a confidentiality agreement). A typical example of trade secret misappropriation would involve an employee leaving his or her current employer to go to work for a competitor and taking a list of clients with him or her. The list of clients is a trade secret of the employer that the ex-employee has misappropriated.

Several unfair competition claims fall in the area of law known as torts, which includes any interference with the rights or interests of another. One tort claim is disparagement that involves a defendant knowingly (or recklessly) making a false statement about the quality of another's product or services. A truthful comparison of the parties' products or services does not give rise to an unfair competition claim. To establish this claim, the plaintiff must also show that he suffered actual harm from the false statements (e.g., lost costumers). Related to disparagement is false advertising. This involves an actor making false statements about his own product, as opposed to false statements about his competitor's products. False advertising is typically regulated by state law, such as under the Uniform Deceptive Trade Practices Act.

A second tort claim is intentional interference with economic (or contractual) relations. A plaintiff has an unfair competition claim when he or she can show that the defendant intentionally induced a third party to breach a contract with the plaintiff. A key aspect to this claim is "inducing" the breach, as opposed to simply providing an opportunity for the third party to breach the contract. Thus, in some jurisdictions, the plaintiff must also show that the defendant acted "improperly" or "maliciously." A typical example of this claim would be a defendant inducing a third party to breach a confidentiality agreement with the plaintiff. The most famous case involving intentional interference with economic relations resulted from a 1983 merger agreement between Pennzoil and the Getty Oil Company that Getty later breached to merge with Texaco, based on Texaco's inducement. A jury held Texaco liable for intentional interference with economic relations and awarded Pennzoil $10.5 billion in damages (the case was settled out of court for $3 billion).

Finally, certain antitrust violations also give rise to unfair competition claims, under either federal or state antitrust laws. Examples of unfair competition claims under antitrust laws include predatory pricing, tying agreements, and price discrimination. Predatory pricing involves a firm charging below-cost prices for its products for the purpose of driving its competitors out of business. Tying agreements involve a business using its strong market position in one product area to force customers to buy a separate product—customers cannot buy the desired product without also purchasing the additional product. For example, in the 1990s, Microsoft was accused of tying its Internet explorer Web browser to the company's operating system software. Because the company had a strong market position in operating software, the act of tying the products together allegedly created unfair competition in the market for Web browsers. Price discrimination involves a seller using different prices for the same product in different locations for the sole purpose of injuring local competition (e.g., the price differential is not based on a cost justification or meeting the competition's prices).

—David Hess

See also Antitrust Laws; Deceptive Advertising; Intellectual Property; Regulation and Regulatory Agencies; Torts

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Unintended Consequences, Law of

It is a truism that human actions have unintended consequences. The sociologist Robert K. Merton, who authored a classic statement of the phenomenon in 1936, noted that the subject has been treated by virtually every substantial contributor to the long history of social thought. The "law of unintended consequences" quickly passed into public discourse. The concept continues to exert a fascination for social theorists, perhaps because it defines the province and basis for social scientific inquiry. Even though it is noncontroversial, its implications are not obvious, and this entry tries to elucidate some of them.

Sources of Unintended Consequences

Merton's article categorizes some of the principal sources of unintended consequences. They include ignorance, error, "imperious immediacy of interest" whose urgency crowds out consideration of other consequences, and "basic values" that mandate particular actions irrespective of their consequences. Last—and most interesting—is the reflexive nature of predictions about social conduct. The prediction itself may affect behavior in such a way as to make the prediction self-defeating or self-fulfilling. (Here, Merton anticipates his own subsequent work on the self-fulfilling prophecy.) As Merton says, every prediction includes a tacit "other-things-equal" clause, but, in the case of a prediction about social conduct, other things won't be equal because the actor has introduced a new "other thing"—his prediction. This is not true of prediction in fields that do not pertain to human conduct; the prediction of the return of Halley's Comet does not in any way influence its orbit.

Unintended Consequences and the Domain of the Social Sciences

If unintended consequences have been enshrined as a "law" of social science, it is because they define the agenda or subject matter or inquiry at the heart of the social sciences. Karl Popper has argued that the characteristic problems of the social sciences arise only out of our wish to know the unintended consequences, and more especially the unwanted consequences, which may arise if we do certain things. Likewise, Friedrich Hayek has contended that the function of social science is to explain how conscious, purposeful human action can generate unintended consequences through social interaction.

In economics, the law of unintended consequences is ubiquitous. It is exemplified by concepts like Adam Smith's invisible hand and moral hazard (the fact that insuring against an undesired event may make it more likely). In sociology, it is illustrated by Robert Michels's "iron law of oligarchy," Max Weber's account of how Protestant thrift and industry were self-defeating because they resulted in the accumulation of wealth that, in turn, corroded those same virtues, and Karl Marx's account of how the bourgeoisie inevitably produces its own gravediggers.

Without unintended consequences, the social sciences as we know them would be inconceivable. In their place there would be psychology. If outcomes were always intended, then intentions (and the needs, hopes, and motives that underlie them) would be the only object of social scientific interest because they would entirely explain social phenomena. Popper calls this the error of "psychologism"—namely, the view that social laws must ultimately be reducible to psychological laws, since the events of social life, including its conventions, must be the outcome of motives springing from the minds of individual men and women.

Social Engineering

Merton notes that unintended consequences "stand in the way of successful social prediction and planning." The law of unintended consequences suggests that social planning is likely to be self-defeating because it is difficult to predict how citizens will react to the new incentives created by the plan. Halley's Comet may not deviate from its orbit, but taxpayers will devise ingenious ways to circumvent or take advantage of a new tax law or regulation.

Michael Oakeshott, Friedrich Hayek, and Karl Popper are among the theorists who have been suspicious of the idea that society can be redesigned from scratch by the application of general, abstract principles. Oakeshott attacked "the assimilation of politics to engineering." Hayek assailed what he called the "fatal conceit"—the view that "all social institutions are, or ought to be, the product of deliberate design." Popper, too, eschewed what he called "utopian engineering." In its place, he favored "piecemeal engineering"—that is, incremental or gradualist social reforms that permitted learning from and adjusting or correcting reforms on a trial-and-error basis.

Even limited government interventions are subject to unintended consequences (though their damage may be more confined). More than 60 years ago, Ludwig von Mises pointed out that government regulations have a tendency to breed more government regulations. That is because the first round of regulations has unintended consequences that necessitate a second round of regulations, and so on. Any student in introductory economics can cite numerous examples of this process at work.

Conspiracy Theories of History

The law of unintended consequences also teaches skepticism of conspiracy theories of history. If unintended consequences doom the grandiose plans of social planners, so too must they frustrate the plots of conspirators to seize power and exercise it clandestinely. Popper used the concept of unintended consequences to denounce what he called the "conspiracy theory of history"—the mistaken theory that whatever happens in society—especially happenings like war, unemployment, poverty, shortages, which people as a rule dislike—is the result of direct design by some powerful individuals and groups. Popper acknowledged that conspiracies happen—and occasionally meet with some success. What he rejected was the idea that *history* is a conspiracy manipulated by the Learned Elders of Zion, or the monopolists, or the capitalists, or the imperialists. Conspirators rarely consummate their conspiracy because they are no more exempt from unintended consequences than are social planners.

Spontaneous Order

Merton notes that undesired effects are not always *undesirable* consequences. One of the central insights of social theory, originating in the Scottish Enlightenment, is that unintended consequences do not necessarily lead to disorder but are in fact the principal source of social order. Adam Smith said that

> every individual is continually exerting himself to find out the most advantageous employment for whatever capital he can command. It is his own advantage, indeed, and not that of the society, which he has in view. But the study of his own advantage naturally, or rather necessarily, leads him to prefer that employment which is most advantageous to the society. (*Wealth of Nations,* Book IV, Chapter 3)

Adam Ferguson observed that human action produced a form of social order superior to that conceived by human design. This insight is echoed in Hayek's concept of "spontaneous order." Examples of spontaneous order include language, common law, and our customs and mores rules. Obviously, society would be unthinkable without these institutions, but they were the result of human action, not of human design.

The idea that order is spontaneous—that it is an unintended consequence of human action—is congenial to both conservatives and liberals. It vindicates conservatives' confidence in traditional social rules. These rules are epistemologically superior to "artificial" rules because they are less vulnerable to subversion by unintended consequences. That is because they transmit knowledge that has stood the test of time. Such rules are, so to speak, "hypotheses" that have withstood repeated attempts to disconfirm them. Groups that adopt the successful rules prosper from having done so without necessarily knowing why.

However, traditional rules won't be adaptive in all future states of society, so spontaneous order also depends on society's capacity to renew its rules. Liberty is essential to this process. It disperses power among citizens, as opposed to concentrating power in the hands of the state. As a result, the process of trial and error permits much greater experimentation, and the impact of mistakes is limited in scope. Successful experiments gradually diffuse, while unsuccessful ones are discarded.

Unintended Consequences and Business Regulation

Perhaps nowhere do unintended consequences have sharper teeth than in the regulation of economic activity. It is now commonplace that many New Deal Era regulatory agencies were "captured" by the industries they were supposed to regulate in the public interest. The Endangered Species Act has created perverse incentives for landlords to destroy species or habitat out of fear of a government taking of their property. If the government tries to protect the domestic steel industry by means of quotas or tariffs on steel imports, it raises the costs of making cars in the United States, and soon automobile executives are clamoring for protection.

In 1993, Congress limited the tax deductibility of pay for the five highest paid executives in each public corporation to $1 million unless it was performance based. In response, corporations switched to granting executives stock options. These changes helped to set the stage for the scandals of the following decade.

—Ian Maitland

See also Austrian School of Economics; Black Market; Campaign Finance Laws; Common Law; Ferguson, Adam; Hayek, Friedrich A.; Invisible Hand; Marx, Karl; Moral Hazard; Smith, Adam; Socialism; Spontaneous Order; Underground Economy; Weber, Max

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United Nations

The United Nations is a forum where countries may discuss common problems and strive for peaceful solutions. It was born after the experience of World War II. The headquarters are located in New York City. The organization is the pivotal international body in the world today to address concerns of the nations of the world: security, social justice, public health, and international business. It is difficult to ascertain who first conceived of the concept of an international body of independent states that used diplomacy first and submitted some national sovereignty for the purpose of world peace. Before the United Nations, various regional alliances and mutual defense pacts were created to assist international diplomacy. The modern United Nations offers the world's first fully operational attempt at international cooperation and offers the possibility of working for positive peace—not just the absence of violence (negative peace), but the promotion of economic development and social justice leading to a positive sense of peace.

The current United Nations charter was signed on June 26, 1945, and the United States Senate approved the treaty on July 28. The need for the United Nations became clear because of the two World Wars of the 20th century. After World War I, a League of Nations was established, but it lacked power to act because member nations refused to cede it real power. As a result, the League was powerless to meet the needs of the emerging threats during the late 1920s. Yielding sovereignty to international organizations still remains as the leading obstacle to success.

To improve on the flaws of the League of Nations, the modern United Nations began with three principal organizational units to promote its mission of securing negative peace (the absence of armed conflict) and the promotion of positive peace (economic development and justice). To secure negative peace, the Security Council was founded with the power to send United Nations troops to a region to quell unrest or to stop aggression. The Security Council was originally formed with 11 members (five permanent and six rotating). The first real test of this came during the Korean crisis in which the northern parts of the country attacked the south. The UN Security Council stepped in and sent troops to the region (thanks largely to the USSR's boycott of the vote). Over time, the Security Council has intervened many times since its inception.

The one major difficulty of the Security Council is that the five permanent members (the Republic of China, France, the USSR [now the Russian Federation], Great Britain, and the United States) all have vetoes. This makes controversial action difficult. For example, during the Cold War, it would have been very hard to authorize an action that either the United States or the Soviet Union opposed (unless one party absented itself from the voting). Since these two superpowers seemed to have contradictory stands on most issues, it created stumbling blocks for action. In the future, the success of the Security Council will lie in its ability to be able to act quickly to use force when necessary to promote the absence of armed conflict (negative peace).

The second major arm of the United Nations concerns economic development and social justice. There are 14 major subunits of the Economic and Social Council. The most important of these for development are the International Monetary Fund (IMF) (which works in concert with the World Bank) and the World Health Organization (WHO). The theory behind this section of the UN is that without the basics of life, namely, food, clothing, shelter, and protection from unwarranted bodily harm (including medical care), there cannot be a lasting positive peace. The IMF along with the World Bank lends money to poor countries so that they might build up the infrastructure of the nation and make it ready to be a member of the economic community. They support projects such as the construction of roads, schools, hospitals, and irrigation projects. The WHO works at eliminating infectious diseases that threaten economic development and the basic well-being of the citizens. While this is a most worthwhile goal, the history of these organizations has been mixed with some real successes and some instances of graft and corruption. The present mood is toward transparency so that nongovernmental organizations (NGOs) might act as watchdogs to lessen the amount of graft and corruption.

The third major arm of the United Nations is the International Court of Justice. This was formed in the wake of the Nazi atrocities that had prompted the Nuremberg Trials. The modern court meets in The Hague in the Netherlands and consists of 15 judges who serve 9-year terms (five being elected every 3 years). In principle, they are the judicial arm of the UN, with power to enforce sanctions against member nations for violations of international law (trade disputes and the like) and for crimes against humanity (such as genocide). In principle, the International Court of Justice might be able to adjudicate international problems that would punish those who violated the rules of war or who violated economic or health policies of the UN. At the writing of this entry, the International Court was trying various individuals for war crimes connected to the Serbia, Bosnia, and Kosovo theater of conflict.

Of course, the short side to the United Nations lies in the willingness of member nations to cede sovereignty to the UN. For powerful countries, such as the G7, the United States, Britain, France, Germany, Japan, Canada, and Italy, there is little self-interested incentive to do so. There is little to promote their concern with ceding power to others. They are content with the status quo. For the rest of the world, it is in their self-interest to belong to a multinational diplomatic forum that seeks to promote their economic, just, and peaceful future. Perhaps the real road to peace will lie with the commitment of nations to such cooperative ends. It will not be easy but such is the ultimate mission of the United Nations.

—Michael Boylan

See also International Monetary Fund (IMF); Nongovernmental Organizations (NGOs); World Bank; World Health Organization (WHO)

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United Nations Environment Programme (UNEP)

The United Nations Environment Programme (UNEP) was created in 1972 by the UN General Assembly. The UNEP functions as the designated authority of the United Nations system in environmental issues at the global and regional level. Its mandate is to coordinate the development of environmental policy consensus by keeping the global environment under review and bringing emerging issues to the attention of governments and the international community for action.

The UNEP states that its mission is to serve as an advocate, educator, catalyst, and facilitator in promoting wise use of Earth's natural assets for sustainable development. Its activities cover a wide range of topics, including the promotion of environmental science and information and environmental law, to an early warning and emergency response capacity to deal with environmental disasters and emergencies.

The UNEP is headquartered in Nairobi, Kenya, and has six regional offices throughout the world: Africa, Asia and the Pacific, Europe, Latin America and the Caribbean, North America, and West Asia. The work of the UNEP is organized through eight divisions: Division of Early Warning and Assessment; Division of Policy Development and Law; Division of Environmental Policy Implementation; Division of Technology, Industry, and Economics; Division of Regional Cooperation; Division of Environmental Conventions; Division of Communications and Public Information; and Division of Global Environment Facility Coordination.

Two of the UNEPs most well-known accomplishments were the special report from the Brundtland Commission, *Our Common Future,* and the 1992 conference it hosted in Rio de Janeiro: the 1992 UN Conference on Environment and Development (known as "Earth Summit"). The Brundtland report introduced the now widespread understanding of sustainable development: development that meets the need of the present without compromising the ability of future generations to meet their own needs. The Earth Summit's purpose was to reconcile worldwide economic development with protection of the environment. *Agenda 21*, a blueprint for sustainable development, was one of the most popular documents created in that conference.

Because environmental sustainability is one of the eight "Millennium Goals" (priorities for international development) declared by the United Nations in 2000, the UNEP continues as a highly visible program with the United Nations. A variety of publications, awards, research projects, and advisory committees help the UNEP to carry out its mission.

Each year, the UNEP publishes approximately 100 books. Through its Web site, the UNEP reaches over 2 million readers each year. One of the UNEPs major reporting activities is the Global Environmental Outlook that tracks environmental change and notes significant trends and emerging issues. Periodic world summits and annual reports on the environment help to create and build on public support.

A conspicuous impediment to the UNEPs effectiveness is the continued lack of support from the United States for the Kyoto Protocol. While other major signatories—like Canada and Russia—have ratified this effort to reduce harmful emissions, the United States still considers the treaty too harmful for its economic growth. Furthermore, UNEPs assertion that humans are responsible for climate change (and, therefore, can positively affect climate change by reducing global warming) continues to be challenged by some members of the scientific community, especially in the United States. Nonetheless, the Kyoto Protocol is advancing and is now entering the compliance stage, even without complete support.

As the United Nations began to change from being the peacekeeper between two superpowers, it began to address more social and economic goals and began to work more with "civil society"—nongovernmental agencies and citizens. So, too, the UNEP began to seek out partnerships with the private sector for funding and management of its strategic goals.

The UNEP works with business and industry to promote basic human rights, labor, and environmental values and has encouraged companies to use Global Reporting Initiative (GRI) indicators in annual reports. In 2004, the UNEP launched the Responsible Investment Initiative to encourage the global investment community to adopt principles of sustainability. The UNEP has also partnered with the International Olympic Committee to safeguard the environment during Olympic Games. Increasingly, the UNEP asserts that environmental degradation and resulting poverty must be recognized as important sources of global conflict, while a sustainable environment would help create a more secure future for humanity.

—LeeAnne G. Kryder

See also Carrying Capacity; Corporate Citizenship; Corporate Social Responsibility (CSR) and Corporate Social Performance (CSP); Developing World; Environmental Ethics; Global Business Environments; Global Reporting Initiative; Kyoto Protocol; Natural Capital; United Nations; United Nations Global Compact

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United Nations Global Compact

The United Nations Global Compact is an initiative to create general principles of voluntary responsible business behavior. In 1999, the UN secretary-general Kofi Annan called on corporations to help make economic globalization beneficial for all in a speech at the World Economic Forum in Davos, Switzerland. A year later he introduced the original nine Global Compact Principles, in the three categories of human rights, labor standards, and protection of the environment. The tenth principle, on corruption and bribery, was added in 2004.

The 10 principles are the following:

Human rights

1. Businesses should support and respect the protection of internationally proclaimed human rights.
2. They should ensure that they are not complicit in human rights abuses.

Labor

3. Businesses should uphold the freedom of association and the effective recognition of the right to collective bargaining,
4. They should ensure the elimination of all forms of forced and compulsory labor.
5. They should ensure the effective abolition of child labor.
6. They should effect the elimination of discrimination in respect to employment and occupation.

Environment

7. Businesses should support a precautionary approach to environmental challenges.
8. They should undertake initiatives to promote greater environmental responsibility.
9. They should encourage the development and diffusion of environmental-friendly technologies.

Anticorruption

10. Businesses should work against all forms of corruption, including extortion and bribery.

These principles are based on widely accepted international documents, including the Universal Declaration of Human Rights (1948), the Declaration on Fundamental Principles and Rights at Work (1998), the Rio Declaration on Environment and Development (1992), and the UN Convention against Corruption (2003). The small UN Global Compact Office partners with six UN agencies that provide expertise and resources in support of business involvement to achieve the 10 principles. The UN agencies are the Office of the High Commissioner for Human Rights, International Labour Organization, UN Environment Programme, UN Development Programme, UN Industrial Development Organization, and UN Office on Drugs and Crime.

Secretary-General Kofi Annan appealed to business executives to join the Compact because it was in their interest to strengthen public support for economic globalization. He argued that responsible business behavior would reduce fears that globalization would endanger vulnerable parties, especially the poor.

Approximately 50 organizations signed up to support the Global Compact when it was officially launched in July 2000. Corporate participation grew rapidly to more than 700 in 2002 and increased to 2,100 in 2004. By 2006, more than 2,700 corporations, based in more than 90 countries, were active participants of the Global Compact. Participation simply requires a letter declaring commitment from the organization's CEO and a report posted on the Global Compact Web site on how the company is meeting one or more of the principles. Early reports were typically single cases demonstrating responsible corporate performance. Annual updates are necessary to maintain active participation status. Information on participation by country, industry, company, and issue can be found in the UN Global Compact database at www.unglobalcompact.org.

About 25 NGOs representing labor, human rights, and environmental concerns are also affiliated with the Global Compact. Early critics of the Compact included NGOs that were concerned that corporations were not sincere in their commitment to the principles but rather would use the Compact for public relations purposes only. While endorsing the concept of specific common standards for business behavior around the globe, they cautioned Annan not to permit corporations to use the stature of the United Nations as a way to improve business reputations without improving their actions. Later, NGO critics accused Annan of focusing on increasing corporate participation rather than on increasing accountability. They recommended that monitoring be instituted to ensure that companies were reporting their cases accurately and continuing to conform to the principles.

In response to this criticism, Global Compact officials and member companies supported the addition of integrity measures that required companies to provide an annual communication on progress to maintain active status as a participant. Companies that missed two annual deadlines were moved to "inactive" status. In October 2006, more than 300 companies were declared inactive because progress reports had not been submitted.

The Global Compact has recently accelerated the creation of country networks of members to provide greater opportunities for sharing best practices in dealing with common and collective issues. By late 2006, Global Compact Local Networks were developing in 60 countries. The emphasis is on creating "learning communities" that use both information and peer pressure to expand voluntary policies and programs.

The Global Compact is also creating formal partnerships with other corporate social responsibility initiatives. One is with the GRI, which is a voluntary effort to design reporting guidelines for sustainability reporting. The two organizations are integrating the voluntary social responsibility implementation focus of the Global Compact with the GRIs reporting framework. The Compact is encouraging its business participants to use the GRI framework to meet its annual requirement for communication on progress.

A second partnership is with the International Organization for Standardization (ISO), which is formulating ISO 26000, a set of voluntary social responsibility guidelines to be released in early 2009. A memorandum of understanding has been signed between the two groups to ensure that ISO guidelines will be compatible with the 10 Global Compact principles.

Such collaboration among organizations working to enhance corporate social responsibility reduces fragmentation that occurs with multiple partial approaches to influencing business practices. Integration and harmonization are expected to help corporations and their stakeholders in formulating and implementing standards for global corporate social responsibility, accountability, and transparency.

—Jeanne M. Logsdon

See also Corporate Citizenship; Corporate Social Responsibility (CSR) and Corporate Social Performance (CSP); Corruption; Global Business Citizenship; Global Codes of Conduct; Globalization; Global Reporting Initiative; Human Rights; United Nations

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Universalizability, Principle of

The *principle of universalizability* is a form of a moral test that invites us to imagine a world in which any proposed action is also adopted by everyone else. Most notably, it is the foundational principle for deontological, or duty-based, ethics. For example, if we are tempted to lie, then we have to think what the world would be like if everyone lied, or in a similar vein, if we consider donating to charity, what would it be like if everyone made the same choice. The principle acts like a litmus test by indicating whether acts are morally acceptable or not. Universalizing some actions will lead to a self-contradiction, indicating that they are morally unacceptable. For example, if everyone lied, the notion of truth telling would cease to have meaning, and human community would become impossible. Likewise, universal theft would undermine our fundamental beliefs in property rights. Universalizing other acts, such as charitable giving, will not lead to a contradiction and thus will pass the benchmark of morally acceptability. Using the test, we can determine a set of general moral principles, sometimes referred to as maxims. Business could not take place without some overarching ideas of universal right and wrong, including a general acceptance of keeping our word and fair dealing, and the intuitive appeal of universalizability suggests that such ideas are derived from a shared notion among all humans about the general principles concerning the way that one should behave.

The principle is based on the idea that moral equality demands equal treatment. It has often been crudely captured in the directive "Do unto others as you would have them do unto you." It presumes that all moral actors are equal and that we cannot favor ourselves by appealing to the particular facts of a situation. Thus, we have to ask what anyone would do when faced with this moral quandary, rather than what *I* would do individually granted my specific situation. We cannot develop a principle by saying that anyone from my background with my desires and tastes would act similarly, since with sufficient qualification that would lead to a test where only someone with my exact qualities would act in a given way, leading to individualized results for everyone who asks the question. Instead, we have to look to what a more abstract moral agent would do absent the context of the issue. For example, we cannot ask whether a manager who grew up in a country where women are not active in the workforce may discriminate on the basis of gender, but more what a neutral moral agent should do when faced with that situation, based on our best projection of the result of universal adoption of his views. It would not matter, for instance, if we believed that the other party in a negotiation was bluffing or that there would be a significant payoff if we could persuade the other party of something that was not true; the principle demands that we have to go to the root issue of whether lying is ever morally acceptable.

The principle of universalizability is the foundation of a formalist moral theory, as opposed to a contextualist moral theory. Formalist ethics takes human reason as its starting point; whereas contextualism holds that the starting point for ethical or moral evaluation of an action or course of action is the context in which it takes place. Context includes, but is not limited to, the particularities of the agent, the circumstances surrounding the actions, and the consequences of actions. Essentially, the principle of universalizability requires that we imagine the world in which the maxim behind action governing all humans operates like a law of nature, for example, the law of gravity. The principle is powerful since it is not dependent on circumstances and so serves to defeat moral relativism, which relies on the particular context of a decision.

A moral theory using the principle of universalizability must accept a conception of human reason wherein reason can determine infallibly a moral course of action. This requires that moral principles be determined a priori, or prior to experience. The principle requires this conception of human reason because it ultimately requires all ethical agents to abstract from personal and particular experience to imagine the "moral world" in which their actions operate like natural laws. The contextualist ethics, on the contrary, would admit that moral principles be determined a posteriori, or arising from experience, or out of reflection on experience. As experience cannot be admitted into moral reasoning, we have to depend on reason alone to produce moral directives.

A maxim is typically defined as a freely chosen action determined by human reason using the universalizability test. The freedom of this will is understood in terms of the autonomy of the will. In this moral framework, autonomy is not understood as the human being's freedom from laws or moral principles, but rather, the human being is subject to moral laws, principles, or directives because they are a product of one's own reason.

The force of moral requirements or prohibitions resides in the all encompassing nature of morality that the principle assumes. In essence, we must imagine that our actions be added to the repertoire of the natural laws that govern human life. A simple example of such a law is the law of gravity that governs the movement of bodies in space. The law of gravity is universal in that all bodies are subject to it, but as a law of nature, it exists outside of natural bodies. The task of the principle of universalizability is to imagine all our acts taking place in a world in which all rational beings would always act according to that maxim whenever the possibility were open. The maxim then takes on the force of a natural law, so that good actions are not merely allowed, but required and conversely, bad acts are absolutely prohibited.

There are two criteria for determining the universalizability of an action: consistency and reciprocity. The criterion of consistency states that the nature of reason itself is to resist inconsistency. There are two ways of viewing the consistency requirement of the principle of universalizability. First, there must be internal consistency, or rational consistency. For instance, one cannot rationally will the maxim "Do *x*, but do not do *x*," or "Preserve life, destroy human beings." It is rationally inconsistent to will to do and not do the same thing at the same time, just as it is logically inconsistent to hold both *x* and not *x* at the same time. In addition to this rational or internal consistency that must be met, there is external consistency that looks to the practical outcome of universalizing. For instance, to will "Always receive gifts but never give them" is inconsistent when universalized because it is impossible for everyone to receive gifts if no one is giving them. In the same way, "Make promises but never keep them" is inconsistent because the very meaning of the term *promise* breaks down if no one is required to keep one.

The second criterion for universalizability is reciprocity. Whatever one wills as an action for oneself, one must also be willing to receive that same action from another. To will "Kill all human beings," one must at the same time be willing to be killed by another. To escape this, one might will "I may kill a human being, but no one can kill me." However, this defies the test of universalizability in that one is making an exception of oneself, analogous to willing that "The law of gravity does not apply to me."

Historically, the primary defender of the principle of universalizability has been Immanuel Kant. The principle forms the cornerstone of his moral theory, captured in the categorical imperative: "I ought never to act except in such a way that I could also will that my maxim become a universal law of nature." For Kant, once the criteria of consistency and reversibility are met, and the maxim can be universalized, it becomes one's *duty* to act in such a way as to fulfill that maxim. At this point, actions are not merely permitted, but are required, or conversely, forbidden. In accordance with the principle of universalizability, actions done *from duty,* that is, because it is required are moral actions and those that are done *in spite of duty* are immoral actions. Only those actions done from duty, in accordance with the principle of universalizability, have worth. If it is one's duty to "always tell the truth," because one would not will to live in a world where this was not the moral law, to do it only because one fears repercussions or shame does not satisfy the moral requirement to act solely out of duty. The result of the principle of universalizability on this level is the requirement of certain actions, "Always tell the truth," or the prohibition of certain actions, "Never lie."

There are two clear benefits in employing the principle of universalizability in moral deliberation. First, moral laws, directives, or principles take on a decidedly objective character. In the process of universalization, the moral agent strips away particularities of time and place, individual circumstances, and emotive or desirous motivations for action. Thus, the moral law that results are required (or forbidden) of *all* moral agents, whomever and wherever they may be. This grounds the claim that certain actions are objectively right or wrong, moral or immoral. The second benefit of using this principle is that the test of universalizability provides a motivating force for moral action. The result of this process *categorically*, or absolutely, requires that a moral agent act in a certain way. Thus, the moral law does not merely suggest specific actions or courses of action but requires that certain actions be done or not be done.

There are also disadvantages to using the principle of universalizability and, more broadly, the formalist ethics that may result. For instance, the principle of universalizability strips away the particularities of agents, leaving no room for human emotion or desire to play a role in moral deliberation. Insofar as emotion and desire are uniquely and essentially human, moral deliberation using the principle of universalizability restricts full expression of one's humanity in moral exercise. Also, in decontextualizing moral reasoning, the principle of universalizability may also remove morally relevant or salient features of situations and other human beings. We often face moral questions where those involved are partial, owe special duties, or have extenuating circumstances that may color our intuitions. For instance, a corporation may hold that safe working conditions ought to apply universally. On the other hand, a foreign subcontractor may want to use much lower standards, and this sets up a conflict with business maxims such as "Operate in such a way that results in maximum returns to investors." The Kantian approach does not in itself tell us which maxim should have priority or how we go about judging between them. Examples like this show there may be times where moral principles clash—such as the corporation's duty to maximize returns to investors and maintain safe working conditions. In this particular situation, the corporation may be forced to rely on the situational context to develop moral priorities.

Another limit of the principle of universalizability and formalist ethics, in general, is the scope of moral concern. The principle is generally limited to other rational agents just like us, and thus may preclude consideration of other objects of moral concern, such as animals, plants, or the environment at large. The claim that we should not be unnecessarily cruel to animals, for example, appears to have moral force, but is not obviously condemned by the universalizability test alone. Some modern formulations of the principle have sought to modify it by incorporating a hierarchy of duties to deal with potential conflicts (suggesting, perhaps that life matters more than property and property matters more than convenience).

—Melissa Mosko

See also Duty; Golden Rule, The; Kantian Ethics; Kant, Immanuel; Neo-Kantian Ethics; Rationality; Rationality and Ethics

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USA PATRIOT Act

The USA PATRIOT Act (Uniting and Strengthening America by Providing Appropriate Tools Required to Intercept and Obstruct Terrorism Act) of 2001 is an act of federal legislation in the United States. It was signed into law by President George W. Bush on October 26, 2001.

The PATRIOT Act governs the authority of the federal government to fight espionage and terrorism and is divided along two areas: domestic law enforcement and foreign intelligence surveillance. The broad nature of the act has also allowed federal agencies to prosecute money laundering and computer fraud, even in situations that did not directly involve terrorism. The act has profound effects on Internet service providers (ISPs), telecommunications providers, banks, financial services companies, and immigration.

The original version of the act included a sunset provision. Several of the section powers defined in the act were due to expire on December 31, 2005. This date was extended to March 2006 as lawmakers argued over which sections would be retained. Legislation passed by the U.S. Congress in July 2005 in HR 3199 repealed this expiration date for certain provisions. A renewal of the act was passed by Congress and signed by President George W. Bush on March 9, 2006. The renewal makes all but two provisions of this version of the act permanent. While several of the original sections were not included in the renewal, the act still retains its broad scope over law enforcement, financial transactions, and surveillance.

Origins

The USA PATRIOT Act had already been proposed in the Congress before the events of September 11, 2001 (9/11). In the following days, President Bush called on the U.S. Congress to provide the federal government with sweeping law enforcement powers to better identify and prosecute terrorists. The executive branch and the congressional leadership centered its legislative efforts on this bill.

The act is an extension of the Foreign Intelligence Surveillance Act (FISA) of 1978 and the Computer Fraud and Abuse Act (CFAA) of 1986. The primary means of extension was the inclusion of terrorism. Terrorism itself was defined in the act as an activity that meets all three of the following criteria: the intimidation or coercion of the government or civilian population, the violation of criminal laws, and the endangerment of human life.

Scope of the Act

The act is divided into 10 sections or titles. Each section addresses specific issues, remedies, and agencies. Section 106 of Title I defines the president's powers regarding international financial transactions within the U.S. jurisdiction. This was a response to the finding that the alleged 9/11 terrorists had received significant funding from outside the country. As a result of this redefinition, it has become more difficult for anyone to transfer funds across the country's borders. Banks and financial institutions must collect, retain, and report more detailed information about each transaction and its participants. These efforts have been criticized by privacy advocates and international groups as a fundamental, and possibly illegal, erosion of the privacy rights of non-U.S. citizens.

Section 104 describes another expansion of governmental authority. The attorney general may request military assistance when weapons of mass destruction (WMDs) are used within U.S. territory or against U.S. facilities. This section weakens the separation between civilian and military authority in law enforcement, as a means of improving communication and coordination between these two institutions. Similar tactics were employed during the Civil War, resulting in the Posse Comitatus Act of 1878. This measure attempted to ban the use of military forces in a civilian capacity. Section 104 appears to be one of several legislative exceptions to the 1878 act.

Discrimination

Title I of the act also addresses discrimination against ethnic and religious groups. After the 9/11 attacks, some lawmakers and citizens were concerned that law-abiding Arab Americans, Muslim citizens, and others might be targets in a "rush to judgment." Section 102 recognizes this issue and states that the civil rights and safety of all American citizens must be maintained.

Racial and religious discrimination are long-standing issues in the United States. During World War II, President Franklin Roosevelt signed the Executive Order 9066 that allowed the civilian government to relocate approximately 120,000 individuals of Japanese ancestry to internment camps. More than 60% of these internees were American citizens. Relatively few internees were of German or Italian descent. The stated purposes of internment were to protect these individuals and to curb sabotage, in a utilitarian effort to preserve safety by denying the rights of an ethnic minority. While the Supreme Court upheld the executive order in 1944, President Ronald Reagan signed legislation in 1988 that provided a formal apology for the government's actions and established a system of monetary reparations to survivors.

Section 102 of the act does not specifically address internment. There are more than 5 million Arab Americans living in the United States. Internment, or any effort to restrict the movements of specific groups, would be difficult and expensive, even if these efforts involved voluntary or electronic tracking schemes.

Immigration

Title IV of the act represents a reform of national immigration laws, with a specific focus on the Immigration and Nationality Act (INA) of 1952. Immigration and Customs Enforcement (ICE), an agency formed in the Homeland Security Act of 2002 from the combined Immigration and Naturalization Service (INS) and the U.S. Customs Service, was given additional flexibility to staff and monitor the country's border with Canada. Immigrants who were members of an international organization that endorsed terrorist acts could be denied entry into the United States. Family members and associates could also be denied entry. The secretary of state and attorney general were given broad powers to investigate and designate any immigrant as a potential threat.

The attorney general was required under Section 416 to establish a computerized system for monitoring foreign students registered in U.S. colleges and universities. Academic administrators at each school are required to enter and update information about foreign students with the Student and Exchange Visitor Information System (SEVIS). The federal government can level substantial penalties against universities if they fail to participate in SEVIS and the associate Student and Exchange Visitor Program (SEVP). The U.S. universities have seen a marked decline in international student enrollment, as the revised student visa policies and procedures, including mandatory visa interviews and processing fees, served as a disincentive for potential students to consider U.S. schools.

Search and Seizure

FISA provides for the Foreign Intelligence Surveillance Court, which operates without public record. FISA also permits the delayed notice of a warrant in specific situations, which are commonly referred to as "sneak and peek." Under this doctrine, a property owner does not have to be informed prior to search. Probable cause is not a requirement for a FISA investigation.

Section 203 of the act allows "foreign intelligence information" to be gathered during criminal investigations by domestic law enforcement and then shared with the intelligence community. Section 218 added a single word to the 1978 requirements for launching a FISA investigation. Government officials could now show that a "significant," rather than sole, purpose of a FISA investigation involved the collection of foreign intelligence information.

The act further allowed the director of the FBI to request a person's telephone records without any notification to that individual. The federal government has argued that the transactional data for Web surfing consist of a list of the URLs or Web site addresses that a person visits. However, server addresses can have meaning in and of themselves. Web server addresses are almost always based on domain names, which are often associated with certain products services, trademarks, or other information that another person may use to either correctly or incorrectly identify a Web site without visiting any of its pages.

Web addresses can also have data embedded within them, through the use of the HTTP GET method. This is a common practice on search engines such as Google and Yahoo. Web developers sometimes use the URL to embed information that has been entered into forms. Web sites that follow this practice include bibliographic databases and some e-commerce sites.

Section 211 of the 2006 version of the act overrides the privacy provisions of the Cable TV Privacy Act of 1984. Subscribers' viewing records are protected, but records of telecommunications activity, including cable modem usage, wireless network transmissions, and telephone calls, are subject to the PATRIOT Act's provisions.

Section 216 of the act allows law enforcement agencies to conduct "roving" surveillance. This provision is one of two sections of the 2006 version of the act that will expire in 2010.

Money Laundering

Section 311 of the act authorized the U.S. Department of the Treasury to require regular reports of international financial transactions conducted through domestic financial institutions. Banks were also required to train employees on specific procedures and responsibilities for these financial transactions. Thus, a significant burden was placed on financial professionals, who must now assume that any international transaction must be reported, and may be perceived, as possible evidence of money laundering by the federal government.

Section 215 of the act gives law enforcement the authority to request business records under FISA. This is the second temporary provision of the 2006 version of the act. It is scheduled to expire in 2010.

Computer Fraud

The act amended the CFAA so that it includes the aiding or harboring of terrorists and perpetrating or assisting attacks on the defense contractors or the government. However, the act also extends its authority to situations in which individuals are harmed or killed. Unauthorized access to or transmission of government computer systems or national security information is prohibited. The unauthorized transmission or possession of computer passwords also qualifies as offense.

Sections 206 and 217 of the act amended the CFAA so that it applies involving computer fraud in cases where at least $5,000 of damages or lost revenues can be claimed. The act has been used in cases such as abuse, Web site defacement, spamming, file sharing, piracy, and theft involving ISPs, music and film publishers, and other organizations. Most of these cases were within the bounds of the act, although only a few of the defendants in these cases were implicated in terrorist activities.

An 8-year statute of limitations exists, and Racketeer Influenced and Corrupt Organizations Act (RICO) procedures can be used to confiscate assets from the accused. This expansion of the federal government's powers allows investigators to monitor an individual's telecommunications without their knowledge or consent.

State and Local Governments

Since its original enactment in 2001, eight states and almost 400 local governments passed resolutions and measures that condemned the act. These measures have little real power, but they do suggest that the PATRIOT Act remains a controversial subject in the United States. Public opinion polls suggest that many voters are poorly informed about the act's purpose and scope.

Effects on the Internet

The act presents several ethical challenges for companies, employees, and government officials. The intent of the act was to provide the federal government with enhanced powers to identify and prosecute terrorists.

In practice, the act has become a valuable tool for the prosecution of Internet-based crime. Law enforcement agencies are better able to work with ISPs, telecommunications firms, and other companies to respond as criminals change and adapt their practices in "Internet time." Legislators and the courts may react after the fact, but the Internet's pervasive influence over society means that the criminals can create much greater damage now than they could in the past. Government has turned telecommunications into a surveillance tool as a means of protecting society in a utilitarian fashion, where the good of the many outweighs the erosion of personal privacy and liberty.

At the same time, some Internet users tend to believe that the Internet is an anonymous marketplace for the exchange of ideas. The act has made this assumption a dangerous one. Telecommunications providers tout the power of their services to rapidly connect users to each other and to information sources. However, U.S. telecommunications providers have, in most cases, been willing to cooperate with the act's broad mandate, sometimes to the detriment of individual privacy.

In the first decade of the 21st century, mobile telephone carriers have extended the Internet's reach to the mobile handset. It is commonly believed that, at some point in the next 10 years, more users will access the Internet through a mobile phone handset than through a personal computer.

In the United States, these carriers archive and store text messages, record data transmissions and telephone calls, and are required by the act to produce this information at the government's demand, and sometimes without the user's knowledge. It has become a trivial pursuit to analyze the pattern of one or more user's mobile phone usage to determine where they were, when they accessed services, and what they accessed. The mobile phone and the personal computer have become, by their very nature as telecommunications devices, instruments of finely detailed surveillance. In the United States, the act means that a vast majority of the population is subject to greater government scrutiny now than at any point in the history of the Republic.

—William A. Sodeman

See also Electronic Surveillance; Immigration Policy; Immigration Reform and Control Act of 1986; Internet and Computing Legislation; Privacy; Workplace Privacy

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U.S. Bureau of Economic Analysis

The Bureau of Economic Analysis (BEA) is an agency in the Economics and Statistics Administration of the U.S. Department of Commerce. Although established in its current form in January, 1972, the BEA actually traces its functional origin back to February 1820, when the Department of the Treasury was directed to provide annual statistics on U.S. foreign commerce. The contemporary mission of the BEA is to promote understanding of the U.S. economy through the provision of the most timely, relevant, and accurate economics account data in an objective and cost-effective manner. The BEA accomplishes its mission through the collection and research of source data, the development and implementation of estimation methodologies, and the dissemination of its reports to the public.

The BEA produces more than 15,000 economic data series each month. It is the source for the National Income and Product Accounts. These accounts feature several widely followed measures of economic activity: gross domestic product, input-output accounts, balance of payments, direct investment estimates, and state personal income. These and other economic statistics are used by businesses, governments, and individuals to understand the U.S. economy. The White House and Congress use the GDP and national account reports in the process of determining budget estimations and projections. The Federal Reserve Board uses information from these accounts when setting interest rates. Businesses, households, and individuals use these statistics to guide financial and investment decisions. International trade officials and businesses use BEA statistics to inform negotiations on trade agreements; to assess international markets for size, direction, and share; and to measure the economic impact of trade policy. State governments and development officials use BEA statistics to better understand state spending, state revenue projections, and business growth.

The BEA follows five core values: integrity, quality, excellence, responsiveness, and innovation. The BEA strives to be the premier trusted source for reliable and consistent information about the performance of the U.S. economy. The BEA also promotes staff excellence and values providing its constituents with the programs and services they need. The BEA is committed to using cutting-edge technology and generating better methodologies to meet the considerable challenge of timely, relevant, and accurate economic measures.

In its FY 2005 to FY 2009 Strategic Plan, the BEA identified three significant challenges. First, it is challenged to understand the structural changes in the U.S. economy and its international interactions. To meet this challenge, the BEA will have to adapt its measures to characterize the structural changes in the economy and to locate quality sources to fill gaps in the BEA accounts. Second, the growing demand for economic analysis requires that the BEA and other agencies (BLS, the Federal Reserve, and the Census Bureau) provide consistent and integrated statistical foundations for account reporting. To meet this integration challenge, the BEA will have to agree on guidelines and timetables with the other agencies to create consistency. Third, the BEA is challenged to build a human capital strategy. To meet this challenge, the BEA will have to focus on its workforce recruitment, selection, training, development, and retention.

Accurate, reliable, and timely measures of economic activity are important to a variety of constituencies and stakeholders in any modern economy. Although the market economy of the United States may be guided by Adam Smith's *Invisible Hand,* agencies such as the BEA provide valuable economic insight regarding whether, where, when, and how policy makers and businesses allocate resources. Policy makers at both the state and federal levels rely on economic measures determined by the BEA in determining tax, fiscal, and trade policies. Businesses rely on economic measures determined by the BEA to analyze and contrast productivity; research and development expenditures; and wages and salaries to their industry sector, their region, and the economy as a whole.

—Frank L. Winfrey

See also Council of Economic Advisers; Federal Reserve System; Gross Domestic Product (GDP); Gross National Product (GNP); Inflation

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U.S. Bureau of the Census

Article 1, Section 2 of the U.S. Constitution states that the population of the United States be counted every 10 years for the purposes of apportioning members of Congress and direct taxes to the states. From the first census in 1790 until the census of 1880, the federal judiciary, through the U.S. Marshals Service, was responsible for the census. In 1880, Congress established a separate census office in the Department of the Interior and in 1902 established the U.S. Census Bureau as a division of the Department of Commerce. The sole purpose of the Census Bureau is to collect data and compile statistical analyses about the people and other select entities of the United States. In addition to the decennial population census, the Census Bureau also performs a Census of Governments every 5 years (covering government organization, government finances, and public employment in every state), as well as more than 100 annual surveys in areas as diverse as unemployment and housing. It is the job of the Census Bureau to collect and store these data, analyze them, and make them publicly available in both raw and analyzed form. It is also the Census Bureau's responsibility to protect the confidentiality of all data collected. The data on individuals are never reported, and raw census data can only be examined by the public after 72 years have passed.

Since its inception, the targets and questions of the census have reflected the political and social characteristics of the day. The first census in 1790 collected the names of every household head, counted the number of people in the household, including 3/5 of a person for each slave in the household, and specifically excluded American Indians. Collecting and tabulating the data on 3.8 million Americans took 18 months. By 1880, the number questions regarding social conditions and demographics had increased, the "3/5 rule" for African Americans had been eliminated, and the census included American Indians and Chinese. This census, the last to be done by hand, counted 50 million Americans and took 8 years to tabulate. It was barely completed by the time the 1890 census was ready to be taken. (In preparation for the 1890 census, a competition to create a tabulating machine was won by Herman Hollerith, and the company he founded to produce the tabulating machines eventually became the beginnings of the IBM Corporation.) By 2000, the census counted 281 million Americans, most census forms were mailed by citizens to the Census Bureau, and the data were made available on the Internet by the middle of 2001.

Since 1790, the census has changed from a simple counting of households to a mechanism for collecting an extremely wide range of demographic and economic data about the United States and its citizens. In the same time, the uses of the data have changed significantly, expanding from its original purpose of assigning congressional representatives to include such things as social service resources allocation, public policy planning, and economic analyses. Finally, access to the data has changed since the inception of the census and the Census Bureau, from data being available to a small number of elected officials and government bureaucrats to today's Internet-based access to every citizen and organization in the country.

Because of these changes, and the evolving demographics and economic dynamics of the United States, the Census Bureau has become a critical component of public policy debate as well as a key actor in political processes. Politically, the decennial census data are used not only to reapportion to states seats in the U.S. House of Representatives but also is the basis for redrawing congressional districts within each state. Economically, many social programs and federal dollars are allocated to states based on Census Bureau data, such data including not only the decennial population data but also more frequent unemployment figures, family income estimates, regional demographics, and household composition analyses. From a social perspective, the equations are simple: More people in a state means greater representation; more people qualifying for services in a state means more federal dollars. For the public to feel that the political processes are working fairly, and for policy makers to feel confident in their decisions, the census bureau must provide data that are viewed by all as objective, accurate, and complete.

The Census Bureau does receive criticism for possibly undercounting some classes of citizens, especially transients, the homeless, and people living in remote areas. The 1990 census was claimed to have missed almost 5 million Americans, many of them children, and mostly the urban poor, ethnic minorities, and the poor in very remote rural areas. Such undercounting has a direct impact on federal funding for social programs and can impact government social service policy for the following decade. With the information so critical to program funding, the undercount has become a social justice issue as well as a quality control question for accurate counting and reporting.

For the 2000 census, the Census Bureau combined mail-in surveys for most households, field workers for those not responding to mailed surveys, and teams of census workers specifically targeted at transient and urban and rural poor people. This good-faith effort to count all Americans was then augmented with a statistical correction to adjust the census numbers to account for those likely missed by those methods. This too proved controversial, as the decennial census is a zero-sum game to some degree. As congressional representation is fixed, gains in one region may require a reduction in other regions. In addition, social programs targeted at one segment of society may require reallocating resources from other programs. Estimating and thus increasing the number of minorities and poor can cast suspicion on the political motivations of the Census Bureau, as well as the numbers themselves. Court cases have affirmed the methods but have split the application of census numbers by collections method. Congressional representation, reapportionment, and redistricting must be based on actual counts. The corrected numbers may then be used for all other governmental purposes.

—Tom Bugnitz

See also Entitlements; Population Growth; Poverty; Racial Discrimination; Women in the Workplace

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U.S. Department of Justice

The Department of Justice (DOJ) was created as an executive department by the U.S. Congress in 1870 (chap. 150, 16 Stat. 162). While the Judiciary Act of 1789 (chap. 20, sec. 35, 1 Stat. 73, 92–93) had originally created the Office of the Attorney General, the legal workload quickly became problematic, requiring the use of private attorneys to work on cases. The use of private attorneys led to heavy expenditures by the government due to ever-increasing amounts of litigation as the country grew. In an effort to control expenses, Congress created the DOJ with the attorney general as its head to handle the legal workload. The 1870 Act specified that the department was to handle the legal business of the United States and put control over federal law enforcement under the attorney general and the DOJ. The contemporary mission of the DOJ has five charges: (1) "to enforce the law and defend the interests of the United States," (2) "to ensure public safety against threats foreign and domestic," (3) "to provide federal leadership in preventing and controlling crime," (4) "to seek just punishment for those guilty of unlawful behavior," and (5) "to ensure fair and impartial administration of justice for all Americans."

Over the years, the DOJ has added deputy attorney generals and structured itself around 39 separate organizations consisting of some 60 specialized offices, agencies, bureaus, programs, and divisions, becoming effectively the world's largest legal office. Many, but not all, of these operational units are of particular interest to businesses and are briefly described.

The Antitrust Division

The Antitrust Division is charged to promote, protect, and preserve the competitive process in the American economy for the benefit of consumers and businesses. The Antitrust Division accomplishes its mission through guidance statements of policy to the business community and, when necessary, the criminal and civil enforcement of the U.S. antitrust laws.

The Asset Forfeiture Program

The Asset Forfeiture Program employs asset forfeiture powers to enhance public safety and security by removing the proceeds of crime and other assets from criminals and criminal organizations. The program manages and disposes of property seized while satisfying valid liens, mortgages, and other innocent owner claims.

The Attorney General

The attorney general is responsible for representing the United States in legal matters generally and providing the president and heads of executive branch departments with legal advice and opinions when requested to do so.

The Bureau of Alcohol, Tobacco, Firearms, and Explosives

The Bureau of Alcohol, Tobacco, Firearms, and Explosives (ATF) enforces federal firearms laws (including firearms commerce conducted by the approximately 106,000 federal licensees), ensures the lawful storage of explosive materials (among some 1,640+ licensees), and investigates arsons and explosions. The ATF also enforces federal criminal statutes that concern the diversion and trafficking of alcohol and tobacco taxes among multiple jurisdictions.

The Civil Division

The Civil Division is the largest legal division in the DOJ. It represents the people of the United States, federal agencies and their employees, members of Congress, and the federal judiciary in a broad range of claims. The Civil Division defends the United States in actions regarding the constitutionality, lawfulness, or propriety of programs and actions by the constituent entities of the federal government. It litigates in areas regarding consumer protection, immigration, international trade, patents, bankruptcies, foreign litigation, and general tort claims involving admiralty, aviation, toxic substances, and the commercial activities of the government.

The Civil Rights Division

The Civil Rights Division works toward ensuring that residents of the United States are not discriminated against on the basis of sex, national origin, language barrier, religion, or disabilities. The Civil Rights Division accomplishes its mission through a combination of certification, coordination, enforcement, mediation, and technical assistance activities. The criminal section of the civil rights division prosecutes violations of federal criminal civil rights laws, such as hate crimes, official misconduct, involuntary servitude, interference with access to reproductive health care, and interference with the exercise of religious beliefs.

The Criminal Division

The Criminal Division of the DOJ prosecutes violations of federal criminal law that involve a wide array of activities: terrorism, drug trafficking, intellectual property theft, commercial distribution of pornographic and obscene material, large-scale Internet fraud, alien smuggling, organized crime, violent crime, and corruption and fraud by corporations and public officials.

The Drug Enforcement Administration

The Drug Enforcement Administration enforces the controlled substances laws and regulations of the United States to prevent the growing, manufacture, distribution, dispensing, or trafficking of illegally produced controlled substances and illicit drugs.

The Environment and Natural Resources Division

The Environment and Natural Resources Division handles all cases concerning the enforcement of federal law related to public lands. The division is responsible for laws pertaining to the prevention and cleanup of pollution; the stewardship of public lands, wildlife, and the nation's natural resources; the acquisition of real property for the federal government through eminent domain; and Indian and Tribal rights, claims, land, and resources.

The Federal Bureau of Investigation

The Federal Bureau of Investigation investigates various forms of fraud, defined as deliberate deception for gain. The FBI has major fraud program initiatives targeted at white-collar crime, corporate fraud, health care fraud, mortgage fraud, identity theft, insurance fraud, telemarketing fraud, and money laundering. It also investigates cases involving antitrust, bank fraud, securities scams and investment fraud, moving company fraud, Spanish lottery fraud, celebrity memorabilia fraud, staged auto accident fraud, Internet fraud, and other areas. The broader mission of the FBI includes protecting the United States against terrorist and foreign threats, enforcing criminal laws, and providing leadership and support services to various governmental partners from the local to the international level.

The Tax Division

The Tax Division, created in 1934, is responsible for civil and criminal matters that pertain to federal tax compliance litigation to promote the fair and uniform enforcement of the tax laws. The Tax Division attorneys work closely with the Internal Revenue Service (IRS) to develop tax administration policies and handle civil and criminal litigation and appeals. The Tax Division has several significant areas of operation: corporate tax fraud, terrorist financing, abusive and fraudulent tax promotions, corporate tax shelters, and foreign bank accounts and offshore credit card transactions.

The U.S. Trustee Program

The U.S. Trustee Program provides oversight and supervision of the nation's bankruptcy system of laws and procedures (chaps. 7, 11, 12, and 13) to promote the just, timely, and economically efficient resolution of cases. The program enforces U.S. bankruptcy laws and monitors the conduct of private trustees and bankrupt parties. Interestingly, bankruptcy cases in the states of Alabama and North Carolina are not within the jurisdiction of the program but rather within the jurisdiction of the Bankruptcy Judges Division of the Administrative Office of the U.S. Courts.

Other DOJ Components

There are a number of other components of the DOJ that have not been covered in this brief overview. They include, but are not limited to, the following: the Office of the Solicitor General, the Federal Bureau of Prisons, the United States Marshals Service, the Executive Office for Immigration Review, the Office of Dispute Resolution, and the Office of Justice Programs.

Summary

The DOJ represents the interests of the United States in legal suits; enforces federal, criminal, and civil laws; encourages and enhances business competition; and investigates, apprehends, prosecutes, and confines criminals, drug traffickers, and terrorists. For the fiscal year 2005, the DOJ employed more than 112,550 persons with an estimated total budget of $23.7 billion.

—Frank L. Winfrey

See also Antitrust Laws; Child Labor; Civil Rights; Consumer Fraud; Disability Discrimination; Electronic Commerce; Eminent Domain; Employment Discrimination; Environmental Protection Agency (EPA); Environmental Protection Legislation and Regulation; Equal Employment Opportunity; Ethics in Government Act of 1978; Federal Trade Commission (FTC); Fraud; Identity Theft; Internal Revenue Service (IRS); Internet and Computing Legislation; Piracy of Intellectual Property; Racial Discrimination; Religious Discrimination; Terrorism

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U.S. Food and Drug Administration (FDA)

The Food and Drug Administration (FDA) is a scientific, regulatory, and public health agency of the U.S. government, responsible for ensuring the safety of foods (except meat and poultry), human and veterinary drugs, biological products, medical devices, cosmetics, and radiation-emitting electronic products. The FDA covers all food products including bottled water, with the exception of meat and poultry, which are regulated by the United States Department of Agriculture. The FDA is responsible for ensuring that the products under their jurisdiction are honestly, accurately, and informatively represented to the public. The FDA also helps speed up innovations that make medicines and foods more effective, safer, and more affordable and helps the public get the information they need regarding the use of medicines and foods. The FDA works with numerous federal, state, and local governments and agencies to carry out its duties, including the consumer product safety commission to enforce the Poison Prevention Packaging Act, the FBI to enforce the Federal Anti-Tampering Act, the Department of Transportation to enforce the Sanitary Food Transportation Act, and the U.S. Postal Service to enforce laws against mail fraud.

The FDA employs more than 9,000 people who work in locations around the country. The FDA staff who work in the Washington, D.C, area focus on product review and regulatory policy. The employees who work in the network of field offices are generally the first point of contact for the public and manufacturers. These employees focus on inspection and surveillance, laboratory work, and public and industry education.

FDA-regulated products play a large role in the lives of Americans, accounting for about 25 cents of every consumer dollar spent. The FDA monitors the manufacture, import, transport, storage, and sale of

$1 trillion worth of products annually, at a cost to taxpayers of about $3 per person. The agency has existed in its present form since 1931, after some reorganization and shifting of duties from other federal agencies.

Overview of the FDA's Product Responsibilities

The FDA is responsible for ensuring that ingredients used in foods are safe and that food is free from contaminants. The FDA approves new food additives and regulates and monitors food labeling to ensure accurate information to consumers. The FDA monitors cosmetic products to ensure they are safe and properly labeled but does not require safety testing of cosmetics.

The FDA requires manufacturers to undergo extensive testing and get preapproval for medicines and medical devices to ensure product safety for both human and animal drugs and devices. The FDA sets drug manufacturing standards, inspects manufacturing facilities, and regulates over-the-counter (OTC) and prescription drug labeling. Medical devices ranging from thermometers to heart pacemakers must receive premarket approval. The FDA sets manufacturing and performance standards and tracks reports of device malfunctioning and serious adverse reactions. The FDA is responsible for the safety of the nation's blood supply and for regulating biologics, which include vaccines, blood products, biotechnology products, and gene therapy.

The FDA sets radiation safety performance standards for microwave ovens, television receivers, diagnostic x-ray equipment, cabinet x-ray systems (such as baggage X-rays at airports), laser products, ultrasonic therapy equipment, mercury vapor lamps, and sunlamps. The FDA accredits and inspects mammography facilities.

If a problem arises, the FDA can take a variety of actions. Usually, they work with the manufacturer to correct the problem voluntarily. Failing that, legal remedies include asking the manufacturer to recall the product, having federal marshals seize products, and detaining imports. The FDA can ask the courts to issue injunctions or prosecute those who deliberately violate the law.

History

Prior to the passage of a food and drug safety law in the United States, unethical companies used fake ingredients and adulterated foods to save money. Patent medicine companies sold medicines containing opium, morphine, heroin, and cocaine without restriction. Drug labels did not list ingredients. On reading of filthy conditions in Chicago's meatpacking plants in Upton Sinclair's novel *The Jungle,* President Theodore Roosevelt in 1905 urged Congress to pass the first food and drug law. In 1938, a new Federal Food, Drug and Cosmetic Act was passed. This modern law has been amended numerous times since 1938 to account for improvements in food and drug safety.

Challenges and Issues for the FDA

The FDA has identified several important challenges and issues for the near future. These are keeping up with advancements in scientific breakthroughs, dealing with more sophisticated products, new public health threats such as terrorism, tougher strains of antibiotic-resistant bacteria, more dangerous foodborne illnesses, international commerce, and providing sufficient consumer information.

The FDA has also been the subject of controversy over the years with regard to various areas under its charge. Among these are issues pertaining to drug safety monitoring, the drug approval process, and broader issues pertaining to the responsibilities of the FDA. The former FDA commissioner Donald Kennedy has blamed Congress for not providing adequate resources to the agency, claiming that the organization is limited in its ability to do its job given the amount of resources allocated to it. The FDA regulates more than $1 trillion worth of products, almost 10% of the country's GDP.

The Cato Institute, a nonprofit, public policy research organization, criticizes the FDA on another matter. The organization calls for an end to the FDA's monopoly on drug approval and advocates for alternative certification organizations. An example of such an organization is the Underwriters Laboratory, which basically sells its reputation for products they certify. The Cato Institute says that because the cost of bringing a new drug to market with all the required testing is so expensive, companies develop only drugs that are likely to be blockbusters and can treat large numbers of patients. The organization believes that allowing alternative certification organizations would speed up the process of drug approval and thus improve the quality of health care.

Marcia Angell, the author of *The Truth About the Drug Companies: How They Deceive Us and What to*

Do About It, criticizes the FDA's safety monitoring. MedWatch was created by the FDA in 1993 to help track serious side effects of drugs and other medical products. She claims that only a small percentage of adverse events are reported to the FDA and that the safety monitoring is limited.

Recently, the FDA has come under intense scrutiny by legislators. David Graham, a medical scientist who conducts drug safety research for the FDA, testified at Senate hearings on concerns about the drug Vioxx and others that the FDA was not capable of protecting America. The issue is a broader societal one, in that drug therapy involves trade-offs. There are risks in taking a drug to treat a medical condition, and there are benefits from taking the drug to treat the condition. Some argue that it is the responsibility of pharmaceutical companies and the FDA to ensure that no harm comes to consumers from any pharmaceutical products. Others argue that the benefits of certain drugs, such as Vioxx, to consumers outweighs the risk and that providing adequate information on the benefits and risks enables a physician and patient to make the best decision for the individual patient. Given the importance of the duty that has been assigned to the FDA, it is likely to remain the subject of controversy and criticism.

—Patrice Luoma

See also Consumer Protection Legislation; Food and Drug Safety Legislation; Regulation and Regulatory Agencies

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Utilitarianism

Utilitarianism represents an old and distinguished tradition in moral philosophy, the influence of which extends to law, economics, public policy, and other realms and is evident in much of our everyday moral thinking. Two fundamental ideas underlie utilitarianism: first, that the results of our actions are the key to their moral evaluation and, second, that one should assess and compare those results in terms of the happiness or unhappiness they cause (or, more broadly, in terms of their impact on people's well-being). Both these ideas have been around for a long time; one can glimpse hints of them in philosophical and religious writings going back thousands of years. However, as an explicitly and self-consciously formulated ethical theory, utilitarianism is just over 200 years old.

By the 18th century, several philosophers were promulgating an essentially utilitarian approach to ethics. However, the English philosopher Jeremy Bentham (1748–1832) is generally considered the founder or at least the first systematic expounder of utilitarianism. In politics and ethics, Bentham and his followers saw themselves as fighting on behalf of reason against dogmatism, blind adherence to tradition, and conservative social and economic interests. They were social reformers who used the utilitarian standard as a yardstick for assessing and criticizing social and economic policies and the political and legal institutions of their day. Among Bentham's backers were his friends James Mill and Mill's son, John Stuart Mill (1806–1873), who went on to become the most important English philosopher of the 19th century. Ardently interested in economics and public affairs, Mill was an articulate defender of utilitarianism and used the doctrine to champion individual liberty and to urge the emancipation of women. Mill, in turn, was followed by Henry Sidgwick (1838–1900), the last of the great 19th-century utilitarians. Unlike Bentham and Mill, Sidgwick was a university professor with a strong interest in the history of ethics. His writings developed and refined utilitarianism as a moral philosophy, bringing it to its full intellectual maturity.

Today, the utilitarian tradition is as alive as ever. Although many contemporary philosophers believe that utilitarianism is profoundly flawed, over the years a number of able thinkers have expounded and defended the theory, honing and elaborating it in surprisingly subtle ways. Nevertheless, utilitarianism's guiding impulse is simple and transparent: Human well-being is what really matters and, accordingly, the promotion of well-being is what morality is, or ought to be, all about.

Basic Utilitarianism

In its most basic and familiar form, utilitarianism holds that an action is right if and only if it brings about at least as much net happiness as any other action the agent could have performed; otherwise, it is wrong. Philosophers generally call this act *utilitarianism,* but the basic utilitarian standard can be used to assess not only actions but also rules, laws, policies, and institutions as well as people's motivations and character traits.

When we are deciding how to act, utilitarianism instructs us to assess the consequences not just for ourselves, but for everyone, of each of the actions we could perform at any given time. In addition to their immediate results, we must bear in mind any long-term consequences and any indirect repercussions that these alternative actions may have. Although we mustn't ignore our own happiness, neither are we to give it more weight than the happiness of anyone else. Utilitarianism, then, tells us to sum the various good and bad consequences for everyone of each possible action and to choose the action that will produce the greatest net happiness. In this way, the theory requires us to strive always to promote as much good as possible.

Welfarism and Consequentialism

Utilitarianism has two distinct philosophical components. The first of these is *welfarism,* the value thesis that welfare or well-being is all that ultimately matters. It is the sole good, the only thing that is intrinsically valuable or valuable for its own sake. Anything else that we think of as good for people—say, friendship, or individual freedom—is good only because, and to the extent that, it contributes to their well-being. Nothing is good unless it is good for individual people, and the supreme utilitarian goal is that people's lives go as well as possible.

Bentham, Mill, and Sidgwick focused on happiness, which they equated with pleasure and the absence of pain. Because of this, their utilitarianism is called *hedonistic.* But these three writers were concerned with happiness only because they identified it with well-being, that is, with what is good for people. In their view, our lives go well just to the extent that they are pleasurable or happy. Happiness, however, is not the only way to spell out the idea of well-being, and not all contemporary utilitarians understand welfare as happiness (and still fewer equate either concept with pleasure). For example, economists, who tend to be utilitarian in their outlook, typically identify well-being with the satisfaction of one's desires or preferences. In keeping with utilitarian tradition, this entry uses *happiness* interchangeably with *well-being*. But it is the latter concept that is the focus of utilitarianism, whether one understands it as happiness or in some other way.

The second philosophical component of utilitarianism is its consequentialist or teleological (goal-oriented) approach to right and wrong. *Consequentialism* is the thesis that actions are right or wrong because, and only because, of the goodness or badness of their outcomes. It is not an action's intrinsic nature or whether it is an instance of a certain type of act (e.g., the telling of a lie) that determines its rightness or wrongness, but rather its specific consequences in a given situation. Utilitarianism differs from other possible consequentialist theories by being welfarist, universalistic (because it takes everyone's interests into account equally), aggregative (because it sums the happiness or unhappiness of everyone to determine the overall value of an action's consequences), and maximizing (because it requires us to produce as much well-being as possible).

Future Consequences

In trying to produce the best outcome, an agent can be unlucky. A conscientious utilitarian might carefully choose the course of action that anyone in those circumstances would have judged conducive to the best result, and yet the outcome might turn out to be terrible. Alternatively, a malicious person might plot harm to a neighbor only to have the plan backfire and produce optimal results. Utilitarians divide about what to say about these cases.

"Actual-outcome utilitarianism" affirms that the unlucky utilitarian acted wrongly and the malicious person acted rightly. We should not, however, blame the unlucky person for acting as a reasonable and well-informed utilitarian would have acted in the circumstances, and we should criticize the malicious agent for seeking to cause harm. In contrast, "expected-outcome utilitarianism" asserts that the correct standard is not the actual consequences of our actions, but rather their probable, foreseeable, or expected results. Hence, the unlucky utilitarian acted rightly and the malicious person wrongly. In practice, however, the difference between the two positions vanishes because, given that the future is uncertain, the most one can ever do is to act so as to produce the greatest expected well-being.

Critics of utilitarianism emphasize that we never know all the consequences of the things we do, still less the future results of every possible action we might have performed. Indeed, the causal ramifications of our actions extend indefinitely into the future. Talking in terms of probabilities does not eliminate this problem. We can rarely do more than guess at comparative likelihoods, and we are always liable to miss some possible outcomes and to overlook some alternative courses of action. Furthermore, comparing people's levels of well-being is tricky and imprecise at best. Finally, even if we were armed with all the relevant information, we would lack time to perform the necessary calculations before having to act.

Utilitarians concede these points and yet argue that they do not impugn the utilitarian goal of maximizing well-being. The correctness of that goal is not undermined by shortfalls in our knowledge of how best to attain it. Well-being is still what we should aim at, however difficult it may be to see the best way to bring it about. Utilitarians also point out that human beings are already well acquainted with the nature and typical causes of happiness and unhappiness. Based on thousands of years of collective experience, we are far from being in the dark about what promotes human well-being and what does not, and that knowledge will frequently suffice to justify our acting one way rather than another.

This response also addresses the complaint that we generally lack time, before acting, to perform the necessary utilitarian calculation. In ordinary circumstances, we can and should follow certain well-established rules or guidelines that can generally be relied on to produce good results. We can, for example, make it a practice to tell the truth and keep our promises, rather than try to calculate possible pleasures and pains in every routine case, because we know that, in general, telling the truth and keeping promises result in more happiness than lying and breaking promises. In this vein, many utilitarians have emphasized the practical necessity of following secondary moral principles. Relying on subordinate moral rules also alleviates the problem that even conscientious agents can suffer from bias or make mistakes in their calculations. In normal circumstances, one is less likely to err and more likely to promote happiness by sticking to certain settled guidelines than by trying to calculate afresh the consequences of various courses of action.

Does Utilitarianism Require Immoral Conduct?

For utilitarians, rightness and wrongness turn on the specific, comparative consequences of the various courses of action available to us. Without knowing something about the particular situation, we cannot judge ahead of time whether acting in a certain way will be right or wrong. We cannot say that actions of a certain type will always be right or always wrong. Utilitarians see this flexibility as a strong point of their normative standard, but their critics view it as a fatal flaw: The utilitarian goal of maximizing welfare, they argue, can sometimes necessitate the agent's acting immorally. The critics concede that it generally conduces to total well-being for people to tell the truth, keep their promises, and refrain from killing or injuring other people, from damaging their property, or from violating their rights. But there can be exceptions, and in unusual circumstances, promoting overall welfare might call for the agent to do something normally considered perfectly immoral—for example, supporting slavery, violating someone's rights, or framing an innocent person for a crime. Many philosophers repudiate utilitarianism because of this possibility.

Utilitarians typically respond by arguing that their theory does not mandate the conduct the critic says it does. Faced with hypothetical examples of detestable actions, policies, or institutions that supposedly maximize well-being, they challenge the imagined facts, arguing, for example, that slavery will not in fact promote overall well-being or that abridging someone's right to free speech to pacify the majority or torturing suspects to obtain confessions will have negative long-term repercussions. And even if it really would maximize well-being, say, to frame an innocent person to forestall a riot, one could never judge with sufficient confidence that this is how things would play out. In response, the critic is unlikely to permit the hypothesized facts to be challenged but, rather, to insist that in the imagined circumstances we really do know that an action or policy we normally consider morally wrong will maximize total welfare. At this point, utilitarians have no choice but to concede that the apparently immoral thing really is the right course of action. But they will deny that this fact provides a compelling reason for rejecting their theory. Ordinary morality is not sacrosanct. If its rules sometimes conflict with utilitarianism, then so much the worse for ordinary morality. We should revise it, not abandon utilitarianism.

Consistent with their own standard of right, however, utilitarians can often endorse the ordinary moral sentiments to which the critic appeals. Although in the far-fetched set of circumstances hypothesized by the critic, slavery or torture maximizes well-being, these are not the circumstances real people ever encounter.

In the world as it actually is, we do much better if people are dead set against doing those things we would normally consider atrocious—that is, if they instinctively reject slavery or refuse even to consider the possibility that framing an innocent person or torturing a suspect might be the right course of action. People who feel this way will do the nonutilitarian thing in the fanciful circumstances imagined by the critic. But they will act better in the world we actually live in, a world in which such dreadful actions will almost certainly diminish net happiness, than will someone who lacked these convictions. In line with this, utilitarianism can underwrite a strong commitment to respecting certain individual rights even if cases are possible in which people will fail to act in a welfare-maximizing way because of this commitment.

Deeper Into Utilitarianism

For utilitarians, whether an agent acted wrongly is distinct from the question whether the agent should be blamed or criticized for so acting (and, if so, how severely). Utilitarians apply their normative standard to questions of praise and blame just as they do to questions of right and wrong. In particular, they will ask whether it will best promote happiness to criticize someone for failing to maximize happiness. Suppose that a well-intentioned agent acted in a welfare-promoting way but that the person could have produced even more good by acting in some other way instead. Should utilitarians criticize this person? Depending on the circumstances, the answer may well be "No." Indeed, praising agents for actions that fail to fulfill the utilitarian standard can sometimes be right. This is because utilitarians applaud instances of act types they want to encourage, and they commend those motivations, dispositions, and character traits they want to reinforce.

Utilitarians take an instrumental approach to motives. Good motives are those that tend to produce right conduct whereas bad motives are those that tend to produce wrongful conduct. And they assess habits, dispositions, attitudes, behavioral patterns, and character traits in the same instrumental way: One determines which ones are good, and how good they are, by looking at the typical results of the actions they lead to. It doesn't follow from this, however, that utilitarians believe that a moral agent's only motivation or sole concern ought to be the impartial maximization of happiness. Indeed, utilitarian writers have long urged that more good may come from people acting from other, more particular motivations, commitments, and dispositions than from their acting only and always on a desire to promote the general good.

Utilitarianism thus implies that one should not always reason as a utilitarian or, at least, that one should not always reason in a fully and directly utilitarian way. Better results may come from our acting from principles, procedures, or motives other than the basic utilitarian one. This last statement may sound paradoxical, but the utilitarian standard itself determines in what circumstances we should employ that standard as our direct guide to acting. The proper criterion for assessing actions is one matter; in what ways we should deliberate, reason, or otherwise decide what to do (so as to meet that criterion as best we can) is another issue altogether.

Utilitarians will naturally want to guide their lives, make decisions, and base their actions on those principles, motives, and habits that produce the best results over the long run. Which principles, motives, and habits these are is a contingent matter, but utilitarians believe that we often do best to focus on the welfare of those relatively few people with whom our lives are intertwined and whose good we can directly affect, rather than on happiness in general. Nor should we forget that our own happiness is also part of the general good; indeed, it will usually be the part that we have the greatest power to affect, one way or another.

Rule Utilitarianism

Although utilitarianism rests on one fundamental principle, it also stresses the importance of following rules, guidelines, or secondary principles that can generally be relied on to produce good results. We should, for instance, make it an instinctive practice to tell the truth and keep our promises, except in very unusual circumstances, because doing so produces better results than does case-by-case calculation. As previously mentioned, relying on such secondary rules counteracts the fact that we can easily err in estimating the value and likelihood of particular results. In general and over the long haul, we are less likely to go wrong and more likely to promote good by cleaving to well-established, welfare-promoting rules—including those rules that identify certain individual rights—than by trying to maximize happiness in each and every action we perform. Moreover, when secondary rules are well known and generally followed, people know what others are going to do in routine and easily recognizable situations, and they can rely on this knowledge when acting. This improves social coordination and makes society more stable and secure.

These considerations have led some utilitarians to adopt a theory called *rule utilitarianism.* It maintains that the utilitarian standard should not be applied to individual actions at all but only to society's moral code as a whole. The rule utilitarian asks what moral code (i.e., what set of rules) a society should adopt so as to maximize well-being in the long run. The principles that make up that code then provide the basis for distinguishing right actions from wrong. An action is not necessarily wrong if it fails to maximize well-being; it is wrong only if it conflicts with the optimal moral code. What is the optimal code for a society to adopt? Rule utilitarians believe that it will not be a one-rule code, commanding us always to bring about as much happiness as we can. Rather, more happiness will come from people following a pluralistic moral code, one with a number of principles of different moral weight.

—*William H. Shaw*

See also Bentham, Jeremy; Consequentialist Ethical Systems; Cost-Benefit Analysis; Hedonism, Ethical; Interpersonal Comparison of Utility; Mill, John Stuart; Sidgwick, Henry; Utility; Utility, Principle of; Well-Being

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Utility

Utility is a term of art employed by philosophers and social scientists to denote what is of value to or what is good for human beings (or, sometimes, sentient beings, more generally). "Utility" is synonymous with "welfare" and "well-being," so to speak of the utility of decisions, actions, or policies is to refer to their impact on the welfare or well-being of people. The specific meaning of the term differs widely, since the notion of human welfare is contentious. Economists, for the most part, share a common understanding of utility, meaning by the term the satisfaction of desires and preferences through the use or consumption of commodities (goods and services). So the terms *utility, welfare, and satisfaction* tend to be used interchangeably in economics. Economists often assume that utility can be represented in monetary terms. While economists usually identify utility with material well-being, philosophers typically have in mind a broader notion of well-being—where material well-being is one part of this broader notion. In the first instance, "utility" refers to individual welfare, but it is also often used to refer to social welfare.

Proponents of the market system see it as a powerful mechanism for promoting utility. In a competitive market system, consumers aim to maximize their own personal utility by purchasing the commodities they want at the lowest prices available. Firms, aiming to maximize their own utility, will produce and sell the commodities that consumers want at the lowest possible prices for fear that consumers will make their purchases from competitors. To produce and sell commodities at the lowest prices possible, firms must employ the most efficient processes and make optimal use of resources. The market system, then, guarantees that firms are producing those goods and services that consumers want in the most efficient way possible and selling them for the lowest prices possible. Hence, the market system maximizes the economic utility of society in general. This line of analysis, developed in *The Wealth of Nations* of 1776 by the classical economist Adam Smith (1723–1790), calls attention to the link between the pursuit of personal utility and the pursuit of social utility. To the extent that individual consumers and firms aim first and foremost to maximize their own personal utility, their behavior can be characterized as egoistic. But competition and market forces ensure that this egoistic behavior inevitably maximizes social utility. The participants in a market economy are led by an "invisible hand," to use Smith's phrase, to promote a goal (the maximization of social utility) that they do not intend to pursue in the first instance. Although this explanation and defense of the market's workings have been sharply challenged, they continue to exert a tremendous influence over many theorists' and practitioners' fundamental understanding of the market system.

A wide variety of contemporary business practices that aim to maximize utility for the firm have the added (intended or unintended) effect of promoting utility for society in general. Environmentally friendly practices, such as reducing packaging material and energy consumption and cutting the firm's production costs, make it more competitive. Society, in general, benefits not only from lower-priced goods but also from the reduced need for waste disposal and from the conservation of natural resources. Practices intended to improve the quality of employees' lives—both in and out of the workplace—also advance the well-being of the firm and society at large. For example, a firm that makes wellness programs available to its employees sees increased productivity as employees take fewer sick days. The firm also avoids the high costs associated with the more serious health care problems that wellness programs help avert. Society as a whole benefits from these programs to the extent that they encourage the more efficient use of health care resources and health in general. Finally, practices involving community investment, philanthropy, and volunteerism also promote utility for both the firm and society at large. For example, a firm that invests in the cultural and educational institutions in its local community benefits by being able to recruit new employees to a thriving community, and the community as a whole obviously benefits when these institutions are flourishing. A concrete example of strategic philanthropy is a computer manufacturer that donates its products to schools. The firm promotes future sales by introducing students to its products early on, and in doing this, it provides significant educational resources to the community. All these business practices improve the reputation of the firm in the eyes of its various stakeholders, and the firm profits from the loyalty and goodwill of these constituencies.

Certain normative views see utility as *the* basic moral concept. This is the case with ethical egoism and utilitarianism. Both these consequentialist views see morality fundamentally as a matter of maximizing utility, though the two views disagree about *whose* utility ought to be maximized. According to ethical egoism, one ought to maximize one's own utility, and, according to utilitarianism, one ought to maximize the utility of all people (or, sometimes, all sentient beings). The moral status (rightness or wrongness) of decisions, actions, and policies is, on these views, exclusively a function of their effect on utility. But concerns about utility are often present in nonconsequentialist views as well, and most plausible deontological approaches recognize a moral duty to promote utility even while denying that morality is *essentially* a matter of maximizing utility.

The notion of utility played an important role in the development of modern microeconomics. Modern value theory considers prices to be determined simultaneously by factors on both the supply side (e.g., production costs) and the demand side. The development of "utility theory" in the 19th century made possible the analysis of consumer demand. Consumers' purchasing decisions (and, in turn, the effects of these decisions on prices) could be explained on the assumption that consumers are rational and will, therefore, purchase bundles of commodities that maximize their utility. The concept of utility was also important to the growth of welfare economics, providing a normative standard by which resource allocations and economic policies could be evaluated. The notion is also employed in development economics.

Utility is a foundational concept in the interdisciplinary fields of decision theory and game theory, which involve the formal (mathematical) study of rational decision making. Decision theory studies decision making in cases where an individual's choice neither affects nor is affected by the choices of others; game theory studies choices involving a strategic component—that is, cases where individuals' decisions do affect one another. The theory of expected utility associated with these fields is regarded by many as offering the most compelling account of practical reasoning available. This theory defines rational action as an action that maximizes expected utility.

Different Conceptions of Utility

This section reviews the main historical and contemporary approaches to understanding utility, identifying the main attractions and drawbacks of each approach.

Hedonism: A Mental-State Approach to Utility

Hedonism is the view that pleasure is the only thing that is good in and of itself and pain the only thing that is bad in and of itself. The most famous defender of this view in the ancient world was

Epicurus (ca. 341–270 BCE). Hedonism was revived in the modern period by Claude-Adrien Helvétius (1715–1771) and was advanced by the classical utilitarians—Jeremy Bentham (1748–1832), James Mill (1773–1836), John Stuart Mill (1806–1873), and Henry Sidgwick (1838–1900). (It should be noted, however, that several different approaches to utility are discernible in Mill's writings, and Sidgwick's account of utility as "desirable consciousness" suggests a hybrid of a hedonistic and desire-satisfaction approach, which is discussed in the following section.)

Hedonism is a *mental-state account* of welfare. According to such an account, an individual's welfare is exclusively a function of the quality of his or her mental states (conscious experiences). The hedonist maintains that an individual's welfare consists solely in his or her having pleasant experiences. (Note that hedonism implies that we can speak meaningfully about the welfare of sentient nonhuman beings.) Mental-state accounts of welfare other than hedonism are possible: These accounts would identify welfare with experiencing mental states other than, or in addition to, pleasure. Hedonism itself can be developed in different ways depending on how "pleasure" is understood. Some hedonists think of pleasure as a sensation that has an agreeable or pleasant quality ("feeling tone") to it and that all pleasures have this same quality. Other hedonists deny that there is any such homogeneous quality; there is, they argue, no feeling in common between, say, the pleasure of eating ice cream and the pleasure of reading a good book. These hedonists understand pleasures to be those sensations that one likes to have and that one wants to continue having just for their qualities as sensations.

Mental-state accounts of welfare are attractive because they straightforwardly reflect the very plausible idea that things have no value to us unless they enter into our conscious experience. (This idea is sometimes referred to as the "experience requirement.") Hedonism, more specifically, is attractive because introspection confirms that pleasure is good and pain is bad. But the stronger claim that pleasure and pain are the *only* things that are of value and disvalue to us has met with numerous objections. One of the most compelling objections to hedonism, and mental-state accounts of welfare more generally, was offered by Robert Nozick (1938–2002). He argued that if the only thing that matters to us is how our experiences feel "from the inside," as the hedonist contends, then we should willingly plug into an "experience machine" that is capable of producing in us any pleasurable experience that we desire. But the idea of plugging into such a machine is unattractive, Nozick claims, and this is because there are things in addition to our experiences that matter to us. It matters to us that we *actually do* certain things and that we *actually are* certain ways, not just that we have the experience of doing these things and being these ways. It matters to us that our experience is based on reality and not illusion. Those who share Nozick's intuition that a life spent plugged into an experience machine would lack something deeply valuable—despite the continuous stream of pleasurable mental states that one would experience—will reject hedonism and mental-state accounts of welfare more generally.

Desire (Preference) Satisfaction Theories

Today, the predominant approach to the idea of utility is to see it as the satisfaction of individual desires (or, as economists say, "preferences"). On this view, a person's welfare is a function of his getting what he wants. People often do desire pleasure, and to this extent the implications of desire-satisfaction and hedonistic theories converge; but people also sometimes forgo pleasure to satisfy other desires, and in these cases the theories diverge. While the satisfaction of any desire typically brings some pleasure, this feeling of satisfaction is not essential according to desire-satisfaction views: What is crucial is that the desired state of affairs has in fact been obtained.

This approach to utility is popular among philosophers and social scientists for various reasons. Because desire-satisfaction theories maintain that the welfare of a person is to be judged from his or her own point of view—that is, what is good for a person is the person's getting what *he or she* wants, not what *someone else* thinks is good for him or her—these theories are democratic, nonpaternalistic, and respect the diversity of individuals' wants. Desire-satisfaction theories also reflect a naturalistic (scientific) approach to value. On this view, values are not mysterious entities; they are the straightforward product of human desires, which are relatively easy to identify and measure. If we want to know what things are good, we can simply ask people what they desire. If we want to know how good a thing is, we can measure the intensity of people's desires by asking them to rank their preferences or by asking them what things they would be willing to trade to get something else. *Revealed preference theory,* developed by the economist Paul Samuelson (1915–), identifies consumers' preferences as they are revealed by purchasing habits.

Despite its widespread appeal, there are problems with treating welfare as desire-satisfaction. Economists tend to identify welfare with the satisfaction of an individual's *actual* desires, largely because they assume that people always have correct beliefs and seek to maximize their own self-interest. This assumption is dubious. A person's desires may be based on false beliefs, or they may be formed without an adequate understanding of relevant facts. Also, troublesome are "adaptive preferences" that are the product of one's social conditioning. For example, a woman living in a patriarchal society may limit her aspirations and desires, believing that it is unnatural for her to want the same sorts of things that her male counterparts do. While her actual (adapted) desires may be satisfied, her welfare may be poor nonetheless. For these reasons and others, it is natural to think that people will sometimes (perhaps often) actually want things that are in fact bad for them.

The most plausible desire-satisfaction theories, such as those offered by Richard Brandt (1910–1997) and James Griffin (1933–), define welfare in terms of *ideal* desires rather than actual ones. (Mill's appeal in *Utilitarianism* to the desires of competent judges to identify "higher" pleasures suggests an ideal-desire view.) On this approach, welfare is identified with the satisfaction of those desires that a person would hypothetically have under ideal conditions—that is, where the person is fully informed, wholly rational, and not subject to any problematic forms of psychological conditioning. While ideal-desire theories avoid many of the pitfalls of actual-desire theories, they also appear to undermine the very features of the desire-satisfaction approach that made it attractive in the first place. It is not clear how we are to know and measure individuals' hypothetical desires. Moreover, to the extent that ideal-desire theories encourage us to consider what people *should* want, rather than what they *actually do* want, this account risks slipping into an objective theory of welfare, which holds that certain things are valuable in themselves regardless of whether they are desired. What really seems to matter on ideal-desire theories is not simply that a person's desire is fulfilled but rather that what the person desires is itself good.

Objective Theories

Objective accounts of welfare maintain that there are certain human states and activities that are good or bad for us apart from any pleasure or pain that they may bring or whether they are (actually or hypothetically) desired. Things that are frequently regarded as objectively valuable include knowledge, physical and mental health, moral virtue, personal and social relationships, the development of one's talents, and the successful pursuit of one's personal projects. On this approach, a person's welfare is a function of his or her possessing these sorts of goods.

Objective accounts of welfare take several different forms, though they often have similar implications. *Objective List (Indexical) Theories,* such as those defended by G. E. Moore (1873–1958) and W. D. Ross (1877–1971), simply catalog goods that are thought to be components of welfare. *Perfectionist Theories* are teleological: They understand welfare as being constituted of those things that are necessary to perfect one's uniquely human nature. This is the approach of Aristotle (384–322 BCE), Thomas Aquinas (ca. 1224–1274), Friedrich Nietzsche (1844–1900), and, recently, Thomas Hurka (1952–). (Mill's chapter on individuality in *On Liberty* also suggests perfectionism.) *Primary (Basic) Goods Theories,* associated with John Rawls (1921–2002), are similar to perfectionist theories in so far as they too understand welfare as involving those things that are necessary to pursuing one's life plan; but, unlike perfectionist theories, they do not posit a unique human *telos*—that is, they do not presume that all rational humans should pursue *the same* life plan. Primary goods are those things that are necessary to achieve whatever rational ends different individuals may choose. Amartya Sen's (1933–) *Capability Approach* assesses individual welfare in terms of a person's capabilities. A capability is the capacity or potential to do or be something, or, as Sen puts it, to achieve certain "functionings." Sen recognizes strong conceptual connections between his approach and Aristotle's, and he acknowledges the important influence of Rawls. But he argues that the capability approach is more sensitive than other objective theories to individual circumstances, such as having physical disabilities, which can significantly affect welfare.

These objective approaches to welfare accord well with many of our commonsense beliefs about welfare. It makes sense to say that we are doing well when we are healthy, when our lives contain things like knowledge and love, when our projects are going well, and so forth. Many of the standard criticisms of subjective accounts of welfare straightforwardly reflect objectivist intuitions. Nozick's thought experiment shows that we want actually to possess and engage in those things that are regarded as objectively valuable, not just have the pleasant experiences associated with them. Furthermore, we tend to think that these are things that people should desire regardless of what they in fact do desire. Of course, subjectivists' intuitions run just as deep and in the opposite direction. They think that it is strange to insist that things have value even if they bring no enjoyment whatsoever and are not desired at all. If we remove these subjective elements, they maintain, what is left has no value.

Measuring Utility

This section considers two basic issues related to the measurement of utility. The first issue is whether utility can be measured cardinally or only ordinally. The second issue is whether interpersonal comparisons of utility are possible, in principle and in practice. These issues obviously have implications for both positive (explanatory) and normative theory: Can the notion of utility really serve the theoretical purposes credited to it? Different conceptions of utility imply different answers to these questions, and this must certainly be taken into account when considering which of these conceptions offers the best understanding of utility. (One could, of course, argue that there is no single "best" understanding of the notion and that different conceptions of utility are appropriate for different theoretical contexts.)

Cardinal and Ordinal Utility

Utility is said to be *cardinal* if it can be measured in terms of its magnitude—that is, if it can be measured on either an interval or ratio scale. Those who regard utility as being cardinal think that expressions such as "*A* produces four units of utility more than *B*" or "*A* produces twice as much utility as *B*" are meaningful. (Units of utility are referred to as *utils.*) Those who regard utility as being *ordinal* think that utility cannot be measured in terms of its magnitude, and, hence, these statements are meaningless. If utility is ordinal, then we can only say things like, "*A* is more valuable than *B,*" but this tells us nothing about the degree of *A*'s value relative to *B.*

Bentham thought that utility, understood in hedonistic terms, is cardinal, and he proposed the development of a "felicific calculus." He believed that all pleasures are intrinsically the same, and, hence, measurable on a single scale. The value of any given pleasure, he believed, can be quantified in terms of its intensity, duration, certainty of obtaining, nearness in time, fecundity, and purity. Bentham's view exercised considerable influence on economists' understanding of utility through the 19th century. Hedonism reached its apex in economics with the work of W. S. Jevons (1835–1882) and F. Y. Edgeworth (1845–1926). Edgeworth envisioned the development of a "hedonimeter" that would measure the pleasures actually experienced by people. (Units of utility, or utils, are commonly referred to as *hedons* within the context of hedonistic theories.) Edgeworth's explanation of consumer behavior assumed that utility is cardinally measurable. At any moment, a consumer has available to him or her all those bundles of goods whose cost does not exceed his or her income. Edgeworth assumed that the consumer could assign a numerical value to each bundle representing its utility (expressed in a *utility function*) and that the consumer would choose the bundle with the highest utility.

By the early 20th century, worries about the difficulty (if not impossibility) of quantifying subjective mental states led economists such as Vilfredo Pareto (1848–1923) and Irving Fisher (1867–1947) to question the assumption that utility must be cardinally measurable to explain consumer demand. Pareto showed that choices could be analyzed simply in terms of the consumer's ordering of (or indifference toward) different bundles of commodities. Thus, only an ordinal ranking of preferences is necessary to analyze consumer demand. This line of analysis was further developed by Eugen Slutsky (1880–1948), J. R. Hicks (1904–1989), and R. G. D. Allen (1906–1983). While Pareto established that cardinal utility is superfluous for economic theory, he did allow that it is useful for explanatory purposes to assume that utility is cardinally measurable, and this assumption continues to be employed as an explanatory device in most introductory-level microeconomics courses.

Interpersonal Comparisons of Utility

Different conceptions of utility have different implications for our ability to make interpersonal comparisons of welfare and, hence, to aggregate (or average, depending on one's approach) individual utilities. All subjective theories—mental-state theories and desire-satisfaction theories—face a common problem, namely, the inscrutability of other minds. If Bentham's claim that all pleasures are measurable on a single scale is true, then it is possible in principle to compare and aggregate individual utilities, as his utilitarianism requires. However, since we do not have direct access to the mental states of others, direct comparisons of individuals' utilities are not possible in practice. Bentham conceded as much in private, and Jevons was explicit on this point, though he did not refrain from comparing and aggregating individual utilities.

Our inability to know the content of other minds is a problem for desire-satisfaction theories, too, since we cannot directly know the strength of one another's desires. But desire-satisfaction theories face a more fundamental problem since they deny that there is an interpersonally valid scale in terms of which we can measure and compare one another's desires and preferences. As the economist Lionel Robbins (1898–1984) argued, because our individual preferences are wholly subjective, there is no way to compare the utility of two (or more) individuals. (Indeed, it is not even clear how to account for *intrapersonal* comparisons of utility across time on the desire-satisfaction approach, given that individuals' preferences change over time.) Robbins concluded, based on the positivist doctrine that all scientific claims must be empirically verifiable, that interpersonal comparisons of utility involve nonscientific ethical and political judgments that fall outside the scope of economics. This opinion dominated economic thought in the 20th century.

The works of Pareto and Robbins invited the development of a new approach to welfare economics. The so-called *old* welfare economics constructed by Alfred Marshall (1842–1924) and his student A. C. Pigou (1877–1959) assumed that utility is cardinal, that interpersonal comparisons of utility are possible, and, hence, that a social welfare function can be constructed simply by summing individual utilities. (Marshall and Pigou measured social welfare in terms of the national dividend or aggregate income.) Marshall and Pigou did not do much by way of elucidating or justifying these foundational assumptions, which were rejected by the proponents of "new" welfare economics. This approach is based on the work of Pareto, Hicks, and Nicholas Kaldor (1908–1986). The dismissal of cardinal utility implied that the traditional understanding of social welfare is untenable: If individual utility is not measurable, then social welfare simply cannot be a function of adding together or averaging the utilities of different individuals. Pareto introduced a purely ordinal criterion for ordering social decisions that did not require interpersonal comparisons of utility. A state of the world S_1 is *Pareto superior* to another state S_2 just in case no one prefers S_2 to S_1 and at least one person prefers S_1 to S_2. In other words, S_1 is Pareto superior to S_2 if and only if no one is better off (in terms of preference satisfaction) in S_2 than in S_1 and at least one person is better off in S_1 than in S_2. A state of the world is *Pareto optimal* if there is no alternative state that is Pareto superior to it. Because most social and economic policy changes benefit some at the expense of others, Pareto superiority is very rarely satisfied in reality. This fact led to the introduction of less restrictive criteria of evaluation, the most famous of which is the Kaldor-Hicks criterion: A state of the world S_1 is *Kaldor-Hicks superior* to another state S_2 just in case those who are made better off in going from S_1 to S_2 could hypothetically compensate those who are made worse off in such a way that, were compensation actually to occur, S_1 would be Pareto superior to S_2. The Kaldor-Hicks criterion (sometimes called the Potential Pareto Test) allows us to consider whether a change from one policy to another that produces winners *and* losers will increase overall utility, but the Kaldor-Hicks criterion yields intransitive rankings (S_1 may be a Kaldor-Hicks improvement over S_2, and S_2 may be an improvement over S_3, yet S_1 may not be an improvement over S_3). Hence, the Kaldor-Hicks criterion cannot be employed to judge the utilitarian merits of alternative social and economic policies. Moreover, because the Kaldor-Hicks criterion considers only the absolute level of utility and wholly disregards how utility is distributed, the fact that S_1 is an improvement over S_2 does not entail that the move from S_1 to S_2 is morally desirable.

If welfare economics remains tenable without interpersonal comparisons of utility, utilitarianism does not. Its application requires such comparisons—as does any moral theory requiring comparisons of persons' welfare. Most contemporary utilitarians believe that the economists and philosophers influenced by logical positivism have greatly exaggerated the difficulties of making interpersonal comparisons of utility. They argue that although we do not have *direct* insight into other minds, we do nonetheless have very reliable *indirect* evidence about the mental states and desires of others. Recent developments in neuroscience encourage some to believe that the objective measurement and comparison of mental states may one day be possible. Edgeworth's hedonimeter may be realized yet. Some utilitarians have argued, contrary to Robbins, that we actually can generate meaningful interpersonal comparisons based solely on preferences. John Harsanyi (1920–2000), for example, argues that we can derive interpersonal comparisons from "extended preferences" expressed in judgments of the form: "I would prefer to be in person *P*'s state rather than in person *Q*'s state." Other utilitarians, such as David Brink (1958–), adopt an objective understanding of utility that avoids the problems associated with subjective approaches altogether. Indeed, this is one of the main attractions of objective conceptions of welfare.

Once a list of objective values or primary goods is articulated, we can simply compare the extent to which two (or more) individuals realize these values or possess these goods. However, it is very difficult to see how these objective values are to be combined so as to yield an indicator of overall welfare. This is because these objective values are incommensurable—they are good in different ways and for different reasons. Jack has more knowledge than Jill, but Jill has deeper and more meaningful personal relationships. Who is better off overall?

Related Topics

The first part of this final section introduces the distinction between total and marginal utility and explains how this distinction has been used in positive and normative theory. The second part introduces the notion of expected utility and the theory of practical reasoning based on that concept.

Total and Marginal Utility

In *The Wealth of Nations,* Adam Smith observed that, although water is essential to life and diamonds are not, the market value of diamonds is far greater than the market value of water. This apparent inconsistency, known as the paradox of value or the water-diamond paradox, was eventually resolved by distinguishing between total and marginal utility. *Total utility* refers to the aggregate sum of utility that an individual obtains from consuming a given amount of a commodity. *Marginal* (or *incremental*) *utility* refers to the additional amount of utility that an individual derives from consuming an additional unit of a commodity. The *law of diminishing marginal utility* states that marginal utility decreases with each additional unit of a commodity that is consumed—that is, each additional unit that is consumed produces less utility than the last. These ideas are illustrated in Table 1, which shows the total and marginal utility that a hypothetical consumer might derive from drinking various amounts of coffee on any given morning.

The development of these ideas in the late 19th century by Jevons, Carl Menger (1840–1921), and Léon Walras (1834–1910) initiated the "marginal revolution" that gave rise to neoclassical economics. Marginalism provided a simple explanation of the law of demand that entails that the demand curve will have a negative slope. Because each additional unit of a commodity produces less utility than the preceding unit, a consumer will pay less for a commodity as its quantity increases. The law of demand, then, is a straightforward implication of the law of diminishing marginal utility. Marginalism also provided a simple resolution of the paradox of value. While water undoubtedly has a higher total utility than diamonds, the relevant comparison is between the marginal utility of water and the marginal utility of diamonds. Since the marginal utility of scarce goods is higher than the marginal utility of abundant goods, consumers are willing to pay higher prices for scarce goods like diamonds than they are for abundant goods like water.

Marginalism also yielded important moral conclusions regarding the distribution of wealth and resources. Pigou argued that, ceteris paribus, a more equal income distribution will increase overall social welfare. This is because the law of diminishing marginal utility implies that additional income will produce more utility for a poor person than for a rich person. (Note how this argument employs interpersonal utility comparisons.) Pigou concluded that progressive income taxation improves social welfare, so long as this redistributive policy does not reduce aggregate income by decreasing incentives to work or save. Brandt, Peter Singer (1946–), and many other utilitarian philosophers have employed similar reasoning to show that utilitarianism supports egalitarian distributions.

Table 1 Total and Marginal Utility

Cups of Coffee Consumed per Morning	*Marginal Utility*	*Total Utility*
0	0	0
1	75	75
2	50	125
3	10	135
4	0	135
5	−15	120

Expected Utility Theory

Expected utility theory studies choices in situations where the decision maker is not certain what the actual outcome of alternative courses of action will be. On this theory, the rational decision maker will maximize *expected utility,* where the expected utility of an action is determined by measuring the utility of each possible outcome of the action, multiplying the utility of each possible outcome by the probability that the outcome will occur, and then summing together the results for all possible outcomes. A simple example involving a lottery illustrates the idea. Suppose that you are considering whether or not to buy a lottery ticket that costs \$5. The payoff in the lottery is \$1 million, and the probability of winning is .00001. There are two possible outcomes if you buy a ticket: Either you will win and collect \$1 million, or you will lose and be out \$5. The expected utility of buying a lottery ticket then is

$$(1{,}000{,}000 \times .00001) + (-5 \times .99999) = 5.00005.$$

Since it is certain that you will not win or lose anything if you do not buy a ticket, the expected utility of not buying a ticket is

$$(0 \times 1) = 0.$$

Because the expected utility of buying a ticket (5.00005) is greater than the expected utility of not buying a ticket (0), it is rational for you to buy the ticket, despite the likelihood of your losing.

The notion of expected utility was introduced by Daniel Bernoulli (1700–1782), who was also one of the first to postulate the law of diminishing marginal utility. However, expected utility theory was not developed in a systematic fashion until the mid-20th century. The approach developed by John von Neumann (1903–1957) and Oskar Morgenstern (1902–1977) applied to decisions made under conditions of "risk"—that is, in situations like our lottery case where the probabilities of the various outcomes occurring are known. Leonard Savage (1917–1971), drawing from ideas developed by Frank Ramsey (1903–1930), extended the scope of expected utility theory by applying it to decisions made under conditions of "uncertainty"—that is, in situations where the probabilities of various outcomes occurring are completely unknown and therefore based on the decision maker's subjective judgment. Today, expected utility theory is employed for both positive and normative purposes. Many utilitarians now understand the theory to require the maximization of expected utility as opposed to actual utility.

Although expected utility theory offers a powerful account of practical reasoning, the theory has been contested. Some have challenged the theory's fundamental assumption that rational action aims to *maximize* utility. For example, Herbert Simon (1916–2001) has argued that it is often rational to engage in "satisficing" behavior—that is, to pursue a course of action that achieves a satisfactory, but less than maximal, result, and Rawls has defended the rationality of employing a "maximin" strategy—choosing the action or policy that maximizes the minimum payoff—in some situations involving uncertainty.

—Michael B. Mathias

See also Bentham, Jeremy; Capabilities Approach; Commensurability; Consequentialist Ethical Systems; Consumer Preferences; Cost-Benefit Analysis; Economic Efficiency; Economics and Ethics; Economics of Well-Being (Post-Welfarist Economics); Egoism; Expected Utility; Game Theory; Hedonism, Ethical; Interpersonal Comparison of Utility; Marginal Utility; Mill, John Stuart; Nozick, Robert; Pareto, Vilfredo; Pareto Efficiency; Primary Goods; Rational Choice Theory; Rawls, John; Revealed Preference; Sidgwick, Henry; Tax Ethics; Utilitarianism; Utility, Principle of; Von Neumann-Morgenstern Utility Function; Welfare Economics; Well-Being

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Utility, Principle of

The principle of utility, also known as the greatest happiness principle, is associated with Jeremy Bentham (1748–1832), the first of the great 19th-century utilitarians. As Bentham and later John Stuart Mill (1806–1873) expounded it, the principle approves or disapproves of actions based on whether they increase or decrease the happiness of everyone affected by the action. The principle of utility constitutes the standard of right and wrong, in terms of which human conduct is to be assessed.

Bentham identified happiness and unhappiness with pleasure and pain, affirming the hedonistic doctrine that pleasure is the only thing that is good in itself. He cataloged different pleasures and pains and described their various sources and the factors influencing our experience of them. The value of any given pleasure or pain is a function of its intensity, duration, certainty, and "propinquity" (or nearness). We must also consider the likelihood that the pleasure (or pain) will be followed by other pleasures (or pains) of the same kind (its "fecundity") and not followed by sensations of the opposite kind (its "purity"). In this way, we can estimate, first, the goodness or badness of an action for any given individual and, then, by taking into account all individuals affected by the action, its overall goodness or badness.

Critics of Bentham have long characterized his theory as crude and lampooned the whole idea of a hedonic calculus by means of which the pleasures and pains of individuals are to be weighed and summed. Bentham, however, was concerned not only with sensory or bodily pleasures and pains, but also with various other forms of satisfaction, enjoyment, and fulfillment—for example, the pleasures of memory or religion and the pain of a bad reputation or of knowing that another is suffering. Still, Bentham held that all pleasures are intrinsically equal, famously remarking that if the amount of pleasure is the same, then the game of "push-pin" is of equal value with poetry. Bentham certainly thought that pleasures involving intellect, imagination, and deep human emotion are, as a rule, superior to simple physical pleasures. But this is because higher pleasures tend to be more pleasurable than lower ones.

Like Bentham, Mill associated happiness with pleasure, but he thought that one could compare and rank pleasures, not just quantitatively but also qualitatively. In other words, some kinds of pleasure are better than others, not because they are more pleasurable, but because they represent pleasures of a higher or more valuable kind. Thus, even though two activities involve equal amounts of pleasure as measured by Bentham, one of the pleasures might be qualitatively superior to the other. We know that one pleasure is qualitatively higher than another, Mill thought, if, putting aside the issue of intensity and duration, those who have experienced both judge the one to be preferable in kind to the other.

Applying the Principle

In applying the principle of utility, one must bear in mind that an action can have both good and bad effects. Accordingly, the principle tells us to choose that action the net outcome of which, taking into account all its consequences, both positive and negative, produces the greatest amount of pleasure. Although the principle of utility is sometimes identified with the slogan "the greatest happiness of the greatest number," this formulation can be misleading. Because actions affect people to different degrees, the action that makes the most people happy may not bring about the greatest happiness. The principle of utility tells us to add up the various pleasures and pains, however large or small, of the courses of action open to us and to select the one that results in the greatest net amount of happiness. Depending on the circumstances, this action may or may not bring happiness to more people than other actions would have.

The principle of utility is often interpreted as equivalent to act utilitarianism, which is the theory that an action is right if and only if it brings about at least as much happiness as any other action the agent could have performed at the time; otherwise, it is wrong. But it is debatable whether either Bentham or Mill subscribed to this view. Their formulations of the principle don't entail it, and it is doubtful that they would have judged a happiness-producing action to be morally wrong just because it failed to maximize happiness. Rather, they may have intended their principle to supply a standard for comparing actions along a continuum of better and worse.

Moreover, neither Bentham nor Mill restricted application of the principle of utility to individual actions. They and the other early utilitarians were social reformers who used the principle as the basis for assessing and criticizing the social, political, and legal institutions of their day. Bentham was particularly interested in penal and legal reform, and the early utilitarians sought to promote social and economic policies, such as free trade, that they saw as tending to bring the greatest benefit to society. In fact, many commentators believe that Bentham, in particular, intended the principle to apply primarily to legislation, administration, public policy, and institutional reform, and not to individual conduct. Mill, too, probably thought that in many contexts the primary focus of the principle of utility should be the rules, policies, or institutions that govern or set the framework in which, say, firms pursue profit or businesspeople act, rather than on the particular decisions they make.

In line with this, some commentators have argued that Bentham and Mill were rule utilitarians. Rule utilitarianism is the theory that the principle of utility should be used not to assess individual actions but rather to select the moral rules that individuals or a society should follow. But both men clearly wanted to apply the principle of utility, at least sometimes, to individual actions. Because of this, classifying them as rule utilitarians is problematic, too.

—William H. Shaw

See also Bentham, Jeremy; Cost-Benefit Analysis; Expected Utility; Hedonism, Ethical; Hedonism, Psychological; Interpersonal Comparison of Utility; Mill, John Stuart; Utilitarianism; Utility

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V

Value-Added Tax (VAT)

A value-added tax (VAT) is a sales tax levied at every step in a production process. The VAT is collected when goods or services are purchased throughout the production process, from the initial purchase of raw materials to the sale of the final product at a retail outlet. In some countries VAT is known as "goods and services" tax (GST).

Consumption Versus Saving

Individuals can do two things with their income: They can consume (spend) it, or they can save it. In an income-based tax system, both consumption and savings are taxed; in a consumption-based tax system, only consumption (income minus savings) is taxed. Consumption taxes are very popular with governments around the globe; the United States is the only developed nation without a broad-based consumption tax at the national level. Some tax reformers want to replace the current income-based tax system in the United States with a consumption-based tax system.

A consumption tax can be levied at either the individual level or the retail level. When it is levied at the individual level, taxpayers add up all income and subtract net savings (saving minus borrowing). The resulting figure is the consumption base on which a tax is levied. When a consumption tax is levied at the retail level, it takes the form of a sales tax or a VAT. A sales tax is collected from the ultimate consumers. A VAT is collected from sellers at each stage of production. Regardless of which level the tax is levied at, and regardless of the point of collection, the consumption tax is ultimately paid for by the consumers.

Consumption taxes can be direct or indirect. The "consumed income tax" is a direct consumption tax because it is levied at the individual level. Such taxes can be personalized through exemptions, deductions, and progressive rates. Both the national sales tax and the VAT are indirect consumption taxes because they are levied at the retail level. Such taxes cannot be personalized.

Methods of Calculation

Two basic methods have been established for computing the VAT: the credit method and the subtraction method. The credit method is used in the European community and Canada, while the subtraction method is used in Japan.

Under the credit-invoice method (the most widely used credit method), an invoice is issued for each sale. The amount of VAT included in the invoice price is separately stated at each stage of the production process, except at the final stage when the product is sold to the consumer. At the end of a designated period (monthly, quarterly, or yearly, depending on the country), the business pays the total tax shown on all sales invoices, reduced by the total tax shown on all purchases invoices. Under the subtraction method, a tax computation at the time of sale is not required. The tax is computed each period by subtracting total purchases from sales and applying the tax rate.

In its purest form, a VAT would be levied, under either of the above methods, on all goods and services at one standard rate. However, this has not been the case in most countries. When an item is exempt from the VAT, no tax is levied on that item. There may be several reasons for exempting an item. First, an item may be exempt to reduce the tax burden on lower-income individuals. For example, most VAT systems currently exempt necessities such as food, health care, and housing. Exemptions can also be granted if the cost of compliance is too high in relation to the revenues generated. Many countries exempt small businesses from the VAT for this reason. When a VAT system has several exemptions, the VAT computation can become quite complex for those businesses that deal in both exempt and nonexempt items.

Zero rating occurs when the rate applied to a particular good or service is zero. This is different from an exemption since the good or service is still included in the VAT system and computation but is taxed at a zero rate. A tax return must be filed for zero-rated items. Zero rating occurs throughout the production process. Multiple rates can be used to further reduce regressiveness of the tax. The VAT systems in some countries apply different rates on items such as candy, consumer electronics, furs, jewelry, advertising, entertainment, hotels, and other luxury goods and services. The political motive for multiple VAT rates is tax equity to mitigate the regressive pattern of the VAT, since poorer individuals often find a higher proportion of their income consumed by the VAT due to its regressiveness.

Under a VAT, exporters are able to obtain credits for the tax, since exports are exempt from this tax, thereby strengthening the competitiveness of exports. Tourists are eligible for rebates of VATs charged on purchases. However, since the tax is often included in the sticker price of the item, visitors may not even realize they are being charged a VAT. Furthermore, VAT claim rules differ from country to country, and claiming refunds can be difficult.

Since its introduction, the VAT has become an important source of budget revenue internationally, which has been a major factor in its success and popularity. The VAT's raw power to raise revenues has been cited as one reason the United States has thus far rejected it as part of tax reform, because of fear it could become a blank check for future tax increases, thus detracting from the need to cut spending.

VAT Evasion

Often, taxpayers are able to evade the VAT. Some of the most common methods for doing so are as follows:

- Understating sales, especially at the retail level and with services such as construction and consulting, where the self-enforcing properties of the VAT break down.
- Inflating claims for VAT paid on inputs.
- Claiming credit for tax paid on inputs used in producing goods that are exempt from the VAT. This is possible if a firm sells both exempt and nonexempt goods and services and can be difficult to detect, since it is not always possible to link specific inputs with specific outputs.
- Collection of VAT by a firm, which does not remit it to the proper authorities and then disappears.
- Claiming VAT credit for noncreditable purchases, such as a car used for nonbusiness purposes.
- Nonregistration for the VAT.
- Diverting zero-rated exports to the domestic market. Here, the producer obtains export papers, claims a refund, and then sells the goods locally.
- Claiming that the transaction is not a taxable event and that it is a gift rather than a sale or that there was an absence of consideration.

The increasing recognition of the difficulties involved in collecting the correct amount of VAT may explain the marked tendency for VATs to get simpler with time. With multiple-rate VAT systems comes the greater ease of fraud, and compliance costs rise as the tax forms become more complex and accounting records need to be more complete. Consequently, a higher average VAT rate is associated with lower compliance. Administrative expenditures by taxing authorities seeking enforcement have a clear effect on compliance.

—Paula J. Thielen

See also Consumption Taxes; Flat Tax; Primary Goods; Regressive Tax

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Values, Personal

Personal values are those values that people adopt as principles that guide their life. They are values precisely because they are valuable to the person. The person freely chooses to give them "value" for guiding behaviors and actions in all aspects of his or her life, from family life to working and social life.

If, for instance, a person plays a sport such as tennis, his or her personal sports values will be reflected on the court. Something similar happens at home or at work. "Fair play," for instance, as a personal value, may be as important on the tennis court, at work, or with friends. The person, although having different dimensions, such as social, interpersonal, communicative, financial, or spiritual, is one and unique. Therefore, if an individual wants to be coherent and consistent with what he or she thinks, says, and does, the person must also show this coherence of values in all levels of life. In this way, the personal values should cover in a transverse way the different fields of personal conduct, from sports to professional life.

Personal values help the person at the moment of choosing, distinguishing the decisions, or actions to be undertaken. Personal values are determining factors when deciding whether to go in one direction or another. For instance, a person who decides not to join a company because it would involve certain dishonest actions has honesty as an action criterion and personal value when doing business. Joining such a company would contradict the individual's personal value.

Development and Cohesiveness of Values

Personal values are one of the points of cohesion between the different facets of the person. Just as cement is necessary to join one brick to another and build a solid building, personal values are the cement of our life. Without them, the personal building can be built but the risk of collapse is much greater.

Everyone has values, including those who deny having them. The denial of personal values—explicit or not—is also a choice. The person is free to be able to state: "I do not have personal values. I do not believe in them." Another very different question is that people are very aware of their personal values and put them into day-to-day practice. In fact, the important thing is that their personal values are shown in their actions, that the level of awareness of personal values is present in daily life. But it is also true that there are people who are not entirely aware of the relevance of personal values.

All effort directed toward placing emphasis on the discovery, development, and consolidation of personal values is not in vain. In this respect, childhood and adolescence are key stages of development in the formation of personal values, particularly through the family and school, although other social factors may be crucial in this formation. Personal values are present, in one way or another, in a person's actions and behaviors. In other words, people show certain values through their actions or omissions of what they do or do not do, and always from the freedom inherent to everyone. It is in this way, through the actions or omissions that are freely chosen, that people build their personal values. What people indeed do indicates what their personal values are. The actions, freely chosen, gradually build them as people.

The personal values that people choose, materialized in actions, have consequences not only for the more immediate environment of the person but also for the person. Personal values, if they are more than just good intentions and are indeed embodied in the person, make the person. Therefore, personal values become significant in that they are materialized in our daily work and life. The person is closely tied to personal values. In the heart of the person we find the values that give sense to the person. Therefore, personal values are also tied to the sense that the person wants to give to his or her life and aims. It is like this because personal values guide the behavior and actions of the person. We must not forget that sense is also orientation and direction.

Deep down is the desire of each person to lead a full life. Personal values help the person to live life to the fullest, with sense, and according to the aims that he or she pursues. The daily fulfillment of these will give the person a calm spirit due to the coherence between his or her personal values and actions to be undertaken and, when faced with adversities, the necessary calmness to face difficulties that may arise.

Personal values are essential elements that a person uses to act with a certain amount of coherence in the different areas of life. For instance, if one has loyalty as a personal value, it will be carried over to the personal, social, and professional areas, by being loyal to one's wife, friends, or work team. If one acts in this way, coherently, with this value that is freely chosen, one will be able to walk with one's head held high.

Values and Decision Making

In the course of any day, people make a series of decisions, although some of these are "automatic" and others very well prepared. People are constantly choosing and deciding: what clothes to wear for the day, which route to take to work, to have a cup of tea or coffee, with or without milk. Each of these decisions requires a different set of assessments, such as whether to drink coffee for its taste or not drink it for health reasons. A person could say, "I like having a coffee very much, but it makes me feel terrible." In this situation, the person chooses between "taste" and "health." The option may appear to be simple, but without doubt the actual choice will be unique to each person. The person decides at that moment whether to drink coffee or not.

Different people choose different options in similar circumstances. The range of possibilities is very high but in the coffee example there are two clear facts: First, the person likes coffee a lot; second, drinking coffee has a negative effect on the person's body. Which option should the person choose? Personal values help the person make the decision. If the personal value is health, the option is clear: Do not drink coffee. If the personal value is taste, it is also clear: Drink coffee. But this decision might not be reached in every circumstance. If someone strongly values preserving his or her health, in 99% of circumstances the person will not drink coffee. In 1% of cases, the person might choose to drink coffee because of its taste or a specific social circumstance. This 1% could increase according to the person. This decision varies a great deal from one person to another.

Drinking coffee or not does not appear to be an excessively important daily decision. The complexity of making the decision would clearly increase if a more important decision had to be made. The assessments made would be very different as would the personal values. What appears to be beyond all doubt is that throughout a day many decisions are made of varied relevance for the person and his or her more immediate environment. Considering the personal values associated with each step, until reaching the final decision, can be very beneficial to the person.

Values and Behavior

The decisions that a person makes gradually shape the person's behavior. The decisions embodied in actions make the person. In other words, they have consequences in the person as well as in people that are affected by the decision. There is a close connection between values and behavior. Behavior is a reflection of how a person positions himself or herself with regard to certain situations in life. It indicates the habitual way the person has of behaving. Therefore, actions allow one to reveal a person's values. Personal values are very tied to the conduct of the person, to how the person really acts. If, for instance, a person is said to be "committed" to his or her work, it refers to a series of values of that person concerning devotion, dedication, motivation, and enthusiasm with regard to the work performed.

Values and Character

Personal values, on the one hand, result in specific attitudes, frames of mind that people show in the face of life events and circumstances in which they are involved. On the other hand, personal values are explicit manifestations of a person's character. The values that each person consolidates throughout life are forged in the background of his or her character. Character, in its Greek etymology, means mark or stamp. Personal values, attitude, and character are three decisive pillars in the configuration of the behavior of a person. For instance, a person exploring processes of personal improvement must first systematically examine his or her habitual behavior. The person can examine and assess this behavior himself or herself or with the help of a trustworthy person who can suggest ways to improve. In the case of companies, managers usually turn to highly qualified consultants to introduce processes of improvement in the performance of professionals.

Any person who thinks that in life one has to try to grow both personally and professionally has to pay a lot of attention to personal values because they can be an excellent way to constantly improve behavior, attitudes, and habits. A change in habits may help to modify, in part, the character of the person. New habits may produce improvements in all areas of the person's behavior.

Company Values

At present, there are many companies that, through different documents, make their company values public. Companies can express their values through several methods. We find them in statements of mission and beliefs, in manifestos of values, in codes of conduct, in "who we are." But strictly speaking, only people have values. Company values only exist through the people of that company. It is the people of the company that make the values of that company a reality or not.

Company values are rooted in the culture of the company. The etymology of the word *culture*, in its Latin origin, also means "care" or "cultivation." "Care" refers to prudence, the tact with which certain actions are carried out or specific decisions are made. "Cultivation" refers to growth and development, making an effort and taking the necessary care so that the tasks or projects at hand go ahead and bear fruit. In the selection process, companies tend to hire people who best fit their values. It also happens the other way round. Good professionals try to work for those companies that best fit their personal values.

Aligning company values with personal values can help people develop more fully within the company. If personal values contradict company values, a conflict of interests between the person and the company can easily occur. It is complicated for a person to work for a company where his or her personal values contradict the company's values. Similarly, companies tend not to hire people whose values differ substantially from the values of the company. Essentially, personal values help a person find balance in all aspects of his or her life, including both work and professional life.

—Carlos María Moreno Pérez

See also Fact-Value Distinction; Fidelity; Green Values; Integrity; Intrinsic Value; Morality, Public and Private; Revealed Preference

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Vatican Bank

The official name of the Vatican bank is the Istituto per le Opere di Religione (I.O.R.), or the Institute for Religious Works. It has been called one of the most secretive financial institutions in the world. The bank is known to manage contributions such as the annual worldwide Peter's Pence collection, used for religious, humanitarian, and social development work, and to support activities of the Holy See, the central administration governing the Roman Catholic Church. The bank also manages funds entrusted to it by religious orders and individuals associated with the Vatican. The nature and extent of its holdings and specific transactions, however, are not disclosed.

In contrast to this lack of official information, the bank often found itself the subject of unflattering publicity under its former president, Archbishop Paul C. Marcinkus, who headed the bank from 1971 to 1989. A native of Cicero, Illinois, he was one of the highest-ranking Americans in the Vatican, serving Popes John XXIII, Paul VI, John Paul I, and John Paul II. Initially charged with papal travel arrangements and security, he was appointed to head the Vatican bank despite a lack of financial experience.

In the mid-1970s, an Italian banking scandal linked the bank with Sicilian financier Michele Sindona. Sindona had advised the Holy See and Marcinkus on handling assets and investments. When Sindona's financial empire collapsed, the Vatican experienced losses estimated to be in the tens of millions of dollars. Sindona later died in a Milan prison after his coffee was laced with cyanide.

The next decade brought another scandal, more Vatican losses, and the death of another former financial adviser. Italy's largest investment bank, Banco Ambrosiano, failed in 1982. At the time, the Vatican bank owned a share in the bank and partnered in many deals with its president, Roberto Calvi. The Vatican denied any wrongdoing but agreed to pay $244 million to creditors of Banco Ambrosiano as recognition of moral involvement in the collapse. Archbishop

Marcinkus avoided arrest and standing trial by claiming diplomatic immunity, with which the Italian high court concurred. Calvi was found hanged in London under mysterious circumstances in 1982. At first ruled a suicide, five people went on trial in 2006 charged with his alleged murder.

Marcinkus was also mentioned in a controversy involving the Vatican and millions in Nazi gold purportedly laundered from Germany after World War II. A U.S. State department report implicated the Vatican in the scheme, and investigators tried to question Marcinkus, who again successfully claimed diplomatic immunity. The issue was recently revived in a lawsuit filed against the Vatican bank by Holocaust survivors claiming the bank profited from assets seized by Nazi leaders from prisoners in World War II prison camps. The bank claimed the matter was outside the jurisdiction of federal courts because it involved foreign policy issues. In January 2006, the U.S. Supreme Court allowed the lawsuit to proceed.

Marcinkus served as governor of Vatican City for a year after he left the bank presidency in 1989. He then retired to Arizona, where he died on February 20, 2006. After Marcinkus retired, the Vatican turned over management of the bank to a board of lay financial experts (i.e., not priests or members of a religious order). The finances of both the bank and Vatican City are now overseen by an economic commission of 15 cardinals.

—*Cynthia Scheopner*

See also Christian Ethics

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Veblen, Thorstein (1857–1929)

Thorstein Bunde Veblen, the son of Norwegian immigrants, was an iconoclastic economist, sociologist, historian, and philosopher whose astute analysis and biting satire on the tide of business enterprise in the latter part of the 19th century and early 20th century has endured to this day. He coined terms such as *conspicuous consumption* and *vested interests*, which remain in the popular lexicon. His fundamental insight was that the "state of the industrial arts" (technology) was a dynamic force in societal change that was often retarded by what he termed *imbecile institutions*. In making this dichotomy between technology and institutions, Veblen was not merely a one-sided technological determinist. Instead, he pointed out that in modern capitalist economies, there is often a conflict between making money and making goods. Where Adam Smith described humans' propensity to truck, barter, and exchange, Veblen spoke of the instincts of workmanship and salesmanship. This dichotomy was carried through in his analysis of the "serviceablility" or intrinsically useful characteristics of goods versus the component of "waste" or merely how they were outward displays of status in society.

Veblen delighted in pointing out what he termed *the barbarian origins of modern society*. The Vikings conquered through war and theft, and Veblen saw elements of this in modern society. Unlike Marx, he did not see the conflict between the workers and capitalists to be the essence of capitalism; rather, a race for reputability on the basis of invidious comparison was, for him, a driving force in the evolution of a modern business economy. If there was an ultimate goal for workers, Veblen would say it was not to own the means of production but rather to achieve a level of leisure enjoyed by only a few. This conflict was played out in a society where the technological potential to produce goods was hamstrung by the demands of business enterprise that goods be sold profitably.

Veblen had a checkered academic career. After graduating from Carleton College, he began graduate school at Johns Hopkins, but then switched to Yale for a doctorate in philosophy. Failing to find an academic appointment, he enrolled at Cornell but then went with J. Laurence Laughlin to the new University of Chicago, where he became an instructor and an editor of the *Journal of Political Economy.* After periods at Stanford and the University of Missouri, his last job was at the New School for Social Research. He never rose above the rank of assistant professor. Veblen spent time as an editor of the liberal periodical *The Dial* and worked for the Food Administration during World War I. While there, he suggested that prosecution of the Industrial Workers of the World, a radical labor union, cease to help with food harvesting. This suggestion was not well received by the vested interests.

Veblen's most famous work was *The Theory of the Leisure Class*. In this work, he discussed things such as dress as an expression of the pecuniary culture, pecuniary canons of taste, devout observances, and higher learning. His second book, *The Theory of Business Enterprise*, was more to the point in the analysis of modern-day capitalism. In this book, he analyzed the role of loan credit in the boom-bust cycle of the economy.

Veblen's fundamental criticism of orthodox economics was that it was pre-Darwinian and hence did not have an evolutionary view of society. Understanding the evolution of institutions and the dynamic role of technological change (in its broadest sense) was essential in making economics evolutionary. Veblen's influence remains today in the economics profession through the Association for Evolutionary Economics, founded by some of his followers in 1967.

—Ronnie J. Phillips

See also Capitalism; Conspicuous Consumption; Cultural Imperialism; Darwinism and Ethics; Economics, Behavioral; Industrial Revolution; Instrumental Value; Marginal Utility; Market Bubbles; Marx, Karl; Marxism; Meaningful Work; Political Economy; Protestant Work Ethic

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Vice

A vice is a serious moral flaw in a person's character. Thus, vices are not trivial personal failings, or minor personality defects, or occasional lapses in behavior, but enduring traits that cause people repeatedly to act in morally deplorable ways. Examples of vice include intemperance, ungratefulness, dishonesty, cowardice, disloyalty, greed, unfairness, and malice.

Yet if vices are serious flaws, and so, one would think, to be avoided if at all possible, why does vice seem so common? One possibility is that vice is a part of human nature. We are, regrettably, morally flawed beings, and though we may resist, in the end vice is an inevitable part of human behavior. It is just a part of who we are.

Although this possibility has the apparent advantage of explaining the prevalence of vice, it suffers from the disadvantage of having no ready account of the presence of virtue. Vice may be common, but so is moral virtue. We often see acts of kindness, courage, generosity, and so on, and for the most part such acts do not require resistance to an underlying tendency toward vice but are instead undertaken willingly, as expressions of the true character of the person who does them. Should we say, then, that both vice and virtue are parts of human nature?

At first glance this may seem right. Were it not, vice and virtue in human behavior would be something of a mystery. On closer inspection, however, it is an empty explanation. It tells us nothing about why some people are virtuous and others vicious, or about how these traits arise from some alleged underlying common human nature, or about how some people are able to change their vices to virtues while others fail. For a better explanation we need to turn to Aristotle, who gave one of the first, and one of the best, accounts of vice and virtue.

Vice as a Lack of Knowledge

Aristotle discussed vice in the context of his lengthy analysis of virtue. Briefly, Aristotle argued that virtue is developed through proper education and practice. For example, people learn to be honest by being taught to behave honestly and by imitating the behavior of honest people. Thus, for Aristotle, a person with vices was uneducated, or had received an incomplete education, in morally correct behavior. Hence, vice is a form of ignorance, and people with vices act as they do because they know no better.

People ignorant of virtue, and so susceptible to vice, do not have a kind of practical knowledge that shows itself in two ways. First, a person might not know how to behave in morally fitting ways in specific contexts. Thus, the person lacks the moral virtue appropriate for that context. Second, and more generally, a person might not know how to read contexts and pick the right behavior for each context. Using Aristotelian terminology, the person in the second case lacks a specific intellectual virtue that is a precondition for the exercise of moral virtues—*phronesis*, or practical wisdom. *Phronesis* is akin to "good sense."

As an example of the first kind of ignorance, consider a situation that requires courageous behavior. Suppose that acting courageously implies understanding the true extent of danger in the situation, having a degree of fear that is appropriate to that danger, and acting to achieve a goal in a way that fully recognizes the danger present and the fear the person feels. Aristotle argued that related to the virtue of courage are two vices: rashness and cowardice. The rash person underestimates the danger present and so has too little fear. Consequently, he tends to be overconfident and to overreact, to go beyond what is prudent or reasonable in the circumstances. The coward overestimates the danger and so has too much fear. Hence, he lacks confidence and does not do enough to accomplish the goal. What the rash person and the coward have in common is inadequate or incomplete knowledge. Neither of them knows the real extent of danger, so neither feels the appropriate amount of fear. Thus, unlike the courageous person, neither of them responds correctly.

Aristotle repeats this kind of analysis for other virtues and the vices associated with virtues. In each case, virtue is displayed by the person who acts optimally in a particular context, given what the context is about and what it requires as a response. Responses that deviate from the optimal point are instances of vice that display excess (e.g., too much fear) or deficiency (e.g., too little fear) relative to the right and virtuous response in a particular context. In each case, virtue depends on knowledge of the situation, while vice demonstrates a lack of knowledge.

In the second kind of ignorance—an absence of what Aristotle called *phronesis*—a person lacks virtue if he does not understand what the situation is about and what it demands. In this case, the person gets neither the situation nor the response right. Someone like this displays a more fundamental want of knowledge. Not only can he not ascertain, for example, the right amount of fear; he cannot even figure out that this is an instance in which fear is the determining variable and courage the correct response. A person without this kind of knowledge might think that the situation requires benevolence, or magnanimity, or trust, or some other virtue, or the person might simply have no idea whatsoever of what the situation is about and what it might require of him.

People lacking *phronesis* are cognitively deficient in a specific way, either by nature or by nurture. If by nature, they are the type of persons who accumulate experiences but somehow do not acquire the knowledge and insight usually associated with experience. Thus, they may never develop practical wisdom. On the other hand, if it is by nurture, the cognitive deficiency indicates that they have received no training or that they have received training that was incomplete or ineffective.

It must be noted that even though, analytically speaking, *phronesis* is a precondition to the exercise of the moral virtues, functionally speaking, the intellectual virtue of *phronesis* and the moral virtues together form a unity whose function and development is dialectically linked. Each occurs with the other, and one cannot occur without the other.

Vice and Weakness of Will

A problem with Aristotle's understanding of vice and virtue, one he discussed himself, is that even if education is necessary for virtue, it is not always sufficient. People educated in virtue can still fail to act virtuously because, to put it simply, knowing what is virtuous does not automatically lead to virtuous behavior. There are big gaps between (1) knowing that x is the virtuous thing to do, (2) knowing how to do x, and (3) doing x. With regard to virtue, it is the kind of gap that occurs when one says to oneself or others, "I know what I should do. I know how to do it. I just do not seem to be able to do it."

Aristotle argued that not doing the virtuous thing when one knows the virtuous thing to do is not quite the same as vice because vice implies ignorance of virtue. Instead, the difficulty is a failure of will—a weakness of will. Fundamentally, it boils down to the fact that the rational will—the wish to do good—is weaker than some desire arising independently of reason. Persons exhibiting this behavior are of one mind but not of one heart. What they lack is self-mastery over their nonrationally generated desires—the capacity to make their rational willing sovereign over all other willing. They may behave in ways that are indistinguishable from those with genuine vices, but the source of their conduct is a weak will, not ignorance.

Here again the problem is due to nature or nurture. By nature, some people might have too strong nonrational desires or too weak a rational will to ever be able to achieve rational self-mastery and, consequently, harmony within themselves. Thus, they are doomed to be conflicted slaves of their nonrational desires. Other people might be able to achieve considerably higher levels of rational self-mastery and inner harmony through self-discipline and training. And some people, by nature, have an extremely strong rational will and thus require little or no training in self-mastery. Most people, however, lie somewhere between the unfortunate slave of his or her appetites and the natural master of himself or herself.

Vice as a Perversion of Knowledge

A different sort of vice is exhibited by people who know what is virtuous, know how to do it, could do it, but nonetheless deliberately choose not to do it. This is the vice of malevolence, or even evil: a conscious, rational, well-orchestrated effort at doing bad. In its most extreme form, malevolence itself becomes the ultimate goal for these people. They have deep insight into the psychological and moral dimensions of the human condition and a high degree of self-mastery, but they invest all that knowledge and power of rational will in a project of immoral behavior, in an attempt to instantiate a complete inversion of the moral universe. In literature, Milton's Satan is a prime example of this kind of vice, but long and bitter human experience shows that there are real people with vices so similar to Satan's that the differences hardly matter.

Vice as Emotional Deficiency

Last, two other vices worth exploring are brutishness and cruelty. These vices are characterized not so much by a lack of knowledge as by a lack of appropriate emotions, or a distortion of appropriate emotions.

Brutishness is an absence of sympathy, a lack of consciousness of other people as creatures of feeling, and a lack of access to their feelings. This lack of feeling for others is an emotional inadequacy, a moral dullness, that can be caused by nature, such as color blindness, or by nurture, such as a lack of aesthetic sensibility due to an upbringing devoid of beauty. When it is caused by nature, people with this incapacity are doomed to stay at a premoral level. They never achieve the emotional sensitivity necessary for moral life. When the lack is caused by nurture, however, training might lead to considerably higher levels of moral sensibility. This latter case has been characterized in literature as the Pygmalion type.

Cruelty is an inversion of the normal human response to the pain of others. Cruel people are conscious of others as creatures of feeling and have access to their feeling. What they do not have is a capacity to get pleasure from someone else's pleasure, like normal people do. Instead, they obtain pleasure from the emotional or physical pain of others. Unlike the brutish person, who is fundamentally insensitive and indifferent to the pain of others, the cruel person is sensitive to others and guiltlessly enjoys deriving pleasure from their pain. Again, cruelty can be the product of nature or nurture. When it is by nature, the person might have very little chance of reform. When it is by nurture, there might be a possibility of improvement through a retraining of their habitual responses to pleasure and pain in others. The classic example of this comes from the psychotherapy of abuse, where it is assumed that most abusers were themselves abused as children and through therapy can come to terms with their abuse and so end the cycle of abuse.

Vice in Business

Every few decades there seems to be an outbreak of bad behavior in business, almost an epidemic of vice. The most recent, exemplified in companies such as Enron and WorldCom, appears to be motivated by the vice of insatiable greed and enabled by other vices such as dishonesty and arrogance. In response, legislation has been passed—for example, the Sarbanes-Oxley Act—corporate codes of conduct have been dusted off and posted in prominent places, and many companies have followed Aristotle's advice and begun ethics-training programs. Whether these efforts will be successful remains to be seen. The pessimist points to human history and argues that, although vice in business may be suppressed for a time, it can never be eliminated, especially when powerful corporate executives have easy access to seemingly endless amounts of money. The optimist, on the other hand, denies that vice is an inherent part of a universal human nature and argues that it is largely a consequence of how we are raised and educated.

If the optimist is right, if education in virtue improves, vice in business will gradually diminish, even in the face of obstacles such as weakness of will. If the pessimist is right, education will at best keep vice at bay, but will never be able to eradicate it.

—Ivan Marquez and Robert Frederick

See also Aristotle; Corruption; Ethics Training Programs; Mandeville, Bernard; Scandals, Corporate; Self-Deception; Virtue; Virtue Ethics

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Violence in the Workplace

Workplace violence is one of the most important security issues faced by companies today, as these activities span a lengthy continuum from coworker bullying and intimidation to verbal threats to homicide. According to the Occupational Safety and Health Administration (OSHA), approximately 1.5 million workers are assaulted and more than 500 people are murdered in the workplace every year in the United States. Despite the dramatic headlines that accompany workplace fatalities, they represented only 0.1% of all violent work incidents in the 1990s. More than three quarters of the incidents involved simple assaults, which are typically attempts to commit an injury or acts that place another in fear of receiving a violent injury.

The U.S. Department of Justice identifies four types of workplace violence, including (1) violent acts by criminals who have no other connection with the workplace but enter to commit robbery or another crime; (2) violence directed at employees by customers, clients, patients, students, inmates, or any others for whom an organization provides services; (3) violence against coworkers, supervisors, or managers by a present or former employee; and (4) violence committed in the workplace by someone who doesn't work there but has a personal relationship with an employee.

Taxi drivers and clerks working late-night shifts at convenience stores are often subject to the first type of violence. These employees may be injured or further harmed when confronted by criminal activity on the job. The first type of violence is more prevalent in industries where employees work alone or at night, are extensively involved with the public, are located in dangerous neighborhoods, carry or have access to cash, and have a greater likelihood of coming into contact with criminals. Approximately 80% of workplace homicides are the result of this type of violence.

Airline attendants are increasingly experiencing the second category of workplace violence when passengers become unruly, drunk, or otherwise violent while in flight. Airline employees across the United States, Australia, and Switzerland staged a campaign to combat "air rage," the uncivil and dangerous acts of passengers that are not only punishable by large fines but can also threaten the safety of everyone aboard the aircraft. Health care workers are also subject to high rates of workplace violence, with nurses the most frequent target of assaults by patients or a patient's friends or family. Emergency rooms, psychiatric wards, acute care facilities, and crisis units are especially dangerous.

Third, disagreements and stress in the workplace may escalate into employee-on-employee violence. For example, a Xerox Corporation warehouse employee opened fire during a team meeting at a facility in Honolulu, killing seven coworkers. The employee was eventually convicted of murder and sentenced to life in prison without parole for the shooting, which was described as the worst tragedy in the company's history. The Hawaii Occupational Safety and Health Division later cited Xerox for failing to enforce workplace violence policies that might have prevented the deaths. In many of these cases, the perpetrator has been recently reprimanded, dismissed, or given other negative feedback that prompted the violent attack.

Finally, some violence in the workplace is the result of domestic disturbances or stalking behaviors.

In these situations, an employee is confronted at work by someone whom he or she knows, such as an abusive spouse or domestic partner. This partner may be highly jealous, fearful, emotionally unstable, fueled by drugs or alcohol, or unable to accept a divorce or the end of a relationship.

Although the U.S. federal government has not issued formal regulations on workplace violence, there are several general statutes and OSHA directives to provide guidance. All employers are subject to the General Duty Clause that requires employers to provide a place of employment free from recognized hazards that cause or are likely to cause death or serious physical harm to employees. To violate this clause, four elements must be present: (1) The employer failed to keep his workplace free of a "hazard," (2) the hazard was "recognized" either by the cited employer individually or by the employer's industry generally, (3) the recognized hazard was causing or was likely to cause death or serious physical harm, and (4) there was a feasible means available that would have eliminated or materially reduced the hazard. OSHA officials have also noted that some workplace violence is the result of random and haphazard events that could not have been foreseen or predicted by management.

In addition to this general duty, OSHA has rules that employers must follow in reporting workplace injuries and illnesses, which could include episodes or the results of violence. OSHA has also issued best practices and educational information for industries where trends and operating conditions seem to increase the risk of violence. For example, best practices for night retail establishments and for social service and health care employers are available. The U.S. Department of Justice has also convened conferences and issued reports for the purpose of curbing workplace violence.

Violence in the workplace became a more prominent issue with the September 11, 2001, terrorist attacks. Until these events, workplace violence was primarily considered in the context of disgruntled employees, dissatisfied customers, and domestic disturbances that moved into the workplace. Today, workplace violence is understood and managed from both an internal and external perspective. Although workplace crimes are often a reflection of general problems in society, employers have a responsibility to be proactive. Specifically, an organization should assess its unique risks, develop a workplace violence policy, implement a prevention program, provide security and monitoring devices, use training to reinforce workplace standards, seek outside assistance from law enforcement, social service agencies, and other groups when necessary, and install safeguards to protect employees and stakeholders from such acts. Companies should also purchase insurance policies to cover the costs of workplace violence, including business interruption, psychological counseling, informant rewards, and medical claims related to injuries.

—Debbie M. Thorne

See also Employee Monitoring and Surveillance; Employee Protection and Workplace Safety Legislation; Occupational Safety and Health Administration (OSHA)

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VIRTUAL CORPORATION

Virtual companies or corporations are networked businesses characterized by the linking of people and business partners via electronic information and communication systems. Increased globalization, coupled with the widespread application of various technologies, has led to shifts in organizational structures and operating methods. These changes in business strategy have given rise to the innovative notion of the virtual organization, while raising some ethical concerns. As exemplified by such companies as eBay and Dell, Inc., this concept is now considered a standard business model.

During the mid-1990s, when dot-com businesses were flourishing, the virtual organization was understood as a business venture that produced a product or provided a service by electronically networking disparate employees and/or organizations. One individual or core team oversaw the company, often working out of a home or a small office. Usually, there was no single business location or product inventory held by the company. Though the core constituents, workforce, suppliers, manufacturing units, and marketing services that composed the company were geographically dispersed, the company was perceived by customers as a single entity with an actual location. Later, this business approach was expanded and became a business principle promoting the operational and economic value of internal organizational networks and external business partnerships. The application of this principle is best exemplified by the notion of the virtual company or corporation.

Virtual in this case does not mean pseudo or temporary. It refers to a company's intrinsic sociotechnical and dispersed nature; that is, its weaving together of discrete human resources and technology into a unified system, as well as its reliance on the Internet and computer-based systems for information sharing, communication, and interactive networking. Vital work relationships and business partnerships form and dissolve as needed, enabling work activities to be accomplished regardless of where employees reside and businesses are located.

Many medium to large businesses function in a global arena, drawing on a worldwide workforce. Such companies are dispersed organizations neither confined by traditional organizational boundaries nor limited by time and distance. Though usually having a central or home office location, a core management team, and full-time employees, they partner with external constituents to provide functions and services that once were part of a company's internal operations. In essence, they are virtual corporations, enterprises that are a structured system of business components operating in different locations characterized by a web of in-house work relationships and contracted partnerships with external businesses. Many employees are teleworkers because they are not confined to doing work on-site or collaborating with coworkers who reside nearby. Teams are often virtual, being composed of globally dispersed members who collaborate and are managed via technology. The organization is understood as the sum total of all the networked components—internal and external.

There are different types of virtual corporations. Some are consortiums of businesses where each constituent contributes equal resources, practical knowledge, professional expertise, and so on, while others are an e-marketplace where several companies collaborate in promoting and distributing various goods or services. Others consist of a core company strategically aligned with satellite organizations. Still others are a group of companies that form a single, coordinated value or supply chain that services customers. Central to each of these corporations is the electronic networking of business units, work teams, production components, suppliers, service providers, logistics companies, customer service staff, and so on, that are dispersed nationally or worldwide.

These organizational networks are established and supported by various forms of information and communication technologies, particularly enterprise resource planning systems, intranets, extranets, e-mail, knowledge and content management systems, collaborative meeting platforms, and supply chain management systems. High-speed or real-time digital systems enable information to be rapidly shared, project teams to be composed of the best talent, work activities to be coordinated and completed in a timely fashion, materials to be delivered in a just-in-time fashion, and customers to be served in a customized manner.

Such corporations handle large volumes of information, relying heavily on electronic forms for its transmission, processing, and storage. The glut of information has become overwhelming, at times hindering productivity and creating debilitating workplace stress. The utilizing and processing of proprietary information, as well as sensitive business and customer data, requires attention to data quality and security. Therefore, it is important that corporations have procedures in place that ensure that data is accurate and that customer or client information is secure from hackers and identity thieves.

The virtual workplace is often described as a 24/7 work environment. Reasons include the significant amount of work time required to deploy business strategies and meet economic goals, increased workload due to limited human resources, and the continuous availability needed to lead or participate in projects. Continuous workplace connectivity, and the stressfulness of working across cultures and time zones, has become a concern because of its impact on employee well-being. The 24/7 virtual work environment has blurred the line between personal and work time and is more impersonal due to the lessened social contact. Staff members often work long hours, and managers routinely take work home or work weekends. Many employees are not taking sick days or vacation time due to heavy workloads and the pressures of processing information. Some employees are beginning to feel that work is dehumanizing and less meaningful.

Last, virtual corporations strive to be agile, fast-paced organizations that readily respond to market shifts and retain competitive advantage, while operating in an efficient, cost-effective manner. This motivates them to seek out the most talented human resources wherever they exist, outsource business functions that are not their core competency, and take advantage of the cost reduction of operating company components in foreign countries. Outsourcing efforts have created anxiety among U.S. workers regarding job security, while offshoring practices, the relocating of production or services overseas, has caused them to question the availability of enough future U.S. employment opportunities. These practices have also raised concern about the exploitation of foreign workers who are willing to work for low wages and in sweatshop-like conditions.

For these reasons, it is important for virtual corporations to be conscious of the work ethic their culture fosters, ensuring that organizational practices fairly compensate employees and respect cultural differences, managers and project leaders have reasonable work expectations, and employees are enabled to effectively handle the information glut, reduce work stress, and maintain a balanced work life.

—Charles F. Piazza

See also Downsizing; Globalization; Networking; Outsourcing

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VIRTUE

The Latin word *virtus* means strength, power. It is the translation of the Greek word *areté*. Broadly speaking, virtue is the excellence or perfection of any being. It is the good and settled disposition of anything appropriate to itself. Every virtue or excellence both brings into good condition the thing of which it is the excellence and causes the work of that thing to be done well. More specifically, virtue applies to people and designates those habits that facilitate good actions. Virtue may refer to a person, a character, a habit, an action, or a tendency.

Virtues and Business

Business ethics relates the concept of virtues to business activities. Sherwin Klein proposes the application of Platonic cardinal virtues to business. Robert Solomon bears an Aristotelian approach to business. In an Aristotelian vein, businesses are a part of the Aristotelian good life, and a business organization is a community, or *polis.* Thus, it is coherent to apply Aristotelian virtues to business. Solomon proposes six essential parameters that circumscribe and define virtues in business ethics. These are (1) community (goals are not only personal but also common), (2) the search for excellence, (3) membership (we define our character within community), (4) integrity (virtues work together to shape a coherent character), (5) judgment (the relevance of prudence in business), and (6) holism (that overcomes the dialectic stakeholders–stockholders). Corporate life within this frame is determined by the character of its members. If we want a good corporation, one that functions well, we need virtues that shape a good character. Aristotelian virtues applicable to business include courage, temperance, friendliness, liberality, magnificence, honesty, fairness, trustworthiness, toughness, justice, honor, loyalty, fidelity, sincerity, reliability, cooperativeness, tactfulness, reasonableness, and openness. If these virtues are practiced, businesses will necessarily work well.

Greek Conception of Virtue

Virtue was a relevant concept for the Greeks. For them, virtue applied to everything; primarily, however, it referred to human beings. It was used to express a quality, an ability, excellence, honor, and nobility. The Greek ideal was a virtuous human being. The Greek *paideia* (education) was the creation of virtuous habits. Courage, moderation, justice, and prudence were highly esteemed virtues for them.

Consequently, early Greek philosophers dealt with virtue. Socrates is widely known for his intellectualism, that is, the idea that nobody acts badly knowingly. According to Socrates, a bad action stems from wrong knowledge. Thus, for Socrates, virtue is mainly intellectual. According to him, virtue is the most appreciated good for humans. His behavior concerning justice is very well known through Plato's *Apology of Socrates:* He prefers to accept being unfairly sentenced to death rather than committing injustice. Plato presents the four main virtues related to the city and the soul: practical wisdom, courage, moderation, and justice. For Plato, the aim of education is virtue.

Aristotle's *Nicomachean Ethics* is a treatise on virtues, where practical wisdom, justice, and friendship occupy a privileged place. According to Aristotle, the virtue of a good eye is to make us see well, and the virtue of a horse is to be good in itself and to win horse races, be useful to riders, and so on. When applied to human beings, virtue is the state of character that makes humans good and do their work well. Human beings have a calling or a task to do, the vital development of their very being. Their excellence or virtue lies in doing this. Happiness, a self-fulfilling activity, consists in a life of virtues. Virtues are the means for happiness.

Nature and Necessity of Virtue

Aquinas defines virtue as a good operative habit. Habits are lasting dispositions. Habits and dispositions are qualities, a way of being of things. Habits are stable in that they are something we have and that we do not lose easily. Virtues are qualities of our faculties: intelligence, will, and passions. They are operative in that they help the capacity to act. They are good in that they help us to act in a right way. They are also good in a broader sense than the moral one. They improve human faculties, enabling people to act according to their very nature. Thanks to virtues, human beings act easily, quickly, pleasantly, and naturally in the right way. Life runs fast and we do not have time to decide or to consider the best process of knowledge in each case. It would be psychologically unbearable to spend the whole day deliberating. We need some habits that facilitate rather automatic reactions. If we want these reactions to be right, we need virtues. In sum, virtues are the excellence of everything and they facilitate the corresponding way of acting of everything, especially human beings.

Intellectual Virtues

Aristotle distinguishes two kinds of virtues, intellectual and moral. The former help the intelligence achieve its goals and the latter help the will to intend what it ought to want. Intellectual virtues grant the intelligence the facility of performing its acts rightly—that is, to achieve truth, in the case of theoretical intellect, and to direct human free actions toward practical truth, in the case of practical intellect.

According to Aristotle there are five virtues: (1) intuitive reason, (2) philosophical wisdom, (3) scientific knowledge, (4) practical wisdom, and (5) art. Intuitive reason is the habit that facilitates the knowledge of the principles from which science proceeds. Philosophical wisdom is an intuitive and scientific knowledge of the highest objects. Scientific knowledge is the habit of deductive reasoning beginning with some given principles. Practical wisdom (or prudence) is the habit of doing well. Art (or technique) is the habit of producing well. Equipped with this constellation of virtues, people can more easily achieve one of their defining natural ends: to know. People need knowledge for theoretical and practical aims. The first three intellectual virtues give support to theoretical knowledge, and the last two (prudence and technique) assist practical knowledge.

Moral Virtues

Moral virtues facilitate the good acts of the will and passions so far as they are ruled by the will and the intelligence. Aristotle considers virtue as a state of character concerned with choice, lying on a mean, that is, the mean relative to us, this being determined by a rational principle. The word *choice* means that the main act of moral virtue is the right decision: The decision to do here and now what is needed for a good conduct. This right decision presupposes a good discernment on means and ways of acting. This is the role of practical wisdom. "Choice" also indicates that the good action is wanted and elected in itself: Intention matters. Virtues facilitate good acts without annulling freedom; on the contrary, they presuppose a constant free conduct.

The most important moral virtues are called "cardinal" (from the Latin *cardo*, "hinge") because all the other good habits hinge on them. They are practical wisdom or prudence, justice, temperance, and fortitude. Prudence is the guide of other virtues. Justice rules social order. Fortitude and temperance harmonize the person's inner order, as he or she is affected by the dictates of the will and passions. Thanks to prudence, human beings can know and judge what they should do. The function of prudence is to apply right reason to action, and this requires a right will. Hence, prudence is not only an intellectual virtue but also a moral virtue. The acts of prudence are three. The first is to take counsel. The second act is to judge. The third act is to command: to apply to action the things counseled and judged. Experience, memory, acuteness, intuition, and caution are other habits related with prudence.

Traditionally, commutative and distributive forms of justice are distinguished from one another. The task of virtue is to make a person good, and to bring his or her actions into line with reason. For Aquinas, this happens in three ways: first, rectifying reason itself, and this belongs to intellectual virtues; second, setting the rectitude of reason in human affairs, and this is done by justice; and third, removing the obstacles to the establishment of this rectitude in human affairs, and this is the task of fortitude.

Temperance helps sustain certain moderation that reason points out as ordered to human actions. Human pleasures are not bad in themselves, but people may long for them in a disordered way. Temperance guides passions to obey reason and will and directs them toward good. The word *fortitude* comes from the Latin word *fortis*, which means strength. Fortitude is the virtue that strengthens people to do good constantly and patiently despite difficulties that may arise. Fortitude is a condition to be prudent, temperate, and just, because whoever wants to act correctly will be confronted with difficulties. There are other moral virtues among the cardinal virtues: They constitute an exhaustive system.

Characteristics of Moral Virtues

Acquisition of Moral Virtues

How do we acquire moral virtues? Aristotle thinks that we are equipped by nature with the ability to receive virtues and that habits bring this ability to completion and fulfillment. He wrote that virtues are good habits, and these are firmly fixed possessions. The way of fixing habits is by repeating the corresponding actions. Thus, people acquire virtues through practice. In his *Nicomachean Ethics,* Aristotle argues that the main methods to foster these practices are education and law. First, education, in the broad Greek sense of *paideia,* shapes personal character. This is the reason why Aristotle says that it is not a small question whether one habit or another is inculcated in us from early childhood. Second, laws have a pedagogical objective. According to Aristotle, a set of concrete virtues leads humans to their natural excellence; this process of virtue building begins with education and is consolidated through laws.

A Mean

Virtue, for Aristotle, is a mean between two vices: one of excess and the other of defect. Aristotle points out that not every action admits a mean: Some have names that already imply badness, such as adultery, theft, and murder. Virtue is not the mean as the middle of a line but as the top of an arch. Aristotle defines virtue as a state of character concerned with choice, lying on a mean relative to us. Practical wisdom is the virtue that determines in each case the point where the virtuous mean lies.

Connection

Virtues are not isolated. They are part of a system, connected to each other through prudence. For Aristotle, the work of prudence is personal, essentially free and variable according to circumstances. What is prudent for one person may not be so for another. The coordination of free prudent actions leads to social coordination. Human beings cannot flourish in isolation. Our fulfillment demands a life with others. Prudence is the axis of connection among the virtues.

Virtue Ethics

Virtue ethics is currently one of the most widespread ethical theories. Deontological ethics focuses on duties, consequentialism on consequences, and virtue ethics on virtues and personal character. Some authors maintain that virtue ethics is unilateral because of its emphasis on the subjective aspect of the ethical relation (an "agent-centered" ethics). However, the Aristotelian virtue ethics also considers the goodness of the act itself and its consequences.

—Ricardo F. Crespo

See also Aristotle; Integrity; Justice, Theories of; Loyalty; MacIntyre, Alasdair; Virtue and Leadership; Virtue Ethics

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Virtue and Leadership

Virtue as Excellence of Character

Virtue is excellence of character, the possession of habits appropriate for a human being within a particular sociocultural context. Used as a synonym of "integrity," virtue suggests wholeness and stability in a person. Virtue is a form of capital, moral capital, because it is a productive capacity that accumulates and develops through investments of time and effort. Virtue is unique because it perfects the human being as a whole and not just in a limited aspect. It may not make a person strong, smart, or successful, but it makes him good as a human being.

Excellence of character depends on cultivating the right habits. Aristotle explains that virtuous habits result from the repetition of virtuous actions, and virtuous actions spring from the nurture of suitable inclinations in accordance with one's nature. There is a feedback mechanism among character, habits, and actions. Actions arise from a person's inclinations, yet actions may also weaken or reinforce inclinations. Similarly, not only do habits forge character; character likewise predisposes or disengages a person from certain habits. Let us now consider the three main analogues of virtue: actions, habits, and character.

Actions that arise from a person's inclinations are the building blocks of moral life. Virtue lies in good voluntary actions, and its goodness springs from three sources: the object or the action itself, the agent's end or intention, and the circumstances in which the act is carried out. The object refers to what the agent does as a humanly meaningful whole and not the mere series of movements he or she goes through: homicide and not simply aiming a gun and pulling the trigger, for example. The object principally determines whether an action is good or evil. Certain actions are evil by their very object and are prohibited without exception: lying, theft, murder, and so forth.

The second criterion examines the agent's intention, whether it is oriented toward his final end. At times, an action choiceworthy in its object becomes ethically flawed due to the agent's intention. To be virtuous, an action has to be performed with a noble end. For instance, it is not enough to give alms; one should also wish to help the poor rather than do it merely for show.

Finally, we have the circumstances surrounding actions. Seemingly "favorable" circumstances cannot change the moral quality of an action from evil to good. For example, no act of torture could be justified even if the fate of a hundred people depended on it. Circumstances affect the degree to which actions are good or evil, making them better or worse.

Every voluntary act leaves a trace in the agent. This by-product is called "habit": a stable disposition or manner of being and doing. Habits vest human nature with a new, improved, and reinforced tendency, a "second nature." After good actions, good habits are the next analogue of virtue.

As habits, virtues and vices arise from the repetition of actions. But not any sort of action, for good actions alone produce virtues. First, to acquire proper habits, actions should express correct reason in practice, as expert doctors or navigators know in each particular case. Second, right habituation equally shuns excess and defect, and third, proper habits come from experiencing appropriate pleasure or pain. For example, a generous person is not only one who normally gives alms but also one who is happy in doing so.

Character describes an individual's personality. It results from the combination of different habits that a person develops. How do we acquire virtue of character? Since it lies in the mean, Aristotle admonishes us to avoid the more opposed extreme. Regarding courage, for example, it would be better to err on the side of rashness than on cowardice, the more contrary extreme. Second, one should avoid the easier extreme depending on one's natural drift. Aristotle also warns that we be careful with pleasures, to which we are already favorably biased. Finally, Aristotle tells us that the rules do not give exact and detailed guidance for action. Virtues of character deal with concrete, contingent actions and feelings beyond the scope of general, theoretical accounts. We are remitted, in the end, to the perception of an already virtuous person who alone is the competent judge in concrete situations.

Leadership as a Character Trait

Joseph Rost defines leadership as an influence relationship that brings about changes reflecting the mutual purposes of leaders and followers. He is right in characterizing leadership as a reciprocal relationship and in affirming that goals have to be agreed on voluntarily by leader and followers. Leadership does not develop merely as the result of pressure or coercion. Its converse, followership, has to spring naturally from the minds and hearts of people who feel respected and valued. Leadership thus becomes a moral relationship based on trust, obligation, commitment, emotion, and a common vision of the good.

Leadership consists in exerting moral influence. A leader earns authority and legitimacy when he seeks the good of followers. Moral influence, in turn, could be understood in a double direction. First, followers demand moral behavior—honesty, integrity, credibility, and trustworthiness—from leaders. Second, leaders shape the choices of their followers, promoting their personal growth. As the leadership theorist James MacGregor Burns commented, leadership is a two-way transformative and intrinsically moral relationship between leader and followers. Thus, leadership becomes a major driving force for people and organizations to become ethical.

Stewardship and servant-leadership stem from this assumption. According to the organizational consultant Peter Block, stewardship underscores a leader's accountability to the organization and its workers. A steward-leader recognizes the power of workers to make decisions and to influence the organization's goals, systems, and structures. He empowers workers so that they can become leaders themselves. For the management theorist Robert Greenleaf, servant-leadership is even more revolutionary in that it shuns high-profile figures. A servant-leader commits himself or herself in the first place to serve the interests of others, providing them with a chance to grow and develop, materially and morally. The integral fulfillment of everyone in the organization is his aim.

Many construe ethical leadership as an emotional relationship based on charisma, that mysterious power possessed by people who are good at influencing others. As a nonrational characteristic, charisma is difficult to define. It has to do with a leader's message, how he says it, and the whole gamut of emotions he evokes. Charm, intelligence, and sincerity also contribute. For this reason, the business and philosophy scholar Robert Solomon opines that charisma is more of a distraction than a help.

In place of charisma, Solomon proposes trust as the basis of ethical leadership. An ethical leader establishes and sustains a framework of trust between himself or herself and followers. Without trust, no dialogue, understanding, cooperation, commerce, or community would be possible. Furthermore, trust lowers transaction costs, facilitates entrepreneurial initiatives, and boosts economic competitiveness. But what is the source of trust? It is none other than virtue.

Rhetoric as the Art of Virtue-Based Leadership

The art of leadership is what was known in the classical world as rhetoric. Aristotle defines rhetoric as an ability, in each case, to see the available means of persuasion. Barring force, the only instrument available to the potential leader is reason. A leader has to persuade his audience through words. However, words alone do not move; they require the complicity of feelings and emotions.

Today, as in Aristotle's time, there are people with a gift for persuasion and others who seem bereft of it. Nevertheless, both types stand to gain by studying the principles of speech and composition. Aristotle was aware of the controversy surrounding rhetoric. Socrates and Plato both thought that Sophist rhetoric was mere flattery, the use of empty words and misleading arguments to one's advantage, an appeal to emotions without regard for truth. In contrast, Plato's ideal rhetorician in the *Phaedrus* was a virtuous person with firm knowledge: rhetoric-wedded persuasive skills with personal virtue and a love of truth.

Aristotle held that rhetoric as a communication art was morally neutral; it could be used for good or evil. He was careful, however, not to separate rhetoric from ethics; rather, he insisted on its subordination to the architectonic discipline of politics. Aristotle argues that the study of rhetoric is useful for three main reasons. First, without rhetoric, the truth can be easily defeated, for true knowledge may not be enough to persuade audiences reliant on feelings and opinions. Second, rhetoric helps the speaker understand an issue by giving him a chance to consider both sides. And third, rhetoric permits one to defend himself without recourse to violence.

According to Aristotle, three instruments are available to the speaker or leader in persuading his followers: the speech or argument itself (*logos*), the speaker's character (*ethos*), and his listeners' emotional disposition (*pathos*). Speech persuades when it shows the truth in a particular case. The truth, however, may prove insufficient for those unable to follow complicated reasoning and dependent on hearsay. Yet this does not mean that true reasoning has to be abandoned. Persuasion also occurs when the public is led by speech to experience appropriate emotions. These emotions become the triggers of action. Those who hold a purely technical view of rhetoric focus exclusively on listeners' emotions. Yet it is also relevant to consider to whom a particular emotion is directed and for what purpose. Insofar as human judgment is affected by emotions, it is not an entirely rational act, but neither should the influence of emotions be exaggerated. Aristotle considers the character of the speaker as the controlling factor in persuasion, because we believe fair-minded people to a greater extent and more quickly. Listeners are convinced mainly by the image of trustworthiness that a speaker or leader projects. And what better way to ensure an image of trustworthiness than by being trustworthy in fact?

Aristotle lists three personal qualities that an aspiring leader should possess: practical wisdom (*phronesis*), virtue (*areté*), and goodwill (*eunoia*). Practical wisdom permits one to form correct opinions over concrete, contingent issues; virtue prods him to express his views justly and fairly; and goodwill ensures that he give the best advice. A person with these characteristics becomes not only a persuasive speaker but an effective leader also.

Whatever a leader's purpose, it would be helpful to learn to present one's arguments well and thus elicit the audience's sympathy. For this, one must turn to rhetoric. But these techniques alone would not work if one lacked virtue, and hence the need for ethics.

—Alejo José G. Sison

See also Aristotle; Ethics of Persuasion; Integrity; Leadership; Moral Leadership; Servant Leadership; Virtue; Virtue Ethics

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Virtue Ethics

Virtue is a condition of a person's character. Having virtue makes doing the right thing the obvious choice among options. Having virtue means that immoral courses of action are ruled out, and this quickens decision making. Virtuous persons would have already determined that they ought to do only whatever is right in a situation. If a person has virtue, this means that he or she does not merely have good intentions but has the ability to act on them. People who manage to be consistently ethical are likely to have virtue to some degree. Those who knowingly act immorally lack virtue. And those who cannot tell the difference between wrong and right lack virtue.

Whether virtue is a set of qualities or just one; whether virtue is a permanent state of character or a temporary condition; whether virtue is the result of a conscious or unconscious process of development, inborn or merely a matter of culture—these are matters for the various authors of virtue ethics to determine. Authors must also decide how virtue relates to an account of right action. Either a description of virtue serves as an addendum to other ethical approaches, and the moral psychology required for virtue is not invoked in a determination of right and wrong, or the requirements of virtue alone determine what right action is. Virtue ethics may be more or less theoretical. The more theoretical accounts revise our commonsense opinions on good character. The less theoretical accounts endorse commonsense notions. Though every contemporary account of virtue derives some inspiration from the ancient accounts, most contemporary accounts are less theoretical than these and more dependent on the criteria of ethics and justice offered by alternative approaches.

There are particular challenges to determining the morality of business decisions and policies with an account of virtue. The description of a virtuous businessperson has utility, of course. The qualities that contribute to a company's success are not always recognized or well understood. Companies may be encouraged to foster or better reward these traits. Yet specific guidelines for business decisions and policies have not, thus far, been traced back to compatibility with a recommended moral psychology. This means that most often virtue serves only as an addendum to other determinations of what is ethical in business. Whatever the role of virtue in ethical theory, further empirical research into the connections between institutional practice and good behavior is sure to be a boon to the study of virtue.

Ancient Accounts of Virtue

The ancient tradition in ethics was committed to an understanding of happiness (*eudaimonia*) as our highest good. Today, we tend to think of happiness as something fleeting, as something we can experience in an afternoon. The ancients meant, by *eudaimonia*, something more like the subjective experience of leading a good life. We are, the ancients explained, tempted to organize our lives around goals that seem immediately good to us: power, pleasure, wealth, and fame. There is, of course, some good in all these, but to pursue them all is problematic since they involve contradictory requirements. To attain great power, you may need to sacrifice pleasure. This may not seem to be a practical impediment, and indeed the ancients would not argue that it was. Many unvirtuous people attain great power. We all trade off various goals for others at any time. The common temptation, warned the ancients, was to pursue these goals in a single-minded or unreflective fashion. In either case, we are failing to reflect on why we pursue what we do. Such reflection, according to the ancients, can be fruitful. Our psychology, the ancients argued, will not find itself satisfied until we come to understand and implement an understanding of the ultimate point of our lives. And the ultimate point of our lives will not be to accumulate goods or accomplishments that can easily be taken away. It will not be to possess things whose care can so easily consume us with worry and attention. The ultimate point of our lives will not, once understood, leave us feeling that we have not had enough no matter how much we have got. The ancients argued that the ultimate goal in our lives would have to be of a different sort of nature than the goods and goals we tend to think make us happy.

The most likely candidate for an ultimate goal would be psychological in nature, since the above requirements would be met only by a change within one's self. Pursuing this goal would transform our pursuit of less long-term goods in our lives. Professional goals, for example, would be put into their proper context within a life. This would make them less likely to disappoint and more likely to be pursued responsibly. Once we discover for ourselves this most final end, we will come to understand what true happiness is, and commonsense accounts of happiness can be abandoned, recognized to be poorly developed. What remains to be explained is how morality fits into this description of an ultimate goal capable of organizing our lives.

Morality

The ancients determined that all our immoral impulses were the result of having goals other than the sort of long-term happiness just described. Whether we lie to our boss, steal from the company, or betray colleagues, we have often calculated the benefits of doing these things from a less than comprehensive perspective on our lives.

The major schools of ancient ethics came to the conclusion that a life lived for the sake of being moral was the best candidate for our most comprehensive and long-term goal, happiness. This is, of course, a striking and bold claim. Some contemporary ethicists reject it as ridiculous on its face. A virtue ethicist will not recognize, for example, that a corrupt businessperson can be happy or that a deceitful person can actually benefit from deceitful practice. The assumptions that underlie these claims are as follows. True value is not as obvious as we think it is (it is not reducible, e.g., to a promotion or a raise). Our psychologies are of such a nature that they can function unimpeded only when moral precepts have been internalized. The consequence of committing one's self to such a life would be the development of the virtues.

It is not helpful to describe ancient descriptions of virtue by listing the terms we use for moral qualities we admire. The ancients, after all, developed the theory described above. Their proposal that we focus on some ultimate, final end is hardly what we would expect to find confirmed by our commonsense judgments about people and their qualities. Commonsense judgments involve all sorts of puzzles. For example, why might a "moral" quality like courage sometimes contribute to bad action? Such puzzles do not exist when the standard for virtue is the ancient one. Clear criteria for virtue are offered by the ancients—it is the psychological condition we develop and require to make moral choices regularly, without tension or weakness of will.

To give a simple example, think of being left alone before the petty cash box in your office. Imagine that it is obvious that you could grab a handful of bills without anyone being the wiser. Many of us might consider taking the money and begin to weigh the consequences of doing so (perhaps double-checking to make sure no cameras are on, that no one is actually nearby, etc.). Others would not even consider taking the money. Those who would not consider taking the money have attained something of virtue. Evidence that considerations of virtue outweigh monetary value comes from thinking about what would happen if your reimbursement from the company for some legitimate expense was short. Even a virtuous person would then ask for the correct amount back. This shows that money has not lost value for the virtuous. Indeed, a dispute about a short reimbursement might happen in front of the very petty cash box that did not tempt the virtuous. For the virtuous, money they deserve has one sort of value; money they do not deserve does not have this same value. This is the effect of committing to a longer-term goal than the simple accumulation of money.

If we practice our commitment to our longest-term goal, we will get better at recognizing which norms apply in a moral situation. There are, of course, all sorts of norms that support not taking the money. A person who refrained from taking could easily recall any one of these ("Do not steal"). To develop virtue requires that the inappropriate and irrelevant norms are not regarded as applicable. ("Jane took from petty cash last month, so I can too.") Think of how common it is for the cost of taxi fares to be misrepresented on an expense report. Those who engage in this practice know, at a very conscious level, that this behavior is wrong, dishonest, and inappropriate. But some other norm encourages the behavior. Likely, it is something like "Everyone else does this" or "Don't be a sucker" or, perhaps, "Do what you can get away with."

In addition, the process of becoming good gets easier as a person's motivation set gets less complicated. To develop virtue requires that your motivations not include contradictions that you may not even be aware of, for example. Those who struggle not to steal, though they desperately want to avoid doing so, have an overly complicated set of motivations with which to contend. Virtue is not assisted by such a condition. To function as a virtuous person, you have to figure out which motivations interfere with doing what you have been able to determine you should do ("Am I too much of a people pleaser? Is that why I gave in to the pressure?").

According to the ancient account, virtue has an intellectual, a dispositional, and an affective component. When these components are described separately, virtue can seem an abstract and theoretical ideal, but we can recognize the effect of the conjunction of these components in the example the author has just given. The intellectual component of virtue is a matter of knowing the money is not yours, that you do not yourself expect to be taken advantage of, and perhaps that the economic system as it exists tends to function well enough for all involved, warranting your endorsement. You would, in other words, be able to explain why stealing is wrong. Virtue ethics does not require that your explanation be technical. Instead, it could be just as the author has described it.

The dispositional component of virtue is a matter of how this propensity not to steal has become second nature to you. You tend not to steal. If you steal in other contexts, and not taking the money in this case was an exception, then your character is not virtuous. To develop a virtuous disposition, you must work on developing the intellectual and affective components of virtue. You must attempt to relate your beliefs about theft, for example, to your understanding of ethics. To find yourself no longer attracted to bad behavior, you must work at internalizing, and truly coming to accept, the coherent account you develop on the topic.

The affective component of virtue is a matter of experiencing pleasure in acting right. People who have made themselves good do not regret money they have not stolen, for example, and they do not see vicious people as having made choices of which they could be envious. This condition comes about only because when we pursue virtue, we become transformed. It is this element that is most frequently left out of contemporary accounts of virtue, even those that hark back to the theory of the ancients.

Virtue Transforms Us

The process of becoming virtuous is much like getting used to being healthy. You must begin by garnering an understanding of what weight loss and health require. If you are misled about this, you are bound to fail. As you start out, you may likely have to reckon with having a taste for donuts and potato chips. This may seem insurmountable, as the donuts and potato chips taste so good and have always proven irresistible in the past. But, perhaps to your surprise, after forcing yourself to exercise for months, you find that not only the exercise itself has gotten easier to do and to include in your day, but eating healthier has gotten easier as well. You no longer even have the taste for junk food and now wonder how anyone could. You have begun to associate junk food with its bad effects: sluggishness and extra weight. Exercise has begun to pay off, and the rewards of it now seem obvious.

This description matches much of how virtue is supposed to work to integrate all our ends: by making what satisfies us fit what is actually good. A junk food fan is not getting optimal feedback from his or her body, and happily, we can transform our tastes. When we act immorally, we are not getting optimal feedback either, and happily, there is, according to virtue ethics, a way to stop ourselves from acting in such an undisciplined fashion. Once we become acclimated to good behavior, perhaps to our surprise, we will recognize that we have come to enjoy and prefer moral to immoral behavior. The temptations of immoral behavior no longer have their allure because the long-term negative consequences of it can be seen as part and parcel of the seeming gains it brings.

Of the ancients, only the Stoics understand our ethical transformation as going so far that we can come to care about virtue to the exclusion of any particular commonsense goods. If we cannot conceivably do this (if even an idealized conception of the human cannot do this) then the Stoics will be wrong about virtue being sufficient for happiness. Other ancient ethicists, such as Aristotle and the Epicureans, are reconciled to the idea that some commonsense goods need only be understood in relation to virtue in order to be properly pursued. To continue the analogy, some ice cream, at some times, might still be perfectly acceptable to the healthy person's system, given that the healthy person is aware of the amount he or she may have and the effects on his or her health.

In contrast to contemporary virtue ethics, however, what matters is that ancient virtue ethics recognizes that virtue involves transformation, and this transformation results from our committing to an accurate understanding of our most final end. This, among other things, makes a eudaimonist account of virtue differ vastly from most modern-day accounts of virtue. Ancient-based accounts of virtue are kept, by their theoretical structure, from having to rely on (or recommend that we follow) a commonsense understanding of the virtues. This is not to say that common sense does not already itself endorse some of ancient virtue theory's insights. We do not, after all, count it as generous when someone gives a gift merely for the sake of impressing someone. Many of the problems associated with the use of virtue ethics come from the invocation of common sense to settle matters that may be better handled by a theoretical standard.

Contemporary Variants of Virtue Ethics

Contemporary accounts of virtue ethics always refer back to ancient accounts, and careful authors highlight both the similarities and differences. Three modifications of the traditional approach are most common in contemporary virtue ethics. The first is that ancient theory is replaced with more commonsense notions about virtue. The second is that the notion of a final end is dropped. The third is, as mentioned, that right and wrong are determined in other ways than through a description of virtue.

Common Sense and Virtue

Often, contemporary accounts of virtue are updated by inserting a commonsense conception of virtue in place of the theoretically defined one. What bravery is, for example, is taken to be obvious, and descriptions of bravery are culled from literature and life experience and used to describe the virtue. Rather than looking to what common sense takes to be virtue, the traditional virtue theories determine what virtue is by seeing what will result from a commitment to morality.

Contemporary accounts of virtue are most often more modest about the effects of attaining virtue. According to traditional accounts of virtue, aspects of ourselves under our conscious control (our emotions, our desires) will be transformed as we become virtuous. Contemporary descriptions of virtue are not this spectacular. Very rarely is a virtuous life described as one that has been transformed.

Contemporary accounts of virtue are also more likely to describe virtue as something some people just have. Role models are often given credit. The ancient schools were, in contrast, convinced that the process of developing virtue would have to be active and acutely conscious. This means that the ancient theories of virtue would not recognize as virtues character traits one attains without effort. According to ancient virtue theory, no one is surprised by the sudden discovery that they are virtuous. It is not the sort of thing you could attain without being aware that doing so was your primary agenda.

There are two possible unanticipated consequences to these modifications of traditional virtue theory in contemporary accounts. One is that virtue may be described in a fashion that is not realistic because of the self-sacrifice required. The other is that virtue may be regarded as something that cannot be attained because it is always fleeting and competing with other types of good qualities.

If common sense is our guide to what is a virtue, feelings such as "compassion" will be considered virtues. This, when associated with the traditional recommendation that one should always act out of virtue, brings us the expectation that one be compassionate all the time. And such a thing, of course, is not possible. Something like compassion could not be a virtue on the traditional account precisely because it could not be something one exhibited all the time. The modernized account leads to a pessimistic take on our natures.

The second possible unintended result of invoking common sense in an account of virtue is that virtue is not associated with a lasting transformation of one's character but with certain habits one could give up or start at will. The problem with this is that virtue talk may become nearly meaningless. Helping someone once might make you "kind," at least that day, and speaking this way will be possible despite how mean you may be most of the time. The traditional accounts can explain why someone may display courage yet be dangerous or be honest yet be untrustworthy. If we are all considered to have a profusion of virtue, we are afforded no clarity when it comes to the nature of good qualities.

No Final End

A second common modification is that the intellectual component of virtue is dropped. This allows us to recognize that we can be inadvertently compassionate and that this counts toward our goodness. The traditional requirement is that one be perfectly conscious of why and that one is acting well. Far more behavior is counted as virtuous, and new standards for such behavior (even consequentialist ones) can be used to assess virtue if the traditional requirement is dropped. The notion that virtue must be developed through a focus on one's final end is abandoned. Sometimes, there is talk of the need to be habituated to virtue, but this is usually taken to be the result of practice encouraged through external incentives, or, if self-directed, the practice is a matter of discipline rather than philosophical exploration of the point of one's life.

The Supplement of Other Criteria for Right Action

A final common change from traditional accounts comes from regarding considerations of virtue to be a sort of addition or supplement to other means of establishing what is right and wrong (e.g., the invocation of a theory such as Rawls's or consequentialism). This is, of course, only to consider character in relation to other ethical approaches. Though such considerations can be referred to as a virtue-based approach and even at times as virtue ethics, there is no serious connection between this focus on character and the ancient accounts of virtue.

Criticisms of Virtue Ethics

Criticisms of virtue ethics abound. All to often criticisms of virtue ethics are made secondhand and without reference to either the ancient texts or the contemporary works of theory. Frequently, a commonsense conception of the virtues is inserted into an interpretation of a theorist's proposals, and as a result, the proposal seems unsound. For example, ancient accounts of the unity of the virtues are frequently dismissed as implausible because it is difficult to imagine our commonsense conception of virtue requiring that to be brave we must also be kind. But given the brief description just offered, it is clear that being naturally brave, or doing some brave action, is not the same as having consciously committed one's self to morality. On the ancient account, bravery requires awareness of the point of your activity. Without this, your actions (which may, of course, in many ways be laudable) are still not virtuous, as they do not meet the intellectual criteria for this type of behavior. And to meet these criteria in the case of courage (you understand why and when it is appropriate) means that you will surely also have an understanding of when, for example, kindness would be required.

Virtue Ethics Is Not Applicable

One objection is that virtue ethics can offer only extremely general advice and role models but no objective guidelines. (Indeed, at times this is claimed of virtue ethics to argue for imprecision in ethics.) This may be the result of Aristotle being more widely known than the other ancient ethicists who shared the structure of his ethical theory. Yet even Aristotle, in Book 9 of the *Nicomachean Ethics,* uses his ethical theory to assess very particular guidelines for behavior. We have evidence of the Stoics doing this far more commonly, however, as they worried very much about the justification of particular prohibitions. Cicero records debates about the type of information one must reveal before a sale. Stoics disagreed, for example, on whether you could profit as much as possible from bringing the first ship of grain to a famine-torn island (the issue concerning whether you should reveal that more ships are imminent), but they were not seeking to recommend only to "be virtuous." The two sides argued over whether it was necessary to endorse the proposition "reveal information about other sellers when the buyer's situation is dire," given a good person's overriding commitment to morality.

One reason critics assert that virtue ethics is applicable in the way an ethical theory needs to be is that virtue ethics provides a different type of standard for rightness than that to which most contemporary ethicists are accustomed. In the traditional accounts, for example, what determines whether an action is right or not is whether the actor is capable of justifying it. We, of course, function as the judges of whether the justification stands or not. But virtue ethics neither offers an abstract and rationalistic justification for a list of right actions nor recommends a set of principles that, if applied, are supposed to clarify which courses of action are right. The criteria of rightness offered by traditional virtue ethics can frustrate philosophers and applied ethicists who are used to handier means of assessing right and wrong. But what is handy to writers is not always what can be invoked by the public at large, and the assessments virtue ethics makes are clearly a refinement of the type of judgments we make in our personal lives all the time. We are not impressed, for example, by a generous gift if it comes from a person giving it just to seek favor.

The Empirical Challenge to Virtue

The most recent challenge to virtue ethics has been leveled by philosophers looking to research in social psychology that suggests human behavior is far more variable than we commonly assume. Gilbert Harman and John Doris are leaders of a movement in philosophy known as situationism or, more generally, empirical ethics. This movement looks to verify the claims of ethical theorists through surveys and experimentation. Past experiments by social psychologists have been used by these philosophers to challenge the moral psychology assumed by any account of virtue. Several of these experiments have found that a large percentage of subjects can be found to be kept from small acts of kindness by minor and irrelevant changes in their environment (their "situation"). A memorable example is that of an experiment that found certain smells can encourage or discourage minor altruistic behavior. The current reasoning of the situationists goes like this: The moral psychology required for virtue is unrealistic since experiments have shown that the majority of us act in ways that are susceptible to small changes in environment. People cannot, they argue, be assumed capable of acting morally regardless of the situation.

The difficulty in accepting this criticism of virtue ethics may be obvious. Virtue ethics of any sort is unlikely to regard the majority of the population as virtuous. Even when virtue is not described as the result of the taxing and lengthy process the ancients describe, it is considered a rare and unique condition. The experiments situationists cite give evidence of some people acting morally, regardless of situational input. This may indeed be a sign of these subjects having virtue. A final obstacle to the situationist critique of virtue is that right action is something virtue ethicists define for themselves. It is difficult to test an ethical theory by using a standard for right action other than the one the theory itself offers. The behaviors social psychologists count as minimally moral (e.g., helping a person to pick up papers) are not necessarily required by virtue. Aristotle's "great man" is described as concerning himself with serious and not trivial moral matters, for example. The conclusions of the psychologists who conduct the experiments are far more limited than the philosophers reporting on these experiments suggest. Social psychologists do not regard themselves as targeting character traits and are certainly not taking aim at an Aristotelian conception of virtue. Experiments would have to be designed around these proposals for them to be tested.

To the extent situationists are requesting empirical verification of the moral psychology associated with a virtue ethic, their influence can be a positive one. Virtue ethics has always been dependent on an accurate description of our moral psychology for its recommendations. It happens to be the case that the results of experiments in social psychology, as the psychologists themselves describe them, can be welcomed by virtue ethics. Indeed, some of the conclusions (e.g., that some of us can be easily swayed by others to change our stated opinion) are what the ancient texts would lead one to suspect is the case. Research could help us settle not only what moral psychology ought to be associated with virtue but also what business environments, policies, and decisions are compatible with virtue. Empirical methods may someday reveal to us both what the virtuous person in business would be capable of recommending and what recommendations would promote virtue.

Other criticisms about the approach are likely to be outdated. It can no longer be said, for example, that virtue ethics cannot be said to describe only right agency and not right action. It cannot be said that virtue ethics involves an opposition to rule-based thinking, to the recommendation of principles, or to more than very general advice about how to live. And it is also no longer considered helpful to merely oppose virtue ethics to two other dominant approaches in the field of ethics: consequentialism and Kantianism. Virtue ethics has had such an impact on the field of ethics that distinctions that had been assumed to be obvious are now difficult to find. Kantians now emphasize Kant's account of virtue, and consequentialists do not shy from discussions of agency.

A Future Role for Virtue in Business Ethics

Virtue ethics has received a great deal of attention in the field of business ethics, though the promises that its entry would transform the field have not been fulfilled. There are two reasons why those interested in virtue still have cause for hope that business ethics can be further refined (and not merely broadened) by discussion of virtue. One is because a traditionally styled virtue ethic has not yet been developed for use in the field of business ethics. Articles have, of course, suggested that such a thing could be valuable, and some article authors have begun work in this direction. The possibility of being able to assess the output of a company according to a virtue ethic's value scheme ought to be attractive to those business ethicists looking to capture the public's imagination and attention. A second reason is due to the possibilities of empirical research supporting some of the ancient claims of virtue ethicists. If social scientists begin to test for the account of moral psychology required for virtue, they may find that certain classes of policies are more conducive to the encouragement of virtue and that certain institutional designs attract the virtuous.

—Jennifer A. Baker

See also Conscience; Consequentialist Ethical Systems; Dignity; Ethical Naturalism; Ethics, Theories of; Goodwill; Honesty; Moral Imagination; Moral Leadership; Moral Point of View; Moral Reasoning; Rationality and Ethics

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VOLUNTARISM

Voluntarism is a term associated with theories that emphasize the primacy of the force of will in contrast to rationalistic or intellectual explanations of God, reality, human nature, or morality. Theological and metaphysical theories of voluntarism have influenced evolving moral, psychological, and political thought.

Theological voluntarism is often traced to the medieval writing of John Duns Scotus, William of Ockham, and those who stressed the importance of the divine will of God. Scotus claimed that God's will determines what is reasonable or right and that God is free to act on this will. Ockham believed that divine will, rather than any form of pure or human reasoning, mandates whether human activities are sinful or good. He claimed that God's freedom is absolutely unlimited and that nature itself is subject to divine will and has no causal or logical inevitability. Divine command theory is associated with the views of Ockham and others who grounded theology and morality in God's will and commands. God was seen as radically free and could have willed other than any reasonable moral order. Theological voluntarists challenged the influential views of Aristotle and Aquinas, who stressed that reason or rationality is critical in trying to understand an ordered, logical universe in which human beings are part of this whole. Heaven, or a final state of fulfillment, was associated with contemplation in the Aristotelian tradition, while voluntarists believed that fulfillment or happiness comes through acts of love and fidelity to God's will. The priorities that earlier Greek and scholastic Christian thinkers had placed on form or matter, rationality, order, and hierarchies were replaced in theological voluntarism with contrasting concerns.

A focus on the will of God, as expressed by theological voluntarists, shifted with the Enlightenment and later philosophical conceptions of the will. These metaphysical conceptions of nature or reality held implications for politics, psychology, and morality. For example, Thomas Hobbes had a bleak view of the consequences of unconstrained human will or desire, and he proposed political remedies such as the power of a strong sovereign state and its regulations and controls to harness human willfulness and excesses. David Hume thought that moral sentiment directed human behavior, and he dismissed reason as influencing human behavior or having a role even in opposing or controlling a powerful will. Metaphysical voluntarism had some of its origin in Immanuel Kant's denial of a capacity for pure reasoning by human beings, but those later advocating forms of metaphysical voluntarism had very different perspectives from those of Kant, or often from one another. Three prominent examples of metaphysical voluntarism can be found in the work of Arthur Schopenhauer, J. G. Fichte, and Friedrich Nietzsche.

Schopenhauer viewed universal will as the ultimate reality, and he insisted that all things are the expression of or are determined by this overarching and powerful will. He found the objectification of this essential will in forces of nature and inanimate matter as well as within all living things. For Schopenhauer, this essential will, as expressed in the human will to live, desire, procreate, and consume, could not be controlled by any final goal or purpose. Such human will and desires could never be fully satisfied and, thus, only led to human frustration and suffering. Even knowledge concerning this dominating will, according to Schopenhauer, only leads to greater pain associated with increasing awareness of vast human egoism and deficiency. For this desperate human condition, Schopenhauer suggested asceticism and available forms of negation of desire, as extreme as starvation and death.

Fichte did not draw as sharp a division or opposition between the human will and human reasoning, nor did he view the consequences of will for human welfare as pessimistically as Schopenhauer did. Fichte conceived of an absolute and incomprehensible ego, of which will was an important part, as an ultimate reality. This ego, however, was an informed and creative force. In contrast, Nietzsche was obviously influenced by Schopenhauer and described a will-to-power. Like Schopenhauer, Nietzsche viewed the will as a force driving all natural phenomena, including human and social potentials. Yet Nietzsche denied a strong link between his conception of a will-to-power and Schopenhauer's more pessimistic version and explanations of will. For Nietzcshe, such will was to be embraced and celebrated, rather than to be denied or struggled against.

Metaphysical voluntarism describes an essential and transcendental will that underlies all phenomena. In contrast, psychological voluntarism and ethical voluntarism consider acts of will and the perceptions, cognitions, value judgments, and other responses associated with this willfulness. Judgment of the goodness or badness of an act depends on that will, and certain standards, those chosen by the actor or by others, should be directed in judgment of that will. Consequences of the focal act are, thus, irrelevant to judgments of an individual's having done right or wrong. While bearing a few similarities to Kantian ethics, and contrary to consequentialist ethical theories, ethical voluntarism differs from an emphasis in Kantian ethics on universal principles or imperatives. Ethical voluntarism is found in the work of William James along with his concern that actions actually produce desired ethical outcomes. James declared that things or acts are good simply because these are desired or willed. Will and self-interests in his view have primacy over knowledge, and knowledge has merely an instrumental role in obtaining human will. Ethical voluntarism, according to James, means acting on multiple desires so as to obtain the most benefits and least frustrations. Josiah Royce, a protégé of William James, is another example of an American theorist who had a voluntarist orientation. According to Royce, we know or interpret reality as an act of will. In contrast to a blind or consuming will, described by Schopenhauer and others, Royce characterized this will as loyalty toward that which we love.

Aspects of voluntarism, as priority placed on individual freedom of action and related ethical judgment with regard to these actions, led some 20th-century theorists in the direction of anarchist proposals as a remedy for avoiding forms of political or authoritarian compulsion. At least some affinities with aspects of ethical voluntarism can be found in theories such as existentialism or the radical, subjective, and individual freedom advocated by Jean-Paul Sartre and certain postmodern theories focusing on individual appropriation of meaning and direction.

—Stephen L. Payne

See also Anarchism; Divine Command Theory; Egoism; Existentialism; Free Will; Hobbes, Thomas; Human Nature; Hume, David; Kant, Immanuel; Postmodernism; Pragmatism

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VOLUNTEERISM

Volunteerism refers to the practice of volunteering one's time or talents for charitable, educational, or other worthwhile activities such as working to preserve the natural environment, organic farming, conservation education, health care for children in orphanages, local activities in one's community, or military service. Volunteers perform a service willingly and without pay.

In the United States, nonprofit organizations serve a critical role in a society that is mostly made up of immigrants seeking to better their lives and the lives of those around them. In other countries, local and national governments often fulfill the functions that volunteers in the United States provide.

According to the Bureau of Labor Statistics of the U.S. Department of Labor, 65.4 million people volunteered for an organization at least once between September 2004 and September 2005. One fourth of men and about one third of women performed a median of 1 hour per week of volunteer work and were involved with one or two organizations during this same time period.

Volunteerism provides considerable social benefits, as volunteers say they gain more than they give as they learn new skills, gain experience, make friends, enjoy their work, and are generally satisfied with their lives. Most volunteers say that they feel a sense of belonging or connectedness in their community as a result of donating their time. Other volunteers say that community service provides a meaningful structure to their lives. Oftentimes, volunteers find a new job or transition to a completely different career through volunteering.

Success Factors

Volunteers are not born; they are cultivated. Organizations that depend on volunteers should strive to create a culture that honors, provides structure for, and recognizes their contributions.

There are several key areas that are critical to the success of both the volunteer and the organization:

- Organizations depending on the critical skills of volunteers need to articulate their vision, mission, and objectives for volunteers to understand their impact on the community in which the organization serves. A clear mission allows the organization to focus on its core competencies and not get sidetracked by attempting to be all things for everyone. This also aids volunteers in understanding what skills they need to possess or be willing to develop.
- It is important that the leadership of the organization provide open lines of communication and the ability to articulate the value and significance of the volunteer's contribution. Volunteers want to feel that they are making a positive impact on others' lives, and it can be very encouraging to know this.
- Volunteers need a passionate supervisor who will provide structure and accountability. Supervisors must be trained in volunteer management and given the necessary tools and resources to carry out the task or service they are responsible for coordinating.
- There is a fine line between micromanagement and careful oversight. Every volunteer must understand his or her role and responsibilities, and this starts with a clear description of the duties and responsibilities that each volunteer is expected to carry out. Oversight can be conducted formally or informally, depending on the individuals or the tasks involved, but it must be done. In addition, oversight of volunteer activities can give team members the feeling that someone cares about their overall success.
- Clear levels of authority are necessary to ensure volunteers are working within the parameters of the job function. It is important for volunteers to feel empowered and creative to solve business issues. However, clearly defined levels of authority help keep a budget, deadlines, deliverables, and results within the bounds of acceptability.
- Necessary training should be provided at the appropriate time. It can make a world of difference for a volunteer who is striving for excellence in his or her service to know how experts in the field carry out similar responsibilities. Training can be provided in the form of books, manuals, films, external seminars, or in-house training events tailored to the volunteers' level of commitment or experience. For those individuals volunteering their services on an ongoing basis, updated training with new materials and information should be available every year.
- If an organization is asking volunteers to undertake specific responsibilities or services, the organization must be serious about the importance of any mandate. There are many organizations needing volunteers, and the daily demands on our time should convince us to respect each other's time. By not providing the necessary tools and resources to get the job done, an organization is wasting precious time and energy and possibly losing the interest of the volunteer.
- Because we are all human, nothing motivates involved individuals and potential volunteers as much as regular public recognition. The impact of public recognition can be both powerful and inspiring as the organization shows its appreciation in honoring individual volunteers. Rewards, unlike recognition, should be private and do not need to be extravagant. Often, taking the time to say thank you or to acknowledge a job well done can create an appreciative culture. Such organizational cultures can in turn allow for strong team environments to flourish.

The most common reason for not volunteering one's time is the "lack of time." We live in a society where daily demands are enormous, and for many in the United States, the abundance of material goods is overwhelming. However, volunteering one's time, talent, or money can range anywhere from 1 hour per month to several hours per day. Helping to reaffirm the dignity of humanity can be reflected by many simple forms of kindness such as providing a meal to the homeless, donating a coat to a child in need, or visiting a forgotten someone in a nursing home. Simply being observant of the needs of people around us can be a great starting place to volunteer. Random acts of kindness can be inspiring and uplifting, and they may just motivate other people to give and help others out of their own creative resources.

—Anne Kohnke Meda

See also Dignity; Economics of Well-Being (Post-Welfarist Economics); Self-Realization; Voluntarism

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Von Neumann-Morgenstern Utility Function

John von Neumann and Oskar Morgenstern extended the theory of consumer preferences by incorporating a theory of behavior toward risk variance. The utility function that bears their names arises from the expected utility hypothesis. Basically, when a consumer is faced with a choice of items or outcomes subject to various levels of chance, the optimal decision will be the one that maximizes the expected value of the utility (i.e., satisfaction) derived from the choice made. Expected value is the sum of the products of the various utilities and their associated probabilities. The consumer is expected to be able to rank the items or outcomes in terms of preference; but the expected value will be conditioned by their probability of occurrence.

The von Neumann-Morgenstern utility function can be used to explain risk-averse, risk-neutral, and risk-loving behavior. For example, consider a project a firm undertook last year having particular probabilities for three possible payoffs. These payoffs were \$10, \$20, or \$30. The respective probabilities of receiving them were 20%, 50%, and 30%. Thus, expected payoff from the project was \$10(0.2) + \$20(0.5) + \$30(0.3) = \$21. This year, the firm will again undertake the project, but this time, the respective probabilities for the payoffs have changed to 25%, 40%, and 35%. It is easy to verify that the expected payoff is still \$21. In other words, mathematically speaking, nothing has changed. It is also true that the probabilities of the lowest and highest payoffs rose at the expense of the middle one, which means there is more variance (or risk) associated with the possible payoffs. The question to pose to the firm is whether or not it will adjust its utility derived from the project despite the project's having the same expected value from one year to the next. If the firm values both years equally, it is said to be risk neutral. The implication is that it equally values a guaranteed payoff of \$21 with any set of probabilistic payoffs whose expected value is also \$21.

If the firm preferred last year's project environment to this year's, it places higher value on less variability in payoffs. In that regard, by preferring more certainty, the firm is risk averse. Finally, if the increase in variability is actually preferred by the firm, it is said to be risk loving. In a gambling context, a risk averter puts higher utility on the expected value of the gamble than on taking the gamble itself. Conversely, a risk lover prefers to take the gamble rather than settle for a payoff equal to the expected value of that gamble. The implication of the expected utility hypothesis, therefore, is that consumers and firms seek to maximize the expectation of utility rather than monetary values alone. Since utility functions are subjective, different firms and people can approach any given risky event with quite different valuations. For example, the agency problem recognizes that a corporation's board of directors may be more risk loving than its shareholders and, therefore, would evaluate the choice of corporate transactions and investments quite differently even when all monetary values are known by all parties.

Preferences may also be affected by the status of an item. Consider the difference between something possessed (i.e., with certainty) and something sought out (i.e., subject to uncertainty). Sellers may overvalue items relative to their potential buyers. This endowment effect, first noted by Richard Thaler, is also predicted by the prospect theory of Daniel Kahneman and Amos Tversky. Risk aversion may be explained in the sense that the disutility of risking the loss of \$1 is higher than the utility of winning \$1. A classic example of this risk aversion comes from the famous St. Petersburg Paradox that offers a person a series of possible payoffs starting with a 50% chance to win \$1, a 25% chance to win \$2, a 12.5% chance to win \$4, and so on. The expected value of this gamble is infinitely large. But how much money would someone pay for the privilege to take this gamble? The fact that the payment (if any) would obviously be very small relative to the expected payoff shows that individuals do account for risk and evaluate the utility derived from accepting or rejecting it. Risk loving may also be explained in terms of status. Individuals may be more apt to take a risk if they see no other way to improve a given situation. For example, patients risking their lives with experimental drugs demonstrate a choice likely to be positively correlated with the gravity of their illnesses.

In summary, the von Neumann-Morgenstern utility function adds the dimension of risk assessment to the valuation of goods, services, and outcomes. As such, utility maximization is necessarily more subjective than when choices are subject to certainty.

—Darren Prokop

See also Agency, Theory of; Consumer Preferences; Expected Utility; Marginal Utility

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W

Wage-and-Price Controls

Wage Controls

Wage controls refer to a form of government intervention where a minimum or a maximum is imposed on wages. Imposing a minimum, or a floor, is aimed at securing a living wage for labor. Imposing a maximum, or a ceiling, on the other hand, is directed at curbing inflation. Wage controls are also considered as a social measure to prevent exploitation of labor. Wage controls are usually used in times of economic instability. Minimum wage, which was first introduced in the United States after the Great Depression, is an example of wage floors.

Some economists argue against wage floors. They contend that wage floors would create surpluses. Since wage floors cause wages to be higher than they would be under free market, employers would not have the incentive to hire as much labor. Thus, wage floors, while providing a living wage for those who have a job, would increase unemployment.

Price Controls

Price controls refer to a form of government intervention where a minimum or a maximum is imposed on the prices of some goods and services. Imposing a maximum, or a ceiling, is aimed at reducing inflation and keeping prices of these goods and services from increasing dramatically. Usually, price ceilings are used in times of economic instability resulting from wars or natural disasters. The prices of goods and services under a price ceiling would be less than their prices under free market. For example, during the 1970s the U.S. government used price controls to prevent the prices of gasoline from increasing; a price ceiling was imposed. Price controls were also imposed during World War II, the Vietnam War, and the Korean War.

Most economists do not favor the use of price controls, at least not for long periods of time. The argument is that the use of price ceilings produces shortages since the demand for the products or services would be much higher than the supply. Supply would not increase to meet the higher demand due to the imposed price ceiling. The price ceiling would make it not profitable for producers to increase supply. The shortages would thus be seen in the form of waiting lines and deteriorating quality. In addition, price ceilings may create black markets where price-controlled goods and service would be traded.

At present, the use of price controls in the pharmaceuticals industry to regulate the prices of prescription drugs is debated. On the one hand, imposing price ceilings on prescription drugs would make them more affordable to patients. On the other hand, price ceilings would have a negative impact on research and development in the pharmaceuticals industry, as investment capital would seek opportunities that yield higher returns.

—Kareem M. Shabana

See also Black Market; Free Market; Living Wage; Regulation and Regulatory Agencies; Rent Control

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Wages for Housework

Wages for housework is a proposal to compensate for work done in the private or domestic sphere. Such work includes, but is not limited to, providing household services that facilitate the laborer's entry into the public workplace (cooking, cleaning, etc.), reproductive activities such as bearing and rearing children, and caring for elderly parents and other dependent persons. The wages-for-housework campaign is usually rooted in the Marxist critique of capitalism; it was advanced by numerous social activists, anticapitalists, and feminists dating back at least as far as the mid-1800s.

Prior to the age of industrialism, the domestic sphere was not sharply split from the productive sphere. Textiles and agricultural products were created within domestic units. With the rise of industrialism, the public workplace replaced the private home for the creation of products. Disproportionately, women were excluded from industry. Those tasks left to women to perform in the home such as child care, laundry, and meal preparation were viewed as nonproductive because they did not earn a wage.

In the late 1800s, Friedrich Engels's *The Origin of the Family, Private Property, and the State* and August Bebel's *Women and Socialism* brought into stark relief the historical development of woman's social confinement within the home as well as the circumstances accounting for the devaluation of domestic labor under capitalism. Their arguments set the foundation for subsequent developments in the campaign to obtain wages for housework.

With the influx of women into the workforce in the 1970s and 1980s, the argument in favor of compensation for domestic labor shifted slightly to acknowledge the hazards of the double workweek on women: Women who entered the labor market were often expected to continue to fulfill all the household duties once they returned home. Middle- and upper-class women could employ domestic labor but, more often than not, poor and minority women were recruited to fill the space left in the home when women joined the public workforce. Usually, those hired to perform domestic duties were paid at wages far below what might be expected in the public sphere.

Proponents of the wages-for-housework campaign are not in agreement over the justification or means of a wages-for-housework program, but in general they argue that women's domestic work creates *use-value* (a Marxist term that means the value of products for immediate consumption that satisfy human desires). The work to care for a family and home provides the conditions for all other labor not only because capitalism needs women to produce excess labor power in the form of children but also because the work women do in private provides the necessary conditions for paid laborers to work in the productive sphere.

An alternative to paying wages for housework is to convert work performed in the home to public economy work through the socialization of domestic labor. That is, the implementation of state-supported services could replace much of the cooking, child care, and even cleaning that constitutes housework. Margaret Benston noted that unless the women were freed from the traditional work they performed in the home, their participation in the nondomestic workforce would be a step back. She argued that the socialization of housework was the single most important factor to end the oppression of women as a group and to give individual women their due respect.

Capitalism, according to advocates of the wages-for-housework campaign, undervalues all caregiving work thereby subjecting women to economic inequality and poverty regardless of whether that caregiving is in the labor market or outside the labor market. Wages for housework would alter social perceptions of caregiving work by attaching a value to that work in the home and closing the division between public and private (domestic sphere) production. A wages-for-housework program could be paid for by the state with money garnered through universal taxes or family-specific taxes.

Contemporary articulations of the wages-for-housework argument compare it with survivor's insurance or social security. The government would disburse regular payments to primary caregivers—male or female—based on total household income and with no restrictions on use of funds. Caregivers could elect to use the financial assistance to purchase quality child care or household assistance, or even to further education or job-training for parents.

Opponents of the wages-for-housework campaign argue that it would entrench a system of gendered division of labor, keep women in the home, and devalue reproductive activity. By receiving a wage for work that they already do or are expected to do, women would be less inclined to develop their talents for service in the public sphere. To encourage men to assume responsibility for housework, wages would have to compete with market wages. In addition, paying a wage for caregiving, opponents argue, turns loving relations or loving activity into commodities thereby transforming familial relations into exchange relations within a capitalist system.

Other objections focus on the feasibility of wages for housework or the infringement on personal liberty that would be required in such a program. Opponents argue that taxing single people to pay for a service they do not directly use is unjust. The distribution of the wages poses additional problems in that a system of accountability is necessary to ensure that job requirements are fulfilled. Opponents fear that if the state pays for domestic labor, privacy and personal liberty would be sacrificed.

Although no thorough system of wages for housework exists in the United States, certain social programs have contributed to changing social perceptions about the value of work performed in the domestic sphere. The work that goes into child care, care of elderly parents, and other adults in need, as well as day-to-day family and household maintenance have captured the attention of social policy, ceasing to be solely private family matters. The wages-for-housework campaigns played an important role in insisting that domestic laborers receive some level of social protection.

—Sally J. Scholz

See also Comparable Worth; Feminist Ethics

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Warranties

Warranties are promises or guarantees made by a seller or lessor about the characteristics or quality of property, goods, or services, on which the purchaser or lessee relies. Warranties are either "express" (i.e., explicit oral or written representations about the quality or identity of the item) or "implied" (i.e., inferred into the contract in accordance with legal requirements). Statements of general opinion or clearly exaggerated claims (called puffery) are not considered warranties. In the event that a warranty is breached, the law usually provides the injured party with the right to monetary damages, repair of the original good, or replacement with substitute goods.

The Uniform Commercial Code (UCC), with its warranty provisions for the sale and lease of goods contained in Articles 2 and 2A, respectively, serves as the primary authoritative law on warranties in the United States. The United Nations Convention on Contracts for the International Sale of Goods (CISG) provides similar warranty rights and duties for certain buyers and sellers involved in global commerce. The CISG's warranty provisions (Articles 35–44) are tailored after the UCC, but contain some important distinctions. This entry looks at the warranty of title, the implied warranties of merchantability and of fitness for a particular purpose, and at express warranties (especially in general as to consumer goods).

Brief History of Warranties

The freedom to contract as desired was a much protected legal principle under early common law, and still is in many ways. Caveat emptor, let the buyer beware, was a natural consequence of such a principle since each party was entitled to enter into a contract as they chose. However, the freedom was not so absolute as to ignore how fraud or duress would impair said freedom and the resultant contract. In that same vein, failure to satisfy a promise about the good as to quality or type would also invalidate a contract as failing to meet its warranty. But it had to be a very specific warranty and expressly communicated as being a warranty to qualify. Not until the late 1800s was the warranty doctrine expanded to include positive affirmations or representations about the character or quality of an article sold. The common law continued to develop warranty law so that an implied warranty of safety for food and drink began in the early 1900s and was then expanded to include consumer products in the 1960s.

Originally, warranties also contained a privity requirement (i.e., any duties or protections imposed by warranty or other legal doctrine extended only to those directly involved in the sales transaction). To protect the consumer, the privity requirement was slowly reduced and then completely discarded as industrialized society, and its chain of distribution caused the relationship between manufacturer and the ultimate consumer to become more distant and thus devoid of the built-in safeguards of face-to-face contracts. Thus, manufacturers, sellers, and lessors became responsible for the ultimate consumer under warranty, negligence, and strict liability theories for the quality and safety of their goods and services. Horizontal privity was also relaxed so as to extend warranty coverage to the buyer's family, household, guests, and even to bystanders in some states.

But it was the UCC, first written in the 1940s, which would expand, standardize, and stabilize sales law (the Uniform Sales Act of 1906 was the precursor to Article 2 of the UCC, although not as widely adopted). The official text of the UCC was dated 1962 and included both express and implied warranties, and since then has been adopted in some form by the entire United States. Also, the federal Magnuson-Moss Warranty Act was passed in 1975 to ensure that sellers of consumer products clearly state the coverage of warranties. Furthermore, the United Nations Convention on CISG was originally passed in 1980 and has been adopted by approximately 68 countries, including the United States (as of 2006).

During this same period, tort law was also addressing product safety through the theories of negligence and then strict liability. Although there is some convergence in the coverage, warranties are based in contract, not in tort, and are a bit more limited in the amount of damages available as a remedy. Yet torts are mentioned very briefly in a few places below to better demonstrate the dimensions of warranty law.

Social and Ethical Implications

The issue surrounding warranties is to what degree should manufacturers, sellers, and lessors be responsible for the risk of defects and nonconformity in goods that they distribute. The ethical basis for warranties is basic fairness in commercial dealings. The risk in commercial dealings has over time shifted from the buyer, under the theory of caveat emptor, to the seller, under warranty and other theories. The consumer protection movement and related legislation of the 1960s was the highpoint in that shift of responsibilities and duties. Since the seller usually has more information, expertise, and control over the item in question, the law has deemed it fair and just to shift the risk. The consumer's vulnerability and dependence supports this approach. And even when the seller may be unaware of certain defects, the risk is still weighted toward the seller because they are believed to be more capable of absorbing the costs than the consumer, and in a better position to protect against it. Thus, they are encouraged to do so by the law of warranties. Some think that warranty laws are still lacking since they can be explicitly waived in the contract. Plus, consumers usually lack the bargaining power to push for better warranties.

The three primary theories protecting consumers and imposing greater duties on sellers are contractual theory, due care theory, and strict liability theory. Each essentially attaches a guarantee to the product intended to promote product safety, quality, and conformity. Although not technically a warranty, the duty imposed by the due care theory on manufacturers to avoid negligence and act as a reasonable person to protect consumers as to the design, materials, production, control, packaging, and information basically extends a promise of product safety and compliance to consumers in these related areas. However, the imprecision of measuring due care and the possibility of unknown dangers render it, like warranty theory, less than perfect.

Under the contractual theory, the duties of the sellers to consumers are contained implicitly or explicitly in the sales contract, which are the basis of the warranties addressed in this entry. Warranties were designed in part to remedy the imbalance of power between buyers and sellers in commercial transactions. Warranties also hoped to provide some stability, regularity, and reliability in contractual relationships.

However, the imperfection inherent in sales contracts and their guarantees, the continuing unequal bargaining and evaluative power between buyers and sellers (especially where there is lack of contract privity), and the ability of sellers to waive such warranties raised serious reservations about the adequacy of the contractual theory, especially as to product safety. These concerns in consumer protection contributed to the law of strict liability in tort, which holds manufacturers responsible for almost any injury resulting from defects in their products, even if they used reasonable care in all aspects of the production and distribution process. This presumably motivates the manufacturer to ensure product safety and consumer protection in ways that warranty law is unable.

These risks are even greater when international sales are involved. When dealing in overseas commerce, businesses must address the diversity in language, standards, and law among various countries. The CISG tries to provide some guidance for such sales agreements, including the expectation of warranties. Yet the parties must still take the time to address the social and ethical challenges created by these cultural differences between nations (especially since many countries have yet to adopt the CISG).

One ethical issue raised by these different international standards involves the requirement to give notice for nonconforming goods. Most economically and technologically advanced countries legally require notice to be given rather quickly (within a year at most), while developing countries find such short time periods very challenging, even unrealistic. The CISG addresses this difficulty by allowing examination of the goods for defects to occur within a period that is “practicable under the circumstances” and notice of nonconformity to be given within “a reasonable time” (not to exceed 2 years). This entry looks at the warranty of title, the implied warranties of merchantability and of fitness for a particular purpose, and at express warranties in general, especially as to consumer goods.

Warranty of Title

The sale of real property such as land, buildings, and other types of real estate generally comes with a warranty of title (leases come with a warranty for possession and use). A general warranty deed guarantees that the title to the property is free from any claims. If another party such as a bank has a lien against the property, then the seller will offer a quitclaim deed, which makes no assurances as to the title of the property and protects the seller from potential liability to the buyer if a claim is made on the property. Otherwise, the seller is liable as guaranteeing transfer of title free from any encumbrances. A special warranty deed ensures that no claims were made against the property while in the possession of the current owner. As to buildings, warranties may be made about the quality of materials, the adherence to building codes, and its ability to accommodate residents. The latter is an implied warranty of habitability that exists with any lease of residential property. The landlord is responsible for providing conditions necessary for living (e.g., water, heat, electricity, and safety requirements). Tenants usually withhold rent if said warranty is breached.

A warranty of title similarly exists under Section 2-312 of the UCC for the sale of goods (or a warranty for use and possession when a lease under Section 2A-211). Although the warranty is implicitly conveyed with the sale of the good, it is not identified as an implied warranty. The warranty may be disclaimed by a clearly communicated writing. However, a sheriff’s sale is an example when the events surrounding the purchase eliminate the warranty since title is known not to be guaranteed under such circumstances. A related warranty against infringement exists when a merchant who regularly deals in patents or types of intellectual property at issue sells such goods. Said merchant warrants that the goods are passed without any claim of a third person as to infringement on the property rights. For example, the seller of compact discs or of computer software warrants, unless otherwise disclaimed, that said goods are not violating copyright laws or rights of a third party.

Express Warranties

Section 2-313 of the UCC indicates that the seller creates an express warranty by any affirmation of fact or promise, description, or use of sample or model that relates to the goods and becomes part of the basis of the bargain. Therefore, the seller’s (or lessor’s) representations about the quality of a product, its uses, and whether it is new or used are all warranties. For example, representations about gas mileage create a warranty about a car’s performance in the sale of that good. Software licenses commonly contain express warranties about the software’s material conformity to certain specifications. However, the licensor often limits the warranty with problems surrounding installation, operation, transit, modification, and hardware.

Advertisements, free samples, models, and other sales materials may create express warranties. Samples come directly from the group of products to be purchased, while a model is a representation of the product when a specific sample is unavailable. International companies need to pay closer attention to their use of samples, models, and the like because they play a significant role in international sales and are given special recognition under the CISG (since communication challenges frequently exist when dealing with different countries and languages).

The specificity of the claim made is a major factor in determining if a warranty has in fact been manifested. Opinions, unless by an expert, do not create a warranty. Usually, express warranties reduced to writing cannot be waived by a contradictory disclaimer. The courts will try to read the express warranty and the disclaimer together so as to provide reasonable protection. Any inconsistency between the two is construed in favor of warranty protection. However, oral warranties may be waived by clear and conspicuous language under the UCC, and by less formal methods under the CISG.

Interestingly, insurance policies include important warranties and assurances made by purchaser (the insured) that serve as the basis of the contractual policy. For example, an insured makes promises about his age and prior medical conditions in connection with a health insurance policy or about the number of drivers and accident history in a car insurance policy. Insurance warranties are "affirmative" (representations about conditions at the time the contract was executed) or "promissory" (about anticipated events for the duration of the policy). Misrepresentations by the insured may allow the seller (insurer) to cancel the policy or to deny coverage, depending on the relevant laws protecting the insured's interest.

Implied Warranties

As stated earlier, implied warranties are not expressly represented in the written or oral sales agreement, but are created and imposed through application of law, usually the UCC. The two primary implied warranties that accompany the sale or lease of goods are the *implied warranty of merchantability* and the *implied warranty of fitness for particular purpose.* They do not apply to finance leases. As its name denotes, the warranty of merchantability, Section 2-314 of the UCC for sales and 2A-212 for leases, imposes on a *merchant* (someone who ordinarily deals in goods of the kind sold) the obligation to sell or lease goods that pass without objection, are of average quality, fit for the ordinary purpose of such goods, are of uniform quality, are adequately packaged and labeled, and conform to promises made on the label. Merchantable goods are of the type that are "honestly resalable in the normal course of business" (Comment 8 for 2-314(2)). The warranty occurs automatically on the sale, and need not be the basis for the bargain. Other implied warranties may arise from course of dealing or trade usage (under Section 2-314(3)(a)).

Most implied warranties can be waived orally or in writing, but must specify the word "merchantability" (and conspicuously) when disclaiming that specific warranty. Other warranties may also be waived by "as is" language or by a course of dealing that has usually disallowed said warranty. For instance, most directly downloadable software license agreements contain a warranty waiver or disclaimer that must be agreed to (by checking and clicking the box) before the software can in fact be downloaded.

The implied warranty for *fitness for a particular purpose* (which obviously differs from the *ordinary purpose* standard of the warranty of merchantability) applies when a buyer relies on the seller's skill or judgment in choosing a product for a particular purpose, and when the seller knows or should know the buyer's purpose. For example, a bike buyer explains how he needs a bike that can handle a certain type of mountain terrain. In recommending a certain type of bike, the store owner (whether or not he or she is a merchant) is held to an implied warranty of fitness for a particular purpose (of the bike's ability to handle mountain terrain). If the bike cannot actually perform as expected, the implied warranty for fitness for a particular purpose has been breached and the bike buyer could most likely return the bike.

This warranty may also be waived by a writing that says "as is" or "with all faults." However, an oral waiver is insufficient. Yet it is very important to remember that other countries and the CISG allow waivers, disclaimers, or limitations of warranties without the same formality of language and conspicuousness required by the UCC. Refusal (to a request from the seller), but not a unilateral failure, to examine the goods for defects waives implied warranties as to the defects that would have been observable on said inspection. Furthermore, a buyer who assumes a discovered and known risk is precluded from recovering damages resulting from such use. Although the seller may also limit certain remedies that the buyer has for breach of warranty, the seller may not limit or exclude the buyer's right to damages from injury or try to shorten the statute of limitations.

To avoid some of the problems of disclaimers, waivers, and misunderstood or deceptive warranties, the federal Magnuson-Moss Warranty Act of 1975 requires sellers of consumer products to articulate clearly and simply the coverage of the warranty, to identify it as full (guarantees repair or replacement) or limited, and to retain all implied warranties when providing a written warranty of any sort. For example, if a company provides a written warranty for its toys, the company cannot disclaim the implied warranties.

Internationally, the CISG, Article 35, contains similar warranty provisions: The seller must provide goods that are (1) fit for the ordinary purpose of such goods, (2) fit for any particular purpose made known, (3) possess the same qualities of a model or sample, and (4) packaged in the normal manner for such goods. The packaging is especially important in light of international deliveries. However, to find a breach, the CISG demands a more substantial deviation than what the UCC requires.

Conclusion

Express or implied warranties are promises about the characteristics or quality of property, goods, or services, on which the purchaser or lessee relies to secure receipt of conforming goods or to provide a remedy for breach of the agreement by the seller. Warranties, which exist under the UCC, CISG, and similar laws in other countries, combine with negligence and strict liability to provide protection to consumers as to product safety and contractual integrity.

—*Mark R. Bandsuch*

See also Consumer Protection Legislation; Contracts; Due Care Theory; Implied Warranties; Liability Theory; Negligence; Product Liability; Torts

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Wealth

Wealth is everything that can be exchanged for money, goods, or services. Originally meaning a state of well-being, it has come to signify material comfort. Thus, it includes material goods and rights to material goods or services represented by money or other financial assets. An individual's or a family's wealth is the dollar value of its assets minus its liabilities at any point in time. Income, on the other hand, is a flow of money. Thus, wealth can be thought of as accumulated income.

The oldest source of wealth was land, which for centuries was the basis of the great European estates. Because of its solidity and permanence, land can be handed down through generations and kept in a family more easily than other forms of wealth. The other great sources of wealth have been trade and manufacture. Today, wealth is generally represented not by land or other hard assets but by financial assets—the stocks, bonds, and other financial instruments that represent an individual's claim on society's resources.

Societal resources consist of anything that can be used to produce goods or services, including land and other natural resources such as minerals and forests; the talents and skills of the population, or human resources; and capital, or man-made resources such as factories and warehouses. Society employs these resources to create wealth; the more efficiently and fully a society uses its resources the more wealth it will create. Because human wants exceed available resources, however, every society must decide what goods and services to produce and how to distribute the production among its members. Therefore, societal well-being may depend as much on the distribution of wealth as on its production.

Historical Attitudes Toward Wealth

The ancient world considered wealth both necessary and good. It was necessary for independence and leisure and thus for freedom. Wealth signified heroism and virtue; the Greek poet Homer depicted the wealthy as deserving their riches through divine right or courage in battle. The poor aroused little sympathy. Their lack of wealth signified their inferiority and lack of virtue.

As men began to accumulate wealth through trade rather than through birth, the view arose that wealth corrupted, at least in the hands of the wrong people. The Bible condemned the greed and vanity of the rich and held that those who gave of their wealth to the poor would be rewarded in the hereafter. Yet the Bible also says that riches are a sign of God's blessing.

Such ambivalent attitudes toward wealth have endured in the modern world. With the rise of capitalism, wealth became a sign of industriousness. The early church disapproved of the business spirit and of profit as the goal of a vocation. This disapproval was overcome by Calvinism, at least in its later stages, which approved of acquisitiveness and the capitalist ethic. In 1899, Thorstein Veblen wrote that the possession of wealth confers honor and that what previously had been evidence of efficiency had become a meritorious thing in itself. Today's society maintains this schizophrenic view of wealth, viewing it alternatively as a sign of honor, virtue, and good breeding and as an unjustified hoarding of society's resources.

Distributive Justice

According to Aristotle all men agreed that in a just society the distribution of wealth must be based on desert. They disagreed on what constituted desert: Criteria included free birth, noble birth, and virtue. The debate continues today, although some now deny that desert is even relevant.

Many observers believe that ideally society's resources should be distributed equally. They argue that since people are morally equal and entitled to equal political rights, they should also receive equal economic shares. But even these observers recognize that enforcing an equal distribution of wealth would require constant and overbearing state intervention. Therefore, they assert that inequalities must be based on some relevant ethical principle and that, whichever principle society adopts, every citizen is entitled to a minimum share of society's wealth sufficient to ensure his or her health and welfare.

Some argue that a market economy results in a just distribution because it allocates wealth according to ability and effort. Thus, a person's wealth is determined by his or her contribution to society. Since in a market economy the value of one's contribution is the price paid by a willing buyer, people's material rewards are based on their value to others.

Yet all people depend on the vast societal infrastructure that is often taken for granted—security, roads, education, and more. Many observers believe that it is impossible to isolate the contribution of any individual; society's resources are a product of a complex and interdependent economic system. Moreover, they add, in the absence of the community, the welfare of all would be so low that no individual has a moral claim to a substantial portion of those resources. Given this reality, the very notion of an individual's "property" is a societal construct, and no one can legitimately be said to "deserve" his or her share.

Still others, notably John Rawls, argue that, because people have done nothing to earn the natural capacities they are born with, distribution based on ability has no moral basis. Moreover, effort is influenced by one's natural abilities and the alternatives open to him or her, which are not distributed equally. The more able are also more likely to pursue success. Consequently, effort is also a morally insufficient basis on which to distribute society's wealth. Rawls, for one, ultimately rejects the notion of desert. He argues that, if people formed a society without knowing their place in it, they would be risk averse: They would create a society in which the poorest people (which could include them) were better off than in any alternative society. Rawls therefore concludes that departures from equality in the distribution of resources are justified only if they help the least well-off.

Libertarians, most prominently Robert Nozick, also deny the relevance of desert, but from a much different perspective. They reject any theory of distribution that relies on a particular end state; that is, that bases the justness of a distribution on a given allocation. Instead, they focus on process: A distribution is just if it arises from another just distribution by legitimate means. Therefore, the possession of wealth is just if the wealth was acquired originally by just means or, after a just acquisition, by one or more voluntary transfers.

Others deny that it can be demonstrated that any wealth was originally acquired by just means. Writing in the 17th century, John Locke based the right to property on the mixing of one's labor with the land. Today, some argue that this conception, though appropriate for a simple agrarian society, does not hold in a complex modern economy in which the value added by any individual's labor cannot be isolated. Others argue that, if property is traced back far enough, it will be discovered that almost all property rights originated through force. Therefore, voluntary transfer cannot serve as a moral basis for the possession of wealth.

Inequality

Capitalist economies generate great disparities of wealth. Although wealth was distributed fairly evenly in early America, with the rise of industrial capitalism in the 19th and early 20th centuries, inequality increased dramatically. After a decline from about 1930 to 1950, inequality began to rise again and increased steeply during the 1980s and 1990s. In 1976, the wealthiest 1% of the population owned 20% of the nation's wealth. By 1999, the top 1% had doubled its share to 40% and owned more wealth than the bottom 95%. In 1997, the top 10% of the population owned 73% of the wealth. The United States had changed from one of the most egalitarian countries in the industrialized world to the most unequal.

Many observers believe that inequality has value because it provides an incentive to produce. If differences in contribution did not result in differences in reward, people would have little reason to assume risk or to put forth exceptional effort. Inequality, therefore, benefits everyone by increasing growth and economic output.

Others argue that inequality denies the moral equivalence of people and leads to the breakdown of social order if too many people believe they have not received their fair share and therefore believe they have little stake in society. Although some assert that moral equality requires only equal opportunity, others argue that extreme inequality makes it impossible to sustain the belief that equal opportunity exists. They argue that extreme inequality destroys incentive because people believe that regardless of their efforts they will not prosper.

Inheritance

Inheritance poses the starkest contrast to an ethic of desert and the greatest challenge to an ethic of equality. Critics of inheritance argue that because the recipients have done nothing to earn their bequests, they have no moral claim to them. Since inheritance is unrelated to contribution it also does not create incentives. Even those who believe that society's wealth is distributed according to individual contribution acknowledge that inheritance is the great exception. Therefore, many believe that the state has a greater right to seize inherited wealth through confiscatory estate taxes than to redistribute wealth through an income tax and social programs. These same critics assert that inheritance bears more responsibility for the unequal distribution of wealth than any other institution. According to this view, inheritance of great wealth provides an unfair advantage to a small number of individuals and perpetuates the concentration of wealth through generations.

Others argue, however, that the right to property necessarily implies the right to direct its disposition after one's death. The libertarian view emphasizes that since inheritance is the result of a voluntary transfer of assets, the concentration of wealth that results from inheritance is just. Because libertarians deny the ethical relevance of any particular distribution, they deny that inheritance presents a special case.

John Stuart Mill charted a middle course. Like today's libertarians, he believed that the essence of property was the right to exclusive possession of anything a person either produced or received by gift or fair agreement from others. He argued that without the power of bequest ownership was incomplete. Yet Mill believed that by permanently concentrating fortunes in few hands, inheritance conflicted with the interests of society. Therefore, he proposed that people should have the power to dispose of all their property by will but that the state should limit the amount any individual could inherit.

Wealth and Democracy

Inequality poses particular challenges in a democracy, in which political power is dispersed among the people rather than concentrated in an individual or a small group. Ideally, all citizens in a democracy are equally able to influence decisions that affect their lives. The wider the distribution of wealth, the greater the number of people who believe they have a stake in their society and the broader the political base for democratic institutions. Great concentration of wealth challenges the belief that people have a real say over the affairs of state and that democracy exists to serve the broader populace.

James Madison wrote that the unequal distribution of property was the greatest source of faction and animosity in politics and that the most important element of a well-constructed union was its tendency to control the violence of faction. Many believe that the great power of concentrated wealth puts today's democracy at risk. In 2000, the average winner of a U.S. Senate election spent almost $8 million. The expense of campaigning requires politicians to solicit funds from and therefore become beholden to wealthy donors; fewer than 1% of the population donates more than $200 to political candidates, while half of donors have incomes of at least a quarter million dollars per year.

This system leaves many citizens believing their interests are not represented. Nevertheless, some argue that the relationship between democracy and wealth is uncertain. They note that some relatively egalitarian societies have been undemocratic, while some democratic regimes have withstood even significant concentration of wealth.

The Responsibilities of Wealth

Because the community plays a vital role in the accumulation of wealth, some argue that those of great wealth owe society a special responsibility. American industrialist Andrew Carnegie was the most prominent spokesman for the view that, after providing moderately for themselves and their families, the wealthy should consider all additional wealth to be held in trust for the benefit of the community. Carnegie further held that the wealthy must devote their wealth to the community during their lifetimes, since it was no sacrifice to bequeath wealth at death.

Others do not begrudge the rich their wealth during their lifetimes, but argue in favor of high or even confiscatory estate taxes to ensure that great wealth is ultimately used to benefit the community. The appropriate level of the estate tax has been a perennial political issue in the United States. Not all the wealthy oppose high taxes; some of the country's richest individuals have lobbied to keep the estate tax in place.

—Barry Bennett

See also Desert; Justice, Distributive; Nozick's Theory of Justice; Property and Property Rights; Rawls's Theory of Justice; Redistribution of Wealth

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Wealth Creation

Wealth is the ownership of assets that are valuable to satisfy human needs and wants. To create wealth is to produce or to cause an increase in these valuable assets, so that the original value is sustained, the factors of production continue in existence, and there is a surplus left over.

The complex and dynamic nature of human needs means that there are many forms of wealth that may be created. To facilitate communication and decision making about wealth creation, therefore, wealth is usually measured in terms of money. Monetary units and currency, however, are not themselves wealth. They represent claims on the things of value that may be owned in exchange for money. This difference between money and wealth is experienced by people who may hold a constant amount of money in an economy that goes through an inflationary period. Their wealth erodes because they can buy fewer items of value as prices increase, although they may have the same amount of money over the inflationary times.

Wealth creation is a rational activity when the benefits of increasing valuable assets exceed the costs of doing so, a condition that takes into account the life of the assets and the time value of wealth discounted at an appropriate interest rate. Typical activities that may satisfy this condition include search, discovery, and exploitation of new productive resources and innovative processes. A society that enables these entrepreneurial activities creates wealth and improves the quality of human life.

Wealth Creation as Rational Economic Action

Valuable assets may be consumed in the present, or they may be stored for future consumption, or they may be invested to create an additional quantity of valuable assets called wealth. Wealth creation is a rational economic activity when the benefits of increasing valuable assets exceed the costs of doing so. This approach to wealth creation implies a choice, and the most often used economic method to make this choice is a cost-benefit analysis that compares the investment costs with the value of wealth likely to be created.

Cost-benefit analysis only gives incomplete guidance, though, because benefits and costs may not be distributed fairly, and the ethical dimensions of wealth creation are not likely to be captured in its measurement techniques. More than 2,000 years ago, for example, the Greek philosopher Aristotle distinguished between pecuniary and socially desirable goals of wealth creation and warned that if money and profit are the only goals then there is no natural limit on greed and corruption.

Important considerations for the ethics of wealth creation include the economic system with which a society creates wealth, the sustainability of these activities for use by future generations, and the justice in the distribution of the wealth that is created.

Economic Systems for Wealth Creation

One reason that productive assets are valued is that they are scarce, and people who believe they can create the most value from them have an incentive to bid up their value until the cost absorbs all the wealth that can be created from them. A system of voluntary exchange contracts between self-interested buyers and sellers informed by market prices is one economic system that enables this wealth-creation process. This market system to create wealth depends, in part, on the trustworthiness of the exchange parties, on government regulations to maintain stable market functions, and on judicial protection for contracting. Advocates of market systems argue that over the long term it is the most efficient path to wealth creation. The failures of the market system to create sufficient wealth in all sectors of society, however, have led some to seek alternative economic systems.

Socialism is an alternative system of wealth creation based on public policy control of productive assets. Rational decision making for wealth creation under central planning forms of socialism, however, is hindered by the planners' deficiency of requisite information about value preferences and prices. In addition, socialism limits individual freedom to pursue a personal path to create wealth. Market socialism proposes to remedy these deficiencies by preserving competitive enterprises empowered to negotiate and enter into voluntary market exchanges, and combining the incentives and information of this marketplace with a socialist system of banking and capital allocation driven by public policy choices for investment.

Issues of Sustainability of Wealth Creation Activities

Some argue that current wealth creation activities are justified only when they do not exhaust the productive resources for future generations. For example, wealth creation activities that require petroleum products ought to consider the rate at which the world's supply of oil is being used up. An economist might argue that the rate of change in the price of exhaustible resources relative to the cost of usage is all the information needed to determine the appropriate rate of depletion. In this economic analysis, if the value of the exhaustible resource over time is rising more quickly than the cost to put it into use, then holding the resource "in the ground" can be an excellent way to create future wealth. Conversely, it may be best to exploit them quickly if the usage cost is rising at a faster rate. In this latter case, the economist notes that the faster depletion increases the resource scarcity, and the laws of supply and demand lead to higher prices offered by buyers that induce more supply than would be economically feasible at the lower price.

This economic analysis of prices and costs for exhaustible resources over time assumes that the appropriate values placed on them by future generations can be accurately forecast by current decision makers. This assumption may be optimistic at best and self-serving at worst. Accordingly, some suggest that the fair way to create wealth today from exhaustible resources is to deplete them at a constant and sustainable rate over time. This approach may substitute one type of myopia for another, however, because we cannot know today what innovations, changes in taste, demographic conditions, and resource discoveries will prevail in the future. For example, we have the English expression "not worth his salt," and the word "salary," because in the past edible salt was a valuable, scarce, nonrenewable resource and a form of wealth.

Issues of Justice in the Distribution of New Wealth

Pareto equilibrium and Rawls's theory of justice are two philosophical approaches to determine the fair distribution of wealth. A Pareto equilibrium framework identifies fairness in terms of three distributive consequences of wealth-creating activities—positive consequences that improve wealth, negative consequences that harm wealth, and neutral consequences with no meaningful impact. In this framework, an unfair action is one that has a negative consequence for some who cannot be compensated to at least a level of neutrality.

Rawls's theory of justice refines this formulation to impose a veil of ignorance over the decision to act so that a just wealth creation activity is one that is approved by someone who does not know place in the outcome. Such a condition of ignorance does not by itself define the moral rules that guide decisions to create wealth. For example, a free decision maker under a veil of ignorance may reasonably define ethical wealth creation as using assets as efficiently as possible, or creating the most wealth possible for the greatest number of people, or distributing newly created wealth as evenly as possible across all members of society. In fact, the freedom to choose how to pursue wealth creation is itself a form of liberty, a moral good that is valued by many.

The pursuit of wealth creation has not always been a freedom available to all. Historical institutions and old laws, though they may no longer govern society today, may in the past have served to either enable or hinder wealth creation and keep certain populations "in their social place." For example, the rate of wealth creation within minority populations of some societies today, such as African Americans in the United States or the Chinese in Indonesia, may be a function of past discrimination and institutional biases that affect historical paths of creation, distribution, investment, and inheritance. To address these historical obstacles to fair and just wealth creation today, some public policy programs to redistribute wealth may be appropriate, such as affirmative action programs in the United States.

Redistributive public policy is a form of social engineering, an intentional intervention in social processes to bring about patterns of activity and wealth creation preferred by public policy on behalf of the society. Social engineering gives all members of society who are interested in protecting and creating their wealth a stake in the public policy process. In political systems with social engineering, powerful stakeholders usually attempt to capture the public policy process for their own advantage. Diligent monitoring is required to avoid corruption as well as tyrannies of the majority or the wealthy.

Just as some minorities have been disadvantaged in the wealth-creation activities within their societies, so too some countries are disadvantaged in the global economy's dominant institutions that create wealth through world trade. For example, many governmental ministers of developing countries, as well as many spokespersons for nongovernmental organizations (NGOs), have criticized the World Trade Organization (WTO) for using tariffs, subsidies, and regulations that protect the wealth of developed countries by creating obstacles to exports from developing countries. Some who protest that wealth creation in a global economy threatens wealth creation in local economies have used civic disruption, mayhem, and violence to stop the activities of the WTO. In response, the WTO, whose professed mission is to lower barriers to trade and facilitate a global economic approach to wealth creation, often meets in remote locations that are not easily accessible to protestors.

Noneconomic Views of Ethical Wealth Creation

There is robust guidance, conversation, and debate within religious and faith-based institutions seeking to add to our understanding of the ethics of wealth creation. According to one popular English translation of the Koran, "The semblance of those who expend their wealth in the way of God is that of a grain of corn from which grow seven ears, each ear containing a hundred grains." One thread from Western religious thought is that for human beings to fully realize that they are created in the image of God implies that they are meant to be virtuous creators from the fruits of God's creations. Criticism of wealth creation as a myopic pursuit of profit is also reflected in modern spiritual or religious definitions of wealth creation. One important outcome from these discussions is the idea of social entrepreneurship, the creation of new business activity to direct our passions to serve and transform society.

Conclusion

A largely economic understanding of wealth creation has been influential in business and society. Our understanding of the ethics and morality of wealth creation arguably is well developed but less influential. If religious injunction or common fear of a future world of depleted resources can lead managers to cooperate with sincere integrity and social responsibility, then moral as well as economic wealth is more likely to be created.

—Greg Young

See also Affirmative Action; Aristotle; Capitalism; Christian Ethics; Commensurability; Cost-Benefit Analysis; Doha Development Round of 2001; Inflation; Islamic Ethics; Justice, Distributive; Market Socialism; Nongovernmental Organizations (NGOs); Pareto Efficiency; Rationality; Rawls's Theory of Justice; Redistribution of Wealth; Religiously Motivated Investing; Smith, Adam; Social Entrepreneurship; Socialism; Stakeholder Economy; Transaction Costs; Utility; Wealth; World Trade Organization (WTO)

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Weber, Max (1864–1920)

Max Weber was one of the leading scholars of his time in Germany and helped found modern sociology. He thought of sociology as a comprehensive science of social action, and his focus was on the subjective meaning that humans attach to their action and interactions within specific social contexts. His system of thought is one in which material interests and ideas are in constant interaction with each other. Thus, he wrote *The Protestant Ethic and the Spirit of Capitalism* in part to counter the prevailing Marxist view of dialectical materialism and wanted to show how the ideals and values of a particular religious system also entered into the shaping of history.

Weber sought to explain why the Industrial Revolution took place primarily in countries that were primarily Protestant in their religious orientation. In doing so, he was not denying material forces but only isolating the religious elements that he thought helped spur industrialization. Thus, he focused on the idea of the calling from Lutheran theology and the notion of predestination from Calvinism that he argued contributed to what he called the spirit of capitalism, the motivations and attitudes that were necessary for rapid industrialization to develop. People were called to work hard and do their best at whatever stations in life they found themselves. And to prove they were one of the elect, they were motivated to make a success of themselves by accumulating wealth and using it to create more wealth. Capitalist accumulation thus came from these aspects of the Protestant religion.

There has been much debate about this idea, but nonetheless, the Weber thesis has some explanatory power relative to the rise of capitalism. Weber also wrote extensively about the rise of modern bureaucracy in both the public and the private sectors of societies. He considered bureaucracy to be a particular case of rationalization applied to human organization. Such bureaucratic coordination of human action was the distinctive mark of modern social structures. Bureaucracies, Weber believed, are efficient goal-oriented organizations designed according to rational principles. This organizational device makes large-scale planning for the modern state and modern economy possible. The key to understanding the modern world, he argued, lies in the consequences of the growth in the power and scope of these organizations. The fact that individuals have limited responsibility and authority within an organization makes it unlikely that they will raise questions regarding the moral implications of the overall operation of the organization.

—Rogene A. Buchholz

See also Protestant Work Ethic

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Welfare Economics

Welfare economics is the branch of economics that studies how individuals and societies exchange goods and the properties of the resulting outcomes. As such, it is concerned with the well-being of individuals and societies. Analyzing exchange and outcome is done through various means, including if the process needs to incorporate rights and duties for participants and whether or not outcomes are seen to be equitable or just.

The broad scope of the subject and the difficulties in defining concepts such as well-being and judging equity causes welfare economics to cut across several disciplines, including history, philosophy, political science, and sociology. Consequently, there is a long and rich literature associated with the topics. Moral philosophers, from Aristotle, the Scholastics, Hobbes, Nozick, and Rawls, have also focused on what constitute the properties of a "good" or just society and how such an outcome might be reached.

In economics, welfare economics originates in the claim by Adam Smith in *The Wealth of Nations* that self-interested individuals, acting in competitive markets, will reach an outcome that is a social optimum. Smith's evocative use of terms such as "the invisible hand," "natural law" and policy prescriptions of laissez-faire, and the paradoxical vision of people being led "as if" by an invisible hand to do a larger social good while they were merely trying to do well for themselves has been a cornerstone of classical and later neoclassical economics. His "invisible hand" as deus ex machina has also been mistaken by some to mean that Smith believed that there was a supraindividual purpose or design (teleogical explanation) to the individualist-based market system.

Smith's claims for markets and self-interest echoes that of the French Physiocratic school that coalesced around François Quesnay in the mid-1700s and with whom Smith had personal contact. Physiocratic doctrine stressed the interrelations of economic sectors and the self-governing and balancing flows of expenditures and resources among the sectors. The Physiocrats identified land as the source of all wealth, natural law as the source of motion in the system, and believed that governments should follow a policy of laissez-faire. This was symbolized in Quesnay's *Tableau Economique*, a circular-flow diagram anticipating the modern-day macroeconomic approach to national income and expenditure analysis.

Others have claimed that Smith's system, while conferring rights to voluntary exchange requires of us no duties (e.g., of honesty, probity). However, a reading of Smith's *Theory of Moral Sentiments* relying as it does on his *impartial spectator* representing society's interest by limiting individual's opportunistic behavior, and his view that competition among sellers would be a natural constraint on opportunism, should at least absolve Smith—if not all his later followers—of that charge.

For other schools of economic thought, for example, the Marxists, Smith's proposition has been viewed as hostilely as they view private property and the competitive process itself. The competitive exchange process, as Marx saw it, is based on asymmetric power and rights between the labor and capitalist classes. Still other schools of thought, for example, the Austrian School, have questioned the notion that there is enough knowledge available to allow individuals to home in to an end state of rest or systemic balance, called an equilibrium. Thus, in their view a social optimum, even if it exists, will not be reached in finite time. Consequently, they stress the subjective characteristics of the process individuals use to exchange and allocate goods.

Welfare economics uses microeconomic, or individual-level, techniques to determine the economic efficiency of outcomes. It seeks to find those outcomes that maximize social welfare by examining the economic activities of the individuals that comprise society. With such wide-ranging goals and scope, welfare economics includes the study of individual motivation, social goals, modes of organization, and operation that will potentially lead to coordinated social states. The field also considers the conditions under which social states might be compared and ranked in order that an optimum might be found.

Ranking criteria have been proposed by many, including the utilitarians following Bentham's principle of "the greatest happiness for the greatest number." For computation purposes, this requires making cardinally additive interpersonal utility comparisons to judge a policy change that redistributes goods. Critics of this approach attack the possibility of making interpersonal comparisons, thus attacking the idea of being able to compute a single number that represents the "greatest good." They ask, "If one person gains and another loses from a change, how can one meaningfully compare a gainer's gains with a loser's losses and sum the two effects?"

Neoclassical economists, following Pareto, relax the requirements that utility is interpersonally comparable and cardinally measurable, but claim that social optima can be found by using Pareto's efficiency criterion. A Pareto-efficient outcome is a distribution of goods such that any change away from it results in at least one person being made worse off. As highlighted by Wicksell, there are an infinite number of Pareto optima, with the social optimum being a proper subset of that set. Thus, following a search for a Pareto optimum is not the same thing as finding a social optimum.

Reflecting the broad scope of welfare economics, methodological approaches to the topic have ranged from the highly mathematically abstract to the literary and, at times, almost poetic. Meanwhile, the ends to which welfare economics has been put have ranged from using mathematical techniques to complete theoretical claims made by—or assumed to have been made by—earlier thinkers, for example, Smith, to practical issues in welfare economics dealing with assessing the outcomes of particular economic policies.

The Goal of Theoretical Welfare Economics

The goal of theoretical welfare economics initially was to formalize and examine the claims made for self-interest as the law of motion and competitive markets and as the system through which a social optimum could be reached. The focus was on answering the following three questions:

1. Under what conditions will individuals, operating in competitive markets, reach an outcome that maximizes the common good?
2. Can any desired distribution of income be reached by a competitive process?
3. Is there a way to aggregate over individual preferences to arrive at a societal preference ordering, consistent with the underlying individual preferences, assuring that a social optimum has been found?

The First Fundamental Theorem of Welfare Economics

The first theorem states that self-interested, utility-maximizing individuals operating in perfectly competitive markets will reach a Pareto optimum. The stimulus for proving this theorem lies in the writings of Smith and is referred to as the invisible hand theorem. The theorem itself was rigorously proven by Lerner, Lange, and Arrow in the 20th century using Walrasian general equilibrium techniques.

Proving the first theorem requires calculus, assuming both that all individual's preferences and all firm's profit functions are smoothly (i.e., no kinks) continuous and do not increase without bounds. Under these restrictions, which deny external effects, public goods, informational asymmetries, and any other types of market imperfections or failures, the first fundamental theorem may be proven.

The idea of searching for "common good" or a social optimum is changed to satisfying the Pareto efficiency criterion. This is not the same sense in which Smith viewed the concept of the common good. For example, Smith referred to "the annual revenue of society" as the aggregate value that competition would maximize. This is a construct closer to today's gross domestic product (GDP) than it is to Pareto efficiency. Smith's construct, and the definition of GDP, corresponds more closely to the idea of the size of the nation's output, where a larger output is preferred to a smaller one.

Pareto efficiency may hold for any given GDP, not just the largest conceivable given the available resources. As such, proving Pareto efficiency says very little about the size of the national output, only that it is being produced most (Pareto) efficiently.

Smith's invisible hand is actualized through the price system where changing prices alter incentives and coordinate self-interested behavior to bring about a state of balance or equilibrium, where the quantity supplied equals the quantity demanded, in each market. Each producer faces the same prices, hence—motivated by profit maximization—seeks to produce where marginal cost equals price, and the fact that all producers of a given good face the same price equates marginal costs across firms, thus assuring efficiency in production. Freedom of entry and exit assures that above-normal profits cannot persist in any industry in the long run.

Individual buyers face those same output prices and maximize utility subject to them, equating marginal rates of substitution across consumers. Given that producers and consumers face the same output prices, marginal rates of technical transformation in production are equated to marginal rates of substitution in consumption.

The first fundamental theorem, though mathematically true, and viewed by neoclassical economists as a tour de force, has been heavily criticized on a multitude of grounds. The criticisms include denial of obvious cases of market failure (e.g., monopoly); some of the assumed "givens," such as consumers' preference functions, may themselves be manipulable through advertising by firms or by social pressures, so individuals may not know their own self-interest; markets are not in equilibrium and a tendency toward equilibrium—if that is what real-life haggling over prices and quantities is achieving—does not imply a monotonic (i.e., always utility and/or profit improving) "march" to equilibrium, mistakes can be and are made in real-life trading and production; not only are tastes fluctuating, but technologies are not fixed; there are external effects, both in consumption and production rampant in real economies that cause observed market prices to deviate from their correct values; the existence of public goods, which even Smith recognized and argued justified a role for governments, is ignored or assumed away in the rigorous proof of the first theorem.

Some of these criticisms are well known and have been addressed. For example, the theorists who proved the first theorem did not suggest that the abstract and simplifying modeling necessary to achieve the proof described anything other than a logical construct that is distinct from and not to be confused with any real-world economy. However, some of the underlying assumptions of individual and business behavior used to prove the first theorem should still be of great interest to ethicists and social scientists. While real-world economies are unlike the theoretical construct used to prove the first theorem, claims of self-interest, profit maximization, and voluntary exchange, necessary for the proof, are also topics of broader concern in social and ethical studies.

In the case of external effects, Pigou suggested using taxes and subsidies to reflect the full social costs and benefits (the cost or benefit not just to the individual taking an action but inclusive of costs imposed or benefits conferred on others) of these activities. Thus governments might assist markets in finding the correct prices. Coase advocated use of the common law of nuisance, recourse to lawsuits, to internalize external costs, thus obviating the need for the government to play its "pricing" role; however, in such a case, government may still have a "Smithian" role to play in the provision of the legal system, as a public good defining property rights and adjudicating disputes.

Lipsey and Lancaster in a seminal paper showed that in the presence of market failure—for example, a monopoly in one industry—changes toward more competition (e.g., deregulation) in other industries may not be optimal. This is known as the theory of the "second best," which questions, at a theoretical level, the policy relevance of the first theorem when its advocates interpret it to mean that more competition is always better than less.

The First Fundamental Theorem of Welfare Economics and Fairness

However strong the above criticisms, perhaps the most significant criticism of the first theorem is that it ignores the distribution of output, the "Who gets what?" question. Competition may be shown under the restrictive assumptions given above to achieve a Pareto-efficient allocation, but there are many such allocations, each with its own size and distribution of output. The first fundamental theorem is silent about the "fairness" (equity) or unfairness of any particular allocation. Critics of the first theorem—as indeed earlier critics of classical economics—were quick to point out that any given Pareto-efficient allocation reached may imply zero (or even negative) prices for some resources (e.g., no income for some labor). Depending on one's beliefs in what constitutes fairness, one may agree that a competitive process may lead to a Pareto-efficient allocation without believing that this is a necessary virtue of competition especially if the competitive process leaves some people with nothing or next to nothing. This result clashes with many ideas of fairness, most obviously "to each according to their need" criterion.

The literature on fairness is immense, spanning almost every known field, discipline, and time period. Neoclassical economics, being a subset of positive economics (the "is" of the is-ought dichotomy), has somewhat self-consciously, but purposefully, steered clear—with John Neville Keynes early on and later Milton Friedman at the tiller—of making pronouncements about fairness almost using this as a bright-line distinction between what is and what is not to be considered "economics."

The favoring of positive economics leads many economists away from considering normative concerns about any given outcome. Positive economics would have us describe "what is" about the outcome, the technical details on marginal rates of substitution and prices, for example, but not to comment on the rightness or wrongness or fairness or unfairness of how much output each person receives. One reason for this prescription to do positive economics is to avoid the wide and deep chasm harboring the demands to discuss and define "fairness" requiring interpersonal comparisons that economic theory may not be robust enough to support.

Alternative approaches to neoclassical economics stress the issue of fairness, not only of outcomes but also of systems—including the system of private property and exchange itself, with Karl Marx and followers the obvious example. Approaches that rely on nonmarket mechanisms typically involve a command-economy approach, where a central authority makes the allocation decisions or calculates the prices at which people and firms produce and trade so that outcomes are considered to be fair under some chosen definition of fairness, for example, an equal distribution of output.

One concern with this approach is that disincentives to work and produce may cause the size of the aggregate economic output to shrink to such a degree that an equal share of a smaller output is not as large as an unequal (e.g., the smallest) share of a larger output. Should this occur it would violate the concept of fairness as developed by Rawls. Another concern with this approach is the arbitrary nature of who gets to choose what is fair and unfair.

The Second Fundamental Theorem of Welfare Economics and Fairness

Still other approaches within economics to address fairness rely on the market mechanism augmented with lump-sum transfers (or side payments), calculated and imposed by a central authority, which achieves the desired distribution of output. This approach is encapsulated in the second fundamental theorem of welfare economics stating that almost any Pareto-efficient allocation may be achieved through the competitive process after the correct lump-sum taxes and transfers have been imposed on individuals and firms. The practical basis of the second theorem has been attacked (Von Mises, Hayek) on the grounds that successfully implementing it in practice requires more information and time than any one authority is capable of acquiring and processing.

A deeper question surrounding the second theorem is which tool should we use to decide which distribution we, as a society, desire? Even if the decision is made in a democracy by a central authority/legislature or bureaucracy, voting usually plays a role in choosing who the bureaucrats and/or authorities are. The type of voting most commonly used in a democracy is majority voting. Majority voting can be inconsistent and may lead to voting cycles. This "voting-paradox" result has been well known since the late 1700s (in Condorcet), refined and generalized subsequently, and weakens any suggested political foundation for judging among different outcomes. The voting paradox may prevent agreement on a unique outcome via majority voting.

Another concern with lump-sum transfers is that while it may be possible to achieve a preferred distribution through transfers, will in fact those transfers take place? This concern highlights current debates on issues such as "free trade," where the theory of comparative advantage shows that gainers from trade can compensate losers such that no one is worse off and at least one person is better off after trade opens up. However, the theory of comparative advantage does not speak to who will be taxed and to whom the transfers will be given. The concern is that the gainers will keep their gains and the losers receive no compensation.

The Third Fundamental Theorem of Welfare Economics and Fairness

The third fundamental theorem suggests another alternative to markets, authority, and voting, and that is the construction of a social welfare function that aggregates the preferences of all individuals into a social welfare function. The social welfare function would then be used to arrive at the optimum allocation of output. This harkens back to Bentham's "greatest good" idea. In work by Bergson and Graaff, it seemed conceivably possible, but highly unlikely, that a nonarbitrary social welfare function could be found in practice that would help resolve the distribution problem.

Arrow's work then showed the logical impossibility of constructing such a social welfare function from individual preferences when the following "reasonable" conditions hold: (a) universal domain, (b) Pareto consistency, (c) independence from irrelevant alternatives, and (d) nondictatorship. Universal domain refers to the property that the social welfare function must include all the individual orderings that are logically possible; Pareto consistency says that if all individuals individually prefer alternative A to alternative B, then A must be socially preferred to B; independence requires that under two alternative preference profiles, if element A is preferred to element B in both, then A remains preferred to B no matter if the ordering of a third element (the "irrelevant" element), C, is reversed in the two preference profiles; finally, nondictatorship implies that everyone's preferences matter, but no one person's preferences can matter too much.

Since Arrow's "impossibility proof," there has been a wealth of research, but his conclusion that it is logically impossible to aggregate the preferences of heterogeneous individuals so that unique and well-ordered social preferences result, has not been reversed. From this vantage point, we reach the dismal conclusion that the attempts to compare economically the social value of different distributions of output lead to paradoxes and impossibilities that yield no clear theoretical answers on which policies necessarily improve society's lot. When everyone's preferences matter, it is impossible using economic theory alone to tell whether or not a policy change makes society better off. This result should make us suspicious of those using economic theory alone when making such claims and should also prompt us to expect the same rigor and self-examination of any social scientist or public policy advocate when making similar claims for policy changes based on their discipline.

—David L. Hammes

See also Arrow, Kenneth; Bentham, Jeremy; Coase Theorem; Common Law; Competition; Consumer Preferences; Economic Efficiency; Economic Incentives; Economics of Well-Being (Post-Welfarist Economics); Equilibrium; Externalities; Fairness; Friedman, Milton; Hayek, Friedrich A.; Is-Ought Problem; Invisible Hand; Justice, Distributive; Marginal Utility; Nozick's Theory of Justice; Pareto Efficiency; Perfect Markets and Market Imperfections; Private Good; Public Good; Rawls's Theory of Justice; Resource Allocation; Self-Interest; Side Payments; Smith, Adam; Social Costs; Utility

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Well-Being

There seems to be a convergence of opinion among researchers in the area of well-being that the notion of well-being can be construed in terms of happiness, life satisfaction, and absence of ill-being. *Happiness* refers to an affective state that involves positive and negative affect. This affect derives from positive and negative emotional reactions we experience from life events. Happiness researchers make the distinction between short-term happiness and long-term happiness. Short-term happiness is mostly influenced by environmental factors, whereas long-term happiness is more dispositional.

Life satisfaction involves cognitive evaluation of one's life. Life satisfaction is a result of comparison of one's current life situations or accomplishments against certain standards of comparison—one's ideal life, expectations of personal utility, individual goals, values, needs, opulence, and the lives of significant others. Also, life satisfaction is a cognitive evaluation of happiness in relation to salient life domains. For example, people may infer that they are highly satisfied with their lives if they judge themselves to be happy in work, family, and social life, and given that these life domains are important to them.

The *absence of ill-being* reflects the health perspective of well-being. This perspective posits that absence of ill-being is a necessary but not sufficient condition of subjective well-being. In other words, people cannot experience high levels of happiness and life satisfaction if they are unhappy with their health. Satisfaction with health is a prerequisite to overall happiness and satisfaction with life.

In the following section, we will focus on the effects of organizations on people's well-being. Organizations affect people's well-being (happiness, life satisfaction, and absence of ill-being) in at least two major ways, work and consumption. In other words, people assume certain jobs in organizations, and their well-being is significantly affected by these jobs and employment circumstances. Organizations also affect people's well-being by offering consumers goods and services that help consumers satisfy their needs. As such, we will describe how organizations affect well-being in relation to two important life domains, namely, work life (i.e., employee well-being) and consumer life (i.e., consumer well-being).

Employee Well-Being

Employee well-being, also called quality of work life (QWL), refers to the degree of satisfaction and contentedness an employee experiences with respect to his or her job and the overall work situation. Much research on QWL has linked specific organizational characteristics and programs to concepts such as employee life satisfaction, happiness, and absence of ill-being. We will highlight some of the important organizational characteristics and programs found to enhance employee well-being.

Employee Well-Being Can Be Enhanced Through Ethical Corporate Mission and Culture

Research has shown that the *ethical corporate mission and culture* of an organization can influence employee productivity and job satisfaction. Employees believe that being associated with an ethical organization gives them a sense of meaning and purpose in their work. Examples of organizations that contribute meaning and a sense of purpose in work include the religious-based or values-based organizations, where the founders or managers are guided by general religious or philosophical principles.

Employee Well-Being Can Be Enhanced Through Teamwork

Research has shown that *teamwork* characterized by reciprocal trust and respect among team members serve to enhance employee productivity and job satisfaction. Teamwork can be induced through role clarification (clarifying and negotiating role expectations of each team member), problem solving (educating team members on how to solve problems by first defining the problem, followed by generating possible alternatives for corrective action, selecting the best alternative, implementing the corrective action, and monitoring the outcome of the corrective action), goal clarification and prioritization (the team is instructed to develop measurable performance goals and prioritize these goals), and conflict resolution (the team is taught how to resolve conflicts through a built-in process to review decisions, team members are induced to learn more about the specialty fields of one another through planned mutual instructions, roles are clarified, and greater communication and openness are encouraged).

Employee Well-Being Can Be Enhanced Through Parallel Structures

Jobs involved in parallel structures provide members with an alternative setting to address problems and propose innovative solutions free from formal organizational structures. *Quality circles* are an example of parallel structures. Quality circles consist of small groups of 13 to 15 employees who volunteer to meet periodically, usually once a week for an hour or so, to identify and solve productivity problems. These group members make recommendations for change, but decisions about implementation of their proposals are reserved to management. Research has shown that parallel structures and quality circles do play an important role in employee productivity and job satisfaction.

Employee Well-Being Can Be Enhanced Through Participation in Decision Making

Substantial research has shown that participation in decision making and high-involvement programs contribute positively and significantly to work motivation and satisfaction. High-involvement programs are thought to be a conduit to help employees express their thoughts and feelings in important organizational decisions. As such, high-involvement programs serve to enhance person-environment fit in the work domain. Allowing employees to participate in important organizational decisions amounts to providing employees with greater work resources that help employees meet work demands more readily. For example, TQM (total quality management) also prescribes employee involvement and empowerment. Research has shown that TQM plays an important role in job performance and employee satisfaction.

Employee Well-Being Can Be Enhanced Through Alternative Work Arrangements

The goal of *alternative work arrangements* is to minimize work-family conflict and help employees balance the demands of their work and family lives. The most common type of work-family conflict is time-based conflict experienced when the time devoted to one role makes the fulfillment of the other difficult. Alternative work arrangements attempt to restructure one's job to allow for more flexibility in managing the hours devoted to work and the hours that are available for family commitments. Research has shown that matching the time preferences of employees with the time demands established by organizations is likely to enhance job performance and job satisfaction.

Employee Well-Being Can Be Enhanced by Internal Promotion

The policy to *promote from within* is yet another QWL program. Self-actualization is the desire to become anything that one is capable of becoming. Progressive firms engage in practices that aim to ensure that all employees have opportunity to self-actualize. Promotion and career advancement are important in that regard. Research has shown that companies that have policies to promote from within have employees who are more productive and satisfied with their jobs than companies that do not have such policies.

Employee Well-Being Can Be Enhanced Through Incentive Plans

There are many *incentive plans* that organizations use to reward their employees and satisfy employee needs for self-actualization, self-esteem, and social recognition. These include individual incentive programs, group incentive programs, profit-sharing plans, and gain-sharing programs. Research has shown that these programs do play a significant role in employee productivity and job satisfaction.

Employee Well-Being Can Be Enhanced by Employment Benefits and Other Ancillary Programs

With respect to e*mployment benefits*, many firms offer at least good employment benefits to their employees that play an important role in employee productivity and job satisfaction. Examples of employee benefits include health insurance, retirement or pension benefits, and supplemental pay benefits. Furthermore, there are many *ancillary programs* described in the literature designed to meet employee nonwork needs. These include child care programs, elder care programs, fitness programs, social programs and events, employee assistance programs, educational subsidies, counseling services, credit union, and others.

In sum, research has shown that programs designed to increase job and life satisfaction (i.e., QWL programs) can increase employee productivity and job performance. In turn, higher levels of productivity and performance serve to increase the organization's profitability.

Consumer Well-Being

Many confuse the concepts of consumer well-being (CWB) with that of consumer satisfaction. CWB goes beyond consumer satisfaction by linking consumer satisfaction with life satisfaction. Much research on CWB has linked specific organizational characteristics and marketing programs to concepts such as consumer life satisfaction, happiness, and absence of ill-being. We will highlight some of the important marketing programs found to enhance CWB.

CWB Can Be Enhanced Through Shopping for Needed Goods and Services

Research has shown that CWB is very much affected by the quality of the shopping experience. Consumers experience higher levels of life satisfaction given that they are satisfied with the quality of shopping facilities and amenities in their local area. Quality of shopping facilities and amenities translate into finding needed goods and services in the various retail outlets within the local area, the quality of these goods and services are deemed acceptable, the prices of these goods and services are deemed acceptable, and the services rendered at the retail outlets dispensing these goods and services are deemed acceptable. Thus, organizations can enhance CWB by making needed goods and services most accessible to consumers in different distribution venues, that these venues provide high-quality goods and services at low prices, and that these venues provide high-quality retail service to consumers.

CWB Can Be Enhanced Through Product Preparation

Research has shown that CWB can be enhanced by designing products that can be assembled easily and safely. That is, life satisfaction of consumers is influenced by the extent to which purchased goods are assembled or prepared for personal consumption. Easy and safe assembly of consumer durables serves to enhance consumer life satisfaction.

CWB Can Be Enhanced Through Product Ownership

Research has shown that ownership of certain consumer goods (e.g., car, house, furniture, and household appliances) may contribute significantly to consumers' quality of life. Here, feelings of status, pride, and security of owning consumer durables play an important part in life satisfaction—consumers who own products that make them feel secure, proud, and having special status and prestige in society tend to experience higher levels of life satisfaction than consumers who do not experience those feelings.

Furthermore, research has shown that the market value and the extent of appreciation or depreciation of owned goods do play a role in CWB—higher levels of appreciation (low level of depreciation) of these goods enhance consumer life satisfaction. Thus, organizations can enhance consumer well-being by marketing products that provide consumers with a sense of security, pride, status, and a high level of market appreciation (or low level of depreciation).

CWB Can Be Enhanced Through Product Use

Consumers experience different levels of satisfaction resulting from the actual use of goods and services, and use satisfaction plays an important role in CWB. Consumption satisfaction is closely related to but distinct from possession satisfaction, the difference being that possession satisfaction focuses on the positive affect that flows from ownership per se, whereas consumption satisfaction focuses on satisfaction that flows from the actual use or *consumption* of the product. Thus, organizations can enhance CWB by providing consumers with goods and services that have high level of consumption utility.

CWB Can Be Enhanced Through Product Maintenance

Maintaining consumer goods plays an important role in the quality of life of consumers. Research has shown that CWB is affected by maintenance satisfaction and product safety. Maintenance satisfaction is the positive affect that consumers experience when they seek to have a product repaired or serviced. Maintenance satisfaction involves satisfaction with maintenance and repairs provided by service vendors in the community (i.e., repair services), and satisfaction with services that facilitate maintenance and repair by the owners themselves (i.e., do-it-yourself support services). Thus, organizations can enhance CWB by providing consumers with quality services that allow consumers to repair their products at low prices. Organizations can also enhance CWB by providing consumers with quality do-it-yourself goods at low prices.

CWB Can Be Enhanced Through Product Disposal

High-quality services related to product disposal (including trade-ins and second-hand selling) do play an important role in CWB. CWB is affected by the degree of satisfaction consumers feel with experiences of getting rid of products (i.e., with the convenience and ease of dumping and the environmental friendliness of the product at the time of disposal). There are many consumer goods for which consumers feel dissatisfied with product disposability: oil-related products, computers, and automotive products. Furthermore, research has shown that CWB is equally affected by the adverse health effects (to consumers and the general public) of environmental pollution brought about through careless ways of disposing used products.

In sum, CWB is the sum total of satisfaction and dissatisfaction that consumers experience through shopping for goods and services, preparing consumer durables for personal use, owning those consumer durables, consuming goods and services, and repairing and maintaining their durables, and finally disposing of those durables. The greater the consumer satisfaction with these marketplace experiences the higher the consumer life satisfaction. To enhance CWB, organizations should make a concerted effort to meet consumers' needs, not only in relation to shopping but also in relation to other marketplace experiences such as product preparation, ownership, consumption, maintenance, and disposal.

Conclusion

Well-being (or life satisfaction, happiness, and absence of ill-being) is influenced by organizational internal and external efforts. Internal efforts can enhance well-being by implementing QWL programs that can enhance satisfaction in work life. Conversely, implementing marketing programs designed to increase consumers' satisfaction with shopping experiences as well as product preparation, ownership, use, maintenance, and disposal can enhance satisfaction in consumer life.

—M. Joseph Sirgy and Dong-Jin Lee

See also Advertising Ethics; Altruism; Benevolence and Beneficence; Consumer Goods; Consumer Rights; Consumerism; Consumer's Bill of Rights; Corporate Citizenship; Employee Relations; Employee Rights Movement; Empowerment; Green Marketing; Meaningful Work; Work and Family; Work-Life Balance

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Whistle-Blowing

"Whistle-blowing" in the context of business ethics refers to a practice of informing either a superior, a compliance or regulatory agency, or the general public of some action done or about to be done by an organization or some individual in that organization that would be harmful, unjust, in violation of human rights, illegal, run counter to the defined purpose of the organization, or otherwise immoral. An alternative definition of whistle-blowing stipulates that it is a purposeful revelation made by a person who somehow has special access to information concerning the organization. This person is aware of either an actual or suspected noninconsequential wrongful action that either concerns or implicates the organization and proceeds to inform an individual in the organization or outside of the organization with the ability to rectify the situation.

An employee of a company or a member of a profession, who knowing that someone in the company or in the profession is engaged in some sort of wrongdoing reports that behavior to an appropriate person, is a whistle-blower. The appropriate party being informed may be either someone in the corporation, the professional body, some public regulatory agency, some governmental agency, or finally, the general public. For example, Sharon Watkins informed her CEO Ken Lay of perceived irregularities in the accounting practices of Enron with respect to Special Purpose entities. Members of professional organizations are often required by their code of ethics to report unethical behavior on the part of fellow professionals in order to regulate their professions.

There are two ethical questions about the activity of whistle-blowing: (a) Is it an acceptable behavior? (b) If it is acceptable, under what circumstances is it obligatory?

There are several arguments against the acceptability of whistle-blowing: First, it involves disloyalty; second, it violates obligations of confidentiality; and third, it creates a distrustful atmosphere and undermines group and corporate morale. These arguments all rest on the fact that most groups have an unspoken expectation that members of the group should be loyal to the group or at least have some obligation of fidelity to the group and hence should not blow the whistle on the group. Analyzing the word "whistle-blowing" supports this presumption. The paradigmatic instance of whistle-blowing is in the context of sports where a neutral official such as a referee blows the whistle to stop play because a foul has been committed by the player of one team against a player of the other team.

Those opposed to whistle-blowing point out the disanalogy between sports and business. In sports, the whistle-blowing is done by a neutral observer, the referee, while in business and other corporate situations, the whistle-blowing is done against one's own team or teammate. Since management technique often emphasizes the importance of "team playing," and whistle-blowing is against the team and hurts the company, whistle-blowing is undesirable. From the perspective of those who expect group loyalty, the one who blows the whistle on a fellow group member is a "stool pigeon," "rat," "fink," or some other ethically reprehensible type of character and whistle-blowing as a dissenting act of disclosure is disloyal. More formally, it is argued that whistle-blowing violates an obligation of loyalty the individual has to either the company or professional group. Defenders of whistle-blowing need to show that either it is not disloyal and is ethically permissible or even if it is disloyal, the obligation to loyalty is overridden by some stronger obligation to the general public.

An argument can be made that if every company's primary obligation is to maximize profit then companies are not the type of entities that are owed loyalty. Since the goal of maximizing profit supports practices such as employment at will that allow a company to terminate an employer for no reason, and since retaining an employee out of loyalty could jeopardize that profit, the employer has no obligation of loyalty. Furthermore, not only is loyalty not required, but it would be foolish for the employee to be loyal to a company that is not obliged to reciprocate such loyalty. Consequently, if no loyalty is owed to a company, loyalty is not an ethical consideration that prohibits an employee from blowing the whistle.

Still, opponents of whistle-blowing could argue that even if a company is not owed loyalty, certain jobs and positions involve interdependent relationships, where some degree of fidelity to one's teammates or where one's obligations of confidentiality, either contractual or professional, require a person with privileged information to avoid divulging that information. For example, an argument against the appropriateness of Mark Felt, known as "deep throat," blowing the whistle on the government to the reporters Bob Woodward and Carl Bernstein of the *Washington Post* during the Watergate scandal is that, as an FBI member with access to confidential materials, he had an obligation to keep those secrets while investigations were being carried out. It could also be argued along similar confidentiality lines that attorney-client privilege prohibits attorneys from divulging information they know about their client, even if divulging such information could prevent serious harm or even death. Hence if one's position or relationship gives one privileged access to information, confidentiality may prohibit whistle-blowing.

In either case, whistle-blowing presents an ethical dilemma where the obligations that arise from the demands of group fidelity, confidentiality requirements, or even employee contracts that expressly (or at least implicitly) prohibit making information public run counter to the permissibility and/or obligation of that employee to blow the whistle. In those cases, the conflict of obligation is between the former obligations and the permissibility or obligation to blow the whistle.

Given these facts, it seems the burden of proof or justification falls on the whistle-blower. The first question is whether whistle-blowing is permissible. Defenders of whistle-blowing maintain that if there is no obligation of loyalty, confidentiality, or fidelity, then clearly whistle-blowing is permissible in conditions where companies violate ethical and/or legal constraints. Even if there are obligations of loyalty, confidentiality, and/or fidelity, there are some cases where whistle-blowing is permissible. Still, even in those cases, leaving loyalty and confidentiality concerns aside, whistle-blowing is permissible only if a certain set of conditions is met before a whistle-blower can justifiably inform on his or her company.

- *Proper motivation:* The whistle-blowing should be done for the purpose of exposing unnecessary harm, violation of human rights, illegal activity, or conduct counter to the defined purpose of the corporation and should be done from the appropriate moral motive, that is, not from a desire to get ahead, or out of spite or some such motive. Nevertheless, whether the act of whistle-blowing is called for is not determined by the motive of the whistle-blower but by the company acting either immorally or illegally. It also needs to be noted that a beneficial act of whistle-blowing might come from purely self-interested motives, such as a reward for blowing the whistle on tax evaders.
- *Sufficient evidence:* The whistle-blower should make certain that his or her belief that inappropriate actions are ordered or have occurred is based on evidence that would persuade a reasonable person.
- *Sufficient analysis of a grave, immediate, and specific matter:* The whistle-blower should have acted only after a careful analysis of the danger: (a) How serious is the wrongdoing? (Minor moral matters need not be reported.) (b) How immediate is the wrongdoing? (The greater the time before the violation occurs, the greater the chances that internal mechanisms will prevent the anticipated violation.) (c) Is the wrongdoing an action that can be specified? (General claims about a rapacious company, obscene profits, and actions contrary to public interest are useless from a practical perspective.)
- *Appropriate channels:* Except in special circumstances, the whistle-blower should have exhausted all internal channels for dissent before informing the public, and the whistle-blower's action should be commensurate with one's responsibility for avoiding and/or exposing moral violations. In this way, the whistle-blower diminishes the concerns about disloyalty and violation of confidentiality obligations. If there are personnel in the company whose obligation it is to monitor and respond to immoral and/or illegal activities, it would be their responsibility to address those issues. Thus, the first place to which the potential whistle-blower should report the unethical activities is to the appropriate persons within the enterprise, and only if those persons do not act is it permissible to inform regulatory or government agencies or the general public. If the above conditions are met, it is permissible to blow the whistle.

When is there an obligation to blow the whistle? A further argument is needed to show that there is a moral obligation to blow the whistle, since it is possible to argue that even if the illegal or immoral behavior of the company abrogates the responsibility of loyalty or confidentiality, there is no consequent Good Samaritan obligation to the general public to blow the whistle.

Since there is no specific role obligation to blow the whistle, except in some professional codes of ethics, the moral obligation does not arise from a promise or relationship. The obligation must arise from some general ethical requirement to serve the general public or some requirement of justice. The best arguments in support of whistle-blowing rest on some tacit agreement that some sort of Good Samaritan principle needs to be applied. The strongest arguments in this case come under the rubric of the obligation to prevent harm. To make the case for the obligatory nature of whistle-blowing requires showing when there is an obligation to the general public to prevent harm.

The obligation to prevent harm rests in a continuum of increasing responsibilities, starting with avoiding harm up to doing good. Doing good is an affirmative duty, and since affirmative duties are difficult to specify, it is difficult to specify a general obligation to do good. Furthermore, the proscriptions against harming are not applicable in the case of whistle-blowing because the whistle-blower is not the individual doing the harm. The whistle-blower simply knows that harm will occur. Hence, on the continuum of obligation, the obligation to blow the whistle depends on some sort of more general obligation to prevent harm, which takes effect only under certain conditions.

The basic recognition of an obligation to prevent harm rests on the insight that there are certain situations where it is unthinkable not to intervene on behalf of a fellow human being. As an example, consider a young child who wanders off from his or her parents and falls into a wading pool and starts to drown. There is no one around except a stranger who is walking by and sees the child drowning. It would be ethically monstrous of the stranger not to save that child. All would agree that the stranger has an obligation to pull the child from the wading pool, thus preventing the child's death. This situation exemplifies the intuition behind the belief that there is an obligation to prevent harm.

What is more, an analysis of the situation will reveal four conditions under which such an obligation accrues to a person. There must be (a) a need (the child is drowning); (b) the person must be capable of preventing the harm without sacrificing something of comparable moral worth (it is a wading pool so the harm preventer is capable of saving the child without putting his or her own life in danger); (c) the person is proximate (nearby), and (d) the person is the last resort (it would be the parents' responsibility if they were there).

When these conditions of need, capability, proximity, and last resort are met, there is an obligation to prevent harm. It follows that in the case of blowing the whistle to prevent harm, similar conditions must hold. If society can be harmed, the whistle-blower is capable of preventing the harm by blowing the whistle, the whistle-blower is close to the problem and no one higher up with more authority and responsibility is responding, there is an obligation to blow the whistle to prevent the harm.

However, the condition of capability needs to be further explicated. There should be some probability that the whistle-blower will have some chance of success. If there is no hope in arousing organizational, societal, or governmental pressure to correct the wrongdoing, then the whistle-blower needlessly exposes himself or herself and his or her loved ones to hardship for no conceivable moral gain. It is important to factor in the reality that there are negative consequences to whistle-blowing that accrue to the whistle-blower, because whistle-blowers violate the spirit of group loyalty (even if not warranted). Studies show that the individual, superior, or company on whom they have blown the whistle usually punishes the whistle-blowers.

Since, in the corporate context, the whistle-blower is seen as disloyal and the whistle-blowing is seen by company loyalists as cause for punitive action, to blow the whistle in such a culture requires a certain moral heroism. Because of that and given the fact that society depends on whistle-blowers to protect it from unscrupulous operators, justified whistle-blowers need some protection. To assure the existence of necessary whistle-blowers (somebody's got to do it), sound legislation is needed to protect the whistle-blower.

In the United States, there are statutes and laws that exist to protect the whistle-blower at both the federal and the state level. In 1982, The Federal Whistleblower Statute was passed to protect employees of defense contractors who blow the whistle and reveal a violation of law by those contractors. In 1986, the federal government passed the federal False Claims Reform Act, which provided a financial reward for someone blowing the whistle on an employee who perpetrated fraud against the government. The Whistleblower Protection Act of 1989 was meant to protect government employees who justifiably blow the whistle on their employers. In 2002, a provision titled "Protection for Employees of Publicly Traded Companies Who Provide Evidence of Fraud" was included in the Sarbanes-Oxley Act, which provided whistle-blower protection for those employees.

The Sarbanes-Oxley Act (1) made it unlawful to "discharge, demote, suspend, threaten, harass, or in any manner discriminate against" one who blows the whistle; (2) established criminal penalties of up to 10 years for executives who retaliate against whistle-blowers; (3) required boards to set up procedures for hearing whistle-blower complaints; (4) gave the secretary of labor power to require a company to rehire a terminated whistle-blower even without a court hearing; and (5) gave the whistle-blower a right to trial by jury to bypass administrative hearings.

While there is evidence of whistle-blower protection in the United Kingdom with the Public Interest Disclosure Act, in the European Union with its charter for whistle-blower protection, in Australia and in countries such as Israel, Ghana, South Africa, and South Korea, more work needs to be done in the international area.

Finally, it is important to note that whistle-blowing is not restricted to corporations. The need for whistle-blowing occurs in all areas of life. Professionals who are held to the standards of their profession are sometimes required by their code of ethics to blow a whistle.

Most professionals have obligations to their profession and the public to blow the whistle on colleagues who violate certain canons of appropriate behavior and are obligated to meet that demand even if it conflicts with friendship and group loyalty. All self-regulating professions need to require whistle-blowing. For example, accountants and engineers have a dual obligation to their clients and to the public. Hence, they have a fiduciary responsibility to report certain illegal or potentially harmful activities if they encounter them in the course of their auditing or accounting or constructing. But beyond the professions, whistle-blowing is required in other walks of life: For example, the participants in an honor code have a responsibility to report violations.

Enlightened companies, aware that harmful, immoral, or illegal behavior that is likely to occur from time to time needs to be reported, have begun to make provisions for regularizing the monitoring of behavior by using ombudsmen, anonymous ethics hot lines, and/or corporate responsibility officers to facilitate whistle-blowing. Such offices provide an outlet for those who feel obliged to report the unseemly behavior of their companies, without the need to go public. These provisions are desirable because they will alleviate the necessity of violating confidentiality obligations by going public and blowing the whistle on harmful or illegal behavior. In summary, while whistle-blowing activity is often viewed unfavorably, it is also a necessary part of human activity, and when done to uphold the standards of society with honest motives, it is often morally obliged and heroic.

—Ronald F. Duska

See also Enron Corporation; European Union; Honesty; Loyalty; Sarbanes-Oxley Act of 2002

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Wilderness

The Wilderness Act of 1964 defines wilderness as an area where the earth and its ecosystems are not subdued or harmed by man, where man is a visitor who does not remain. In the United States, and throughout the world, wilderness is important for human recreation and economic development as well as for the protection of ecological systems. In this respect, the consumption of wilderness is necessary for human progress and prosperity, but the preservation of wilderness as wilderness is also vital. The modern notion of wilderness emerged during the 18th and 19th centuries from Romantic writers and artists who were inspired by the beauty of nature and from Enlightenment writers and philosophers who contrasted the potential of rational human society with the harsh forces of the natural world. New England Transcendentalists praised nature for its profound simplicity, sustaining elegance, and its essential lessons for human life. Concurrently, the Industrial Revolution precipitated ever-increasing demands on natural resources for fuels, chemicals, and raw materials. Thus, the natural environment gradually became recognized as a valuable commodity, even while it diminished from overuse.

The History of Wilderness Protection

Wilderness protection and environmentalism in the United States are divided into three different phases or generations. The first generation, occurring at the turn of the 20th century, included components of wilderness preservation and conservation, while the second and third generations were marked by global environmentalism and resource conservation. The U.S. government first established the Department of the

Interior in 1849 to manage land, natural resources, and wildlife conservation. Although forestry management faced setbacks during the Civil War, it regained a close alliance with American industry after the war, sustaining resources for logging and mining businesses. Several decades later, to strengthen wilderness protection efforts, Congress enacted the General Revision Act of 1891, later renamed the Forest Reserve Act. This Act founded the Forest Service inside the U.S. Department of Agriculture and gave the president unilateral power to conserve wilderness through designating forest reserves. Conservationist Gifford Pinchot pioneered the creation of the Forest Service, emphasizing the importance of resource management in economic development and forestry. In 1903, President Theodore Roosevelt created the first national wildlife refuge, Pelican Island in Florida, to protect the 5-acre mangrove island as the last rookery of brown pelicans on the east coast of Florida.

Throughout the early years of wilderness policy development, American preservationists, who valued wilderness for its own sake, sought absolute protection of the land. Henry David Thoreau's *Walden Pond* offered a radical critique of civilization's destruction of nature in the mid-1800s. At the turn of the century, John Muir encouraged Theodore Roosevelt to establish Yosemite Park, arguing that nature was man's connection to God. Aldo Leopold's reflections in *Sand County Almanac* contributed to the emergence of the ecology movement and the concept of the farmer as conservationist.

Congress also demonstrated an interest in preservation, establishing the first national park in 1870, later to be renamed Yellowstone, and opened Sequoia National Park in 1890. The U.S. National Park Service was created in 1916 to oversee the increasing number of national parks, landmarks, and historic sites. In 1924, Aldo Leopold gained protection for the Gila Wilderness in New Mexico in obtaining its designation as the first official U.S. wilderness area.

In the private sector, organized interest groups directed wilderness protection projects, political lobbying, and garnered national interest for wildlife recreation. The Appalachian Mountain Club, started in 1876 in Boston by Edward Pickering, focused on the creation of national forests and outdoor education. The Audubon Society, formed in 1886 under the guidance of George Bird Grinnell, began with a mission to lobby for the protection of endangered species, particularly birds. In 1892, John Muir founded the Sierra Club to defeat a proposition to reduce the boundaries of Yosemite National Park. The Wilderness Society, founded in 1935 by Bob Marshall, became a steadfast wilderness preservation organization with a mission to halt the spread of commercialization and growth.

The advent of The New Deal, World War II, and postwar commercialization shifted American sentiment away from wilderness protection and more toward environmental concerns. What was once an elite effort to save recreational places became a pluralistic concern to better society overall. Dust bowl conditions across the Midwest and Southwest created by land-abusive intensive farming required new land and soil management techniques. Rachel Carson's research regarding the toxic effect on the environment and individual health resulting from widespread pesticide use shocked many Americans into awareness of their role in the earth's ecosystems.

Although many second-generation environmental activists focused on pesticides and nuclear energy, wilderness preservation efforts did not cease altogether. The Wilderness Act of 1964, authored by Howard Zahniser of The Wilderness Society, assigned wilderness its first legal definition and created the National Wilderness Preservation System (NWPS). At that time, the designated NWPS included 54 areas, encompassing a total of 9.1 million acres in 13 states. In signing the Wilderness Act, President Lyndon Johnson recognized the importance of securing an enduring resource of wilderness for present and future generations. Furthermore, it was deemed that congressionally designated boundaries around wilderness could only be altered by another act of Congress. In 1970, the Petrified Forest National Park and Craters of the Moon National Monument became the first national park sites to include designated wilderness areas.

In the 1970s, environmentalism emerged as a popular cause, following the antiestablishment rebellion and antiwar fury of the 1960s. Back-to-nature sentimentalists found common cause with environmental scientists in creating Earth Day, an annual celebration to heighten awareness of the man-made threats facing a broad range of natural ecosystems. Progressive theories reintroduced an older belief in the land ethic and asserted the natural rights of plants, trees, and animals. Organizations such as the National Audubon Society, the Sierra Club, and The Wilderness Society saw their memberships multiply dramatically. Courtrooms across the United States became battlegrounds for lawsuits between environmentalists and corporations, each asserting the priority of their competing interests.

Due to increasing globalization, third-generation U.S. environmentalism in the 1980s and 1990s focused primarily on the global sustainability of natural resources and climate control. In the United States, the Forest Service, the National Park Service, the Bureau of Land Management, and the Fish and Wildlife Service were instructed by Congress to recommend land for wilderness designation as they deemed appropriate. The passage of the Alaska National Interest Lands Conservation Act in 1980 added more than 56 million acres of wilderness to the NWPS. This largest single addition established 10 new national park sites, 9 wildlife refuges, and additional Bureau of Land Management conservation units.

At present, the first-generation wilderness protection organizations continue to gain support and lobby for policy-based protections. The Sierra Club directs efforts for responsible community development and has initiated campaigns to preserve endangered wildlife in Alaska and the national forests. The Appalachian Club maintains a focus on developing recreational and educational wilderness programs. The Audubon Society and the Wilderness Society uphold strict conservation agendas, working to protect species' habitats from oil drilling, suburban development, and from invasive wild species of plants and animals. Several more private organizations such as the National Resource Defense Fund, the World Wildlife Fund, and Campaign for America's Wilderness have issued strong additional support for recreational and educational purposes and contribute resources for scientific research.

The conflict between the resource conservation and wilderness preservation interests groups is ongoing and has been described as a struggle between the ghosts of Gifford Pinchot and John Muir over the future of U.S. environmentalism. However, Ramachandra Guha, an Indian environmental scholar, pointedly chided those who focus on this debate as the central dilemma of the global environmental movement. To the extent that the issues of overconsumption of natural resources by developed countries and the reliance on increasing militarization to resolve political, social, and economic challenges are overlooked, Guha argues, the real threats to environmental survival are not recognized. Military violence, resulting in widespread environmental degradation or annihilation, and social disparities, resulting in continuing exploitation of the lower classes, are problems of such magnitude that they trivialize the question of preservation versus conservation. Indeed some believe that without a radical restructuring of the goals of the environmental movement in ways that acknowledge worldwide social and political trends, the national debates over wilderness resources would be reduced to an irrelevant sibling squabble in the face of a major disaster.

Wilderness Protection and American Business

Over the 20th century, the chief concern for protecting wilderness was confronting business growth, especially mining, logging, livestock grazing, and oil drilling. Environmental organizations worked to support legislation on the local, state, and federal level to place boundaries around public land. More recently, third-generation environmentalist organizations have formed partnerships with corporations to increase preservation awareness and initiatives. Many companies respect wilderness for its own sake and contribute support for outdoor recreation for the public as well as their own employees.

Since the 1990s, many businesses have operated under conditions mandated by third-party certification systems. Logging, drilling, and mining corporations tend to be major donors to international conservationism. Chevron honors annual conservation awards; BHP Billiton and Alcoa sponsor conservation workshops for mining industry directors and managers. The World Wildlife Fund partners with Fortune 500 companies and many financial institutions to preserve wildlife and initiate educational preservation programs. The National Fish and Wildlife Foundation has worked with ExxonMobil to initiate more than 100 conservation projects worldwide.

Corporate directors and business executives are often found on the boards of leading conservation organizations, a trend that started with business tycoons such as John D. Rockefeller and Stephen Mather. Contemporary businesspeople continue this tradition, both as a means to build connections to conservation watchdogs and to further their own agendas within the conservation movement.

However, critical environmentalists argue that large corporations are too anthropomorphic and are unable to recognize the inherent value in preserving and protecting wilderness. These new partnerships are criticized for allowing corporations to hide their true environmental impact behind *greenwash* and weaken the vigor of the environmental movement overall. For example, several major oil companies have been accused of initiating massive rebranding and advertising campaigns to conceal their environmental destruction.

On the political level, individuals are generally divided between two philosophies regarding business growth and wilderness protection. While some citizens believe that protections must be enforced politically to maintain a desired amount of wilderness and wildlife, others believe that the mechanism of a free marketplace can determine environmental decisions and preserve wilderness as necessary. Environmental activists continue to fight for regulations and restrictions for business, believing that businesses consider wilderness as a resource and not necessarily a valuable entity in itself, a conflict that will continue to challenge both sides.

The Current State of Wilderness

Since 1964 when the NWPA was passed, the designated wilderness lands have been expanded nearly every year. Currently, these lands include 680 wilderness areas in 44 states, consisting of 106,619,208 acres. Wilderness designation may be initiated by a recommendation from a federal agency, a public or private organization, or even an individual. Such a recommendation must follow a route of congressional approval and obtain a signature of the U.S. president to achieve the designation. Criteria taken into account in the wilderness lands designation process include the following: The area must be largely unaffected by any presence of humans and appear as natural; the area must provide opportunities for solitude; the area must offer opportunity for primitive recreational, low-impact activities such as cross-country skiing and hiking; and the area must contain features of ecological, geological, scientific, educational, scenic, or historical significance. Furthermore, it is expected that the recommended area be a minimum of 5,000 acres or be a roadless island.

The challenge of the act is to preserve the land in its wild and natural state, relatively free of human impact and control, while at the same time providing for use and enjoyment of the designated areas. In the past 40 years, recreational use of wilderness lands has increased tenfold, and more than 12 million people now visit these areas each year. While the National Wilderness lands are designated and protected for the purpose of such visitors' enjoyment and appreciation, the impact of increased human traffic threatens the continued sustenance of the indigenous ecosystems. Despite the official expansion of acreage designated as protected wilderness, the increasing use of this land for approved purposes effectively tramples the life on it even while championing conservation. The tension between the use and protection of wilderness, apparent to participants in and observers of the environmental movement since its earliest days, continues unresolved.

—Robbin Derry

See also Acid Rain; Biodiversity; Bureau of Land Management; Deep Ecology; Environmental Ethics; Environmentalism; Gaia Hypothesis; Greenhouse Effect; Land Ethic; Natural Resources; Natural Resources Defense Council; Pollution; Speciesism; World Wildlife Fund

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Winner's Curse

The winner's curse is the unfortunate consequence of an auction in which the winning offer for an item was bid so much higher than the item's worth that the winner cannot recover enough value to justify the price paid.

A free market can function like an auction—sellers offer their goods and buyers offer their bids of the prices they are willing to pay for those goods.

Bidders, though they may be sensitive to price and prefer to pay the lowest amount possible, "win" the auction when a seller accepts the highest price offered. In a free market for scarce goods, as in an auction, buyers may willingly increase their bid to maximize the likelihood of purchasing, or winning, the goods they want. One consequence of this auction-like process is that winning buyers may come to regret the high price they willingly paid, and to feel "cursed" by their inability to recover enough value to justify it.

The winning buyer paid more for the goods than any other potential buyer was willing to pay. Perhaps the winner made an error in judgment and inaccurately assessed the value. In addition to overly optimistic forecasts, such errors also may be caused by incorrect or incomplete information about the goods. These information problems may arise when sellers bluff buyers by misrepresenting the attributes of the goods. Governments may regulate commerce to criminalize untrue statements, false appearances, and misrepresentations. This government action to interfere with a free market is justified to ensure the most efficient allocation of social resources. The market forces of supply and demand better support economic efficiency when buyer-seller decision making is based on accurate information.

The winner's curse may not be due to any misrepresentation by the seller about the features of the goods. The curse may arise from an attribute of the buyer whose winning bid was higher than all other bidders in the market. Did they all have better information about the true value of the goods than the winner had? If so, then the winner indeed bid too high based on overestimating the net benefits or utility to be had from the purchase.

Calculating utility, however, is a cost-benefit analysis, and it is often extremely difficult to do it with precision and accuracy. One important cause of such poor analyses is that the benefits are not all measured in the same units as costs, or may not be possible to quantify at all. How does one put a precise value, for example, on the pride or joy of ownership?

In addition, utility and benefits are just forecasts at the time of purchase. The purchase costs, however, must typically be committed before the benefits can be realized. The magnitude of the benefit actually realized may be less than the anticipated forecast. In short, for the winner, utility is a subjective judgment of value in an uncertain future. The winner may feel cursed by regrets if that future does not meet the relatively high expectations.

The winner is the buyer who forecast more optimistically about the future than any other bidder, but that buyer may not be likely to comprehend the error in a society characterized by closely held information and deficiencies in the distribution of knowledge about prices. Thus, the winner's curse is more likely to be observed in open societies where buyers have access to broad economic knowledge. Interestingly, such societies tend to have more productive economies that, over the long term, efficiently increase the supply of goods and drive down prices. Over the long term, one would expect that human nature would become increasingly sensitive to the winner's curse in an economy becoming more efficient—overpaying when prices are declining seems that much more unfair. In this context, the winner's curse can be viewed as the buyer's perception that distributive justice has been violated by the terms of the buyer-seller exchange.

The buyer's market savvy and sophistication may also influence the likelihood of a winner's curse. An inexperienced buyer may lack the required knowledge to value goods accurately and to make appropriate bids. Principles of commutative justice for new and inexperienced buyers suggest that neutral sources of reliable information are important means to increase fairness and reduce winner's curse.

Conversely, an experienced buyer may have established good and trusting relationships with sellers that may become entwined with the value of the goods considered in a purchase decision. In this case, the high price of a winning bid reflects the value of the goods plus the value of the relationship. Winning buyers, however, may feel "cursed" after the purchase if they attempt to justify the costs only on the benefits embedded in the features of the goods without considering the benefits of sustaining and nurturing the relationship with the seller. Such an error in evaluating benefits is likely to be found in relationships built on trust that foster purchase decisions based on reciprocity, or preferences to favor the seller even in transactions not justifiable by the economic efficiency of the exchange.

Characteristics of the seller may bring about a winner's curse. Large sellers with substantial market power may unethically manipulate the supply of goods to cause artificial shortages. In this case, the buyer's decision making would be based on disinformation, or engineered misinformation, about future availability of opportunities to purchase the goods at more reasonable prices. Recently, for example, some electric utilities in the United States were alleged to have reduced their productive capacity during peak seasonal demand, inducing customers to agree to long-term contracts at unnecessarily high prices. Governments in many societies criminalize such hoarding practices.

Even sellers intending to be ethical may cause a winner's curse by creating excitement and competitive fever among potential buyers. Advertising and promotional techniques that motivate buyers with emotional appeals may discourage rational purchase decisions and encourage impulsive buying. For this reason, governments may require sellers to offer "cooling-off" periods of several days during which a buyer may cancel a contract without penalty. Also, ethical sellers may offer generous "money-back" warranties to signal their integrity and guarantee that they will not take advantage of buyers who feel cursed by their purchase.

When potential buyers fear overpaying for goods, then they may stay away from the marketplace to reduce their exposure to the winner's curse. Their aggregated absence represents a decline in demand that may harm the economic welfare of society. Accordingly, business managers, government regulators, and advocacy groups should be alert to opportunities to reduce the likelihood of the winner's curse.

—Greg Young

See also Advertising Ethics; Cost-Benefit Analysis; Justice, Distributive; Market Power; Warranties

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Women in the Workplace

The study of women in the workplace is the investigation of women's roles in and access to work environments beyond the home. This area of research draws on economics, social statistics, business history, feminism, and cultural history to create a narrative of how women have gradually moved into major participation in the workforce of contemporary society.

A limited way of approaching this field would be to look at the roles and numbers of women in corporate America over the decades of the 20th century. This perspective could tell the story of how U.S. women, including immigrants of all races, have moved from the factories and mills of the early 1900s to the broader range of corporate positions by the end of the century. It would necessarily incorporate the effects of the World Wars, the Great Depression, the dust bowls, the postwar social upheavals, the waves of the women's movement, and the national transition from manufacturing and agricultural jobs to service and technology that dominate corporations at the turn of the 21st century. This is an important and valuable story. But it is not the whole picture of women in the workplace.

A fuller story can be told about the roles of women in the work of exploring and settling a new nation, the roles of colonial women and slave women and of freed women and independent entrepreneurs to build a more complete understanding of American working women. European women have worked through different but parallel social and economic histories while expanding their recognized contributions to the workforce. Similarly, Asian, African, Middle Eastern, and South American women have their own complex stories to tell about women's emerging participation in the workplace. Thus, a nuanced and thorough understanding of women in the workplace could be the work of a lifetime.

This entry focuses predominately on the history of working women in the United States but also acknowledges parallel developments in other nations and regions. Social norms and laws affecting women's rights to vote, to own and inherit property, to establish businesses, to work in traditionally men's jobs are all powerful determinants of where women are in work environments. While there are unique patterns and histories in each country, there are also some common trends. These trends will be highlighted in the concluding overview of women in the workplace.

Early Roles

It is not uncommon to hear references to women entering the workforce, as if it was a new phenomenon in the latter third of the 20th century. While it is valuable to recognize the relatively recent and dramatic changes in women's access to the professions, and the great influx of middle-class women into the workplace, it is also important to fully credit the roles that women played in the economic landscapes of earlier centuries.

In America, the patterns of Elizabethan England and feudal laws came over with the early settlers. Women's roles were assumed to be those related to home and family. But in the early settlements, men's roles were also much about home and family. Homesteading meant building a home, finding a way to make a living on the land, and all family members were thoroughly involved. In addition to cooking, feeding, gardening, making clothes, doing the laundry, women tended animals, kept an eye on the crops, and often participated fully in the exchange of animals, produce, grains, and prepared goods that were common in order to acquire shoes, seeds, kitchen utensils and cookware, building supplies, and whatever else couldn't be grown on the land. Women also taught school, ran boarding houses, produced clothing for sale, opened bakeries; in short, used the traditional skills familiar to most women of that period to earn income. These occupations, rediscovered by women periodically throughout the 18th, 19th, and 20th centuries in times of economic need, became safe and recognized economic activities for women.

Native American women at this period were actively engaged in running trading businesses, selling furs, maple sugar, and wild rice to European explorers. Frequently, they provided domestic services, such as cooking and sewing to the fur trade forts. The indigenous women were valued for their translating and negotiating skills, which gave the explorers access to land, rivers, tools, canoes, blankets—all essential to survival in the wilderness. Gender divisions within the Native American tribes attributed negotiating and trading skills to women, thus women were as actively engaged as men in the economic business of the communities. However, as white women arrived in the newly opened trading posts, they brought expectations of the social and economic hierarchies of the old world. The emergent family patterns and gender roles were a mix of European standards and native practices.

Surprisingly, the gendered divisions of labor from Europe and Africa were encouraging women in particular businesses. Slave women brought to the Americas from western Africa came predominately from matrilineal tribes where it was common for women to be producers and traders. In Germany, the Netherlands, France, and England, women were often found as dealers in foods, ale, and clothing. As these traditions moved across the ocean, women settlers contributed to the building of economic bridges with Native Americans.

Civil and Common Law on Women's Economic Status

Just as numerous cultural patterns were transported to the New World with the various groups of explorer and settlers, so too multiple legal systems were imported and coexisted in the early centuries of American history. Western European countries, excluding Great Britain, followed versions of civil law derived from the Roman legal system of legislated statutes. These laws were premised on the family, meaning married partners, as the central unit of society. Laws regarding economic transactions and property rights were designed to protect the continuity of patrilineal families. However, property rights were held jointly by the husband and wife, and where civil law prevailed in the New World, wives could inherit half of the wealth, land, or personal property accumulated during her marriage, since she was a coequal owner of that property. Despite this access to property and financial resources under civil law, husbands and fathers held absolute legal authority, thereby circumscribing women's claim to resources by the family claim.

In contrast, common law evolved from British feudal privileges and followed customs, traditions, and judicial decisions. Feudal rights and privileges were granted by lords and barons, on the basis of military obligations and triumphs. Women were excluded entirely from this authority or ownership, and thus had no rights to property. Judicial decisions were premised on prior comparable cases, so that the common-law system developed according to how things had always been done. Under this system, women were allowed the use of marital property as long as the marriage lasted. If she was widowed or divorced, she might retain claim to her personal belongings, but certainly would not inherit real property.

Both legal systems created cultures that were powerfully patriarchal. Women's economic rights were severely limited, thus limiting their ability to own or run businesses, to take over the enterprise of a deceased husband, and, having little or no collateral, to take out loans for the purpose of acquiring land or opening a store. Married women were not legally independent agents.

In addition to the differing legal codes in different colonies, not all women were treated alike. White and Hispanic women had more privileges than African American or Native American women, creating class differentiations that were enforced by women and men of the dominant European cultures. Access to education, property, decent wages, as well as to the basics of food and shelter were all more limited for the poorer members of society. While slavery was a strong component of this class system, classism and racism extended well beyond slavery and served to reduce the economic freedom of many women in the colonies to a bare minimum.

Industrial Expansion of Capital Markets

As cities grew over the 18th and 19th centuries, and the Industrial Revolution got under full steam, women's role in production and trading extended as well. During the period of the American Revolution, British businesses were frequently boycotted, creating an opportunity for small businesses to offer such things as millinery, dry goods, books, and household supplies. Women entering these businesses could do so as an extension of their household roles and expertise. Young girls could be apprenticed to female artisans and storekeepers to supplement their parents' income and to learn trades that they might put to use for their own families' benefit in the future. By the end of the American Revolution, the laws of primogeniture, which prohibited women from inheriting property, were changed in every state, and women's economic status began the incremental move toward equality with men.

During the first Industrial Revolution, between 1830 and 1880, the growth of mills and factory production centers, provided manual labor for young girls and women who needed work. While the dominant business of the American colonies and territories was still agriculture, the mills introduced an alternative to the hard labor of farms. Making shoes and textiles was not pleasant work, the conditions, wages, and hours being entirely at the will of the owner, but it offered an opportunity to earn and save small sums. Entrepreneurial women were occasionally able to achieve notable success in business, particularly selling items to women—lotions, medicines, hats, small time-saving inventions for the household and were able to exploit the increasing tolerance for women's claims to conduct business independently. It was a period that saw the emergence of the women's movement following the Seneca Falls Convention in 1848, and gradually legal changes were made to enable women to enter contracts and hold property. Parallel to the abolition movement that supported economic freedom for slaves, women and men also began to consider the rights of women to achieve parity with men in the marketplace.

However, as the 19th-century industrial growth contributed to wealth accumulation, distinct social classes became apparent, with a robust classism in tow. Higher-class women did not need to work outside the home, and they imbued their domestic talents with a moral superiority. Lower-class women were forced by poverty to leave their children and homes to undertake wage labor, often in service to the higher-class families. Middle-class women were the ones most affected by the Industrial Revolution as whether and how one worked established social rank, which determined marriage prospects and one's station in life. A cult of domesticity encouraged women's roles as mothers, wives, homemakers, and for middle- and upper-class women it conveyed the message that this was truly the appropriate and ideal role for women. Men could conduct the public and economic life of the family, while genteel women were expected to defer to their husbands and maintain the harmony and order of the home. Of course, not all women were willing to conform, but those who refused to adopt the norms of the passive female, risked social scorn. Where domestic deference was touted as a virtue, nonconformance was glaring.

By the late 1800s, women engaging in businesses were less constrained by law, but were still hemmed in by custom and tradition. Women's businesses, like men's of that period, were small, usually employing fewer than five workers. Women entrepreneurs were most often older, widowed or married, and applied their domestic talents to the marketable production of clothing, foods, or related services. The most apparent differences from men's businesses were the level of capitalization and available credit: Women business owners were frequently referred to as penny capitalists.

A further area of organizational specialization emerged for women in the 19th century, that of founding and running moral reform organizations. Temperance campaigns were popular and directed largely by women. Churches were established by women often incorporating contemporary issues of moral concern, such as women's rights, rights of slaves and freed blacks, and alcoholic abstinence, along with a growing interest in spiritualism and healing. Women were not universally accepted as preachers, but many people were willing to attribute a moral superiority to women, lending strength and credibility to their role as church leaders.

Women's Role in the Incorporation of America

Dramatic changes occurred in the structure of business organizations over the 50-year period spanning roughly 1880 to 1930. Women's participation in this transitional period was essential. In the manufacturing world, women were the cogs of the massive garment and textile industries, as indicated by the individual labor rights groups that sprung up at the time: Shirtwaist Workers, United Cloth Hat and Cap Workers, Buttonhole Workers, International Glove Workers, the Boot and Shoe Union. In the service industries, women were hired as telephone operators, sales clerks, laundresses, among other roles critical to the explosive growth of industry. Women's contributions enabled the widespread success of corporate evolution, while the entrenched discrimination against women in the workplace became increasingly apparent.

At the dawn of the 20th century, small companies were being rapidly swallowed up by larger corporations dominating industrial mass production. Approximately 300 companies held 40% of the country's manufacturing assets. The economic focus of the nation shifted away from small businesses as major transportation, banking, retail, communications, manufacturing, and insurance companies emerged. Although the women's rights movement succeeded in securing women's right to vote in 1920, women in the workplace were still limited by the lack of education and professional training, little access to credit and capital, discriminatory hiring practices and protective labor legislation.

Women were in sex-segregated jobs, often those that demanded precise manual labor, such as sewing factories and assembly lines. The hiring of lower-class children, orphans, and immigrant women into factory jobs prevented them from acquiring an education that might enable them to move out of poverty. The working conditions were only minimally regulated, if at all, creating environments with significant risks to health and longevity. Searching for a forum for redress, women and girls became a significant component in the labor movement, voicing pleas for safer workplaces and staging marches and rallies to garner public support. Tragedies such as the Triangle Shirtwaist Fire served to catalyze federal regulatory efforts for factory buildings and attention to workplace safety standards. Despite the vocal role of working women in labor unions and the heavy reliance on women in the bottom of the workplace pyramid, a majority of men in union leadership and corporate management regularly announced their belief that women's rightful place was in the home, and that women should work only if their circumstances required it. These espoused beliefs enabled them to establish higher wages for men as the rightful family breadwinners.

In addition, working women were constrained by legislation from participating in many occupations that were considered too difficult or challenging for the frailer sex. As a result, women were relegated lower-paying jobs, with fewer opportunities for advancement, or for the achievement of financial independence. In 1908, the U.S. Supreme Court case *Muller v. Oregon* gave employers the right to prohibit women from working long hours, or from jobs that were deemed to be physically taxing, particularly to the reproductive function of women. Louis Brandeis, representing the state of Oregon, used traditional gender roles to successfully argue that women should be treated as a special category due to their reproductive role, thereby fostering legislation that would limit women's job rights for decades. While this is often referred to as protective labor legislation, it has been a matter of debate whether it was more protective of women's health or men's jobs.

From 1870 to 1930, women's proportional enrollment in colleges and universities more than doubled, reaching 44% of the student population. Women were increasingly able to choose jobs and aim for careers other than teaching. Despite continuing low wages and inadequate child care, some women combined motherhood with paid work. Women were achieving a new stereotype, that of being better people persons, and accordingly they were channeled into retail, service, and secretarial positions. These were more respectable than factory jobs and better working conditions certainly, but were still undoubtedly labeled as women's jobs. This period of history saw a major gain in wage work for young single women, and by the Great Depression, all those who were still employed were grateful for income, regardless of the gendered nature of the task. Women were admitted to professional schools, in small numbers, but obtaining jobs in law firms, hospitals, or management ranks was nearly impossible while companies could legally engage in discriminatory hiring and promotion practices.

The Great Depression and World War II were periods of intense social anxiety resulting partly in a return to the comforting assurance of women in traditional family roles. Although women filled in men's jobs when they were needed, due to war or hardship, these were temporary roles, with temporarily elevated earning power for women. The strain of loss, sacrifice, and violent warfare reinforced a longing for a secure family, the preserver of traditional values, among which motherhood ranked high on the list. The baby boom of the late 1940s and 1950s was the result, with a renewed cult of domesticity buoyed by postwar prosperity. Advertisements for consumer products celebrated joyous, carefully coiffed women thriving on floor waxing, the preparation of hot lunches for their children, and the achievement of brilliant white laundry. Once again, "working women" generally indicated those who could not afford to stay home.

But the new economic prosperity also created opportunities for women entrepreneurs. For example, Esther Mentzer, a working class child of Hungarian immigrants, grew up in Queens, New York above the family's hardware store, while her uncle conducted chemistry experiments in a backyard laboratory to create skin potions. From this experience, Mentzer and her husband built a small business producing facial cream in their kitchen, distributed to beauty parlors and eventually on a larger scale to New York department stores. Esther Mentzer became Estee Lauder, creating an international cosmetics company, responding to women's interest in beauty and skin care. Her knowledge and ability grew with the demands of the business, propelling her to a level of success among women in business with few peers in the world.

The Emergence of the Businesswoman

Despite the renewed enthusiasm for women as homemakers in postwar economies, it was increasingly evident across the globe that women were capable researchers, explorers, thinkers, and leaders, in addition to being mothers and wives. Marie Curie, Amelia Earhart, Eleanor Roosevelt, Elizabeth Windsor, Rachel Carson, Golda Meir, and Indira Gandhi are notable among the many accomplished women of the 20th century. If these lists didn't include women in business in the 1960s, it wasn't because they lacked the ability to lead or inspire. Although entrepreneurial women in business were visible, they were not a frequent sight, and discriminatory business practices and laws continued to work against the vast numbers of women in the workplace.

In 1963, U.S. President John F. Kennedy signed the Equal Pay Act, and it was followed closely by Title VII of the 1964 federal Civil Rights Act, which included the term *sex* as a nondiscriminatory category. Ironically, the term was inserted at the last moment by an amendment designed to ensure the defeat of the act. The passage of these acts signaled the end of advertisements for men's jobs as distinct from women's jobs and mandated equal pay for equal work. Many labor and business associations lobbied unsuccessfully against these acts in the congressional hearings stage, as burdensome, costly, and intrusive for private enterprise. Despite this opposition, the legal groundwork was laid for the efforts to achieve gender parity in workplace roles and wages. This official step was a radical departure from the legally entrenched gender-segregated workplace that had evolved from the European roots of American society and predominated for centuries.

The path of women into the mainstream workplace has never been a direct linear route, and this stage was no exception. Although increased legal rights for working women had been affirmed, there was no immediate visible effect on wages. In 1955, women's wages were 64% of men's wages, and by 1961 they had fallen to 59% and stayed close to that level through the decade. The Civil Rights Act provided for the establishment of the Equal Employment Opportunity Commission to oversee compliance, but it was quickly overwhelmed with the task and broadly considered ineffective.

The women's movement gained strength and confidence from the civil rights movement and antiwar protests of the 1960s. Each demanded social change and the righting of perceived and experienced wrongs. Widespread frustration and anger about racism and sexism in so many social institutions prompted activists to work toward increased integration of schools and workplaces. Although women and blacks faced different types of barriers and prejudices, they were often united as they had been a century earlier, to push for basic civil rights and the dismantling of the systems of privileges that enabled white men to hold all economic, political, academic, and civic authorities.

By the 1970s, increasing numbers of women and minorities were admitted into schools of law, medicine, and business. Affirmative action policies were used to recruit and admit those whose educational background or experience might not have previously gained them admittance. Similarly, businesses, along with law firms and medical practices, actively recruited women in an attempt to be seen as part of the solution rather than part of the problem. However, 10 years later, affirmative action itself was accused of being discriminatory, and the argument that women were inherently disadvantaged in the workplace was losing strength. The initial rush of women into MBA programs and managerial jobs dropped off again, as many women of the baby boom era discovered that in the absence of changes in men's attitudes toward and participation in parenting, it was extremely difficult to work full-time, raise a family, and live up to performance standards set according to the benchmarks of men who didn't have primary family responsibilities.

Women faced the conflict of the idealized worker and the idealized mother, according to Joan Williams, a researcher in the American family. The idealized worker is a male, whose life is focused on the demands of his work. While he may have a family, his commitment to them and their needs is superseded by the needs of his employer, who may insist on long hours or geographical moves. For many corporations in America, this idealized worker is still a fundamental standard against which all men and women are measured. At the same time, women are socially measured against the standard of the idealized mother—one who is willing and able to drop everything when a child needs her and who would prefer to be with her children than to be working outside the home. Obviously, women cannot be both an ideal worker and an ideal mother, according to these stereotypes. But most of our economic and welfare policies, health benefits, divorce laws, and business traditions embrace these ideals, creating an environment that makes it difficult for women to choose to work and mother at the same time. These arguments point to the need for changes in men's attitudes and roles for women's roles and achievements in the workplace to be sustainable.

Nonetheless, more women are in the workplace than ever before, and although there is significant variance by work specialization, women's wages are rising slowly to close the remaining gap to achieve parity with men's wages. By the 1990s, women outnumbered men as recipients of bachelor's and master's degrees. Historian Joan Hoff has suggested that the legal status of women changed more in the last quarter of the 20th century than in the previous 200 years. Credit, property, and capital are more readily available to women.

These remarkable achievements have not brought about true equity in the workplace. Many men and women still work in sex-segregated blue-collar jobs, and while women in executive roles are not the rarity they once were, corporate board meetings or executive gatherings are nearly always dominated by men with women playing a minor role. In 1992, 25% of working women were employed part-time, while only 11% of working men were part-time. Black women are more likely to be limited to part-time work involuntarily than white women. Latino women are more likely than whites to work in seasonal industries and, therefore, to face regular unemployment.

While women have made great strides in workplace rights and accomplishments, familiar challenges persist. In the United States as well as in most other parts of the world, women are still expected to be the primary parent, to be on call for children and aging parents. Around the globe, women are largely responsible for housework. These demands on women's time and energy place unequal burdens on women trying to compete in a marketplace with men for jobs and opportunities. Gender stereotypes in education and the workplace still linger—girls and women are often steered toward jobs requiring relational skills, while boys and men are expected to do better in mechanical and technical fields. Despite these recalcitrant attitudinal barriers to gender equality in the workplace, women now have rights and opportunities that enable them to pursue individual goals of accomplishment.

—Robbin Derry

See also Comparable Worth; Diversity in the Workplace; Employment Discrimination; Equal Employment Opportunity; Equal Pay Act of 1963; Family-Friendly Corporation; Gender Inequality and Discrimination; Glass Ceiling; Hostile Work Environment; Preferential Treatment; Reverse Discrimination; Sexual Harassment; Sweatshops; Wages for Housework; Women's Movement; Work and Family

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Women's Movement

The women's movement refers to the social movement by women to achieve full economic and civil rights. The beginning of this struggle in the United States is generally traced to the Seneca Falls Convention in 1848, organized by Elizabeth Cady Stanton and Lucretia Mott. An afternoon conversation between friends about women's place in society resulted in a resolution to work together for change. One week later, on July 19, 1848, these bold women launched a revolution that continues to this day, as women and men around the world strive to establish and protect equal economic, civil, legal, and social rights for all women.

In the United States and most Western nations, women have achieved the legal and economic rights defined as goals in the early stages of the movement. But these did not come without lengthy debates and challenges, and those at the forefront of the movement were often ridiculed and ostracized for advocating such things as women's right to vote, women's right to own property, women's right to child custody in a divorce, and women's right to obtain training to work in any profession. Although most of these now seem commonplace and normal, in the life of our nation and modern society, they are quite recent accomplishments.

Over seven generations, the women's movement mobilized citizens, largely women, to rally workers; to propose legislation; to picket in the streets; to write pamphlets, books, and letters; to engage in civil disobedience; and to run for office in order to persuade a majority of American voters to recognize women as full citizens, not dependent on men to formulate their opinions or exercise their rights. These activists were jailed, jeered, and booed, but they were rarely ignored. The women's movement aroused intense sentiments, both pro and con, from the outset. Stanton predicted that there would be misconception, misrepresentation, and ridicule, and she was proved right repeatedly. While media scoffing intimidated some women, a much larger number were enraged at the attempts to humiliate women and responded by further committing themselves to the cause of equal rights. The waves of support for women's rights continue through the present time and have extended to include a focus on women in developing countries and also to address issues beyond those envisioned by the early leaders, such as pornography and social security benefits allocations.

Founding Mothers

Elizabeth Cady Stanton, a social activist in the temperance and abolition movements and an experienced journalist, and Lucretia Mott, also a committed abolitionist, set the date and the tone for what became known as the Seneca Falls Convention. It was envisioned as a relatively small gathering in a local chapel to discuss the social and civil rights of women. They advertised with a small notice in the *Seneca County Courier* and invited their respected friend and orator Frederick Douglass to speak. His presence and reputation as a freed slave was indicative of the close ties between the women's movement and abolitionists. In preparation for the convention, Stanton gathered her beliefs, grievances, and goals into a Declaration of Sentiments, modeled after the U.S. Declaration of Independence, opening with the assertion that all men and women are created equal.

The 2-day conference, reportedly attended by some 300 participants, focused on debating the resolutions contained within Stanton's Declaration, the most contentious being the call for women's enfranchisement through equal voting rights. Most of the resolutions were passed unanimously and claimed equal rights in property ownership, educational access, civil and religious leadership roles, marital status, and trade and professional labor. The demand for women's vote was seen as too audacious by many within the movement and it was shocking to outside observers. Stanton saw it as absolutely foundational to all other rights, just as the American patriots had argued in their early rebellion against the rule of the British monarchy.

The Seneca Falls Convention gained unexpected and wide press coverage, nearly all of it negative, except that by Frederick Douglass's newspaper *The North Star.* While there were strong ties between the abolitionists and the women's movement, these social activists were fighting for radically different kinds of liberation. Blacks were fighting against oppression and the view that they were a race of lesser human beings, unable to excel, learn, and lead. Women were fighting against excessive protection and the view that they were delicate and should be limited to the realm of family life. Sojouner Truth's 1951 speech, "Ain't I a Woman?" was a powerful cry for equal rights for black women within the women's rights movement. While women and men of both races continued to participate within the women's movement, dissension about full participation mirrored the widespread disagreements throughout the country about the true equality of the races.

The Declaration of Sentiments had expressed the strong hope that future conventions would be held all across the country to rally broad support. Indeed the impetus created by the Seneca Falls Convention, and furthered by Quakers, abolitionists, and temperance workers, did result in a series of local gatherings. Speeches were made, petitions were circulated, and a surprising number of ordinary citizens listened carefully. As the country erupted in civil war over economic and civil rights, women took on greater responsibilities beyond the family circle, and as happened nearly a century later, many women emerged more confident of their own abilities and more ready to demand full legal rights. However, the supporters of women's suffrage were still a minority.

Working for the Vote

Over the latter half of the 19th century, women's right to vote emerged as the major focus of the women's movement. There were certainly other critical issues facing women, but it was the consensus of the activists that by obtaining the vote, they would be in a better position to determine social policies that would better their lives. Susan B. Anthony joined Stanton in 1869 in founding the National Suffrage Association. Although the right to vote was the main platform of this organization, it was also committed to other issues related to women's rights, such as workers' rights and labor unions. In the same year, the more conservative American Woman Suffrage Association was formed by Lucy Stone, Henry Blackwell, and Julia Ward Howe. The groups differed on strategies and tactics, a central question being whether to focus on a constitutional amendment or state by state referenda. By 1890, the associations merged into the National American Woman Suffrage Association (NAWSA), concentrating efforts on the passage of a constitutional amendment. In 1890, Wyoming became the first state to grant women the right to vote in all elections. However, another 30 years passed before this right was secured at the federal level.

Many arguments against women's suffrage were voiced, even by women themselves. Some claimed that women didn't want the vote, that women would only add to the number of unqualified and insufficiently educated voters, or that it would jeopardize national security. Others suggested that differences in women's biological and social nature would prohibit them from properly apprising the issues and candidates. The pro-suffrage arguments focused on principles of equality and liberty, and more pragmatically, the beneficial social changes women could make if given the vote.

The early decades of the 20th century saw intense political debate about women's suffrage as the activists regularly engaged in disruptive demonstrations and White House pickets extending for months. In 1919, the 19th amendment favoring women's suffrage obtained the necessary votes in Congress to be sent to the states for ratification. It was ratified on August 18, 1920, granting women the right to vote. Shortly thereafter, the National League of Women Voters was created from the remnants of the NAWSA as a nonpartisan organization whose goal was to help newly enfranchised women exercise their voting rights and responsibilities.

A key leader of the National Women's Party, the radical wing of the suffrage movement, Alice Paul, recognized that obtaining the vote would not entirely solve women's struggle for equal rights. By 1923, Paul had drafted an Equal Rights Amendment, proposing a broad assurance that men and women would have equal rights throughout the United States. But Congress was not willing to tackle this debate again, having weathered the suffrage issue so recently, and the proposal was sent off to congressional committee where it languished for nearly 50 years before reemerging in 1972 for reconsideration.

The Battle for Birth Control

Meanwhile, as the push for suffrage was beginning to succeed, another issue central to women's freedom gained national attention. If women were ever to be free to play a major role in politics or business, they would need to have some control over the demands of pregnancy, childbirth, and child rearing. Margaret Sanger, a public health nurse, argued vehemently that women must have the right and the opportunity to learn about and obtain birth control to control their own bodies. That a woman would publicly advocate educating women about their bodies and sexual functions was appalling to a large part of society. In the late 1800s, the Comstock Law had been passed, prohibiting transportation of obscene, lewd, or lascivious material. Contraceptive devices and contraception educational information fell into the lewd and lascivious category, prompting Sanger and her followers to consistently defy this law by publishing birth control information and distributing it broadly. In 1916, free-love advocate and anarchist Emma Goldman was arrested for distributing birth control literature in New York and successfully gained national publicity with her ensuing trial. The same year Sanger opened the first family planning clinic in New York, but it had a short life before it was shut down by police for violating the Comstock Law.

The first legal birth control clinic was established in 1921 by Sanger and two colleagues, concurrently founding the American Birth Control League. By 1936, birth control under medical supervision was legalized in many states, but Sanger recognized that this kind of access was insufficient for many of the women who needed birth control the most. Estelle Griswold and Dr. Lee Buxton opened a birth control clinic in Connecticut in the early 1960s expressly to challenge a state law banning the sale of contraceptive drugs and devices. In 1965, *Griswold v. Connecticut* was taken to the Supreme Court. The Supreme Court declared the Connecticut law unconstitutional, stating that it violated the right to marital privacy, and effectively legalizing birth control for married couples in the United States.

Margaret Sanger died a few months later at the age of 87, having devoted her life to furthering women's right to control their own sexuality and reproduction. She saw this issue in terms of a woman's right to choose the course of her life and to control her own body. Some critics of birth control saw it then as now as interference in a divine plan. Others saw it as interference in man's right to patriarchal control of his family. That women might be free to choose their livelihood and to control when and if they became mothers was startling and disorienting to many people who believed that women's essential purpose was to reproduce and raise families. As women gained the freedom to express their independent views, it was increasingly clear that not all women were willing to settle comfortably into that stereotype.

The Second Wave

What is referred to as the second wave of the women's movement, a broad collection of feminist activism, gathered momentum through the 1960s. Numerous factors contributed to this broad-based swelling of concern and interest in women's rights. In 1961, the director of the Women's Bureau of the Department of Labor urged President John Kennedy to take an active role in addressing workplace discrimination against women. Kennedy appointed Eleanor Roosevelt as chair of the newly formed Commission on the Status of Women, and their report in 1963 documented widespread gender discrimination. State and local commissions for women were promptly established and followed the federal lead in recognizing discrimination as a problem that demanded innovative solutions.

The Feminine Mystique, published by Betty Friedan in 1963, is commonly seen as an early impetus of the 1960s wave of the women's movement. Based on a survey she had conducted among fellow Smith College graduates, in anticipation of their 20-year class reunion, Friedan described the deep dissatisfaction felt by women who were trapped into homemaker roles by social expectations and limited work opportunities. It was the first book to articulate the anger and enormous frustration experienced by middle-class educated women at the widespread intellectual oppression. Friedan's book, immediately controversial, sparked an activist flame among hundreds of thousands of women who realized they could look beyond their homes to fulfill their potential.

The Equal Pay Act of 1963, signed by Kennedy, went into effect in June, 1964. It was designed to reduce the pay differential between men and women for substantially equal work within the same organization.

Title VII of the 1964 Civil Rights Act subsequently prohibited employment discrimination on the basis of race, religion, national origin, or sex. The ensuing Equal Employment Opportunity Commission (EEOC) was established to investigate the enormous number of discrimination complaints, but it was quickly apparent to watchful feminists that the EEOC was either unwilling or unable to address these complaints adequately. In response Betty Friedan joined forces with women leaders of several state Commissions on the Status of Women to form an organization that would lead the fight for women's civil rights.

The National Organization for Women (NOW) was established in 1966 for the stated purpose of bringing women into full participation in the mainstream of American society, with equal rights and privileges as men. Betty Friedan served as the first president of NOW and worked closely with Rev. Pauli Murray, the first African American woman Episcopal priest, to draft the early statements and guidelines of the organization.

In the late 1960s, NOW was sharply divided over the inclusion of lesbian feminists. Notable lesbian members complained about being marginalized, and Friedan and others admitted candidly to their discomfort with lesbianism. A group of lesbians, calling themselves the Lavender Menace, took the stage at NOW's 1970 Second Congress to Unite Women, expressing their anger at the evident homophobia. An open discussion resulted; the emergent understanding and acceptance directly shaped NOW's feminist stance and activism. By the 1971 NOW conference, a resolution was passed recognizing lesbian rights as a legitimate concern of feminism. The 2006 NOW statement of purpose makes it clear that the organization stands against all oppression, including racism, sexism, and homophobia, as well as classism and ableism.

While several of these issues have been adopted in society as appropriate targets for legal action, such as racism, and discrimination against people with disabilities, NOW's championing of the rights of the gay community and the rights of women to choose an abortion if necessary have provoked a significant backlash among more conservative citizens. Many people do not accept that gays and lesbians should be able to marry or raise children, or that they should be free from discrimination in their jobs. Many people also do not believe that abortion should be a legal right for women. Over the decades of the second wave of feminism, words such as "strident" and "aggressive" were used to characterize and denigrate NOW's style of advocating for freedom from oppression. As a result, fewer and fewer women were comfortable being characterized as feminists, although they might readily state that they were in favor of equal rights for women.

Among the opponents of NOW and liberal women's rights groups have been other activist groups identifying themselves as profamily. They argue that women's demands for equality with men, for example, in business or the military, result in higher divorce rates, a loss of reliable parenting for children, and more conflicts in the home. These activists argue that men's roles and women's roles should be distinct, that a family should have a mother and a father, preferably with the father working, and the mother focused on parenting or homemaking.

Equal Rights

From the 1960s through present day, women's groups, both local and national, have organized to protect women such as battered women's shelters and rape crises centers, while other organizations have provided women with health information, birth control, reproductive planning counseling, and abortion services. For most feminists, the availability of these services and protections are part of obtaining equal rights within society: the right to physical safety, the right to make decisions about work and family, the right to complete health care information, and the right to protect one's children. Most of these are issues that women's rights groups have addressed since the Seneca Falls Convention, more than 150 years ago.

In 1972, Title IX was included in the Education Code specifying that girls and boys should have equal access to education programs. The number of women in professional schools and the resulting professions has more than quadrupled in the past 35 years. Ultimately, "equal access" was understood to include resources for athletic and academic programs at the elementary, secondary, undergraduate, and graduate level. The inclusion of athletic resources in the Title IX mandate was fiercely debated, since the reallocation of limited resources to women's sports forced the reduction of some men's sports. As a result, girls' and women's participation in sports has seen a phenomenal increase, from high school teams through the Olympics.

Another key issue articulated by the Seneca Falls activists was women's right to own property and maintain their own financial assets. Financial independence has been one of the most recently won stages of women's social equality. Only within the last quarter of the 20th century have women been able to get a bank loan without a male cosigner. Well into the 1970s, married women were issued credit cards exclusively in their husbands' names. Women's salaries were routinely set lower than men's for comparable work. While women have not yet achieved full earning parity with men in many jobs, women in most democratic countries are now able to obtain loans, bank accounts, credit cards, make investments, and own property, without being asked questions about marital status or being given permission by men.

As women have gradually been accepted as working peers in business, government, and educational institutions, these organizations have been forced to face new questions about schedules, employee expectations, and benefits. With women working through pregnancies and child-rearing years, new policies have been articulated regarding leave for maternity, birth, and parenting responsibilities. These have now been extended to include men's parenting responsibilities as well as women's. Parenting issues have prompted a review of other related concerns such as the needs of an aging workforce to look after aging parents or parents with disabilities. These are not just the concerns of human resource departments. The traditional, that is, 1950s and 1960s, norms of the ideal worker, one who puts his or her job before any personal interests or demands, have been dismantled. While men and women in most jobs need to sacrifice many aspects of their lives to the priorities and demands of work, there is a greater tolerance for workers with whole lives. Many workplaces have created flextime for white-collar jobs, and have made adaptations to the realities of men's and women's lives outside of work, in the interest of building a loyal workforce.

However, more women working full-time has meant fewer women home with children. As a result, there has been a greater need for alternative sources of child care, full-time as well as before and after school. This need is addressed in part by many elementary schools offering extended child care to cover hours when parents are not at home. Other families have solved the gap by hiring babysitters or nannies. But millions of children are left to take care of themselves at home alone while parents work. The problems of these "latchkey" children and youth, for example, watching too much television, spending unsupervised time on the Internet, eating junk food, experimenting with alcohol and drugs, engaging in early and promiscuous sexual activities, are frequently attributed to be the fallout of increasing numbers of women working outside the home.

New Issues Emerge

Although society is still working on achieving some of the basic issues of women's rights that were recognized by the Seneca Falls Convention, contemporary discussions include a range of concerns that reflect a dramatic reshaping of our social abilities and available options. For example, should affirmative action programs seek to address and compensate for past discrimination practices in employment and education? Should a woman be free to hire out as a surrogate mother by carrying a baby to term for another woman or couple? Should women be accepted into the military service as active combatants? Whose responsibility is it to establish the boundary between flirting and sexual harassment? Should businesses be expected to accommodate women's reproductive lives by providing child care services or enabling them access to competitive jobs even after time off for motherhood? Should men have equal time off for parenting responsibilities?

Many of these questions have been successfully addressed in other countries. For example, Norway, among others, has generous parental leave policies, with little or no adverse effects on job advancement. Israel has long accepted women into military service. The professional opportunities for women also vary dramatically around the globe, from countries where women have served as prime minister or president, to countries where women have not yet achieved the vote or the right to attend school.

The women's movement in the United States has achieved significant accomplishments in women's educational, political, professional, social, and civil rights over the past 160 years since the Seneca Falls Convention. There is much to be celebrated and recognized as the work of women and men dedicated to equality in daily life. However, a great deal still remains to be done for women to be fully represented in state and federal legislatures, in all branches of the government, and in the many corporations that control much of the wealth of the country. Given the history of the women's movement, the potential for ongoing development in equality is strong.

—Robbin Derry

See also Affirmative Action; Birth Control; Civil Rights; Comparable Worth; Employment Discrimination; Equal Employment Opportunity; Equal Opportunity; Equal Pay Act of 1963; Feminist Theory; Gay Rights; Gender Inequality and Discrimination; Patriarchy; Pornography; Women in the Workplace

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WORK AND FAMILY

The expectations of an organization and the ability of a worker to balance professional obligations with family responsibilities is a topic of great importance to society, its organizations, and individuals. For millions of working adults, questions about how to balance the needs of their employer with the needs of their personal lives provides a daily challenge. For work organizations, the ability to develop and maintain a stable workforce capable of achieving the organization's goals is not a simple task. When employees face personal demands that conflict with work requirements, organizations can suffer. Organizations need their employees to focus on their jobs and not be distracted by competing demands on their time created by children or aging parents. The balance of work and family at the national level involves policy decisions regarding the allocation of scarce resources, as well as regulatory decisions.

From a societal perspective, current work-family balance pressures stem from a market-based economy. By their design, market-based economies are based on a structure whereby people are largely self-sufficient and are rewarded for hard work. Adults are expected to provide for themselves and their families. Increased economic pressures are pushing more people into the workforce and transforming the jobs people perform. Previously stay-at-home spouses now often work part-time or full-time to help their family financially. The increased pressures on families and the effort required to care for households place stress on our national infrastructure and support systems. Tasks once performed by a family member are now often contracted out. The increased demand for services, such as child care, has spawned a growth in service-based businesses.

From an organization's perspective, work settings require employees to trade their talent and time for compensation. Increasingly in the United States that trade-off is not a simple one. The expectations that employers place on employees are increasing. Technology, once designed to liberate people from their desks, now gives employers unlimited access to their employees regardless of time or location. Foreign and domestic competition forces employers to place greater emphasis on productivity and efficiency. In addition, organizations are challenged with the task of motivating and retaining an increasingly pressured workforce. Organizations today face more competition, and this forces them to increase their demands on employees.

The question of an appropriate work-family balance is often felt most closely at the individual level. Demands for working adults are increasing both professionally and personally. For salaried employees, the 40-hour workweek has often expanded to 50 or more hours per week. Contingent workers now face the task of working more than one job in order to maintain economic stability. Employees also have personal lives that require maintenance, and for some people, this can be a significant drain on one's time. The end result is that people are pushed to the limit.

Obviously, work-family balance issues are important for us nationally, organizationally, and personally. The issue of work-family balance involves a complicated interplay among three factors: societal issues, organizational issues, and personal issues. All these factors culminate in a network of support systems. Although the list may not be complete, these key factors provide both a context in which to become informed on the topic and serve as a mechanism for exploring solutions.

Work-life balance refers to the integration of a person's personal and work life and is particularly complex when an employee has family obligations. Some argue for a separation between these two components in one's life, others assert that the integration of one's work and personal life can be a source of synergy or stress. The three core factors, societal issues, organizational issues, and personal issues provide an interplay that profoundly affects the success with which one can live an integrated life.

Societal Issues

In a broader historical context, work-family balance issues seem to have intensified as the wealth of the community allows people more leisure time. It is true that many Americans have the wealth to live at a more leisurely pace, but our society is typically characterized by a long workweek and high-stress work environment. Four recent trends point to a far more complex set of trade-offs that confront the average worker or family: increased household hours spent outside of the home, increased dependence of families on market-based support systems, more geographically dispersed communities, and decreased national attention to potentially harmful working conditions.

Time Demands

The rising costs of housing, health care, and education are putting pressure on families to collectively work more hours, as wages fail to keep pace, particularly during cyclical economic downturns. The classification of the worker determines whether the length of the average workweek has increased in recent years. The average workweek for hourly wage earners has not changed significantly in the past 30 years; 40 hours is still the standard. For professional or salaried occupations, the workweek is often longer.

But a definite trend is the increasing number of dual-income households and single working-parent households. The number of married women participating in the workforce has increased from 35% in 1966 to 61% in 1994. Married women who were part of the workforce and who had children less than 3 years of age increased from 21% to 60% over the same period. Single-earner married couples are no longer the norm. A majority of children do not have the benefit of a stay-at-home parent. Compare this with 65 years ago when two thirds of all households consisted of a married couple with a single-income earner. From 1970 to 1993, the proportion of dual-earner couples increased from 39% to 61% of all married couples.

Furthermore, more hours are spent in transit to the office and driving to and from other non-work-related obligations, such as dropping off and picking up children at school or day care, running household errands, and visiting extended family. This means less time for leisure and domestic tasks that require routine attention. Consequently, there is a growing dependence on services to compensate for increased hours spent at work and on the road. And coordinating and managing these many services points to yet another dimension of the organization and time-management challenge that is at the heart of the work-family balance issue.

Reliance on Market-Based Support Systems

Support systems for individuals and families take four forms: personal, employer, government, and market-based. It is important to see first how the increased dependence on market-based services over the other forms of support is reshaping communities and society as a whole.

Personal support systems traditionally consisted of family members and friends are, for many demographic groups, largely disappearing, with families relying on a patchwork of costly professional services to manage home or domestic life. This phenomenon is in part due to the greater mobility of the workforce, which results in families moving away from their extended families and established communities for a better job. The increased presence of women and, more recently, retired-aged people, in the workforce also diminishes the role and availability of these traditional support systems.

Government support systems are largely aimed at families either living below the poverty line or unemployed for extended periods of time. Employer-provided support systems, in the form of services and benefits, can be fairly extensive, but are also scaled out and back as the labor force contracts and expands, respectively, and thus are not a consistent source of support.

Not surprisingly, working families have come to rely on commercial services. As an increasing number of collective family hours are spent in the workplace, and as other sources of support are either less accessible or less reliable, the demand for professional services has risen. These services include, but are certainly not limited to, laundry, house cleaning, child care, lawn care, handy work, mail order, and online retail for clothes and household goods, grocery delivery, and even dog walking. In fact, the service sector has grown to dominate the U.S. economy.

Although designed to help the full-time employee, these services are costly, and workers must weigh the costs in relation to the benefits of working full-time or more hours. For these services are costly, particularly during times of inflation, and may represent a significant share of the household budget. The amount spent on child care and education varies by household income. However, the growth in expenditures is telling. According to the U.S. Department of Agriculture, in 1995, the families in the lower third of the economic bracket spent $7,500 per year on child care. By 2005, that number had increased to $12,000 per family. For those in the upper third, the amount was $20,760 in 1995 and $36,000 in 2005. Clearly, the growth in cost has had the greatest impact on those who are least able to pay for the cost of child care.

There are real drawbacks in depending on professional services. Support systems are pieced together to bridge continuing gaps in services needed. And the quality of services is not easily ascertained as it might be when relying on personal or employer-based support systems. This means that households spend more time researching and identifying quality service providers. Fortunately, the growth in the Internet has facilitated the speed with which these assessments can be done.

Changing Geography

Community infrastructures that connect work and nonwork activities have become more geographically dispersed. The average commute-to-work time nationally is 24.4 minutes, according to the U.S. Census Bureau's 2004 American Community Survey. Many American workers also spend a considerable amount of time traveling nationally or internationally for work. Time on the road also contributes to work-family balance issues as it represents time away from family and home for which most workers are not explicitly compensated through their employer.

As metropolitan areas expand outward from the city center, people experience longer driving distances between daily destinations, whatever they may be. This work dispersal is a significant departure from the communities that existed in the mid-20th century, where families lived in closer proximity to one another, to work, and to other community commercial and public resources. Time spent in transit appears to be a significant contributing factor in the work-family balance tension. Some employers are responding to this constraint on their workforce by locating common services, such as a dry cleaning facility, child care, a post office, or a gym, on the work "campus."

Families with children face unique constraints on their time. Families are having fewer children, but the demands of keeping up with one child grow with a rise in school commitments, sports obligations, and other extracurricular activities in sprawling communities. Concern for safety means more organized, highly structured activities for adults and children. This increases the demands on people's time. The demand for time is also exacerbated with the very specific time demands for children's activities. Pick-up and drop-off from school must occur within a very narrow time window. Being 15 minutes late can have significant consequences for parent and child alike and adds to everyone's stress level.

Working Conditions

The incidence of depression and other stress-related psychological disorders are intertwined with shifts in work-family balance. Mental exhaustion is not given the same attention as physical exhaustion in the workplace. Consider the United States' many laws under the Occupational Safety and Health Administration (OSHA), designed to protect workers from physical harm while on the job. No such equivalent protections exist for mental stress due to working conditions. OSHA's laws largely resulted from union pressure for reform. But unions are, for the most part, absent in white-collar professions. Furthermore, unions do not carry the weight they once did in championing the causes of blue-collar workers. Employers also face increased competition, and their ability to respond to this challenge may be constrained by the marketplace. Persistent time constraints and work-related mental stress are as likely to affect the long-term performance and retention of workers across professions and, furthermore, the functionality of parents.

The impact of an overworked population on the long-term productivity, efficiency, and health of the nation is just beginning to be assessed. Workers are living on the edge and activities must run like clockwork to meet their conflicting demands. Pressure to perform on the job while maintaining some resemblance of a personal life further stresses individuals. One can explore the effect of exhaustion and stress on the individual. The increased potential for accidents at work, on the road, and at home due to current work patterns is an important issue.

Organizational Issues

Organizations play a pivotal role in the work and family balance of their employees with specific expectations and rewards based on market forces and individual performance. Organizations also provide workers with definite rules, policies, and norms that they establish for the work environment. Since organizations have a significant influence on their internal environment, they have real power to positively and/or negatively contribute to their employees' work-family balance. Nonetheless, organizations are influenced by many market forces that are beyond their immediate control.

Market Forces

Micro- and macroeconomic forces that influence work-family balance are interconnected. From a macroeconomic perspective, business cycles, globalization, growth in government, and inflation affect the labor market and the economy as a whole. Yet macroeconomic forces clearly affect individual job security and income potential and accommodations that employers can offer their employees.

Business cycles tend to strongly influence growth, unemployment, and price stability. When businesses are affected, so are its workers. Recessions tend to limit employment options, increase the cost of living, and increase work hours while economic expansion has the opposite effect. A second macroeconomic factor is the growing global competitive pressure on industry. The convergence of foreign and domestic markets has delivered increased financial opportunities to corporate America, but also raised the bar for U.S. companies. In the search for increased productivity, companies feel significant pressure to cut costs, boost profits, and consolidate businesses. Labor is expensive in the United States relative to other countries and, as such, companies look to technology and outsourcing to reduce costs and to distinguish themselves from their domestic and foreign counterparts. Large-scale layoffs and corporate cannibalization are common features of the current market environment and, as such, so are job and income insecurity for workers. Contributing to the problem are frequent incentives for top managers to orchestrate layoffs and implement other cost-cutting policies.

The significance of the growth in government—as an employer and contractor—should not be underestimated. U.S. federal government expenditures represent roughly 20% of the total U.S. economy. Its increased presence in the economy over the last century has both detracted from and added to work-family balance.

Government agencies are serving as testing grounds for new employment and workplace practices, such as the 9-hour workday with one day off every 2 weeks, on-site day care facilities, and job-share programs. Traditionally, the private sector lags behind in introducing such practices, but they tend to seep into the fabric of mainstream employment practices eventually. But there is some evidence that the growing size of government and its federal deficit may be crowding out other forms of investment. While federal spending for national defense and social insurance programs increases, local and state spending is shrinking, and many social service programs for families, such as support for public education systems and social services, are being downsized or eliminated. Finally, the increasing costs of health care, housing, education, child care, and elderly care are significant burdens on American households and, in part, explain why more families rely on a dual-income earner model for added financial security.

Microeconomic issues also play a role in work-family balance. Industry consolidation has meant that more and more workers are employed by mega-corporations rather than a locally owned or smaller, regional business. On the one hand, large, national and international businesses have more resources—both human and technological—at their disposal that allow them to more easily accommodate flextime, or virtualized, working arrangements. On the other hand, they are less apt to be attuned to individual employee needs. In addition, large corporations are typically public companies that are accountable to shareholders with increased pressure to cut costs and increase profits. This may detract from the flexibility of the corporation to create policies that relieve pressure on their employees.

Labor Force Supply

Whereas two-parent families once divided responsibilities so that one spouse focused on work outside of the home and the other, inside the home, today both parents typically work outside of the home. In addition, single-parent households are far more prevalent. These days, more than two thirds of U.S. households have children, with more than 25% of those households having only one parent. Because households are constrained in this way, family members must be more proactive in pursuing unique job arrangements such as job shares and contractor, consultancy, and shift or part-time work arrangements.

Job shares allow two workers seeking more flexible schedules to effectively share responsibilities that equate to a single 40-plus-hour per week job. For many jobs, part-time hours are impractical, given the nature and scope of the work involved. Two professional employees may either split the project load associated with a job in half or overlap on projects, seamlessly shifting work back and forth between them. Hourly paid work also accommodates a job share construct. The downside for employers is that they might need to cover health care and other benefits for two employees, rather than one. On the other hand, the flexibility can lead to higher retention of existing employees and a deeper and richer worker pool to draw from when looking to hire. In addition, the employer might arrange a collective 50-hour week with its job share employees, while it can contractually only require 40 hours per week from its traditional employees.

Workers wanting more control over their hours and the ability to flex their hours up and down as needed might choose to become contractors or consultants, thus allowing them to accept or reject work on a case-by-case basis at a negotiated rate per hour or flat fee. The term *contractor* was once primarily associated with the construction industry. But now it is fairly common for companies to rely on contractors and consultants offering a broad array of professional and manual services, particularly in less certain economic times. Because contractors and consultants are not employees of the company, companies can readily terminate or cut back expenses associated with this workforce, as needed. On the other hand, employers can add depth to their workforce quickly without burdening the company further with costly health care and retirement benefits associated with permanent employees.

Many workers will move in and out of the part-time workforce, accepting work only when their household is experiencing a financial crunch. For example, many stay-at-home parents will seek part-time employment or shift work when their children enter college to supplement the household income. As the rate of inflation for college tuition rises, alternative work schedules are becoming a more common scenario.

Employer Demands

Employing organizations face conflicting demands. Productivity is a serious issue for organizations because they must remain competitive to survive. Successful organizations rely on a loyal and committed workforce and must get the most from their workers on a per-hour basis to maintain their market position. Yet organizations must be concerned with the work and family balance of their employees, and pushing their people too hard can force breakdowns, resulting in medical and personal consequences for the employees and negative impacts on productivity.

Personal Issues

Demographics

The demographic issues that significantly affect work-life dynamics include age, gender, education, and family status. Because responsibilities differ by stage in life, the age of the worker profoundly affects the tension felt in work-family balance. Those with split responsibilities either for the care of children or aging parents feel the pressure most acutely.

A person's age has the potential to shape expectations for work and personal life. One's age (and life stage or career) can influence the meaning of work, expectation of employer, ability to work varied work hours, and demands outside the work environment. People early in their work life typically have high energy and are interested in quick advancement to positions of increased responsibility. Working long hours is less frequently a problem for this group, and outside interests may or may not provide a work-family balance issue. People in mid-career frequently have significant interests and demands outside work.

Individuals in the later stages of their career frequently have more difficulty working long hours and may have reached a career plateau or are preparing for retirement.

Gender can play an important role in work-family balance for several reasons. Two factors are particularly critical. The first area is equal pay and the second is sex segregation in the workplace. Although laws require equal pay for equal work, the definition of "equal work" is narrow, which means that "equal pay" is frequently not a reality. Women are often paid less than men in comparable jobs, usually justified by subjective factors such as commitment and ability to work extra hours. The practical reality of lower pay means that unless women are able to otherwise compensate for their lower pay, they will likely have a lower standard of living than men. Another more pervasive location for gender influence in the work-family balance is in the choice of careers. Although men and women are free to choose their careers based on personal interests and ability, men and women tend to cluster in different career paths. Historically, men have chosen to become physicians or engineers. Women have pursued comparably lower-paid jobs in education and nursing.

Usually, the more education people have, the more choices they have in regard to their employment. Advanced college degrees usually prepare people for professional and highly skilled jobs that require more hours than the standard 40-hour workweek. Individuals with lower degrees of education frequently get paid by the hour, and given increases in the cost of living, many hourly employees need additional work to supplement their income. Both educated and less educated workers feel pressured in balancing work and family needs; yet those who are educated usually have more options and are less likely to remain in a difficult work situation.

Family status plays an important role in work-family balance because of the importance and time commitment that family members require. Single working adults can frequently focus on their work more fully because they do not have a family that needs to be accommodated. While single people may struggle with work-family balance and avoid acute child care pressures, single people with responsibilities for aging parents may find themselves in a similar bind as their colleagues with children.

For families, the work-family balance issue is heavily weighted on two factors: Do both partners work, and are there children in the family? Increasingly today, both partners have jobs outside the home. With both partners working, much of the work previously completed by a stay-at-home spouse is either done after work or contracted out. Assuming both partners work full-time, the coordination needed to perform basic household duties can become overwhelming. Contracting others to perform some or all of these tasks can be expensive and not always a viable option, as noted previously.

Work Environment

Many of the balance issues faced by employees stem from the working environment. Specifics of the job can either make the balance between work and life easier or more difficult. The work environment falls into two categories. The first relates to income. The second relates to working conditions, and this refers to work specifics such as number of hours worked, flexibility, and ability to enter and exit the workforce.

A person's income has the potential to influence the work and family balance. Of primary concern is the level of income. Does a person make enough money to meet financial obligations to hire others to perform support services? Being able to buy a support system frees up the employee's time for other responsibilities.

An employee's working conditions also influence family balance. The number of hours worked per week is a critical factor in determining life and work balance. The more employees work, the less time they have for their personal obligations. The work-family balance issue for an employee who works 20 hours per week cannot be compared with someone working 60 hours per week. Not only does the number of hours worked count, so too does the flexibility of those hours. Does an employee have the ability to change the work schedule to accommodate personal appointments? Flexibility of hours worked can play a significant role in how people can use their time to take care of personal business.

Another issue is a person's ability to enter and exit the workforce based on personal needs. Some careers offer the ability for people to work part-time without major consequences. Other careers offer people the ability to enter and exit the workforce based on what their personal needs are. For example, some people may be able to leave work for several months to take care of personal business and then return to work without difficulty. The ability or inability to do so can go a long way in helping a person be an effective employee as well as a responsible person.

Work Location

The geography or area in which people work can influence their life's balance in a number of ways. The cost of living varies significantly across the country. How much people have to pay for rent or their mortgage determines what type of job they seek. In cities that have a high cost of living, people frequently move to the outskirts and then commute 1 or 2 hours each way to work. A high cost of living and/or high commute time can limit how one spends time away from work.

Often the type of work correlates with where people must live. Employers from one industry frequently position themselves near each other and create a synergy for employment in that field. To succeed in some fields, one must be willing to live near the key employers. Location can be a limiting factor when there are two people working in a household, each with different skills resulting in different optimum locations. The phenomenon of married professionals with competing careers has caused the number of nonmilitary couples who are temporarily separated in their marriage to rise. About 7% of married couples are temporarily separated due to the demands of their careers; this amounts to millions of couples. Care of the nuclear family becomes problematic with separated couples. The demands of caring for children with one parent who spends a great amount of time on the road increase exponentially for the parent or worker who remains in the home city.

Support Systems

Households do not exist in a vacuum. Numerous support systems for individuals and families form a network, although not a seamless one. That network is composed of four general categories: personal, employer, government, and market-based. Personal and government support systems might have represented the core support systems at one time. However, as these structures have contracted, employer- and market-based services have begun to fill the void left behind. But this trend has perhaps also led to the increased self-reliance of American households.

Family, friends, neighbors, and community groups have traditionally served as key resources for households. Even today, they offer a breadth of support in the form of social outlets and security systems, both financial and physical. Social outlets, whatever form they take, provide stress relief and a means of decompression from work. Such outlets are not something that can be readily replaced by either employers or products; yet these systems do influence the form they take. For example, people may be more socially intertwined with their work colleagues or people they've met in a personal financial management class than they are with their neighbors.

Support from friends and family might also serve as a financial safety net in the event that a person loses a job or experiences financial hardship. The government may step in, in such situations, and offer relief in the form of unemployment insurance or welfare, but there is a stigma associated with this form of assistance that is not necessarily an issue when relying on family or friends for financial support, and benefits are limited. Another component of the personal security system is physical support in the event of an illness or threat of harm to body or property. The universal time crunch has resulted in perhaps less reliance on friends and family and more dependence on contracted services. For example, people might need in-home care for a family member released from the hospital after surgery when unable to take time off from work or rely on extended family members for assistance. But whether people have the same degree of confidence in this support mechanism and can afford such contracted services, is a separate question.

The increased geographic mobility of the workforce has put significant physical distance between extended family members and lessened the degree of involvement in, and continuity of, community-based programs, such as neighborhood associations, neighborhood watch, carpools, and so on. As people spend more time outside of the home, there is less time to interface with these personal networks that are tied to one's home.

Paying for support systems is a relatively new phenomenon. An increased reliance on contracted services stems from both push and pull factors. On the one hand, technology has been a catalyst for significant growth in both the services and consumer products markets. On the other hand, the evolving demand for products and services that serve to fill the time vacuum is leading to expansion in these markets.

Employers are induced by market forces to make available and, in many cases, subsidize "concierge" services for employees, much as they are induced to provide standard benefits, such as 401K matching and stock options. Benefits of every kind increase when the labor market tightens. During the 1990s, when labor markets were extremely competitive and the technology boom was at its peak, many on-site services were born (on-site discounted vacation and theater-booking services, dry cleaning, windshield repair, banking, and limited health services). But when the economy contracts, these services may disappear and employees must turn to the other three systems of support for assistance.

Market- and employer-based support systems are explicitly a function of the market in the sense that their provision is profit driven. But personal and government support systems are implicitly a function of the market. Financial and physical support from family members and friends are likely to decrease during economic downturns due to constraints on time and money. Government support systems, which tend to be countercyclical, often expand during economic recessions to offset the impacts on the economy, but the size of government deficits limit its ability to function in this way. Efficiency and equity are, therefore, undisputable tradeoffs because the risk of not having adequate support systems is an underperforming, overburdened workforce.

Conclusion

Given this brief discussion on the issues of work and family balance, a number of issues arise. At a macrolevel is the question of whether work and family balance is important. Research that tracks the health and well-being of humans suggest that the costs of not integrating work and personal lives are significant. These costs are illustrated on a microlevel for individuals, organizations, and society.

On a personal level, as humans with intrinsic value, ethicists assert that workers deserve to be able to work with dignity and not feel that they are sacrificing their personal lives in the process. The costs of disintegration between one's work and personal life comes in the form of stress, increased costs due to contracting for personal services, and mental and physical health breakdowns.

In many ways, organizations are the center of this discussion on work and family balance. Their response to increased competition has been to expect more from employees. This expectation is not an irrational response from the organization's perspective. Their survival depends on the talents and efforts of their people. However, employees are increasingly stretched. Organizations have a responsibility to remain competitive, while also providing job opportunities that are sustainable for human and organizational life.

At a societal level, the work and family balance issue is also important. The government is responsible for distributing common resources and as such, can fund programs to ease pressures on those working. The government is also in a position to influence labor law and provide incentives to those organizations that honor those who work.

As those in the "baby bust" generation, those who are in their mid-30s, move into positions of responsibility, the conversation may change. Many fathers of this generation are unwilling to miss out on the joys of parenting. Because comparatively their numbers are small, this generation can demand flexibility where in times of a glut of labor, the negotiating power of the employee is not high. The conversation among individuals, employers, and the government will continue as we strive to both maximize productivity and assure healthy, well-balanced personal lives.

—Robin S. Koenigsberg,
Aimee Wheaton, and
Catharyn A. Baird

See also Affirmative Action; Comparable Worth; Diversity in the Workplace; Employee Assistance Programs; Equal Employment Opportunity; Equal Pay Act of 1963; Family-Friendly Corporation; Feminist Ethics; Gender Inequality and Discrimination; Living Wage; Meaningful Work; Stress, Job; Work-Life Balance

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Worker Rights Consortium (WRC)

The Worker Rights Consortium (WRC) is a nonprofit watchdog organization that helps affiliated colleges and universities enforce manufacturing codes of conduct in factories that produce clothing and other goods bearing their names and logos. The WRC has authored its own model code of conduct that includes, for example, provisions requiring payment of a living wage and compliance with the Occupational Safety and Health Administration (OSHA) health and safety standards. However, while the WRC encourages affiliated schools to adopt a code as strong as the WRC code, it does not require that they do so. The WRC conducts investigations of working conditions at factories where university goods are produced. When problems are identified, the WRC works with licensees, factory managers, workers, and worker advocates to correct the problems. According to WRC's Web site, the investigations are carried out by teams comprising "knowledgeable representatives of the local community, including officials of local labor rights NGOs and/or local academic experts, and at least one member of the WRC staff or Governing Board." The WRC launches factory investigations in response to worker complaints or on a proactive basis—for example, where local nongovernmental organizations (NGOs) suspect there are problems or where there is little information about a major source of university goods. The WRC's Web site says that it is committed to "meticulous objectivity and methodological rigor." The results of these investigations are published on the group's Web site.

The WRC says that the collegiate licensing is now a $3-billion-a-year business. Schools earn 8% on the wholesale value of the apparel they sell. In 2005, the University of Texas earned $5 million in licensing revenue. The companies that pay schools these royalties in exchange for the right to use their logos on caps, sweatshirts, jackets, and other items range from Ben Silver Blazer Buttons of Charleston, SC, to Nike.

There are more than 150 colleges and universities affiliated with the WRC. Affiliates agree to adopt a manufacturing code, advise the WRC of the names and locations of factories that produce their logo goods, and pay the WRC fees that are $1,000 or 1% of gross licensing revenues (but no more than $50,000), whichever is greater. Roughly 40% of the WRC's funds come from affiliation fees. The remaining 60% is raised through grants from philanthropic foundations and the federal government. Past grantors have included the Rockefeller Foundation and the New World Foundation.

The WRC held its founding conference on April 7, 2000. The organization's Web site claims that it was created by college and university administrations, students, and labor rights experts. That may or may not be technically accurate, but the reality is that the impetus behind the WRC was student antisweatshop activists in United Students Against Sweatshops (USAS) together with UNITE (the apparel and textile workers union) and labor rights activists. USAS itself had been suckled by the AFL-CIO. USAS disrupted campuses by means of tactics such as occupying the offices of college presidents and hunger strikes to coerce their colleges into affiliating with the WRC. Few, if any, college administrations have been able to resist these tactics.

The WRC was conceived by labor and its allies as an alternative to the Fair Labor Association (FLA). The FLA grew out of a Clinton White House initiative—the Apparel Industry Partnership (AIP)—to bring together industry, labor, and consumer and human rights groups to formulate labor standards for the overseas suppliers of U.S. retailers. However, three members of the AIP (the AFL-CIO, UNITE, and the Interfaith Center on Corporate Responsibility) eventually broke with the FLA.

The main points of difference between the FLA and the supporters of the WRC concerned (1) the code's failure to include a living wage provision (FLA required for the higher of the local minimum or prevailing wages, while the WRC called for a "living wage"), (2) the identities of the investigative teams that were to monitor working conditions (WRC guidelines called for the monitors to be "local worker-allied groups"), (3) publication of the findings of investigations (the WRC committed to publishing the reports), (4) inspections (the WRC insisted on carrying out unannounced checks), (5) certification of "good" factories (the WRC's guidelines barred colleges from certifying that companies were compliant with their codes of conduct), and (6) inspection schedules (the WRC charged that FLA would certify companies as compliant based on a single inspection of 30% of a company's factories every 10 years).

Developments of note since the WRC was founded include the fact the organization has backed off mandating that affiliates include a living wage in their codes of conduct. Many economists (even ones sympathetic to the antisweatshop movement) had warned that "living wages" might price workers in poor countries out of the world market. However, the WRC is considering a proposal for "designated suppliers program" that would phase in a living wage requirement. In the 6 years since its founding, the WRC appears to have completed reports on fewer than 20 factories. Compare that with the fact that goods with the University of Michigan logo are produced in 3,866 factories.

—Ian Maitland

See also AFL-CIO; Child Labor; Exploitation; Fair Labor Association (FLA); Global Codes of Conduct; International Business Ethics; International Labour Organization (ILO); Living Wage; Sweatshops; Working Conditions

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Work Ethic

The notion of work ethic refers to the personal character attributes fundamental to an individual's attitude toward work. Two key components of this concept are the internal qualities possessed by the individual and the external qualities manifested in work behavior. While down through the ages in both the East and the West the essential characteristics of good work behavior have been discussed, it is difficult to identify one specific set of desirable qualities, because work, and the manner in which it is approached, is a multidimensional human phenomenon.

How work is understood and valued depends on personal experience, as well as the meaning society places on human labor, productivity, and work commitment. During some periods of history, work has been perceived as degrading and servile, while at other times it has been considered noble and a sign of achievement and favor. Work can be viewed as a job, a mere service for hire. It can be an occupation or career, a particular desired line of employment or profession, or it can be a vocation, a calling that provides personal fulfillment. Each of these interpretations set different work expectations and values for the individual. For these reasons, some hold that there is not a universal work ethic.

Besides social norms and interpretations, there is another reason why a single work ethic is difficult to identify. Individuals work for a variety of reasons. During hard economic times, work is motivated by the need to survive, to obtain financial resources that enable the garnering of necessities such as food, clothing, and housing. When necessities are secured, a person's desires often turn toward purchasing luxury items and engaging in entertainment. On other occasions, work is performed to express one's self, or out of a sense of generosity or charity toward a friend or a person or group in need.

Work habits, attitudes, values, and ethics are all interrelated. An individual's work ethic expresses how the person comprehends the value of work, as well as personal accountability for performing tasks in an acceptable manner. A work ethic stems from an individual's personal life experiences and is shaped by work history, professional associations, education, culture, family heritage, religious affiliation, personality, and so on. The modern Western understanding of work ethic has been significantly influenced by a conceptualization of work grounded in perfection, the goodness of labor, and the necessity of hard work. This notion, rooted in Calvinistic thought, is often referred to as the Protestant work ethic, a concept founded in Max Weber's sociological analysis of religion.

Specific religious precepts no longer are associated with the 21st-century notion of work ethic, giving rise to a secular understanding of work and the factors that motivate people to strive for work excellence. For many, employment is a crucial aspect of life that provides personal value. It is not unusual, particularly in the American society, for a person's identity and sense of purpose to be closely related to a job or chosen career path.

Having steady employment that provides a reliable source of income is a significant factor for many people. A common American belief is that there is an unwritten social contract promising that honesty and hard work performed well will result in being able to afford basic necessities, and have economic profitability, safety, and personal fulfillment. Loss of a job can have traumatic effects, including decline of self-esteem, depression, and even suicide.

Globalization and technology have shifted the nature of work. For decades in the Western world, work has customarily been categorized as manual labor and professional work and described as full-time, part-time, and temporary. These categories are now too limited to capture all forms of work. Since many business enterprises are driven by information, more and more employees focus on processing information and managing organizational knowledge. This phenomenon has created a new category of employee known as the knowledge worker. This type of work draws on employees' mental qualities and skills rather than on their physical attributes and task-processing capabilities.

Organizations strive to hire workers who are dependable, persevering, perceptive, resourceful, self-initiating, adaptable, independent, collaborative, considerate, appreciative, dedicated, and honest. These attributes are considered by some to be the core elements of the modern work ethic needed for success and employability.

There is another dramatic change occurring in the workplace. Besides employees who have steady on-site work assignments with benefits, the modern workforce consists of contingent workers, individuals who are routinely contracted only on a nonpermanent, as-needed basis, and teleworkers, employees who work off site, at times from home, via phone and computer-based technologies. Employees working in either of these ways are confronted by several challenging work ethic issues. Contingent workers are challenged to identify with the employing organization and work with a professional commitment and loyalty comparable to permanent members of the organization's community. Teleworkers are faced with the responsibility of monitoring their work hours, ensuring they reduce nonwork distractions, focus on assigned tasks, and work the contracted hours.

Inherent in an organization's culture and managerial practice is a corporate work ethic. The demands of work in a postmodern information age are different from those of the previous industrial age. Globally dispersed teams, virtual collaborative work networks, rapid response times to market changes, and advances in information and communication technology have changed the way work is conducted. Organizations operate with smaller workforces. Job security is gone. Focus on gaining market share, maintaining profitability, and having competitive advantage, have led to long workweeks, with employees often taking work home. The boundary between work time and personal time has disappeared. This 24/7 work environment has increased workplace stress and strained employees' personal and family relationships.

Numerous layoffs, downsizing practices, and outsourcing strategies have severely eroded the sense of loyalty and commitment that once existed between employer and employee. Such a work environment marked by reduced trust and respect has left many workers feeling exploited and devalued. Some even question if hard work still leads to being rewarded personally and professionally.

For these and other reasons, a growing segment of the workforce believes that work is losing meaning and personal fulfillment. They seek a new business work ethic that respects employees as valued resources, and reestablishes the boundary between work and personal time, providing a healthy work-life balance, flexibility in employment schedules, and more control over their work time and careers.

—Charles F. Piazza

See also Integrity; Meaningful Work; Protestant Work Ethic; Virtual Corporation; Work and Family; Work-Life Balance

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WORKING CONDITIONS

Working conditions refer to a person's job environment. These conditions encompass aspects such as hours, safety, benefits, and advancement possibilities. They have become of concern because of the extent to which satisfactory conditions are denied or abridged. Determining which employee and employer rights and responsibilities should be recognized and appreciating the nature of the employment relationship are helpful in examining working conditions and their evolution.

Rights and Responsibilities

Working conditions and other employer responsibilities depend on the perceived rights of employees. There are at least two sources of rights—natural rights and civil rights. Natural rights are those rights that are considered universal and attributable to human beings vis-à-vis their *human* status, regardless of societal norms. Civil rights, on the other hand, exist as created by a particular society's legal system. They tend to be relatively clear: They are codified and exist in writing. While there can be overlap between legal and natural rights—such as in the Bill of Rights of the U.S. Constitution—many legal rights are recognized only by particular societies and are not presumed to be natural rights. Many legal rights are, therefore, only culturally sanctioned and are thereby limited in their application.

Civil rights are central to the relationship between employees and employers. In most countries around the world today, local laws identify the legal rights of employees—some of which are positive (and therefore generally require the provision of real resources), while others are negative (and require only that others not interfere with the pursuit of a person's exercise of his or her rights). For example, in countries that require certain employee benefits (i.e., health care, vacation, etc.), the positive legal right of employees to those benefits is accompanied by the responsibility of employers to provide those benefits. Similarly, in countries where employees have a legal right to form unions, this negative right imposes on employers the obligation not to interfere with the formation of employee unions. The right to form unions can also imply a positive right, in that it can impose on employers the duty to negotiate with their employees' unions.

A significant amount of the debate surrounding working conditions stems from conflicting views on employee and employer rights and responsibilities. Do people have a right to work? What working conditions are workers entitled to? If these entitlements exist, do they derive from natural law or civil law? For example, might workers have a natural right to a workplace free of physical beatings by employers but only a legal right to sanitary facilities?

Answers to these sorts of questions determine the kinds of working conditions to which employees should reasonably be entitled. Whereas most people would likely agree that natural rights and legal rights should be respected, there is considerable disagreement as to the extent of natural and legal entitlements, particularly across cultural boundaries. While there are some bright-line distinctions, there are many areas that remain ambiguous.

Most people, for example, tend to agree that violence leading to physical harm should not be permitted in the workplace. In contrast, it is unlikely that many people—if anyone—would contend that the provision of recreational facilities is a right that employees are entitled to. There are, however, many other issues that generate considerable controversy. Day care for infants is one of these issues. More and more in the United States, day care is becoming a necessity because couples are having to rely on income from both spouses. Having children can create an impediment to both spouses working and can create additional financial burdens on the family. Day care is therefore viewed by some people as a "right," because of its practical necessity for them to be able to work. Other people nevertheless maintain that, in the absence of a legal guarantee, it remains a matter to be determined through employer-employee negotiations.

Some people contend that employee rights are only those rights that emerge as part of specific employment arrangements or agreements. Others, however, suggest that employees should enjoy the same basic rights as persons in general, such as human dignity, moral autonomy, physical safety, reasonable privacy, and due process.

Human dignity refers to respecting people's personal autonomy and personal space and not making them do things they object to doing on moral grounds. Of course, there is a meaningful distinction between a person simply not wanting to do something distasteful versus a person who opposes a request. There is obviously a distinction between simple likes and dislikes and meaningful objections. In Kantian terms, respecting dignity translates into treating people as ends in and of themselves, not merely as means to ends.

Similarly, moral autonomy refers to respecting the rights of individuals to make their own choices as to appropriate courses of behavior. In the work environment, this covers a range of situations, such as the right not to follow directives that are morally questionable or even offensive. In addition, the right to blow the whistle on inappropriate practices by reporting alleged wrongdoing to external sources could also be considered linked to moral autonomy.

Physical safety is another significant concern. The view is that a person's life and/or health should not be placed in jeopardy because he or she chooses to work. When a person goes to work, he or she relies on his or her employer to maintain reasonable safety standards. It, therefore, becomes the responsibility of the employer to maintain safe working conditions so that employees are not put at personal risk in the workplace.

Not everyone agrees—there is an argument that all that is necessary is disclosure. It then becomes the employee's choice as to the level of risk he or she is willing to accept. While there is the view that there are some risks that no one should take (voluntarily or otherwise), that view is often considered overly paternalistic. There are jobs that are necessary—or, at the very least, important—but that involve some degree of risk. Mining, for example, is notorious for physical safety issues. Perhaps the answer lies not in eliminating risky jobs but in improving and emphasizing appropriate care with regard to how laborers in those sorts of jobs are treated and protected.

One perspective is that the requisite level of safety maintained by the employer is determined through the bargaining process. The problem is that not everyone agrees that the bargaining process is effective. Employers and employees are not necessarily in equal bargaining positions. Employers are often better situated to choose among qualified candidates than employees are able to choose among possible positions, particularly if employers end up offering similar sorts of positions. In fact, the hiring/job acceptance process very rarely resembles a bargain, except at the higher levels of management. Manual laborers rarely have the opportunity to engage in meaningful bargaining for jobs.

Privacy is a much more amorphous right, particularly in the United States, where there exists a distinction between public and private workplaces vis-à-vis the Constitution and the respective guaranteed rights. Although it tends to mean different things to different people in different audiences, a right to "reasonable" privacy can be thought of as a right to personal space and ideas and the right to control knowledge about basic personal information (i.e., health).

Finally, the right to due process is a right that emerges when other rights are violated. It is the right for a person to be notified of actions taken against him or her and the corollary right to have the opportunity to be heard in his or her defense.

These rights create the fabric that holds together reasonable expectations of fair working conditions, at least in many Western societies.

Nature of the Employment Relationship

The employment relationship varies by country and by state. In many countries in Europe, local laws favor employees and protect their interests. In France, for example, employees receive liberal leave time by law. Every employee is entitled to two and a half paid vacation days per month, which amounts to five full weeks of vacation per year. Statutory provisions require good causes for terminating employees. This is true in other countries as well, such as Canada, Germany, Great Britain, Italy, Japan, and Sweden. This is not true, however, everywhere. Other countries, such as Egypt and El Salvador, do not provide explicit protection for worker rights.

Employment at Will

The United States adheres to an approach to employment that is commonly known as employment at will (EAW). This means that, in the absence of an agreement to the contrary, the relationship is considered "at will" and either the employer or the employee can alter and/or terminate that relationship at any time, for any reason—except an illegal reason. Today, the majority of jurisdictions in the United States follow EAW, and the majority of American employees are therefore at-will employees. Although employers are required to adhere to specific federal and state legislations regulating basic working conditions, they are not obligated beyond those minimum standards.

As long as legal requirements are met, employers and employees are generally considered free to set their own terms. This stems in large part from the prevalence of EAW. EAW leaves the determination of most employment terms and working conditions to the discretion of employers and employees: It is expected that the parties address their specific concerns during the negotiation process of commencing the employment relationship. The relationship that results is, therefore, assumed to be with the agreement of both employers and employees. According to this view, apart from natural law and civil law guarantees, the only working conditions to which workers are entitled are those to which employers have previously agreed, and those conditions are expected to be enforced.

Although EAW is straightforward and clear, it continues to engender considerable controversy. One argument is that in the absence of explicit legal guarantees, the doctrine of EAW possibly translates into a license for employers to treat employees arbitrarily. Private employers in the United States, for example, are not required to explain the rationale for employment-related decisions (i.e., terminations) or to offer the employee the opportunity to respond to concerns. In other words, private employers are not required to provide due process. Public workplaces, in contrast, often recognize due process as an employee right.

This distinction illustrates one of the problems with EAW. Due process, a right considered fundamental according to the U.S. Constitution, can be disregarded by private employers. The reason for this is that the guarantees of the Constitution apply only to relationships between individuals and the government. Whereas public employees are considered to have a relationship with the government, private employees do not. Even though the nature of their employment is often comparable (i.e., teachers in public and private schools perform essentially the same roles), their protected rights differ in a meaningful way.

Opponents of EAW, therefore, assert that EAW should be abandoned because it allows these sorts of disparities to exist and enables employers to disregard rights that perhaps should be considered basic, even if not explicitly guaranteed by law. The view is that employers should behave responsibly even in the absence of explicit legislation. Their view is that there should be recognition of human dignity—that is, employees are human beings, not robots. Advocates of EAW, however, argue that if employers and/or employees are dissatisfied with EAW as the doctrine governing their employment relationship, it is their responsibility to bargain for some other sort of relationship.

It is important, however, to distinguish EAW as a doctrine from its implementation in specific instances. As advocates of EAW point out, it does not identify reasonable conditions or terms—it merely lays the groundwork for employers and employees to determine for themselves the appropriate terms of employment and working conditions. In many ways, EAW is ideal for it leaves the determination of working conditions to those actually performing the work. Many people, therefore, consider EAW not only morally unproblematic but, in fact, morally superior to alternatives. In contrast with those who argue that EAW violates human dignity, it can be argued that EAW actually promotes human dignity by providing for free contracting between the parties.

Right to Work

Another point of contention has to do with the "right to work." Although international instruments such as the Universal Declaration of Human Rights assert that a right to work exists, this is not reflected in the legal systems of most countries around the world. There is no mention of such a right, for example, in the U.S. Constitution. There are those who contend, however, that such a right is implied: If work is required for a person to sustain himself or herself and/or his or her family, then the right to work is simply inherently connected to the right to life.

There is significant controversy concerning the possible existence of a right to work. Many rights theorists assert that if there were a right to work, it would impose a duty on someone else (i.e., private and or/public employers) to hire, and natural rights are not generally positive rights. Other people, however, argue that such a right is inherently implied by other rights—such as the right to sustain life, particularly in societies as they exist today, where earning a living has become a precondition for having the means to obtain basic necessities (i.e., food, shelter, etc.).

In the global arena, this becomes somewhat complicated. Common labor rights tend to be considered fundamental according to Western moral thinking and are often explicit civil rights in Western societies. Although the Universal Declaration of Human Rights is intended to identify the minimum standards for people around the world, it is generally consistent with Western moral thinking, and this is one of the greatest criticisms of it. While it remains aspirational, it does not account for cultural differences.

Evolution of Working Conditions

Concern for working conditions dates back centuries. It heightened as a result of the Industrial Revolution, in particular, as the number of jobs increased drastically. As the United States and the rest of the countries were going through the Industrial Revolution, a number of work-related problems surfaced. The harsh working conditions and job insecurities of the time made the work environment dangerous places. That fact of the matter is that the United States and the rest of the industrially developing world were proceeding through uncharted waters.

It was not necessarily the case that employers set out to violate rights but that they did not implement the necessary processes and procedures to make sure that rights were protected. Their lack of experience as they moved into this new era of industrialization and opportunity created temptations that they did not adequately resist. Countries such as the United States responded with legislation aimed at addressing problems as they were identified. At the same time, wealth also increased as a result of the increased production spurred by the Industrial Revolution. An alternative view is that civil rights emerged naturally as result of this wealth and the enhanced knowledge that accompanied it.

The Industrial Revolution refers to the era during which significant changes took place with regard to technology, innovation, social structuring, and culture. The workforce increased, and this led to an overall increase in the population as increased wages led to larger families. Both the United States and England went through these sorts of eras at roughly the same time. During this era, conditions of employment, many of which had been prevalent previously, became more visible. Child labor, for example, denounced as both a legal and a moral wrong, existed prior to the Industrial Revolution. It was during this time, however, that it became particularly noticeable. Child labor in agricultural societies, such as those that existed in the United States and England prior to the Industrial Revolution, was often obscured because of the inherent seclusion of people within these societies.

This led to the passage of significant legislation aimed at protecting workers from unreasonable conditions. In England, a series of "factory acts," for example, specifically protected categories of rights. The Factory Act of 1819, for example, limited the number of hours a child could work to 12 hours per day. Similar acts passed during following years banned children from factories and limited the number of hours women could work. The Factory Act of 1874 limited the workweek to 56.6 hours. This era was characterized by the passage of numerous, similar laws by both England and the United States as they wrestled with the arduous task of trying to find the appropriate parameters for proper working conditions.

One of the consequences of the Industrial Revolution was that it caused people to pay attention to the nature and conditions of employment. In the wake of the Industrial Revolution, the value of collective bargaining was recognized. At first, complaints were issued in localized or limited settings, which did not give workers much of a chance against their factory bosses and organized leaders of the industrial world. With no voice or power with which to negotiate with/against their bosses, a number of labor unions came into existence.

Labor Practices

Generally speaking, concern about labor practices in the United States—and many Western democracies—tends to revolve around consideration for the conditions under which people work. Concern generally targets wage laborers and blue-collar workers—that is, manual laborers, factory workers, and so on, for it is these workers who tend to be most vulnerable to mistreatment and exploitation because they often do not have a voice.

Of primary concern is forced labor, which is considered both morally reprehensible and illegal today in most Western democracies. Forced labor occurs when people are compelled to work against their will. This can happen when people do not have the means to stand up for themselves.

In spite of strong prohibitions against it, forced labor remains a problem throughout the world today. Even in the United States today, large numbers of cheap laborers are smuggled in through human trafficking from countries such as China, Mexico, and Vietnam. Many of these people are required to put in long hours in poorly maintained facilities. While these laborers are not always physically "forced" to work, they effectively have no other choice. Because these people are not given any resources (financial or otherwise), they have no option but to live and work under these conditions—often considered "sweatshops" because of the presence of physical and mental abuse, the poor safety conditions, and the typically long hours worked. If the practices are illegal, the problem is not of rights but of enforcement. If legal practices truly violate rights, then the law and its enforcement should be brought into conformity with those rights.

Compensation is another major concern. It is not just the hours worked but the wages paid for those hours that is considered significant. The United States, in addition to other countries, has legislated a "minimum wage" to guarantee a base rate. In fact, in many industries, hourly wages are significantly higher. The concern then becomes the number of hours worked. While the goal is to limit the number of hours laborers are expected to work, one way of achieving this is by requiring significantly higher pay—that is, overtime pay, when more than a certain number of hours (i.e., often 40 hours) are worked in a week. Overtime pay is often at least double regular pay.

One way blue-collar workers have found to address their concerns is through the formation of labor or trade unions. In this way, they are able to exercise more power as a group than they could separately as individuals. An important condition of work is therefore the right to engage in this sort of collective bargaining.

Labor Unions

Although many people recognize the value of collective bargaining, labor unions have proved controversial. Labor unions are organizations formed to represent the interests of workers. Different groups of workers come together to help voice their opinions/concerns in their immediate workplace arenas. The anticipated result of this is to leverage the power of an organized employee base to enact changes in working conditions, wage payments, work benefits, and so on.

While a number of benefits can be attributed to the unionization of workers throughout the United States, labor unions have suffered a controversial past. The majority of the controversy lies in the manner in which the early unions went about achieving their goals. Some of the first unions were disorderly and ostensibly corrupt. They engaged in violent activities to motivate specific companies and industries to change conditions. As part of this, they often attempted to physically prevent other laborers from working when the union workers went on strike, so as not to undermine their efforts. Instead of serving as an organization that could leverage its participants' voices to increase transparency and communication between employers and employees, these unions actually stood as an impediment to successful employer-employee relationships. Business leaders and government officials grew wary of the potential power of these organizations and sought to dismantle them. This merely increased antagonism between employers and employees.

The negative view of unions was further intensified by the opening of the global market and the increased economic competitiveness induced by the availability of cheap, capable human labor from alternative sources (i.e., developing and emerging countries). Companies in the United States are now compelled to compete in a global workplace with employers who can hire whoever they please from locations anywhere in the world without having to deal with unions. Workers who participate in unions generally receive higher wages and get a larger number of benefits. In addition, companies who hire unionized workers risk potential strikes and sudden loss of productivity. Both these conditions place the American corporations at a disadvantage as compared with other businesses around the globe.

Legislation

Around the world, many countries have responded to concerns about employee and employer rights and responsibilities through legislation. The United States, for example, has dealt with worker safety by passing the Occupational Safety and Health Act on December 29, 1970. It directly addresses the safety, health, and welfare of employees. The United States also has minimum wage laws. Other countries around the world have passed similar laws, along with many others.

While such legislation is often useful in delineating rights and responsibilities, significant concerns remain that excessive legislation can also interfere with effective bargaining opportunities. One of the primary arguments in favor of EAW in the United States is that employment is contractual, and it is important that parties be allowed to strike whatever bargain works for them. If employers and employees are not interested in negotiating specific terms, EAW provides the default terms. To overlegislate limits the ability of employers and employees to create the arrangements of their choosing.

At the same time, however, there is also the view that the bargaining positions are not equal, and employees remain vulnerable to potential abuses by employers and other employees in the absence of restrictions against such things as excessive workweeks, discrimination, and so on. For this reason, societies continue to rely on legislation to set minimum employment standards.

Conclusion

Working conditions today in the United States and other Western democracies have improved tremendously. In the 1960s and 1970s, nearly a third of all workers belonged to labor unions. More recently, there has been a sharp decline in unionization, in that only about 10% of the American workforce belongs to a union. Concern remains, however, particularly as a result of the increasing amount of time we spend in workplaces and because of the increasing industrialization and globalization of the world. As multinational corporations extend industrialization throughout developing and emerging countries, new concerns have arisen regarding those populations not yet protected by norms and legislation governing worker's rights and workplace standards. The difficult task of defining and ensuring worker's rights worldwide still remains.

—Tara J. Radin and Nadan Sehic

See also Benefits, Employee; Child Labor; Civil Rights; Diversity in the Workplace; Employee Monitoring and Surveillance; Employee Protection and Workplace Safety Legislation; Employee Relations; Employee Rights Movement; Employment Contracts; Employment Discrimination; Empowerment; Equal Employment Opportunity; Equal Opportunity; Equal Pay Act of 1963; Free Speech in the Workplace; Genetic Information in the Workplace; Hostile Work Environment; Human Rights; Industrial Revolution; Job Security; Just Wage; Labor Unions; Living Wage; Maquiladoras; Meaningful Work; Minimum Wage; National Labor Relations Board; Occupational Safety and Health Administration (OSHA); Reverse Discrimination; Revolving Door; Right to Work; Sweatshops; Violence in the Workplace; Whistle-Blowing; Workplace Privacy

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Work-Life Balance

The essential issue of work-life balance is the inability of many workers to achieve parity with regard to their responsibilities to a job and/or a profession, and their obligations and commitments to their private, family, nonwork lives. Work-life balance is not a new problem. It has long been a part of everyone's work-life experience. But in the latter part of the 20th century, the accelerated pace, stress, and complexity of our jobs and our careers has placed this phenomenon at the center of every conversation about our collective work lives. Work-life balance is not a gender or family rights issue. It is a problem that touches every member of the workforce and is closely related to two fundamental questions: (1) Do we live to work or work to live? (2) Do workers' rights include the right to not always have to be working?

At the end of the 19th century, the major goal of the American labor movement was simple and distinct: 8 hours for work, 8 hours for rest, and 8 hours for what we will. For brief periods in the 20th century, for some workers in specific industries, this goal was achieved. But the 40-hour standard week is either a memory or a still-sought-after dream for most Americans. Depending on whose statistics you want to accept, as a nation we are working more now than ever.

In 1989, *Newsweek* reported that 85% of the American workforce put in more than 45 hours a week on the job. Economist Juliet Schor estimates that annual hours on the job, across all industries and occupations, have been increasing over the past 20 years, so the average employee is now on the job an additional 163 hours, or the equivalent of an extra month per year. In her 1991 best seller *The Overworked American*, she claimed that one fourth of all full-time workers spent 49 or more hours on the job each week. Of these, almost half were at work 60 hours or more. In 1997, in her important analysis on work and the family, *The Time Bind*, Arlie Russell Hochschild reported that both men and women workers average slightly more than 47 hours per week. Finally, in a 1999 study, a Cornell University research project found that on average, Americans work 350 hours more per year than Europeans—and 70 hours more a year than even the Japanese, whose language contains the word *karoshi* that means "death from overwork." If some of these figures and projections are accurate, by the year 2010, the average workweek could exceed 58 hours.

What has to be kept in mind is that these figures only reflect hours on the job and do not represent the other aspects of our workday such as getting to and from the job as well as household and family responsibilities. A 1999 survey conducted by the Families and Work Institute of New York concluded that both spouses, in a double-income household with kids, put in a minimum of 15 hours per day on work, commuting, chores, and children. These figures, based on a Monday through Friday schedule, mean that both spouses have already "logged-in" 75 hours before the weekend. Moreover, although Sundays in many households are still reserved for family outings and social events, Saturday is usually just another workday. "Honey-do-lists" are drawn-up, chores are assigned, projects attended to, and kids are schlepped to music lessons and the mall. According to a 2001 *Harvard Health Letter*, nonworking, no-chores, leisure time has eroded to 16.5 hours per week per person.

Whatever the exact amount of time each of us is putting into the job, it is both palpably and statistically clear to most of us that we are working harder and longer than ever before. And more than just the extra time we are putting in on the job, the tempo, intensity, and stresses associated with our work seems to be accelerating. We cram more and more into each day, and yet we feel that we never have enough time to do all that must be done.

Besides all this, two other factors in the work-life balance equation need to be taken into account: vacations and fatigue. A recent report from the United Nations points out that U.S. workers average 49.5 weeks of work each year. Joe Robinson, former editor of *Escape* magazine, claims that we're the most vacation-starved country in the industrial world! In this society, says Robinson, we perversely allow downtime for machinery for maintenance and repair, but we don't allow it for the employees. There is only one other country with fewer vacations days than America (10 to 13) and that is Mexico (6). And what is worse, says Robinson, is that in America these vacation days are not required by law, but rather are the result of negotiated contracts or custom and tradition. In comparison to the mandated vacation schedules of other industrialized nations, American workers are suffering from a serious leisure lag: Italy, 42 days; Germany, 35 days; Sweden, 32 days; Denmark, 30 days; Ireland, 28 days; and even the work-addicted Japanese get 25 mandated vacations days a year.

In a 1995 cover story, *Newsweek* reported that 25% of us say we're fried by our work, frazzled by the lack of time, and just plain exhausted. Symptoms of exhaustion and fatigue are now among the top five reasons why people consult their doctors. According to a survey conducted in 2001 by the National Sleep Foundation, our workaholic lifestyle is turning America into a "nodding off nation," with 40% of those surveyed reporting difficulties staying awake during the day and on the job. The poll reported that although people need between 7 and 10 hours of sleep each night, 62% of those surveyed sleep less than 8 hours per night. Sleep researchers are now in general agreement that chronic lack of sleep may be as bad for a person's health as smoking, a poor diet, and a lack of exercise. We need sleep to rest and build out brains, to heal, to clear our cobwebs, to slow aging and dementia, and to help avoid obesity, diabetes, and hypertension. We need sleep to be fully present in our own lives.

Like it or not, too many of us, out of desire or necessity, choice or chance, put too much time in on the job. We have made a fetish out of work. It's now part of our character and culture. We have become addicted to the *promise* of work. Work *promises* we will get ahead. Work *promises* power, money, and influence. Work *promises* we will be accepted, respected, and successful. And so, we work. We work because we need to, because we need money. We work out of habit and desire. We work to occupy time. We work to establish our place in the pecking order, to guarantee status and prestige. And, too often, we work because we simply don't know what else to do with ourselves, because we think we must and should. It has simply become standard to respond to the conventional salutation of "Hello, how are you?" with some version of the refrain "*I am so busy!*"

According to the Families and Work Institute 1999 study, 63% of Americans say they want to work less, up from 17% in 1994. In another 1999 study conducted by NYU and the University of Pennsylvania, it was found that 45% to 50% of workers (80% of those working more than 50 hours per week) said they would prefer to work fewer hours, and more than 25% said they would take a pay cut to make it happen. Another survey in 2000 found that even college students and recent grads place "flexible hours" at the top of the list of the job benefits they most desire—above health insurance, vacations, and stock options.

And yet the problem remains unchanged. Too many of us work more and more in the manic pursuit to maintain our lives and our lifestyles. As a society, we are suffering from the frenzy, frustration, and fatigue. To turn around the words of Thorstein Veblen, "We have become a harried working class rather than a leisure class."

—Al Gini

See also Protestant Work Ethic; Right to Work; Social Costs; Stress, Job; Violence in the Workplace

Further Readings

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Workplace Privacy

Privacy can be viewed as an entitlement, and therefore as a fundamental right, or as one interest to be balanced against others. Privacy in the workplace concerns the balance between the right of the employee to personal space and the management of his or her personal information with the right of the employer to manage that workplace and to make effective decisions. Some means of gathering information about employees may focus on inappropriate information, or the employer may use methods that are unreasonable or intrusive. Yet the employer also legitimately seeks to know as much about the employee as possible and the employee seeks to prevent unreasonable intrusions. Technology has muddied the issues involved because it allows for access to information using methods never before considered.

This discussion will first highlight the reasons why an employer may opt to collect information or otherwise monitor the workplace, as well as the concerns of employees based on this monitoring, and the resulting impact of the information-gathering processes. We will explore the nature of monitoring, the various means by which the employer is able to and does monitor the workplace (including the regulation of off-work acts as well as drug testing), and present the legal and ethical constraints in doing so.

Why Do Firms Seek Personal Information or Monitor Their Workplaces?

There are numerous bases that support the choice of a firm to monitor. One justification for an employer's choice to monitor stems from the law itself that, more and more, holds an employer liable for the acts of its employees. With this in mind, employers seek greater and greater amounts of information about possible and current employees to protect themselves from the tort of negligent hiring or vicarious liability. On the other hand, investigating areas that bear little, if any, relevance to the individual's ability to perform a job exposes the employer to liability for privacy invasions, as will be discussed below. Employers must determine whether it is appropriate to investigate an employee's driving record for a position as an accountant or to conduct a credit check for an individual who works as a delivery person. Employers also point to the proliferation of employee theft that may be uncovered through some form of surveillance or monitoring. The U.S. Department of Commerce found in 1990 that businesses lose approximately $40 billion each year to employee theft and that 75% of this theft is usually undiscovered. In addition, monitoring may uncover and thus prevent increasing employee industrial espionage.

The reasons for monitoring can, therefore, be categorized into two categories: managing the workplace and protecting against or preparing for issues involving legal liability. An employer's interest in managing the workplace may require it to ensure compliance with affirmative action by investigating the backgrounds, ethnicities, races, or other traits of its workers. In addition, to appropriately administer workplace benefits, the employer would contend that it must gather information related to employee needs. Information may also assist the employer to place workers in appropriate positions and to ensure effective, productive performance that is not lost to excessive use of technology such as the Internet. Reports evidence a rise in personal use of technology, with 86% of employees admitting sending or receiving personal e-mails at work, with 55.1% admitting to having received politically incorrect or offensive e-mails at work, and 62% of firms finding employees accessing sex sites during the workday. Though seemingly extreme, 10% of employees spend more than half the workday on e-mail or surfing nonbusiness sites.

An employer's interest in self-protection against legal liability also serves as justification for monitoring or other information-gathering techniques. More than 20% of firms have been ordered to produce employee e-mail in the midst of a legal claim as of 2004. Information regarding the following as well as other areas of compliance are well served by appropriate information collection and maintenance: hostile environment, sexual harassment, software licensing laws, proprietary information or trade secrets, competitive intelligence, financial fraud, theft, defamation/libel, and discrimination.

In the American Management Association's 2001 survey, more than two thirds reported that they engaged in monitoring as a result of their concerns for legal liability. Given the courts' focus in many cases on employer response to claims of sexual harassment or unethical behavior, among other complaints, firms believe that they need a way to uncover these inappropriate activities. More than 10% of firms have reported receiving a subpoena for employee e-mail and one third of the largest firms report firing employees for inappropriate e-mail. Without monitoring, how would they know what occurs? Moreover, as courts maintain the standard in many cases of whether the employer "knew or should have known" of wrongdoing, the state-of-the-art definition of "should have known" becomes all the more vital. If most firms use monitoring technology to uncover this wrongdoing, the definition of "should have known" will begin to include an expectation of monitoring.

Many forms of monitoring are simply made easier or more effective through technology. While in the past, employees may have been asked to insert a card into a time stamp machine to ensure for both the employee and the employer that the worker is being paid for the time they were at the workplace, they may now be asked to place their hand on a scanner to effect the same information transfer. Without more, this type of monitoring represents merely a development without necessarily greater intrusion.

Why Are Employees Concerned?

Notwithstanding these persuasive justifications for monitoring in the workplace, there also remain several reasons to limit monitoring. First, monitoring may create a suspicious and hostile workplace where work morale is affected negatively. In addition, monitoring or certain forms of information gathering may cause increased workplace stress and pressure, negatively affecting performance and having the potential to cause physical disorders such as carpal tunnel syndrome. In addition, monitoring can be perceived as constraining the right to autonomy and freedom of expression. One study found that monitored workers suffered more depression, extreme anxiety, severe fatigue or exhaustion, strain injuries, and neck problems than unmonitored workers. Finally, given the pressure on workers to be at the workplace for increased hours, it may be important to conduct some personal business at the office, when necessary.

The Impact of Monitoring

With the advent of new technology, new ethical issues emerge. That is because we consider the advances of the technology before we consider the implications. Notwithstanding issues in connection with production, marketing, finance, and other areas of a firm's operations, we now have countless issues relating to ethics with which we were never before confronted. For instance, the law has not necessarily caught up with emerging challenges such as the implications of new technology with regard to distinguishing between work use and personal use of technology, managing flextime, protecting against medical concerns for telecommuters, monitoring the use of the Web to spread information and misinformation, and managing fair use or disclosure.

Technology, however, does not present us with new value judgments but instead simply new ways to gather the information on which to base them. Sorting through these issues is challenging, nevertheless. Consider the impact of September 11, 2001, on an employer's decision to share personal employee information with law enforcement. Private firms may be more willing today to share private information than they would have been previously. Similarly, the International Labour Organization (ILO) found that a significant implication of technology is the dissolution of boundaries between leisure and work time, and the place of work and place of residence. The ILO's World Employment Report for 2001 expressed grave concerns about the resulting deterioration of the foundations of our edifice of agreements, norms, rules, laws, organizational forms, structures, and institutions, all of which have a stronger influence on our behavioral patterns and systems of values that we are aware.

Firms also experience unanticipated challenges, for which they often find themselves ill prepared. Consider one firm's lesson that problems with e-mail use and abuse might also extend beyond the end of the employment relationship. After an employee was fired by Intel Corporation, he began to air grievances about the company via e-mail. He repeatedly flooded his former employer's e-mail system with mass e-mails that its security department was unable to block. Intel sought and obtained an injunction on the theory of trespass to chattels. A California appellate court rejected the former employee's appeal that the injunction violated free speech principles.

Do we need "new ethics" for this "new economy"? Perhaps not, since the same values one held under previous circumstances should, if they are true and justified, pervade and relate to later circumstances. However, the perspective one brings to each experience is affected through the understanding and use of new technology and other advances. However, as economist Antonio Argandoña cautions, there has been a change in values that may be caused by the opportunities created by the technology. On the other hand, he points to the possibility of new technology also bringing good, development of depressed regions, increased citizenship participation, defense of human rights, and other potential gains. The industries and organizations that have spurred on this revolution are perhaps the ones most empowered to determine its direction.

Stakeholder perception is often based on the transmission of information—communication is key. If new technology is dependent on and has as its substance information and data, economist Antonio Argandoña contends that there are significant moral requirements then imposed on that information and suggests the following as necessary elements:

- *Truthfulness and accuracy:* The person providing the information must ensure that it is truthful and accurate, at least to a reasonable degree.
- *Respect for privacy:* The person receiving or accumulating information must take into account the ethical limits of individuals' (and organizations') privacy. This would include issues relating to company secrets, espionage, and intelligence gathering.
- *Respect for property and safety rights:* Areas of potential vulnerability, including network security, sabotage, theft of information, impersonation, are enhanced and must therefore be protected.
- *Accountability:* Technology allows for greater anonymity and distance, requiring a concurrent increased exigency for personal responsibility and accountability.

Firms have responded differently to this call for responsibility in the development, manufacture, marketing, and service related to new production or other corporate activities. *Reason* magazine included a customized cover on its June, 2004, issue of a satellite picture of each recipient's neighborhood with the individual's home circled. While a magazine will have its recipients' home addresses, this magazine chose to use the image to illustrate its cover article on the power and importance of databases, one type of a "we know where you live" mentality. The article focused on the balance between the possible invasions of privacy afforded by information database management and the realistic benefits the technology could bring, such as instant credit, customized advertisements, and personalized mortgage offers. Nick Gillespie, *Reason*'s editor in chief, explains that the article challenges readers to consider how they would feel if they received a magazine that only had stories and ads that pertained to themselves, quite a marketing opportunity. The ethical question is what we are willing to give up of our personal information, privacy, and autonomy in order to get those possible benefits.

How Do Firms Monitor or Otherwise Collect Information?

The American Management Association has conducted surveys of mid- to large-sized U.S. firms that evidence an increasing trend with regard to e-mail monitoring. While its 2003 survey reported that 52% of firms monitored e-mail communications, up from 47% in 2001, its 2004 survey reported that 60% engaged in monitoring. The 2004 survey also found that 10% of these firms also monitored instant messages of its employees. Much of this monitoring is on an occasional basis rather than by regular routine. The most prevalent subject of monitoring is Internet connections (74%) followed by e-mail monitoring (43%) and videotaping (18%). Of firms that monitor, 84% notify their workers that they do so. More interesting is the fact that 16% do not notify their workers of the monitoring. In actual numbers, estimates regarding the number of workers subject to surveillance are difficult to measure. One estimate contends that the e-mail and/or Internet use of 14 million U.S. workers is under constant surveillance each day, increasing to 27 million around the globe.

One's understanding of the technology or other collection processes is critical to the protection of rights. When we mistakenly believe that no one is watching, we may engage in activities that we would otherwise refrain from doing. For instance, one may believe that hitting the "delete" key does actually delete an e-mail message. However, it does not always delete that message from the server so it might have a negative impact in a lawsuit or be able to be retrieved by that person's supervisor.

Almost 80% of mid- to large-sized firms in the United States have Internet access policies, but there remains a problem. More than 60% of these companies have disciplined employees for violations of these policies (with 25% reporting that they have terminated an employee for a violation). The leading violations include access to pornography, online chat forums, gaming, investing, or shopping at work.

To address some of the issues that are presented by computers, specifically, the Computer Ethics Institute has created "The Ten Commandments of Computer Ethics." The Commandments include the following: not snooping around in other people's computer files, thinking about the social consequences of the program one is writing or the system one is designing, and always using a computer in ways that ensure consideration and respect for fellow humans.

Unfortunately, many of the ethical issues that arise in the area of managing information are not readily visible. When one does completely understand the technology, one might not understand the ethical implications of decisions. While most users may believe that others cannot read their e-mail, experts say that any system is penetrable. Employers have been known to randomly read e-mails to ensure that the system is being used for business purposes. These issues may be compounded by the fact that there exists a knowledge gap between people who do understand the technology and others who are unable to protect themselves precisely because they do not understand. One might not expect to be fired for sending out an e-mail; but if one thought about it a bit, that person might have known what to expect.

Notwithstanding the fact that many individuals actually believe they are safe from such intrusions or express no concern about the sharing of their personal information, reports of intrusion horror stories abound. James Russell Wiggins's employer conducted a background check and fired him because the report showed a prior conviction for cocaine possession. Wiggins explained that the information was patently false, but the company would hear of no reinstatement. Later it was discovered that his identity had been confused with that of James Ray Wiggins; a lawsuit ensued. Indeed, according to a congressional report, half of all credit reports and background checks contain mistakes. The American worker is becoming more aware of the possibility for intrusions or violations, as well. A survey conducted by Louis Harris & Associates and Dr. Alan Westin showed that 89% of the American public is concerned about threats to their personal privacy, with 55.5% saying that they are "very concerned."

Technology has also allowed monitoring of personnel in manners never before contemplated. In one of the first legal analyses of privacy, legal scholars Louis Brandeis and Samuel Warren warned in 1890 of numerous mechanical devices that then threatened to bring what was said in the closets to be shouted from rooftops. Consider the plight of airline reservation clerks who have telephonic headsets that monitor the length and content of all telephone calls, as well as the duration of his or her bathroom and lunch breaks. In one instance, telephone calls received by airline reservation agents were electronically monitored on a second-by-second basis; agents were allowed only 11 seconds between each call and 12 minutes of break time each day. Other airline reservationists have complained that they are evaluated regarding how many times they use a customer's name during a call or how often they try to overcome a customer's initial objections to buying a ticket. The stress is increased, as those who were monitored report, because they believe that, if one listens long enough to any customer service provider, there is likely to be a human error at some point.

Under previous circumstances, one could usually tell if someone had steamed open a letter over a teapot. However, today, one usually cannot discover if someone reads the e-mail that person sent yesterday to a friend. Access can take place unintentionally, as well. In doing a routine background check, a supervisor may unintentionally uncover information of an extremely personal nature that may bear absolutely no relevance to one's work performance. This occurs because the information, though previously unavailable or too burdensome to uncover, is now freely available from a variety of sources.

Moreover, because technology allows us to work from almost anywhere on this planet, workers are seldom out of the boundaries of their workplaces. For instance, just because an employee may opt to go to a friend's wedding, a supervisor will still be able to reach that person. The question that remains, however, is whether it is acceptable for the supervisor to try to reach the employee, just because he or she has the ability. Continuous accessibility blurs the lines between our personal and professional lives. Total accessibility creates expectations, and therefore conflicts, with which workers and employers never before had to wrestle.

Another challenge posed by the new technology accessible in the workplace is the facelessness that results from its use. If one has to face someone as he or she makes a decision, that person is more likely to care about the impact of the decision on the person involved. Conversely, when one does not get to know someone because he or she does not have to see that person in order to do business, the decision maker often does not take into account the impact of decisions on that person. They become merely a name at the other end of an e-mail correspondence rather than another human being. Given the ease and informality of electronic communications, we often "say" (write, e-mail, etc.) things to each other that we would never say to someone's face, precisely because we do not have to consider the impact of what we are saying. We are more careless with our communications because they are easier to conduct—just hit a button and it is sent.

Electronic Performance Monitoring

As introduced above, technology invades and affects the employment relationship through employee electronic performance monitoring. Considerable controversy surrounds the issue of whether it is ethical and/or legal for an employer to monitor the actions of employees through electronic surveillance. This type of monitoring may take the form of recording telephone calls of customer service representatives, electronically counting the number of keystrokes a word processor makes during the day, installing video cameras in the workplace, and so on. While the employer may argue that it has the right to monitor in order to adequately and accurately appraise its employees and maintain quality levels, employees contend that the monitoring causes undue stress, pressure, and is too invasive.

Although installing video cameras in the washrooms of the workplace may be considered extreme, the line has not yet been drawn in the more gray areas of monitoring. The questions of what extent is too great or what constitutes humane or inhumane use of this technology remain unanswered by both the courts and the ethicists. Instead, it is critical for the employer to consider how to craft a more ethical or humane practice. Due notice given to employees that they will be monitored plus the opportunity to avoid monitoring in certain situations would solve some of the ethical problems. For instance, if an employer chooses to monitor random phone calls made by its customer service representatives, it could notify the workers that certain calls may be monitored and these calls would be signified by a "beep" on the line during the monitoring. In addition, if a worker is making a personal call, they may use a "nonmonitored" phone to avoid a wrongful invasion of his or her privacy.

However, this may not solve all the concerns about monitoring. Suppose the employer seeks to ensure that its service representatives handle calls in a patient, tolerant, and affable manner. By telling the worker which calls will be monitored, the employees may be sure to be on their "best behavior" during those calls. Random, anonymous monitoring may better resolve the employer's concerns (but not those of the worker). One study found that electronic performance monitoring has significant undesirable impacts on monitored workers, such as a lower perception of the fairness of the evaluation, health problems, and increased stress, all results that could also negatively affect productivity and thus the employer's interests.

Legal Status of Employee Monitoring

Protections in this arena fall under the general heading of privacy protections and, as such, are governed by the U.S. Constitution and federal statutes, state constitutions or legislation where available, and the common law through precedent. The Constitution protects against unreasonable searches and seizures but is limited in its application to public sector workplaces. Federal statutes represent spotty protections based on tremendously specific and particular circumstances. State protections exist to a small extent, such as the California Constitution's inclusion and recognition of a right to privacy. The area of the law with the most significant impact on privacy rights in the workplace is therefore court holdings, common law through precedent.

The prohibition of intrusion into seclusion, developed on a state-by-state basis but generally considered as universally applied, would hold an employer liable when it is found to have intentionally intruded in the private affairs of an employee if that intrusion would be highly offensive to a reasonable employee. Accordingly, the gray area exists in the determination of whether an act would be highly offensive to a reasonable employee.

In the case of monitoring telephone calls, monitoring is permitted in connection with quality control. Notice to the parties to the call is often required by state law, although federal law allows employers to monitor work calls without notice. If the employer realizes that the call is personal, monitoring must cease immediately.

With regard to monitoring e-mail messages, the courts were originally divided. However, there is now general consensus that under most circumstances, employers may monitor employee e-mails. Even in situations where the employer claims that it will not, its right to monitor has been held to persist. However, where the employee's reasonable expectation of privacy is increased (such as a password-protected account), this may affect the court's decision. Although not yet completely settled, the monitoring of voice mail messages appears to be subject to a similar analysis as e-mail messages. Finally, in connection with the monitoring of an employee's use of the Internet, where the employer has provided the equipment and/or the access to the Internet, courts have confirmed that the employer may track, block, or review Internet use.

Regulation of Off-Work Acts

The regulation of off-work acts is a challenging legal arena since, in the at-will environment, employers can generally impose whatever rules they wish. However, they may then run afoul of a variety of statutes, common-law privacy protections, and even legislation protecting against discrimination on the basis of various off-work acts. For instance, New York's lifestyle discrimination statute prohibits employment decisions or actions based on four categories of off-duty activity: legal recreational activities, consumption of legal products, political activities, and membership in a union.

Across the nation, there are other less broad protections of off-work acts. A number of states have enacted protections specifically on the basis of consumption or use of legal products off the job. These statutes originated from the narrower protection for workers who smoked off-duty. Currently, abstention from smoking cannot be a condition of employment in at least 29 states and the District of Columbia (and these states provide antiretaliation provisions for employers who violate the prohibition). In fact, instead of simply identifying the right to use lawful products outside of work, Rhode Island goes further by specifically prohibiting an employer from banning the use of tobacco products while not at work.

On the other hand, employers are not prohibited from making employment decisions on the basis of weight, as long as they are not in violation of the American with Disabilities Act (ADA) when they do so. The issue depends on whether the employee's weight is evidence of or due to a disability. If so, the employer will need to explore whether the worker is otherwise qualified for the position, with or without reasonable accommodation, if necessary. If the individual cannot perform the essential functions of the position, the employer is not subject to liability for reaching an adverse employment decision. However, employers should be cautious in this regard since the ADA also protects workers who do not have disabilities but who are perceived as having disabilities, a category into which someone might fall based on their weight.

Laws that protect against discrimination based on marital status exist in just under half of the states. However, although a worker might be protected based on marital status, they are not necessarily protected against adverse action based on the identity of the person they married. For instance, some companies might have an antinepotism policy, where an employer refuses to hire or terminates a worker based on the spouse working at the same firm, or a conflict-of-interest policy, where the employer refuses to hire or terminates a worker whose spouse works at a competing firm.

Since about one third of workers have dated an office colleague, policies and attitudes on workplace dating are especially impactful. Although only about 12% of workplaces have policies prohibiting workplace dating, a New York decision reaffirms the employer's right to terminate a worker on the basis of romantic involvement. In *McCavitt v. Swiss Reinsurance America Corp.*, the court held that an employee's dating relationship with a fellow officer of the corporation was not a recreational activity, within meaning of a New York statute that prohibited employment discrimination for engaging in such recreational activities. The employee contended that although the personal relationship between the two involved had no repercussions whatever for the professional responsibilities or accomplishments of either and the employer had no written antifraternization or antinepotism policy, he was passed over for promotion and then discharged from employment largely because of his dating. The court agreed with the employer and found that dating was not a recreational activity.

The majority of states protect against discrimination on the basis of political involvement, although states vary on the type and extent of protection. Finally, lifestyle discrimination may be unlawful if the imposition of the rule treats one protected group differently than another. For instance, as discussed elsewhere, if an employer imposes a rule restricting the use of peyote in Native American rituals that take place during off-work hours, the rule may be suspect and may subject the employer to liability. Similarly, the rule may be unlawful if it has a disparate impact on a protected group.

Most statutes or common-law decisions, however, provide for employer defenses for those rules that

(a) are reasonably and rationally related to the employment activities of a particular employee, (b) constitute a bona fide occupational requirement, or (c) are necessary to avoid a conflict of interest or the appearance of a conflict of interest.

Drug Testing

With regard to drug or other substance testing, the employer has a strong argument in favor of testing based on the law. Since the employer is often responsible for legal violations of its employees committed in the course of their job, the employer's interest in retaining control over every aspect of the work environment increases. On the other hand, employees may argue that their drug usage is only relevant if it affects their job performance. Until it does, the employer should have no basis for testing.

Consider the possibilities of incorrect presumptions in connection with drug testing. For instance, in his book *Drug Abuse in the Workplace: An Employer's Guide for Prevention*, Mark de Bernardo suggests that crudely wrapped cigarettes, razor blades or eye droppers, frequent trips to the bathroom, or dressing inappropriately for the season may be warning signs of drug use. On the other hand, it does not take a great deal of imagination to come up with other, more innocuous alternative possibilities. Yet an employer may decide to test based on these "signs."

In a study examining the attitudes of college students to drug-testing programs, researchers found that virtually all aspects of drug-testing programs are strongly accepted by some individuals and strongly rejected by others. The only variable that the researchers found indicative of a student's attitude was whether the student had ever used drugs in the past. Where a student had never used drugs, he or she was more likely to find drug-testing programs acceptable. The following factors contribute to greater acceptance and approval by workers:

- Programs that use a task force made up of employees and their supervisors
- A completely random program
- Effective communication of procedures
- Programs that offer treatment other than termination for first-time offenders
- Programs with no distinction between supervisory and other workers

In *Skinner v. Railway Labor Executives' Association*, the court addressed the question of whether certain forms of drug and alcohol testing violate Fourth Amendment protections against unreasonable searches and seizures. In *Skinner*, the defendant justified testing railway workers based on safety concerns—to prevent accidents and casualties in railroad operations that result from the use of alcohol or drugs. The court held that the government's interest in regulating the conduct of railroad employees to ensure safety presents special needs beyond normal law enforcement that may justify departures from the usual legal requirements.

It was clear to the court that the governmental interest in ensuring the safety of the traveling public and of the employees themselves plainly justifies prohibiting covered employees from using alcohol or drugs on duty or while they are subject to being called for duty. The issue then for the court was whether the means by which the defendant monitored compliance with this prohibition justified the privacy intrusion absent a warrant or individualized suspicion. In reviewing the justification, the court focused on the fact that permission to dispense with warrants is strongest where the burden of obtaining the warrant is likely to frustrate the governmental purpose behind the search and recognized that alcohol and other drugs are eliminated from the bloodstream at a constant rate and blood and breath samples taken to measure whether these substances were in the bloodstream when a triggering event occurred must be obtained as soon as possible. In addition, the court noted that the railway workers' expectations of privacy in this industry are diminished given its high scrutiny through regulation to ensure safety. The court therefore concluded that the railway's compelling interests outweigh privacy concerns since the proposed testing was not an undue infringement on the justifiable expectations of privacy of covered employees.

In positions in which public safety is not at risk, the courts have generally agreed with the employers that they are justified in testing all employees and job applicants. Several major retail employers, including Home Depot, Ikea, and Wal-Mart, have comprehensive drug-testing policies for both job applicants and employees. Many stores will also promote their "drug-free" workplace policy as a marketing strategy. With just a few exceptions, such policies are legal throughout the United States.

Other Forms of Monitoring

Employers are limited in their collection of information through other various forms of testing, such as polygraphs or medical tests. Employers are constrained by a business necessity and relatedness standard or, in the case of polygraphs, by a requirement of reasonable suspicion. With regard to medical information specifically, employers' decisions are not only governed by the ADA but also restricted by the Health Insurance Portability and Accountability Act (HIPAA). HIPAA stipulates that employers cannot use protected health information in making employment decisions without prior consent. Protected health information includes all medical records or other individually identifiable health information.

Is a Balance of Interests Possible?

A balance is possible between the employer's interest in managing the workplace and the employees' privacy interest. The employer has a right to manage the workplace. In more specificity, employers want to manage the workplace so that they can place workers in the appropriate positions. They want to ensure compliance with affirmative action, administer workplace benefits. They want to ensure effective or productive performance. They need to know what their workers are doing in their workplace. The employer's perspective is as follows: "I am paying them to be there working. If they are not working, I should know that and either pay them less or hire different workers." It is a relatively understandable concern.

Employees, on the other hand, want to be treated as free, equal, capable, and rational individuals who have the ability to make their own decisions about the way their lives will unfold. They are interested in their own personal development and valued performance (the lack of privacy may prevent "flow"), conducting some personal business at the office, being free from monitoring for performance reasons (wary of increased stress or pressure from monitoring), being free from monitoring for privacy reasons, and being able to review and to correct misinformation in data collected. While workers need to be able to conduct involuntary personal matters at the office (such as scheduling a doctor's appointment), workers contend that they also have the right to conduct voluntary personal business as well (such as e-mailing friends). Perhaps the resolution lies in the precise definition of voluntary or involuntary personal matters.

It is indisputable that the Internet has certainly promoted First Amendment values of free speech and association; yet the accessibility of personal information over the Internet has also allowed employers to find employees' personal information in areas that were previously not so easily invaded. Only a few areas remain off-limits, including education records, military service records, and some medical information. In addition, technology allows individuals to engage in activities that at one time were uncomfortable or inappropriate; using new technological advances, these individuals are not allowed to remain faceless. As a result, a worker who might never have explored certain areas during working hours might feel completely comfortable exploring those same areas using the Internet with no obvious form of recognition.

There are ethical, economic, and efficiency bases for monitoring. A supervisor may have completely justifiable reasons for considering this type of monitoring or for evaluating an employee based on the information collected. In addition, the more complicated a task, the more necessary effective workplace supervision becomes. On the other hand, workers feel a lack of respect from their employers, which may in turn affect productivity or the culture of the workplace. An employer must be aware of the possible impact on the workplace culture if it chooses to monitor.

Furthermore, while the law may offer some protection in specific areas of our personal lives, it is incomplete—in part a result of the swift advance of technology, one which the law often has a hard time capturing. However, where an employer does have a policy regarding these issues, this policy is legally binding and the employer will be held to its enforcement. Many firms have now included a statement in their personnel policy manuals that explains that the Internet shall be used for business purposes only and that important company business communication may be delayed if the Internet is used for nonprofessional communications, creating a "traffic jam" on systems.

It is important to note that the increased incidence of employee monitoring has occurred simultaneously with significant institutional and structural changes in the labor market and working conditions. For example, telecommuting, flextime, and more liberal family leave policies are institutional labor market features that have become much more widespread in the past 10 years. Employers in the past were able to monitor their employees' work and productivity in person on the job. Yet in recent years, there has been an increase in the number of telecommuters from 8.5 million in 1995 to 11.1 million today.

In addition, the structure of the labor market has changed with an increase in the number of nonstandard workers. Nonstandard workers are defined as those who do not have a "regular" full-time job and include four main categories of workers: temporary help, on-call workers (such as substitute teachers), contract workers (such as those who provide cleaning, security or landscaping services), and independent contractors (individuals who obtain their own customers to whom they provide a service or product). In the 1990s, non-standard workers (including other part-time workers) comprised between 25% and 30% of the labor force. These institutional and structural changes may make it more important for employers to be able to monitor employee job performance electronically since there is less face-to-face monitoring possible in the new work environment. However, the question still remains regarding the extent of monitoring that is necessary.

Given the varied perspectives on monitoring by the employee and employer, the most effective means to achieve monitoring objectives while remaining sensitive to the concerns of employees is to strive toward a balance that respects individual dignity while also holding individuals accountable for their particular roles in the organization. Ann Svendsen, director of the Center for Innovation in Management, concluded that a company that maintains trust, a cooperative spirit, and shared understanding with its stakeholders creates greater coherence of action, better knowledge sharing, lower transaction costs, lower turnover rates, and organizational stability.

A monitoring program developed according to the mission of the organization, then implemented in a manner that remains accountable to the affected employees, approaches that balance. The following may serve as parameters for a monitoring policy that endeavors to accomplish the goals described above:

- No monitoring in private areas (i.e., restrooms)
- Limited to within the workplace
- Employees should have access to information gathered through monitoring
- No secret monitoring—advance notice required
- Should only result in attainment of some business interest
- May only collect job-related information
- Agreement regarding disclosure of information gained through monitoring
- Prohibition of discrimination by employers based on off-work activities

The above parameters allow the employer to effectively and ethically supervise the work done by his or her employees, to protect against misuse of resources, and to have an appropriate mechanism by which to evaluate each worker's performance, thus respecting the legitimate business interest of the employer. These guidelines respect the personal autonomy of the individual worker by providing for personal space within the working environment, by providing notice of where that "personal" space ends, and by allowing access to the information gathered, all designed toward achievement of a personal and professional development objective.

—Laura P. Hartman

See also Business Law; Chief Privacy Officer (CPO); Electronic Surveillance; Employee Monitoring and Surveillance; Employment Discrimination; Genetic Information in the Workplace; Genetics and Ethics; International Labour Organization (ILO); Occupational Safety and Health Administration (OSHA); Privacy

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World Bank

The World Bank, officially the International Bank for Reconstruction and Development (IBRD), was one of the three institutions that were conceived at the 1945 Bretton Woods, New Hampshire, conference. It was to initially aid in the reconstruction of war-torn Europe following World War II but ultimately finance development in lesser-developed countries. The World Bank has expanded since its conception to include both the IBRD and the International Development Association (IDA), and it is a part of the World Bank Group, which consists of the World Bank and three other agencies: International Finance Corporation (IFC), Multilateral Investment Guarantee Agency (MIGA), and International Centre for Settlement of Investment Disputes (ICSID). The World Bank Group's mission is to fight poverty and to improve the living standards of people in the developing world, with each agency specializing in different aspects of development.

The World Bank Group interacts with both the public and the private sectors. The World Bank deals directly with the governments of developing countries: the IBRD provides low-interest rate loans, policy advice, and technical assistance to low- and middle-income countries; the IDA provides grants and interest-free loans to the world's poorest countries. The other three agencies of the World Bank Group interact with the private sector by encouraging foreign private investment in developing countries. The IFC provides financing to private corporations in countries where capital is limited; the MIGA provides guarantees to foreign investors against losses due to noncommercial risks such as war and civil disturbance; and the ICSID provides a forum for conciliation and arbitration of international investment disputes between governments and private foreign investors.

The World Bank Group commands tremendous power and influence in both the public and private domains of development around the world. Not only is it the biggest and richest development finance institution in the world, its model for development is used and imitated by developing countries and nongovernmental agencies working on development projects; and hence, the economic, social, and environmental impact of development is heavily dependent on the policies that the World Bank Group promotes.

Structure of the World Bank Group

The World Bank Group's five agencies are run by member countries and a president who presides over all of them. The IBRD membership is contingent on membership in the International Monetary Fund (IMF), and membership in the IDA, IFC, and the MIGA is conditional on membership in the IBRD. There is no formal application for membership in the ICSID; a country must simply ratify the ICSID convention, which can take place as soon as the country has become a member of the IBRD.

The agencies' member countries are represented by a board of governors. Each member country appoints a governor who serves a 5-year term. If the IBRD member country is a member of the IDA or the IFC, the IBRD governor also serves as the governor of the IDA and the IFC. The MIGA governor is appointed separately. The board of governors is the ultimate policy maker of the agency. It determines membership acceptance, the amount of authorized capital, and the distribution of income. The board of governors convenes yearly at the Bank's Annual Meeting, which is held in Washington, D.C., 2 out of every 3 years.

The board of governors elects the president of the World Bank Group to a 5-year renewable term. By tradition, the president is a citizen of the largest shareholder country, which has always been the United States, and thus, the U.S. government essentially determines who will hold the position.

The day-to-day operations of the bank are delegated to the board of executive directors who work on-site at the Bank headquarters in Washington, D.C. They decide on loans, guarantee proposals, and IDA credit; determine policies that guide the Bank's general operation; and report on operations, policies, and budgets to the board of governors. The Bank has 24 executive directors who are chosen by the member countries. The five largest member countries (the United States, Japan, the United Kingdom, Germany, and France) each appoint an executive director. The remaining member countries appoint the other 19 executive directors through an election that is held every 2 years.

World Bank

Currently, the IBRD is owned by 184 countries. It is run like a cooperative with member countries as shareholders. The number of shares a country has is based on the size of its economy, and a country's voting rights is proportional to its shareholdings. The voting power of each country has varied over time, but the United States has always held the largest share: 36% at the time of the Bank's conception and 16.4% today. The G-8 countries (the United States, Japan, Germany, the United Kingdom, France, Canada, Italy, and Russia) represent 46% of the total voting power.

The World Bank agencies, the IBRD and the IDA, have the same staff and the same policy guidelines, but their source of funds and country eligibility for loans is different. The bulk of the IBRD loanable funds is borrowed on capital markets and from governments and central banks. It can borrow at a very favorable interest rate due to the guarantee of its members' callable capital. The Bank uses its high credit rating to lend its money out to borrowing countries at rates that are considerably more favorable than what the borrower could get on the market. The loans' low fixed-interest rate and relatively long time period of maturity make them very attractive.

The Bank focuses its lending on those countries that can effectively use assistance that is determined by the comprehensiveness of the country's development strategy and the degree of the country's commitment to development. IBRD loans are generally granted to middle-income countries for a specific project that contributes to poverty reduction, delivery of social services, environmental protection, or economic growth. Over the years, the Bank has shifted its efforts from growth-oriented projects toward projects and policy advice that are more explicitly focused on poverty reduction.

The process for receiving an IBRD loan is typically initiated by the borrower who identifies and prepares a project proposal. The borrower and the Bank negotiate the various terms of the project, which include objectives, components, outputs, performance indicators, implementation plan, and schedule of disbursing the loan funds. Once the Bank approves the loan, the borrower initiates the project. The Bank supervises the project's progress and evaluates its results.

The IDA was founded in 1960 to supplement the IBRD's development aid. The less developed countries were in need of better rates than the IBRD could offer at that time, and thus, the IDA (a separate account managed by the Bank) was created to fill this gap. The largest source of the IDA's funds come from new contributions from donor countries, of which 70% comes from the G-8 countries. Additional funds come from internal resources such as repayments and investment resources, and a small portion comes from retained profits of the IBRD.

The IDA loans (typically called credits) are made with no interest charge and for a period of time that is so long, it is virtually grant aid. Because of the favorable terms of the IDA money, there is a great deal of competition for it. The eligibility criteria for IDA money are as follows: First, the country must have a per capita gross annual income of $865 or less, and second, the country must not be creditworthy for loans on IBRD terms.

History

The history of the World Bank and its strategy can best be understood by looking at the objectives and philosophy of each of its nine presidents. The first president, Eugene Meyer, formerly the publisher of the *Washington Post*, had a contentious 6-month term due to differences of opinion with the executive directors about the Bank's strategy. Contrary to the desires of the executive directors, Meyer wanted to move cautiously. Not a single loan was approved during his tenure.

In 1947, John J. McCloy, a prominent Wall Street lawyer, was selected as the second president. He accepted the position on the condition that the president has authority over the executive board; this structural hierarchy remains in place today. McCloy was concerned with winning the confidence of Wall Street and with advancing the Bank's reputation as a quality lending institution. The only reconstruction loans that were ever made by the Bank (four in 1947) were done during McCloy's reign (1947–1949).

Eugene Black (1949–1963), the third president, is credited by some as having defined the Bank's niche. Infrastructure lending (roads, railroads, electric power, ports) became the type of projects that were supported with an emphasis on gross national product growth. The IFC (1956) and the IDA (1960) were created during Black's presidency.

The fourth president, George Woods (1963–1968), started to transition the Bank to become more innovative; it began to make loans for education and agriculture rather than simply for infrastructure. But some would say it was Robert McNamara's presidency (1968–1981) that made the Bank what it is today. He brought a sense of moral mission to the Bank, with an emphasis on poverty reduction. Urban-poverty alleviation, education, and health projects were a significant part of the Bank's portfolio. McNamara also instituted an intensification of research and long-term planning. The Bank prepared 5-year country lending plans that strongly guided its actions. Near the end of McNamara's term, he launched the structural adjustment loan, which stressed macroeconomic stabilization and put the IBRD policies closely in line with the IMF.

The next three presidents each served a 5-year term: A. W. Clausen (1981–1986), Barber Conable (1986–1991), and Lewis Preston (1991–1995). During the tenure of these three presidents, the development strategy promoted privatization, deregulation, and trade liberalization. The MIGA (1988) was created during Conable's term to encourage foreign direct investment in developing countries.

James D. Wolfensohn, the ninth president, finished his second term in 2005. He made several changes to the Bank during his tenure that are of significance: decentralized management, pushed staff out into the field to developing countries, empowered developing countries to have more of a voice in their development, and increased the Bank's interaction with nongovernmental organizations. In recent years, a notion of development that is broader than economic growth has been endorsed by many in the international community. To support this end, 189 countries at the UN Millennium General Assembly in 2000 endorsed the Millennium Development Goals, and the World Bank announced that it would join the United Nations as a full partner in implementing the goals needed to have sustainable poverty reduction. These eight goals are as follows: (1) eradicate extreme poverty and hunger; (2) achieve universal primary education; (3) promote gender equality and empower women; (4) reduce child mortality; (5) improve maternal health; (6) combat HIV/AIDS, malaria, and other diseases; (7) ensure environmental sustainability; and (8) develop a global partnership for development.

The tenth president, Paul Wolfowitz, took office in June 2005. He was previously the U.S. deputy secretary of defense and the chief architect of the U.S. invasion of Iraq. Besides holding several U.S. government positions, he taught at Yale University and Johns Hopkins University. Wolfowitz's role in the controversial Iraq war and his lack of development experience made his nomination somewhat controversial. But he won support, and since his unanimous approval, he stated that sustainable development and poverty alleviation, particularly in Africa, were his primary goals for the World Bank.

World Bank and Its Critics

There has been much debate over the role of the World Bank and its competency. Because of the power and influence of the United States, some have questioned the Bank's true motives: Is it acting in the general interest of development, or is it promoting the interest of the United States? Even if the Bank could refrain from this bias, some argue that the Bank is an interest group itself that is more concerned with maintaining its position and enhancing its power than promoting the general interest of development.

Some are also concerned with the Bank's accountability and transparency to the citizens of both the borrowing countries and the lending countries. The Bank has a virtual monopoly on the services it provides, so some argue that there are no sufficient checks on its activities. In addition, the Bank defines the development policies, carries out the assessment of the state of development, and evaluates the success of its projects and programs. Few outside the organization have access to enough of the information to be able to accurately assess the soundness of its operations.

In addition to the concerns of the Bank's structure, there has been controversy over a more fundamental issue, the Bank's approach to development. While the aim of the Bank has not changed over the years, its approach to achieving it has evolved. In the past, the Bank was focused on solving technical problems using market-based reforms: planning approaches, trade liberalization and privatization, and macrostability. In the 1980s and 1990s, the Bank has directed its efforts to implementing the Washington Consensus policy, which relies on trade liberalization, deregulation, and privatization. This globalization policy, which some argue, will lead to the destruction of natural resources, social ills, and economic destabilization, particularly in developing countries, has spurred antiglobalization protests, disrupting several World Bank meetings around the world. Protestors have forced the Bank to take extra security precautions at several Washington, D.C., annual meetings, to end their 2000 Prague meeting a day early, and to cancel their 2001 Barcelona development conference. Today, the Bank prescribes broader objectives than simply increasing the gross domestic product. To truly raise the living standard of those in developing countries, the Bank emphasizes a need for democratic and sustainable development. What has been missing, according to some, is a focus on the institutional infrastructure that is required to make markets work. Others argue that the real problem is the capitalistic strategy used to solve the problem of poverty. Some claim that the poor continue to be poor, not because they have been ignored or left behind by progress, but because they are the victims of the so-called progress.

The world has seen great progress toward the World Bank's mission; the percentage of the developing world's population living in absolute poverty (less than US$1 per day) has declined from 28% in 1990 to 21% in 2001. Still, there are 1.2 billion people living in absolute poverty today, and the number of people living below $2 per day has risen in the past 25 years from 2.4 billion to 2.7 billion people. Some argue that this is an indication that the World Bank has not yet realized a winning strategy to poverty alleviation.

—*S. L. Reiter*

See also Bretton Woods Institutions; Global Business Environments; Globalization; International Monetary Fund (IMF); World Trade Organization (WTO)

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WorldCom

WorldCom began in 2002 as the second largest long-distance U.S. telephone service provider with operations in 100 countries, 20 million customers, and assets of $107 billion. Seven months later, the company became the largest bankruptcy in U.S. corporate history as the result of a 5-year accounting fraud that totaled more than $11 billion. WorldCom experienced a breakdown of corporate governance. The CEO handpicked new board members, controlled the board's agenda, dictated policies, and enriched directors through generous consulting contracts, stock option distributions, and perks. Employees concerned about the fraud feared questioning executive authority and had no safe outlets to report the wrongdoing.

Growth Through Acquisitions

WorldCom's rise and fall parallels that of its long-time CEO Bernie Ebbers. Ebbers, born and raised in Canada, graduated from Mississippi College with a degree in physical education. He worked as a factory manager before earning a small fortune acquiring regional motels. When the U.S. government ended AT&T's long-distance telephone monopoly in 1984, Ebbers and several other local investors funded Long Distance Discount Services (LDDS) and offered 30% discounts to small businesses in Mississippi.

Ebbers took over as CEO of the financially struggling LDDS in 1985. He quickly generated a profit by applying the management techniques that led to his motel success: offer the lowest price, cut costs, acquire a competitor, consolidate resources, and use the new cost savings to acquire another competitor. Ebbers took LDDS public in 1989 and 6 years later changed its name to WorldCom. WorldCom shocked the telecommunications market in 1997 by purchasing MCI, the second largest company in the industry and more than three times the size of WorldCom, for $37 billion, which at the time was the largest acquisition in U.S. corporate history. Under Ebbers's leadership, WorldCom's revenue jumped from $8.6 million in 1986 to $37.8 billion in 1999, aided by more than 60 acquisitions.

When WorldCom's stock peaked in June 1999, the high-profile Ebbers, who borrowed large amounts of money to buy company stock and real estate, became the 376th richest person in the world, with an economic worth of $1.4 billion. Ebbers, who maintained that a proposed code of ethics was a colossal waste of time, was also the recipient of perks from investment bankers earning large fees funding WorldCom's $70 billion worth of acquisitions. Salomon Brothers' Jack Grubman allocated Ebbers's stock in 21 initial public offerings, which Ebbers quickly sold for $11 million.

Accounting Fraud

In 1999, Ebbers instructed Scott Sullivan, WorldCom's chief financial officer, to do whatever was necessary to meet Wall Street's high quarterly expectations and pay off the company's burdensome acquisition debts. Sullivan fraudulently withdrew money from an accrual account and claimed it as revenue to meet second quarter 1999 financial projections. He continued doing so for the next six quarters, falsifying more than $3 billion in revenue.

In search of more cash to pay operational expenses, Ebbers bid $129 billion for Sprint, then the third largest telecommunications company, later that year. Combined, WorldCom-MCI and Sprint would control nearly 40% of the long-distance market, slightly less than AT&T. However, in June 2000, the U.S.

Justice Department ruled that acquiring Sprint would violate antitrust laws. Ebbers could no longer grow WorldCom by buying large competitors, causing a management crisis.

WorldCom's revenue and profits were also damaged by cutthroat competition with AT&T, the collapse of the dot.com market, and an economic recession. Ebbers received margin calls from brokers because his investments were leveraged with WorldCom's declining stock. WorldCom's board of directors eventually loaned Ebbers $400 million from the company, enabling him to pay his margin calls without dumping WorldCom stock on the already depressed stock market. Ebbers rewarded Stiles Kellett, chair of the board's Compensation Committee, by leasing him a corporate jet for a nominal price of $1 a month plus some incurred expenses.

By early 2001, Sullivan used up all the excess cash in WorldCom's accrual accounts. At the end of the first quarter of 2001, Sullivan began to illegally capitalize more than $3 billion of regular operating expenses to meet Wall Street projections by delaying the recording of daily expenses, a practice he would continue the next four quarters.

Sudden Collapse

Enron, audited by Arthur Andersen, unexpectedly declared bankruptcy at the end of 2001. In March 2002, the SEC extended its investigation to WorldCom, another major Arthur Andersen client. WorldCom's stock dropped below $5 a share, causing credit problems and more margin calls for Ebbers.

At the end of April 2002, the board of directors forced Ebbers to resign. He received a very generous severance package of $1.5 million a year for the rest of his life and other lavish perks. A week later, WorldCom's credit rating fell to junk bond status. Sullivan then drew down WorldCom's entire $2.65 billion line of credit under false pretenses, the banks not knowing about the company's fraudulent bookkeeping dating back to 1999.

In late June, Cynthia Cooper, WorldCom's internal auditor, notified the board of directors about massive accounting irregularities. The company announced a $3.8 billion accounting fraud, restated earnings, and fired Sullivan. The SEC filed charges against WorldCom for falsifying revenue by an amount that turned out to be more than $11 billion. An avalanche of lawsuits were soon filed on behalf of 2.5 million shareholders, and WorldCom filed for bankruptcy protection.

During the trial, Ebbers claimed to be ignorant of any wrongdoing. The jury disagreed, found Ebbers guilty of fraud, and he was sentenced to 25 years in jail. Sullivan's 25-year jail sentence was reduced to 5 years for cooperating with federal investigators. After filing for Chapter 11 bankruptcy in July 2002, WorldCom reorganized and changed its name to MCI. The firm has now adopted a new code of ethics, implemented an ethics hotline to report wrongdoing, and has established an ethics officer position.

—Denis Collins

See also Arthur Andersen; Fraud; Manipulation, Financial; Sarbanes-Oxley Act of 2002

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World Economic Forum

The World Economic Forum (WEF) is an independent, international, not-for-profit organization based in Geneva, Switzerland. Founded in 1971 by Swiss business professor Karl M. Schwab, the WEF serves as a platform for business and political leaders from numerous countries to discuss and debate social and economic issues of global concern. According to the WEF, its mission is to improve the state of global political, economic, and social affairs in coordination with various industry and governmental partners. The core membership of the WEF consists in about a thousand corporations, most of which are among the foremost multinational corporations in the world. Member corporations must meet annual revenue requirements and pay significant annual fees in support of their membership in the WEF. The WEF's annual meeting is held in Davos, Switzerland. Along with representatives from its corporate members, assorted political leaders, academics, journalists, and leaders of nongovernmental organizations (NGOs) are invited to participate at the open sessions at the Davos meeting. Apart from the open sessions, numerous informal meetings, workshops, and assorted industry networking activities take place at the annual meetings of the WEF. Unlike the open forums, these informal sessions are generally closed off from media access. In addition to its annual meeting in Davos, a number of regional meetings are also held by the WEF in various locations around the world to further promote its mission. The WEF also funds various social and economic initiatives and publishes economic reports on different aspects of the global economy.

In recent years, a number of interest groups, including environmental, labor, and antiglobalization organizations, have held highly publicized protests during the annual meeting of the WEF in Davos. These demonstrations are indicative of the strong opposition to the WEF from certain quarters. While the WEF promotes itself as an impartial forum for the discussion of global social and economic issues, critics of the WEF accuse the organization of serving solely as a mechanism for the promotion of corporate economic interests. Such critics have argued that the WEF's activities are geared more toward securing profits for its corporate members than actually addressing global social and economic problems, that it functions largely as a political lobbying organization for corporate interests, and that its membership, largely stemming from the United States, Europe, and Japan, is not truly reflective of global demographics. In recent years, the WEF has taken several positive steps to respond to some of these criticisms, including inviting more NGOs to participate in its annual meetings, expanding its membership base from underdeveloped nations, and initiating a series of dialogues with groups traditionally critical of the organization. Despite such gestures, many critics of the WEF remain unappeased. In many ways, this ongoing debate is not surprising, as the dispute over the WEF is connected to the larger arguments about the nature and direction of globalization. As such, it is likely that the function of the WEF within the global economy will remain contested in the foreseeable future.

—Daniel E. Palmer

See also Developing Countries, Business Ethics in; Development Economics; Globalization; International Business Ethics; Multinational Corporations (MNCs); Nongovernmental Organizations (NGOs); World Trade Organization (WTO)

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World Health Organization (WHO)

The World Health Organization (WHO) was established on April 7, 1948. The WHO is an agency-institution within the structure of the United Nations. It was developed through the discussions that originated in the San Francisco Conference, April to June, 1945, and the International Health Conference at New York (convened by the United Nations Economic and Social Council), June to July, 1946. Prior to the establishment of the WHO, three key dates indicate the institutionalization of health on an international scale: 1851, The First International Sanitary Conference held in Paris; 1907, the agreement setting up the Office International d'Hygiène Publique signed in Rome; 1919, Health Organisation of the League of Nations that led to the creation of the body that developed into the WHO.

The WHO is governed by 193 member states through the World Health Assembly, meeting annually in Geneva. The Assembly manages three key roles: It legitimates the varied programs initiated by the organization, it agrees on budget policies, and it decides on key policy discussions that arise within the organization.

The organization prioritizes two key activities. (1) It advises and supports health systems in a variety of countries to develop health administration, delivery, and prevention. The use of health teams to combat specific health problems such as HIV/AIDS, tuberculosis, and other communicable diseases are supported by projects that improve basic health needs such as sanitation, nutrition, and hygiene. (2) The organization has evolved into an intergovernmental negotiating body that assists a variety of governments and nongovernmental organizations (NGOs) in seeking to regulate a range of sectors that affect health. This role is supported by the publication of health statistics and wide medical information that is used by a range of agencies formulating health policies. In the global health field, key demands include the following:

- Extensive work taking place at the country level in the community and with government—capacity building for local health care systems
- Health Action in Crisis (HAC)—managing emergency situations, coordinating response of governments, NGOs, and related agencies to prevent disease
- Advocacy for health care initiatives globally—lobbying, providing literature and educational material, publicity campaigns
- Working in collaboration—globally providing technical assistance and expertise to support WHO projects

While not a regulator in the rigid rule-making sense, the WHO is an important organization in shaping the regulatory conditions in a variety of sectors and settings, a role that establishes health-related compliance procedures such as influencing food management policies through its Food Safety Department. The public relations media arm of the United Nations is well served by goodwill ambassadors who raise the profile of the organization and the health-related matters it tackles.

Health is defined in the constitution of the organization as a state of complete physical, mental, and social well-being and not merely the absence of disease or infirmity. The central aim of the institution is to promote high levels of health to all peoples. The impact and consequence of conflict should not go unnoticed. Psychological rehabilitation, mine victim support, and range of related health concerns noted in children and adults caught up in conflict between and within states proliferate in ongoing civil wars and social unrest.

The headquarters of the WHO is located in Geneva, Switzerland. Everyday operations are coordinated through the Secretariat, which is made up of staff in Geneva and in regional offices. Regional offices work alongside governments and a range of NGOs in coordinating policies and implementing programs and projects.

The global concerns of health security are represented by the Global Outbreak Alert and Response Network, which alerts the international community to outbreaks that threaten cross-border health security. The response network assists in combating international infectious outbreaks, ensuring that technical assistance and expertise are rapidly deployed to crisis zones, thus contributing to long-term epidemic preparedness and capacity building.

The WHO is split into six regions. The separation of countries into regions is based on geography and political agreement, a structure not necessarily without contention from its members. The six geographical areas within the organization are the following: The Eastern Mediterranean (HQ, Cairo), Western Pacific (HQ, Philippines), Southeast Asia (HQ, New Delhi), Europe (HQ, Copenhagen), Africa South of the Sahara (HQ, Brazzaville), and the Americas (HQ, Washington, D.C.). It should be noted that each region contains a number of diverse countries, each containing numerous nations and communities.

Each of the regional offices has relative autonomy in delivering a range of health initiatives directed to the needs of the area. The Eastern Mediterranean office focuses on four key priority programs: the Tobacco Free Initiative, Roll back Malaria, Stop Tuberculosis, and Building Community—cross-country-based health initiatives. The office has a special program in polio eradication. HIV/AIDS programs are directed to areas of need throughout the region.

The regional office for the Western Pacific has a range of activities to address health concerns related to immunization and health management. Special initiatives include the "3 by 5" response to AIDS/HIV-related health concerns, which was launched by the Joint United Nations Programme on HIV/AIDS (UNAIDS) and the WHO in 2003. The aim of the program is to provide low- and middle-income countries with life-prolonging antiretroviral treatment. The office is also active in pandemic preparedness.

Southeast Asia has evolved as a distinct area following World War II. The Southeast Asia office is responding to natural disasters such as the earthquake that struck Pakistani Kashmir. Health management programs are being implemented to check the spread of communicable diseases and improve awareness and prevention of noncommunicable diseases. Diabetes is receiving attention, its incidence resulting in particularly targeted attention.

The Regional Office for Europe focuses its attention on noncommunicable diseases such as heart disease and cancer, which are linked to alcohol misuse, obesity, and smoking. The development of health systems is a concern in countries such as Russia. Serious emergencies relating to maternal and child health, communicable diseases, and psychological rehabilitation are notable in the North Caucasus.

The Regional Office for Africa focuses on resources and programs for fighting HIV/AIDS and other communicable diseases. While other noncommunicable and prevention needs persist, resources are overwhelmingly directed to treating the HIV/AIDS crisis.

The health of the America's region is covered by the Pan American Health Organization. The Northern areas are prolific in sedentary lifestyles, which results in high treatment costs for noncommunicable diseases. In Latin America and the Caribbean, programs have been implemented to tackle reemerging diseases such as cholera and tuberculosis, transferring resources from the wider disease-prevention programs and general health improvements.

Although delivered by the regions, most of the big issues are global. The UN Millennium Development Goals have a direct impact on health in its widest sense. The eight defined goals in the program continue to be impeded by politics (obstructions in the decision-making process), culture (misunderstandings arising through language and belief systems), and resources (scarce funds), factors that frustrate the overwhelmingly positive goals of the WHO.

—Paul D. Sheeran

See also United Nations

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World Resources Institute (WRI)

The World Resources Institute (WRI), a 501(c)(3) nonprofit organization based in Washington, D.C., focuses on creating sustainable solutions for protecting and enhancing the natural environment. Founded more than 20 years ago, the WRI's mission is to move human society to live in ways that protect Earth's environment and its capacity to provide for the needs and aspirations of current and future generations.

Using innovation and research in practical ways, the WRI is a think-tank dedicated to solving seemingly intractable problems such as global climate change, greenhouse gas emissions, biodiversity, and degradation of ecosystems. By engaging with special interest groups, corporations, public advocates, and government agencies, the WRI creates extensive programs domestically and internationally to deliver both short-term results and long-term goals. In creating mutually beneficial arrangements with NGOs, corporations, and environmental organizations, the WRI seeks to improve the lives of people while promoting viable sustainable development goals. For example, the WRI supports market-based emissions trading for encouraging innovative means to reduce carbon emissions from greenhouse gases.

Active internationally, the WRI has been involved in major international negotiations such as the 1992 Rio Declaration, the 1992 UN Framework Convention on Climate Change, and the 1997 Kyoto Protocol. The WRI works with intergovernmental bodies such as the International Finance Corporation of the World Bank and the Equator Banks to encourage sustainable practices and systems worldwide.

The WRI has built a global network of international organizations, local activists, scientists, governments, entrepreneurs, and businesses throughout the world. Working closely with nearly 400 partners in more than 50 countries on a broad spectrum of sustainable development issues, they work to enhance our collective ability to catalyze permanent change.

The WRI and its president Jonathan Lash, for example, worked in 2005 with General Electric and its CEO and Chairman Jeffrey Immelt to create ecoimagination initiatives to reform business approaches with respect to the environment and development. Jonathan Lash, the only leader of a nonprofit environmental organization ever to be named one of the "100 most influential people in finance" by *Treasury and Risk Management* magazine, focuses on creating a vision for the future. The WRI's Sustainable Enterprise Program specifically targets work with businesses to create profitable solutions to environment and development challenges. The WRI brings together corporations, entrepreneurs, investors, and business schools to accelerate change in business practice. The program improves people's lives and the environment by helping business leaders and new markets thrive.

The WRI, in collaboration with The Aspen Institute, publishes a biennial report—*Beyond Grey Pinstripes*—examining the business schools' ability to prepare future managers in understanding the intersections of social, environmental, and economic perspectives in a competitive global economy. Started in the 1990s, *Beyond Grey Pinstripes* grades universities from around the world on their coursework, research, and institutional support for examining businesses' economic and social impacts. The WRI and The Aspen Institute share information on leading coursework, student opportunities, faculty pioneers, and institutional support for social, environmental, and ethical programs/curricula in business schools around the world. A searchable Web site shares ratings, criterion, syllabi, and supporting information by the participating business schools. By 2005, 54% of the participating schools required a course in ethics, CSR, sustainability, or business and society, a near 60% increase since 1991. In-depth reports from the WRI/Aspen Institute database focus specific attention on business and society topics such as activities in China, MBAs and women, CSR and finance, and corporate governance.

The WRI organizes its resources, ideas, and implementation expertise around primary program areas such as domestic and international climate change, access and information, and markets and enterprises. These program areas overlap creating a network of expertise at the local, national, and international level on specific topics (e.g., climate change) based on factual knowledge (i.e., access and information) and shared engagement among public and private enterprises. These three WRI program areas (domestic and international climate change, access and information, and markets and enterprises) are discussed below.

Climate change, a priority area for WRI, focuses on both domestic (the United States) and international policy initiatives. Since its inception, the WRI has been involved with creating policies to reduce greenhouse gas (GHG) emissions within the United States. The U.S. government's refusal to address international global climate change, with significant per capita GHG emissions and refusing to ratify the multilateral Kyoto Protocol, has encouraged the WRI to work with individual states, private enterprises, and international NGOs for climate change friendly policies in a carbon-constrained world. Engaging companies to create innovative technologies and voluntarily reduce emissions; working with individual U.S. states to pass laws limiting GHG emissions; and cocreating a Greenhouse Gas Protocol to harmonize international accounting and reporting standards with the World Business Council for Sustainable Development (WBCSD) are three examples of how the WRI creates multiparty coalitions to solve complex issues. The WRI works with private enterprises to encourage development of alternative energies such as hydrogen, renewable energy (wind, solar), market-based trading mechanisms, and procuring climate-friendly technologies.

Access and information are focused on guaranteeing public access to information, decision making, and transparency regarding natural resources and the natural environment. As codified in Principle 10 of the 1992 Rio Declaration, relevant, timely information leads to informed decision making and better choices to avoid unnecessary risks to citizens' health and well-being. While 178 governments agreed to the Rio Declaration, actual practice has lagged behind. Informed participation with transparency and accountability, the WRI believes, leads to better win-win-win opportunities and the ability to affect public policy. Dispersion of innovative technologies, meaningful public participation in environmental policies, and right-to-know initiatives are consistent with WRI's goals for its access program.

A third priority area for the WRI is focusing on markets and enterprises and their sustainable development programs, policies, and practices. Markets as institutional and governance mechanisms build incentives, systems, and appropriate reviews, oversight and expand economic opportunity, and encourage environmentally sensitive design and operations. By engaging with private enterprises, the WRI seeks to meet essential human needs, create jobs and wealth in communities and enhancing the quality of life. Engaging with institutional investors and focusing on financial flows are of particular interest since financial opinion leaders can encourage environmentally sustainable practices. The WRI works with institutions and private enterprises for adopting and advancing sustainability standards to assess environmental impacts of institutional investments. In the coming years, the WRI has identified sustainable growth via private enterprise in emerging economies as a key goal. By promoting sustainable economic growth through investment and the use of innovative technology, low-income markets are a great opportunity for private investment and sustainable development. These market opportunities can deliver social and environmental benefits.

—Jennifer J. Griffin

See also Aspen Institute's Business and Society Program; Biodiversity; Environmentalism; Environmental Protection Legislation and Regulation; Greenhouse Effect; Kyoto Protocol; Pollution; Sustainability

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World Trade Organization (WTO)

The World Trade Organization (WTO) is a global trade agreement with 150 member states accounting for 97% of the world trade. Currently, 30 other nations are negotiating membership. The purpose of the WTO is to promote fair competition and efficiency. Its approach is rooted in the standard classical economic theory of Adam Smith. Instead of each country producing the full range of products that its own market demands, all nations pool their resources to provide the best value for all consumers. In this way, products will tend to be produced where labor costs are cheapest, passing the savings onto consumers and helping to grow commerce on an international scale. Furthermore, lesser-developed countries also benefit as demand for their cheaper labor tends to rise, ultimately also increasing their wages. Thus, globalization tends to benefit all nations, thereby working to achieve the utilitarian ethical goal of the greatest good for all concerned.

History, Structure, and Function

The WTO was created in 1995 by the "Uruguay Round" of talks held by member nations of the General Agreement on Tariffs and Trade (GATT), which includes the United States. GATT was established by the United Nations (UN) Conference on Trade and Employment in Havana in 1948 to promote free international trade. The WTO is in effect, the long-delayed successor to the anticipated International Trade Organization (ITO), which was intended to follow GATT when its charter was agreed on at the Havana UN conference of 1948. However, creation of the ITO was subsequently blocked by the United States, in fear that such a regulating body might compromise rather than benefit American commercial interests.

The WTO is a voluminous trade pact, now totaling more than 30,000 pages. Its primary objective is to help trade flow smoothly, freely, fairly, and predictably. It does this by

- administering trade agreements;
- acting as a forum for trade negotiations;
- settling trade disputes;
- reviewing national trade policies;
- assisting developing countries in trade policy issues, through technical assistance and training programs; and
- cooperating with other international organizations.

WTO decisions are generally made by consensus. Its agreements are then ratified by all member states. Although majority vote is an option, it is rarely used. The WTO's top decision-making body is the Ministerial Conference, which meets at least once every 2 years in a given member state. Its next governing body is the General Council, which includes ambassadors and heads of delegation in the Geneva headquarters, as well as officials sent from member states to Geneva. The General Council also meets as the Trade Policy Review Body and the Dispute Settlement Body. The third governing body consists of the Goods Council, Services Council, and Intellectual Property Council (TRIPS), which all report to the General Council. Finally, numerous specialized committees, working groups, and working parties deal with individual agreements and areas such as the environment, development, membership applications, and regional trade agreements.

Originally, GATT only dealt with trade-in goods. But the WTO also facilitates trade-in services. This includes banks, insurance firms, telecommunications companies, tourist agencies, hotels, transportation companies, and so on. The rules governing such trade appear in the General Agreement on Trade in Services. WTO members have thereby made individual commitments, stating which of their services sectors they are willing to open to foreign competition, and how open those markets are.

More than 75% of WTO member states are developing countries. Thus, all WTO agreements contain special provisions for them, including extended periods for compliance, measures to increase their trading opportunities. The WTO even provides support to help them build infrastructure, handle disputes, and implement technical standards.

The WTO also includes an appellate body to resolve trade disputes between member states. Complaints are usually directed at nations erecting unilateral protectionist barriers to competition from foreign suppliers. If a complaint is upheld by the appellate body and the member nation in question continues to act in breach of the ruling, it can be subjected to severe penalties, including retaliatory import tariffs against its own goods. For example, a mid-sized American television manufacturer recently brought China before the U.S. International Trade Commission for breaching WTO rules by "dumping" televisions on the U.S. market at unfairly low prices achieved through government subsidy and an undervalued currency. The company prevailed, thereby compelling China to raise the prices of its television exports to competitive levels, thus enabling the American manufacturer to remain in business. Unfortunately, few small- to medium-sized U.S. manufacturers have been able to remain solvent long enough to bring forth such suits in the face of rapid offshore outsourcing (offshoring) trends accelerated by the WTO agreement. Most U.S. manufacturers have either gone out of business or offshored production. Whether this trend will be counterbalanced by new industries and growing foreign investment in the U.S. labor remains to be seen.

Noneconomic Concerns

Despite general agreement that the WTO has worked to the benefit of the majority, some fear that its globalized system of free trade still marginalizes the interests of large numbers of people by overlooking important noneconomic concerns. The most commonly voiced concerns can be grouped into the following three overarching categories:

1. Does the WTO marginalize the environment, animal welfare, and human rights?
2. Does the WTO increase consumption at the expense of sustainability?
3. Does the WTO erode national sovereignty, thereby enriching wealthy nations at the expense of poor nations?

Does the WTO Marginalize the Environment, Animal Welfare, and Human Rights?

To promote international trade, the WTO must repress protectionist measures. One important way in which this is accomplished is by the "product/process" distinction. This rule only permits nations to restrict imports based on the "product," that is, its quality. Thus, if it presents a danger to its consumers, its import can be restricted. But it becomes much more difficult for a nation to restrict imports of a product based on the "process" in which it is produced. This is because of the fear that if a country restricted imports merely because the exporting country had different environmental, health, and social policies from its own, the door might be opened to a flood of gratuitous protectionist abuses.

This distinction thus compelled the WTO to reject appeals by various nations including the United States and the European Union of mistreatment of animals such as dolphin kills from non-dolphin-safe tuna fishing, fur derived from animals caught in steel-jaw leghold traps, cosmetics tested on animals, beef treated with hormones, genetically modified organisms such as fruit and vegetables, and so on. In some of these cases, such as discontinuing non-dolphin-safe tuna fishing, agreements were made outside of the WTO though suspicion remains that the practice still exists. More recently, since the massive public protest that effectively canceled the 1999 WTO meeting in Seattle, the WTO has shown more willingness to take exception to the product/process distinction based on Article XX of GATT. It allows for exception necessary to protect public morals, necessary to protect human, animal, or plant life or health, and relating to the conservation of exhaustible natural resources. Thus, in 2001, the United States succeeded in maintaining its ban on imports of shrimp caught in nets dangerous to sea turtles so long as it made ongoing, serious, good-faith efforts to reach multilateral agreement on its own. Other complaints based on the process of production, such as the mistreatment of workers, child labor, or the depletion of endangered species, have not been raised before the WTO. Hence it is not yet clear how it might rule on such issues.

Does the WTO Increase Consumption at the Expense of Sustainability?

By facilitating trade across the globe, the WTO encourages nations to import myriad goods with no restriction on the distance traveled or the amount of energy and natural resources consumed. So long as the transaction costs involved in making the exchange internationally are less than the differences in production costs, trade will likely occur. But critics point out that this promotes the overconsumption of natural exhaustible resources such as petroleum needed to ship so many goods. Thus, instead of keeping production in relatively close proximity to both supply and demand, in this new paradigm a country such as the United States may ship raw materials abroad only to import the very products those materials produced. The results are often products that take much more energy and natural resources to produce than necessary.

Furthermore, since globalization promotes economic growth by giving consumers more buying power, that is, providing them with more goods at lower prices, critics argue that this fuels perilous overconsumption. In response, free-market defenders influenced by the "cornucopian" economic theory of Julian Simon point out that thanks in part to technological advances stimulated by a free market, the costs of depleting natural resources often decline as consumption increases. For example, as petroleum becomes scarce, new means of extracting it are invented. And as the resource becomes entirely depleted, research in alternative fuels is stimulated. Thus, according to this thinking, consumers never have to make sacrifices in the interest of sustainability. However, critics respond that this overlooks natural resources that are intrinsically valuable and can never be restored or replaced. Examples include old-growth rainforests, wild salmon fisheries, and global climatological stability threatened by global warming from increased fossil fuel consumption. But as mentioned above, the WTO allows for restrictions relating to the conservation of exhaustible natural resources. Thus, its member states could still achieve consensus on such issues.

Does the WTO Erode National Sovereignty, Thereby Enriching Wealthy Nations at the Expense of Poor Nations?

Once a nation joins the WTO, it undergoes considerable pressure to remain a member. As international trade industries grow, employing substantial numbers of people, the threat that such industries will collapse becomes so palpable that canceling WTO membership becomes virtually unthinkable. The WTO sees this as a positive constraint since it promotes discipline by discouraging protectionist policies that are bad for business. But this arguably creates a moral hazard in which policies that may be in the best interest of a nation's citizens are disregarded. For example, diversified local industries may be replaced by a small number of foreign-owned, large-scale suppliers. It may also become impossible for lesser-developed countries—as has been the case in Africa—to begin producing life-saving drugs and medical treatments at a price their people can afford. The preexisting intellectual property rights of the exporting nations would forbid it. What has sometimes happened instead is that after prolonged debate and litigation during which time numerous people suffer and/or die from lack of treatment, public pressure mounts to the point of compelling pharmaceutical companies to begin offering their treatments free or at greatly reduced prices.

While there is indeed pressure for lesser-developed countries to join the WTO, it is unlikely that they undertake greater risk in joining than developed countries. Indeed, the WTO has been a boon to lesser-developed counties as jobs in developed countries become offshored where they can be performed more cost-effectively. As a result, developed countries sacrifice jobs in the short term in the hopes that the added economic return of offshoring will ultimately create more jobs for their own citizens at home.

Conclusion

The WTO has undoubtedly achieved its principle goal of promoting economic growth on a global scale. Furthermore, it has recently made progress in addressing noneconomic ethical issues. Whether this progress will continue will likely depend on the general public's degree of awareness and concern. Some have argued that the WTO should be a stepping-stone toward the establishment of a bona fide global democratic governing body better able to balance economic and broader social interests, for example, a reformed United Nations. Assuming such a body would be advantageous, its major stumbling blocks would be garnering the support of multinational corporations benefiting from the status quo and the question of how to represent the citizens of nondemocratic nations.

—Julian Friedland

See also Animal Rights; Developing World; Development Economics; Economic Efficiency; Entitlements; Ethical Imperialism; Fairness; Global Business Environments; Globalization; Greenhouse Effect; Smith, Adam; Sweatshops; Utilitarianism

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World Wildlife Fund

The World Wildlife Fund (WWF) is a transnational conservation organization supported by 5 million members worldwide, dedicated to protecting and conserving endangered species and natural environments, and increasing awareness of threatening global issues such as climate change and overharvesting. The WWF directs conservation projects in more than 100 countries, and partners with numerous environmental and nonenvironmental groups to cosponsor initiatives in more than 30 countries, focusing on policy development, education, and advocacy.

The WWF was founded on September 11, 1961, by biologist Sir Julian Huxley, ornithologist Sir Peter Scott, director general of the British Nature Conservancy Max Nicholson, and Prince Bernhard of the Netherlands. Originally known as The World Wildlife Fund, an International Foundation for Saving the World's Wildlife and Wild Places, the fund emerged from the significant concerns of prominent members of the research-based World Conservation Union (IUCN). These scientists recognized the potential loss of wilderness and native animals in Africa, Asia, and Latin America as a disaster in the making, accompanying economic development after decolonization and World War II. It was quickly evident that major financial resources would be required to effectively protect the land and its indigenous species; hence, the WWF was initially conceived as the fund-raising arm of the IUCN. Since its genesis the fund has been dedicated to building scientific, technical, and financial resources in service of conservation activities. In addition, they have formed partnerships with major institutions worldwide, including universities, nongovernmental organizations, government agencies, lobbying groups as well as corporations. The fund's objectives promote the conservation of natural resources while paying heed to regional economic development.

Traditionally, the WWF embarked on many local area conservation projects, in which scientists were sent to developing countries to examine the endangerment of local animals and the deterioration of their habitats. Originally, the WWF sought to put a halt to development in particular wildlife areas by working with local authorities to form national parks within specified boundaries. These efforts met with limited success, because migrating animals are not easily contained within boundaries established by humans. As the indigenous people of developing countries became more empowered, the WWF made a more conscious effort to integrate the perspectives of the local populations into its conservation agenda.

Among its most celebrated breakthroughs are debt-for-nature swaps, the international ban on ivory trading, and its outreach to protect the giant panda. The swaps resulted from the recognition of the economic circumstances of developing nations and providing solutions for countries' massive accumulated debt. Thomas Lovejoy, vice president of the WWF in 1984, proposed acquiring portions of countries' debt in exchange for the conservation of their natural resources. The WWF works with major financial institutions to retire specific amounts of a developing country's debt by asking banks to sell the debt back to the country at a highly discounted rate. The bank then donates the revenue received from that sale back to the country in its local currency to fund local conservation projects. At the same time, the WWF and other land-preservation groups contribute significant funds to support these conservation projects.

In protecting African wildlife from local hunters, the fund employs wildlife trade experts through an organization called TRAFFIC to enforce international laws against illegal trade of particular wild plants and animals, including poaching and elephant hunting. In 1979, the fund hallmarked itself as the first conservation organization to enter the borders of China. The WWF partnered with the Chinese government to protect the habitat of the giant panda, from which the fund inherited its signature panda logo. The fund has also led renowned efforts to conserve the homes of endangered species such as tigers and rhinos.

Meanwhile, the WWF contributes great resources to scientific research and technological advancements. From its own "Green Building" U.S. headquarters in Washington, D.C. to the WWF's Conservation Science Program (CSP), the fund champions technology as one of the most effective approaches to preserving the health of ecological systems. The CSP, founded in 1990, assembles teams of scientists to research specific biodiversity issues, apply their expertise directly to current field projects and to publish their technological advances and findings in scientific journals.

As it has grown, the WWF has confronted critics in its policy initiatives and outreach efforts from economic, cultural, and environmental standpoints. Many radical environmentalists point to the WWF's promotion of third-wave environmentalism, a strategy that attempts to persuade corporate polluters to internalize pollution costs in their production methods. Moderates promote these efforts as pragmatic, while extreme environmentalists consider it working with the enemy, as corporations trade finances for favors and corporate directors have gained seats on the board of the WWF. The WWF has received funding from major oil corporations, including Amoco, Exxon, and Mobil, as well as chemical giants, Dow and Du Pont.

From the opposite side, proponents of economic development have attacked the WWF's fundamental perspective, arguing that "sustainable development" is infeasible and that conservation efforts directly impede economic development in Third World countries. Furthermore, some critics charge that the WWF is insufficiently concerned with the local hierarchies and power struggles within the cities and communities of developing countries, while granting recognition to political leaders and bureaucrats. The WWF's agenda of collaborative economic development is considered by some to be merely the means of attracting funds from large international development organizations.

Under its current president and CEO, Carter S. Roberts, the WWF has amplified its protection of the Amazon Rain Forest, linking up with the World Bank and the Brazilian government to establish the Amazon Region Protected Areas initiative. The fund directs additional campaigns, including partnering with the Scripps Institution of Oceanography to conserve the well-being of the oceans' ecosystems.

By the end of 2005, the WWF directed 1,200 field projects around the world. The executive board secretariat resides in Gland, Switzerland, and maintains a second central hub in the United States.

—Robbin Derry

See also Biodiversity; Deep Ecology; Environmental Ethics; Environmentalism; Greenhouse Effect; Land Ethic; Natural Resources; Ozone Depletion; Pollution; Pollution Externalities, Socially Efficient Regulation of; Speciesism; Tragedy of the Commons; Wilderness

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Z

ZAIBATSU

The *zaibatsu* has been central to industrialization and modernization in Japan. The word *zaibatsu* has two distinct meanings depending on the context. For journalists, it means a financial clique or a wealthy person. For academics of business, history, and management, it means huge industrial conglomerates. In Japan, the word means financial clique or a wealthy person. In the rest of the world, it refers to industrial conglomerates.

Zaibatsu is a word used mainly in Japan. The word *zaibatsu* consists of "*zai*" and "*batsu*." In Japanese, *zai* means money or possessions and *batsu* means a closely united group of people who do not allow others easily to join their group. The *zaibatsu* originated late in the Edo Period (1603–1867) and was formed early in the Meiji Period (1868–1912). The origin of the *zaibatsu* is "*gōshō*" or a wealthy merchant in the days of the Edo period. According to the history of Japan, a *gōshō* was authorized by the Tokugawa regime to buy and sell commodities on a large scale when it involved transportation from one place to another.

After the Meiji Restoration in Japan in 1868, the Meiji government adopted fundamental policies for building a modern nation: *fukoku-kyōhei* and *shokusan-kougyō*. *Fukoku-kyōhei* policies are intended to enrich the country and strengthen its military powers. *Shokusan-kougyō* policies are intended to increase production and develop industries. Early in the Meiji period, the Meiji government owned and controlled businesses to promote the industrialization of Japan. During this time, the *zaibatsu* form had been part of political merchant activities. These businessmen with political contracts were referred to as *seishō*. During the middle of the Meiji period, these businesses were disposed of for a petty sum. Thousands of government-owned businesses, including mining, trading, financing, and war industries, converted to private enterprises.

Later the phrase "from *seishō* to *zaibatsu*" or "from political merchants to *zaibatsu*" was used to mean that the *zaibatsu* developed directly from political merchants. In the late Meiji period, the Japanese economy was practically dominated by the giant, family-owned business combines, or *zaibatsu*. The four major *zaibatsu* companies were Mitsubishi, Mitsui, Sumitomo, and Yasuda. Since then, the holding companies of *zaibatsu* have functioned as "*zaibatsu-honsha*." All *zaibatsu* were groups of companies owned and entirely controlled by the *zaibatsu* family. Membership in the *zaibatsu* family was limited to a group of individuals living under one roof and usually under one head.

During World War I, the *zaibatsu* and their companies changed their strategies. First to diversify their businesses, the *zaibatsu* exploited opportunities in the new areas or actively merged and acquired nonmember companies and their subsidiaries. The diversification of the *zaibatsu* and their companies required them to use equity financing. Thus, most of the *zaibatsu* companies pushed forward with an initial public offering. Second, the *zaibatsu* and their companies established The Industry Club of Japan in 1917 to influence governmental policy or legislators in the area of economic policy. This federation promoted the *zaibatsu*-centered industrial policies to protect the interests of the *zaibatsu* and its companies against the organized labor movement.

During and following the Great Depression, the sociopolitical power of the *zaibatsu* met with severe criticism and accusation from the public. When the economic depression in Japan was serious, the *zaibatsu* formed a powerful family-controlled commercial combine; each *zaibatsu* consisted of companies to provide funds and financial services and a trading company to buy and sell goods and services on behalf of the member companies. Anti-*zaibatsu* sentiments of those days in Japan had some influence on businesses of the *zaibatsu* and its directly affiliated companies. First, the *zaibatsu-honsha* offered its securities to the public to meet the demands of the times and the public. However, the stock was not as good as it looked. The *zaibatsu* also made voluntary donations to the public, but only the Mitsui Foundation was centered on corporate philanthropy.

During the Sino-Japanese War (1937–1945) and the Pacific War (1941–1945), all the *zaibatsu* companies were of great economic importance and included heavy industry, the mining industry, the light industry, and the finance industry. When the *zaibatsu* had accumulated a huge amount of capital through its political merchant activities, a Japanese movement of militarism and ultranationalism was formed. This is one reason why the General Headquarters of the Allied Powers (GHQ) established the *zaibatsu* dissolution program and the Elimination of Excessive Concentrations of Economic Power or Antimonopoly Act.

GHQ adopted the anti-*zaibatsu* policies and legislation in hopes of eliminating the *zaibatsu* family control and the *zaibatsu*-centered financial structure. The purpose of these measures was to reform business and society in Japan and convert the *zaibatsu* companies into publicly held corporations. Several years after the *zaibatsu* were dissolved completely, some groups of businesses that once belonged to the same *zaibatsu* emerged. These groups cannot be conceptualized as *zaibatsu* companies; they are not owned exclusively by a single family or an extended family. What emerged here is the "*keiretsu*," bound neither by family ties nor by pure holding companies. The *keiretsu* are business groups bound by cross-shareholdings and dispatching of company executives. Now, these companies are generally classified as companies of *zaibatsu* descent.

—Norihiro Mizumura

See also *Keiretsu*

Further Readings

Bisson Thomas, A. (1954). *Zaibatsu dissolution in Japan.* Berkeley: University of California Press.

GHQ Supreme Commander for the Allied Powers. (1956). *History of the nonmilitary activities of the occupation of Japan 1945–1950: Elimination of zaibatsu control* (SCAP, Monographs, RG331). (From microfilms in Japan National Diet Library, Administrative, Research and Legislative Reference; original paper in U.S. National Archives and Records Services)

Morikawa, H. (1992). *Zaibatsu: The rise and fall of family enterprise groups in Japan*. Tokyo: University of Tokyo Press.

Appendix: Business Ethics Periodicals

This appendix presents a selected guide to periodicals that are for researchers, practitioners, and the interested layperson. The reader seeking articles on business ethics will find a number of significant research journals and annual series. In addition, there are many trade magazines (those read by primarily businesspeople) and popular press sources. Other “born digital” resources, such as online-only journals, society newsletters, and Web sites also may be useful, peripherally. The publications discussed here are primarily English language, although their contents may be international in scope. Also highlighted are the electronic databases currently most effective for finding articles in these periodicals and the few research-related born digital resources.

Core Academic Journals

Relatively few academic journals are devoted to business ethics and cover a full range of topics and methodological approaches associated with the field. Generally, the three publications doing both are the field’s core journals *Journal of Business Ethics, Business Ethics Quarterly,* and *Business & Society.* Their readership predominantly consists of theorists and practitioners.

All three contain articles that are theoretical, empirical, or literature reviews. Other regular features include book reviews, thematic issues, conference announcements, and calls for papers. The publishers’ Web sites for these three journals offer free e-mail alerts for the tables of contents of each new issue, as do several of the other journals mentioned later in this appendix.

Journal of Business Ethics (JBE) began in 1982 as a quarterly, but has expanded to seven volumes per year (28 issues), with a circulation of approximately 7,500 institutional subscriptions worldwide. Its audience is academics and anyone else interested in business ethics topics. From 1997 to 2003, articles that focused on education were published separately in *Teaching Business Ethics* (ISSN 1382-6891, Kluwer). Currently, this topic is reincorporated into *JBE.* Similarly, the *International Journal of Value-Based Management* (ISSN 0895-8815, Kluwer, 1988–2003) became integrated into *JBE.* (ISSN 0167-4544; Springer; URL: http://springerlink.metapress.com/openurl.asp?genre=journal&issn=0167-4544)

Business Ethics Quarterly, launched in 1991, is the official publication of the Society for Business Ethics and has a paid circulation of more than 1,050. Six to twelve double-blind peer-reviewed articles appear per issue. The intended audience is researchers, teachers, and business practitioners who are interested in conceptual and methodological aspects of business ethics, especially those approaches that address international business, economics, and values. (ISSN 1052-150X, Philosophy Documentation Center; URL: www.pdcnet.org/beq.html)

Business & Society: A Journal of Interdisciplinary Exploration has appeared quarterly since 1960 and presently has a circulation of more than 700. This official publication of the International Association of Business and Society focuses on social issues in management and business ethics. The articles address ethics and values, business-government relations, corporate governance, environmental management, and international issues. In addition to research and book reviews, it provides relevant dissertation abstracts. (ISSN 0007-6503, Sage; URL: http://bas.sagepub.com)

Other Scholarly Journals

Since business ethics research is often interdisciplinary in nature, many useful articles appear in the periodicals of other fields. Also, material can be found in journals that focus entirely on a single topic within the field of business ethics. Below is a selected list of significant peer-reviewed journals of both kinds, presented in alphabetical order. Which titles among them are most important depends on the reader's focus and research interests. Some of the most highly regarded research titles among this group are *Academy of Management Review, Business & Society Review, Business Ethics: A European Review,* and *Organization Science.* Typical supplemental contents are conference announcements and book reviews.

Academy of Management Review, a highly regarded management journal, has appeared quarterly since 1976 and features a number of articles each year on ethics-related topics. In addition to research, book reviews, and announcements, there is a Publications Received list. (ISSN 0363-7425, Academy of Management; URL: http://aom.pace.edu/amr)

Business & Professional Ethics Journal, published quarterly since 1981, contains articles that compare professions or cover ethics topics in areas like marketing, health care management, human resources, and global labor. Half of the issues reprint selected papers from international conferences. More recently, the journal has appeared irregularly and incorporates the publication *Professional Ethics* (ISBN 1063-6579, 1992–2004). (ISSN 0277-2027, University of Florida Center for Applied Philosophy and Ethics in the Professions; URL: www.ethics.ufl.edu/BPEJ)

Business and Society Review: Journal of the Center for Business Ethics at Bentley College has appeared quarterly since 1972. Each issue has about a dozen articles by academics and practitioners that contain scholarly research, commentary, policy analysis, or book reviews. Some issues are thematic. (ISSN 0045-3609, Blackwell; URL: www.blackwellpublishing.com/journals/BASR)

Business Ethics: A European Review is considered a top business ethics journal by many, appearing quarterly since 1992. It covers current issues and emerging concerns, from a European perspective, on topics related to the ethical practices of corporations and individuals. The audience is academics and businesspeople. (ISSN 0962-8770, Blackwell; URL: www.blackwell-synergy.com/loi/beer)

Corporate Governance: An International Review (CGIR), produced bimonthly since 1992, publishes research on trends in the development and improvement of organizations' governance, boards, and directors. *CGIR* frequently includes articles about ethics-related issues. (ISSN 0964-8410, Blackwell; URL: www.blackwellpublishing.com/journals/CORG)

Corporate Governance: The International Journal of Business and Society, published five times a year since 2001, includes articles on real-world performances of boards and CEOs and corporate social responsibility. Articles are research, policy analysis, or case studies, occasionally gathered into thematic issues. (ISSN 1472-0701, Emerald; URL: www.emeraldinsight.com/cg.htm)

Corporate Reputation Review: An International Journal, appearing quarterly since 1996, produces articles on reputation management, highlighting best practices and current trends. Article treatments include research, case and industry studies, and policy analysis. (ISSN 1363-3589, Palgrave Macmillan; URL: www.henrystewart.com/corporate_reputation_review)

Electronic Journal of Business Ethics and Organization Studies, is an online journal published in Finland, semiannually since 1996. It contains research, primarily in English, and is open access (free to readers) online. (ISSN 1239-2685, University of Jyväskylä, Business and Organization Ethics Network, School of Business and Economics; URL: http://ejbo.jyu.fi/index.cgi?page=cover)

Ethics in Film is an online journal, begun in 2005, that focuses on using film to teach ethics, including business ethics examples. (ISSN not available, Center for Business and Society, University of Colorado; URL: www.ethicsinfilm.com)

Greener Management International: The Journal of Corporate Environmental Strategy and Practice, produced quarterly since 1993, has articles and case studies with an international scope that focus on environmentally sustainable business practice. Recent examples of thematic issues have included sustainable performance and business competitiveness, chemical risk management, and greening supply chain management. (ISSN 0966-9671, Greenleaf; URL: www.greenleaf-publishing.com)

International Journal of Business Governance and Ethics, published quarterly since 2003, focuses with interdisciplinary perspectives on aspects of corporate social responsibility and ethical decision making within organizations. (ISSN 1477-9048, Inderscience Publishers; URL: www.inderscience.com/ijbge)

Journal of Business Ethics Education (JBEE) began publishing quarterly in 2004. Currently, it is the only journal exclusively devoted to articles on teaching business ethics, since content for the former *Teaching Business Ethics* is now reincorporated into *JBE,* and the *Journal of Management Education* is more broadly focused. *JBEE* contains research articles and curriculum materials. (ISSN 1649-5195, Senate Hall and Carnegie Bosch Institute; URL: www.senatehall.com/journals.php?journal=5)

Journal of Corporate Citizenship, produced quarterly since 2001, publishes articles that link theory with practice about corporate citizenship, addressing global and local perspectives. (ISSN 1470-5001, Greenleaf; URL: www.greenleaf-publishing.com/jcc/jccframe.htm)

Journal of Management Education has appeared bimonthly since 1975 with articles on teaching business students and managers. Ethics-related items appear in nearly every issue. Articles may be theoretical and empirical research, essays, reviews of instructional materials, as well as teaching tools, such as exercises and assignments that use discussion, case method, role playing, and writing. The December issue has an annual index. (ISSN 1052-5629; URL: www.sagepub.com/journal.aspx?pid=181)

Journal of Public Policy and Marketing (JPPM) published semiannually since 1982, *JPPM* contains articles on social, ethical, public policy, and economic aspects of marketing. (ISSN 0748-6766, American Marketing Association; URL: bear.cba.ufl.edu/centers/jppm)

Organization Science, one of the top research journals in management, began publishing in 1990. Its bimonthly issues focus on systems and behavior in organizations, drawing from the fields of management, sociology, psychology, economics, and communications. Usually, there are several ethics-related articles per year. (ISSN 1047-7039, Institute for Operations Research and the Management Sciences; URL: www.marketingpower.com/content1056C342.php)

Review of Social Economy, published quarterly since 1948, is the official publication of the Association for Social Economics and concentrates on topics like the relationships between social values, economics, and ethics. Themes include social justice, poverty, income distribution, gender, environment, and humanism. (ISSN 0034-6764, Routledge; URL: www.tandf.co.uk/journals/titles/00346764.asp)

Teaching Business Ethics appeared quarterly from 1997 to 2003 and is now incorporated into *Journal of Business Ethics* (see above). (ISSN 1382-6891, Kluwer Academic)

Zeitschrift fuer Wirtschafts und Unternehmensethik (Journal of Business, Economics and Ethics), begun in 2000, is published three times per year. Theoretical and empirical articles are primarily in German, but some are in English, and all articles have English abstracts. (ISSN 1439-880x, Rainer-Hampp-Verlag; URL: www.zfwu.de)

Annual Book Series

Annual series have been a key format for distributing business ethics articles, especially before many journals published ethics-related articles regularly. Below is a selected list of the most relevant ones, presented in alphabetical order.

Annual Editions: Business Ethics has run from 1989 to present, reprinting articles from diverse academic journals and popular magazines that focus on basic concepts drawn from many perspectives. (ISSN 1055-5455, McGraw-Hill/Dushkin; URL: www.dushkin.com/annualeditions/ae-list.mhtml)

IABS Proceedings, published since 1990, includes papers presented at annual meetings of the International Association for Business and Society, the producers of *Business & Society.* (ISSN not available; URL: www.iabs.net)

International Business Ethics Review covers international aspects of corporate social responsibility. The International Business Ethics Institute of Washington, D.C., has turned out three to five academic articles annually since 1997 but began more frequent publication in 2005. The print copies are free on request. (ISSN not available; URL: www.business-ethics.org/iberpub.asp)

Issues in Business Ethics has appeared irregularly since 1990, producing single-topic volumes that are collections of previously unpublished scholarly articles on ethics in international management. (ISSN 0925-6733, Springer-Verlag Dordrecht; URL: www.springer.com/sgw/cda/frontpage/0,11855,5-40385-69-33114156-0,00.html)

JAI Press (now called JAI/Elsevier) generates several annual titles, each with original research articles. The most notable include the following:

Research in Ethical Issues in Organizations (ISSN 1529-2096, 1999 to present)

Research on Professional Responsibility and Ethics in Accounting (ISSN 1574-0765, 1995 to present; called *Research on Accounting Ethics* prior to 2004)

Research in Corporate Social Performance and Policy (ISSN 0191-1937, 1978–1998)

JAI also publishes *Advances in Bioethics, Research in Social Problems and Public Policy,* and others. (URL: www.elsevier.com/wps/find/books_browse.cws_home?pseudotype=SER)

Ruffin Series in Business Ethics, appearing biennially since the 1990s, publishes the papers delivered at the renowned lecture series at the Darden School sponsored by the University of Virginia's Olsson Center for Applied Ethics and the Ruffin Foundation. (ISSN not available, Philosophy Documentation Center; formerly published by Oxford University Press, 1998–2004; URL: www.pdcnet.org/ruffin.html)

Soundings: A Series of Books on Ethics, Economics and Business has appeared irregularly since 1987, produced by the University of Notre Dame Press. (ISSN not available; URL: www3.undpress.nd.edu/dyn/series/36)

Transparency International, based in Berlin, Germany, has two annual publications that are available free online: *Global Corruption Report,* www.globalcorruptionreport.org, and *Corruption Perceptions Index,* www.icgg.org/corruption.cpi.html (copublished with the International Center for Corruption Research).

Trade Journals, Newsletters, and the Popular Press

Some periodicals are used primarily for locating news, trends, commentary, and case study material. Below is an alphabetical list of selected publications that are geared toward researchers, businesspeople, students, and the public:

Business Ethics: The Magazine of Corporate Responsibility (BE), formerly *Business Ethics Magazine,* publishes quarterly with a circulation of about 10,000 (current issue is free online). *BE* covers trends and includes special features like reports on teaching ethics in MBA programs, interviews with corporate leaders, awards, and an annual ranking of the "100 Best Corporate Citizens." (ISSN 0894-6582, New Mountain Media; URL: www.business-ethics.com)

The Conference Board's *Research Reports* and *Executive Action Reports* frequently include publications that address ethics topics, with items such as "Why Ethical Leaders are Different," "Using Ethical Analysis to Guide Offshoring," and "Corporate Citizenship Reporting: Best Practices." (ISSN 0732-572X; URL: www.conference-board.org/publications)

Compact Quarterly: Corporate Citizenship in the World Economy is the official newsletter (free online) of the United Nations' Global Compact, which began in 1999 as an initiative promoting corporate responsibility worldwide by encouraging company participation in adhering to principles promoting human rights, labor standards, the environment, and anticorruption. (ISSN not available, United Nations; URL: www.enewsbuilder.net/globalcompact)

CQ Researcher, a weekly, frequently publishes issues on business ethics topics that are particularly good for basic overviews of subjects currently appearing in the U.S. and international news. Each issue includes a chronology of the topic, pro/con arguments, and essays. Past issues have addressed the following: "Whistleblowers," "Disabilities Act," "Religion in the Workplace," "Lobbying Boom," "Corporate Crime," "Child Labor and Sweatshops," "Drug Company Ethics," "Asbestos Litigation," "Diversity in the Workplace," and "Contingent Work Force." (ISSN 1056-2036, Congressional Quarterly; URL: www.cqpress.com/product/Researcher-Online.html)

Ethics Newsline, free online, summarizes each week's ethics-related news, and includes features like statistics, quotes, research reports, commentary, charts, and illustrations. (ISSN not available, Institute for Global Ethics; URL: www.globalethics.org/newsline/members/index.tmpl)

Ethics Today, produced by the Ethics Resource Center, Washington, D.C., is a monthly free e-mail newsletter and accompanying Web site that contains news, white papers, research reviews, and educational resources on organizational ethics (formerly *Ethics Journal,* ISSN 1060-0698, 1991–1996). (ISSN not available; URL: www.ethics.org/erc-publications/newsletter.asp)

Ethikos: Examining Ethical and Compliance Issues in Business has come out semimonthly since 1987, focusing on corporate ethics programs and reporting on experiences with corporate compliance programs (incorporates *Corporate Conduct Quarterly,* ISSN 1061-8775, 1991–1999). (ISSN 0895-5026, Ethics Partners, Inc.; URL: www.singerpubs.com/ethikos)

European Business Ethics Newsletter, biannual since 2003 (free online), publishes news and announcements related to the activities of the European Business Ethics Network. (ISSN none available; URL: www.ebenuk.org/info_resources.html)

Philosophy for Business, appearing monthly since November 2003 (free online) from the International Society for Philosophers, features articles and book reviews for a broad audience about the philosophical aspects of business. (ISSN not available; URL: www.isfp.co.uk/businesspathways)

Society for Business Ethics Newsletter has been published twice a year since 2004 (free online) by the producers of *Business Ethics Quarterly* and includes items like conference calendars, calls for papers, job announcements, and other association business. (ISSN not available; URL: www.societyforbusinessethics.org)

Research Databases

Online databases allow simultaneous searching of hundreds of periodicals, across a broad chronological range. They save the researcher time by searching widely for relevant articles, covering both the journals typically devoted to business ethics and those from allied fields that occasionally produce ethics-related articles.

More than 12 commercial services may be used effectively to locate articles on business ethics. The major, broad-based management databases are the primary choices to research business-ethics-related topics because they cover the largest range of relevant academic literature, as well as news, commentary, case studies, and policy analysis articles. The leading databases cover six or more journals that are central to business ethics, along with a significant number of other academic and trade journals of secondary importance to the field. They are as follows:

ProQuest's ABI/Inform Global

EBSCO's Business Source Premier

Another strong resource, the *Bibliography of Business Ethics Articles* (www.isbee.org/biblio/EthicsArticles.php), is available online at no charge. Created and maintained as a project of the International Society of Business, Economics, and Ethics, it contains about 4,000 citations (dating from 1992 to present) that are handpicked from nine central business-ethics-related journals. This bibliography of high-quality sources is easily accessible, although it has limitations, compared with commercial databases, in terms of the range of journals, the citation-only format, how fast new content is added, and its search engine's features.

Secondary choices for research databases on business ethics topics are the major interdisciplinary academic databases or those others that are dedicated to specific disciplines (e.g., philosophy, psychology). They contain fewer of the periodical titles that publish business ethics research. Listed in order of most-to-least coverage are

Expanded Academic,

International Bibliography of the Social Sciences,

Business Periodicals Index,

Emerald Insight,

Business and Company Resource Center,

Philosopher's Index,

PAIS International,

Social Science Index,

IBZ/Internationale Bibliographie der Geistes- und Sozialwissenschaftliche Zeitschriftenliteratur (International Bibliography of Periodical Literature in the Humanities and Social Sciences),

IBR/Internationale Bibliographie der Rezensionen Geistes- und Sozialwissenschaftliche Literatur (International Bibliography of Reviews of Scholarly Literature in the Humanities and Social Sciences),

Dietrich's Index Philosophicus, and

Social Science Citation Index.

Other highly specialized databases may be useful occasionally, depending on the research topic. Examples are *Communication Abstracts, Criminal Justice Abstracts, Environmental Science and Pollution Management, POESIS, PsycINFO, Religion Index, Risk Abstracts,* and *Worldwide Political Science Abstracts.*

A notable feature of commercial databases is that they provide a controlled vocabulary that not only assists searching by subject (e.g., corporate social responsibility) but also by specific article treatments, so that researchers can combine their subjects with keywords such as "case studies," "peer review," "editorial," or "statistical" (keywords vary by database). Free Internet search engines, even Google Scholar, currently do not offer this kind of powerful search refinement feature.

Google Scholar does outperform the commercial databases in one area: The contents published in annual book series, many of which are original research articles, currently are ignored by these commercial database sources, with the exception of the *Ruffin Series,* which is available through *ABI/Inform* and *POESIS.* Google Scholar is providing some incomplete, but promising, indexing that uncovers the material in these annual series. Comprehensive tracking of items in annuals, however, is best done from each publisher's Web site.

Obtaining the Materials

The majority of the databases and individual journal titles listed here are subscription services that typically are accessed through academic and public libraries, academic departments and research centers, corporate intranets, and other private libraries. Affiliated users of these libraries should inquire locally about what is available to them. Even when the home library does not own specific articles, users often may request them through their library's interlibrary loan service. Alternatively, individuals without a library affiliation may find pay-per-print access directly through the databases and journal publishers or via article supply vendors such as Ingenta or the British Library Document Supply Center. Online availability of older items may vary, however, and some may only be available through libraries and interlibrary borrowing.

Miscellaneous Digital Resources

Useful Web sites that support business ethics research come in a variety of forms, with links to business ethics periodicals, news, or other documents. BELL: The Business Ethics Link Library (http://libnet.colorado.edu/Bell/frontpage.htm) is a comprehensive collection of resources compiled by the business library at the Leeds School of Business, University of Colorado, that primarily provides many dozens of examples of the codes of ethics of business and organizations. BELL also serves as a useful first stop for links to ethics periodicals, education programs, and other ethics and corporate social responsibility online resources. In addition to the already-mentioned newsletters by the Ethics Resource Center, European Business Ethics Network, and the Society for Business Ethics, there presently are two well-established English language Internet sites that contain news, commentary, announcements, and the occasional case study. They are the business ethics section of Management Logs, www.managementlogs.com/business_ethics.html, a Web log by more than 12 international contributors, and *RISQ: Review of International Social Questions*, www.risq.org/category4.html, a publication by 18 international researchers, journalists, and policy makers. These sites host journalistic reporting and interviews and have supplemental features like notifications for new content, useful links, and interactive discussions. More sites such as these are likely to appear as interest in and the study of business ethics become more widespread.

—Adele L. Barsh

See also Business Ethics Scholarship

Further Readings

Urlich's periodicals directory. (Annual). New Providence, NJ: R. R. Bowker. Retrieved from www.ulrichsweb.com/ulrichsweb

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Entry titles are in **bold.**